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# THE BANGLADESH ACCOUNTANT

January-March 2012

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## PUBLIC SECTOR ACCOUNTABILITY

The Bangladesh Accountant

Public Sector Accountability

January-March 2012

ইসলামী ব্যাংক আমার ব্যাংক



বিন্দু বিন্দু করেই মহাসিন্ধু.....

ইসলামী ব্যাংক

একাল আগামীকাল মহাকালের ব্যাংক

আমরা বর্তমানের সঞ্চয় দিয়ে গড়ে তুলছি

আমাদের ভবিষ্যত প্রজন্মের অপার সম্ভাবনা

গ্রাম-বাংলার মানুষের সঞ্চয় অভ্যাস সৃষ্টি ও সঞ্চয় সেবার মধ্য দিয়ে গড়ে উঠেছে আমাদের ২৯.১ হাজার কোটি টাকার আমানত তহবিল। ৬০ লাখ গ্রাহকের মুদ্র সঞ্চয়ের সে অর্থ থেকেই আমরা মানুষের মৌলিক চাহিদা পূরণ ও দেশের আর্থ-সামাজিক উন্নয়নে বিনিয়োগ করছি। সকল ক্ষেত্রেই গুরুত্ব দিচ্ছি সবুজ ব্যাংকিংকে। কাজ করছি, দেশ-জাতি ও আর্ট-মানবতার সেবায়।

আমাদের ২৫১টি শাখায় সকল শাখায় রয়েছে অনলাইন সুবিধাসহ আধুনিক ব্যাংকিং সেবার নব সংযোজন। রেমিট্যান্স আয়েরসহ বৈদেশিক বাণিজ্যের জন্য রয়েছে বিশাল আন্তর্জাতিক নেটওয়ার্ক।

আমাদের ১০ হাজার কর্মী আপনার সেবায় নিয়োজিত।



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The issue of Public Sector Accounting is one of the most pressing one following the global financial crisis and sovereign debt crisis around the world. The emphasis on improved governmental financial reporting and popular demand of accountability and transparency is felt more than ever before. Catering to the needs of diverse stakeholder groups, particularly the citizenry of the concerned states, it is necessary to bring timely changes in robust public sector financial management ensuring high quality financial reporting and credible auditing systems.

The international conference held on the theme of "Strengthening Bangladesh Public Sector Accounting and Auditing- Global Reforms and The Way Forward" few months back was a manifestation of the ICAB's proactive initiatives and firm

commitment to serve the public interest and adding value to the economic growth of the nation. The conference envisaged ICAB to serve as an effective forum of interaction among Government planners and decision makers, donor agencies, regulators and professional experts in the accounting fraternity. Effective Public Financial Management can come through better quality Accounting and Public Auditing process. Adoption of International Standards on Auditing provides the basis for financial reporting with greater transparency.

It is at this backdrop that the Editorial Board of ICAB decided to focus on the theme "Public Sector Accountability" in the current issue of the Journal. I believe the contents of this issue will add to the knowledge of our readers and generate thoughts and address the urgent issues in depth.

Lastly, I would expect feedbacks from our esteemed readers, their suggestions and opinions would help us bringing meaningful improvement or any shortcomings that the journal might have.

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**M. Farhad Hussain FCA**  
Chairman, Editorial Board



## INSTILL CONFIDENCE IN ACCOUNTING PROFESSION OF BANGLADESH

Bangladesh, despite having many challenges still shows positive trends to be an emerging economy. The country is getting prominence internationally for many reasons and undoubtedly, accounting professionals has many opportunities with bigger responsibilities. The Institute of Chartered Accountants of Bangladesh (ICAB) has been playing significant role for capacity building of the accounting profession. The Institution is also taking active part in many development agendas, suggesting measures against the impediments for development, creating awareness, promoting sustainable growth and policy of the nation through its activities. ICAB has strengthened its institutional capacity to provide confidence to its stakeholders besides assisting its members and students.

The present demand for services of Chartered Accountants (CAs) in Bangladesh far exceeds its supply and ICAB is bringing reforms and proactive action plans to increase its membership by attracting more quality students. The institute is constantly focusing on the quality professionals enriched with highest state of ethics and responsibility. To achieve those standards, the institute has given

due importance on holding adequate training, members conferences, seminar including sessions on ethics, etiquettes etc regularly. Beside its own domain, ICAB is also imparting training to NGOs, power sector professionals and other Government organizations whenever requested.

ICAB has been working to ensure that its curriculum and examination processes are at par with global standards. Since, ICAB signed an MOU with the ICAEW in 2009, new curriculum has been introduced, and examination procedures have been standardized. Now, members of ICAB can become ICAEW members after passing only three paper exams and completing ICAEWs Structured Training in Ethics. ICAB is also pursuing reciprocity agreements for its members with other renowned Institutes of the world.

As a member of IFAC, ICAB is obligated to adopt and disseminate the knowledge and application of Accounting Standards issued by International Accounting Standards Board (IASB). The Institute is drawing much attention to ensure the observance of standard through its "Quality Assurance Board" (QAB). ICAB

has taken the initiative to launch the workshop in association with IFRS Foundation UK and SAFA in Bangladesh for the first time. The presenters were the IFRS experts Mr. Paul Pacter (Member, IASB, UK and IFRS expert) and Mr. Michael Wells (Director, IFRS Education Initiative, and International Accounting Standards Board (IASB) and IFRS trainer). With the recent observance of SMEs contribution to the world economy, the workshop on IFRS for SMEs holds great importance for Bangladesh. It is tested that the Small and medium-sized enterprises (SMEs) play a critical role in innovation, advancement, and sustainable development of world economies.

The increasing demand on good corporate reporting and disclosure has broadened the role of the accounting professionals more than ever. Apart from specialized traditional Accounting and auditing services, the chartered accountants now render many more than they had been doing so far. Now it stresses that that traditional financial reporting boundaries should also include information on environmental issues and corporate social responsibility carried out by the company. Accountants need to



take the lead in managing risk of maintaining sustainable reporting besides their traditional role in financial reporting. ICAB deeply believe that sustainability reporting is essential for moving the nation forward. ICAB manifested its commitment by holding international conference before and would like to do so in its future endeavor.

Despite ICAB's contribution, the CA profession was never without problems, many are because of misconception, and some are due to lack of self awareness of the professionals. Despite that, accountancy profession in Bangladesh has grown to support the changed business and economic climate where the noble role of CAs is undeniable. The role

of ICAB members as decision-makers, auditors and consultants to ensure sustainable reporting can bring the business organization under scrutiny which ultimately leads towards sustainable development. Therefore, ICAB is committed to work towards transparency and accountability in accounting, auditing and reporting by adapting international standards. We are ready to work and collaborate with accounting professionals, government, non-government agencies and business leaders towards development and progress of the nation.

ICAB, being one of the prime institutions of the country, would like to establish itself as think-tank

of the nation. ICAB responded to the crises issues like share market, its demutualization, good corporate governance, forthcoming national budget etc along with its key professional issues and never hesitated suggestion, speeded thought provoking ideas to the concerned and the citizens as a whole.

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**Md. Syful Islam FCA**  
President, ICAB



# Strengthening Public Sector Accounting and Auditing in Bangladesh

Anwaruddin Chowdhury FCA



## Executive Summary

As we stand on the threshold of the second decade of the new Millennium, in the wake of 9/11 (nine eleven) and the West's so called "war on terror" on the political front; the corporate frauds in the last decade, and now confronting the implications of the "global financial crisis", (the worst economic recession in history), together with environmental issues like global warming - Bangladesh has demonstrated remarkable resilience and proactive responses to these diverse global challenges- warranting concerted global actions in this progressively evolving scenario, and provoking well-focused and politically sensitized debates, summits and conferences.

The events of the past three years have highlighted the need for economies all round the world to have access to reliable financial information as a precondition for the restoration of confidence in the global marketplace. This is a need that Accountants are uniquely prepared to meet, whether as preparers or auditors of financial statements, as business advisers or indeed as regulators. The standard setters and accounting professionals firmly believe that well presented financial reports act as a 'sine-quo-non' to the

proper functioning of a developing economy like Bangladesh.

The first Ministerial meeting of the WTO held in December 1996 had identified Accountancy as the most internationalized and the most important service sector for promoting trans-border flow of funds. Good financial reports promote investor confidence, facilitate the flow of investment funds and thereby encourage economic growth. Financial Reporting is the "lingua franca" of business. The language of business has now taken a specific dimension- that of the International Accounting Standards / International Financial Reporting Standards (IAS/IFRS), promulgated by the International Accounting Standards Board (IASB), and by process of analogy for audit purposes- that of the International Standards on Auditing (ISA), issued by the IAASB of the International Federation of Accountants (IFAC). The application of IAS/IFRS renders high quality financial information that satisfies the "qualitative characteristics" of understandability, relevance, reliability and comparability. By process of analogy, harmonization in Government/ public sector accounting and auditing through convergence onto Accrual based IPSAS and ISSAI or ISA respectively, would render high quality reporting and credible audit of the

Government departments and public sector entities/ institutions.

CAPA's Policy Statement fully supports the convergence towards IPSAS by all member countries in the Asia Pacific region to assist in the improvement of public sector financial management. From a public interest perspective, effective monitoring of financial performance within public sector entities is critical. CAPA supports accrual-based financial reporting as the only means to provide necessary high quality, transparent reporting of public sector activities and position.

The Global Financial Crisis and recent Sovereign Debt Crisis around the world, has warranted greater emphasis on improved governmental financial reporting and increased levels of accountability and transparency in public financial management. Many countries initially adopting cash-based accounting have moved to sophisticated modified cash or accrual basis. A recent Report by the IPSAS Board indicated that over 80 countries have either adopted or have processes in place to adopt international accounting standards for public sector financial management reporting, including several Asian countries.

The Office of CAG Bangladesh has traditionally practiced a reliable system of cash basis Government Accounting, reportedly ensuring adequate levels of transparency and accountability. In recent years and in line with global reforms, the OACG has consolidated its traditional method through compliance with the Cash Basis IPSAS (Financial Reporting under the Cash Basis of Accounting) for the country's Public Sector Accounting and Auditing. Given adequate resources and technical support, the OACG is prepared to implement Accrual based accounting on a pilot basis and then move onto Accrual based IPSAS. The CAG

Bangladesh is also reportedly compliant with the INTOSAI Auditing Standards. The CAG has also committed to implement IFAC endorsed ISSAIs within a feasibly practicable timeframe for "audit" of Government/ public sector institutions.

The essential "objective" of this Paper is to review the status of Public Sector Accounting and Auditing in Bangladesh – evaluate the present Challenges and aim at formulating Strategies (policy issues and recommendations) for future "strengthening of public sector financial management reporting", in accordance with the best regional and global practices. There are debatable, futuristic and pluralistic connotations in the subject and the field of discussion is so vast that one can hardly do justice to its magnanimity in a limited page technical Paper, endeavouring to synthesize the Bangladesh Perspectives of Public Sector Accounting and Auditing.

### **Preamble**

The globalization of economies poses "challenges" both for the developed and developing world. Bangladesh itself confronts a multitude of global challenges (internal and external) which need to be addressed by concerned authorities - ranging from such issues as corruption, bureaucracy and governance on the one hand to poverty alleviation and employment generation on the other. These "challenges" also encompass Government responses to the impact of such globalization forces as unification of economies and establishment of trading blocks; acquisition and mergers of corporate entities into conglomerates; phenomenal advancement in information, communication technologies; innovative solutions for electronic business transformation and mobile wallet applications; banking sector technological

“ WITH THE INCREASED EMPHASIS ON ACCOUNTABILITY IN THE GOVERNMENT ENVIRONMENT, THE ROLE OF PUBLIC SECTOR AUDITING HAS BECOME INCREASINGLY IMPORTANT. THE CONCEPT OF ACCOUNTABILITY FOR PUBLIC RESOURCES IS KEY IN OUR NATION'S GOVERNING PROCESS AND A CRITICAL ELEMENT FOR A HEALTHY DEMOCRACY. LEGISLATORS, GOVERNMENT OFFICIALS, AND THE PUBLIC WANT TO KNOW WHETHER GOVERNMENT SERVICES ARE BEING PROVIDED EFFICIENTLY, EFFECTIVELY, ECONOMICALLY, AND IN COMPLIANCE WITH LAWS, RULES AND REGULATIONS. ”



automation for payments/settlement and electronic funds transfer; financial inclusion and digitalization of the country (Vision 2021); harmonization of financial reporting and audit practices as a vehicle for economic growth; capital market development; changes in legal regulatory frameworks for implementation of corporate governance and social reporting practices; and ensuring improved reporting, monitoring and oversight of public sector financial management aimed at better governance through increased levels of accountability and transparency in Government accounting and auditing.

The Global Financial Crisis (GFC) 2008-09 (triggered by the US sub-prime mortgage market collapse and imposing colossal trillion dollar Government bailout packages in the developed economies), escalated by the recent Eurozone Sovereign Debt Crisis (with consequential contraction of major European economies), is precipitating the entire global economy into a deep recession. While Bangladesh and the regional countries have demonstrated remarkable

resilience earlier, our Governments are now seriously concerned on safeguarding our national economies against the repercussions of the deteriorating global recession (negative impact on macro-economic stability and economic growth). The prevailing global economic scenario has concurrently accentuated the need for improved Government financial reporting, for ensuring enhanced levels transparency and accountability. In this backdrop, the Conference theme of "Strengthening Bangladesh Public Sector Accounting and Auditing- Global Reforms and The Way Forward" is both timely and topical.

The Conference is a manifestation of the ICAB and CAPA's proactive initiatives and firm commitment to serving the public interest and adding value to the economic growth of the region, It is envisaged to serve as an effective forum of interaction among Government planners and decision makers, donor agencies, regulators and professional experts in the accounting fraternity. The Conference is envisaged to catalyze Government recognition to effect necessary changes for

implementing robust public sector financial management, ensuring high quality financial reporting and credible auditing systems, catering to the needs of diverse stakeholder groups, particularly the citizenry of the concerned states.

The simmering GFC has highlighted the critical nature of financial reporting for proper functioning of markets and the importance of achieving a single set of high quality accounting/reporting standards. The G-20 Summit in Pittsburg in November '09, declared the GFC as a global problem which required a common, strategic approach for devising a global solution. The Summit leaders underscored the need for convergence onto a uniform set of high quality globally harmonized financial reporting standards, and accentuated on the critical role of Accountants for restoration of market confidence and recovery of the global economy. Albeit the reference was to private sector financial reporting and audit based on the IAS/IFRS and the ISA respectively, the substance of the statements is equally significant for public sector accounting and auditing. Hence, this Conference imparts the added dimension of deliberating on issues of harmonization of public sector accounting and audit practices through implementation of IPSAS and ISSAI.

The credit crisis has raised several public sector accounting issues. Governments have extended credit to banks, guaranteed the liabilities of banks, purchased impaired debt instruments and in some instances have assumed control of banks. The unique nature of the credit crisis and the unprecedented response by Governments around the world has reinforced the importance of high-quality standards for financial reporting by

Governments. The credit crisis has increased the need for accountability in the public sector and for transparency in its financial dealings and thus the implementation of IPSAS by the economies.

This Conference will evaluate the present "challenges" and aim at devising "strategies" for the future development of public sector accounting and auditing in Bangladesh. Speakers will explore various topics including the global scenario of public sector financial management and developments in the region, country experiences in transition to accrual-based accounting, and the future directions of fiscal sustainability in Bangladesh and the Asia Pacific region.

## **Public Sector Management And Accountability In Bangladesh**

### **Importance of Public Sector Management in the Economy**

The Public Sector emerged as the driver of economic growth consequent to the industrial revolution in Europe. With the advent of globalization, the public sector faced new challenges in the developed economies. Public sector management is one of the basic elements of Bangladesh's governance structure with the aim at achieving greater efficiencies in governmental operations, reduce corruption and system losses. However in practice, the public sector has encountered governance issues to prevent rampant corruption, causing significant wastage of national resources. Public financial management is an integral component of the overall management process in the country. It plays a significant role in the economic, efficient and effective use of public resources.



Therefore, high quality public sector financial management, incorporating high quality accounting and auditing practices is indispensable for national economic growth. Public Sector Accounting and Auditing are necessary for proper procurement of Government resources; supply of goods and services through formation of budgets; recording and reporting of assets and liabilities; and Keeping proper records for preparation of accounts and presentation of financial information for decision making purposes.

### **Bangladesh Economy- Recent GDP Growth and Macro-economic Stability**

Bangladesh has made significant strides in its economic sector performance since 1971. It recorded 6.7 % GDP growth fiscal 2010-11. Bangladesh is considered

as a developing economy, which has recorded GDP growth above 5% during the last several years. Microcredit has been a major driver of economic development in Bangladesh. Although over 60 % of the population is employed in the agriculture sector, about 70 % of exports revenues are derived from the readymade garments industry. The biggest obstacles to sustainable development in Bangladesh are overpopulation, poor infrastructure, corruption, political instability and a slow implementation of economic reforms. GDP growth for the current 2011-12 is expected to exceed 6%, although inflation is spiralling and investment declining. At present, the country's foreign exchange reserves exceed US \$ 10 billion and inward remittances amount to US \$ 11 billion.

However, maintaining the enabling

environment to allow a repeat of the growth performance in FY12 will be a challenging task considering the growing downside risks. The capital (securities) market is on a significant downward trend with Dhaka Stock Exchange market capitalization having declined drastically from about US \$ 47 billion in 2009 to US \$ 24 billion present. There is a credit crunch in the economy and the Government is borrowing heavily from the banking sector to finance its public expenditure and annual development programmes. Foreign and domestic investment in the economy is also on a downward trend. Despite the apparent negativities, Bangladesh's macro-economic stability is satisfactory and the country's economic management has been applauded by the donor communities. Bangladesh is presently termed as one of the next 11 emerging economies worldwide.

### Accountability Overview

The concept of Public Accountability in social form is as old as human history, being traceable to Babylonian civilization around 2050 BC. 'Accountability' connotes an "obligation to give an account or be answerable for a duty or trust conferred". Financial accountability is indispensable for achieving economic success. The motives behind the establishment of the public sector institutions are economic growth, social welfare, and promotion of distributive justice. The public sector has different primary objectives compared to that of the private sector. These encompass socio-political and macroeconomic objectives like poverty alleviation, employment generation, economic growth, ensuring good governance, accountability and transparency in decision-making

process through quality financial reporting and credibility in auditing process. Sound financial management and reporting a sine-quo-non for achieving adequate levels of transparency, accountability, fiscal sustainability and thereby improved governance.

Public sector auditing is a key element to ensuring the government's accountability to all stakeholders in the public interest. Public sector accounting and auditing standards provide frameworks for high quality reporting and auditing, enabling improved government management, decision-making, oversight and accountability. PPP can strengthen these objectives.

### Public Sector Accountability in Bangladesh

The GOB must ensure that public funds are expended in the optimum manner, ensuring economy, efficiency, and effectiveness and reflecting accountability of expenditure decisions and transparency of information. To ensure proper financial management, there must be an adequate system of budgeting, accounting and financial reporting, internal control and Auditing of the Government Ministries & Divisions, LGIs, Sector Corporations, Missions, SOEs and SOBs. Accountability refers to stewardship of resources and individuals entrusted for their utilization and management. The essential components of accountability include

- Accountability for:
- financial resources;
  - faithful compliance and adherence to legal requirements and administrative policies;
  - efficiency and economy in operation;

- results of government programmes, reflecting their accomplishments and effectiveness.

Accountability in the public sector environment is a very complex process. Public sector auditing is regarded as an essential tool for ensuring accountability. Financial Accountability of the Government departments and institutions has become a well-publicized, widely debated, somewhat sensitively politicized issue, being frequently discussed by the Donor community, civil society and professional groups. Bangladesh's development partners also favour strengthening of the sectoral development process, particularly emphasizing LGIs and the SOEs/SOBs and foreign aided projects.

With the increased emphasis on accountability in the government environment, the role of public sector auditing has become increasingly important. The concept of accountability for public resources is key in our nation's governing process and a critical element for a healthy democracy. Legislators, government officials, and the public want to know whether government services are being provided efficiently, effectively, economically, and in compliance with laws, rules and regulations. They also want to know whether government programs are achieving their objectives and desired outcomes, and at what cost. Government officials are accountable to legislative bodies and the public for their activities and related results.

### Review Of Public Sector Accounting And Auditing Status In Bangladesh

#### Public Sector Accounting in

## **Bangladesh - Office of the Comptroller and Auditor General**

Public Sector Accounting system and maintenance of public accounts in Bangladesh, dates back to the mid-1800s, the days of British-occupied India. Since its independence in 1971, Bangladesh has started a series of reforms in the accounting and auditing fields in association with donor agencies. The Accounts Code was revised and updated in 1996 with the UK DFID funding. During 2000 and 2001, Government Audit Codes, Audit Standards, Code of Ethics and Manuals for Audit Directorates were developed and updated with technical assistance from UNDP, DFID and Netherlands Govt.

The powers and functions of the Auditor General in relation to keeping of accounts of the Government [Section 3(1)] are incorporated through enactment of the Comptroller and Auditor General (CAG) Additional Functions Act 1974 and CAG amendment act 1975. It conferred some additional functions including the preparation of appropriation and finance accounts as well as the preparation of commercial accounts and general financial statements. The CAG's office prepares the annual Appropriation Account of the Government, which is submitted, to the President who causes them to be laid before Parliament under Article 132 of the Constitution. Section 5 of this Act gave legal mandate to the audit responsibility of the Auditor General in respect of audit of accounts of local authorities and statutory public bodies. This section has strengthened the position of the Auditor General with regard to audit of accounts of statutory public authorities, public enterprises, corporations, and local authorities.

