Pakistan Public Sector Accounting and Auditing
A Comparison to International Standards

Country Report

May 2007

Financial Management Unit
South Asia Region
GOVERNMENT FISCAL YEAR
July 1 - June 30

CURRENCY EQUIVALENTS
(Exchange rate effective May 1, 2007)
Currency Unit = Pakistani Rupee (PKR)
US$1 = approx. PKR 6.99

Abbreviations and Acronyms

AATI  Audit and Accounts Training Institute
ADB  Asian Development Bank
ACCA  Association of Chartered Certified Accountants, UK
AGP  Auditor General of Pakistan
CGA  Controller General of Accounts
CFO  Chief Financial Officer
CFAO  Chief Finance & Accounts Officer
DAC  Departmental Accounts Committee
DAGP  Department of the Auditor General
FAPC  Financial Audit Policy Committee
FPSC  Federal Public Service Commission
FAM  Financial Audit Manual
IAASB  International Auditing and Assurance Standards Board
IAS  International Accounting Standard
ICAP  Institute of Chartered Accountants of Pakistan
IES  International Education Standards for Professional Accountants
IFAC  International Federation of Accountants
IFRS  International Financial Reporting Standard
INTOSAI  International Organization of Supreme Audit Institutions
IPSAS  International Public Sector Accounting Standard
IPSASB  International Public Sector Accounting Standards Board
ISA  International Standard on Auditing
NAM  New Accounting Model
FACT  Program for Accountability and Transparency (UNDP)
PEFA  Public Expenditure and Financial Accountability
PFM  Public Financial Management
PIFRA  Project for Improvement of Financial Reporting and Auditing
PIPFA  Pakistan Institute of Public Finance Accountants
SAI  Supreme Audit Institution
SDAC  Special Departmental Accounts Committee
SOE  State-Owned Enterprise
UNDP  United Nations Development Program

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Acknowledgments

This assessment of accounting and auditing standards and practices in the public sector is part of a review program in the South Asia Region. It has been carried out in active collaboration with the Government of Pakistan and various stakeholders, particularly the offices of the Auditor General and the Controller General of Accounts. Discussions were also held with senior officers of the Audit and Accounts Training Institute (AATI) and the Project for Improvement of Financial Reporting and Auditing (PIFRA). In particular, the following individuals contributed their valuable time and expertise to this assessment:

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Mr. Hammad Younis, PIFRA
Mr. Khan, PIFRA

The review was conducted through a participatory process that involved the stakeholders listed above. The responses to the diagnostic questionnaires were especially useful, as were the reports, manuals, and information available from the PIFRA Project and recent World Bank assessments of public financial management in Pakistan.

The World Bank Task Team was responsible for this report with general guidance from the advisors and the development partners who collaborated on this review program. The draft
report developed after a consultative workshop in Islamabad on December 16, 2006 was provided to the Government for comment, and the comments made have been considered in this country report.

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Executive Summary

1. This assessment of public sector accounting and auditing is generally meant to help implement more effective public financial management (PFM) through better quality accounting and public audit processes in Pakistan and to provide greater stimulus for more cost-effective outcomes of government spending. More specific objectives are (a) to provide the country’s accounting and audit authorities and other interested stakeholders with a common, strongly-founded, knowledge as to where local practices stand against the internationally developed norms of financial reporting and auditing; (b) to assess the prevailing variances; (c) to chart paths for improving the accordance with international standards; and (d) to provide a continuing basis for measuring improvements.

2. Annex A explains the methodology used for the assessment. The desired actions indicated by this assessment are summarized below.

3. **Adopt International Public Sector Accounting Standards.** The International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants (IFAC) issues International Public Sector Accounting Standards (IPSAS). Annex B gives a general description of IFAC and a listing of the IPSAS. At the present time, Pakistan does not comply with the IPSAS in preparing its annual accounts. The country’s accounts do not provide a statement of cash receipts and payments which (a) recognizes all cash receipts, cash payments, and cash balances controlled by the entity; and (b) separately identifies payments made by third parties on behalf of the entity in accordance with paragraph 1.3.24 of this IPSAS. In addition, the country’s accounts do not provide accounting policies and explanatory notes. A general program is underway for the adoption of accounts in a form specified in its New Accounting Model (NAM). This form of reporting was developed in 1998 and adopted the then proposed modified cash basis of accounting standard. The IPSASB has not approved this form of reporting as an official standard. It has established standards for accrual-based reporting and also the Cash Basis IPSAS together with guidance for transition to an accrual basis of accounting. Under the guidance of the Auditor General of Pakistan (AGP), the Controller General of Accounts (CGA) needs to restructure the present cash basis of financial reporting to conform fully to the Cash Basis IPSAS. While the IPSAS-2 reporting format has been designated by the Auditor General as additional reporting requirements for the government, it would be appropriate to set up a committee to review and steer the process to implement Cash Basis IPSAS on a continuous basis. With strengthened capacity effected by recruiting financial reporting specialists for the CGA administration, a transition to full Cash Basis IPSAS—while also adopting the Modified Cash Basis IPSAS as per the New Accounting Model (NAM)—can be smoothly accomplished, although the problem of consolidation of controlled entities would still

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1 The modified cash basis of accounting helps in controlling not only cash but also commitments against budget, allowing the production of a statement of receipts and payments, a statement of assets and liabilities, and a cash flow statement.
The Government noted in its response to the draft report that the requirements of the cash basis of accounting have been incorporated in the NAM Manual of Accounting Principles and its Procedures Manual and that the progressive implementation of the NAM will meet all the requirements. As a next step, a transitional path should be developed that presents the full accrual information to best serve the general financial statements as required under Section 7(b) of the CGA (Appointment, Functions and Powers) Ordinance 2001. Annex C includes the pertinent text of the Constitution and the AGP and CGA Ordinances. Benefits from adopting accrual reporting are set out in Annex D.

4. A Supplementary Table of Standards and Gaps of this report provides a matrix detailing the current standards, the present position, and options for improvement. A summary of the accounting standards issues is shown in Table ES1.

<table>
<thead>
<tr>
<th>Standard</th>
<th>Current status</th>
<th>Activity required to adopt international standards</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Does the Public Sector Accounting Law adopt IPSAS?</td>
<td>Only partially. The notification of the adoption of the IPSAS-2 cash flow reporting format as part of the overall reporting requirements of the government is a step in the right direction.</td>
<td>A committee should be set up to review and steer the process to implement full cash basis of financial reporting on a continuous basis. The financial reporting specialists should steer the process as key members of the committee. Upon implementation of the Cash Basis IPSAS as additional reporting requirements of the government, the committee should gradually begin the transition to adopting accrual-based IPSAS. The PIFRA project is providing the necessary support for computerization of the accounts and capacity building of the staff.</td>
</tr>
<tr>
<td>2. Does the education and training of accountants accord with IES?</td>
<td>Partly. A comprehensive training strategy is directed toward the professionalization of accounting staff through IES-compliant qualifications.</td>
<td>Implement the training and professionalization strategy, and include IPSAS in AATI syllabi.</td>
</tr>
<tr>
<td>3. Does the code of ethics match international standards?</td>
<td>Yes. The Auditor General has adopted the INTOSAI Code of Ethics.</td>
<td>The code of ethics should be made a part of the staff contracts.</td>
</tr>
<tr>
<td>4. Is there a body to prescribe public sector accounting standards?</td>
<td>Yes. The Constitution of Pakistan delineates the authority of the Auditor General of Pakistan to prescribe the form, principles, and methods of accounts of the Federation and of the Provinces with the approval of the President.</td>
<td>While IPSAS should be the core framework for financial reporting, with the Modified Cash Basis under the NAM, IAS/IFRS should be the approved standards for accounting and financial reporting for all state-owned enterprises.</td>
</tr>
<tr>
<td>5. Are financial statements presented in accord with the IPSAS?</td>
<td>To a limited extent. The Cash Basis IPSAS for financial reporting is not yet followed, nor is the accrual-based IPSAS. The CGA has the responsibility for</td>
<td>There are 3 identified gaps: (1) Accounting policies and notes to the accounts are absent. (2) Third party transactions are not included. (3) Controlled entities' financial</td>
</tr>
<tr>
<td>Standard</td>
<td>Current status</td>
<td>Activity required to adopt international standards</td>
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<tr>
<td>----------</td>
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<td>--------------------------------------------------</td>
</tr>
<tr>
<td>6. Is the statement of cash receipts and payments in IPSAS form?</td>
<td>No. A basic statement of cash receipts and payments is provided but this information is currently presented in formats inconsistent with the IPSAS.</td>
<td>A statement of cash receipts and payments as per the IPSAS Cash Basis can be prepared using existing information from the accounting records. This work requires some restructuring of the financial reporting formats.</td>
</tr>
<tr>
<td>7. Are accounting policies and explanatory notes required?</td>
<td>No. Statements of accounting policies are not provided in the budget or accounts documents.</td>
<td>There is a need to state the accounting policies and the basis on which the accounts are prepared.</td>
</tr>
<tr>
<td>8. Are other disclosures in accord with IPSAS?</td>
<td>Partly. Financial statements are not available within 6 months of the reporting period; some items are not disclosed, and presentation does not meet some transparency requirements.</td>
<td>It would be necessary to reduce the reporting lag, improve reconciliations, and disclose further information (e.g., on the treatment of foreign currency).</td>
</tr>
<tr>
<td>9. Does the government issue a consolidated financial statement that consolidates all controlled entities?</td>
<td>No.</td>
<td>A statement of cash receipt and payment as per the Cash Basis IPSAS can be prepared. Further steps will be needed to consolidate the financial information of the controlled entities.</td>
</tr>
</tbody>
</table>

5. Implement the Financial Audit Manual that has been prepared using the IFAC-issued International Standards on Auditing (ISA), as well as of the International Organization of Supreme Audit Institutions (INTOSAI). The Auditor General of Pakistan has approved the new Financial Audit Manual, which follows the modern risk-based certification audit approach. A program for implementation of this Manual is in preparation. The Auditor General has already formally adopted the INTOSAI Auditing Standards with minor modifications. The INTOSAI recognizes that its Auditing Standards are broad in nature and that the IFAC-issued International Standards on Auditing provide a further level of detail for public sector audit guidance. The INTOSAI is working with IFAC in the longer term to develop practice notes to assist with the implementation of each ISA in the public sector. Annex B lists the INTOSAI and IFAC standards.
6. Improve the jurisdiction, mandate, and functions of the Auditor General of Pakistan as envisaged in the Auditor General Ordinance 2001, and strengthen the reporting and disclosure processes of audit conclusions. Auditing practices need to be revised in line with the INTOSAI Auditing Standards, IFAC-issued International Standards on Auditing, and the new Financial Audit Manual. Reporting of audit results needs to be more timely and to be disseminated more publicly. The incentives for auditees to take action on audit findings would increase by facilitating easy access to, and greater dissemination of, audit reports. And this would be helped by more focused and effective report writing and report follow-up processes.

7. A Supplementary Table of Standards and Gaps of this report provides a matrix detailing the current standards, the present position, and options for improvement. A summary of auditing issues is shown in Table ES2.

<table>
<thead>
<tr>
<th>Standard</th>
<th>Current status</th>
<th>Activity required to adopt international standards</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Is the SAI statutory framework in accord with the needs of the INTOSAI Auditing Standards?</td>
<td>Partially. Some additional powers need to be established by legislation as set out below.</td>
<td>Some revisions in the Auditor General Ordinance 2001 are required.</td>
</tr>
<tr>
<td>2. Is there a body to prescribe public sector auditing standards?</td>
<td>Yes. It has been construed from various provisions of legislation, including Section 22 of the Auditor General Ordinance 2001 that the Auditor General would be the standard-setting authority for public sector auditing. Thus, the Auditor General adopted INTOSAI Auditing Standards as recommended by a committee of senior officers in the DAGP.</td>
<td>To improve on this, the Auditor General should coordinate with ICAP to form a Public Sector Committee for review and adoption of ISA.</td>
</tr>
<tr>
<td>3. Have INTOSAI and IFAC audit standards been adopted?</td>
<td>Partly. The Auditor General has adopted INTOSAI Auditing Standards.</td>
<td>A Public Sector Committee should be used to adopt ISA and develop formal implementation notes for guidance.⁷</td>
</tr>
<tr>
<td>4. Has a code of ethics equivalent to the INTOSAI Auditing Standards been adopted?</td>
<td>Yes.</td>
<td></td>
</tr>
<tr>
<td>5. Is the accountability process in the SAI in accord with INTOSAI Auditing Standards?</td>
<td>Yes.</td>
<td></td>
</tr>
<tr>
<td>6. Does the SAI legal framework meet the INTOSAI Auditing Standards for independence and powers?</td>
<td>Largely.</td>
<td>The Auditor General needs improved legislation to exclude limitations on jurisdiction, mandate, and function of this position; and improved offence clauses together with enhancement in transparency and disclosure of audit</td>
</tr>
</tbody>
</table>

⁷ Pakistan should nominate persons to the Reference Panel of the INTOSAI Working Group on Financial Audit Guidelines, which is a subcommittee of the INTOSAI Auditing Standards Committee.
<table>
<thead>
<tr>
<th>Standard</th>
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</tr>
</thead>
<tbody>
<tr>
<td>7. Does the education and training of the auditors accord with INTOSAI and IES?</td>
<td>Partly. Staff needs more professional training.</td>
<td>The AATI should continue to review its syllabus to cover all areas recommended by the IFAC educational standards.</td>
</tr>
<tr>
<td>8. Is the SAI equipped with the audit methods and technologies to meet the INTOSAI Auditing Standards?</td>
<td>Yes. But not implemented in full at the moment.</td>
<td>Improved methodologies are being implemented. The technology required to support a management information system for the Auditor General is missing. The requirements are being acquired through PIFRA. The implementation plan will review capacity for implementing the new Financial Audit Manual.</td>
</tr>
<tr>
<td>9. Does the SAI have the requisite quality assurance programs to meet international standards?</td>
<td>Partly. Internal quality assurance and supervision provide review arrangements among the field audit offices.</td>
<td>Improved working paper guidance and computerization combined with more effective supervision and more independent quality review processes are needed.</td>
</tr>
<tr>
<td>10. Does the process to plan the audits meet international standards?</td>
<td>Partly. Improved methodologies are being implemented.</td>
<td>The audit process should be risk-based allowing sufficient flexibility to the auditors to articulate and apply appropriate audit procedures on methodically selected samples to arrive at representative audit conclusions.</td>
</tr>
<tr>
<td>11. Does the process of supervising the audits meet international standards?</td>
<td>Partly. Working paper systems and audit methodologies do not currently enable effective supervision. Improved methodologies are being implemented under PIFRA.</td>
<td>The revised working paper structure should be implemented together with the new Financial Audit Manual for audit supervision.</td>
</tr>
<tr>
<td>12. Does the process of evaluating the reliability of internal control meet the international standards?</td>
<td>Partly. Improved methodologies are being implemented.</td>
<td>The methodology needs to be more risk- and systems-based.</td>
</tr>
<tr>
<td>13. Does the process used in audits to assess compliance with laws meet international standards?</td>
<td>Partly. Improved methodologies are being implemented.</td>
<td>The methodology needs to be risk- and systems-based and may be integrated as planned with the annual certification audit.</td>
</tr>
<tr>
<td>14. Does the audit process used to obtain evidence to support conclusions meet international standards?</td>
<td>Partly. The evidence to support audit criticisms on individual transactions is for the most part better than that available to provide the more general audit assurance</td>
<td>More rigorous plans for audit testing need to be developed as per the Financial Audit Manual. The evidence for more general audit assurance needs better organization.</td>
</tr>
</tbody>
</table>

Guidance is provided by (1) a general prescription of a model law developed by the UNDP Program for Accountability and Transparency (PACT) and (2) the Model National Audit Office Act by The Association of Chartered Certified Accountants, UK, 2004.
<table>
<thead>
<tr>
<th>Standard</th>
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</tr>
</thead>
<tbody>
<tr>
<td>15. Does the audit analyze the financial statements to establish whether acceptable accounting standards for financial reporting and disclosure are complied with?</td>
<td>Partly. The existing structure of the financial statements only provides limited scope for financial analysis that is useful for certification audit.</td>
<td>The full implementation of IPSAS would improve the DAGP’s ability to do meaningful and reliable financial analysis.</td>
</tr>
<tr>
<td>16. Does the auditor prepare an audit opinion on the financial statements in a form that accords with international standards?</td>
<td>Not fully at this stage. The Auditor General signs an opinion on the accounts; but because the financial statements are not prepared in accordance with adequate standards, the wording of the audit opinion does not contain all of the requirements of ISA 700, <em>The Auditor’s Reports on Financial Statements</em>. The wording does not clearly indicate the financial reporting framework used to prepare the financial statements, nor does it state the auditor’s opinion as to whether the financial statements give a true and fair view (or are presented fairly, in all material respects) in accordance with that financial reporting framework.</td>
<td>The CGA program to provide annual accounts in the IPSAS format needs to be established reliably. The timetable and program for the implementation of the newly adopted Financial Audit Manual needs to be specified to accord with the availability of auditable accounts. The Manual is aimed at forming an opinion on the truth and fairness of the financial statements so that the Auditor General can sign an opinion in accordance with ISA 700. The audit methodology specifies how the audit work can be planned to meet the confidence level that is implicit in the audit opinion, and identify the level and extent of audit testing required in order to express that opinion.</td>
</tr>
<tr>
<td>17. Does the consideration of fraud and error in an audit of financial statements accord with international standards?</td>
<td>Partly. Audits focus on examining transactions for discrepancies and regulatory breaches. Much of the reporting seems to relate to fraudulent behavior and suggesting recoveries without exposing the facts in detail.</td>
<td>The testing needs to be more statistically based. Forensic audit training is needed to categorize the observation as either a mistaken violation or a deliberate and intentional act to take undue benefit.</td>
</tr>
<tr>
<td>18. Are the Auditor General’s reports made public?</td>
<td>Apparently. But only after tabling in the Parliament and consideration by the Public Accounts Committee. The legislation does not specifically require publication.</td>
<td>The audit legislation should formally provide for reports to be made public, and publicly available when tabled in the Parliament.</td>
</tr>
<tr>
<td>19. Is the process for taking action on audit recommendations sufficiently effective to meet international standards?</td>
<td>Partly. Improved audit, Public Accounts Committee, and departmental administrative processes are needed for follow-up of audit reports. There is an enormous backlog by the Public Accounts Committee in reviewing the audit observations. Effective review of the backlog is becoming increasingly impossible.</td>
<td>Improved audit methodology and report writing on the one hand and reform of the fundamental processes for scrutiny on the other, are required to reduce this backlog.</td>
</tr>
</tbody>
</table>
8. The Commercial Audit Wing of the Auditor General Pakistan should perform a stronger review role for the compliance with International Accounting Standards and International Financial Reporting Standards (IAS/IFRS) by the state-owned enterprises. Since the financial statements of many of the state-owned enterprises (SOE) are not audited by the Auditor General of Pakistan, there are transparency issues relating to the use of public funds in these enterprises that may not be subjected to legislative scrutiny by the Public Accounts Committee. The reasons include, but are not limited to, the lack of capacity in the office of the Auditor General to coordinate and review the work of the external auditors of these enterprises. There is a need for specialized training in the use of international accounting and auditing standards, and in using the work of other auditors. Many of the state-owned enterprises are outside the IAS/IFRS and other financial reporting and enforcement regimes of the Securities and Exchange Commission of Pakistan and the State Bank of Pakistan. Those state-owned enterprises registered by the Securities and Exchange Commission of Pakistan should be audited by professional accounting firms that are selected by, and report through the Auditor General. There is a need for the DAGP Commercial Audit Wing (after it is strengthened) to review all state-owned enterprises for IAS/IFRS compliance. In addition, the Corporate Finance Wing in the Ministry of Finance, whose responsibility is to do more general monitoring, will be strengthened under a proposed capacity-building project. This project, funded by the World Bank, has not yet started.