The Office of the Comptroller and Auditor General (OCAG) is the Supreme Audit Institution (SAI) of Bangladesh, being a constitutionally established office, independent of the government for discharge of its power and functions. Article 128(4) of the Constitution provides that OCAG shall not be subject to the direction and control of any person or authority. The mandated responsibility of the Constitution ensures that the CAG plays the key role in both public sectors accounting and auditing for GOB.

In 1985, the Ministry of Finance, by an Executive Order passed the task of maintaining accounts to a newly established office of Controller General of Accounts (CGA) but the legal framework remained as before. The CGA is still under the administrative control of the CAG for his officers and staff. Practical separation, from a functional perspective, is now being implemented.

Bangladesh, being a parliamentary democratic form of Government, the control of public finance is the exclusive prerogative of the Parliament. Article 83 of the Constitution of the People's Republic of Bangladesh lays down that no tax shall be levied or collected except by or under the authority of an Act of Parliament. The financial procedures are laid down in Articles 81-92 in Part V of Chapter II of the Constitution. Article 87 of the Constitution requires a statement in respect of each financial year, known as the Annual Financial Statement, of the estimated receipts and expenditures of the government for the year be laid before the Parliament. The final stage in the process of disbursement and appropriation in implementing the budget is audit of the government accounts to ensure that obligations

and outlays follow the provisions of the authorizing and appropriating legislation and adherence to rules and regulations in incurring expenditure of funds.

In the cycle of accountability, under S. 131 of the Constitution, the CAG is empowered and legally responsible to prescribe forms and determine the manner, for preparation and maintenance of Government accounts and formulation of Government Accounting Standards. The CAG Accounts Code describes the forms and manner for compilation and disclosure Government Accounts, as well as for the Audit of the Government accounts. The Public Accounts Committee, which considers the reports along with the principal accounting officers of the departments and ministries, constitute important links.

The Controller General of Accounts (CGA) is entrusted with matters related to Government Accounts. The Government Accounts comprise of Appropriation Accounts and Financial Accounts. Three are Four Appropriation Accounts relating to Civil, Defense, T&T and Railways-which are compiled by 3 Accounting Circles under CAG. The Finance Accounts comprise of the Government's Balance sheet prepared under the cash basis, incorporating cash and other balances.

Government Accounts are kept on Cash basis by single entry method, as distinct from commercial accounts prepared under Accrual accounting double entry system (involving "preparation" of Manufacturing, Trading and Profit and Loss Accounts and a Balance Sheet for the purpose of determining the profitability and financial position of an entity at a particular date.) However, the

CAG Public Sector Accounts are now purportedly prepared as compliant with Cash Basis IPSAS (Financial Reporting under the Cash Basis of Accounting), showing detailed particulars of cash flow movements. Accounts compilation process in the CGA has been recently computerized and the Account Code updated accordingly. Donor funded reform initiatives for conversion of Railways accounts to accrual basis are in progress.

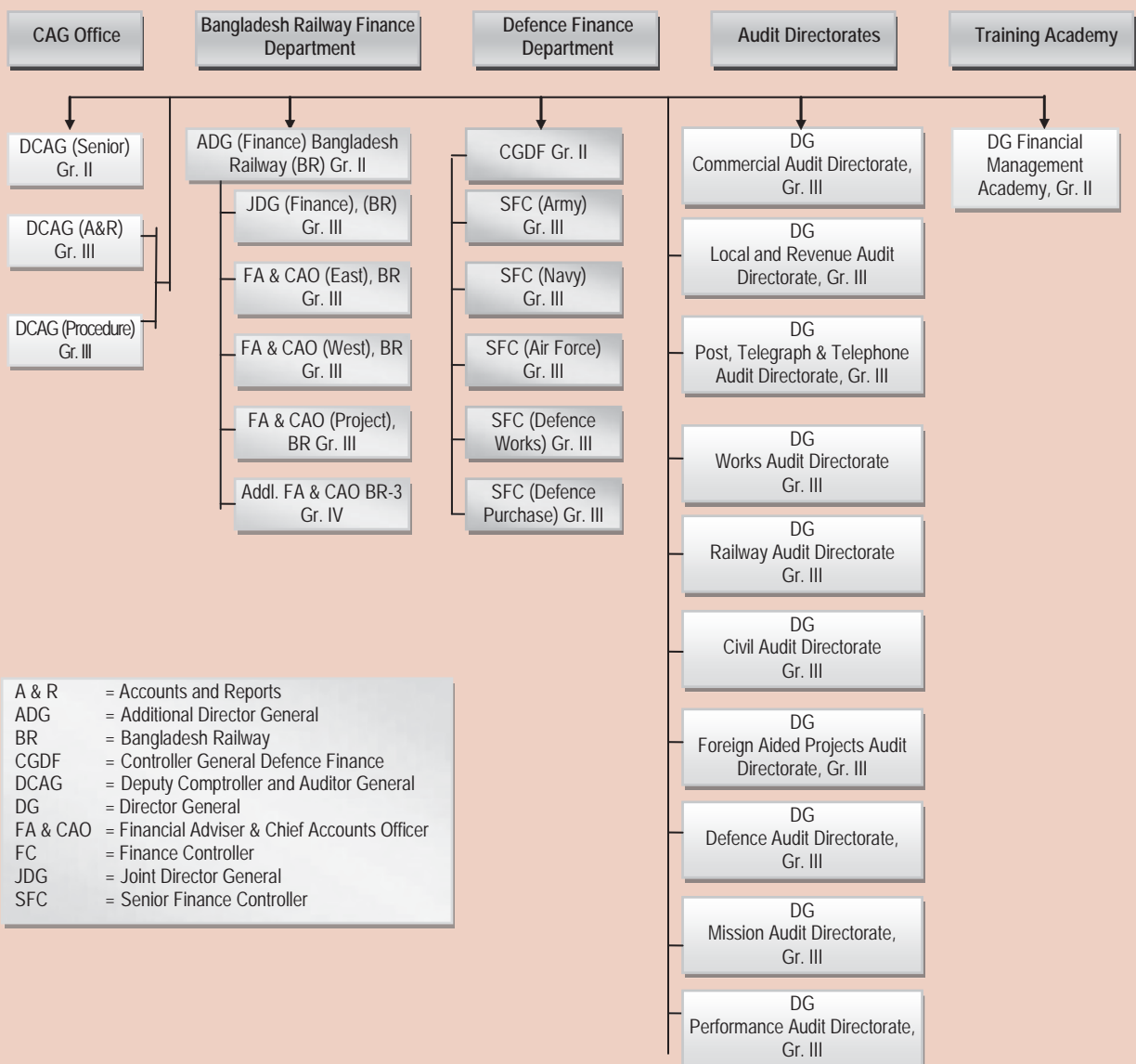
Government accounts are maintained for accountability of the Government

and ensuring transparency and good governance of the country, and not for making profit. Government transactions are made in 35 or more Ministries, Departments, Directorates, Law Courts and other Agencies. The Government accounts/ payments are classified under numerous heads for identifying the nature of payments or receipts and the department to which it may relate.

The CAG/Auditor General is the head of the Government Audit Department. The OCAG has

under him ten Directorates of Audit including the Directorate of Commercial Audit, Directorate of Works Audit, Directorate of Civil Audit, Directorate of Mission Audit, Directorate of Defence Audit, Directorate of Posts, Telegraphs and Telephone Audit, Directorate of Railway Audit, Directorate of Foreign Aided Projects Audit and the Financial Management Academy (Exhibit-1).

**Exhibit 1: OCAG Organogram**



- A & R = Accounts and Reports
- ADG = Additional Director General
- BR = Bangladesh Railway
- CGDF = Controller General Defence Finance
- DCAG = Deputy Comptroller and Auditor General
- DG = Director General
- FA & CAO = Financial Adviser & Chief Accounts Officer
- FC = Finance Controller
- JDG = Joint Director General
- SFC = Senior Finance Controller

## Public Sector Auditing in Bangladesh

In addition to CAG (DG Commercial Audit), an external, independent audit by CA Firms is conducted annually in respect of autonomous bodies, sector corporations, SOEs and SOBs. Two independent Firms of Joint Auditors are appointed to undertake the audit of such public sector entities (just like the audit of private sector entities). The Auditors (Chartered Accountants Firms) submit their usual Audit Report as well as a Confidential Report addressed to the Secretary of the concerned Ministry (SOBs-Finance). These reports are not addressed to the stakeholders as is the practice in the case of private sector audits. Government Ministries, Divisions, Departments, Subordinate Government offices, and Local Government Institutions are completely outside the purview of any kind of external professional audit by independent firms of Chartered Accountants.

### Exhibit 1: OCAG Organogram

- Government Ministries
- Divisions and Departments
- Subordinate Offices
- Foreign Aided Project
- Local Government Institutions
- Autonomous Bodies
- Statutory Corporations
- Public Sector Enterprises
- Public Sector Financial Institutions
- Foreign Diplomatic Missions,

While the OCAG has not defined Auditing in its absolute context, the Government Auditing Standards issued by authority of CAG has described Financial Statement Audits as the examination of the

financial statements of an audited entity with the primary objective of expressing an opinion on whether the financial statements truly present the expenditures and receipts in the case of accounts prepared on cash basis (government accounts). In the case of accrual accounts, the opinion shall be whether financial statements present a true and fair picture of the financial position results of operations, and cash flows. Financial statement audits can be of government ministries and government commercial enterprises. The audit of government commercial enterprises involves reviewing, commenting upon, or supplementing, the audit report of the statutory auditor of the enterprise, and/or conducting supplementary audit as considered appropriate.

It is apparent that the Government Audit makes a clear distinction between Receipts & Payments Audit (cash based accounts) and True and Fair View Audit (accruals based accounts), depending on the accounting system used. The CAG powers and responsibilities have been established by Bangladesh Constitution. In the performance of his functions, the CAG is independent of the Executive Government. The CAG is accountable to the Parliament, and not to any Government Ministry. The Constitution of the People's of Bangladesh places the OCAG and CAG in a unique position of trust which requires that all work of the office be carried out in accordance with the highest professional standards. This entrusts the CAG with a responsibility to ensure high standards of quality, adopt best practices and set benchmarks against which to measure the quality and audit work output. It is therefore incumbent upon the CAG to establish and codify

internationally acceptable and modern professional standards to govern CAG audit work efficiently and effectively.

The CAG is empowered to conduct audits of the financial administration and performance management processes of the public sector. The legislation requires that professional standards and practices must be adopted in the performance of audits. In doing so, audits will not necessarily detect fraud or waste in the use of public funds. While auditors should be alert to situations, which may entail such occurrences, audits are primarily directed to forming opinions on:

- the completeness and accuracy of recording and reporting financial transactions
- compliances with the Government's internal administrative control procedures, and
- systems to manage the achievement of required performance outcomes.

The CAG has a responsibility to report to the Parliament at least once each year on any matters arising from the exercise of these auditing powers. In doing so, the Auditor-General is providing an independent and credible source of information to the Parliament. It can use this information to assist its responsibility to have the Government remain accountable for the performance of the public sector entities, which administer the Government's directives. OCAG performs oversight functions and should provide an unbiased objective assessment regarding the utilization of public funds in economic, efficient, and effective manner (value for money audit).

Rules regarding accounting and auditing of public sector corporations are outlined in the ordinances for establishing the organization. However, the wordings of the various ordinances are identical. Corporations Nationalization Order (PO 27) requests audit of corporations by Chartered Accountants Firms: "is to

be audited by Chartered Accountant firms".

It is apparent that the government audit aims at ensuring that the financial transactions of the government are executed properly under sanctions and authorities, are correctly recorded, and conform to the rules of financial

propriety. As such, it is an audit to ensure that public funds are not misused. It has been often argued that government audit; with its emphasis on compliance with rules and procedures, tends to stifle the initiative of executives and adversely affects their performance.

### Exhibit 3 - Legal Jurisdiction of Public Sector Audit

Government / Public Sector Organisations	Applicable Laws	Audit authority/by
Ministries	Constitution	C AG
Departments/ Divi sions/Directorates	Constitution	CAG
Autonomous /Semi Autonomous Bodies	CAG (Addl. Functions) Act.	CAG CA firms
Local authorities	Relevant laws	CAG, CA Firms
State Owned Banks and DFIs	CAG (Addl. Functions) Act.	CAG, CA firms
Government Owned Ent ities (PLC)	CAG (Addl Func) /CA 1994	CAG, CA Firms
Nationalised industries	Nationalisation Order,1972	CAG, CA Firms
Foreign Aided Projects	CAG (Addl Func Act), Donor	CAG, CA firms
Government Educational institutions/Hospitals	Constitution	CAG

## The Role of Public Sector Accounting and Auditing Standards

### Role of International Public Sector Accounting Standards (IPSAS) - An Overview

The IPSAS represent international best practice in financial reporting by public sector entities. In many jurisdictions, the application of the requirements of IPSASs has enhanced the accountability and transparency of the financial reports prepared by Governments and their agencies.

IPSAS are developed by the International Public Sector Accounting Standards Board (IPSASB), an independent standard setting body under the auspices of the IFAC. While the IPSASB has no power to compel countries to adopt IPSAS, the standards do play an increasingly important role in the development and revision of

national public sector accounting standards. IPSAS has taken on this important role because the standards reflect an accrual-based approach not found in most other public sector frameworks and provide universal standards that are not based on individual national laws. IFAC's IPSASB has developed Standards that apply to both the accrual basis and the cash basis of accounting. At present, there are 32 IPSAS on the accrual basis of accounting and one standard on the cash basis of accounting (Appendix II). Countries are adopting the cash based standards see this as a stepping-stone towards the eventual adaption of the accruals-based IPSAS. The IPSASB has also developed guidance on the transition from cash- to accrual-based reporting. The traditional emphasis on cash accounting has been found inadequate through failure to recognize true costs, and all assets and liabilities. Cash accounting can

too easily neglect asset management, accumulating arrears, future liabilities (e.g. pensions), and contingent liabilities (e.g., guarantees).

**Global Adoption of IPSAS**  
Many countries initially adopting cash based accounting have moved to more sophisticated modified cash or accrual based accounting. A recent IPSASB report stated that over 80 countries either have adopted, or have processes in place to adopt, international accounting standards for public sector financial management reporting, including a number of Asian countries.

Australia, New Zealand, and Canada have chosen not to fully adopt IPSAS and have developed their own accounting standards for the public sector. However, the UK public sector has chosen to adopt IFRS to be supplemented by IPSAS as necessary. New Zealand was the

first country to apply Accrual accounting in the public sector followed by Australia. Korea dominates public sector accrual accounting in Asia. South Africa and Kenya have also started implementing public sector accrual accounting based on IPSAS. Central Government accounts in Germany, Ireland, and Spain are based on cash basis accounting method while other countries of European Union like Finland, Sweden and the United Kingdom use full accrual accounting and some (Belgium, Denmark, and Italy) use hybrid systems accounting that incorporate elements of both methods.

### IPSAS and the UN

The UN General Assembly adopted IPSAS in 2006 for deriving the following benefits:

- Improved internal control and transparency with respect to assets and liabilities generally;
- The alignment with best accounting practices through the application of credible, independent accounting standards on a full accrual basis;
- More comprehensive information about costs that will better support results based management;
- The integration of non expendable equipment in to

the accounting system, with resulting improvements in the accuracy and completeness of non-expendable equipment record;

- Improved consistency and comparability of financial statements as a result of the detailed requirements and guidance provided in each standard.
- Improved allocation of resources

Although in many developing countries the cash based IPSAS are seen as a transitional step towards the future adoption of accrual accounting, in reality this may take many years to accomplish.

### Exhibit 4 - Public Sector Accounting Implementation Status in SAARC Countries

India	<ul style="list-style-type: none"> <li>• Union &amp; State Government – Cash Accounting</li> <li>• Local bodies moving to Accrual-Based Accounting</li> <li>• ICAI technical assistance to local bodies for implementation of Accrual accounting system and developed important guidelines towards Government Accounts. Government Accounting Standards Advisory Board (GASAB) is developing Accrual-based Government Accounting Standards</li> <li>• World Bank funded Pilot Project are underway for Accrual accounting</li> <li>• World Bank and Union Government are working together for adaptation of IPSAS</li> </ul>
Pakistan	<ul style="list-style-type: none"> <li>• Federal &amp; Provincial Government – Cash based IPSA, moving to Accrual Accounting</li> <li>• Local bodies moving to Modified Cash Accounting</li> <li>• Accounting Model being implemented for conversion into Accrual Accounting</li> <li>• CGA &amp; AG are cognizant of IPSAS</li> <li>• ICAP and ICMAP are cognizant of IPSAS</li> </ul>
Sri Lanka	<ul style="list-style-type: none"> <li>• Central Government &amp; Provincial Councils - adopted Cash IPSAS and moving to Accrual based Standards</li> <li>• Local bodies applying Accrual Accounting partially.</li> <li>• ICASL's Public Sector Committee is developing Accrual-Based Accounting Standards for use by PSEs based on IPSAS</li> </ul>
Bangladesh	<ul style="list-style-type: none"> <li>• Central Government – Cash Based IPSAS</li> <li>• Local Government Institution- Cash Accounting</li> <li>• Autonomous Bodies, Sector Corporations and SOEs-Accrual Accounting</li> <li>• Foreign Aided Project – IPSAS Compliant and Accrual Accounting</li> <li>• ICAB set up a Committee on Government Accounting System</li> <li>• ICAB members cognizant of IPSAS</li> </ul>
Nepal	<ul style="list-style-type: none"> <li>• Cash-Based Government Accounting System</li> <li>• IPSAS are included in the curriculum of ICAN</li> <li>• Plans for movement to Accrual-Based Accounting System</li> </ul>

## IPSAS in Bangladesh

- In Bangladesh there is no objective implementation of IPSAS in Government Accounts. Accrual accounting has not been adopted or implemented in any form or manner by the CAG office in Government Accounts. The conversion on to accrual accounting has encountered serious impediments, especially regarding valuation of assets.
- Even at the present time, Bangladesh does not comply with the Cash Basis IPSAS, Part 1, in its annual accounts. The Government of Bangladesh (GoB) needs to restructure the present cash basis reporting to conform fully to the Cash Basis IPSAS.

## Role of Public Sector Auditing Standards

These standards are broad statements of auditors' responsibilities. They provide an overall framework for ensuring that auditors have the competence, integrity, objectivity, and independence in planning, conducting, and reporting on their work. Auditors will face many situations in which they could best serve the public by doing work exceeding the standards' minimum requirements. As performance and accountability professionals, public sector auditors should not strive just to comply with minimum standards, which represent the floor of acceptable behavior, but they need to do the right thing according to the facts and circumstances of each audit situation.

International and national institutions worldwide have now become concerned about the auditing standards and practices of public sector institutions. The



INTOSAI, IFAC and FEE have issued many such standards. While the national audit authorities in different countries such as GAO in the USA, NAO in the UK, ANAO in Australia have also issued many standard guidelines to be followed in public sector auditing.

## INTOSAI Public Sector Auditing Standards and ISSAIs

The International Organization of Supreme Audit Institutions (INTOSAI) is the professional organization of Supreme Audit Institutions (SAIs) in countries that belong to the United Nations or its specialized agencies. SAIs play a major role in auditing government accounts and operations, and in promoting sound financial management and accountability in their governments. INTOSAI supports its members by providing opportunities to share information and experiences about the auditing and evaluation challenges facing them in today's changing and increasingly interdependent world.

INTOSAI has recently published a Strategic Plan for 5 years Overview 2011-2016 covering its Mission, Vision, Strategic Goals and Strategic Priorities. INTOSAI's goals encompass (a) Accountability

and Professional Standards, (b) Institutional Capacity Building, (c) Knowledge sharing and Knowledge Services, and (d) Model International Organization. The Core Values encompasses (a) Interdependence, (b) Integrity, (c) Professionalism (d) Credibility (e) Inclusiveness (f) Cooperation, and (g) Innovation. The INTOSAI based Government Auditing Standards are similar to the ISA issued by IAASB and IFAC Public Sector Auditing Guidelines. INTOSAI experts participate in the development of ISAs. The ISAs are an integrated part of the ISSAIs of INTOSAI on financial Audit. The International Professional Standards of Supreme Audit institutions (ISSAI) framework, formally established in 2007 reflects the ambition of the INTOSAI to provide its membership and other interested parties with a framework of professional high-quality auditing standards. The first complete set of ISSAIs was presented and endorsed by IFAC at the INTOSAI congress in South Africa in 2010, through a Memorandum of Understanding to Strengthen Accountancy and Improve Collaboration (MOSAIC). INTOSAI's ambition and aspiration for the ISSAI framework were expressed in the South Africa

Declaration. Many new ISSAs have been developed and presented since the adoption of the ISSAI framework in 2007. The framework now includes some 70 standards and guidelines.

The INTOSAI based Government Auditing Standards are said to be applied by OCAG Bangladesh. IFAC issued Public Sector Accounting and Auditing Standards, are not adopted in the preparation and presentation of financial statements or in the public sector audit of Government departments and enterprises. The exchange of knowledge among INTOSAI members and the resulting findings and insights is a guarantee that public sector auditing continuously improves. The ISAs are developed, approved and issued by the IAASB of IFAC. INTOSAI experts participate in the development of ISAs. INTOSAI Guidelines on financial auditing consist of an ISA together with an INTOSAI Practice Note showing modifications and elaborations that needs to be considered in public sector auditing. INTOSAI issues two sets of professional standards: 1)The International Standards of Supreme Audit Institutions (ISSAIs) and; 2) the INTOSAI Guidance for Good Governance (INTOSAI Gov).All ISSAIs and INTOSAI Gov convey the generally recognized principles and shared professional experiences of the international community of Supreme Audit Institutions. The INTOSAI based Government Auditing standards have been meant for application in the conduct of audit, there are significant limitations of technically competent personnel for ensuring their application.