9. Continue to improve public financial management through the reform program. Public financial management relies on a comprehensive and timely accounting and financial reporting system. This system should be supported by a professional audit function that assures competency and reliable information within the system. Current enforcement of adequate compliance with financial regulations in the general budget sector and corporate governance in the public enterprise sector falls short of satisfactory performance. The Country Financial Accountability Assessment for Pakistan concluded that there are significant challenges remaining within the country’s public financial management reform agenda to improve the effectiveness and productivity of public spending. Ongoing reforms and capacity-building measures will help to strengthen performance in the PFM arena. Accountability based on the formal adoption of international accounting and auditing standards is a timely step for the Government of Pakistan to take now. And the implementation of these standards needs to be supported by a more comprehensive PFM reform program to achieve substantial positive impact. The PIFRA II is covering most of the required reform elements. The Finance Division has issued in September 2006 a memorandum covering a new system of financial control and budgeting which includes inter alia the specific duties and responsibilities of Principal Accounting Officers, Chief Finance and Accounts Officers, and Financial Advisers. Economy and regularity are the two main principles to be observed.

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5 Establishment Division O.M. No F.3(2) Exp. III/2006 dated 13/9/2006
10. **Improve accounting and auditing skills of the Pakistan Accounts and Audit Service.** For bringing about improvements in compliance with international standards there is a need for properly trained staff. Current programs are providing strong support in this area. The success will depend on how well the strategies are implemented.

**I. Introduction**

1. This assessment of public sector accounting and auditing is generally meant to help implement a more effective public financial management (PFM) through better quality accounting and public audit processes in Pakistan and to provide greater stimulus for more cost effective outcomes of government spending. More specific objectives are: (a) to provide the country's accounting and audit authorities and other interested stakeholders with a common, sound knowledge as to where local practices stand in accordance with international standards of financial reporting and auditing; (b) to assess the prevailing variances; (c) to chart paths for improving the accordance with international standards; and (d) to provide a continuing basis for measuring improvements.

2. As part of the general support program in South Asia for assessment and improvement of public sector accounting and auditing, the World Bank, with the cooperation of member governments, is conducting a Review of Public Sector Accounting and Auditing Practices in member countries. In conducting this assessment, a set of diagnostic questionnaires [developed to be consistent with the context of the PFM Performance Measurement Framework used by the Public Expenditure and Financial Accountability (PEFA) Program], was used to gather substantial insight into country performance with regard to the external auditing and financial statement reporting PFM indicators. Annex A discusses the methodology used for conducting the assessment in this report.

3. The diagnostic questionnaire was used to gather information on national standards and practices for accounting, financial reporting, and auditing in the government budget sector and in the state-owned enterprise (SOE) sector. Conducted in cooperation with country authorities, the diagnostic questionnaires incorporate the principles contained in the public sector accounting and auditing standards promulgated by the International Federation of Accountants (IFAC) and the International Organization...
of Supreme Audit Institutions (INTOSAI). Annex B summarizes the international accounting and auditing frameworks that were used in this assessment. The responses to these questionnaires stimulated further discussions among the World Bank team and senior staff in the offices of the Auditor General of Pakistan (AGP) and Controller General of Accounts (CGA). These discussions examined accounts and audit reports and working papers as a means to jointly explore the quality of processes and products.

4. The maintenance system for public accounts in Pakistan is long standing. Since 1997, the World Bank Project for Improvement of Financial Reporting and Auditing (PIFRA) has supported the comprehensive reform efforts by the Government of Pakistan to streamline its accounting and auditing systems and procedures, while developing the institutional and individual capacities for better public financial management. The initial reforms included some separation of audit and accounts activities through promulgation of legislation relating to separate roles for the Auditor General and the Controller General of Accounts. They also included designing modern accounting and auditing processes and devising a comprehensive human resource management plan. The replacement of inefficient manual and outdated accounting processes in the general government sector by faster and updated computerized programs (using the accounting software package SAP R/3) is underway with a program to computerize all district accounting offices by the end of 2007. Annex C includes excerpts from Pakistan auditing and accounting legislation.

5. The second phase of the PIFRA project, PIFRA II, will help the government to build capacity to improve the accuracy, comprehensiveness, reliability, and timeliness of intra-year and year-end government financial reports at federal and provincial levels. The PIFRA II will also initiate the process at district and sub district levels thereby strengthening the financial accountability cycle. The project would therefore directly support the commitment of the Government of Pakistan in improving public financial management, accountability, and transparency, and enhance the capacity of public sector managers to meaningfully use credible financial information for better and informed decision-making. It will facilitate public oversight of the use of public monies, and increase the national and international credibility of the national and provincial governments’ financial statements and assurance processes.

6. The reform efforts need to include identification of the relevant international standards of accounting and auditing applicable to the public sector and help achieve compliance with those standards. Adoption of International Public Sector Accounting Standards (IPSAS) for accounting and financial reporting and the IFAC-issued International Standards on Auditing (ISA) in addition to the INTOSAI Auditing Standards are important steps in improving the basis for adequate public financial management.

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8 PIFRA II has 4 core components: (a) financial accounting and budgeting systems, (b) capacity building for the office of the Auditor General of Pakistan, (c) capacity building for the office of the Controller General of Pakistan, and (d) project management.

II. Public Sector Accounting

A. Institutional Framework for Public Sector Accounting

7. The institutional framework for public sector accounting should include adherence to international accounting standards and use of qualified accounting staff to provide timely, relevant, and reliable financial information that is needed to support all fiscal and budget management, decision-making, and reporting processes. The diagnostic questionnaires, which were used in this assessment, have collected information on the current arrangements and the apparent gaps in Pakistan for accounting laws and regulations; education and training of public sector accountants; application of a code of conduct; and numbers and characteristics of public sector accountants.

(1) Accounting Laws and Regulations

8. The Constitution of Pakistan delineates the authority of the Auditor General of Pakistan for prescribing the form, principles, and methods of accounts of the Federation and of the Provinces with the approval of the President. Under these conferred powers, the Auditor General has endorsed the Accounts Codes (Volume I to IV) and a New Accounting Model (NAM) for implementation when practicable. The PIFRA project is computerizing the accounting functions to enable the New Accounting Model to be implemented. Accounting functions are the responsibility of the Controller General of Accounts.

9. A committee should be setup to review and steer the process of implementation of IPSAS on a progressive basis. The committee should have oversight of the financial reporting specialists in steering the adoption of IPSAS towards the accrual basis of accounting. The NAM development in 1998 used the IFAC-issued Guidelines for Governmental Financial Reporting and best practice from other countries. There is now an opportunity to apply the IPSAS, that have been developed since 1998, in the New Accounting Model and review the accounting model during its implementation. The Auditor General of Pakistan and Controller General of Accounts have already been engaged in deliberations to move towards adopting IPSAS. The

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12 The New Accounting Model sets the national standards of accounting and financial reporting. Pricewaterhouse Coopers analyzed differences between IPSAS and the New Accounting Model in 2004. The New Accounting Model is being implemented using the cash basis of accounting and will gradually move towards the accrual basis. Formal adoption of IPSAS would enable the customization of the NAM financial reporting formats in compliance with relevant IPSAS requirements.
adoption of IPSAS II cash flow formats is a step in this direction. The NAM Financial Reporting Manual provides for such reporting, which generally complies with Cash Basis IPSAS. This reporting also includes the optional disclosure requirements that are required to accord with IPSAS, such as third party payments and receipts that need to be identified and shown in a separate column. State-owned enterprise results should be consolidated into the annual accounts. Annex D discusses the benefits of accrual basis of reporting.

10. **The PIFRA project is supporting the implementation of the New Accounting Model.** Institutional and individual capacities in both the public sector financial management agencies, as well as the executive/service delivery formations are being developed through implementation of a comprehensive capacity development program mainly sponsored by PIFRA. The PIFRA project is supporting the implementation of the New Accounting Model through the implementation of computer accounting hardware and software application to all district accounts offices.

11. **(2) Education and Training**

The Audit and Accounts Training Institute (AATI) is a countrywide network providing professional training in public financial management to both accounting and executive arms of the government. The AATI conducts long-term courses that lead to the Pakistan Institute of Public Finance Accountants (PIPFA) certification. The AATI also conducts short courses for professional development.

12. **The AATI has included the use of IPSAS in its course work.** Through the technical assistance provided under the PIFRA, AATI has revitalized its syllabi and learning methodologies. It is now geared to teach areas of practical application, including IPSAS. The AATI has developed a comprehensive annual training program and has set targets for the first year.

13. **Offering international education standards will help to develop more professional audit and accounting staff.** The strategy is to offer learning opportunities to develop qualifications that are compliant with the IFAC International Education Standards (IES) and acceptable to other professional accountancy bodies. The AATI has been cooperating with professional accountancy bodies to seek acceptance of AATI qualifications that would meet the qualifications for professional accreditation of other professional bodies — the Association of Chartered Certified Accountants (ACCA), UK;

13 Notification of financial reporting policy, dated June 29, 2005, adopts Cash Basis IPSAS with a trial implementation of the policy for FY2004-05 and effective date in FY2005-06.

14 The annual financial statements consists of the following: (a) statement of assets and liabilities, (b) statement of revenues and expenditures (by function and by object), (c) statement of cash flows, (d) notes to financial statements, (e) summary of appropriation accounts by grants and appropriation, (f) appropriation accounts by economic function and department/division (g) appropriation accounts by grant, and (h) analysis of revenue by division/department.

15 The PIPFA is a body of professional accountants and an associate member of the International Federation of Accountants. It is a joint initiative of the Auditor General of Pakistan, the Institute of Chartered Accountants of Pakistan, and the Institute of Cost and Management Accountants of Pakistan.
Institute of Chartered Accountants of Pakistan (ICAP); and Institute of Cost and Management Accountants of Pakistan (ICAMP).

14. The selection and training of government accountants differs from one departmental cadre to another, and falls short in ensuring the qualifications essential for providing competent professional accounting service in the public sector. The bachelor of commerce/accounting is the minimum academic requirements for an individual seeking to work in the departmental cadre of public sector accountants. However, the inter-departmental cadre civil servants do not require such qualifications; they are recruited as generalists through the Federal Public Service Commission. These inter-departmental officers are given nine-months of probationary training at the AATI and are encouraged to take further specialist training. Nevertheless, this approach continues to fail to provide for competent professional accounting service, equivalent to that provided by the private sector with its ICAP requirements.

(3) Code of Conduct

15. A code of ethics should be included in staff contracts. The INTOSAI Code of Ethics has been adopted by the Auditor General of Pakistan and should be followed by staff doing audits and maintaining accounts. The same has been included in the AATI syllabus. As such, the code of ethics is part of the overall guidance provided by the head of an organization to each staff member. Non-compliance of the code could lead to actions in accordance with Efficiency and Discipline Rules of the Government of Pakistan. The code of ethics should be made a part of staff contracts upon acceptance of a job, or separately signed by the employees as a legally enforceable document.

(4) Public Sector Accountant Arrangements

16. Duality of control over accounting staff should be resolved. With the exception of a few departmentalized accounts, the Government follows a regime of centralized accounting offices that keep accounts of all departments in their regional jurisdiction. Out of 10,000 staff posted in the accounts offices, 921 staff members are employed by the federal government. The remaining staff comes mainly from the treasury services under the provincial finance departments. These provincial offices serve under the technical supervision of the Accountant General who is responsible to the Comptroller of General Accounts; but treasury staff is answerable to the Secretary of Finance of the relevant province. This duality of control over the accounting staff remains a problem of administration and authority and needs to be resolved.

17. Budget officers (chief financial officer) should be adequately qualified to maintain internal financial control. The budget officers should have the qualifications

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16 Some adaptations and deletions were made by a committee constituted by the Auditor General of Pakistan in connection with issuing the INTOSAI Code of Ethics and Auditing Standards. Only one paragraph relating to political neutrality (paragraph 21) was deleted from the Code of Ethics and minor changes of nomenclature were made.
to undertake responsibility for maintaining systems of internal financial controls that manage risks, and for preparing regular financial management reports for the principal accounting officer.\(^\text{17}\) The principal accounting officer is generally supported by a budget officer from within that line agency. These agency staff members require substantial training to equip them with the necessary tools of financial management to effectively assist the principal accounting officers. New positions of Chief Finance and Accounts Officers (CFAO) have been introduced under the system of financial control and budgeting introduced in September 2006. The system specifies that the CFAO shall be a well-trained and experienced officer. It is important that the Establishment Division which is to arrange the postings of these officers, ensures that this requirement reflects the expertise needed for the function.

18. Internal audit units should be established as per staffing and operational planning developed under PIFRA. Under PIFRA, a comprehensive plan was developed to initiate the internal audit function in government agencies for which a center of excellence is envisaged within the office of the Comptroller of General Accounts. Chief audit officers have been posted in 15 federal ministries with responsibilities for internal audit, reconciliation of accounts, coordination with departmental and parliamentary Public Accounts Committees, and the financial propriety of expenditure and receipts. More funding should be arranged to enable an effective internal audit function as per the staffing and operational plans developed under PIFRA.

B. Accounting Standards as Practiced

19. The diagnostic questionnaires collected information on the current arrangements and the apparent gaps in Pakistan for setting public sector accounting standards, and for presenting financial reports.

(1) Setting Public Sector Accounting Standards

20. In the existing format of the finance and appropriation accounts, there are considerable departures from Cash Basis IPSAS. Gradually the budget sector is being converted to the NAM Chart of Accounts. Conversion to the NAM reporting framework is dependent on the roll-out of the PIFRA accounting systems and the implementation of all the accounting functions. Pensions, general provident fund, and asset accounting are examples of functional modules yet to be implemented. Government accounts are presented in the old formats of the finance and appropriation accounts.

(2) Presenting Financial Reports

21. Use of the cash basis of financial reporting provides a necessary scope to the implementation of the New Accounting Model. One particularly useful feature of

\(^{17}\) The principal accounting officer is usually the secretary of a ministry or head of the line department.
the Cash Basis IPSAS format is the disclosure of third party payments in separate columns on the face of the statement of cash receipts and payments. These disclosures enable users to identify the total amount of payments made; the purposes for which they were made; and whether, for example, the payments were made from amounts allocated or appropriated from general revenue or from special purpose funds or other sources. A case in point within the government sector is the payment of the electricity utility, WAPDA, by the central government, which then deducts these payments at source from its transfers to provincial governments. Provincial governments in turn deduct at source from transfers to local governments. As provincial and local governments are not well-notified of these deductions (as would be required in meeting Cash Basis IPSAS), they become a source of confusion and inefficiency. The government entities are unaware of their power costs and hence less likely to seek ways to be more economical. Also, as bills are already “paid,” there is less incentive for the utility to ensure that its records reconcile with customers’ records.

22. Table 1 identifies the current position and steps required if the Cash Basis IPSAS were to be adopted.

<table>
<thead>
<tr>
<th>Requirements</th>
<th>Current deficiencies</th>
<th>Activity required to adopt Cash Basis IPSAS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial statements presented in IPSAS</td>
<td>The Pakistan reporting structure focuses on consolidated fund and public accounts and the Cash Basis IPSAS for financial statements is not followed.</td>
<td>A statement of cash receipt and payment as per the Cash Basis IPSAS can be prepared using existing information from the accounting records. Also, for each entity (i.e., ministry and department), an additional statement in accord with Cash Basis IPSAS can be prepared. This may require some restructuring of the NAM computerized reporting formats.</td>
</tr>
<tr>
<td>Information required in accordance with IPSAS in the statement of cash receipts and payments</td>
<td>All this information is available on the government reporting system, but is in formats inconsistent with IPSAS. Some negative balances are appearing in the finance accounts. The cash balance appearing in the financial statements is not reconciled with the bank accounts and receivables are appearing from bodies that no longer exist.</td>
<td>This work requires restructuring of the reporting formats and rectification of errors in recording and compiling the accounts. Third party payments would be shown separately in the Cash Basis IPSAS format.</td>
</tr>
<tr>
<td>Accounting policies and explanatory notes</td>
<td>Statements of accounting policy are not provided in the budget or accounts documents.</td>
<td>There is a need to state the accounting policies for various elements of the financial statements and the basis on which the accounts are prepared.</td>
</tr>
<tr>
<td>General considerations</td>
<td>At present financial statements are not available within 6 months of the reporting period; cash balances that are available for use and cash</td>
<td>It would be necessary to reduce the reporting lag; and to disclose further information. Legislation should enforce specific timelines for the publication of</td>
</tr>
</tbody>
</table>

18 It is understood that changes in the financial reporting formats would not be considered as a departure from the new structure of accounting policies and practices as approved by the Auditor General with the consent of the President.
### Requirements

<table>
<thead>
<tr>
<th>Current deficiencies</th>
<th>Activity required to adopt Cash Basis IPSAS</th>
</tr>
</thead>
</table>
| information about the entity  
- presentation of comparative information | balances that are subject to external restrictions and un-drawn borrowing facilities are not disclosed, and presentation does not meet certain transparency requirements. Although the authorization date is mentioned on the accounts, it is not clear when these financial statements become accessible to the general public or media. | annual audited financial statements of the government. |
| Correction of errors disclosed  
- nature of error  
- amount of correction  
- comparative information restated | The nature of errors in prior periods, the amount of the correction, and the fact that comparative information has been restated, or that it is impracticable to do so, is not disclosed. | Further training and better supervision of accounts officers would be needed to correctly classify expenditures and disclosure of errors rectified prior to the reporting period and restatement of comparative information where practicable. |
| Consolidated financial statements | The government budget sector is a reporting entity, as well as an economic entity. | A statement of cash receipt and payment as per the Cash Basis IPSAS can be prepared. Further steps will be needed to include controlled entities as per IPSAS and Section 7(b) of the CGA Ordinance. |
| Treatment of foreign currency cash receipts, payments, and balances treated in compliance with IPSAS | The government largely follows IPSAS except for the disclosure aspects in respect of accounting treatment of foreign currency. | Need to comply with the disclosure aspects of the accounting and financial reporting treatment of foreign currency. |
| Effective date of IPSAS Part I and transitional provision compliance. | The government has not formulated a migration path and timeline for achieving Cash Basis IPSAS, Part I, compliance. | Need for the Auditor General to formally adopt IPSAS and for the CGA to prepare an implementation plan and timeline setting out specific steps to be taken, including disclosure, if necessary, of application of the transitional provision (i.e., full compliance achieved within 3 years) for reporting periods beginning on a date within 3 years of first adoption of IPSAS. |

| C. Assessment of Accounting and Auditing in State-Owned Enterprises |

23. **It should be mandated by law that the financial statements of the state owned enterprises be prepared in accordance with the IAS/IFRS.** Many state-owned enterprises are registered under the Company Law. Under the Companies Ordinance
1984, it is obligatory for all listed companies to present their financial statements in accordance with IAS/IFRS. These companies are required under the Companies Ordinance to be audited by a chartered accountant. The Institute of Chartered Accountants in Pakistan has mandated the observance of International Standards on Auditing by its members. Upon receipt from the IFAC, exposure drafts of proposed International Standards on Auditing are sent to ICAP members for comments. These comments are returned for consideration by IFAC. When the final standard is issued, ICAP adopts the International Standard on Auditing without modification. For non-listed companies, the implementation and enforcement of IAS/IFRS is not finalized. Enforcement of International Standards on Auditing for the audit of non-listed companies is less stringent than that for the listed companies. State-owned enterprises, which are not incorporated under the Company Law, do not usually apply IAS/IFRS for accounting and financial reporting. The financial statements are generally audited after a long lag time.

24. **There are serious issues relating to the use of public funds in state-owned enterprises that are not subjected to legislative scrutiny by the Public Accounts Committee.** A review of a sample of financial statements of state-owned enterprises that are audited by Chartered Accountants indicated that the audit reports generally contained either significant qualifications and/or emphasis of matter paragraphs modifying the audit opinion. The Auditor General of Pakistan while conducting the regularity or performance audit cannot utilize the qualifications given in the audit report on the financial statements. The Auditor General does not have access to the management letter given by the external auditors to the state-owned enterprises, nor do they have access to the financial audit working papers. Thus serious issues relating to the use of public funds are not subjected to legislative scrutiny by the Public Accounts Committee through consideration of the Auditor General’s reports. The preferable practice is for the Auditor General to be able to review the working papers and reports of the contracted audit firms.

25. **There is a need for specialized training in the utilizing of IAS/IFRS, ISA, and using the work of other auditors.** The resources for auditing public sector enterprises in the DAGP are in short supply; and DAGP staff generally is not adequately trained in accounting. The need for additional specialized training in the applications of IAS/IFRS and ISA and using the work of other auditors has been recognized as a need. Greater provision of this training could be provided perhaps through the AATI or outsourced to the private sector institutions.