In the absence of its own auditing standards, the C&AG office has taken guidance from a variety of sources: basic principles and guidelines pertaining to the Office

laid down in the Constitution, Guidance contained in the existing Audit Code and Audit Manuals, standards recommended by INTOSAI and those used by other national audit officers, the 'Government Auditing Standards' have been formulated to cover come fill an important the lacking and fulfill the long-felt need to have C&AG own standards, which meet expected requirements and are also consistent with international norms. However, Bangladesh took up the INTOSAI standards in 2006-2007 in a pilot basis and consequently it is now applied in the national accounting system.

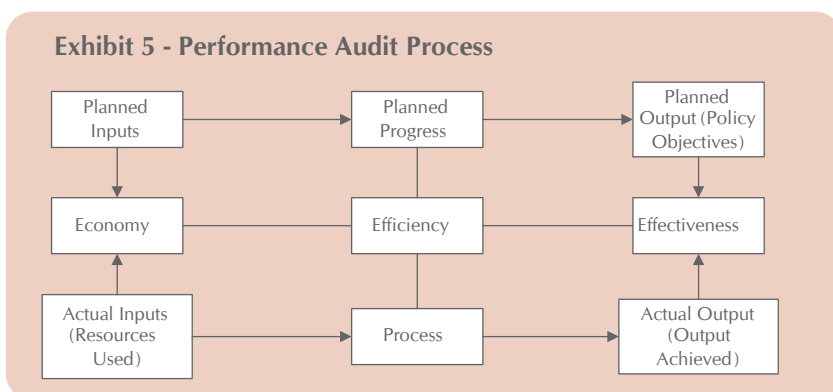
### Bangladesh Public Sector Auditing Standards

The CAG (Bangladesh) consider the INTOSAI standards in 2006-2007 in a pilot basis. OCAG is contemplates to implement the ISSAIs within a foreseeable timeframe in the public sector audits in Bangladesh. In Bangladesh, four INTOSAI certified expert trainers are extending the support to practice INTOSAI under CAG. The CAG formulated Government Auditing Standards are aimed at modernizing the Government Audit function and has been developed as part of its reform agenda. The practical implementation of the standards is expected to play a significant role in the enhancement and

transparency of information, accountability and good governance of the public sector.

The Document on 'Government Auditing Standards' lays down the basic standards that auditors are expected to meet in conducting their audits. Although designed primarily for the guidance of auditors and officials of the Audit Department of Bangladesh. These standards are also beneficial for internal auditors of public sector organizations as well. OCAG prepared Audit Code Manual explains the methodologies and approaches to various types of audit applied in the Public Sector. OCAG has also prepared Performance Auditing Manual, which serves as an effective tool for assessing the Economy, Efficiency and Effectiveness of Public Sector operational activities (value for money audit). (Exhibit 5). Refer Appendix for Performance Audit Directorate.

The evaluation of Public Sector operations, functions and responsibilities is assessed by OCAG through a three-tier modality comprising of (a) Financial audit, (b) Compliance audit, and (c) Performance audit. OCAG is also taking initiatives to develop expertise for conducting Environmental, Social, IT, and Public Debt Management audit on a pilot basis.



## Strengthening Public Sector Accounting and Auditing Practices

### The Need for Reforms - Overview

Ever since the establishment of the OCAJ Bangladesh and the additional functions conferred upon it the organization has been carrying out the task of audit of all the public, autonomous and semi-autonomous institutions. Within a spell of 30 years, the nature of Audit Methodology remains traditional and orthodox. Codes and manuals dates back to 1935. Therefore, Global requirement to ensure effective stewardship and enhancing good governance make it imperative on the part of the SAI of Bangladesh to move along the way. Ensuring accountability is another priority. In doing so the justifiability behind the expenditure needs to be explored.

A change is required when existing systems or practices cannot fully serve the purpose for which they have been established. This change approach either termed as 'reformation', 'renovation', 'restructuring' or 'improvement' need a sea of change in the mind set. To make the change approach effective recognizing the past and identifying the deficiencies of the present day practice are primary requirements for those who are engaged in the task and those who will be benefited. There is a strong demand that good public sector external audit is necessary for the OCAJ to have any material impact. This requires willingness of the executive branch to accept and respond to external scrutiny over its management of funds and ensure that action is taken for reform. It also requires public presentation of the audit reports to ensure public support for effective action.

### The Need for Reforms – IPSAS Implementation

Adaptation and implementation of IPSAS is not a requirement for the Government or any of its entities, it is a best practice issue, IPSASB or even IFAC cannot enforce compliance. The success of IPSAS adaptation and implementation depends on the efforts of various stakeholders who support the improvement of financial management and reporting in the public sector.

- Governments as the leading user of IPSAS standards will therefore require undertake massive capacity building to enlighten its accountants on IPSAS.
- This would be a challenge both in terms of capacity building costs and in terms of the required change management issues from the traditional cash accounts to a more business like accounting under accrual basis IPSAS.
- Capacity building will likewise require to be undertaken to ensure that it does not become an implementation drawback
- The adaptation of new financial reporting framework will herald significant changes to the systems and process of financial reporting by the government. People generally resist change and therefore change management processes require to be incorporated to the adoption and implementation roadmap.

### Limitations / Weaknesses

Interaction with OCAJ reveals that they are still focused on receipts and payments transactions and have not made tangible progress since its establishment in 1985, towards accrual accounting or using globally acceptable

accounting and auditing standards till 2010.

The reality is that the OCAJ office has many limitations, both internal and external, that inhibit its' capacity to carry out quality audits in accordance with globally acceptable auditing standards. The constraints to audit effectiveness are overwhelming, warranting the need for comprehensive reforms for urgent implementation. There needs to be a more comprehensive plan for Bangladesh to adopt the Cash Basis IPSAS as part of a longer-term program to adopt accrual-based reporting for each government entity in accordance with the IPSAS. There should be a plan for the CAG to adopt the ISA, as well as more high-level INTOSAI Auditing Standards in routine auditing work.

The role of Audit as an integral part of the country's governance structure was seriously limited and the Auditor General's image and effectiveness were significantly jeopardized.

- CAG audit approach has been essentially conventional and traditional, focused only on review of transactions for compliance with specified rules and regulations.
- Bangladesh Accounting and Auditing System are unable to produce timely and comprehensible reports.
- Materiality review tests are limited
- Public Audit has failed to achieve the desired objective and credibility impact.
- The Information provided to parliament through annual Audit reports was of limited use.
- There is no objective implementation of IPSAS in Government Accounts. Bangladesh does not comply

with the Cash Basis IPSAS, Part 1, in its annual accounts.

- Accrual Accounting has not been adopted or implemented in any form or manner by the CAG office in Government Account. The conversion on to accrual accounting has encountered serious impediments and is reportedly being held up in abeyance.
- There is no objective implementation of IPSAS in Government Accounts.
- There has not been any tangible development towards PPP (Public Private Partnership) for Government Auditing in Bangladesh.



However, an assessment on CAG of Bangladesh reveals the reality that the offices effectiveness is far below its potential in promoting accountability, transparency, and good management practices. This is so because its reports are limited in scope, do not raise the important issues, are poorly researched and are not timely.

The CAG have serious limitations to carry out quality audits to internationally accepted auditing standards. Lack of professionalism, emanating from deficiency in knowledgeable, technical skill and professional competence resulted in rather mediocre performance of the Auditor General's Office.

- Lack freedom to hire suitably qualified, trained staff to meet the needs of his office.
- The Ministry of Finance has control over the CAG Budget
- C&AG office is not outside the ambit of the Government bureaucracy.
- Responsibility for both Audit and Accounts is a conflict of Interest
- Audit Staff are not adequately qualified and trained
- Training and Professional

development are not systematic.

- Audit Methodology is deficient and yet to be modernized.
- Audit Planning, evidence and quality control are weak.
- Audit Scope is limited as performance audit is not carried out.
- Audit reports have limited usefulness to meet the user needs: the number of reports is too large, too detailed and often late and report focuses on trivial issues and there is no systematic follow-up.

The CAG lacks the expertise and resources to deal with the issues and the volume of audits. Strategic operational planning is lacking in the financial management system. Executive agencies ignore many audit observations leaving them unresolved indefinitely.

### **Challenges in Public Sector Accounting and Auditing**

The main Challenge entails sophisticated implementation of Cash based IPSAS and Transition to Accrual accounting. This adoption by the Government will lead to

wave of clear modernization of financial reporting by the public sector. It is definite that all public sector organizations will follow suit.

Transition to IPSAS as an accounting framework will improve the quality and consistency of financial management and good governance in the entire public sector. The CAG Auditors, in refocusing management attention on the parliamentary accountability, have the capacity to play a significant part in improving the status quo in respect of public interest protection and good governance. Particular challenges include: (i) improving the financial governance arrangements for public corporations; (ii) improving the financial reporting of public corporations; and (iii) improving public expenditure management practices. These Challenges all involve redefining and relevant modifications in accounting and auditing arrangements/ modalities.

The institutional framework should include adherence to International Accounting Standards (IAS) and the

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. A well designed set of diagnostic questionnaires may be used in this assessment to facilitate the collection of information on the current arrangements, and the apparent gaps in the present accounting laws and regulations of Bangladesh; education and training of public sector accountants; application of a code of conduct; and numbers and characteristics of public sector accountants.

The Bangladesh Government auditing and accounting rules and procedures are still emergent and inadequate for financial management and reporting requirements to reflect the expected level of accountability of the OCA and transparency of the public financial information. This impedes satisfactory "oversight function" of the Comptroller and Audit General of Bangladesh CAG office. In the absence of its own standards, the CAG office has to take guidance from a variety of sources: basic principles and guidelines pertaining to the Office laid down in the Constitution, Guidance contained in the existing Audit Code and Audit Manuals, Standards recommended by INTOSAI etc.

Bangladesh Audit Department's approach to audit has been essentially conventional, focusing only on the review of transactions for compliance with specified rules and regulations. Materiality review tests are also be limited. Public Audit has failed to achieve the desired objective and credibility impact. The information provided to Parliament through annual audit reports was of limited use. The role of audit as an integral part of the



country's governance structure was seriously limited and the Auditor General's image and effectiveness were significantly jeopardized.

The executive agencies ignored many of the audit observations leaving them unresolved indefinitely. The Public Accounts Committee also fails to resolve these voluminous observations for years together, thereby greatly undermining the value and impact of audit output. Lack of professionalism, emanating from deficiency in knowledgeable, technical skill and professional competence resulted in rather mediocre performance of OCA.

The positive news is that C&AG office recognizes the importance of introducing modern auditing techniques, reorienting staff skills, undertaking intensive training and making organizational changes. To this end, the office has initiated some reforms based on technical assistance projects funded by UNDP and DFID which are currently under way to introduce modern auditing standards, develop audit manuals, train

trainer, conduct course and strengthen the Financial management Academy, FIMA. CAG strongly supports the drive to introduce performance audits in the short term and does feel the need for systematic human resources development and better communications and parliamentary liaison.

Therefore, reforms of a policy and legal nature are needed in organizational structure and in enhancing the financial and administrative powers of the office. The CAG needs to be independent of the Government, particularly the MoF and report administratively and functionally only to Parliament.

The shortcomings are many but the potentials for improvement are enormous. Real change will only begin with an acceptance of the prevailing situation. It will require committed leadership and a clear strategy for overcoming the barriers to change: the departmental rivalries, the hostility of unions, the fears of individuals and the sheer size of the contemplated changes.

OCAG office has no choice but to make a start and the time to make it now.

The executive agencies ignored many of the audit observations leaving them unresolved indefinitely. The Public Accounts Committee also fails to resolve these voluminous observations for years together, thereby greatly undermining the value and impact of audit output. Lack of professionalism, emanating from deficiency in knowledgeable, technical skill and professional competence resulted in rather mediocre performance of the OCAG.

**The major Challenges may be summarized as follows:**

- Inability to provide timely, relevant, and reliable financial information that is needed to support all fiscal and budget management, decision making, and reporting processes;
- Improving the financial governance arrangements for public corporations;
- Improving the financial reporting of public corporations;
- Application of a code of conduct and characteristics of public sector accountants.
- Improving public expenditure management practices;
- Formatting a strategic planning for the Supreme Institution.
- Adaptation of Cash Basis IPSAS and International Standards
- Transition from Cash basis IPSAS to the Accrual based IPSAS.
- Implementation of the standards in public agencies
- Modernization of Public sector Auditing
- Transparent and effective Financial Reporting
- Timely and accurate information to the stakeholders.

- Parliamentary support over the rules and regulations
- Strong project management, monitoring and review procedures.

**Capacity Building and Institutional Development of CAG Bangladesh**

- To ensure the freedom to CAG office in recruitment of suitable staff
- To enhance the tenure for the CAG
- To Separate the audit and accounting functions of the CAG office
- Undertaking Professional development of CAG Staff
- Parliamentary voting to the CAG budget.
- Timely Preparation and submission of Audit Reports
- Enhancing Quality of Audit and its effectiveness
- Modernization of financial Audit.
- Shift of emphasis from transaction based financial audit to that based on performance and results.
- Update and modernize the manuals
- Introduce performance /value for money Audit
- Develop human resources Management strategies to meet newer and emerging needs
- Improve the image of Audit nationally and internationally as a strong oversight institution for good governance
- Regional and international cooperation for the benefits of SAI Bangladesh.

**Focus Areas for Strengthening Public Sector Accounting and Auditing**

Financial accountability is indispensable for achieving economic success. To ensure proper financial accountability, there must be an adequate system

of budgeting, financial reporting, internal control, and Auditing of the Government Ministries & Divisions, Local Government Institutions, sector corporations, SOEs and SOBs.

Any system of democratic Government must have a robust mechanism to ensure transparency and accountability in public sector financial management. The office of the CAG, the Supreme Audit Institution of the state, is one such mechanism. Under its legislative mandate, The C & AG audits the income and expenditure of the GOB and thereby subjects its practical conduct and operations as a whole to regular, independent investigation and review. It acts as a 'Watchdog' over the financial integrity and credibility of reported information. It focuses its work on three main issues:

- Is the government keeping proper accounts and records and presenting its financial information accurately?
- Did the government collect or spend the authorized amounts and for the purposes intended by the Parliament?
- Were programs and activities run economically and effectively?

Through its audit, it provides parliament, its main client, with assurance, comments, and analyses on the information provided by GOB departments and thus assists Parliament in holding the government to account for its stewardship of government funds. The C & AG has the constitutional mandate to strengthen the country's democracy by enabling oversight, accountability, and governance in the public sector through auditing, thereby building public confidence.

The structured role of the

professional organization, the adaptation of the International Public Sector Accounting Standard (IPSAS), implementation of the Public private partnership (PPP) in cross transfer of skills, knowledge, expertise and the accountability of the government officials could play a significant role in strengthening the overall public sector accounting and auditing practices.

### **Follow up the CAG Function**

The environment for an effective SAI (CAG) requires a comprehensive approach to public financial management. They are not stand-alone institutions, rather part of over public financial management architecture that also includes budgeting, accounting, internal control, audit and legislative oversight and government response.

The existence of the Supreme Audit Institution in Parliamentary Democracy serves as catalyst to ensuring transparency and achieving accountability in Government operations. The basic objective of CAG audit function is to ensure stakeholders of the fairness of the government entities financial statement and compliance with applicable laws and regulations. The C&AG auditors, in refocusing management attention on the parliamentary accountability, have the capacity to play a significant part in improving the status quo in respect of public interest protection and good governance.

### **The Reforms Agenda**

#### **ICAB Twinning Project with ICAEW**

The World Bank – CFAA Project study on Public Sector Auditing in Bangladesh (2000) had clearly indicated the C & AG office needs

to professionalize its office staff through adequate training & professional development for developing and enhancing skills and competence for the attainment of audit objectives. The study had recommended a Public Private Partnership in professional training through collaboration with the ICAB & ICMAB. Since both the institutes entail a combination academic course, job training, and qualifying examinations for attainment of professional degrees, C & AG office was advised to liaise with the institutes for professional training & skill development of their auditors. It was recommended that the Auditor General Office should consult the ICAB for facilitating the conduct of their academic training courses and qualifying departmental examinations.

#### **SCOPE, SPEMP B and Railways Projects**

There are two technical assistance projects presently under implementation, which are involved with capacity building and institutional development of the OCAG. The US \$ 10 million CIDA funded 5 year project Strengthening Comptrollership and Oversight of Public Expenditure (SCOPE) Project is being implemented since March 2008. The SCOPE project entails:

- Enhancing CAG capacity for conducting Performance Audits.
- Enhancing CAG capacity for Financial and Compliance Audits as prescribed by ISSAIs.
- Enhancing capacity for IT Audit and computerization (application of IT solutions).
- Strengthening OCAG Information System infrastructure, including development of Audit Management and Monitoring

System [AMMS]  
The Strengthening Public Expenditure Management Programme (SPEMP B) is a capacity building, multi-donor funded project lead by the WB. SPEMP-B will operate in three functional components:

- Strengthening of Institutional Arrangements of OCAG
- Enhancement of Quality Audit and Expansion of Audit Scope
- Strengthening the Financial Management Academy [FIMA]

These two projects are not concerned with Accrual accounting or Convergence with IPSAS, but are basically aimed at capacity building of OCAG and improving the governance, budgetary control and oversight of public expenditure.

An ADB funded project for capacity building reforms in Railways Division, has been contemplating to implement "accruals" accounting, for improved financial management of the Railways. The conversion onto accrual accounting has encountered serious impediments (particularly with regard to valuation of assets) and is reportedly being held up in abeyance now.

#### **Role of Accounting Profession - ICAB**

The professional Accountancy organization of a country, when properly structured and supported can have a powerful impact and bring greater reform and development for the benefit of the public interest by acting as a centre of professional excellence (resource) for the Government, regulators, and the private sector to develop the overall economy of a country.

As a member of IFAC, ICAB is committed to serving the public interest. ICAB holds the accountability to be responsive to researches and practices on the standards developed by the IPSAS Board. ICAB should play a role to incorporate the requirements of IPSASs in to the national public sector accounting systems for financial reporting by the Governments. ICAB should use its best endeavours in playing the role of communicator in compliance with IPSAS by the supreme accounting and auditing authority of Bangladesh. ICAB could assist with the implementation of IPSAS or public sector accounting standards that incorporate IPSAS.

The ICAB has a positive role in educating and training its members, developing awareness and for proactively positioning itself as a self-regulatory profession to drive mandatory and voluntary CG practices through implementation of Best Code of CG Practices and related provisions for enabling the desired levels of accountability and transparency in the corporate information and discussion.

The ICAB should contribute to CG practices through ensuring “quality financial reporting” and “audit practices”. As the custodian of accounting and auditing standards, the ICAB is constantly engaged in the adoption of International Accounting Standard (IAS) promulgated by the International Accounting Standard Board as Bangladesh Accounting Standards (BAS) and the International Standards on Auditing (ISA). The ICAB Council, through its Technical and Research Committee exercises stringent vetting procedures in the adoption process, to overcome any inconsistencies and ensure conformity with local laws and regulations.

The ICAB had completed a project titled “Development of Accounting and Auditing Standards in Bangladesh” in 2003, financed by the World Bank’s Institutional Development Fund. Under the project a series of reports have been prepared, including a Report on Corporate Governance, one on Professional Ethics, and survey Report on Non-Financial Companies. The project has also supported the development of extensive course materials on a good number of IAS and ISA. Workshops were organized to train 600 participants on these Standards, including ICAB members and SEC officials.

### **Private Sector Independent Audit**

#### **Private Sector Accounting and Financial Reporting**

Accounting standards provide definitions of the accounting policies that should be adopted for the treatment of specific categories of transactions. The concept derives from the commercial accounting, where the need has been recognized to prescribe standards for commercial entities in the presentation of their accounts. In Bangladesh, the ICAB has been adopting the standards - IAS/IFRS as BAS/BFRS and the ISA as BSA for over two decades.

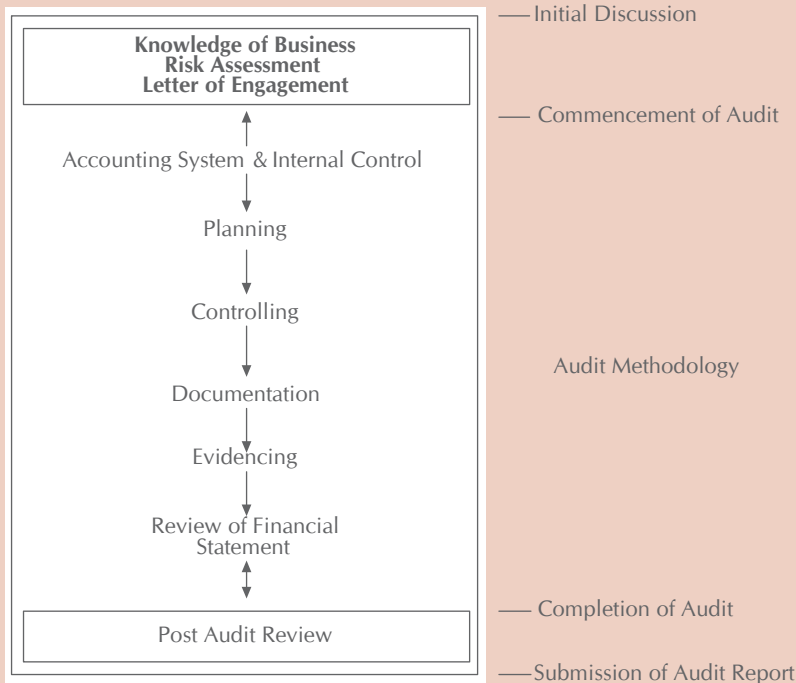
#### **Audit Objectives and Audit Methodology**

From the private sector perspective Auditing (External/Independent Audit) is defined as an “independent” examination of the Financial Statements and other related information of an entity, whether profit-oriented or not, and irrespective of its size or legal form whenever such an examination is conducted with a view to expressing an opinion thereon. The

“objective” of an audit of financial statements, proposed within a framework of recognized accounting policies (generally accepted accounting principles-IAS/BAS) is to enable the Auditor to form and express an opinion on the truth and fairness” of the Financial Statements of the audited entity. Financial Statement comprise of a Balance Sheet (reflecting the financial position), an Income Statement/Profit & Loss Accounts (reflecting the results of operations), Cash Flow Statement and a Statement of Changes in Equity. Audit enable the rendition of an honest, unbiased objective, independents expert “true and fair view” professional opinion on the financial information of the auditee. Audit opinion lends “credibility” of the financial information to a wide range user groups (shareholders, investors, lenders, employees, tax authorities etc.) and other stakeholders, which may be relied upon for decision-making purposes.

Audit administration is the entire process of managing and conducting an audit from the point of initial discussion and commencement of the audit to the time of completion of the audit and submission of the audit report. It incorporates audit methodology or the procedures for conducting the audit and formulating the audit opinion. Audit Methodology is designed to enable an adequate review of the accounting system and related internal controls, and ensuring that the audit is adequately planned, controlled and documented at each stage of its progress from initiation to completion, in order to ensure quality, efficiency and effectiveness and provide evidence of the work done (i.e., that the audit was carried out in accordance with the basic principles).

**Exhibit 6 - Diagrammatic Representation of Audit Administration**



**Significance of ISA in Audit Practices Harmonization**

The International Standards on Auditing (ISA) are issued by the IAASB of the IFAC, to effect world-wide, globalized "harmonization" in the Generally Accepted Auditing Standards (GAAS), for application in the conduct of audit and formulation of audit opinion of reporting entities. This renders increased credibility on audited FS as bases for investments, credit and similar decisions.

The ISA normally represent the formalization and codification of existing best auditing practice (nationally and internationally) which professional members are expected to observe in practice. These standards therefore prescribe the GAAS for conducting and reporting on the audit of corporate and other entities. The ISA are intended to narrow down the areas of differences and dissimilarities and overcome inconsistencies and incongruities in audit practices world-wide. Each ISA is concerned with specific subject matter (such as audit planning, controlling, documenting, evidencing reviewing etc.) regarding the conduct of audit and formulation of audit opinion.

The ISA are promulgated by IAASB of IFAC as "definitive" standards (subject to local adaptation) which are meant for mandatory application wherever adopted. The ISA are devised to overcome deviations and achieve improvement in the degree of infirmity in auditing methodologies and reporting, thereby effecting harmonization in audit practices.

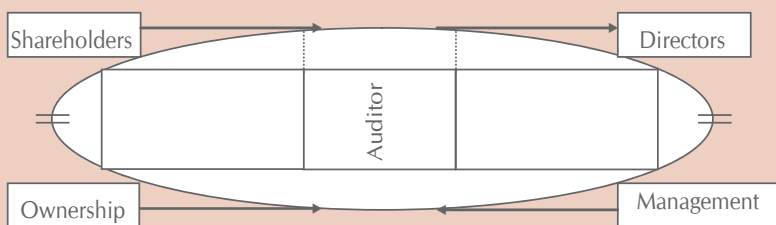
**Benefits of Harmonization through ISA**

In order to arrive at a defensible

**Harmonization of Audit Practices**  
An audit is an independent examination of the Financial Statements and other related information of an entity, whether profit oriented or not, irrespective of size or legal form, whenever such an examination is conducted with a view to expressing an opinion thereon. Under the Stewardship System of Financial Reporting, the shareholders who represent the "ownership" of the company are distinct from the board of directors who represent the "management" of the company. The shareholders appoint the directors at the company AGM to

run the company in the best interest of the ownership. The shareholders need an honest, unbiased, objective, independent, expert professional opinion on the truth and fairness of financial information presented by the directors, alongwith an assessment and evaluation of the performance of responsibilities entrusted to them. Management is unlikely to render that opinion with any degree of objectivity. Hence the Auditor acts a bridge helping to make management accountable to the ownership and other users of financial information through the Audit Report.

**Exhibit 7 - Accountability for Stewardship System for Financial Reporting**



opinion, the auditor must provide evidence of a "state of the art" or "first class audit". This should ensure that the audit entailed an adequate review of the accounting and internal control systems and had been planned, controlled and documented at each stage of its progress from initiation to completion to ensure quality, efficiency and effectiveness and provide evidence of the work done i.e. that the audit was carried out in accordance with the "standardized" Basic Principles Governing an Audit of Financial Statements (preferably in accordance with the ISA).

Standardization of audit practices through consistent application of ISA would result in qualitative improvement in the audit function. Standardization overcomes inconsistencies and narrows down differences in the formulation of audit plan, method of conducting audit and arriving at the audit opinion. This would lead to global harmonization of auditing practices, thereby rendering the auditor's opinion more "credible" and acceptable to user groups for investment and other decisions. Good quality audit and credibility of audit opinion on Financial Statements are vital for attracting Foreign Direct Investments and for Capital Markets Development in Bangladesh.

### **Public Private Partnership in Government / Public Sector Auditing**

Public Private Partnership in Government Audit reflects a mutually beneficial partnership between the Government (CAG) and private sector auditors (ICAB/ Chartered Accountants) intended to derive synergy from sharing of knowledge and expertise in conducting the audit of public sector institutions. Governments

across the world to work are collaborating with the private sector for effective public financial management –accounting, reporting and auditing. There has been growing trend towards more out sourcing of private sector accounting and assurance service and management consultancy even within traditional government's service delivery channels. In a performance based budgeted framework, state governments nowadays are more focused on the actual service and outcomes rather than mere delivery. Integration and transfer of public and private sector skills, knowledge and expertise have become an increasing means for efficient resource management and enabling high quality reporting, for financial inclusion and sustainable development.

The involvement of Private Audit Firms in the conduct of Government Audit will ensure the application of the ISA of IAASB and IFAC public sector auditing standards. This would impact qualitative improvement in public sector audit methodology and reporting process. Pubic Private Partnership in Government

Auditing would enable the application of appropriate levels of knowledgeability, technical skills and professional competence for the CAG auditors.

### **Public Sector versus Private Sector Audit**

It indicates that though the public sector auditors under the Auditor General's office play a most important role and engaged in the core area of public sector activities, the private sector auditors (Chartered Accountants) are also performing audit works in the public sector. Government ministries, departments, and subordinate government bodies under them are the absolute domain of government auditors. However, in case of public corporations, enterprises, nationalized banks and financial institutions, or companies those required to prepare their accounts according to the double entry system, and prepare the Balance Sheet and Profit and Loss Accounts are under the purview of both the private and public sector auditors.

#### **Exhibit 8- Differential Audit Approaches and Methodologies**

##### **Government / Public Sector Auditors**

- Provision of funds duly authorized by the competent authority;
- Propriety of payments, duly acknowledged and recorded;
- Proper classification of charges and expenses.
- Expenditure is in pursuance of a recognized policy or custom.

##### **Private Auditors (Professional Accountants)**

- Independent examination and report on FS
- Compliance with the legal and statutory requirements
- Compliance with uniform accounting policies
- Compliance with the IAS / IFRS
- Independent opinion on truth and fairness of FS.

There are deficiencies of both public and private sector auditors. The public sector auditors give attention in examining expenditure incurred by the organization. Their examination emphasizes on the authorization, budget allocation, and compliance with the government rules and regulations. The general feeling is that they do not have in depth knowledge about the double entry system and commercial accounting conventions, standards and practices. On the other hand, the private or professional accountants limit their comments on the accuracy of financial statements without looking into the government rules and appropriateness of the expenditure.

### **Public Private Partnership – A Strategic Alliance**

Accounting profession and government audit agencies are working in close cooperation in most of the developed countries. In Bangladesh, in the public enterprises both the public sector auditors and private auditors are working which might be deemed as duplication of works. Developing countries like Bangladesh has inadequate resources and require judicious spending of resources. This duplication can easily be avoided considering the standard practices in other countries. The objectives of auditing in the public enterprises be kept in mind.

### **PPP in Developed Countries**

In UK, the National Audit Office is looking after the government institutions whereas the Audit Commission is responsible for the audit of local authorities and other autonomous organizations. Audit Commission appoints the chartered accountant firms to conduct audit of the organisations under their

jurisdiction. They scrutinize the audit reports and submit it to the concerned agencies. Public Audit Forum has been formed comprising the members of NAO, Audit Commission, and private audit firms to develop auditing standards and issues related to coordination among them.

In New Zealand, it is the common practice to appoint the professional accountants with private sector audit experience in the higher positions in government audit office. In the USA, as a matter of strategy, private sector firms as agents to supplement C& AG's own resources are appointed to conduct audit of many public sector bodies.

### **PPP in Bangladesh and the emerging initiative**

There has not been any tangible development towards PPP for Government Auditing in Bangladesh. Under leadership of incumbent president, ICAB has enhanced the level interaction with concerned authorities like the C&AG and MoF, but true PPP in Government auditing is still very remote.

In Bangladesh, it is not provided for in the Constitution or in any Act of Parliament that the C&AG should be professionally qualified Chartered Accountants and/or the C&AG official should be professionally qualified /part qualified accountants as deemed appropriate.

The Private Sector Audit falls under ambit of the "legal regulatory framework" comprising essentially of the Companies Act 1994, (for all companies) Securities and Exchange Rules 1987, (for listed companies) and other relevant statutes (Bank Company Act 1994), quasi statutory provision, other

regulatory rules, directives & circulars etc. According to the Section 212 of the Companies Act 1994 no person shall be appointed as Auditor of any Company unless he is a Chartered Accountant within the meaning of the Bangladesh Chartered Accountants Order 1973, (PO No 2 of 1973). The terms of appointment and removal, qualifications and disqualifications, rights & powers and duties & responsibilities, are defined in the relevant provisions of the Companies Act 1994 (Section 210-213).

However, case of government audit and accounts, the officers and staff of the Audit Department are not required to be professionally qualified as Chartered Accountants or Cost Accountants. Government Auditors are required to be university graduates, who after recruitment to the Audit and Accounts Cadre services, receive intensive on the job training in various Directorates of the Audit Department. They have to qualify in rigorous departmental examinations, comprising of book keeping and accounting functions – salaries, stores, works accounts etc. Government Auditors also undergo regular training for upgrading their knowledge and skills in the FIMA.

In Bangladesh, a Dialogue may be initiated for materializing public and private sector audit partnership. The detailed modalities may be developed and streamlined between concerned authorities in due course (Ministry of Finance - C&AG Office: Ministry of Commerce – ICAB).

- Work together for development of public sector auditing standards
- Exchange of knowledge through different training programs

- Some audit works including special investigation, performance related audit, may be outsourced to the private audit firms
- Lateral entry of professional accountants in the government audit service
- Recruitment in the government audit service should be treated as a technical service and preference to be given to the graduates with accounts, audit, and finance background.
- Government audit service till now is clerical based which should be upgraded.

As in the USA, Canada, Australia and New Zealand, the South Asian Countries, including Bangladesh, may consider Constitutional and/or legislative amendments incorporating necessary provision for mandatory appointment of a professionally qualified Chartered Accountants as the Auditor General of the country. High-level officials of the C&AG office (including DG of the nine Audit Directorates may also be appointed from professionally qualified members of the ICAB, rather than conventionally from senior members cadre services (PSC – audit and accounts services). Preference should also be given to some kind of professional training attainment in the recruitment of other officials and staff of the C&AG office. Such policies would surely develop, improve and enhance the quality of Government Audit and the credibility of the C&AG Audit Reports.

### **Public Private Partnership – A Strategic Alliance**

Public Sector increasingly engages in collaborating arrangements to determine and deliver public policy. Strengthening the system of public financial accountability calls

for the accounting professions- public and private – to work together improving government accounting policy, standards and practices. As Governments face increasingly complex and challenging issues of our inter-dependent world, a harmonized approach is the answer to these challenges.

The CAG Bangladesh in a recent Statement explained that “Collaboration with the Private Sector Auditing Profession through exchange of information and expertise may help strengthen Public Sector Auditing of Comptroller and Auditor General. Experience of the Private Sector Enterprises with regard to Internal Controls, Internal Audit, Performance budgeting etc. may also help CAG’s audit to recommend improvements in the Public Sector Enterprise management in those important area”.

A “strategic alliance” through Public Private Partnership in Government Auditing should also be established through involvement of Chartered Accountants in conducting and reporting on public sector audit of government institutions – including local authorities and autonomous bodies. In the long term, Government ministries, divisions, and departments may also be brought under the purview of external independent audit by professional firms of Chartered Accountants. The “public private alliance” may be effected by involving professional CA Firms in phases to audit the accounts of the government institutions/public sector entities – either on a rotational basis or phase by phase with the Audit Directorates of the C&AG.

A realistic, plausible approach

would be to “outsource” a certain percentage/volume of Government Audits to well reputed professional firms of Chartered Accountants on a regular (yearly) basis, being rotated phase by phase from audit entities (government accounts). This would enable application of professional skills and competence to public sector auditees. The C&AG Auditors would also be among team members of the outsourced audits, thereby getting relevant exposure to audit methodologies, techniques and approach as used by the professional firms.

The World Bank reiterated in the RIBEC project, explained improving availability of resources, and stressed the need for separation of audit from accounting function to establish credibility of C&AG audit. It must be appreciated that Government accounts and audit are different from commercial accounts and audit. Accordingly, the C&AG, besides being the SAI, also required to keep the Government accounts. Chartered Accountants are generally not appointed for auditing Government accounts. Necessary legislative amendment may be made for ensuring audit of Government accounts by professionally qualified Chartered Accountants (having development necessary skills for Government accounts and audit through adequate relevant training).

However, there has been long standing collaboration between Financial Reporting Councils, Accounting and Auditing Standards setting bodies and relevant Government bodies (SAI & Accountant General Office) in formulation and adoption of IPSAS that best suits the specific country reporting requirements. Through partnership agreements, the professional bodies and the

accountancy profession in general are increasingly engaged in working with governments in implementing IPSAS (Cash, modified or accrual) as part of enhanced financial reporting and increased disclosure in the use and accountability for resources of government.

Based on the thoughts and comments discussed above, it is apparent that some kind of a Strategic Alliance in the form of PPP in Government Auditing may be considered as a top priority discussion agenda, warranting immediate attention of concerned legislative and Government authorities, and particularly that of the OCAg and ICAB.

### **Policy Issues, Strategies And Recommendations**

An effective prescription needs sound diagnosis. Policy Issues and Recommendations regarding Public Sector Accounting and Auditing should be adequately broad based and well addressed to cover the entire spectrum of the Government agencies and Public sector institutions, ensuring appropriate levels of governance, accountability and transparency. The political will for adoption/ adaptation of IPSAS and ISSAI /ISA for public sector accounting and auditing respectively should be considered on a top priority basis and implemented through proper legislative process.

Keeping the above background and the Paper coverage in perspective, may I propose that the learned participants present in this forum and readers of this Paper, (particularly professionals from the OCAg and accounting fraternity), give careful consideration of the following and take necessary initiatives in their respective capacities to help improve the

level of Public Sector Financial reporting and Audit Practices..

Based on the above, the following Policy Issues and Recommendations may be formulated:

- Bangladesh represents a low income, developing country. The pace of economic growth depends largely on optimum utilization of limited resources.
- The national economy should be dynamic, sustainable growth oriented and free from bureaucratic controls. Macro economic fundamentals, such as low rate of inflation and current account deficit, stable currency, comfortable foreign exchange reserves, inward remittances, exchange convertibility and export growth must be ensured.
- Government must exercise strong political will, commitment and a firm sense of determination to forge ahead with practical implementation of the Reforms agenda for implementation of desired changes in the economy.
- Governments must take into cognizance the value addition rendered by accounting professionals and provide them with due recognition thereof.
- The Government/CAG must acknowledge that in this era of globalization, Accountancy has emerged as the unified language of business, enjoying commonality world-wide and that the IPSAS and ISSAI, just as much as the IAS/IFRS (Accounting) and ISA (Auditing) will impact a positive dimension towards the global harmonization of Public Sector Accounting and Auditing.
- The structured role of the CAG as a professional institution, the adaptation of the IPSAS, implementation of Public

private partnership (PPP) in cross transfer of skills, knowledge, expertise and the accountability of the government officials could play a significant role in strengthening the overall public sector accounting and auditing practices.

- Inducting/associating professionally trained manpower under one pool and assigning them to the audit directorates according to their demand and compliance would be a pragmatic step the right direction for development of audit quality.
- Additional training institutes maybe established on a regional basis professional with qualified trainers. Local and foreign experts could be utilized to upgrade the training standards.
- The CAG may be involved with concerned authority to invoke necessary judicial action for affecting the auditee' compliance with information requirements.
- Value for Money/Performance Audit should be properly conducted by establishing and enunciating public sector audit criteria for conducting Government auditor and presenting audit reports thereon. The office should have its methodology specialists. The C&AG should have staff competent to comment on the reliability and accuracy of work measurement standards.
- The functions of audit directorates may be rearranged (rotated) so that more than one audit team does not auditing the same institute or organization at the same time.

The objective of the audit report of the CAG is to inform the Parliament about activities of the organizations audited. The citizens

should also have access to the activity reports of the Auditor General. To facilitate the easy flow of information and ensure accessibility to the media the Auditor General's office may establish a News and Reports cell. Capacity Building and Institutional Development of OCAg Bangladesh

- To ensure the freedom to CAG office in recruitment of suitable staff
- To enhance the tenure for the CAG
- To Separate the audit and accounting functions of the CAG office
- Undertaking Professional development of CAG Staff
- Parliamentary voting to the CAG budget.
- Timely Preparation and submission of Audit Reports
- Enhancing Quality of Audit and its effectiveness
- Modernization of financial Audit.
- Update and modernize the Financial, Compliance and Performance Audit Manuals
- Introduce performance /value for money Audit
- Develop IT, Social and Environment Audit Guidelines.
- Regional and international cooperation for the benefits of SAI Bangladesh.

## The Way Forward

Measures for Addressing the Challenges

To facilitate the Way Forward in "devising strategies" for development of Public Sector Accounting and Auditing Practices in Bangladesh, the following Issues may be considered.

- CAG accounting laws and regulations should focus on IPSAS and ISSAI / ISA

implementation

- Better technology and an integrated financial management system are needed for improved public sector accounting and auditing
- All Government departments should use full Cash basis IPSAS and move toward application of Accrual basis IPSAS
- The GOB can be assisted in moving in an appropriate timeframe from the Cash Basis IPSAS to the Accrual IPSAS by utilizing an IFAC study on the transitional path to Accrual IPSAS
- Ensuring an effective selection and training framework as the current practices for selection and training of government accountants do not provide accounting staff with satisfactory skills
- A more focused recruitment process designed to meet the separate knowledge needs of the CAG and the CGA would be more efficient and more effective.
- A phased and progressive education program combined with practical experience is needed
- A code of conduct for accountants based on IFAC or ICAB codes is needed
- The Chief Financial Officer (CFO) functions need to be upgraded
- Formalized arrangements are needed for setting public sector Standards.

Some Policy Issues for Addressing The Challenges

1. The CAG should be independent from civil service rules governing recruitment and transfers.
2. The CAG should be guaranteed a fixed tenure at least five years to pursue and implement

objectives according to his own vision and mission.

3. The CAG budget should not require the approval of the MoF as is the case at present .The Speaker should present the CAG's budget to Parliament for approval.
4. A separate Performance Auditing team should be established.
5. A quality assurance Unit should be set up to ensure that quality benchmark, such as auditing standards are being adhered to review completed audits to determine the quality of work
6. To set up a strategic planning unit responsible to deal with issues of strategy, planning and policy for developing vision, mission and achieving corporate objectives.

## Conclusion / Epilogue

### Conclusion

Admittedly, the Adoptability of IPSAS and/or Accrual-based accounting, or for that matter the application of ISSAI or ISA, in Public Sector Accounting and Audit practices, may not be a "panacea" for overcoming all economic ills (shortcomings) prevailing in the public sector financial reporting and auditing systems in Bangladesh or the SAFA/CAPA regions. However, it would be a pragmatic step towards restoration of financial discipline and strengthening public sector financial management - through more objective financial reporting and credible auditing. The essential purpose for standardization would be to set the basic foundations of sound governance, for ensuring higher levels of transparency in financial reporting and thereby greater accountability in the Government/ public sector decisions. Implementation of the Standards

would positively help achieve the qualitative characteristics that are necessary to reflect a set of globally comparable "true and fair view" credible financial statements of the Government departments and public sector institutions and entities.

It is apparent that the Government must have the political will to legislate and the CAG to implement global best practices in public sector accounting and auditing. The CAG should consider "recommending" the "strategies" (Policy Issues) formulated from this Conference deliberations and forward these to the President after obtaining necessary consent of the Prime Minister, aimed at future improvement in public sector financial management and development of public sector accounting and auditing in line with best global practices. The Government should synergise a strong, cohesive accounting profession by encouraging leadership on emerging issues like Public Sector Financial Management and ensure coordination with national (ICAB), regional (CAPA/SAFA) and international (IFAC/INTOSAI) professional bodies for achieving the objectives of global harmonization in public sector accounting / financial reporting and auditing practices.