26. **The Commercial Audit Wing of the Auditor General of Pakistan should perform a monitoring role for the compliance of IAS/IFRS by state-owned enterprises.** Monitoring of state-owned enterprises needs improvement. There is currently no Public Sector Enterprises Monitoring Board as established in other countries. This role is performed by the Corporate Wing of the Ministry of Finance. Some proposals

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19 The Report of Observance of Standards and Codes – Accounting and Auditing in, Pakistan, 2005, provides the implementation status of IAS IFRS and related issues.

are in place for strengthening the Corporate Wing. There is little involvement of the Auditor General in the selection of the external auditors of these state-owned enterprises. The respective ministries/departments with which individual state-owned enterprises are attached exercise varying levels of monitoring on these bodies. Many of these state-owned enterprises are outside the enforcement mechanisms (of IAS/IFRS and other financial reporting) by the Securities and Exchange Commission of Pakistan and the State Bank of Pakistan. Hence, there is a need for the Commercial Audit Wing of the Auditor General of Pakistan to be strengthened to perform a more comprehensive review role for the compliance of IAS/IFRS by state-owned enterprises.

III. Public Sector Auditing

A. Statutory Framework for Public Sector Auditing

27. Effectual scrutiny by the legislature to ensure effective implementation of fiscal and expenditure policies needs comprehensive and competent external audits that are underpinned by international standards on auditing. The environment for an effective Supreme Audit Institution (SAI) requires a comprehensive approach to public financial management. Supreme Audit Institutions are not stand-alone institutions. They are part of a PFM architecture that includes budgeting, accounting, internal control, audit and legislative oversight, and government response. Improving the way the supreme audit institution functions is integral to providing information for improving the overall PFM system. But the action must be within the executive branch yet under the watchful eyes of the legislature and the public. A strong demand for good public sector external auditing is necessary for the supreme audit institution to have any impact. This requires willingness of the executive branch to accept and respond to external scrutiny over its management of funds and to ensure that reform action is taken. It also requires public presentation of the audit reports to ensure public support for effective action. All of these requirements are covered by the INTOSAI and IFAC auditing standards listed in Annex B. These should be adopted by the Auditor General of Pakistan. The Government noted in its response to the draft report that the statutory framework included considerations of the Constitution and that it was not appropriate to compare with the frameworks of other countries as the frameworks reflect the choices made by the people of each country. Recognizing this, the report does not make comparisons between country’s Constitutions; rather it identifies how the Constitution for Pakistan or other elements of the legal statutory framework make provision for the auditing principles that are set out in INTOSAI guidance.

28. The diagnostic questionnaires have collected information describing current arrangements and the apparent gaps in the country in the following areas:

21 Although there is a requirement to get approval of the selected auditor’s (CA) name, in many cases it is not observed. Even with compliance, in practice management finalizes the selection of the audit firm, a practice that throws into question the independence of these auditors.

22 Scope, quality, and follow-up of external audit is performance indicator No. 26 in the PFM Performance Measurement Framework supported by the World Bank and other development agencies.
Institutional framework for the Supreme Audit Institution,
Process for setting auditing standards,
Use of code of ethics or conduct,
Arrangements to ensure accountability in the Supreme Audit Institution,
Arrangements to ensure independence,
Arrangements to ensure adequate skills and qualifications for the auditors,
Arrangements for providing training,
Arrangements to ensure auditor competence,
Arrangements for quality assurance.

29. Those areas with significant scope for improvement are discussed below.

(1) Statutory Framework

30. The Auditor General’s Ordinance 2001 requires some improvements. The Auditor General is appointed under provisions stipulated in the Constitution of Pakistan 1973 (as amended). The Auditor General’s (Functions, Powers and Terms and Conditions of Service) Ordinance 2001 details the mandate, role, and powers of the Auditor General of Pakistan. The Ordinance requires some improvements to remove jurisdictional limitations on the AGP mandate: (a) make an explicit mention of the proprietary, efficiency, effectiveness, and economy in the use of public funds; and (b) provide for necessary dissemination arrangements for the audit reports.

31. The Auditor General of Pakistan should have the authority to conduct a full range of audits for all government-owned or -controlled entities. The Auditor General has full authority for auditing all budget sector receipts and expenditures from all government accounts, including defense expenditures. The Auditor General has the authority to audit any body or authority established by the government, or which has received a loan or grant; however, there are some exclusion clauses allowed for, in the Constitution as well as in the Auditor General’s Ordinance. Article 169(b) of the Constitution limits the powers and function of the Auditor General in relation to any authority or body established by the government depending on the provisions contained in the respective legislation establishing that authority body. Similarly, Sections 9 (explanation), 11 (proviso), 15, and 16 of the Ordinance impose certain conditions on the powers and function of the Auditor General in relation to the audit of public sector enterprises. These jurisdictional limitations are under review; potential revision of the Ordinance to remove the restrictive or exclusion clauses is underway by a committee of the Auditor General, Secretary Finance, and Secretary Law. The Public Accounts Committee of the Parliament is pursuing this issue.

32. The Auditor General of Pakistan should have the authority to conduct a full range of audits, including regularity, financial, and performance audits. The

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There are minor exclusions of practice relating to receipts kept as local funds or so called non-public funds by some institutions.
Auditor General’s (Functions, Powers and Terms and Conditions of Service) Ordinance, 2001 specifies the following types of audits:

- Section 7, Certification Audit (Accounts)
- Section 8, Regularity Audit
- Section 9, Audit of Authorities having loans or grants from public money
- Section 12, Audit of Receipts
- Section 8 & 9, Receipts and Expenditures (includes authorities and bodies substantially financed by loans and grants)
- Section 10, Study reports (which may include performance, governance, debt-management, or environment)
- Section 15, Audit of Companies and Corporations established under the public sector.

33. There is no explicit mention of the proprietary, efficiency, effectiveness, and economy of use of public funds in the Auditor General’s Ordinance, yet many of the senior staff categorized these as the main objectives of the AGP audit. The proposed review of the Ordinance to resolve jurisdictional issues should also look into providing for a specific mandate of the Auditor General in relation to proprietary, economy, efficiency, and effectiveness of utilization of public funds along the lines of the model legislation proposed by the UNDP or the ACCA.²⁴

34. The legislation should clearly set out penalties and their appropriate application in the event of noncompliance with auditing requirements. Section 14 of the Auditor General’s Ordinance applies to any person or authority hindering the audit functions of the Auditor General with regard to inspection of accounts; this person or authority shall be subject to disciplinary action under relevant Efficiency and Discipline Rules, as applicable to their actions. Section 14 does not mention who would initiate such an action. Either the Auditor General, Public Accounts Committee, Public Accounting Officer, or another body could potentially initiate the action. Consequently, the implementation of this section could be problematic. In case of any hindrance or problem, the Public Accounts Committee generally issues directives to the executives with regard to compliance of auditing requirements. This process is lengthy and subject to many delays thereby reducing the effectiveness of the provision. The Auditor General should have specific powers to initiate action against persons who refuse to provide auditable accounts and relevant records to the DAGP staff.

35. Necessary dissemination arrangements for the audit reports should be clearly laid down in the legislation. The legislative scrutiny is not supported by public scrutiny due to un-disseminated audit reports and government financial statements. There is confusion as to when audit reports and government financial statements become public documents. Specific provisions in the Auditor General’s Ordinance should make public

²⁴ Section 21 of the Model Law developed by the UNDP Program for Accountability and Transparency (PACT); and Sections 32 and 55 of A Model National Audit Office Act, The Association of Chartered Certified Accountants, UK, 2004.
the audit reports and other documents in line with the ACCA model legislation as follows:25

- All reports issued by the Auditor General shall be considered public documents when the reports are presented to Parliament. As public documents they shall be made available to the public for a minimal cost-recovery fee.
- The Auditor General may make his/her reports publicly available in electronic format on the Internet.
- The Auditor General shall provide copies of his/her published reports to the government archivist, all public and university libraries (in relevant locations); National Broadcasting Corporation; and the press.
- The Auditor General or his/her staff may provide comments and interviews to the press or other media on the subject of any published audit reports.

(2) Setting Auditing Standards

36. **The IFAC-issued International Standards on Auditing should be formally adopted, preferably by way of mention in the Financial Audit Manual.** There is an Audit Code which lays down the basic principles of auditing in line with the Constitutional provisions and the Auditor General’s (Functions, Powers and Terms and Conditions of Service) Ordinance 2001. The Auditor General of Pakistan adopted the INTOSAI Auditing Standards in 2002 with minor adaptations. The INTOSAI Auditing Standards form the basis of the auditing methodology and process for the office of the Auditor General of Pakistan. This methodology and process is further explained in the Procedure for Certification Audit of Appropriation and Finance Accounts prepared by the Auditor General. The Auditor General has approved the new Financial Audit Manual which would gradually replace the current procedures.26 The INTOSAI recognizes that the INTOSAI Auditing Standards are broad in nature and that the IFAC-issued International Standards on Auditing provide another level of detail for public sector audit guidance. The INTOSAI is working with IFAC in the longer term to develop practice notes to assist with implementation of each ISA in the public sector. Therefore, explicitly prescribing the IFAC standards as the applicable auditing standards in addition to the INTOSAI Auditing Standards would ensure that the relevant developments in the auditing process are learned and applied on a continuous basis.

37. **A committee should be set up to review and adopt the International Standards on Auditing on a continuous basis.** It has been construed from various provisions of the legislation, including Section 22 of the Auditor General’s Ordinance 2001, that the Auditor General would be the standard-setting authority for the public sector auditing. As an active member of INTOSAI, the Auditor General usually

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26 Chapter 4 of Financial Audit Manual mentions that the INTOSAI Auditing Standards have been considered as the general framework for the auditing methodology and procedures. Although the new Financial Audit Manual does not mention specifically the International Standards on Auditing, the overall approach and methodology is consistent with them.
subscribes to the declarations of the international organization for implementation with regard to transference to the local setup and environment. Therefore, the INTOSAI Auditing Standards were adopted. The adoption process consisted of a review of the INTOSAI Code of Ethics and Auditing Standards by a committee of senior officers assembled by the Auditor General. A similar committee should review and adopt the IFAC-issued International Standards on Auditing for effect on a continuous basis. It would be useful to include on this committee representation from the Institute of Chartered Accountants of Pakistan, which is in the process of adopting ISA compliance by its members. The process of ISA adoption should start with input at the exposure draft stage and continue through to issuing practical guidance on local application of the International Standards on Auditing. Pakistan has nominated persons to the Reference Panel of the INTOSAI Working Group on Financial Audit Guidelines, which is a subcommittee of the INTOSAI Auditing Standards Committee. The Government can similarly nominate persons for an ISA-adoption committee under the jurisdiction of the Auditor General, as per his/her authority under the Constitution, (Section 170).

(3) Code of Ethics

38. Improved monitoring for adherence to the Code of Ethics is needed, as well as review by the Controller General of Accounts. The INTOSAI Code of Ethics, which was prepared for auditors, was adopted by the Auditor General of Pakistan in 2002 to be followed by the DAGP audit staff and the CGA staff responsible for maintenance of accounts. Some minor adaptations and deletions were made while issuing the INTOSAI Code of Ethics and Auditing Standards to make them compatible with the local setup and environment. There is a need for taking practical steps to ensure compliance with the Code of Ethics. These steps might include guidance from the procedural mechanisms included in the IFAC Code of Ethics for Professional Accountants and review of the INTOSAI Code by the Controller General of Accounts to compare the ICAP Code for relevance for accountants.

(4) Ensuring Independence

39. Notwithstanding the limitations identified earlier, the legislation provides a strong enabling environment where the Auditor General of Pakistan can perform its scrutiny functions with considerable independence. The Constitution guarantees the protection of service of the Auditor General of Pakistan. Similarly, the charged expenditures of the DAGP are not subject to Parliamentary vote, therefore protecting the DAGP budget. Section 19 of the Auditor General’s Ordinance gives the Auditor General full powers to incur expenditures within the budgetary provisions. As the head of a civil service cadre, the Pakistan Audit and Accounts Service, the Auditor General has substantial control over personnel and over the Audit and Accounts Training Institute, a powerful internal training and professional development mechanism. The overall status of the Auditor General ensures the independence of the position and an effective organization within the DAGP by virtue of the Auditor General’s constitutional mandate; protection of term in office; financial and human resource independence; exercise of authority over the type of, schedule, and duration of audit; powers to examine records;
direct liaison with the parliamentarians in the Public Accounts Committee; and INTOSAI representation. However, the Auditor General does have some limitations regarding managing staffing. In order to create new posts, the Auditor General must negotiate with the Ministry of Finance/government, which in practice does not considerably infringe on the AGP independence. However, the recruitment of civil servants in the Pakistan Audit and Accounts Service is done through the Federal Public Service Commission, an arrangement that has significant expertise issues.

40. The AGP term of office is secure. The Auditor General of Pakistan is appointed by the President of Pakistan and his oath is administered by the Chief Justice of Pakistan. The AGP term of office is 5 years or until the attainment of 65 years of age by the incumbent, whichever is earlier. The Auditor General is secure in this position throughout the term and can carry out mandates without fear of retribution. Once appointed, the Auditor General can only be removed by reference of the Supreme Judicial Council and affirmed by majority vote in the Parliament (the same procedure for removing a Supreme Court judge). Therefore, even the appointing authority does not have the termination powers. Re-appointment is not allowed before two years after vacating the office, thereby limiting opportunities for re-appointment. The UNDP model legislation recommends a 12-year term, and the ACCA recommends appointment to retirement age of 65. The Government noted in its response to the draft report that it considered that the Constitutional guarantees sufficed and that a longer term was not needed.

41. The Auditor General’s Ordinance sets the AGP’s right to access information and obligation to report to the President. The Section 14 of the Auditor General’s Ordinance 2001 indicates the powers of the Auditor General in connection with access to all offices having accounts and other related documents and some guidance on how to deal with any person hindering the audit functions. Article 171 stipulates that the Auditor General shall submit reports to the President who in turn delivers the same to the Parliament. The Parliament sends these reports to the Public Accounts Committee for detailed scrutiny. There has never been an amendment to any audit reports after being submitted to the President.

42. Before submission to the President, there is ample opportunity for the executive to resolve the audit observations through holding of (Special) or Departmental Accounts Committee meetings or simply by taking administrative action as recommended in the Audit Information Report. Nevertheless, the resolution of issues often does not occur.

43. The audit reporting requirements need to be made more specific. Section 7 of the Auditor General’s Ordinance 2001 relates to the certification audit. This section assigns responsibility to the Auditor General for certifying accounts on the basis of the AGP audit for each financial year and presenting corresponding notes, comments, or recommendations related to those accounts. The Ordinance does not specify the timeline for submission of the certified annual accounts. Similarly, the Ordinance does not require the Auditor General to submit an annual report on his/her performance. Section 7 states the minimum audit requirements from the Auditor General as the certification of
annual accounts. The Auditor General must plan to have available the resources needed to conduct the certified audit and know how much time can be allocated to other types of audits in a year in addition to the mandatory certification of accounts. The PIFRA is trying to achieve an integration of the certification and regularity audit by introducing more concurrent audit activities focusing on regularity and compliance as part of the certification audit. This would also lead to a timely certification of the accounts and meaningful and complete representation sent to the legislature.\(^\text{27}\)

44. **Legislation should provide an environment in which the Auditor General is free to meet with the media on audit reports.** In Pakistan, unlike in other countries, the audit report is never discussed with the media. The only point in time when the press gets formal acknowledgement of an audit report is when the Public Accounts Committee deliberates on the audit observations. The model legislation for Supreme Audit Institutions reads, “The Auditor General or his/her authorized staff may provide comments and interviews to the press or other media on the subject of any published audit reports.”\(^\text{28}\)

45. **There are some issues which can hamper the independence of the audit staff on individual assignments.** The separation of audit and accounts has resolved the independence issue to some extent. However the rotations of assignments, including deputations to other departments and back to audit offices, need to be reviewed. Similarly, the dependence on the auditee organizations for providing logistics can affect the highest level of independence. It is preferable to adopt the IFAC Code of Ethics with regard to procedures for enhanced independence as required by rotation of assignments and nominal dependency for logistics on some auditees.

46. **Improved processes of the Public Accounts Committee and departmental administrations are needed for following up audit reports.**\(^\text{29}\) Despite many opportunities, resolution of audit observations frequently does not occur before submission of reports to the President and subsequent review by the Public Accounts Committee. This suggests an apparent indifference by senior departmental managers. It is important that there be certainty that audit observations are dealt with seriously by the legislature and the central agencies, such as the Ministry of Finance. This lack of resolution at the audit stage has led to an enormous backlog by the Public Accounts Committee in hearing the audit observations. Improved audit methodology and report writing, and reformation of the fundamental processes for scrutiny need to be undertaken to reduce this backlog. Better protocols may be useful between the Auditor General and various departments to ensure that auditor access is made easy and disruption in departments is kept at a minimum. In addition, better protocols would help ensure that

\(^{27}\) There is a lack of connection between certification and regularity audit reporting. The certification audit gives partial compliance in the form of "can be relied upon" subject to both qualifications contained therein, as well as the issues reported elsewhere in regularity audit reports. The certification audit reports are seldom discussed by the Public Accounts Committee thereby limiting the general dissemination/availability and use of the government financial statements by the stakeholders.


\(^{29}\) *Legislative scrutiny of external audit reports* is performance indicator No. 28 in the PFM performance measurement framework supported by the Bank and other development agencies.
draft audit reports are reviewed quickly by the departments for accuracy and fairness and that the Auditor General and departments, as far as possible, reach an agreement on reports before they are made public. Similar protocols are needed between Parliament and the Auditor General covering, for example, how the audit reports will be handled. An audit-observation tracking system is being implemented under PIFRA II, which would improve the post-audit accountability system. However, the primary responsibility of follow-up of actions is with the Public Accounts Committee secretariat that is closely coordinated by the Auditor General for compliance with its part of directives/recommendations. The Auditor General does not have statutory power for imposing sanctions directly.

(5) Accountability in the Supreme Audit Institution

47. The Office of the Auditor General of Pakistan should be accountable for its performance and report to the legislature. The Inspection, Regulation, Vigilance, and Monitoring of the Training Wing are independent branches of the Office of the Auditor General of Pakistan, which performs its functions under a Deputy Auditor General. This function is a kind of internal audit within the Office of the Auditor General that conducts inspections of all activities, including field audit offices. It is the intended good practice of the Office of the Auditor General to prepare an annual report each year, but other priorities interrupt meeting the schedule. The last annual report was published for 2002. The Corporate Audit Plan (2001-2002) contained the vision and mission statement that was reinterpreted into the annual audit plan. An annual report for the year 2004 is still under preparation and a 3-year plan is in the process of being written. The Office of the Auditor General does not undergo peer review or an independent performance audit, nor does any independent external body audit its activities. However there are interconnected arrangements for audits within the field audit offices that provide peer review assurance within the organization. The Office of the Auditor General should undergo an accountability mechanism in line with that suggested under the proposed legislation for Supreme Audit Institutions involving review of the annual corporate plan and annual report by the Public Accounts Committee. The Office of the Auditor General should prepare and disseminate its annual corporate plan, as well as the annual performance report of its office in a timely manner.

(6) Qualifications and Skills for the Auditors

48. The AATI should continue to review its syllabus in order to cover all areas recommended by IFAC-issued International Educational Standards (IES). In an effort to meet the AATI and higher academic and professional qualifications, an elaborate system of training of accounting and auditing staff at different hierarchical levels exists at

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30 Although the Public Accounts Committee writes "directives" for its decisions, many stakeholders perceive in line with the decision of NWFP High Court declaring these as "recommendations," which are subject to voluntary compliance by the executive.
local and foreign universities and professional training bodies. The Auditor General has developed a comprehensive training plan. The PIPFA qualification has become mandatory for audit officers. The syllabi of AATI probationers have been revamped. A substantial portion of funding in PIFRA II has been earmarked for auditing and accounting training. All these factors contribute to the enhancing of the qualifications and skills of the auditors. The AATI should ensure that all IES-recommended areas are covered by all training providers and in all training material.

(7) Training

49. **Despite good training opportunities available for auditing staff, further upgrading is needed.** The AATI annual training plan provides many opportunities for their continuing professional development. The training plan encompasses more than 50 different short courses or workshops. Civil servants are required to take 12 working days of mandatory training. Allocating certain training days in each annual audit plan is good practice for time budgeting. Rigorous capacity-building exercises are being identified, designed, and delivered as part of PIFRA II. There are currently too few auditors with ICAP qualifications in the Office of the Auditor General. These auditors must have adequate professional expertise and technical knowledge to carry out the certification audits and to recommend that the Auditor General sign audit opinions. The current AATI arrangements are not yet adequate to meet international standards for auditing annual accounts and signing audit opinions. Further upgrading of AATI courses and of promotion criteria for senior audit staff is needed.