### Epilogue

Time has now come for appropriate authorities, like the CAG, to take cognizance of the usefulness of adoptability and practical implementation of the international public sector accounting and auditing standards to ensure adequate levels of transparency and credibility of reported financial information and of forming strategic partnership with professional accountancy

bodies like the ICAB and ICMA. This would impart tremendous synergy and quality assurance through sharing of knowledge, technical skills and professional expertise. The CAG may consider leveraging the professional services of Chartered Accountants through mutually beneficial, strategic Public Private Partnerships in Government/ Public Sector accounting and Auditing.

A robust, burgeoning professional community or the OCAG is not imperative for its own sake. Standardization of Public Sector Accounting and Auditing for improved Public Sector Financial Management is indeed necessary as a professional engine to propel the requisite level of economic growth for the regional countries. May we accentuate on that, by resolving here, at this appropriate forum, that the Government, CAG and Profession must work together coherently, by pooling their resources, sharing each other's experiences, in responding to the emerging Challenges and devising Strategies for effective functioning of SAI - as a means of ensuring the well-being and emancipation of our people and thereby contribute towards the socio-economic upliftment, leading to overall development, peace progress and prosperity of Bangladesh and the region.

We must, however, keep pace with the effluxion of time as otherwise we would be answerable to posterity for our actions and attitudes. May ALLAH's Providence be our Guide!!

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***The Author is Council Member & Past President, ICAB.  
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## Abbreviations

IAASB	-	International Auditing and Assurance Board
ASOSAI	-	Asian Organization of Supreme Audit Institutions
BAS	-	Bangladesh Accounting Standards
C& AG	-	Comptroller and Audit General
CAG	-	Comptroller and Auditor General
CAPA	-	Confederation of Asian and Pacific Accounts
CFAA	-	Country Financial Accountability Assessment
CFO	-	Chief Financial Officer
CGA	-	Controller General of Accounts
DFID	-	Department for International Development
FEE	-	Federation European Encomptables
FIMA	-	Financial Management Academy
GAO	-	Government Accountability Office
GFC	-	Global Financial Crisis
IAS	-	International Accounting Standard
IASB	-	International Accounting Standard Board
ICAB	-	Institute of Chartered Accountants of Bangladesh
ICMAB	-	Institute of Cost and Management and Accountants of Bangladesh
IFAC	-	International Federation of Accountants
INTOSAI	-	International Organization of Supreme Audit Institute
IPSAS	-	International Public Sector Accounting Standards
IPSASB	-	International Public Sector Accounting Standards Board
ISA	-	International Standards on Auditing
ISAR	-	International Standards on Accounting and Reporting
ISSAI	-	The International Standards of Supreme Audit Institutions
LGIs	-	Local Government Institutions
NAO	-	National Audit Office
NCBs	-	Nationalized Commercial Banks
NBFIs	-	Non Banking Financial Institution
OCAG	-	Office of the Comptroller and Auditor General
PPP	-	Public Private Partnership
RIBEC	-	Review of Public Expenditure Control
SAFA	-	South Asian federation of Accountants
SAI	-	Supreme Audit Institutions
SEC	-	Securities and Exchange Commission
SOB	-	State Owned Banks
UN	-	United Nations
UNCTAD	-	United Nations Conference on Trade and Development

## Appendix I - International Public Sector Accounting Standards (IPSAS) 2011

### Cash Basis IPSAS—Financial Reporting Under the Cash Basis of Accounting

- IPSAS 1 — Presentation of Financial Statements
- IPSAS 2 — Cash Flow Statements
- IPSAS 3 — Accounting Policies, Changes in Accounting Estimates and Errors
- IPSAS 4 — The Effects of Changes in Foreign Exchange Rates
- IPSAS 5 — Borrowing Costs
- IPSAS 6 — Consolidated and Separate Financial Statements
- IPSAS 7 — Investments in Associates
- IPSAS 8 — 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 Contingent Assets
- IPSAS 20 — Related Party Disclosures
- IPSAS 21 — Impairment of Non-Cash-Generating Assets
- IPSAS 22 — Disclosure of Financial Information about the General Government Sector
- IPSAS 23 — Revenue from Non-Exchange Transactions (Taxes and Transfers)
- IPSAS 24 — Presentation of Budget Information in Financial Statements
- IPSAS 25 — Employee Benefits
- IPSAS 26 — Impairment of Cash-Generating Assets
- IPSAS 27 — Agriculture
- IPSAS 28 — Financial Instruments: Presentation
- IPSAS 29 — Financial Instruments: Recognition and Measurement
- IPSAS 30 — Financial Instruments: Disclosures
- IPSAS 31 — Intangible Assets
- IPSAS 32 — Service Concession Arrangements - Guarantor

## **Appendix II - INTOSAI Financial Audit Guidelines representing the fourth level (Auditing Guidelines) of the International Standards of Supreme Audit Institutions (ISSAI)**

- ISSAI 1000 – General Introduction to the INTOSAI Financial Audit Guidelines
- ISSAI 1003 – Glossary of Terms to the INTOSAI Financial Audit Guidelines
- ISSAI 1200 – Overall Objectives of the Independent Auditor and Conduct of Audit in Accordance with ISA
- ISSAI 1210 – Agreeing the Terms of Audit Engagements
- ISSAI 1220 – Quality Control for an Audit of Financial Statements
- ISSAI 1230 – Audit Documentation
- ISSAI 1240 – The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements
- ISSAI 1250 – Consideration of Laws and Regulations in an Audit of Financial Statements
- ISSAI 1260 – Communication with Those Charged with Governance
- ISSAI 1265 – Communicating Deficiencies in Internal Control to Those with Governance and Management
- ISSAI 1300 – Planning an Audit of Financial Statements
- ISSAI 1315 – Identifying and Assessing Risks of Material Misstatements by Understanding Entity Environment
- ISSAI 1320 – Materiality in Planning and Performing an Audit
- ISSAI 1330 – The Auditor’s Responses to Assessed Risks
- ISSAI 1402 – Audit Considerations Relating to an Entity Using a Service Organization
- ISSAI 1450 – Evaluation of Misstatements Identified during the Audit
- ISSAI 1500 – Audit Evidence
- ISSAI 1501 – Audit Evidence – Specific Considerations for Selected Items
- ISSAI 1505 – External Confirmations
- ISSAI 1510 – Initial Audit Engagements – Opening Balances
- ISSAI 1520 – Analytical Procedures
- ISSAI 1530 – Audit Sampling
- ISSAI 1540 – Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures
- ISSAI 1550 – Related Parties
- ISSAI 1560 – Subsequent Events
- ISSAI 1570 – Going Concern
- ISSAI 1580 – Written Representations
- ISSAI 1600 – Special Considerations – Audits of Group Financial Statements (Incl. Work of Component Auditors)
- ISSAI 1610 – Using the Work of Internal Auditors
- ISSAI 1620 – Using the Work of an Auditor’s Expert
- ISSAI 1700 – Forming an Opinion and Reporting on Financial Statements
- ISSAI 1705 – Modifications to the Opinion in the Independent Auditor’s Report
- ISSAI 1706 – Emphasis of Matter Paragraphs and Other Matter Paragraphs in Independent Auditor’s Report
- ISSAI 1710 – Comparative Information – Corresponding Figures and Comparative Financial Statements
- ISSAI 1720 – The Auditor’s Responsibilities Relating to Other Information in Documents Containing Audited FS
- ISSAI 1800 – Special Considerations – Audits of FS Prepared in Accordance with Special Purpose Frameworks
- ISSAI 1805 – Special Considerations – Audits of Single FS and Specific Elements, Accounts or Items of FS
- ISSAI 1810 – Engagements to Report on Summary Financial Statements

**Appendix III (A) - Adoption Status of International Accounting Standards (IAS)**  
by ICAB as Bangladesh Accounting Standards (BAS)

IAS/ BAS	Title of Adopted IAS as BAS	Effective Date- Applicable on or after
1	Presentation of Financial Statements	1 Jan 2007
2	Inventories	1 Jan 2007
7	Statement of Cash Flows	1 Jan 1999
8	Accounting Policies, Changes in Accounting Estimates and Errors	1 Jan 2007
10	Events After the Reporting Period	1 Jan 1999
11	Construction Contracts	1 Jan 1999
12	Income Taxes	1 Jan 1999
16	Property, Plant and Equipment	1 Jan 2007
17	Leases	1 Jan 2007
18	Revenue	1 Jan 2007
19	Employee Benefits	1 Jan 2004
20	Accounting for Government Grants and Disclosure of Govt Assc	1 Jan 1999
21	The Effects of Changes in Foreign Exchange Rates	1 Jan 2007
23	Borrowing Costs	1 Jan 2010
24	Related Party Disclosures	1 Jan 2007
26	Accounting and Reporting by Retirement Benefit Plans	1 Jan 2007
27	Consolidated and Separate Financial Statements	1 Jan 2010
28	Investments in Associates	1 Jan 2007
29	Financial Reporting in Hyperinflationary Economics	Not adopted
31	Interests in Joint Ventures	1 Jan 2007
32	Financial Instruments: Presentation	1 Jan 2010
33	Earnings per Share	1 Jan 2007
34	Interim Financial Reporting	1 Jan 1999
36	Impairment of Assets	1 Jan 2005
37	Provisions, Contingent Liabilities and Contingent Assets	1 Jan 2007
38	Intangible Assets	1 Jan 2005
39	Financial Instruments: Recognition and Measurement	1 Jan 2010
40	Investment Property	1 Jan 2007
41	Agriculture	1 Jan 2007

**Appendix III (B) - Adoption Status of International Financial Reporting Standards (IFRS)**  
by ICAB as Bangladesh Accounting Standards (BAS)

SL #	IFRS / BFRS	Title of Adopted IFRS as BFRS	Effective Date- Applicable on or after
1.	<b>BFRS 1</b>	First-time Adoption of International Financial Reporting Standards	1 Jan 2009
2.	<b>BFRS 2</b>	Share-based Payment	1 Jan 2007
3.	<b>BFRS 3</b>	Business Combinations	1 Jan 2010
4.	<b>BFRS 4</b>	Insurance Contracts	1 Jan 2010
5.	<b>BFRS 5</b>	Non-current Assets Held for Sale and Discontinued Operations	1 Jan 2007
6.	<b>BFRS 6</b>	Exploration for and evaluation of Mineral Resources	1 Jan 2007
7.	<b>BFRS 7</b>	Financial Instruments: Disclosures	1 Jan 2010
8.	<b>BFRS 8</b>	Operating Segments	1 Jan 2010
9.	<b>IFRS 9</b>	Financial Instruments	Adopted by ICAB and going to publish in 2011
10.	<b>IFRS 10</b>	Consolidated Financial Statements	
11.	<b>IFRS 11</b>	Joint Arrangements	
12.	<b>IFRS 12</b>	Disclosure of Interests in Other Entities	(Effective Date on or after 1 Jan 2013)
13.	<b>IFRS 13</b>	Fair Value Measurement	
	<b>IFRS for SMEs</b>	BFRS for SMEs (Small Medium Size Entities)	1 Jan 2013

**Appendix- IV (A) - Adoption Status of International Standards on Auditing (ISA)**  
by ICAB as Bangladesh Accounting Standards (BAS)

Sl. #	ISA/BSA	ISA/ BSA Title
1.	200	Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing
2.	210	Agreeing the Terms of Audit Engagements
3.	220	Quality Control for an Audit of Financial Statements
4.	230	Audit Documentation
5.	240	The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements
6.	250	Consideration of Laws and Regulations in an Audit of Financial Statements
7.	260	Communication with Those Charged with Governance
8.	265	Communicating Deficiencies in Internal Control to Those Charged with Governance and Management
9.	300	Planning an Audit of Financial Statements
10.	315	Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment
11.	320	Materiality in Planning and Performing an Audit
12.	330	The Auditor's Responses to Assessed Risks
13.	402	Audit Considerations Relating to Entities Using Service Organization
14.	450	Evaluation of Misstatements Identified during the Audit
15.	500	Audit Evidence
16.	501	Audit Evidence—Specific Considerations for Selected Items
17.	505	External Confirmations
18.	510	Initial Audit Engagements—Opening Balances
19.	520	Analytical Procedures
20.	530	Audit Sampling
21.	540	Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures
22.	550	Related Parties
23.	560	Subsequent Events
24.	570	Going Concern
25.	580	Written Representations
26.	600	Special Considerations-Audits of Group Financial Statements (Including the Work of Component Auditors)
27.	610	Using the Work of Internal Auditors
28.	620	Using the Work of an Auditor's Expert
29.	700	Forming an Opinion and Reporting on Financial Statements
30.	705	Modifications to the Opinion in the Independent Auditor's Report
31.	706	Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report
32.	710	Comparative Information—Corresponding Figures and Comparative Financial Statements
33.	720	The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements
34.	800	Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks
35.	805	Special Considerations –Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement
36.	810	Engagements to Report on Summary Financial Statements
		Total BSA / Code of Ethics /BSQC 1 /Framework

**Appendix IV (B) - Adoption Status of International Auditing Practice Statements (IAP)**  
by ICAB as Bangladesh Auditing Practice Statements (BAPS)

Sl. #	IAPS / BAPS	BAPS Title
1.	1000	Inter-Bank Confirmation Procedures
2.	1004	The Relationship Between Banking Supervisors and Banks' External Auditors
3.	1005	The Special Considerations in the Audit of Small Entities(withdrawn in 2010)
4.	1006	Audits of the Financial Statements of the Banks
5.	1010	The Consideration of Environmental Matters in Audit of Financial Statements
6.	1012	Auditing Derivative Financial Statements
7.	1013	Electronic Commerce-Effect on the Audit of Financial Statements
8.	1014	Reporting by Auditors on Compliance with IFRS (withdrawn in 2010)

# Improvement of Accounting System of Public Enterprises is Essential to Ensure the Accountability of Public Sector

Md Shahadat Hossain FCA



Accountability is a concept in ethics and governance with several meanings. It is often used synonymously with such concepts as responsibility, answerability, blameworthiness, liability, and other terms associated with the expectation of account-giving. Accountability cannot exist without proper accounting practice. In other words, an absence of accounting means an absence of accountability. There are various types of public enterprises in Bangladesh. Some of them are providing various services including utility service; some are running as commercial organizations with the objective of making profit as well as providing social service under the ownership of the Government of Bangladesh. Bangladesh Power Development Board, Dhaka Water Supply and Sewerage Authority, Bangladesh Jute Mills Corporation., Bangladesh Railway etc are the examples of those enterprises. It is pertinent to mention here that due to loss incurred by those public enterprises a substantial amount is spent as subsidy every year from the government fund which is collected from the people of the country in the form of tax. So, to ensure the proper accountability of public sector, it is all the more essential to ensure the proper accounting system. For each type of public enterprises there are different accounting systems. Accounting system of each type of organizations is determined

by the respective law / order. For example, there is separate accounting code for Bangladesh Railway. Similarly accounting system of each sector corporation is determined by the presidential order by which the corporation was established. Almost all the public enterprises prepare their financial statements based on the information determined by them which is conformed to the accrual basis and double entry system of accounting. However, in the system there remain lack of accrual basis, in brief, some of them are described below;

In most of the cases inventories are not measured and valued in the systematic manner. In the financial statements value of inventories is taken from the general ledger. This figure is not reconciled with the store ledger. In most of the cases obsolete, damage items are being carried forward since long without any provision or write off. In some cases store –in-transit is brought forward year after year without any adjustment.

In many cases receivable balance due to sales and for other purposes is not presented in the financial statements of the public enterprises with correct measurement. This incorrect measurement takes place in way of non-reconciliation

with the subsidiary ledger and some times due to making no provision for bad and doubtful debts.

In many cases amount of cash at bank balance is not measured correctly. This balance is presented incorrectly by the way of non-reconciliation of bank balance with the bank statement, due to not receiving any payment advice from the concerned department by the accounting office or department. Due to not making provision or write off of unrealizable fraud, forgery, emblazonment transit loss from the bank account, the cash at bank balance does not give the true picture.

Payables for procurement of materials and receiving services are not properly measured and presented in the financial statements by the various public enterprises. This inaccurate measurement and presentation happen due to lack of system of non-reconciliation between general ledger balance and subsidiary ledger balances. Sometimes this happens due to not receiving the material procurement documents by the accounts department of the concerned public organization. In many organizations there is a system of non-accepting the bills despite taking, delivery of materials due to not having sufficient budget for the respective materials in respective year. In many cases different payable balances are being brought forward since pre-liberation period which have no scope of repayment.

Property, Plant & Equipment is the most important asset items of the Organization. Almost all the public enterprises own property, plant & equipment valued at a quite significant amount. But in most of the cases value of such property, plant & equipment is not measured and presented in the financial statements correctly. Due to various reasons such incorrect measurement of value takes place. Some of them are

mentioned below:

- i) Fixed Asset register is not maintained by most of the public enterprises properly.
- ii) Values of general ledger balances are not reconciled with the register balance.
- iii) Depreciation on property, plant & equipment is not charged regularly.
- iv) Cost and accumulated depreciation of many items which have been physically declared obsolete, damaged, is not adjusted properly.
- v) Physical inventory of property, plant and equipment is not taken by the management on regular basis.
- vi) Sometimes it also happens that asset is purchased but due to having no budget, bill cannot be paid and therefore asset is not valued and accounted for properly.

Tax liability/ asset is not presented in the financial statements properly. Especially deferred tax liability / asset is not calculated and accounted for in the financial statement of public enterprises. In the financial statements of public enterprises especially in the financial statement of various industrial units of sector corporations there are fixed assets valued at-huge amount. Due to difference of depreciation rates between corporation and tax authority there arise temporary gap of allowing expenditure under the heading depreciation. But most of the public enterprises do not calculate and account for the effect of those temporary differences of fixed assets in respect of tax accounting.

According to the Government service Rule, which is applicable to the public enterprise, all employees will get gratuity/ pension after his retirement equivalent to two months basic salary for each service year. As per accounting system this retirement

“ PROPERTY, PLANT & EQUIPMENT IS THE MOST IMPORTANT ASSET ITEMS OF THE ORGANIZATION. ALMOST ALL THE PUBLIC ENTERPRISES OWN PROPERTY, PLANT & EQUIPMENT VALUED AT A QUITE SIGNIFICANT AMOUNT. BUT IN MOST OF THE CASES VALUE OF SUCH PROPERTY, PLANT & EQUIPMENT IS NOT MEASURED AND PRESENTED IN THE FINANCIAL STATEMENTS CORRECTLY. ”



benefit should be provided in the financial statement based on actual calculation. But many of the public enterprises do not follow the system. Some organizations charge retirement benefit on lump sum basis and some organizations charge based on actual payment in a year.

Shortcomings in proper recognition and measurement of revenue and expenditure are another hurdle of preparation of correct financial statement of public enterprises. The reason of incorrect recognition and measurement of revenue and expenditure is the corresponding incorrect recognition and measurement of receivable and payable respectively which have been elaborated earlier.

In case of almost every public enterprise, current liabilities are not presented in the balance sheet. The part of long term liability which is repayable within next year should be presented under the head current liability. But violating the accounting norms most of the public enterprises present that liability under long term liability.

To present commitment and contingent liability as on balance sheet date is one of the requirements of proper accounting. In almost all the public enterprises there remain commitment of supply and or contingent liability. But none of the public enterprises measures the contingent liability and commitment and presents it in the financial statements.

Reasons of non compliances of accounting system as described are presented below:

Lack of proper knowledgeable person is one of the hindrances to prepare the financial statement. Most of the public enterprises do not have professional accountants and even there remain personnel who do not have accounting background in the accounts department. Due to not having professional accountant in the organization they are not in a position to comply with all the related accounting system and standard.

Government bureaucratic system is another obstacle to prepare the

financial statement correctly and properly. For example, after completion of a work or supply of materials, the bill should be accounted for on accrual basis. But in the public enterprise that should be checked with budget provision first and if budget is available, in that case this will be accepted for approval and payment and, if budget is not available, the bill will not be accepted and it will be deferred for next financial year. After receiving the bill, this will be checked by relevant department. After having this approval, this bill will be forwarded to accounts department for payment and accounting. This is a long drawn time consuming process. Due to this, proper accounts can not be prepared.

For preparation of complete and correct accounts lack of inter departmental co-ordination is one of the limitations which the public enterprises are facing. For example, on receiving a bill against supply or completion of the work, this will be scrutinized for payment but according to accounting norms this should be accounted for. To resolve this situation there should be a close co-ordination between bill approving department and accounts department to account the pending bills which are waiting for approval. This lack of co-ordination creates hindrance to prepare complete accounts.

Apathy to prepare complete financial statements is another shortcoming in case of public enterprises. Due to want of proper accounting knowledge and having no accountability for non preparation of correct accounts, the management of public enterprises is not resolute to prepare complete and correct accounts of the organization.

Due to not giving emphasis on

accounts and accounting system by the senior managements of the organization, accounts are not prepared properly. Most of the public enterprises do not consider the financial statements as the decision making tools. From the activity of public enterprises it appears that they prepare financial statement merely to comply with the contents of rule, Act, ordinance etc.

There remains serious lack of accountability for preparing correct and complete financial statements of public enterprises. In most of the cases they do not bear any comment or feed back which is necessary to improve the quality of preparing financial statements.