(8) Auditor Competence

50. **The new Financial Audit Manual should be implemented.** The development of a new Financial Audit Manual for auditing the financial statements of federal and provincial governments was outsourced to foreign consultants under PIFRA. The consultants have developed the guidelines and the methodologies with the help of the Accounting Policy Wing, which would be responsible for future maintenance and updating of the Manual. In addition, the Office of the Auditor General through PIFRA procured an audit department management system with modules for audit planning and implementation, risk assessment, personnel management, and recommendation tracking. An action plan for implementation of the new Financial Audit Manual is needed for an effective FY2004-05 and FY2005-06 audit. The implementation of the new Financial Audit Manual should be linked to the capacity-building and computerization activities.

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33 The Audit Command Language software has been acquired for computer-assisted audit techniques and applied on some transaction data in SAP R/3 systems in accounting offices.
(9) Quality Assurance

51. Audit documentation and report writing for quality assurance needs improvement. Supervision occurs at the field audit office level where the Director General personally certifies the quality of audit reports; there is further review at the Deputy Auditor General level for quality assurance. Finally there is a Quality Assurance Review Committee at the Office of the Auditor General of Pakistan, which reviews all audit reports before their release. This process needs to be supported by formal mechanisms and adequate working papers as per ISA 220, Quality Control for Audit Work. The new Financial Audit Manual (Chapters 5 to 15) describes in detail the procedures for direction, supervision, and review of audit work. The World Bank’s project team was not able to review recent audit reports because they had not been made public. Therefore, scrutiny of this important area is incomplete and inadequate in this assessment.

B. Auditing Standards as Practiced

52. The diagnostic questionnaires have collected information about the current arrangements for the audit methodology and the apparent gaps in the country in the following areas:

- audit planning,
- audit supervision,
- reviewing internal controls,
- reviewing compliance with laws,
- ensuring adequate audit evidence is collected,
- analyzing whether the financial statements accord with accounting standards,
- preparing audit opinions,
- reporting on fraud, and
- reporting on compliance.

Out of this exercise came recommended activities that will help bring local standards in line with international standards.

(1) Audit Planning

53. The planning process should collect information about the audited entity. Certification audit procedures suggest that the audit staff prepare work flow, procedure diagrams, or systems outlines, and list the main accounting areas in order to be familiarized with the audited entity; however, this does not include risk assessment and determination of materiality levels, which are more or less pre-defined by the procedures. The procedures define the objectives of each of the six audit areas: establishment costs, contingencies, pensions, receipts, general provident funds, and accounts compilation. The objectives are not refined in accordance with risks of understatement, overstatement,
or misstatement that can be associated with any of the audit areas; and audit tests are not accordingly articulated. Internal audit function is evaluated as part of the regularity audit. However, since internal audit in government departments is in its infancy, the certification audit does not place reliance on the internal audit.

54. **Engagement of chartered accountants, as part of the audit teams for conducting of certification audit, can build skills.** The planning documents currently prepared do not identify specific risks. The new Financial Audit Manual should introduce more comprehensive planning requirements based on the specific objectives of the audits. Engagement of chartered accountants as part of the audit teams for conducting certification audit can be very helpful in skill development. The memorandum of understanding between the Auditor General of Pakistan and the Institute of Chartered Accountants of Pakistan may be utilized for procuring such services with ICAP quality assurance support. The Government’s response to the draft report noted that in addition to these interactions the DAGP is partnering with the international bodies INTOSAI, ACCA, and IIA.

(2) **Audit Supervision**

55. **When implementing the new Financial Audit Manual, the supervisory staff—including the Director and the Deputy Director—should test and demonstrate the new audit methodologies in the presence of field audit teams.** The current supervision process generally concentrates on reviewing the findings of the audit team and documentation of the audit evidence, and referencing and sequencing of the audit working papers; less emphasis is placed on involvement in the field work and on the overall assurance levels achieved. The shift should be made toward the risk-based audit approach. In the risk-based audit approach, the auditor minimizes risk through applying judgment in the design and conduct of field testing in order to provide the required assurance that the financial statements provide a true and fair view.

(3) **Reviewing Internal Management Control Procedures**

56. **The new audit methodology and process should be rolled out immediately to improve environmental risk assessment, compliance testing, and sampling.** The existing certification audit procedures are mechanical and do not provide the requisite flexibility to the auditor to exercise judgment and innovation in achieving a higher degree of assurance. The techniques used for compliance testing and sampling need improvement. For example, the results of compliance testing have limited impact on the sample size for the substantive procedures, and the results of the compliance testing are seldom used to tailor the selection of sample transactions based on an identified pattern of errors. Therefore, the new audit methodology should be rolled out as early as possible without waiting for the implementation of the New Accounting Model and

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34 An Internal Audit Plan and Internal Audit Manual were developed under PIFRA I, and chief audit officers posted in 15 ministries have been given the exposure training.
computerization of the accounting systems. An audit methodology should answer the following points:

- What is the audit confidence level?
- What are the requirements for audit planning, audit work papers, and audit reporting?
- How is audit materiality determined, and what is an acceptable level of audit risk and confidence?
- How is an appropriate mix of audit work developed to address the audit risks?

57. The audit should be completed by a process that provides information on how audit errors are summarized and evaluated against audit materiality.

**(4) Audit Evidence**


**(5) Analyzing Financial Statements**

59. The transaction-based financial statements provide some limited scope for financial analysis that is useful for the audit. The auditor’s ability to perform and use the various analyses of financial statements is hampered when these lack meaningful and reliable information with respect to assets or liabilities balances. However, analysis of the ratios of one expenditure head to another head, comparison of variations of expenditures over time, and relationships among financial and non-financial information (e.g. number of staff to payroll) can provide useful indicators of possible errors.

**(6) Reporting on Financial Statements**

60. There should be a reference to the financial reporting framework used when preparing financial statements (including identifying the country of origin of the framework when the IAS framework is not used). There is no specific reference to the reporting framework in any procedures in use in Pakistan. The only mention relates to the provisions of Section 5(a) of the Controller General of Account Ordinance 2001 when read with the Article 169 of the Constitution. The IPSAS should be identified as the relevant financial reporting framework in the audit certificate once the accounts are prepared in this form.

61. The audit certificate should completely comply with the specimen formats given in the Financial Audit Manual and procedures being followed. The opinion
paragraph gives an expression that the financial statements "can be relied upon." This is not consistent with the specimen audit reports given in the Procedures for the Certification Audit, which requires stating that "the accounts are complete and accurate in all material aspects."

62. The audit report should be a stand-alone document giving complete assurance on the financial statements and should not refer to other reports. The certification audit report makes mention of the other AGP reports covering aspects of financial governance or economical, efficient, and effective utilization of public resources, which are submitted separately to the President. These reports provide information relating to weaknesses in the system of financial control or accounting, in addition to those mentioned in audit comments annexed to the audit certificate. The details of all such referenced AGP reports mentioned in the audit certificate on the financial statements should be reattached to the audit certificate for a complete analysis.

(7) Reporting on Fraud

63. Forensic audit training is needed. The Supreme Audit Institution does not focus on fraud in a sufficiently systematic way. Much of the reporting seems to relate to fraudulent behavior and to suggest recoveries without detailing the facts. The ISA 240, *The Auditor's Responsibility to Consider Fraud and Error in an Audit of Financial Statements*, requires the auditor to obtain information that is used to identify the risks of material misstatement due to fraud; to evaluate the design of the entity’s related controls, including relevant control activities; and to determine whether they have been implemented. The auditing standard also requires the auditor to inform the auditee’s management and the Board, if there is one, of any fraud and failure in internal control that led to the fraud. The auditor’s report should identify the action that the entity is taking about the fraud. The Auditor General on special request may cooperate with other government agencies, like the National Accountability Bureau, on specific incidence of fraud.

(8) Reporting on Compliance

64. The audit should be understood as a tool for gradual improvement in the control systems and processes over time. The general tendency is for the audit to cover and report on all compliance issues confronting an organization instead of emphasizing the most critical issues. The audit report can add significant value if the auditors focus on more critical issues with impact on the organization and recommend ways to resolve those issues.
### IV. Action Plans

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<tr>
<th><strong>Accounting Standards Issue</strong></th>
<th><strong>Current status</strong></th>
<th><strong>Action to be taken to move towards international standards</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Has the Public Sector Accounting Law adopted IPSAS?</td>
<td>Partially. The notification of the adoption of the IPSAS-2 cash flow reporting format as part of the overall reporting requirements of the government is a step in the right direction.</td>
<td>NAM needs to be reviewed and streamlined to ensure that the policies and procedures contained therein are consistent with and have references to IPSAS.</td>
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<tr>
<td>2. Does the education and training of accountants accord with IES?</td>
<td>Partly. A comprehensive training strategy is directed toward the professionalization of accounting staff through IES-compliant qualifications.</td>
<td>As training programs are revised, the International Education Standards will be the basis for further revisions required.</td>
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<tr>
<td>3. Does the ICAB Code of Ethics match international standards?</td>
<td>Yes. The Auditor General has adopted INTOSAI Code of Ethics.</td>
<td>This will be implemented through more regular training.</td>
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<tr>
<td>4. Is there a body to prescribe public sector accounting standards?</td>
<td>Yes. The Constitution of Pakistan delineates the authority of the Auditor General of Pakistan to prescribe the form, principles, and methods of accounts of the Federation and of the Provinces with the approval of the President.</td>
<td>The AGP considers that the Constitution empowers the AGP to prescribe public sector accounting standards, and that currently this is sufficient.</td>
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<tr>
<td>5. Are the financial statements in accord with the IPSAS standard?</td>
<td>Partly. The Cash Basis IPSAS for financial reporting is not yet followed, nor is the accrual-based IPSAS. The CGA has the responsibility for preparing and maintaining the accounts of the Federation, the Provinces and district governments. The CGA also lays down the principles governing internal financial control but certain accounting offices still remain with the provincial governments.</td>
<td>Work is in progress on both the cash flow statements and budget to actual</td>
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<td>6. Is the statement of cash receipts and payments in IPSAS form?</td>
<td>No. A basic statement of cash receipts and payments is provided but this information is currently presented in formats inconsistent with the IPSAS.</td>
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<td>7. Are accounting policies and explanatory notes required?</td>
<td>No. Statements of accounting policies are not provided in the budget or accounts documents.</td>
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<td>8. Are other disclosures in accord with IPSAS?</td>
<td>Partly. Financial statements are not available within 6 months of the reporting period; some items are not</td>
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<td>9. Does the government issue a consolidated financial statement which consolidates all controlled entities?</td>
<td>No.</td>
<td>A Committee will be formed to study the issue and make recommendations on the best way forward to achieving this. The July 2007 Workshop to be conducted by the World Bank for the CGA establishment will follow-up on this.</td>
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<tr>
<td>1. Is the SAI statutory framework in accord with the needs of the INTOSAI Auditing Standards?</td>
<td>Partially. Some additional powers need to be established by legislation as set out below.</td>
<td>Some revisions in the Auditor General Ordinance 2001 are being considered in respect of district audits. Adequate mandate and other issues as specified in point number 6 below also need to be examined.</td>
</tr>
<tr>
<td>2. Is there a body to prescribe public sector auditing standards?</td>
<td>Yes. It has been construed from various provisions of legislation, including Section 22 of the Auditor General Ordinance 2001 that the Auditor General would be the standard-setting authority for public sector auditing. Thus, the Auditor General adopted INTOSAI Auditing Standards as recommended by a committee of senior officers in the DAGP.</td>
<td>The AGP considers that the law empowers the AGP to prescribe public sector accounting standards, and that currently this is sufficient.</td>
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<tr>
<td>3. Have INTOSAI and IFAC audit standards been adopted?</td>
<td>Partly. The Auditor General has adopted INTOSAI Auditing Standards.</td>
<td>A decision has been made to adopt the ISAs as per the INTOSAI standard setting processes by which the ISAs will be incorporated into the International Standards of Supreme Audit institutions.</td>
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<tr>
<td>4. Has a code of ethics equivalent to the INTOSAI Auditing Standards been adopted?</td>
<td>Yes</td>
<td>Current actions are considered to be sufficient.</td>
</tr>
<tr>
<td>5. Is the accountability process in the SAI in accord with INTOSAI Auditing Standards?</td>
<td>Yes</td>
<td>Current actions are considered to be sufficient.</td>
</tr>
<tr>
<td>6. Does the SAI legal framework meet the INTOSAI Auditing</td>
<td>Largely.</td>
<td>Improved legislation excluding limits on jurisdiction, mandate, and function, providing improved offence and</td>
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<tr>
<td>Standards for independence and powers?</td>
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<td>immunity clauses and requiring enhanced disclosure of audit conclusions are to be considered.</td>
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<tr>
<td>7. Does education and training of auditors accord with INTOSAI and IES?</td>
<td>Partly. Staff needs more professional training.</td>
<td>The AATI will continue to review its syllabus to cover all areas recommended by the IFAC educational standards.</td>
</tr>
<tr>
<td>8. Is the SAI equipped with the audit methods and technologies to meet the INTOSAI Auditing Standards?</td>
<td>Yes. Though not fully implemented at the moment.</td>
<td>Improved methodologies are being implemented. Technology to support a management information system for the Auditor General is not in place at present. The requirements are being acquired through PIFRA. The implementation plan will review capacity for implementing the new Financial Audit Manual.</td>
</tr>
<tr>
<td>9. Does the SAI have the quality assurance programs to meet international standards?</td>
<td>Partly. Internal quality assurance and supervision provide review arrangements among the field audit offices.</td>
<td>Improved working paper guidance and computerization combined with more effective supervision and more independent quality review processes are being implemented as per the FAM. This will be supported through establishing a function of quality management in the DAGP.</td>
</tr>
<tr>
<td>10. Does the process of planning the audits meet international standards?</td>
<td>Partly. Improved methodologies are being implemented.</td>
<td>The audit process as per the FAM will be risk-based allowing sufficient flexibility to the auditors to articulate and apply appropriate audit procedures on methodically selected samples to arrive at representative audit conclusions.</td>
</tr>
<tr>
<td>11. Does the process of supervising the audits meet international standards?</td>
<td>Partly. Working paper systems and audit methodologies do not currently enable effective supervision. Improved methodologies are being implemented under PIFRA.</td>
<td>The revised working paper structure should be implemented together with the new Financial Audit Manual for audit supervision.</td>
</tr>
<tr>
<td>12. Does the process to evaluate the reliability of internal control meet international standards?</td>
<td>Partly. Improved methodologies are being implemented.</td>
<td>The methodology is to be more risk- and -systems based as per the FAM.</td>
</tr>
<tr>
<td>13. Does the process used in audits to assess compliance with laws meet international standards?</td>
<td>Partly. Improved methodologies are being implemented.</td>
<td>The methodology is to be risk- and -systems based and PIFRA is to review whether the audit planning arrangements may be revised so that some regularity audit aspects are integrated as per the FAM with the annual certification audit, and other aspects are carried out using performance audits.</td>
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<tr>
<td>14. Does the audit process used to obtain evidence to support conclusions meet international standards?</td>
<td>Partly. The evidence to support audit criticisms on individual transactions is generally better than that available to provide the more general audit assurance on the summary figures in the financial statements.</td>
<td>More rigorous plans for audit testing are being implemented as per the Financial Audit Manual. The evidence for audit assurance is to be organized as per FAM requirements.</td>
</tr>
<tr>
<td>15. Does the audit analyze the financial statements to establish whether acceptable accounting standards for financial reporting and disclosure are complied with?</td>
<td>Partly. The existing structure of the financial statements only provides limited scope for financial analysis that is useful for the certification audit.</td>
<td>The implementation of IPSAS for the annual accounts as per plans set out above will improve the DAGP’s ability to carry out meaningful and reliable financial analysis because the accounting policies and reporting will be in accordance with international norms and standards.</td>
</tr>
<tr>
<td>16. Does the auditor prepare an audit opinion on the financial statements in a form that accords with international standards?</td>
<td>Not fully at this stage. The Auditor General signs an opinion on the accounts; but because the financial statements are not prepared in accordance with adequate standards, the wording of the audit opinion does not contain all of the requirements of ISA 700, The Auditor’s Reports on Financial Statements. The wording does not clearly indicate the financial reporting framework used to prepare the financial statements, nor does it state the auditor’s opinion as to whether the financial statements give a true and fair view (or are presented fairly, in all material respects) in accordance with that financial reporting framework.</td>
<td>The timetable and program for the implementation of the newly adopted Financial Audit Manual is to be specified in detail and broad timetables have been established under the PIFRA project. The FAM is aimed at forming an opinion on the truth and fairness of the financial statements so that the Auditor General can sign an opinion in accordance with ISA 700. The FAM audit methodology specifies how the audit work can be planned to meet the confidence level that is implicit in the audit opinion, and identify the level and extent of audit testing required in order to express that opinion. The AGP intends to issue the opinion for the 2005-06 federal accounts as per ISA 700.</td>
</tr>
<tr>
<td>17. Does the consideration of fraud and error in an audit of financial statements accord with international standards?</td>
<td>Partly. Audits focus on examining transactions for discrepancies and regulatory breaches. Much of the reporting seems to relate to fraudulent behavior and suggesting recoveries without digging out the facts in detail.</td>
<td>The testing is to be more statistically based as per FAM. Forensic audit training is needed under PIFRA to improve the ability of the audit staff to categorize the observation as either a mistaken violation or a deliberate and intentional act to take undue benefit.</td>
</tr>
<tr>
<td>18. Are the Auditor General’s reports made public?</td>
<td>Apparently. But only after tabling in the Parliament and consideration by the Public Accounts Committee. The legislation does not specifically require publication.</td>
<td>The audit legislation should formally provide for reports to be made public, and publicly available when tabled in the Parliament with appropriate immunity arrangements for the auditors.</td>
</tr>
<tr>
<td>19. Is the process for taking action on audit recommendations sufficiently effective to meet international standards?</td>
<td>Partly. Improved audit, Public Accounts Committee, and departmental administrative processes are needed for follow-up of audit reports. There is an enormous backlog by the Public Accounts Committee in</td>
<td>Improved audit methodology and report writing are in process so as to improve the report contents. Changes to the processes for departmental and parliamentary review processes will improve timeliness in scrutinizing and</td>
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<td>reviewing the audit observations. Effective review of the backlog is becoming increasingly impossible.</td>
<td>reporting on audit reports, and separately activities are being planned to reduce the backlog of unresolved audit objections.</td>
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Annex A. Methodology of the Assessment

As part of the general support program in South Asia for assessment and improvement of public sector accounting and auditing against international standards, the World Bank, with the cooperation of member governments, is conducting the Review of Public Sector Accounting and Auditing Practices in member countries. The development of the PFM Performance Measurement Framework by the Public Expenditure and Financial Accountability (PEFA) Program has opened the way for a diagnostic tool to be developed that is referenced to the accounting and auditing standards of the International Federation of Accountants (IFAC) and the International Organization of Supreme Audit Institutions (INTOSAI), and other relevant international benchmarks. This exercise provides substantial insight into country performance in regard to the external auditing and financial statement reporting financial management indicators.

A set of 6 questionnaires were used to collect relevant information on country practices:

1. **The public sector accounting environment**—collecting basic information about financial laws and standards-setting arrangements, educational requirements for accountants compared with IFAC International Education Standards, ethical requirements compared with the IFAC Code of Ethics for Professional Accountants.

2. **Public sector accounting practices for the general budget sector if using the cash basis of accounting**—compared with the requirements of the Cash Basis International Public Sector Accounting Standards (IPSAS).

3. **Public sector accounting practices for the general budget sector if using the accrual basis of accounting**—compared with the IPSAS requirements that govern accrual reporting for the public sector.

4. **Public sector auditing environment** compared with the provisions of the INTOSAI Code of Ethics and the INTOSAI general standards.

5. **Public sector auditing practices** compared to the requirements of the INTOSAI field standards and reporting standards, and the IFAC International Standards on Auditing.

6. **Accounting and auditing practices for state-owned enterprises** compared with the requirements of the International Financial Reporting Standards (IFRS) and International Standards on Auditing that govern commercial reporting.

The responses to the diagnostic questionnaires, prepared by the relevant country authorities with the help of in-country experts retained by the World Bank, are supplemented by a due diligence review conducted by members of a World Bank task team.