Ignorance about benefits of standard accounts and demerits of incorrect, incomplete financial statements of an organization is one of the main factors for not preparing correct, complete & standard financial statements of a public enterprise. The management of most of the public enterprises is not aware of the impact of correct and incorrect financial statements on the organization and therefore they do not feel the necessity of preparing financial statements properly.

Lowering the deserving professional fees, annual audit fees is also one of the causes for preparation of less quality financial statements of the public enterprises. No doubt, the Chartered Accountants give various guidelines / suggestions which are helpful to improve the quality of Financial Statements. But



due to less fees than deserving paid by the entity, the auditor does not feel due incentive to give any valued suggestion. At present, fees structure of the sector corporation and other public enterprises is very poor. Due to this poor audit fees Chartered Accountants do not feel comfortable to give any useful suggestion through their audit work which is helpful to improve the quality of the presentation of financial statements. This is one of the vital issues for less quality accounting system of the public enterprises.

As mentioned earlier, every year a substantial amount is spent as subsidy from the government fund due to loss incurred by the public enterprises, but the reason of incurring loss is not reflected in the

financial statements because of their being prepared without the following of all the standards of accounting. It clearly indicates the lack of accountability in public sector. So, to make sure the accountability and good governance in the public sector there is no other alternative but to improve the accounting system and to comply the International Financial Reporting Standards as adopted by the Institute of Chartered Accountants of Bangladesh at the time of preparing financial statements . Professional assistance also needs to be taken during preparation of financial statements.

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***The Author is a Council Member of ICAB***



# An Alternative Financial System for Inclusive Growth and Sustainable Development

Md Abdus Salam FCA



## Introduction

Experiences and experiments with growth in twentieth century end up with an unpleasant conclusion that growth could not be made sustainable without following the path of inclusive growth. This has resulted in disparity in income at country as well as global level. In a recent meeting of the World Economic Forum (WEF) in Davos, Switzerland it was raised that the widening gap between the rich and poor was going to be a threat for the sustainable growth of the world economy.

The Organization for Economic Cooperation and Development (OECD) in a study found that the income of the 1.0 per cent super rich have doubled in less than three decades in the US. The average income of the mega rich 10 per cent of the people of 34 nation of the OECD is nine times more than the poorest ten per cent.

The major theme of protest is 99 per cent of the poor are paying for the sins of 1.0 per cent. This issue is being debated in areas where laissez faire capitalism was taken for granted and where talk of inequality used to be mocked as class warfare. Europe is simmering with discontent. So is the Arab world.

This together with global financial crisis

repeatedly pushing the global economy into plunge almost every decade has further raised the question whether the banking system based on interest can at all contribute to promote sustainable development. It is sometimes argued that the mainstream banking based on interest itself accelerate cyclical fluctuation i.e., expedite recession.

Emergence of Islamic banking and its rapid expansion in developing and developed world raised hopes and concern whether the world is getting a suitable world economic order to face frequent ups and downs in growth and make the development sustainable.

In this article the above concerns have been addressed from the perspective of systemic capacity of the newly emerged banking known as Islamic Banking.

## Mainstream Perception of Inclusive Growth and Sustainable Development

### Inclusive Growth

Inclusive Growth refers to the pace and pattern of growth simultaneously, which are interlinked and must be addressed together. Rapid pace of growth is unquestionably necessary for substantial

poverty reduction. But the growth to be sustainable in the long run, it should be broad-based across sectors, and inclusive of the large part of a country's labor force. This definition implies a direct link between the macro and micro determinants of growth.

Five interrelated elements of inclusive growth.

- Poverty Reduction and increase in quantity and quality of employment
- Agricultural Development
- Social Sector Development
- Reduction in regional disparities
- Protecting the environment

The inclusive growth approach takes a longer term perspective. The focus is on productive employment rather than on direct income redistribution. The approach provides avenues for increasing incomes for excluded groups. In short, inclusive growth is about raising the pace of growth and enlarging the size of the economy providing a level playing ground for investment and increasing productive employment opportunities.

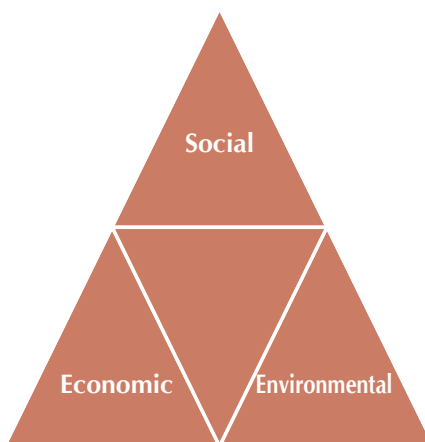
### Sustainable Development

Sustainable development is the development that meets the present needs without compromising the ability of future generations to meet their own needs. It contains:

- the concept of needs, in particular the essential needs of the world's poor, to which overriding priority should be given; and
- the idea of limitations imposed by the state of technology and social organization on the environment's ability to meet present and future needs."

Meeting the needs of the future depends on how well we balance social, economic, and environmental objectives—or needs—when making

decisions today. The concept may be presented in diagrammatic form as below:



Services	Equity	Biodiversity
Household Needs	Participation	Natural Resources
Industrial Growth	Empowerment	Carrying
Agricultural Growth	Social Mobility	Ecosystem Integrity
Efficient Use of Labour	Cultural Preservation	Clean Air and Water

### Financial Inclusion as Understood and Practiced in Mainstream Banking

Financial inclusion is the availability of banking services at an affordable cost to disadvantaged and low-income groups. The basic concept of financial inclusion is having a saving or current account with any bank. In reality it includes loans, insurance services and much more.

Financial inclusion mainly focuses on the poor who do not have formal financial institutional support and getting them out of the clutches of local money lenders.

### Barriers to financial inclusion in Bangladesh

Bangladesh Bank has identified ten barriers including poor banking infrastructure, particularly in rural

“ FINANCIAL INCLUSION MAINLY FOCUSES ON THE POOR WHO DO NOT HAVE FORMAL FINANCIAL INSTITUTIONAL SUPPORT AND GETTING THEM OUT OF THE CLUTCHES OF LOCAL MONEY LENDERS. ”

areas, now stand in the way of financial inclusion in Bangladesh. In Bangladesh, about half of the adult population is un-banked (48.49 percent) in terms of deposit accounts in the banks .

The major barrier is geographical or physical access measuring the average distance from household to bank branch. However, the branches per 1,000 square kilometres could be used as crude indicator for providing an initial idea to the barriers of inclusion.

As a competitive and cost effective strategy, major banks focus on large scale of loans instead of providing services for small size of loan. As a result, rational business decisions prevent a major portion of people from accessing loan services including small and medium enterprises (SME) and agriculture loan.

Promoting technological and institutional innovations as a means could expand the financial system access and usage. However, less than four people per 1,000 populations in the country are using credit cards identifying the technological and infrastructural weaknesses.

Other weaknesses of financial inclusion include:

- Lack of proper documentation
- Inadequate financial literacy or education
- High requirement of minimum balance
- Low income
- Lack of suitable product structure of banks and micro-financial institutions (MFIs)
- High cost of product and
- Absence of credit bureau and insurance of MFI borrowers.

Recent trend in mobile banking

indicates that financial inclusion is scaling up in Bangladesh especially in rural areas where no bank branch is available.

### **Financial inclusion and growth expediting programs by Bangladesh Bank**

Despite a large number of bank branches and micro finance institutions in our country, a large segment of our population particularly rural poor have scant access to banking services. Bangladesh Bank and the Government of Bangladesh (GoB) have adopted several remedial measures to bridge these gaps in financial inclusion such as: a) Refinance schemes; b) Opening of SME and Special Programs Department; c) Agriculture credit programs; d) Infrastructural development loans programs for environment friendly investments in solar energy, Biogas plants and Effluent Treatment Plants (ETP); e) motivational programs for financial institutions on Corporate Social Responsibilities etc.

### **Why Alternative Banking?**

#### **Repeated Global Financial Crisis: Interest-based Financial System failing to Manage Risk and Allocate Capital**

Repeated financial crises leading to plunge global economy into recession has been regular phenomenon which questions sustainability of the banking system based on interest. Joseph Stiglitz says, America's financial system failed in its two crucial responsibilities: managing risk and allocating capital. The industry as a whole has not been doing what it should be doing ... and it must now face change in its regulatory structures. Regrettably, many of the worst elements of the US financial system ... were exported to the rest

of the world. It was all done in the name of innovation, and any regulatory initiative was fought away with claims that it would suppress that innovation. Dishonesty in the finance sector dragged us here, and Washington looks ill-equipped to guide us out. The analysis by Stiglitz is a serious blow to the institutional viability of the financial system under capitalism, known now a days as 'casino capitalism'.

### **To get rid of a Greedy Soulless banking that crushing the Economy**

The problem is that banking institutions based on interest no longer want to perform the human functions they've performed for a thousand years. Financing has become a robotic form of mass production, designed to generate ever-increasing wealth within an artificial system by draining it from the real world. In a word, banks have lost their souls.

A recent report blames last May's "flash crash" on software run wild, while the new "robo-signing" mortgage scandal looks a lot like (and is) old-fashioned fraud. The "flash crash," which caused the stock market to plunge 600 points and bounce back within minutes, was computer-driven. In the "robo-signing" scandal the "robots" weren't machines, but bank employees who "mechanically" signed legal statements without checking their accuracy. But both are symptoms of a common disease. They both stem from the banks' insatiable desire to earn the maximum amount of money while expending the minimum amount of effort, with the least possible real-world interaction. That's led to a mechanized form of banking that's devouring the economy.

## Pro-cyclicality of Interest-based banking system

A number of causes like wrong Fed policy, deregulation or the bad innovation of so-called credit derivatives and last not the least the failure of the financial system in managing risk and allocating capital are blamed to be the reasons of the 2008-09 credit crunch.

Jan Kregel considers the subprime crisis in the US has little to do with the mortgage market, or subprime mortgages per se, but rather with the basic structure of the financial system that produces overestimates of creditworthiness and under pricing of risk. The bottom line is that the system has been structured to make credit too cheap, leading to excessive risk in order to provide higher returns. The financial fragility that was identified in Minsky's work cannot be eliminated, only be damped by systemic policies.

Minsky identified fragility of conventional banking system based on interest in the context of business cycle. He finds lending mechanism of interest-based banking system as an internal cause of accelerating business cycle, i.e. recurring boom and recession in capitalist economy.

It is the 'spread' between the fixed payment commitments to bank against uncertain cash flow of the borrowers that widens while the economy switches over from boom to recession. The implication is that interest-based conventional banks become more and more alert and desperate in recovering dues from the borrowers which lead to foreclosure of already sick enterprises, bringing other solvent units in line of foreclosure by diverting funds from such units to the already sick ones.



## Need for a Counter-cyclical Banking System

Minsky Credit Cycle applied to the last three credit boom and asset bubbles (including the recent one in October 2008) is interpreted as follows: (a) all of the three credit cycles started with the economic boom and ended with recession. That means, each credit cycle is linked to business cycle with the implication that crisis in financial sector generates instability in real sector following each boom and accelerates recession or depression in the economy. In other words, financial sector has a pro-cyclicality effect on the real sector and that works through the fixed payment commitment of the borrowers against their uncertain cash flows.

IMF's main task should be to analyze the interaction between the real economy and the financial

system, and monitoring, particularly while implementing supervisory standards and stability risk in the context of Article IV consultations and the ESAP.

This calls for bringing reforms in contractual obligations of and relationship between the financier and borrower so that corrective measures can be taken towards removing pro-cyclical character of the financial institutions.

## Resilience of Islamic Banking during Global Recession

A new IMF study compares the performance of Islamic banks and conventional banks during the recent financial crisis, and finds that Islamic banks, on average, showed stronger resilience during the global financial crisis.

But the study also finds that Islamic

banks faced larger losses than their conventional peers when the crisis hit the real economy.

The study looked at the effects of the crisis on bank profitability, credit, and asset growth in countries where both types of banks have a significant market share. The new working paper adds an empirical dimension to the debate on the relationship between Islamic banking and financial stability, a topic that has generated renewed interest since the global crisis.

Islamic finance is one of the fastest growing segments of the global financial industry. In some countries, it has become systemically important and, in many others, it is too big to be ignored. It is estimated that the size of the Islamic banking industry at the global level was close to \$820 billion at end-2008. The largest Islamic banks are located in the countries of the Gulf Cooperation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates).

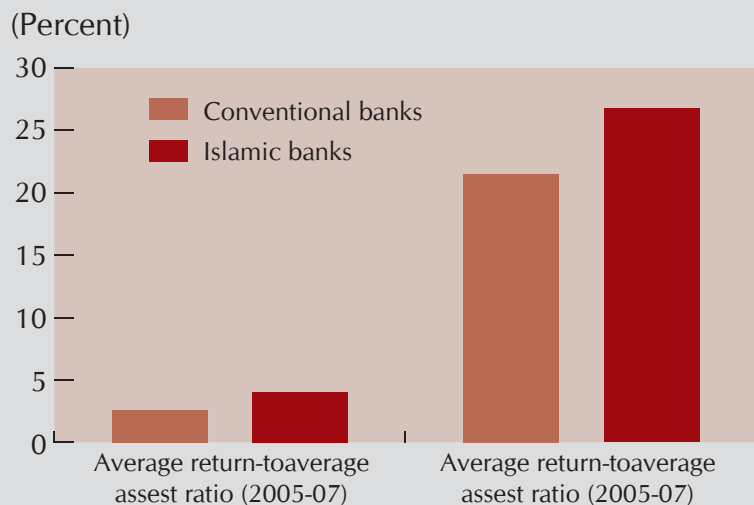
Chart 1, 2 & 3 show Before the Crisis Position, After the Crisis Effects and Deepening Impact respectively using bank-level data covering 2007 – 10 for about 120 Islamic banks and conventional banks in eight countries—Bahrain, Jordan, Kuwait, Malaysia, Qatar, Saudi Arabia, Turkey, and the United Arab Emirates. The key variables used to assess the impact are the changes in profitability, bank lending, bank assets, and external bank ratings.

The analysis suggests that Islamic banks fared differently from conventional banks during the global financial crisis. Factors related to the Islamic banking business model helped contain the adverse impact on their

Chart 1

## Before the crisis

Islamic banks were more profitable than their conventional peers in the runup to the crisis.



Sources: IMF staff estimates and calculations

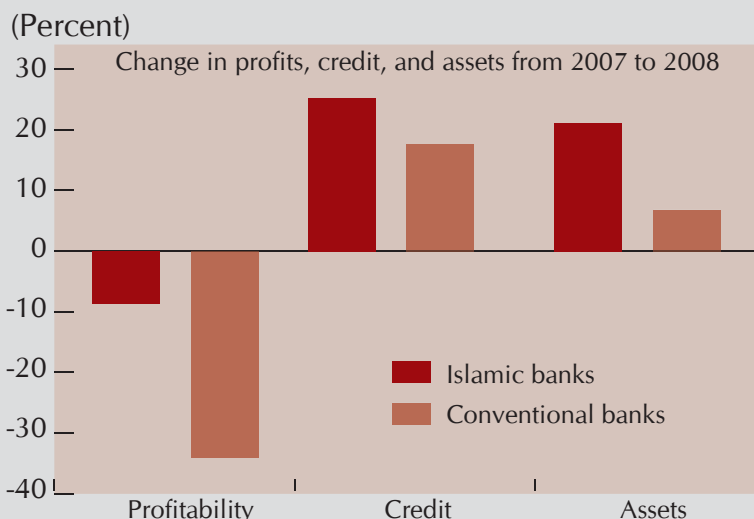
profitability in 2008 (see Chart 2). In particular, smaller investment portfolios, lower leverage, and adherence to Shariah

principles—which precluded Islamic banks from financing or investing in the kind of instruments that have adversely affected their

Chart 2

## Initial crisis effect

Islamic banks saw only a minor impact on profitability in the early stages of the crisis, while credit and asset growth remained strong.



Sources: IMF staff estimates and calculations

conventional competitors—helped contain the impact of the crisis on Islamic banks in that year.

The following year, however, weaknesses in risk management practices in some Islamic banks led to a larger decline in profitability compared to that seen in conventional banks (see Chart 3).

The weak 2009 performance in some countries was associated with sectoral and name concentration—that is, too great a degree of exposure to any one sector or borrower. In some cases, the problem was made worse by exemptions from concentration limits, highlighting the importance of having a neutral regulatory framework for both types of banks.

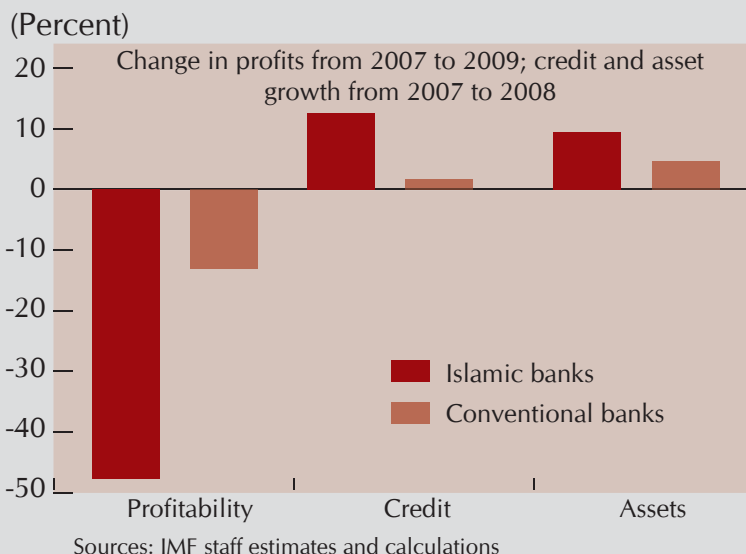
Despite the higher profitability of Islamic banks during the pre-global crisis period (2005–07), their average profitability for 2008–09 was similar to that of conventional banks, indicating better cumulative profitability and suggesting that higher pre-crisis profitability was not driven by a strategy of greater risk taking. The analysis also shows that large Islamic banks fared better than small ones, perhaps as a result of better diversification, economies of scale, and stronger reputation. Development of the industry might therefore be achieved, the paper suggests, through establishing large, well-managed Islamic banks that can compete with existing banks.

Islamic banks contributed to financial and economic stability during the crisis, given that their credit and asset growth was at least twice as high as that of conventional banks. This growth was due to their higher solvency and to the fact that many Islamic banks lent a larger part of their portfolio to the consumer sector, which was less affected by the

Chart 2

## Initial crisis effect

As the crisis moved to the real economy in 2009, Islamic banks saw a steep decline in profitability.



crisis than other sectors in the countries studied. These findings were corroborated by external rating agencies' reassessment of Islamic banks' risk, which was generally found to be more favorable than—or similar to—that of conventional banks.

In view of their robust growth during the crisis, Islamic banks will likely take a growing market share in the future—but this implies greater supervisory responsibility, the study found.

### Islamic banking as new alternative to interest-based banking system

Islamic banking is emerging as a new alternative to interest-based system. While Islamic banks play a role similar to conventional banks, fundamental differences exist between the two models. The main difference between Islamic and conventional banks is that the former operate in accordance with

the rules of Shariah, the legal code of Islam. The central concept in Islamic banking and finance is justice, which is achieved mainly through the sharing of risk. Stakeholders are supposed to share profits and losses, and charging interest is prohibited.

There are also differences in terms of financial intermediation. While conventional intermediation is largely debt based, and allows for risk transfer, Islamic intermediation, by contrast, is asset based, and centers on risk sharing. One key difference between conventional banks and Islamic banks is that the latter's model does not allow investing in or financing the kind of instruments that have adversely affected their conventional competitors and triggered the global financial crisis. These include toxic assets, derivatives, and conventional financial institution securities.

## Advantage of Islamic Banking

Islamic banking has gained a foothold in Muslim countries and internationally in the financial markets. Islamic banking offers a better financial architecture on several economic grounds.

- It reduces the dichotomy between financing and the use of funds leading to integration of real and financial sectors of the economy.
- The direct linkage between financing and application of

funds under Islamic banking means an end to untied cash as found in interest based economies.

Thus an important causes of the mismatch between aggregate demand and supply in the economy will be removed.

- This means less demand-pull inflation.
- Linkage of financing to economic activity will help ease supply constraints resulting in employment generation.

## Operation of an Islamic Bank

From an operational point of view, Islamic banking system is based on the prohibition of the interest rate and on sharing the risk in the relations between the bank, the loan receiver and the investors. By applying the profit and loss sharing method, the remuneration (or absence of remuneration) of deposits and of the operating investments of the bank isn't connected with the temporal dimension. Western banks whose activity of capital intermediation is based on the payment of an interest rate is determined in a percentage of stake set in the contract.

Islamic banking has shown a new conception of the relation between economic activity and religion. Its "raw material" isn't money but a new network of relations, collaborations, participations whose aim isn't the dividend speculative maximization but the way to a new approach in the conduct of business, in which moral motivations and of sustainable development could find a place, as God has created all things in the suitable quantity to satisfy human needs, and their shortage is the consequence of human behaviour driven by the desire for accumulation.