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[35] The PFM Performance Measurement Framework has been developed as a contribution to the collective efforts of many stakeholders to assess and develop essential PFM systems, by providing a common pool of information for measurement and monitoring of PFM performance progress, and a common platform for dialogue.

[36] The PEFA Program is a partnership among the World Bank, the European Commission, the UK’s Department for International Development, the Swiss State Secretariat for Economic Affairs, the French Ministry of Foreign Affairs, the Royal Norwegian Ministry of Foreign Affairs, the International Monetary Fund and the Strategic Partnership with Africa. A Steering Committee, comprising members of these agencies, manages the Program. A Secretariat is located in the World Bank in Washington, DC.
Various documents are examined as part of the review, including relevant laws, codes of conduct, national accounting and auditing standards, accountant selection and promotion processes, training needs assessments, accountancy training course outlines, curricula and accreditation methods, sample accounts, and sample audit reports and working paper sets.

A country report on the assessment is prepared for each country and reviewed by an expert panel of advisors before examination by the World Bank country team. The draft is then shared with the Government for response before finalization. Discussions will also be held with the relevant stakeholders to devise an implementation plan to address the way forward with a view to minimize variances from international standards.
Annex B. Accounting and Auditing Standards

This annex contains a summary of the frameworks that have been used for the public sector accounting and auditing assessment.

The International Accounting Standards Board (IASB), the International Federation of Accountants (IFAC) and the International Organization of Supreme Audit Institutions (INTOSAI) are cooperating in setting international standards for accounting and auditing.

The IASB is an independent, privately funded accounting standard-setter based in London, UK. The Board members come from nine countries and have a variety of functional backgrounds. In the public interest, IASB is committed to developing a set of high quality, understandable, and enforceable global accounting standards that require transparent and comparable information in general purpose financial statements. In addition, the IASB cooperates with national accounting standard-setters to achieve convergence in accounting standards around the world. The IASB issued International Accounting Standards (IAS) from 1973 to 2000. Since 2000, they have issued International Financial Reporting Standards (IFRS).

IFAC has its headquarters in New York, USA and comprises 163 member bodies, mainly the national professional accountancy bodies of most countries around the world. The IFAC Board established the International Public Sector Accounting Standards Board (IPSASB) to develop high quality accounting standards for use by public sector entities around the world in the preparation of general purpose financial statements. These are the International Public Sector Accounting Standards (IPSAS). The full text of Standards and Exposure Drafts currently on issue is available at http://www.ifac.org/publicsector. The first 20 IPSAS are based on IAS to the extent appropriate for the public sector. IFAC also has established the International Auditing and Assurance Standards Board (IAASB) to prepare and promulgate International Standards on Auditing (ISA) and is now working in cooperation with INTOSAI on preparing public sector guidance on the use of ISA.

INTOSAI includes the Auditors General from almost all national government audit departments around the world and has its Secretariat in the Vienna offices of the Auditor General of Austria. Its Auditing Standards Committee, chaired by the Auditor General of Sweden, produces the INTOSAI Code of Ethics and Auditing Standards, a set of standards at a higher and more generic level than the IFAC-issued ISA. The Auditing Standards Committee is working with the IAASB to prepare practice notes explaining the application of each ISA in the public sector.37

The various standards are listed on the following pages.

International Public Sector Accounting and Education Standards

International Public Sector Accounting Standards

IPSAS 1, *Presentation of Financial Statements*
IPSAS 2, *Cash Flow Statements*
IPSAS 3, *Net Surplus or Deficit for the Period, Fundamental Errors and Changes in Accounting Policies*
IPSAS 4, *The Effects of Changes in Foreign Exchange Rates*
IPSAS 5, *Borrowing Costs*
IPSAS 6, *Consolidated Financial Statements and Accounting for Controlled Entities*
IPSAS 7, *Accounting for Investments in Associates*
IPSAS 8, *Financial Reporting of Interests in Joint Ventures*
IPSAS 9, *Revenue from Exchange Transactions*
IPSAS 10, *Financial Reporting in Hyperinflationary Economies*
IPSAS 11, *Construction Contracts*
IPSAS 12, *Inventories*
IPSAS 13, *Leases*
IPSAS 14, *Events After the Reporting Date*
IPSAS 15, *Financial Instruments: Disclosure and Presentation*
IPSAS 16, *Investment Property*
IPSAS 17, *Property, Plant and Equipment*
IPSAS 18, *Segment Reporting*
IPSAS 19, *Provisions, Contingent Liabilities and Assets*
IPSAS 20, *Related Party Disclosures*
IPSAS 21, *Impairment of Non-cash Generating Assets*
Cash Basis IPSAS, *Financial Reporting under the Cash Basis of Accounting*

International Education Standards

IES 1, *Entry Requirements to a Program of Professional Accounting Education*
IES 2, *Content of Professional Accounting Education Programs*
IES 3, *Professional Skills*
IES 4, *Professional Values, Ethics and Attitudes*
IES 5, *Practical Experience Requirements*
IES 6, *Assessment of Professional Capabilities and Competence*
IES 7, *Continuing Professional Development*
IES 8, *Competence Requirements for Audit Professionals*
International Financial Reporting Standards
and Accounting Standards

IFRS 1, First-time Adoption of International Financial Reporting Standards
IFRS 2, Share-based Payment
IFRS 3, Business Combinations
IFRS 4, Insurance Contracts
IFRS 5, Non-current Assets Held for Sale and Discontinued Operations

IAS 1, Presentation of Financial Statements
IAS 2, Inventories
IAS 7, Cash Flow Statements
IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors
IAS 10, Events After the Balance Sheet Date
IAS 11, Construction Contracts
IAS 12, Income Taxes
IAS 14, Segment Reporting
IAS 16, Property, Plant and Equipment
IAS 17, Leases
IAS 18, Revenue
IAS 19, Employee Benefits
IAS 20, Accounting for Government Grants and Disclosure of Government Assistance
IAS 21, The Effects of Changes in Foreign Exchange Rates
IAS 23, Borrowing Costs
IAS 24, Related Party Disclosures
IAS 26, Accounting and Reporting by Retirement Benefit Plans
IAS 27, Consolidated and Separate Financial Statements
IAS 28, Investments in Associates
IAS 29, Financial Reporting in Hyperinflationary Economies
IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions
IAS 31, Interests in Joint Ventures
IAS 32, Financial Instruments: Disclosure and Presentation see also: See also Financial Instruments - other issues
IAS 33, Earnings per Share
IAS 34, Interim Financial Reporting
IAS 36, Impairment of Assets
IAS 37, Provisions, Contingent Liabilities and Contingent Assets
IAS 38, Intangible Assets
IAS 39, Financial Instruments: Recognition and Measurement see also: See also Financial Instruments - other issues
IAS 40, Investment Property
IAS 41, Agriculture
INTOSAI Code of Ethics and Auditing Standards

**Code of Ethics**

**Integrity.** Auditors have a duty to adhere to high standards of behavior (e.g. honesty and candidness) in the course of their work and in their relationships with the staff of audited entities.

**Independence, objectivity and impartiality.** The independence of auditors should not be impaired by personal or external interests. There is a need for objectivity and impartiality in the work and the reports, which should be accurate and objective. Conclusions in opinions and reports should be based exclusively on evidence obtained and assembled in accordance with the SAI’s auditing standards.

**Professional secrecy.** Auditors should not disclose information obtained in the auditing process to third parties except for the purposes of meeting the SAI’s statutory responsibilities.

**Competence.** Auditors must not undertake work which they are not competent to perform.

**Basic Postulates for Auditing Standards**

(a) The SAI should consider compliance with the INTOSAI auditing standards in all matters that are deemed material. Certain standards may not be applicable to some of the work done by SAI's, including those organized as Courts of Account, nor to the non-audit work conducted by the SAI. The SAI should determine the applicable standards for such work to ensure that it is of consistently high quality.

(b) The SAI should apply its own judgment to the diverse situations that arise in the course of government auditing.

(c) With increased public consciousness, the demand for public accountability of persons or entities managing public resources has become increasingly evident so that there is a need for the accountability process to be in place and operating effectively.

(d) Development of adequate information, control, evaluation and reporting systems within the government will facilitate the accountability process. Management is responsible for the correctness and sufficiency of the form and content of the financial reports and other information.

(e) Appropriate authorities should ensure the promulgation of acceptable accounting standards for financial reporting and disclosure relevant to the needs of the government, and audited entities should develop specific and measurable objectives and performance targets.

(f) Consistent application of acceptable accounting standards should result in the fair presentation of the financial position and the results of operations.

(g) The existence of an adequate system of internal control minimizes the risk of errors and irregularities. It is the responsibility of the audited entity to develop adequate internal control systems to protect its resources. It is also the obligation of the audited entity to ensure that controls are in place and functioning to help ensure that applicable statutes and regulations are complied with, and that probity and propriety are observed in decision making. The auditor should submit proposals and recommendations where controls are found to be inadequate or missing.

(h) Legislative enactments would facilitate the cooperation of audited entities in maintaining and providing access to all relevant data necessary for a comprehensive assessment of the activities under audit.

(i) All audit activities should be within the SAI’s audit mandate.*

(j) Legislative enactments would facilitate the co-operation of audited entities in maintaining and providing access to all relevant data necessary for a comprehensive assessment of the activities under audit.

(k) SAIs should work toward improving techniques for auditing the validity of performance measures.

(l) SAIs should avoid conflict of interest between the auditor and the audited entity.

* The full scope of government auditing includes regularity and performance audit.

**Regularity audit embraces:**

- Attestation of financial accountability of accountable entities, involving examination and evaluation of financial records and expression of opinions on financial statements;
- Attestation of financial accountability of the government administration as a whole;
- Audit of financial systems and transactions including an evaluation of compliance with applicable statutes and regulations;
- Audit of internal control and internal audit functions;
• Audit of the probity and propriety of administrative decisions taken within the audited entity; and
• Reporting of any other matters arising from or relating to the audit that the SAI considers should be disclosed.

**Performance audit entails the audit of economy, efficiency and effectiveness, and embraces:**

- Audit of the economy of administrative activities in accordance with sound administrative principles and practices, and management policies;
- Audit of the efficiency of utilization of human, financial and other resources, including examination of information systems, performance measures and monitoring arrangements, and procedures followed by audited entities for remedying identified deficiencies; and
- Audit of the effectiveness of performance in relation to the achievement of the objectives of the audited entity, and audit of the actual impact of activities compared with the intended impact.

## General Auditing Standards

The auditor and the SAI must be independent.
The auditor and the SAI must possess the required competence.
The auditor and the SAI must exercise due care and concern in complying with the INTOSAI auditing standards. This embraces due care in planning, specifying, gathering and evaluating evidence, and in reporting findings, conclusions and recommendations.

The SAI should adopt policies and procedures to recruit personnel with suitable qualifications.
The SAI should adopt policies and procedures to develop and train SAI employees to enable them to perform their tasks effectively, and to define the basis for the advancement of auditors and other staff.
The SAI should adopt policies and procedures to prepare manuals and other written guidance and instructions concerning the conduct of audits.
The SAI should adopt policies and procedures to support the skills and experience available within the SAI and identify the skills which are absent; provide a good distribution of skills to auditing tasks and assign a sufficient number of persons for the audit; and have proper planning and supervision to achieve its goals at the required level of due care and concern.
The SAI should adopt policies and procedures to review the efficiency and effectiveness of the SAI’s internal standards and procedures.

## Field Standards

(a) The auditor should plan the audit in a manner that ensures that an audit of high quality is carried out in an economic, efficient and effective way, and in a timely manner.

(b) The work of the audit staff at each level and audit phase should be properly supervised during the audit; and documented work should be reviewed by a senior member of the audit staff.

(c) The auditor, in determining the extent and scope of the audit, should study and evaluate the reliability of internal control.

(d) In conducting regularity (financial) audits, a test should be made of compliance with applicable laws and regulations. The auditor should design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the financial statement amounts or the results of regularity audits. The auditor also should be aware of the possibility of illegal acts that could have an indirect and material effect on the financial statements or results of regularity audits.

## Reporting Standards

(a) At the end of each audit the auditor should prepare a written opinion or report, as appropriate, setting out the findings in an appropriate form; its content should be easy to understand and free from vagueness or ambiguity, include only information which is supported by competent and relevant audit evidence, and be independent, objective, fair and constructive.

(b) It is for the Auditor General to decide finally on the action to be taken in relation to fraudulent practices or serious irregularities discovered by the auditors.
# International Standards on Auditing

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Annex C. Pakistan Auditing and Accounting Legislation

(A) The Constitution of the Islamic Republic of Pakistan

169. The Auditor General shall, in relation to -
(a) the accounts of the Federation and of the Provinces; and
(b) the accounts of any authority or body established by the Federation or a Province,
perform such functions and exercise such powers as may be determined by or under Act
of Majlis-e-Shoora (Parliament) and, until so determined, by order of the President.

170. The accounts of the Federation and of the Provinces shall be kept in such form and
in accordance with such principles and methods as the Auditor General may, with the
approval of the President, prescribe.

171. The reports of the Auditor General relating to the accounts of the Federation shall be
submitted to the President, who shall cause them to be laid before the National Assembly
and the reports of the Auditor General relating to the accounts of a Province shall be
submitted to the governor of the Province, who shall cause them to be laid before the
Provincial Assembly.

(B) Auditing Legislation

Extracts from the Auditor General's (Functions, Powers and Terms and
Conditions of Service) Ordinance, 2001

Section 4. Term of Office – The Auditor General shall, unless he resigns earlier or is
removed from office in accordance with the Constitution, hold office for a fixed term of
five years from the date on which he assumes such office or he attains the age of sixty-
years, whichever is earlier…

Section 7. Auditor General to certify accounts. – The Auditor General shall, on the
basis of such audit as he may consider appropriate and necessary, certify the accounts,
compiled and prepared by Controller General of Accounts or any other person .....and
shall submit the certified accounts with such notes, comments or recommendation as he
may consider necessary to the President....

Section 8. Provisions relating to Audit – The Auditor General shall –
(a) audit all expenditures from the Consolidated Fund ....to ascertain whether the
moneys shown in the accounts as having been disbursed were legally available for
and applicable to the service and purpose to which they have been applied....
(b) audit all transactions..
(c) audit all trading, manufacturing, profit and loss accounts and balance sheets and
other subsidiary accounts....
(d) audit, subject to provisions of this Ordinance, the accounts of any authority or
body established ...
Section 9. Audit of receipts and expenditure of holders of authorities substantially financed by loans and grants.

Section 14. Powers of Auditor General in connection with audit of accounts. (1) The Auditor General shall have authority-

(a) to inspect any office of accounts...
(b) to require that any accounts, books, papers...
(c) to enquire or make such observations...

(2) The officer in charge of any office or department shall afford all facilities....
(3) Any person or authority hindering the audit functions or the Auditor General regarding inspection of accounts shall be subject to disciplinary action under relevant Efficiency and Discipline Rules, applicable to such person.

Section 22. Power to make regulations....

(C) Accounting Legislation

Extracts from the Controller General of Accounts (Appointment, Functions and Powers) Ordinance, 2001

Section 4. Controller General of Accounts. – There shall be a Controller General of Accounts who shall be appointed by the President from amongst the officers of the Accounts Group and shall be a PBS 22 officer.

Section 5. Functions of the Controller General. - The functions of the Controller General shall be –

(a) to prepare and maintain the accounts of the Federation, the Provinces and district governments in such form and in accordance with such methods and principles as the Auditor General may, with the approval of the President, prescribe from time to time;
(b) to authorize payments and withdrawals from the Consolidated Fund and Public Accounts...
(c) to prepare and maintain accounts of such organizations and authorities established, set up or controlled by the Federation or Provinces as may be assigned to him by the President or, as the case may be, the Governor of a Province;
(d) to lay down the principles governing the internal financial control for Government departments in consultation with the Ministry of Finance...
(e) to render advice on accounting procedure for new scheme, programmes or activities undertaken by the Government concerned;
(f) to submit accounts compiled by him... to the Auditor General .... within the time-frame prescribed by the Auditor General;
(g) to provide .... information
(h) develop and maintain as efficient system of pension, provident funds and other retirement benefits...
(i) to co-ordinate and ensure resolution of audit observation of the Audit Department with the concerned departments; and
(j) to prescribe syllabus, standards and provide facilities for training of officers and staff under his administrative control.

Section 6. Certain offices to work under the control of the Controller General...

Section 7. Reports. – From the accounts directly kept or maintained by him or by accounts officers subordinate to him, and from the accounts kept and maintained by other entities, including self-accounting entities, the Controller General shall –
(a) prepare each year the appropriation and finance accounts....for submission to the Auditor General....
(b) prepare and submit to the Auditor General for each financial year a Consolidated and General Financial statement ....
(c) ....

Section 12. Power to make regulations. ...
Annex D. Benefits of Accrual Accounting


1.18 The IFAC Public Service Committee has commented extensively on the benefits of accrual accounting for governments and individual public sector entities in previous Studies (Studies 5, 6, 8, 9, 10 and 11) and Occasional Papers (Papers 1, 3, 5, 6 and 7). In order to provide some context for readers who are not familiar with the Public Service Committee’s other publications, this section contains a summary of the benefits of reporting on the accrual basis.

1.19 The information contained in reports prepared on an accrual basis is useful both for accountability and decision-making. Financial reports prepared on an accrual basis allow users to:

- assess the accountability for all resources the entity controls and the deployment of those resources;
- assess the performance, financial position and cash flows of the entity; and
- make decisions about providing resources to, or doing business with, the entity.

1.20 At a more detailed level, reporting on an accrual basis:

- shows how a government financed its activities and met its cash requirements;
- allows users to evaluate a government’s ongoing ability to finance its activities and to meet its liabilities and commitments;
- shows the financial position of a government and changes in financial position;
- provides a government with the opportunity to demonstrate successful management of its resources; and
- is useful in evaluating a government’s performance in terms of its service costs, efficiency and accomplishments.

Financial Position

1.21 Accrual accounting provides information on an entity’s overall financial position and current stock of assets and liabilities. Governments need this information to:

- make decisions about the feasibility of financing the services they wish to provide;
- demonstrate accountability to the public for their management of assets and liabilities recognized in the financial statements;
- plan for future funding requirements of asset maintenance and replacement;
- plan for the repayment of, or satisfaction of, existing liabilities; and
- manage their cash position and financing requirements.

1.22 Accrual accounting requires organizations to maintain complete records of assets and liabilities. It facilitates better management of assets, including better maintenance, more appropriate replacement policies, identification and disposal of surplus assets, and
better management of risks such as loss due to theft or damage. The identification of assets and the recognition of depreciation help managers to understand the impact of using fixed assets in the delivery of services, and encourage managers to consider alternative ways of managing costs and delivering services.

1.23 Accrual accounting provides a consistent framework for the identification of existing liabilities, and potential or contingent liabilities. The recognition of obligations meeting the definition of a liability and the criteria for recognition:

- compels governments to acknowledge and plan for the payment of all recognized liabilities, not just borrowings;
- provides information on the impact of existing liabilities on future resources;
- means that it is possible to allocate responsibility for the management of all liabilities; and
- provides necessary input for governments to assess whether they can continue to provide current services and the extent to which they can afford new programs and services.

1.24 Accrual accounting highlights the impact of financing decisions on net assets/equity and may lead governments to take a longer term view when making financing decisions than is generally possible when relying on cash or modified cash reports. Information on net assets/equity also means that governments may be held accountable for the financial impact of their decisions on both current and future net assets/equity. Changes in an entity’s net assets/equity between two reporting dates reflect the increase or decrease in its wealth during the period, under the particular measurement principles adopted and disclosed in the financial statements. Under the accrual basis of accounting, the financial statements will include a Statement of Financial Position which discloses information about assets and liabilities. Where assets and liabilities are not equal, a residual figure for net assets/equity will be reported. Where this figure is positive it can be interpreted as the net resources that may be applied for the provision of goods or services in the future, and therefore the community’s investment in the reporting entity. Where the figure is negative, it may be viewed as the amount of future taxation or other revenues which are already committed to paying off debt and other liabilities. Net assets/equity can comprise some or all of the following components:

- contributed capital;
- accumulated surpluses and deficits; and
- reserves (for example revaluation reserve; foreign currency translation reserve).

Financial Performance

1.25 Accrual accounting provides information on revenues and expenses, including the impact of transactions where cash has not yet been received or paid. Accurate information on revenues is essential for assessing the impact of taxation and other revenues on the government’s fiscal position, and in assessing the need for borrowing in the long term. Information on revenues helps both users and governments themselves to assess whether current revenues are sufficient to cover the costs of current programs and services.
1.26 Governments need information about expenses in order to assess their revenue requirements, the sustainability of existing programs, and the likely cost of proposed activities and services. Accrual accounting provides governments with information on the full costs of their activities so that they can:

- consider the cost consequences of particular policy objectives and the cost of alternative mechanisms for meeting these objectives;
- decide whether to fund the production of services within government sub-entities, or whether to purchase goods and services directly from non-government organizations;
- decide whether user fees should cover the costs associated with a service; and
- allocate responsibility for managing particular costs.

1.27 Accrual accounting can provide financial information on whether sub-entities are delivering specified services, and delivering them within agreed budgets. The same information, at a more detailed level, can also be used within sub-entities for the management of activity and program costs.

1.28 Accrual accounting allows an individual entity to:

- record the total costs, including depreciation of physical assets and amortization of intangible assets, of carrying out specific activities;
- recognize all employee-related costs and to compare the cost of various types of employment or remuneration options;
- assess the most efficient way of producing their goods and services and of managing the resources over which they have been delegated authority;
- determine the appropriateness of cost-recovery policies; and
- monitor actual costs against budgeted costs.

**Cash Flows**

1.29 Accrual accounting provides comprehensive information on current cash flows and certain projected cash flows, including the cash flows associated with debtors and creditors. It can therefore lead to better cash management and may assist in the preparation of more accurate cash budgets.
Supplemental Table of Standards and Gaps

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<td>A. Assessment of the National Public Sector Accounting Environment</td>
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<td>Timely, relevant, and reliable financial information is required to support all fiscal and budget management, decision-making, and reporting processes.</td>
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<tr>
<td>(1) The Accounting Law</td>
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<tr>
<td>1. For reliability, the requirements for public sector accounting and reporting should be specified by law, cover all government-owned entities, specify the methods by which accounting and auditing standards are to be set for the public sector, specify the reporting requirements and lay down timetables for the publication of audited annual accounts.</td>
<td>The Constitution of Pakistan delineates the authority of the Auditor General of Pakistan (AGP) to prescribe the form, principles, and methods of accounts of the Federation and of the Provinces with the approval of the President. Under these conferred powers, the Auditor General endorsed the Accounts Codes (Volume I to IV) as the accounting conduct. Currently the New Accounting Model (NAM)\textsuperscript{38} is being implemented with the use of SAP R/3 applications.</td>
<td>The public sector accounting is undergoing a comprehensive reform sponsored by the PIFRA project of the World Bank. There is a need to maintain the existing momentum of activities.</td>
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<td>The New Accounting Model covers the accounting guidance related to the budget sector (the federal, provincial and district governments), self-accounting entities and development projects.</td>
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<td>The accounts-maintenance and the audit functions have been separated through assigning the accounts maintenance to the Controller General of Accounts.</td>
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<td>2. Compliance with IPSAS for non-commercial bodies and IAS for commercial bodies is needed for consistent transparency.</td>
<td>Developing a new financial reporting and accounting model in 1999 sought guidance from the provisions of the financial procedures given in the Constitution of Pakistan, the generally accepted accounting standards as suggested in INTOSAI Accounting Standards; IFAC-issued Guidelines for Governmental Financial Reporting, best practices followed in other countries, and essential aspects of the existing system. However, a specific direction to apply IPSAS is neither given in the CGA Ordinance nor in the New Accounting Model. There are serious deliberations in progress to move fully toward IPSAS. The adoption of IPSAS-2 cash flow formats(^{39}) of cash flow statement as recommended in the Cash Basis IPSAS is a positive step toward this objective. The NAM Financial Reporting Manual provides for such reports, which to a large extent comply with the reporting requirements under the Cash Basis IPSAS, including many optional disclosure requirements. However, there are certain deficiencies like non-disclosure of payments/receipts by third parties on behalf of the reporting entity that need to be identified and resolved before the implementation of NAM reporting framework is completed.</td>
<td>A committee should be set up to review and steer the process of implementation of IPSAS on a continuous basis. This may involve adoption of the Cash Basis IPSAS to start with and then gradually adopt the Accrual Basis IPSAS as per the guidance given in the IFAC Public Sector Committee’s Study No. 14 relating to transition toward the accrual basis of accounting. The institutional and individual capacities are lacking in both the public sector financial management agencies, as well as the executive/service delivery formations. These are being overcome through implementation of a comprehensive capacity development program mainly sponsored by the PIFRA. The PIFRA project is supporting the implementation of NAM through the application software which is being gradually rolled out to various districts accounts offices and other sites. Initially the idea is to expand technology-driven financial management throughout the country while keeping the functionality simple and using the cash basis of accounting. Early efforts have resulted in more than 41 productive sites out of 127. This is indicative of the fact that the PFM reforms have entered into an advanced stage.</td>
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\(^{39}\) Notification of financial reporting policy dated June 29, 2005, which states that the adoption of the IPSAS-2 cash basis of financial reporting as part of the annual finance accounts reporting with effect from FY2005-06 and the trial run of implementation of the policy for FY2004-05. The same has been confirmed for implementation by the CGA office in July 2005.
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<td>of implementation with envisioned benefits. The ADB also assists in improving the accounting and financial management of externally financed development projects (and particularly the implementing agencies involved in the earthquake rehabilitation and reconstruction). Steadily the efforts would be redirected toward vertical development through expanded functionalities and integrated financial reporting.</td>
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(2) **Education and Training of Public Sector Accountants**

3. For reliability, the curriculum requirements for the accounting qualifications of public sector accountants should accord with internationally recognized standards of accounting training as established in the International Education Standards for Professional Accountants (IES).

|              | The Audit and Accounts Training Institute (AATI) is a countrywide network providing the essential training in public financial management to both accounting and executive arms of the government. The AATI conducts long-term courses for staff and probationers which lead to PIPFA Certification\(^{40}\) and short term courses for professional development. In case of probationers, the Federal Public Service Commission (FPSC) conducts the independent examinations. In addition, there are many civil servants from the Pakistan Audit and Accounts Service who have earned masters or higher degrees from foreign or local universities. The AATI is seeking exemptions from other professional bodies [including the UK Association of Chartered Certified Accountants (ACCA), Institute of Chartered Accountants of Pakistan (ICAP), and Institute of Cost and Management Accountants of Pakistan (ICMAP)] on the basis of FPSC exams and/or Pakistan Institute of Accountancy examinations. |
|              | While the AATI's long-run focus is on specialized training and continuing professional development, the strategy to professionalize the staff in audit and accounting agencies of Pakistan through IES-compliant professional qualifications is appreciable. |

\(^{40}\) PIPFA, a professional body of accountants, is a joint initiative of the Auditor General of Pakistan, ICAP, and ICMAP, and an associate member of IFAC.
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<td>Public Finance Accountants (PIPFA) exams. Arrangements are also underway with identified reputable tuition providers for passing the remaining exam papers of these bodies as a measure to encourage audit and accounts staff to opt for these professional qualifications.</td>
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<td>4. For reliability, public sector accountants should be provided with continuing professional training requirements that accord with internationally recognized standards of accounting training.</td>
<td>AATI has revitalized its syllabi and learning methodologies through the technical assistance provided under the PIFRA and is now geared toward teaching of practical application areas, including the IPSAS. The AATI has developed a comprehensive annual training program and is striving to achieve set targets for the first year. To work in public sector accounting, a candidate must meet the minimum academic requirements, a graduate with commerce/accounting background. The civil servants who are recruited through the Federal Public Service Commission are also given one-year probationary training in AATI and exams conducted by FPSC; successful completion earns them membership in the PIPFA. The Government of Pakistan prescribes a minimum mandatory 12 days per year for in-service training. For accounting and auditing staff, these requirements are being mainly met by the AATI.</td>
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### (3) Code of Ethics for Public Sector Accountants

The INTOSAI Code of Ethics covers integrity, independence, objectivity, and impartiality; professional secrecy; and competence. The IFAC Code covers integrity, objectivity, independence, confidentiality, technical and professional standards, competence and due care, and ethical behavior.

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<td>5. For reliability, public sector accountants should be required to adhere to the principles laid down in a code of ethics that are at least in accord with the internationally recognized standards for professional accountants. This may be based on IFAC or INTOSAI codes.</td>
<td>INTOSAI Code of Ethics was adopted by the Auditor General of Pakistan and is to be followed by the staff that do audits or are responsible for maintenance of accounts. The same has been included in the AATI syllabus. One paragraph (21) relating to political neutrality has been deleted, apart from minor changes of nomenclature that have been made generally to substitute ‘SAI’ with ‘the Auditor General of Pakistan.’ Para 21 is deleted since public servants in Pakistan are not allowed to participate in political activities.</td>
<td>As such, the code of ethics is part of the overall guidance provided by the head of the organization to the staff members, for which non-compliance may lead to trial of action in accordance with Efficiency and Discipline Rules of Government of Pakistan. However, the code of ethics should be made a part of staff contracts or separately signed by employees as a legally enforceable document. Since the INTOSAI Code was designed for auditors, the CGA should review the ICAP Code for use by CGA accountants.</td>
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### (4) Public Sector Accountant Arrangements

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<td>6. For timeliness, relevance and reliability, there should be a professionally qualified Chief Financial Officer (CFO) function to be responsible to the Principal Accounting Officer (PAO) for maintaining systems of internal financial controls that manage risks, and for preparing regular financial accounts for each government entity.</td>
<td>With the exception of a few departments where the accounts have been departmentalized, the country follows a regime of centralized accounting through the accounts offices keeping accounts of all departments in their regional jurisdiction. The principal accounting officer is generally supported by a budget officer from within that line agency. Out of about 10,000 staff posted in the accounts offices, 921 (173 gazetted) are employed by the federal government. Remaining staff come mainly from the</td>
<td>The funding should be arranged to establish the internal audit units as per staffing and operational plan developed under PIFRA to enable an effective internal audit function as a fourth pillar of governance. The CFO functions and internal auditing within each government entity should be strengthened. Duality of control in accounting offices</td>
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<td>7. The CFO should also be responsible for the maintenance and management of the chart of accounts, to ensure the most appropriate technological support</td>
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42 Some adaptations and deletions were made by a committee constituted for the purpose by the Auditor General of Pakistan while issuing the Code of Ethics and Auditing Standards of INTOSAI.

43 Usually the Secretary of a Ministry or head of the line department is the principal accounting officer.
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<td>for financial management practices, manage training and education needs for</td>
<td>treasury services under the provincial finance departments.</td>
<td>should be resolved.</td>
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<td>financial management, report on key performance indicators, and assist program</td>
<td>Under PIFRA, a comprehensive plan has been developed to initiate the internal audit</td>
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<td>managers to develop an effective financial approach to the delivery of expected</td>
<td>function in government agencies for which a center of excellence is envisaged within the CGA office. As a starting point, chief audit officers have been posted in 15 federal ministries. Main initiating responsibilities of the chief audit officer are internal audit/control, reconciliation of accounts, coordination with regard to Departmental/Public Accounts Committees, and financial propriety of expenditure and receipts. The ADB through a technical assistance in relation to emergency assistance project would initiate an internal control unit for implementing agencies involved in the rehabilitation and reconstruction activities. The same internal control unit is planned to be strengthened over time to become a Center of Excellence in Internal Auditing for all federal government offices.</td>
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**B. Assessment of National Public Sector Accounting Standards**

Financial reporting must be adequate to meet the accountability demands of stakeholders

(1) *Framework for the Preparation and Presentation of Financial Statements.*

<p>| 8. National accounting standards should accord with international standards to provide consistency. The responsibility for establishing the national accounting standards for the public sector should be well-defined to provide reliability. | The Government has not explicitly adopted IPSAS. The Auditor General of Pakistan has the Constitutional mandate to prescribe the form, principles, and methods of accounts of the Federation and of the Provinces with the approval of the President. The Auditor General has a similar role for any authority or body established by the | Formal adoption of IPSAS would enable the customization of the NAM financial reporting formats in compliance with relevant IPSAS (moving from the cash basis in the short term to accrual basis in the longer term). A statement of cash receipt and payment as |</p>
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| Federation or the Province subject to provisions of the relevant legislation. The NAM sets the national standards of accounting and financial reporting.  
The accounting firm, Pricewaterhouse Coopers, analyzed differences between the IPSAS and the New Accounting Model in 2004. Currently NAM is being implemented using the cash basis of accounting and would gradually move toward the accrual basis. | per the Cash Basis IPSAS can be prepared using existing information from the accounting records.  
There is a need to state the accounting policies and the basis on which the accounts are prepared.                                                                 |                                                                                                                                                                                                                           |
| (2) Preparation and Presentation of Financial Statements on the Cash Basis.                                               |                                                                                                                                                                                                                          |                                                                                                                                                                                                                           |
| 9. Financial statements presented in the IPSAS standard                  | Earlier to the New Accounting Model, the Combined Accounts Codes were applied; gradually the budget sector is being converted to the NAM Chart of Accounts, posing a challenge to conversion to the NAM reporting framework. While a number of accounting sites have yet to be upgraded to the SAP R/3 accounting system, other sites which are productive lack some functional aspects relating to pensions, general provident fund, fixed assets, etc. This limits the ability of the Auditor General to prepare financial reports on NAM formats. Therefore, for the time being, the government accounts are presented using the old formats of the Finance and Appropriation Accounts.  
In the existing format of Finance and Appropriation Accounts, there are departures from the Cash Basis.                                                                 | The existing Finance and Appropriation Accounts incidentally provide partial information as required under Cash Basis IPSAS; however there are considerable departures to be resolved for full compliance. Aggregation of all SOEs into the accounts is likely to occur in the longer term.  
The presentation of the financial position and annual operations of the government can be considerably improved. The disclosure of required information as per IPSAS should be made integral to the government systems. There is a need to comply with the disclosure of the treatment of foreign currency. Errors in the accounts affecting the accuracy of |
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<td>IPSAS. As a result, important information is not presented and disclosed.⁴⁴ Although the authorization date is mentioned on the accounts, it is not clear as to when these financial statements become accessible to the general public or media.</td>
<td>financial information should be immediately reconciled and rectified.</td>
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C. Assessment of Accounting and Auditing in State-Owned Enterprises

Financial Statements should comply with IAS and IFRS.

10. The financial statements should include (a) balance sheet, (b) income statement, (c) statement of changes in equity or a statement of recognized gains and losses, and (d) cash flow statement [IAS 1.8]

The financial statements should present fairly (or give a true and fair view of) the financial position, financial performance and cash flows of the entity. [IAS 1.13]

The financial statements should be prepared on the accrual basis of accounting [IAS 1.27]

The financial statements should be prepared using the accounting policies established by the International Accounting Standards. [IAS 1]

Under the Companies Ordinance 1984, it is obligatory for all listed companies to present their financial statements in accordance with IAS/IFRS.⁴⁵ These companies are required to be audited by a chartered accountant under the Companies Ordinance. ICAP issues IFAC International Standards of Auditing (ISA) for mandatory use by its members. Upon receipt of ISA from the IFAC, the exposure draft is sent to ICAP members for comments. These comments are returned for consideration by IFAC. When the final standard is issued by IFAC/IAASB, ICAP adopts the standard. The ISAs are adopted in Pakistan without any modification.

For non-listed companies, the implementation and...

It should be mandated by law that the financial statements of SOEs should be prepared in accordance with the IAS/IFRS.

The Deputy Auditor General (Commercial) Audit is responsible for auditing the public sector enterprises which is an under resourced institution. There is a dire need for specialized training in areas like IAS/IFRS, ISA, and using the work of other auditors.

There is an opportunity for the Commercial

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⁴⁴ There are negative balances appearing in the Finance and Appropriation Accounts, the cash balance appearing in the financial statements is not reconciled with the bank, and receivables appearing from bodies which no longer exist. The overall format of the Finance and Appropriation Accounts is not user-friendly.


⁴⁶ A requirement for getting approval of selected auditors (chartered accountants) is in many cases not observed. Even with compliance, in practice management finalizes the selection of the audit firm which also puts into question the independence of these auditors.
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<td>Enforcement of IAS/IFRS is being finalized. The enforcement paradigm of ISAs for the audit of non-listed companies is less stringent than that for the listed companies. There is no Public Sector Enterprises Monitoring Board as established in other countries. Such an organization (a Board as well as an Experts Advisory Cell) did exist in Pakistan during the 1970s-90s, which was disbanded subsequently. There is a Corporate Finance Wing in Ministry of Finance, whose responsibility is to do such monitoring. It is weak and hence monitoring is poor. Under the capacity-building project it is to be strengthened, but the program is yet to start. Strengthening this Wing in MoF would be more sensible than re-introducing a Board.</td>
<td>Audit Wing of the DAGP (after strengthening) to monitor SOE for IAS/IFRS compliance.</td>
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<td>A review of a sample of SOE financial statements which are audited by chartered accountants indicate that the audit reports generally contained either significant qualifications or emphasis of matter paragraphs modifying the audit opinion. In addition, SOEs which are not incorporated under the Company Law, do not usually apply IAS/IFRS in accounting and financial reporting.</td>
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<td>For public sector enterprises whose financial statements are not audited by chartered accountants, IAS/IFRS are not generally followed, and financial statements are generally audited after a long delay.</td>
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<td>There is little involvement of the DAGP in selection of the external auditors of these SOE. The DAGP while conducting regularity or performance audit does not have access to the qualifications in the audit report on the financial statements. The DAGP is neither provided with the management letter given by the external</td>
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<td>auditors to the SOE nor given access to financial audit working papers. Thus, serious issues relating to the use of public funds are not subjected to legislative scrutiny by the Public Accounts Committee.</td>
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II. Public Sector Auditing

A. Assessment of the Public Sector Auditing Environment

Effective scrutiny by the legislature through comprehensive, competent external audit enables accountability for the implementation of fiscal and expenditure policies.

The environment for an effective SAI requires a comprehensive approach to public financial management. Supreme Audit Institutions are not stand-alone institutions; they are part of a PFM architecture that also includes budgeting, accounting, internal control, audit and legislative oversight, and government response. Improving the way the SAI functions is integral to providing information for improving the overall PFM system but the action must be within the executive branch under the watchful eyes of the legislature and the public. A strong demand for good public sector external auditing is necessary for the SAI to have any impact. This requires willingness of the executive branch to accept and respond to external scrutiny over its management of funds and to ensure that action is taken for reform. It also requires public presentation of the audit reports to ensure public support for effective action.

(1) Statutory Framework

11. Statutory auditing requirements should be established by legislation.

| Legislation exists: The Constitution of Pakistan, 1973 (as stands amended); and the Auditor General’s (Functions, Powers and Terms and Conditions of Service) Ordinance, 2001. | There is an Audit Code which lays down the basic principles of auditing in lieu of the Constitutional provisions and the Auditor General Ordinance 2001. | The Auditor General adopted INTOSAI Auditing Standards in 2002 with minor adaptations. These standards form the basis of the auditing methodology and process for the DAGP which is further explained in |

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<td>12. The SAI should have the authority to conduct a full range of audits for all government owned or controlled entities including regularity, financial, and performance audits. (INTOSAI Lima Declaration Sections 18-19)</td>
<td>Yes, AGP has full authority for auditing all budget sector receipts and expenditures from all government accounts including the defense expenditures.(^{47}) The AGP has the authority to audit any entity or body established by the government or which has received a loan or grant; however there are some exclusion clauses in the Constitution, as well as in the Auditor General’s Ordinance 2001. Article 169(b) of the Constitution limits the powers and functions of the AGP in relation to any authority or body established by the government depending on the provisions contained in the respective legislation establishing that authority/body. Similarly, Sections 9 (explanation), 11 (proviso), 15 and 16 of the Auditor General’s Ordinance pose certain conditions on the AGP powers and function in relation to the audit of the public sector enterprises. These jurisdictional limitations are under review. A committee of the Auditor General, Finance Secretary, and Law Secretary are looking at potential revision of the Auditor General’s Ordinance to remove the restrictive or exclusionary clauses. The Public Accounts Committee of the Parliament is pursuing this issue.</td>
<td>The proposed review of the Auditor General’s Ordinance 2001 to resolve jurisdictional issues may also look into providing for a specific AGP mandate in relation to economy, efficiency, and effectiveness of utilization of public funds along the lines of model legislation.(^{48}) All commercial SOEs, registered by the Securities and Exchange Commission of Pakistan, should be subject to world-class audits by qualified firms selected by and reporting through the Auditor General. In this way the Auditor General need not do the audits directly, but can ensure proper coverage and reporting.</td>
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\(^{47}\) There are minor exclusions of practice relating to receipts kept as local funds or so called non-public funds by some institutions.