## Strengths and System efficiency of Islamic banking

### Objectives of Islamic Banking

In line with the principles of maqasid-al-shariah Islamic banks pursue the following objectives in their operation:

- Support promotion of economic development with distributive justice.
- Optimum allocation of scarce resources by allocating

## Difference between Islamic and Conventional Bank:

Main difference	Islamic bank	Conventional bank
Principles	Islamic banks follow the Principles of Sharia'h.	Conventional banks follow the principle of payment and receipt of fixed rate of interest in their operations and activities.
Source of earnings	Profit, service charges and consultancy fee is the main source of earnings of Islamic banks. Profit is variable which may be negative in case of loss.	Interest is the main source of income for conventional banks that is charged on different types of loans/products. (Difference between interests charged from borrowers and paid to depositors). It assures a predetermined rate of interest.
Risk sharing	Risk is shared among borrower, lender and bank.	Risk is fully transferred to others.
Profit maximization	It aims at maximizing the profit but subject to principles of Sharia'h.	It aims at maximizing the profit without any restriction even at the cost of other stakeholders.
Objectives	Islamic bank works as a trading concern to generate its income.	It generates income as financial intermediary. Its prime goal is the maximization of shareholders' value at any cost.
Nature of earnings	Income of Islamic banks varies depending upon business borrowers and environment. It may be negative in case of loss.	Income of conventional bank is constant even if business borrowers suffer from loss because it charges fixed rate of interest irrespective of profit volume.

financial resources in terms of profitability.

- Ensure equitable distribution of income and resources among the participating parties: the bank, the depositors and the entrepreneurs.

### Strengths and Efficiencies of Islamic Banking

Islamic banking, essentially known as profit-loss-sharing banking, is conceived as more production-oriented and growth promoting than its conventional counterpart. This is because the bank's earnings are directly linked to the earnings generated from the venture financed by it. Further, replacement of interest with the principle of profit-loss sharing increases the horizon of investment opportunity in an economy. It also promotes efficient allocation of financial resources, ensures equitable distribution of income and promotes stability in the economy. Thus, Islamic banking is efficient by all macroeconomic efficiency considerations. The efficiency of the Islamic banking system can best be illustrated by the investment decision model as presented below:

#### Investment Decision Model: Conventional and Islamic Banking

Figure 1a represents the investment decision model under conventional banking and Figure 1b represents the same under Islamic banking. The generalized banking decision-making process is modelled in Figure 2, which is derived by superimposing Figure 1b on Figure 1a.

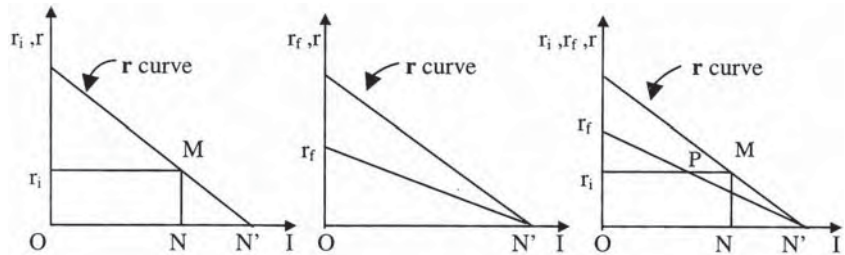


Fig-1a: Investment Decision by Conventional banks	Fig-1b: Investment Decision by Islamic banks	Fig-2: Investment Decisions by Conventional and Islamic banks
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The horizontal axis of Figure 2 depicts the level of investment,  $I$ , at different rates of interest ( $r_i$ ) for a Conventional bank and financier's rate of return ( $r_f$ ) for Islamic bank.

#### Investment Decision under Conventional Banking

In Conventional banking, the rate of return to the bank is fixed regardless of the profitability of the projects it has financed. The case is opposite to what happens with the Islamic banking. Under the Conventional banking framework, as depicted in Figure 1a, the bank charges a fixed rate of interest to finance only those projects which have rates of return higher than or equal to the rate of interest. Thus, the Conventional banking system could be termed a Fixed Return Mechanism (FRM).

#### Investment Decision under Islamic banking

Under Islamic banking (technically known as the profit-loss sharing system of investment financing), the bank receives a variable rate of return as it shares a percentage of profit earned by the entrepreneur. Thus, the Profit-loss-sharing system of investment financing may be termed a Variable Return Mechanism (VRM). Since the

Islamic banking system does not charge interest on any financing transactions, neither the bank nor the client receives or pays a fixed rate of return on an investment financed.

#### Investment Opportunity Utilization

Investment opportunity means total number of projects, calculated in money terms, in an economy, which are waiting to be financed having their internal rates of return greater than or equal to zero, i.e.,  $IRR \leq 0$ , assuming no cost of fund (borrowing) and non-existence of other alternative opportunities for investment. For a clear understanding of the concept we may refer to Figure 2. The vertical axis shows different rates of return of bank-financed projects while the horizontal axis indicates the amount of investment that could be made at different rates of return. The downward sloping rate of return curve,  $r$ , indicates that projects available in an economy can be arranged in the descending order of their rate of return and can be financed as long as the rate of return is greater than or equal to zero. If so, according to Figure 2,  $ON'$  is the investment opportunity level.

Under the assumption that fund is available at zero cost, the investment opportunity utilization test can be applied to compare efficiency level of different banking systems.

### **Utilisation of investment opportunity by Interest-based Banking System**

Figure-2 shows that there exists ON level of investment opportunity. Assuming availability of investible funds, the optimum level of investment under the conventional banking framework will be determined at the point ON, where the rate of return,  $r$ , and rate of interest,  $r_i$ , intersect at point M.

With Ori rate of interest, an interest-based bank is interested to finance ON level of investment. Projects beyond ON level are rejected for financing under the Conventional banking system because the rate of interest exceeds the rate of return from those projects making them non-profitable for the entrepreneurs and non-viable for bank financing. That means, under conventional banking a portion of investment opportunity always remains unutilized.

### **Utilization of investment opportunity by Islamic Banking**

An Islamic bank can finance up to the level ON' of investment, thereby utilizing the extra potential investment opportunity of NN'. This is possible for Islamic banking since it can remain at least at the level of the average rate of return earned by the conventional bank by counterbalancing the losses incurred in the low profit zone (right of point P) by the excess profit earned in the high profit zone (left of point P), thereby achieving the average rate of profit

to the level of the conventional bank. Thus, the Islamic bank can utilize more of the potential investment opportunity remaining untapped in the economy. With a microeconomic analysis in a dynamic sense, Mukherji (1984) finds that compared to a capitalist firm, the firm in a Zero Interest Rate Economy will have a high rate of growth at low profit margin.

### **Efficient Allocation of Resources and Islamic Banking**

The Islamic banking system is very efficient in allocating resources in the economy. Allocative efficiency is concerned with the best possible utilization of the community's scarce financial resources so as to attain the maximum benefit to society. There are two broad ways to promote economic welfare in a world of scarcity: (a) prioritize the projects in order of social benefits and allocate the resources accordingly until the resources are exhausted, and (b) meet each obligation with the least possible amount of resources.

Allocative efficiency is not only limited to prioritizing projects in order of decreasing desirability and employing resources according to that order, but also putting them to their best possible use since all desirable options cannot be satisfied at a time.

An optimum allocation of investible funds may be possible if (a) each project ranked under categories of socio-economic desirability is given a particular weight and funds are separated accordingly; and (b) funds so separated for a particular category of projects are then allocated in terms of its profitability, assuming that all other conditions have been satisfied.

Thus in order to make an investment financing system efficient, one must follow two criteria so far as allocative efficiency is concerned: (a) projects should be prioritized in terms of decreasing desirability, and (b) projects should be prioritized in terms of their profitability (in descending order).

Unfortunately, the conventional banking system does not satisfy these criteria. In spite of the fact that conventional banks take into account the profitability of the project, the collateral position, and the personal integrity of the borrowers, their interest earnings do not have any direct relation to profits to be generated from the projects they finance. Therefore, profitability does not work ultimately as a principal criterion for fund allocation. Chapra refers to the contention of Ralph Turvey that, under Conventional banking, the rate of interest is irrelevant to investment decisions and hence should be replaced by the price of existing equipment or share prices. In Figure 3 we do not find any causal relation between the downward sloping  $r$  and the horizontal  $r_i$  curves.

On the other hand, the above mentioned fund allocation criteria fit quite appropriately to the mechanism of Islamic banking satisfying social welfare conditions.<sup>31</sup> This is true because the very basis of Islamic banking is profit-loss sharing where profitability stands first in order among the deciding factors in selecting a project for financing. While the first criterion narrates the distributional aspect of resource allocation, the second allocates resources for their most productive utilization.

## Distributive Justice under Islamic Banking

The rationale behind allowing banks to use public money to finance investment is obviously the contribution it makes to economic development of a country. Today, economic development is not merely meant for increased production of goods and services. Rather it means, according to the latest evolution of the concept, growth plus equitable distribution.

A banking system may influence distribution in two stages. First, it influences distribution through the deployment of financial resources among different sectors, regions and different income groups. Secondly, it affects distribution by the way it distributes the incomes generated by the financing process among the stakeholders (the depositors, the bank, and the entrepreneurs). Hence, in order for a banking system to be an efficient one, it should ensure equitable distribution of investible funds among different sectors, regions and different income groups as well as distribution of risks and returns among the stake holders.

The criteria that might be used here for identifying relative distributive efficiency of the two systems of banking are as follows:

- (a) Classifying deposits and advances in terms of account size or, if possible, in terms of income size;
- (b) Profit-income or interest-income ratios between the entrepreneurs and the bank, and that of the bank and the depositors; and
- (c) Rural-urban classification of deposits and advances;

It is found from Figure 2 that conventional banking maintains a flat rate of interest regardless of the

profitability of the projects financed by it. In other words, a bank's income under the conventional system is by no means related to profit accrued from the projects it finances. Therefore, the bank receives only the fixed interest as its income. The entrepreneur is the only party that benefits from the profits of the business venture.

## Economic Stability and Islamic Banking

Built-in shock absorption capability: Islamic banking by mechanism has built-in capacity to stabilize the economy in which it operates. This is exemplified by contractual obligations Islamic banking maintains in its asset and liability sides. As a system Islamic banking essentially being a Profit-Loss-Sharing (PLS) financial institution, it offers depositors with a provisional rate of profit which is adjusted plus or minus with actual profit earned. So, Islamic banks has no fixed payment obligation with the depositors. Similarly, Islamic banks being a PLS financial institution, shares a ratio of profit earned by the borrowing investor, not a fixed rate of return like rate of interest. That means, it shares higher profit from the financed project if it earns high profit, and shares lower if profit is lower from the project. The implication is that during time of recession an Islamic bank is ready to receive lower and even negative profit from its investment. This unique character of the Islamic banking system works as built-in stabilizer of cyclical fluctuation or business cycle or any other shocks in the economy.

## Islamic banking and Inclusive Growth

A recent study done by the IMF shows that income inequalities are

rising and despite the unprecedented gains in per capita incomes regional, inter-personal, rural-urban and gender income disparities have widened and are getting worse. How can this be overcome and these inequalities between different classes of human beings be minimized if not completely eliminated? Islamic economic System of which Islamic finance is an integral part suggests that it is possible to achieve inclusive growth and poverty alleviation if we follow the precepts and practices of this system.

## Objectives and features of Islamic Economic System

Unlike positive economics the entire edifice of Islamic economy is built upon a set of objectives or maqasid. In other words, Islamic economics is normative in nature with the objective of the Shariah being to promote the well being of all mankind which lies in safeguarding their faith, their human self, their intellect, their posterity and their wealth. Islamic system tries to promote a balance between market, family, society and the state.

It does so by promoting both the material and the spiritual urges of the human self, foster peace of mind, enhance family and social solidarity.

In Islamic economic model the market mechanism makes the allocation and distribution of resources subject to a double layer of filters. Unlike the Western model, the Muslim is not expected to behave in a way that is exclusively concerned with his immediate self gratification. He/She has to consider as to how his/ her selfish behaviour impinges upon the collective interests of the society. For this restraining

influence a Muslim realizes that his beliefs and Faith have embedded his/ her self-interest in a longer term perspective - stretching it beyond the span of this world to Life Hereafter. This interest in Hereafter cannot be served except by fulfilling his or her social obligations.

At the macro level, Islamic economic model in its ideal form tends to combine the positive aspects of the capitalist economy and socialist economy while minimizing their negative consequences. Islamic System overcomes the deficiencies of both the systems as it is solidly based on private property and market mechanism but has also explicitly built in equity and distribution through compulsory deduction of Zakat i.e. transfer payments from the asset holders to the poor segments of the population. Islamic economic model addresses the distribution issues explicitly after growth takes place and market has allocated the gains.

At the sectoral level, the introduction of Islamic banking has promoted financial inclusion by bringing those who have so far remained outside the conventional banking system thus deepening the financial sector.

There are believers in Islamic Faith who do not use the Conventional banking system because of their strongly held views that this system is based on riba. They withdraw themselves from banking operation based on interest and remain excluded. These people can be included by expanding Islamic banking operation to their doorstep.

### **Role of Islamic Banking in Financial Inclusion**

The role of the banking is the

general economic improvement of the public at large rather than of few groups. How can the Islamic banks help the poor and also help in reducing income inequalities? Most of the conventional banks' presence is limited to metropolitan areas and big cities. Islamic banks spread their geographical presence by locating their branches or other delivery channels in these potentially attractive but underserved areas and use IT tools and alliances with Post Offices, and other distribution outlets to develop cost effective business model.

It provides ethical solutions for preventing financial crisis due to its reliance on mostly real asset-backed transactions, avoidance of sub-prime securities and avoidance of financial leverage from hybrid products like derivatives and associated creative accounting.

Islamic finance is also less prone to inflation and less vulnerable to gambling like speculation, both of which are fuelled by the presence of huge quantities of debt instruments and derivatives in the market.

It stimulates real sectors in the economy instead of financial engineering, performs the critical function of mobilizing savings and intermediates them for investment to generate growth and alleviate poverty among the excluded and un-bankable segments of the poor and low income groups, thereby enabling them to participate and benefit from economic growth.

Islamic banking is an alternative system based on equity and justice and socially responsible investment, largely insulated from subprime crisis and is welcomed by all communities. As many as 40% customers in Malaysian

Islamic Banks are Chinese and in UK Islamic banks' 20% customers are Christians, Hindus and Sikhs.

Internationally, Islamic banking is one of the fastest-growing segments in financial services, holding assets of \$1.4 trillion. About 70 countries, including UK, USA, Japan, Singapore and France, have amended banking regulations to provide a level playing field for Islamic banking along with the conventional system.

## **9. Islamic Banking and Sustainable Development**

The elements of sustainable development as mentioned earlier have great emphasis in Islamic teachings. Interestingly, the growing content of sustainable development philosophy is moving away from neo-classical economy and reaching closer to Islamic economics paradigm by emphasizing on justice, equity and redistribution (Iqbal, 2005).

Yousri (n.d.) proposed a new definition for the concept of development from an Islamic paradigm, 'Development is a structural change in the socio-economic environment, taking place concurrently with adoption of Islamic laws and ethical values, and triggering off human productive capacities towards maximum and best possible utilization of available resources, within balance between material and spiritual targets.'

Yousri (2005: 25-26) clearly identified that the conventional definition of development has different meaning to the Islamic sphere as suggested by him. The development emphasised by conventional counterpart looks only into material benefits i.e. economic, social and environmental issues, albeit

Islamic enterprise is more comprehensive that does not only regards on material and social position yet it emphasise as well on moral and spiritual aspects (Hasan, 2006: 7; Kahf, 2002: 33). However, Hasan (2006: 8) enlightens that for the most part of definition described by the Commission is in harmony to the Islamic ambit which addresses the concept of development as a whole to every mankind and not only to Muslims. This is consistent with the axiom of tazkiyyah briefed earlier. Clearly, this could evident from the holy sources of Islam; the Quran and hadith specifically mention on the economics, social and environmental elements that promote sustainable development such as helping the poor and needy, enhancing social justice and environmental issues i.e. conserving the plants and protect the animals. Also, the holy sources prescribed the urge of utilizing the natural resource in a beneficial way and should never waste it.

### CSR and Islamic Banking

CSR from the western perspective has evolved since more than half a century ago, mean while CSR from an Islamic perspective has just started to make an appearance in the modern literature for not more than a decade although the features and traits discussed are already practiced since the era of our Prophet (pbuh).

Among others, Dusuki has produced a number of articles pertaining to CSR from Islamic perspectives. His article on 'What Islam Says about CSR' articulates on CSR theory in a more holistic respect distinguishing it from the Western view of CSR (Dusuki, 2008b). It encompasses the idea of achieving success and happiness not only in this world e.g. profit maximisation and business

sustainability, but also to achieve falah and happiness in the hereafter. Moreover, Dusuki (2008a) articulates that Islamic banks should upholds social objectives instead of seeking profit maximisation solely.

Taqwa-paradigm was introduced by Dusuki which act as the core element in implementing CSR from Islamic point of view. He further enhances the importance of this theory by identifying four main elements which are human dignity, free will, equality and rights, and, trust and responsibility.

However, most of the scholar of Islamic economics such as Ahmad (1980), Chapra (1979), Naqvi (1994), Siddiqi (1980) and Zarqa (1980) asserts the axiom of tawhid is paramount in understanding Islamic principles which is supported with other additional axioms that is of importance in this matter in the philosophical tenets. These supplementary elements are rububiyah (oneness of God), ukhuwwah (brotherhood), 'adl (justice) and tazkiyyah (purification and development) is of importance to create a society that accentuate the spiritual goodness embodied in Islam and contribute it to the development of a better system.

The principle of 'adl carries breadth meaning and scope that is very crucial axiom in the field of finance. As mentioned clearly in the Qur'an and hadith, it is instructed upon us to fulfil promises (contract), giving exact measure and weight of goods sold, pay wages to workers in a timely order and in fairness, avoid misrepresentation, never hoard goods, no price fixing, disclosure of cost price, defects and many more.

In addition, the concept of brotherhood that is established in the nation creates a sense of

belongings that motivates and guides our attribute of love, passion and justice among each other (Iqbal, 2005: 11; Yousri, 2005: 30). This attribute is important in creating a caring and responsible society.

The characteristic of CSR and sustainable development from Islamic perspective discussed above is inculcated in the Islamic economic system. This implies that it is also relevant for Islamic banking to practice it explicitly. However, to enhance the socioeconomic justice in the Holy Quran (17: 26 – 27): "And give the relative his right, and [also] the poor and the traveler, and do not spend wastefully. Indeed, the wasteful are brothers of the devils, and ever has Satan been to his Lord ungrateful."

### Effects of Islamic Banking on the Economy

- Better integration of the real and financial sectors of the economy
- Better business ethics –banks will only entertain economically viable financing requests
- Instead of being lenders, Islamic banks will provide financing by coming in as traders (murabaha), lessors (Ijara) or partners (mudaraba; musharaka)Islamic banks will stay away from financing prohibited activities e.g. producing alcohol etc
- There will be greater transparency in their transactions with clients –depositors as well as fund-seekers-due to compliance with the avoidance of gharar (ambiguity)resulting in clear contracts for every transaction
- Greater economic stability –it is well known in traditional finance literature that interest

based debt finance is an important source of economic instability when compared with equity finance

## Conclusion and Policy Implications

The recent global financial crisis has brought meaningful changes in the international financial panorama. Important normative reforms are at present in the pipeline to reinforce the international financial system to prevent the coming of another such crisis.

Islamic finance can contribute to the refounding of new bases for Western finance through instruments that bring back ethics into business and in the choice of investments and can enable a financial system in dire straits to get back the trust it has lost and build again its image of respectability.

A financial system organized and modeled on rules of ethical behaviour can represent the way to come out of the present economic crisis and to restore the savers' and the investors' trust, whose choices are decisive for the upturn in the real economy.

The global financial system needs a greater adaptation to shared ethical standards, to moral rules aiming at the achievement of the common good through a wise management of economy and markets must be led by the values and the responsibility of people. The ethical principles that represent the foundation of Islamic finance can be useful for this aim and they could create a new confidence between banks and clients, almost completely prejudiced at present, and lead the international banking system to play their role with a new spirit based on the stimulus

and support to economic growth. Public rescue operations, carried out in the latest months to face the current financial crisis, won't be enough to put global economy back on its feet if trust among economic operators isn't restored.

The present financial crisis has corrupted and partially destroyed the patrimony of relationships that virtually involved the world economy. The economic institutions need to refinance themselves with ethical motivations and with those religious inspirations that lead to responsible work and to an ethical behaviour, to disinterested solidarity without opportunisms, to hope in new opportunities for everybody, to reciprocal trust.

Islamic finance can give an important contribution to the ethical refoundation of global economy. It can help to restart economy and to promote the financing to the development of the poorest countries on Earth, in the decisive areas of tourism, of agriculture, of telecommunications and of infrastructures.

The unsuitability of the present market discipline, that has enabled many people to enter the financial market with the only aim to realize the highest profit, is one of the gaps in the present financial system that has been caused by the absence of precise rules on risk sharing and on the right behaviour to be adopted by the contracting parties. In this respect the Islamic banking, that has strong and simple rules aiming to prevent unfair speculations, that is based on values that imply reciprocal collaboration and support in the firm's activity and a great care choosing the most rational investments, can give its contribution to ensure a correct functioning of the international

financial system to the benefit of the world economy.

In the present economic context, still characterized by a situation of economic and financial crisis, Islamic finance has shown energy and the possession of margins of further growth in terms of profits and opportunities for investment. Thus, the crisis has also increased the interest in Islamic finance, seen as a form of financial brokerage that can promote financial stability and contribute to redraw the world economic system, helping it to regenerate, to become efficient and far-seeing.

Today Islamic finance has evolved up to become a vital and competitive element of the international financial system. Consequently to the global financial crisis, discussions turn more and more widely on the prospects of the potential and relevant role of Islamic finance to contribute to global financial stability and to support the global economic growth.

The growing internationalization of Islamic finance in recent years has been followed by new global models of economic and financial interconnections. This phenomenon can be observed in the reinforcement of the economic bonds of the latest years between Asia and Middle East in commerce and the investments in a wide range of sections.