\(^{48}\) Model Law developed by the UNDP Program for Accountability and Transparency (PACT) and A Model National Audit Office Act, The Association of Chartered Certified Accountants, UK, 2004, Section 32 & Section 55.
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|          | The Auditor General’s Ordinance 2001 specifies the following types of audits:  
• Section 7, Certification audit (accounts).  
• Section 8, Regularity audit.  
• Section 9, Audit of authorities having loans or grants from public money.  
• Section 12, Audit of receipts.  
• Section 8 & 9, Receipts and Expenditures (includes authorities and bodies substantially financed by loans and grants).  
• Section 10, Study reports; Performance, governance, debt management, or environment audits are covered under this section.  
• Section 15, Audit of companies and corporations established under the public sector (PTCL, PPAF, etc).  
Note: Section 22 gives the Auditor General, the powers to make regulations with the prior approval of Federal Government for furthering the purpose of the Auditor General’s Ordinance.  
There is no explicit mention of the proprietary, efficiency, effectiveness, and economy in the Auditor General’s Ordinance, yet many of the senior staff categorized this as the main objectives of the DAGP. | Resolve vagueness in Section 14 of the Auditor General’s Ordinance 2001 regarding the enforcement of action (whether the executive or Public Accounts Committee must initiate action). The Auditor General should have specific powers to initiate action against persons who refuse to provide |
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| relevant Efficiency and Discipline Rules, as applicable. Section 14 does not mention who would initiate such an action (possibly the Auditor General, Public Accounts Committee, Principal Accounting Officer or any other body). Therefore the implementation of this section may be problematic. | auditable accounts and relevant records to DAGP staff. Specific provisions in the Auditor General’s Ordinance 2001 should be made for making the audit reports public in line with the ACCA’s model legislation as follows:\(^{49}\)  
(1) All reports issued by the Auditor General shall be considered public documents when the reports are presented to Parliament. As public documents, they shall be made available to the public for a minimal cost-recovery fee.  
(2) The Auditor General may make his/her reports publicly available in electronic format on the Internet.  
(3) The Auditor General shall provide copies of his/her published reports to the government archivist, all public and university libraries in relevant locations, the National Broadcasting Corporation, and the press.  
(4) The Auditor General or his/her staff may provide comments and interviews to the press or other media on the subject of any published audit reports. |  
In case of any hindrance or problem, generally the Public Accounts Committee issues directions to the executives to comply with the auditing requirements. This process is lengthy and subject to many delays thereby reducing the effectiveness of the provision and rendering the Auditor General without recourse.  
In addition, the legislative scrutiny is not supported by the public scrutiny due to non-dissemination of audit reports and government financial statements. |
### (2) Setting Auditing Standards

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<td>14. The government should have adopted the INTOSAI Auditing Standards and the IAASB International Standards for Auditing for public sector entities. (ISA 200.5 and INTOSAI Auditing Standards1.0.14)</td>
<td>The Auditor General has adopted the INTOSAI Auditing Standards with some minor adaptations. These standards have been used as the basis of the Audit Manual, in which Chapter 4 clearly mentions that the INTOSAI Auditing Standards are considered the general framework for the auditing methodology and procedures. Although the Audit Manual does not mention specifically International Standards on Auditing, the overall approach and methodology is consistent with the these standards. INTOSAI recognizes that the INTOSAI Auditing Standards are broad in nature and that the IFAC ISAs provide a further level of detail for public sector audit guidance. It is working with IFAC in the longer term to develop practice notes to assist with implementation in the public sector of each ISA. Therefore, prescribing the ISAs as the applicable auditing standards in addition to the INTOSAI auditing standards in an explicit manner would ensure that the relevant developments in the auditing process are learnt and applied on a continuous basis.</td>
<td>The International Standards on Auditing should also be formally adopted, preferably through legislation. It has been construed from various provisions of the legislation, including Section 22 of the Auditor General’s Ordinance 2001, that the Auditor General would be the standard-setting authority for the public sector auditing. The Auditor General, as an active INTOSAI member, usually subscribes to the declarations of the international organization for implementation as per the local setup and environment; therefore the INTOSAI Auditing Standards have been adopted with minor modifications. The adoption process consisted of an in-depth review of the INTOSAI Code of Ethics and Auditing Standards by a committee of senior officers established by the Auditor General. There is a need for a similar committee to review and adopt the International Standards on Auditing for use on a continuous basis. The committee might also be represented by local professional bodies. The Institute of Chartered Accountants of Pakistan is already running a process for ISA adoption. The adoption process might start with inputs given at the exposure draft stage and continue through to issuing practical guidance on local application of international standards.</td>
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<td><strong>(3) Code of Ethics</strong></td>
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<td>15. The INTOSAI Code of Ethics should have been fully adopted by the SAI (IFAC ISA 200.4 and INTOSAI Code of Ethics 4), communicated to all staff and applied.</td>
<td>The INTOSAI Code of Ethics was adopted by the Auditor General of Pakistan in 2002. The Code must be followed by all staff who are doing audits or are responsible for maintenance of accounts. Some minor adaptations and deletions were made while issuing the INTOSAI Code of Ethics and Auditing Standards to make them suitable with the local setup and environment.</td>
<td>Improved monitoring for the code is needed.</td>
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<tr>
<td><strong>(4) Accountability in the SAI</strong></td>
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<td>16. There should be an accountability process in the SAI. (INTOSAI Auditing Standards 1.0.20)</td>
<td>Any DAGP staff, being government public servants, who are caught in misconduct, would be subject to the Efficiency and Discipline Rules of the Government of Pakistan. In such a case the inquiry officer exercises the powers of a Civil Court to establish the guilt.</td>
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<td>17. There should be clear responsibility in the SAI for (i) advising on internal finance, keeping proper financial records and accounts, and maintaining systems of internal control; and (ii) for ensuring compliance with laws and regulations</td>
<td>A Manual of Standing Orders of the Auditor General regulates the internal procedures of the organization. The Manual is being updated. In the existing structure of the DAGP, the administrative and functional issues are all delegated to the Additional Auditor General (Administration). The Inspection, Regulation, Vigilance and Monitoring of Training Wing, an independent branch of the DAGP under a Deputy Auditor General, is a type of internal audit unit that conducts inspections of all activities, including in-field audit offices.</td>
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<td>18. The SAI should prepare an annual report on its operations and performance that is separate from its reports on its audits. It should provide an objective,</td>
<td>It is the intended good practice of the DAGP to prepare an annual report each year, but other priorities interrupt meeting the schedule. The last annual report was</td>
<td>The Auditor General should prepare and disseminate an annual corporate plan, as well as the annual performance report of the</td>
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<td>19. The SAI should prepare a corporate plan or equivalent.</td>
<td>The Corporate Audit Plan (2001-2002) contained the vision and mission translated into an annual audit plan. A 3-year plan is under process.</td>
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<td>20. The SAI should undergo peer review or independent performance audit.</td>
<td>The DAGP does not undergo a peer review or independent performance audit; nor does any independent external body audit its activities. However, there are interlocking arrangements for audits within the field audit offices which provide peer review assurance within the organization.</td>
<td>The DAGP should undergo an accountability mechanism in sync with that suggested under the ACCA-proposed legislation for SAIs, involving review by the Public Accounts Committee of annual corporate plans and annual reports.</td>
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(5) Independence provided by the Legislation

21. Legislation needs to be adequate for the following core principles of SAI independence if the SAI is to provide effective external scrutiny:
   (1) The existence and de-facto application of an appropriate and effective constitutional and legal framework.
   (2) The independence of the SAI Heads, including security of tenure and legal immunity in the normal discharge of their duties.
   (3) A sufficiently broad mandate and full discretion in the discharge of SAI functions.
   (4) Unrestricted access to information.
   (5) The obligation to report on their work.
   (6) The freedom to decide on the content and timing of their reports and to publish and disseminate them.
   (7) The existence of effective follow-up mechanisms on SAI recommendations.
   (8) Financial and managerial autonomy and the availability of appropriate human, material and monetary resources.
   (Core Principles of SAI Independence, INTOSAI Sub-committee on SAI Independence, 2004)

22. The legislation should spell out in detail the extent of the SAI independence. (INTOSAI Lima Declaration Section 5)

23. The legislation should assure the independence of The Constitution guarantees the protection of service of the Auditor General of Pakistan. Once appointed, the Auditor General can only be removed by a Supreme Judicial Council and a majority vote in the Parliament. Similarly, the expenditures of his office (being the | Adopt IFAC Code of Ethics procedures for enhanced independence requirements in the environment of rotation of assignments and nominal dependency for logistics on some of the auditees. |

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<td>the SAI Heads and “Members” (in collegial organizations) and that there is security of tenure and legal immunity in the normal discharge of their duties. (INTOSAI Lima Declaration Section 6)</td>
<td>charged expenditures) are not subject to vote in the Parliament and therefore avoid any general cuts in the grants.</td>
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<td>Section 19 of the Auditor General’s Ordinance 2001 gives the Auditor General full power to incur expenditures within the budgetary provisions. Being the head of a civil service cadre (i.e., Pakistan Audit and Accounts Service), the Auditor General has independence in personnel management.</td>
<td>The separation of audit and accounts has to some extent resolved the independence issue. However, the rotations of assignments, including deputations to other departments and back to audit offices, need to be reviewed.</td>
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<td>The AGP independence as a whole and the DAGP’s effectiveness at financial accountability is ensured by the overall stature of the Auditor General through its constitutional mandate; protection of term; financial and human resource independence; exercise of authority over type, schedule and duration of audit; powers to examine records; direct liaison with the parliamentarians in the Public Accounts Committee; INTOSAI representation, etc.</td>
<td>However, the accountability process after the audit involving legislative scrutiny and implementation of PAC’s recommendations/directives by the executive is lengthy and needs considerable improvements. An audit observation tracking system is being implemented under PIFRA II which would improve the post-audit accountability system. Similarly, the audit reports and certified accounts are not made public immediately after</td>
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<td>being laid to the parliament; therefore public scrutiny based on the audit findings cannot be exercised. The application of a Code of Ethics, rotation of staff among the field offices, and continuous training ensures that the AGP personnel do not develop too close a relationship with the entities that they audit. In addition, the close audit supervision ensures that the field audit staff does not mingle with the clients. However, the dependence on the auditee organizations for the provision of logistics sometimes can affect the highest level of independence.</td>
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<td>Some limitations are evident. The audit law should be more powerful in the areas of the AGP’s budget and personnel powers.</td>
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<td>24. The SAI’s constitutional/statutory/legal framework should ensure that it has available sufficient human, material and monetary resources. (INTOSAI Lima Declaration Section 7)</td>
<td>The fact that the Auditor General is head of the Pakistan Audit and Accounts Service ensures independence in human resource planning and development. The recruitment of civil servants is done through the Federal Public Service Commission. The annual budget is approved as a charged expenditure and can only be discussed in the Parliament but not subject to voting. The Auditor General has full powers for incurring expenditures out of the approved budget. The direct liaison with the Parliament also ensures that Auditor General justifies the expenditure.</td>
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<td>25. A fixed term must be long enough to survive changes of government and avoid pressures concerning re-appointment impinging too early in the term of office of the SAI office holder. A single non-renewable appointment is preferable to avoid those pressures. (INTOSAI Working Group on SAI Independence, 2004)</td>
<td>The Auditor General is appointed by the President of Pakistan and his oath administered by the Chief Justice of Pakistan. The termination of AGP services before expiry of the term follows the same procedures as removal of a Supreme Court judge from office (i.e., through the Supreme Judicial Council and endorsement by the Parliament). Therefore, even the appointing authority does not have termination powers. The AGP term is 5 years or the attainment of 65 years of age by the incumbent, whichever is earlier. During this term, the Auditor General can carry out the mandate without fear of retribution. If terminated, re-</td>
<td>The term is short by international standards.</td>
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<td>26. The legislation should ensure that the Head of the SAI is free to determine the organization of the audit office, including personnel and contract management systems and material acquisition/disposal policies and procedures. The SAI should be able to determine personnel policies, including the selection, recruitment, training, remuneration, promotion, discipline, and dismissal of staff and contract personnel. (INTOSAI Lima Declaration Section 6)</td>
<td>Appointment is not allowed before the expiry of two years after vacating office, thereby limiting any bargains for re-appointment.</td>
<td>The AGP is empowered to investigate the use of public monies or assets by a recipient regardless of its legal nature at least for the first year (Section 9 of AGP Ordinance 2001). The continued use of these public funds may go beyond the scope of the Auditor General due to the jurisdictional issues relating to audit of the public sector enterprises. The fact that the Auditor General is head of the Pakistan Audit and Accounts Service ensures independence in human resource planning and development. The recruitment of civil servants is done through the Federal Public Service Commission. The AATI is an internal system for initial training and continuing professional development of staff. For new posts creation, the Auditor General has to negotiate with the Ministry of Finance.</td>
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<td>27. There should be unrestricted access to information. (INTOSAI Lima Declaration Section 10)</td>
<td>The Section 14 of the AGP Ordinance 2001 ensures that the Auditor General has access to all offices having accounts and other related documents and indicates how to deal with any person hindering the audit functions.</td>
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<td>28. The legislation should give the SAI the right and obligation to report on their work. (INTOSAI Lima Declaration Section 16) The legislation should give the SAI the right and obligation to report effectively on its work, and the freedom to decide on the content and timing of its reports and to publish and disseminate them expeditiously. (INTOSAI Lima Declaration Section 17)</td>
<td>Article 171 provides that the Auditor General shall submit the reports to the President who shall cause them to be laid before the Parliament. The Parliament sends these reports to the Public Accounts Committee for detailed scrutiny. There has never been an amendment in the audit reports after being submitted to the President. Section 7 relates to the Certification Audit which assigns</td>
<td>Section 7 narrates the minimum audit requirements for the certification of annual accounts. The Auditor General has to plan keeping in view the resources in hand, how much time can be allocated to other types of audits in a year, in addition to the mandatory certification of accounts. PIFRA is trying to achieve an integration of</td>
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<td>responsibility to the Auditor General to certify the accounts on the</td>
<td>There is ample time before submission to the President for the executive to resolve any audit observations through (Special)/Departmental Accounts Committees or simply by administrative action as recommended in the Audit Information Report.</td>
<td>the financial certification and regularity audit by introducing more concurrent audit activities focusing on regularity and compliance as part of the certification audit. This would also lead to a timely certification of the accounts and meaningful and complete representation sent to the legislature.</td>
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<td>basis of his audit for each financial year and present his notes,</td>
<td>The audit reports purportedly become public after these are discussed by the Public Accounts Committee; but the mechanism is unclear. This gap analysis report was refused access to any recent reports because they were not public. As the Public Accounts Committee is often not in session and discussions are held years after the event, this method of publication of audit reports substantially varies from international standards and is considered unsatisfactory.</td>
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<td>comments, or recommendations in relation with those accounts. The law</td>
<td>The study team was unable to establish what audit reports were public. The law does not specify when the Auditor General is free to publish and disseminate its reports to the public and what should be the mechanism of dissemination. The senior audit staff generally perceives it as the function of the legislature.</td>
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<td>does not specify the timeline for submission of the certified annual</td>
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<td>accounts. Similarly, the law does not require the Auditor General to</td>
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<td>submit an annual report on its performance.</td>
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\^51 There is a disconnect /lack of connection between certification and regularity audit reporting. The certification audit gives partial compliance in the form of ‘can be relied upon’ subject to both qualifications contained therein, as well as the issues reported separately in regularity audit reports. The certification audit reports are seldom discussed by the Public Accounts Committee thereby limiting the general dissemination / availability and use of the government financial statements by stakeholders.
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<td>29. To the extent the findings of the Supreme Audit Institution's findings are not delivered as legally valid and enforceable judgments, the Supreme Audit Institution shall be empowered to approach the authority which is responsible for taking the necessary measures and require the accountable party to accept responsibility. (Lima Declaration Section 11.2)</td>
<td>This primary responsibility of follow-up of actions is with Public Accounts Committee secretariat which is closely coordinated by the Auditor General for compliance of its part of directives/recommendations. The Auditor General does not have any statutory power for imposing sanctions directly. An Assistant Auditor General (PAC) maintains the record of the follow up of audit observations and actionable points emanating from the PAC deliberation on the audit reports. Lately, the ADM Plus software has been procured for recommendation tracking. Holding mock / pre-PAC preparation is noted for properly addressing the observations and recommendations.</td>
<td>There are many audit observations and findings that have not received action.</td>
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(6) **Qualifications and Skills of the Auditor**

The SAI needs qualified accountants to sign audit opinions. Auditors must have adequate professional expertise and technical knowledge to carry out audits.

| 30. The syllabi of the government’s and SAI’s accounting schools should cover all areas recommended by the International Federation of Accountants’ educational standards (IES) | There is an elaborate system of training the accounting and auditing staff at different hierarchical levels through the AATI, and higher academic and professional qualifications at local and foreign universities and professional training bodies. The Auditor General has developed a comprehensive training plan with the help of foreign consultants. PIPFA courses have become | The AATI should continue to review its syllabus to cover all areas recommended by IFAC IES. There is a need to build the number of staff with ICAP qualifications. |

52 Although the Public Accounts Committee writes the word ‘directives’ for its decisions but many stakeholders perceive in line with the decision of NWFP High Court declaring these as ‘recommendations’ which are subject to voluntary compliance by the executive.
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<td>mandatroy for Audit Officers. Syllabi of AATI probationers have been revamped. The substantial portion for funding in PIFRA II is for training in auditing and accounting.</td>
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<td><strong>31.</strong> There should be adequate professional criteria for recruitment and promotion of auditors. (INTOSAI Lima Declaration Section 14 and INTOSAI Auditing Standards 2.1.4)</td>
<td>The academic criteria used for recruitment and promotion of auditors: For assistant audit officer – B-Com is the minimum qualification. For audit officer – PIPFA. For civil service – 9 months’ professional course at AATI, leading to PIPFA qualification. FPSC conducts the final examination.</td>
<td>These arrangements are not adequate to meet international standards for auditing annual accounts and signing audit opinions. Further upgrading of the AATI courses and the promotion criteria for senior audit staff is needed.</td>
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<td><strong>(7) Training</strong></td>
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<td><strong>32.</strong> The SAI should operate a continuing professional development program for its professional personnel. (INTOSAI Lima Declaration Section 14 and INTOSAI Auditing Standards 2.1.5-2.1.12)</td>
<td>The annual training plan of AATI provides many opportunities for the continuing professional development of staff. The plan encompasses more than 50 different short courses or workshops. There is also a requirement of mandatory training of 12 working days by applicable to civil servants in BPS 17 &amp; 18. There is also a mechanism of allocating certain training days in each annual audit plan for the sake of time-budgeting. Finally, rigorous capacity-building exercises are being identified, designed, and delivered as part of PIFRA II.</td>
<td>PIFRA II reform process should be continued in relation to the capacity-building of auditing staff.</td>
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<td><strong>(8) Audit Competence</strong></td>
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<td><strong>33.</strong> The SAI should equip itself with the full range of up-to-date audit methodologies, including systems-based techniques, analytical review methods, statistical sampling, and audit of automated information systems. Audit manual development was outsourced under PIFRA to foreign consultants who developed the guidelines and methodologies with the help of the Accounting Policy Wing which would be responsible for</td>
<td>An action plan for implementation of new Financial Audit Manual should be developed for auditing the financial statements of federal and provincial governments and implemented</td>
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<td>(INTOSAI Auditing Standards 2.2.37)</td>
<td>future maintenance and updating of these manuals. The DAGP through PIFRA procured audit department management system for audit planning and implementation. Audit planning, risk assessment, personnel management, and recommendation tracking are various modules. Audit Command Language has been acquired for computer-aided audit techniques and applied on the transaction data in SAP R/3 systems in accounting offices.</td>
<td>in sync with the capacity-building and computerization activities.</td>
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(9) **Quality of the Audit**

34. The SAI should have the quality assurance programs in place to ensure audit performance and results. Written quality control policies and procedures should be communicated to the audit personnel in a manner that provides reasonable assurance that the policies and procedures are understood and implemented. (ISA 220.7)

35. Quality control procedures should cover:
   - Direction: Assistants to whom work is delegated need appropriate direction.
   - Supervision: covering the following functions during the audit: (a) monitor the progress of the audit, (b) become informed of and address significant accounting and auditing issues, and (c) resolve any differences of professional judgment between personnel and consider the level of consultation that is appropriate.
   - Review: The work performed by each assistant needs to be reviewed by personnel of at least equal competence. (ISA 220.8-220.17)

<p>| | There is quality supervision at the field audit office level where the Director General personally certifies the quality of audit reports. There is further review for quality assurance at the Deputy Auditor General level. Finally the Quality Assurance Review Committee at the DAGP reviews all audit reports before their release. The new Audit Manual (Chapter 5 to Chapter 15) describes in detail the procedures for direction, supervision, and review of audit work. | The audit documentation and report writing skills need to be improved. |</p>
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<td><strong>B. Assessment of Public Sector Auditing Standards and Practices</strong>&lt;br&gt;Results from the audits should hold the executive to account for fiscal and expenditure policies and their implementation.</td>
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<td><strong>(1) Planning</strong></td>
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<td>36. The planning process should collect information about the audited entity and its organization in order to identify important aspects of the environment in which the audited entity operates, develop an understanding of the accountability relationships, determine whether appropriate action has been taken on previously reported audit findings and recommendations, assess risk, and determine materiality. (IFAC ISA 300.6-300.9)</td>
<td>The certification audit procedures suggest that the audit staff should prepare work flow, procedure diagram, or systems outline; and list the main accounting areas in order to familiarize themselves with the audited entity. However, this does not delve into the risk assessment and determination of materiality levels which are more or less pre-defined by the procedures.</td>
<td>The new audit methodology manual should introduce more comprehensive planning requirements based on the specific objectives of the audits. Engagement of chartered accountants as part of the audit teams for conducting of certification audit can be very helpful in skill development. The memorandum of understanding between the Auditor General and the ICAP may be used for procuring such services with quality assurance support from the ICAP.</td>
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<td>The planning process should identify the scope of the audit, and specify the audit objectives and the tests necessary to meet them. (ISA 300.10-300.12)</td>
<td>The procedures define the overall objectives of the certification audit and the objectives of each of the six audit areas: establishment costs, contingencies, pensions, receipts, general provident funds, and accounts compilation. However, the objectives are not further refined in accordance with the risk of understatement, overstatement, or misstatement that can be associated with any of the audit areas; and audit tests are not accordingly tailored.</td>
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<td>The planning process should review the internal audit of the audited entity and its work program, identify key management systems and controls, and carry out a preliminary assessment to identify both their strengths and weaknesses, and determine the</td>
<td>The internal audit function is evaluated as part of the regularity audit. However, since the internal audit in government departments is in its infancy, the certification audit does not put considerable reliance on the internal audit.</td>
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54 Internal Audit Plan and Internal Audit Manual was developed under PIFRA I, and chief audit officers posted in 15 ministries have been given exposure training.
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<td>approach to be adopted in the audit. (ISA 300.9)</td>
<td>Planning documents formally prepared do not identify the specific risks; however the consideration of complaints, newspaper cuttings, and problems experienced during previous audits, together with the value judgment, use of hindsight, and threshold for materiality are envisaged at the planning stage of audit under the new Financial Audit Manual.</td>
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<td>The planning process should highlight special problems foreseen when planning the audit. (ISA 300.10)</td>
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<td>The planning process should prepare a budget and a schedule for the audit, and provide for appropriate documentation of the audit plan and for the proposed fieldwork. (ISA 300.10) The planning process should identify staff requirements and a team for the audit. (ISA 300.11)</td>
<td>The audit plan, which allocates the human resources available to various audit assignments, is prepared annually.</td>
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<td>The planning process should familiarize the audited entity about the scope, objectives and the assessment criteria of the audit and discuss with them as necessary. (ISA 300.7)</td>
<td>For the certification audit, the accounting entities, including the Accountant General and District Accounts Offices, provide the majority of auditable documents supporting the financial statements. Initial discussions with them give the auditor the required understanding as to how the accounts have been compiled.</td>
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(2) **Supervision**

<p>| 37. The process of supervision should ensure that the members of the audit team have a clear and consistent understanding of the audit plan. (INTOSAI Auditing Standards 3.2.3a) | The Director Audit or Deputy Director Audit initially briefs the audit team usually comprising the audit officer and assistant audit officer before sending them to the auditee. Later the Director / Deputy Director supervises the team on site, the frequency of which varies depending on a number of factors. The Deputy Director Audit is often part of the exit meeting with the auditee sharing the Audit Information Report. | Improved working paper guidance and technology combined with more effective supervision and independent quality review processes are needed. |</p>
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<td>38. The process of supervision should ensure that the audit is carried</td>
<td>The supervision process generally emphasizes the findings of the audit team and documentation of the audit evidence; however, lesser emphasis is placed on the overall assurance levels achieved and referencing and sequencing of the audit working papers.</td>
<td>There is a need for more guidance on the audit testing to be undertaken and the functions of supervision. Working papers need to be more structured.</td>
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<td>out in accordance with the auditing standards and practices of the SAI.</td>
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<td>(INTOSAI Auditing Standards 3.0.3b)</td>
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<td>39. The process of supervision should ensure that the audit plan and</td>
<td>The audit team usually keeps the Deputy Director or Director Audit informed of significant developments in the field.</td>
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<td>action steps specified in that plan are followed unless a variation is</td>
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<td>authorized. (INTOSAI Auditing Standards 3.0.3c)</td>
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<td>40. The process of supervision should ensure that working papers</td>
<td>Only the tenable audit observations are printed. The Quality Assurance Committee is an important forum where each audit observation is reviewed from the auditee’s standpoint and dropped if found weak.</td>
<td>The process of audit supervision takes the audit findings through the quantification of the most likely error (by extrapolation of the known errors) which may lead to a qualified audit certificate issued by the Auditor General.</td>
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<td>contain evidence adequately supporting all conclusions, recommendations</td>
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<td>and opinions. (INTOSAI Auditing Standards 3.0.3d)</td>
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<td>41. The process of supervision should ensure that the auditor</td>
<td>The process of audit supervision takes the audit findings through the quantification of the most likely error (by extrapolation of the known errors) which may lead to a qualified audit certificate issued by the Auditor General.</td>
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<td>achieves the stated audit objectives. (INTOSAI Auditing Standards</td>
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<td>3.0.3e)</td>
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<td>42. The process of supervision should ensure that the audit report</td>
<td>The audit reports generally include the audit conclusions, recommendations, and opinions; but these are divided into both the regularity audit and certification audit. The audit certificate on the financial statements points to the regularity audit reports, among other audit reports, as covering the significant aspects of financial governance, or economical, efficient, and effective utilization of public resources. However, there is no formal linkage at the working level between the certification audit and the regularity audits conducted by the Auditor General.</td>
<td>There is obvious opportunity to use the results of regularity audit while planning and conducting the certification audit and also to conduct the regularity checks as part of the compliance testing procedures during the certification audit. Efforts are underway through PIFRA to integrate the certification audit (Section 7) and the regularity audit (Section 8) into one certification audit product through implementation of the Financial Audit Manual.</td>
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<td>includes the audit conclusions, recommendations and opinions, as</td>
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<td>appropriate. (INTOSAI Auditing Standards 3.0.3f)</td>
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<td>43. The process of supervision should ensure that the audit report</td>
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<td>includes the audit conclusions, recommendations and opinions, as</td>
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<td>appropriate. (INTOSAI Auditing Standards 3.0.3f)</td>
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<td>conclusions, recommendations, and opinions, as deemed appropriate. The Quality Assurance Committee emphasizes that only the tenable audit observations are printed. Each audit observation is reviewed from the auditee or audience standpoint and dropped if found weak. This sometimes may lead to removal of loosely drafted paragraphs without consultation with the audit staff having exact knowledge of the observation. The process—from communication of the Audit Information Report to creation of advance or draft paragraphs then resolution of these through DAC/SDAC before submission of printed reports to the Public Accounts Committee—provides ample opportunity for the executive/auditee to resolve the audit observations. On this basis only properly identified, documented, and unresolved audit observations are brought to the attention of the most senior SAI officers for reporting. However PAC assessments have shown substantial numbers of unjustified audit observations so there are major flaws in the process. Risk assessment procedures for the certification audits, as well as identifying formations for regularity audit, does not take into account the results/findings of the previous audits. The audit review process feeds-back into process improvement through the FAPC Wing, which keeps reminding the field audit offices about the qualitative changes in formats, evidence gathering, and the broad policy toward impact-oriented audit reports.</td>
<td>The audit process should be risk-based allowing sufficient flexibility to the auditors to articulate and apply appropriate audit procedures on intelligently selected samples and to arrive at correct audit conclusions. A stakeholders’ workshop was held where representatives of Public Accounts Committee and auditees were also present and deliberated generally on all issues relating to the audit process. To take the process forward, there is need for more focused workshops to identify the most critical issues and come up with concrete recommendations for resolution.</td>
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### (3) Internal Controls

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<td>44. The auditor should obtain an understanding of the entity and its environment, including its internal control, sufficient to identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, and sufficient to design and perform further audit procedures. (ISA 315.2)</td>
<td>The certification audit procedures presently in use prescribe the compliance checklists for each audit area based on the government systems/procedures, but does not encourage identification of a lower number of critical controls that impact the contents of the financial statements leading to a flexible design of substantive procedures and innovative selection of samples for these.</td>
<td>The new audit methodology and process should be rolled out immediately to improve the process of environmental risk assessment, compliance testing, and sampling procedures; and the implementation of the Financial Audit Manual should not be coupled with the implementation of New Accounting Model.</td>
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<td>After obtaining an understanding of the accounting and internal control procedures, the auditor should obtain a sufficient understanding of control activities to assess the risks of material misstatement at the assertion level and to design further audit procedures responsive to assessed risks. (ISA 315.90)</td>
<td>The compliance checklists for each audit area cover the assertions of existence and operation of internal controls. Since the checklist is based on the prescribed government procedures the effectiveness assertion is assumed.</td>
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<td>The auditor should document in the audit working papers: (a) conclusions reached about susceptibility to material misstatement due to error or fraud; (b) the understanding obtained of the entity’s accounting and internal control procedures; and (b) the assessment of control risk. (ISA 315.122-123)</td>
<td>The auditor assesses the control risk for each identified control and thereby identifies the risk of likely error in the form of proportion of departures ascertained. However the compliance procedures are not based on systematic environmental assessment and evaluation of the entity’s accounting and internal control systems. Instead the control tests are based on the predefined checklists as part of the audit procedures for six key audit areas.</td>
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<td>The auditor should perform tests of controls to obtain sufficient appropriate audit evidence that the controls were operating effectively at relevant times during the period under audit. (ISA 330.23)</td>
<td>The failure to obtain sufficient appropriate audit evidence for any material financial statements assertion leads to qualifications in the auditor’s opinion.</td>
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<td>When the auditor cannot obtain sufficient appropriate audit evidence as to a material financial statement assertion, the auditor should express a qualified opinion or a disclaimer of opinion. (ISA 330.72)</td>
<td>At the conclusion of the fieldwork the audit team shares with the auditee an Audit Information Report identifying all observations for management comments.</td>
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<td>(ISA 315.12)</td>
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**(4) Compliance with Laws**

45. The auditor should obtain a general understanding of the legal and regulatory framework applicable to the entity and the industry and how the entity is complying with that framework. (ISA 250.15)

The auditor should perform testing and other procedures to help identify instances of non-compliance with those laws and regulations where non-compliance should be considered when preparing financial statements. (ISA 250.18-250.19)

Generally, management is responsible for establishing an effective system of internal controls to ensure compliance with laws and regulations. In designing steps and procedures to test or assess compliance, the auditor should evaluate the entity's internal controls and assess the risk that the control structure might not prevent or detect non-compliance. These evaluations should be used to report to management on defects in the system of internal controls and the steps that should be taken to improve the system. (ISA 250.17)

The auditor should obtain written representations that management has disclosed to the auditor all known actual or possible non-compliance with laws and regulations whose effects should be considered when preparing financial statements. (ISA 250.23)

The SAI should use regularity audit to make sure that the State budget and accounts are complete and valid. The audit procedure may result, in the absence of irregularity, in the granting of a "discharge". If not other processes are needed to resolve irregularities.

In certification audit, compliance with the legal and regulatory framework is ensured to an extent only. Whereas regularity audit, due to its wide scope and greater coverage, provides greater assurance in relation to compliance with laws and regulations.

The management designs the systems, and an auditor independently assesses those systems and provides feedback to the management. The auditor does not obtain written representations as to whether the management has disclosed to him all known actual or possible noncompliance with laws and regulations whose effects should be considered when preparing financial statements.

There is no formal procedure for granting discharge to an auditee after the successful completion of a formation under his control. The auditee remains accountable despite the fact that the external audit obtained substantial assurance regarding the state of affairs and the financial statements. For instance, the special audits can cover more than one previous year while tracing any future incident and therebyprobe into any specific matter well after the conclusion of the annual audit.

Certification audit is required to provide assurance to adequate levels of materiality. Greater assurance from compliance (regularity) audit is not required. If the Auditor General wishes to undertake audits aimed at ensuring that expenditures are properly controlled, then such audits should be designed on modern principles.
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<td>(5) Evidence</td>
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<td>46. When obtaining audit evidence from tests of control, the auditor should consider the sufficiency and appropriateness of the audit evidence to support the assessed level of control risk. (ISA 500.10) When obtaining audit evidence from substantive procedures, the auditor should consider the sufficiency and appropriateness of audit evidence from such procedures together with any evidence from tests of control to support financial statement assertions. (ISA 500.12) The results of the compliance tests do have an impact on the sample size for the substantive procedures, however the results of the compliance tests are not used to tailor the selection of sample transactions based on identified pattern of errors. The new Financial Audit Manual should be implemented immediately discarding these mechanical procedures.</td>
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<td>47. When inventory is material to the financial statements, the auditor should obtain sufficient appropriate audit evidence regarding its existence and condition by attendance at physical inventory counting. (ISA 500.5) When in substantial doubt as to a material financial statement assertion, the auditor should express a qualified opinion or a disclaimer of opinion. (ISA 500.18) The Auditor General’s Ordinance 2001 under Section 13 specifically entitles the Auditor General to audit the accounts of stores and stock kept in any government office, however the scheduling of the certification audit does not allow for the presence at the physical inventory counts. The regularity audit generally covers the physical inspection of assets and inventories procured if existing at the time of the audit. In accordance with the procedures for the certification audit Step 4 of the Final Accounts Examination, the Auditor General assesses the type of audit certificate as unqualified, qualified, disclaimer, or adverse, depending on the nature and quantum of the disagreement/uncertainty.</td>
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(6) Analysis of Financial Statements

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<td>48. In regularity (financial) audit, and in other types of audit when applicable, the auditor should analyze the</td>
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<td>The results of the compliance tests do have an impact on the sample size for the substantive procedures, however the results of the compliance tests are not used to tailor the selection of sample transactions based on identified pattern of errors.</td>
<td>The new Financial Audit Manual should be implemented immediately discarding these mechanical procedures.</td>
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<td>The Auditor General’s Ordinance 2001 under Section 13 specifically entitles the Auditor General to audit the accounts of stores and stock kept in any government office, however the scheduling of the certification audit does not allow for the presence at the physical inventory counts. The regularity audit generally covers the physical inspection of assets and inventories procured if existing at the time of the audit. In accordance with the procedures for the certification audit Step 4 of the Final Accounts Examination, the Auditor General assesses the type of audit certificate as unqualified, qualified, disclaimer, or adverse, depending on the nature and quantum of the disagreement/uncertainty.</td>
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| financial statements to establish whether acceptable accounting standards for financial reporting and disclosure are complied with. (INTOSAI Auditing Standards 3.6.1) Analysis of financial statements should be performed to such a degree that a rational basis is obtained to express an opinion on the financial statements. The auditor should ascertain whether: 
(a) financial statements are prepared in accordance with acceptable accounting standards; 
(b) financial statements are presented with due consideration to the circumstances of the audited entity; 
(c) sufficient disclosures are presented about various elements of financial statements; and 
(d) the various elements of financial statements are properly evaluated, measured and presented. (ISA 200.2-200.12) | decision has been made to adopt the IPSAS – 2, cash flow statement standard with effect from FY2005-06 and to test run this by FY2004-05. The accounting policies are not disclosed in the Finance and Appropriation Accounts. The conversion to the NAM financial reporting framework would take time. The auditor’s ability to perform and use the various analysis of the financial statements is hampered when the financial statements only reflect the recording and disclosure of mere transactions and lack the meaningful and reliable information in respect of assets or liabilities balances. | compliance with Cash Basis IPSAS and should report all material departures in the audit report. The adoption of Cash Basis IPSAS would improve the AGP’s ability to do meaningful and reliable financial analysis. |
| **(7) Reporting on Financial Statements.** | This exists but not in a proper form. | The IPSAS and New Accounting Model should be identified as the relevant financial reporting framework in the audit certificate. The audit certificate should completely comply with the specimen formats given in the audit manual / procedures being followed. |
| 49. The auditor should provide an opinion paragraph in the audit report. (ISA 700.4) There should be a reference to the financial reporting framework used to prepare the financial statements (including identifying the country of origin of the financial reporting framework when the framework used is not International Accounting Standards). (ISA 700.12-15) The opinion paragraph should contain an expression of opinion on the financial statements stating the auditor’s opinion as to whether the financial statements give a true and fair view (or are presented fairly) in all material respects. (ISA 700.17) | There is no specific reference to the reporting framework. The only mention relates to the provisions of Section 5(a) of the Controller General of Account Ordinance 2001 read with the Article 169 of the Constitution. The opinion paragraph gives an expression that the financial statements “can be relied upon.” This is not consistent with the specimen audit reports given in the Procedures for the Certification Audit, which requires stating that “the accounts are complete and accurate in all material aspects.” | |
### Standard | Present position | Options for Improvement
--- | --- | ---
50. The SAI should provide a detailed report amplifying the opinion in circumstances in which it has been unable to give an unqualified opinion. Reports should be made where weaknesses exist in systems of financial control or accounting. (ISA 700.17) | The certification audit report does mention the other AGP reports covering aspects of financial governance or economical, efficient, and effective utilization of the public resources which are submitted separately to the President. These reports provide information relating to weaknesses in the system of financial control or accounting in addition to those mentioned in audit comments annexed to the audit certificate. | All the referenced AGP reports mentioned in the audit certificate on the financial statements should be reattached to the audit certificate. 

### (8) Reporting on Fraud
51. The SAI should report fraudulent practices or serious irregularities discovered by the auditors. (INTOSAI Auditing Standards 4.0.7) ISA 240 establishes standards and provides guidance on the auditor's responsibility to consider fraud and error in an audit of financial statements. The standard requires that — when planning and performing audit procedures and evaluating and reporting the results thereof — the auditor consider the risk of material misstatements in the financial statements resulting from fraud or error. | The Auditor General on specific request can provide information to the government agencies, including the National Accountability Bureau and the legislature, about a specific incident of fraud. Audits focus on examining transactions for discrepancies and regulatory breaches, and much of the reporting seems to relate to fraudulent behavior and suggesting recoveries without digging out the facts in detail. | Forensic audit training is needed. The Supreme Audit Institution does not focus on fraud in a sufficiently systematic way. ISA 240 requires the auditor to obtain information that is used to identify the risks of material misstatement due to fraud; and evaluate the design of the entity’s related controls, including relevant control activities, and determine whether they have been implemented. ISA 240 also requires the auditor to inform management of the auditee and the Board, if there is one, of any fraud and the failure in internal control that led to the fraud. The auditor’s report should identify the action that the entity is taking about the fraud. 

### (9) Reporting on Compliance
52. With regard to regularity audits, does the auditor prepare a written report, which may either be a part of the report on the financial statements or a separate report, on the tests of compliance with applicable laws | Reports submitted to the Parliament:  
- Annual Regularity Audit  
- Special Audit Reports  
- Performance Audit Reports | The general tendency is for the audit to cover and report on all issues confronting an organization instead of emphasizing issues as compliance type and other most critical
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| and regulations? (INTOSAI Auditing Standards 4.0.7) | • Environmental Audit Reports  
• Governance Audit Reports  
• Procurement Audit (Proposed)  
• Third Party Validations  
• Foreign Aided Projects – Financial Statements Certification. | issues. The audit report can add significant value if the auditors focus on more critical issues with impact on the organization |