The growth of Islamic finance in the latest years is due also to the greater role played by emergent economies in the worldwide financial and economic system, above all in Asia and in the Middle East, characterized by the application, to a various extent, of the principles in the Islamic Law. The two regions have a history of strong commercial and financial

bonds that flourished along the famous “silk route”, place of transit for centuries of goods and raw materials that the ancient eastern civilization exported to the West.

Today the Islamic finance has revitalized these economic bonds by reinforcing the financial bonds and, by favouring a greater integration of the new financial centres in Asia, it can set the basis for a revival of the prospects of growth and of social-economic development of these regions and start a new season of the “silk route”, with the inevitable positive effects to solve the present global economic crisis.

Islamic finance, taking advantage of the potential offered by globalization, has intensified its relationships not only with the Western world but also with the emergent countries. This policy has favoured the diversification of investments and has avoided the risk of concentration of the activities in few markets. The commitment of Islamic finance in reinforcing the links between the markets of the emergent countries, that have a relatively better growth prospect, with the Western financial systems has the opportunity to contribute not only to global financial stability but also to global growth prospects.

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# Bangladesh Perspective of Public Sector Accounting & Auditing: Status Review, Issues and Reforms

Ahmed Ataul Hakeem FCMA



## Introduction

The key purpose of prudent public sector financial management is to manage the public financial resources with economy, efficiency and effectiveness. The primary goal is to provide the citizens with targeted services and products for which the Parliament has allocated resources.

In this perspective the responsibility of the Office of the Comptroller and Auditor General of Bangladesh (OCAG) as the Supreme Audit Institution is to assure the Parliament and the people at large that they are receiving best possible value for the taxpayers' money.

The Office of the Comptroller and Auditor General of Bangladesh has been working since independence to make the government more transparent and accountable in utilizing public resources. The powers and mandate of the Comptroller and Auditor General (CAG) lies in the Constitution of the Peoples Republic of Bangladesh. The CAG is performing two sets of responsibilities to fulfill its constitutional mandate – that of the Comptroller and the independent Auditor. The OCAG also continuously tries to ensure good quality of its products and service by evolving its business process and capacity in light of the

international best practices. To do so the OCAG is adopting and adapting good practices, standards, guidance through cooperation from and collaboration with peer SAls, INTOSAI and professional bodies.

## Background of Public Sector

### Accounting and Auditing in Bangladesh

Public sector auditing and accounting system in Bangladesh was inherited as a legacy of the British colonial administration dating back to the 18th century. The Office of the Comptroller and Auditor General in India was established in 1936 under the provisions of the British India Act of 1935. The objective of establishing the Office was to ensure accountability and transparency of the Viceroy to the British Sovereign. The perspective of the Supreme Audit Institutions has changed over time and OCAG Bangladesh is now working to establish accountability, transparency of the Government to the citizens of this country.

The office of the Comptroller & Auditor General in Bangladesh commenced its activities from 1973 with the appointment of the first CAG. The mandate, authority and conditions of service of the CAG are

prescribed in the Constitution of the People's Republic of Bangladesh in Part VIII titled 'The Comptroller & Auditor General of Bangladesh'. Articles 127-132 of the Constitution lay down the basic legal framework for the Supreme Audit Institution of Bangladesh.

Although the provisions made in the Bangladesh Constitution provides for immense independence to the CAG for fulfilling his/her responsibilities independently, efficiently and effectively, due to the nature of the Rules of Business of the Government, CAG cannot utilize full financial and administrative independence at present.

Articles 127, 129 and 130 of the Constitution make provision for conditions of service of the C&AG in such a way that the Auditor General can remain independent of its prime auditee – the Government. Article 128 provides the authority and mandate to conduct audits, among which the most important provision is provided by clause (4) of Article 128, which states that the CAG shall not be "controlled and influenced by any authority" when performing his/her audit functions. As per constitutional provisions [Article 128(2)], the OCAG auditors are also allowed full, unrestricted access to all records and documents of any government department or government-owned entities. Article 131 gives the authority to the CAG to prescribe the manner and forms of government accounts with the approval of the Hon'ble President. And Article 132 states that the audit reports will be submitted to the President, who shall place these reports before the Parliament.

The mandate and responsibilities provided by the Constitution ensure that the CAG has to play a key role in both the public sector accounting and auditing arena.

## Public Sector Accounting in Bangladesh

### Maintaining Government Accounts:

The Comptroller & Auditor General's (Additional Functions) Act, 1974 and Comptroller & Auditor General's (Additional Functions) (Amendment) Act, 1975 provide CAG with the responsibility of keeping accounts of the Government. The Act was promulgated under clause (3) of Article 128 of the Constitution, which states that the Parliament may require the CAG to exercise such functions, in addition to auditing responsibility given under clause (1) of Article 128, as such the law may prescribe.

As part of the responsibility of Comptrollership and the authority provided under the Additional Functions Act 1974 and amendment Act 1975, the CAG is empowered to authorize payments from the treasury and incorporate all valid transactions into the Accounts of the Republic (Government Accounts) after conducting pre auditing functions. The Civil, Defence and Railway Accounts Departments under the CAG consolidate the Accounts of the Republic, after these are reconciled with the executives who maintain their own accounts following the General Financial Rules (GFR).

The Accounts of the Republic consists of the Appropriation Accounts and the Financial Accounts. Appropriation Accounts show the expenditure status of a particular Ministry/Division vis a vis budgetary grants. Historically four Appropriation Accounts such as Appropriation Accounts (Civil), Appropriation Accounts (Defence), Appropriation Accounts (PT&T) and Appropriation Accounts (Bangladesh Railway) are compiled by the three accounting circles under the CAG, i.e. Controller General of Accounts (CGA), Controller General Defence Finance (CGDF), Chief Accounts Officer (T&T) and Additional Director

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At present the Cash Basis Treasury Single Account (TSA) system is practiced in Bangladesh. Under TSA government funds are managed by a central entity and individual departments and entities do not control the 'cash' they have been appropriated or otherwise authorized to spend. This system serves the versatile needs of public sector entities in Bangladesh and complies with requirements of the Cash Basis IPSAS by ensuring proper presentation of general purpose financial statements/government accounts, transparent financial reporting and enhanced comparability of financial statements /government accounts etc.

General (Railway Finance), respectively.

The Finance Accounts is the balance sheet of the Government, maintained under the cash basis system of accounts and incorporates cash and other balances of the Government. The Finance Accounts is compiled by CGA through consolidating the balances of the three accounting circles under OCAG.

**Government Accounting Standards:**

On the other hand, Article 131 of the Constitution empowers CAG to prescribe forms and manners of government accounts or to formulate government accounting standards. The Account Code issued by the Comptroller and Auditor General describes the forms and the manner in which the Republics' Accounts are maintained compiled and disclosed.

The concept of Consolidated Fund, Treasury Single Account and the limit of financial authority

provided by the Parliament through Annual Budget are the features of present Cash Basis government accounting system. This time-tested and comprehensive Cash Basis Accounting System has been efficiently and effectively used by the public sector.

It should be noted that the financial statements prepared using Cash Basis Accounting principles provide readers with information about the sources of cash raised during the period, the purpose for which cash was used and the cash balance at the reporting date. This is standardized by the International Public Sector Accounting Standards Board (IPSASB) through a comprehensive Cash Basis IPSAS. The standard also acknowledges the right of governments and National Standard Setters to establish accounting standards and guidelines for financial reporting within their Jurisdictions and suggests that IPSASs may assist such standard- setters in developing new standards or revision of existing standards in order to contribute to greater comparability.

In the last three decades different reform initiatives have been introduced in the public sector accounting practices. Accounts have been decentralized up to upazilla levels, 13 digit economic codes have been introduced in place of the old alpha numeric codes, accounts compilation process in the CGA has been computerized and keeping in line with these changes the Account Code has been updated. At present reform initiatives are going on in railway accounting practices.

**Accounts of the Republic: Ensuring Accountability & Transparency**

It should be noted that the main purpose of public sector accounting is to serve the requirements of the Parliament. The authority to spend money is granted by Parliament through passing of Appropriation Bill. When budget is approved and passed by Parliament responsibility for the control and use of public monies lies with the Principal Accounting Officer (PAO) or Secretary to the Ministry or Division. The Principal Accounting

Officer is responsible for the safeguarding of public funds following the standards of financial propriety and for maintaining regularity of expenditure from the public funds. He is accountable not only for the expenditure against the budget but also for the propriety of each individual transaction.

Accounting records and financial information help keep the Government abreast of the trend of receipts and expenditure vis a vis budget estimates. Therefore, as part of the public sector accountability regime the CAG submits audited Annual Appropriation Accounts and Finance Accounts to the Parliament, with specific opinion on the reliability, accuracy, completeness and timeliness of the accounts. The Audit opinion is designed to assist the Parliament and especially the Public Accounts Committee to examine to what extent the PAOs have been able to achieve the targets set by the Parliament through the Annual Budget.

## Public Sector Auditing in Bangladesh

### Mandate and Organization of OCAG

All public receipts and expenditure of the government departments, local government institutes and parastatal bodies are under the audit jurisdiction of the OCAG, with the mandate to submit the audit reports thereof to the Parliament through the Hon'ble President. The OCAG performs oversight functions of the financial operations of the State. The office provides unbiased, objective assessment of whether public resources are responsibly and effectively managed within the approved budget to achieve intended results in an effective,

efficient and economical manner.

This assessment of Government activities is conducted by OCAG primarily through financial audits, compliance audits and performance audits. The Office has also conducted audits in specialized areas that have become pertinent not only in Bangladesh, but all over the world as well. OCAG has already conducted Environmental audit, Social Audit, IT Audit and Public Debt Management Audit on a pilot basis and still more new issues and areas are being evaluated for future audit engagements.

All audits are conducted by the OCAG through ten Audit Directorates, which are responsible for examining different functional areas of the Government. These are:

1. Commercial Audit Directorate audits all public sector entities and state owned enterprises and public holding companies.
2. Local and Revenue Audit Directorate audits all civil government departments, local and statutory bodies and the National Board of Revenue.
3. Civil Audit Directorate audits the Office of the Controller General of Accounts (CGA) and all Upazila, District, Divisional and Chief Accounts Offices under CGA.
4. Works Audit Directorate audits all public works expenditures of the government, local government and autonomous bodies.
5. Foreign Aided Project Audit Directorate audits all development and technical assistance programmes and projects in the public sector funded by foreign aid.
6. Railway Audit Directorate audits all establishments of Bangladesh Railway.

7. Post, Telegraph and Telephone Audit Directorate audits all establishments of Postal Department, Bangladesh Telegraph and Telephone Board, Bangladesh Telecommunication Regulatory Commission (BTRC).
8. Defence Audit Directorate audits all units/formations of the defence forces including army, air force and navy and the Office of the Controller General Defence Finance (CGDF) and all related field services offices of the Defence Finance Department under CGDF.
9. Mission Audit Directorate audits all overseas missions, nationalized banks, shipping corporation offices and Biman Bangladesh Airlines offices operating abroad.
10. Performance Audit Directorate is responsible for conducting performance audits of selected issues or bodies.

### Ensuring Quality Products and Services

The OCAG relentlessly strives for high quality in all its services and products. To ensure effective audit performance a two-tier Quality Control system has been established in all the Audit Directorates. The Deputy CAG [Accounts & Reports] also conducts quality control functions of all audit reports finalized by the Audit Directorates. Guidelines and procedures for conducting quality controls have also been prepared and communicated by OCAG.

Besides, the OCAG has also made additional provisions for independent Quality Assurance functions. The Central Quality Assurance Committee [CQAC] headed by the Deputy CAG [Senior] examines all audit reports placed before the C&AG for



approval by the Deputy CAG [Accounts & Reports].

An additional quality assurance step has been introduced by OCAg for performance audit engagements. The Performance Audit Directorate has the responsibility to quality assure each performance audit plan and report that are prepared by different functional Audit Directorates, before sending them to OCAg for final approval.

As OCAg strives to ensure good governance, accountability and transparency across the government, it also takes into account the importance of transparent, accountable and effective functioning of its own organization. As a result OCAg has introduced peer review within the organization. Also an Annual Report is published by OCAg every year describing the achievements made and the challenges faced by the organization. The Annual Report is widely circulated with the objective that SAI Bangladesh's achievements can be clearly

assessed by all its stakeholders.

### Capacity Building in OCAg Bangladesh

In order to fulfill the mandate given to OCAg by the Constitution of the Peoples Republic of Bangladesh and to effectively satisfy the expectations of the stakeholders with highest quality reports and services, various capacity building measures have been taken by OCAg. Following are ongoing capacity building initiatives of OCAg:

- Attempts have been made to further operationalise and update the mandate of the OCAg through formulation of an 'Audit Act' that provides a better statutory framework in accord with INTOSAI auditing standards.
- In line with the International Standards for Supreme Audit Institutions (ISSAIs), measures are being taken to address matters relating to collaboration with professional accounting institutes including partnerships

and secondments to address various common issues related to public financial accountability and good governance.

- Adoption of international standards for auditing and accounting provides the basis for competent financial reporting and transparency. Accordingly, the OCAg is in the process of adopting ISSAIs formulated by INTOSAI in collaboration with IFAC. A core group of promising officers have been chosen as change managers in financial audit and they are conducting pilot audits following INTOSAI standards under the supervision of expert public sector auditors as part of their training. They will act as trainers for the next generation of financial auditors.

- The diversified nature of the public sector entails that the OCAg also attains capacity to conduct different types of audit other than financial audit. Keeping this in mind the CAG has created an IT Audit Core Group and a Performance Audit Core Group. The members of the core group are being given both theoretical and on the job trainings by on-going CIDA funded SCOPE project. These auditors will act as trainers in the future and help sustain the best practices in OCAg.

- OCAg is also working in collaboration with the International Organization for Supreme Audit Institutions [INTOSAI] and the Asian Organization for Supreme Audit Institutions [ASOSAI] in capacity building programmes. Some of areas covered in these capacity development initiatives include

Environmental Audit, Social Audit, Fraud Audit, Public Debt Management Audit, Quality Assurance in Performance & Financial Audits, IT Audit, Strategic Development for SAls, Training for Trainers.

- We are in the process of computerizing the audit business process, from planning to follow-up of audit and PAC recommendations. The planned Audit Management and Monitoring System [AMMS] will ensure better management and supervision of audit work and electronic working papers will enable auditors to maintain a minimum level of quality in their work. We are also confident that AMMS would help us to substantially reduce the total time needed for audit overtime.
- OCAG is also taking initiatives to improve its relationship with the stakeholders. A Media and Communication Cell has been established. Workshops and seminars have also been conducted to exchange views with different level of stakeholders and to train OCAG staff in communication and public relations. OCAG also plans to conduct press briefing once audit reports are submitted in the Parliament. As CAG's main stakeholder are the people, so it aims to take its products to the actual stakeholders.

At present two projects implemented in OCAG are working towards assisting the Office in its capacity building initiatives. The Strengthening Comptrollership and Oversight of Public Expenditure [SCOPE] Project is being implemented with the assistance from CIDA since

March 2008. SCOPE project is working in the following areas:

- Enhancing capacity for conducting Performance Audits
- Enhancing capacity for Financial and Compliance Audits following ISSAIs
- Enhancing capacity for IT Audit and use of IT
- Strengthening Information System infrastructure in OCAG, including development of Audit Management and Monitoring System [AMMS]

Another new project, Strengthening Public Expenditure Management Programme [SPEMP-B] is in the process of being initiated with the assistance from a consortium of Development Partners, with World Bank in lead. The areas of OCAG capacity building that the SPEMP-B will work on are as follows:

- Component 1: Strengthening Institutional Arrangements of OCAG
- Component 2: Enhancement of Quality Audit and Expansion of Audit Scope
- Component 3: Strengthening the Financial Management Academy [FIMA]

## Conclusion

Public Sector accounting and auditing functions are the pillars for the accountability and transparency of the Government to ensure good governance. The Office of the Comptroller & Auditor General of Bangladesh plays a vital role in ensuring efficient and effective accounting and auditing functions in the public sector.

The major function of accounting information is viewed as that of aiding the process of organizational control. The accounting records are the most reliable and dependable source of information for the top management in their decision making process. Financial information of the Government is used not only by the public sector entities, but also by different national and international organizations and agencies for various purposes. Therefore, it is essential that accounting and financial information of the government represents accurate and reliable position of the Ministries and Departments regarding all sorts of transactions in a timely manner. Through the accounts compilation functions and audit activities, OCAG can enhance the reliability of the government financial management system and cater to the need for reliable and dependable information of the stakeholders.

Therefore, to improve the quality of its outputs and services, the OCAG has undertaken several technical assistance projects for the enhancement of its functions and professional capacity building of its staff over the years.

The Office of the Comptroller & Auditor General of Bangladesh is also in the process of examining the areas for collaboration with the Institute of Chartered Accountants of Bangladesh (ICAB). The issue of secondments of members of OCAG and ICAB between the institutions can help in learning from and understanding of each other's intricacies in accounting and auditing practices and thus creating synergy within the auditors' fraternity of Bangladesh. OCAG is also discussing with ICAB for their cooperation for professional certification of newly



recruited BCS officers of SAI Bangladesh. OCAG expects some exemption for field articleship, taking into consideration the experiences of its staff. It should be noted that other Supreme Audit Institutions, such as National Audit Office (NAO) UK, has established similar collaboration arrangements with private sector accounting institutions. Recently a Team has been formed with members from both OCAG and ICAB to identify areas of cooperation and to finalize this in a Memorandum of Understanding (MOU).

Sustainability of these initiatives will help OCAG in satisfying its mandate by improving quality of accounting and auditing functions in the Public Sector.

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# Shadow Banking System - and its Crucial Role in the Economic UPS and Downs

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## Abstract

The term "Shadow Banking System (SBS)" has been attributed to remarks in 2007 by Paul McCulley (an American economist who used this term and that became famous during the financial crisis of 2007-2009) to describe a large segment of financial intermediation that is routed outside the balance sheets of regulated commercial banks and other depository institutions. SBS refers to the financial intermediaries involved in facilitating the creation of credit across the global financial system but whose members are not subject to regulatory oversight. The SBS is made up of financial entities which have the same functions as traditional banks but which are subject to little regulations. Like traditional banks shadow banks provide credit and liquidity but, unlike their traditional counterparts, they do not have access to central bank funding or safety nets like deposit insurance. According to McCulley, the global SBS includes all agents involved in leveraged loans which do not have access to deposit insurances and/or to rediscount operations of central banks. These agents are not subject to the prudential regulations of the Basel Agreements as well.

## Who are the SBS entities?

The SBS entities that make up the system is made up of non-depository banks as well as other financial entities which included money market funds, hedge funds, private equity funds, securitization, securities lenders, mediators, structured investment vehicles, pension funds and insurance companies. Broadly, it also includes investment banks and mortgage brokers. Two examples of well-known big shadow banking institutions in the USA are Bear Stearns and Lehman Brothers.

## How they work?

As mentioned, the SBS entities do not take deposits like traditional banks. Instead, they rely on short-term funding provided either by asset-backed commercial paper (ABCP) or by the repo market (sale on repurchase agreement), in which borrowers offer collateral as security against a cash loan and then sell the security to a lender and agree to repurchase it at an agreed time in the future for an agreed price. The SBS is built up alongside the traditional banking system, using some of the tools of modern finance like interest rate swaps and credit default swaps with the idea to make credit cheaper for the borrower and easily available as there are a lot of regulations

in/on the traditional banking system to protect the payment system. The SBS in some way encouraged by regulators with the intension to get some of the risks (interest rate risks, credit risk, etc) off the balance sheet of the traditional banking system. The traditional banks have become an originator of loans which they package, securitize and then sell to the SBS, which then raise funds in the money market from mutual funds and ABCP that they issue to whoever. It is just avoiding the traditional banking system entirely in this regard, and also avoiding all the regulations of the traditional banking system as well as all the regulatory supports of the traditional banking system. Shadow banks are often based in tax havens; invest in long-term loans like mortgages, providing credit across the financial system by matching investors and borrowers individually or by becoming part of a chain involving numerous entities, some of which may be traditional banks.

The role of SBS in world economy  
The SBS is an important sector of a financial system, facilitating capital formation and economic growth. Generally, the entities of the SBS have raised short-term financial instruments to finance long-term, illiquid and risky assets through multiple steps of credit intermediation. Disruptions in the credit markets have made them subject to rapid de-leveraging, selling their long-term assets at depressed prices. SBS is also important for the economy because it provides funds to traditional banks and the traditional banks lend those funds to borrowers and continue to growth of the wider economy. The SBS also offers credit and provides liquidity to borrowers in addition to that provided by the traditional banking system. Some specialized shadow bankers can often provide credit more cost-efficiently than traditional banks. Shadow banking institutions like hedge funds often take on risks that mainstream

banks are either unwilling or not allowed to take.

According to the Financial Stability Board [(FSB), a regulatory task force for the world's group of top 20 economies (G20) whose secretariat is in Basel, Switzerland] the SBS makes up 25-30% of the total global financial system and this sector was worth about USD 60 trillion in 2010 (roughly half of the amount of global banking industry), having grown from an estimated USD 27 trillion in 2002. Although the sector's assets declined during the global financial crisis, they have already returned to their pre-crisis peak.

Below graph shows how the liabilities of SBS and Traditional Banks in the USA had grown-up from 1950 to 2010.

### **SBS in the world economic crisis**

While the financial crisis originated in 2007 in the USA as a disaster, it evolved into a banking sovereign debt, and ultimately political crisis of global scale. That economic crisis can (at least partially) be linked to the vulnerability of the shadow banking industry. As mentioned at the beginning of this article, the term "shadow banking system" started to be used widely at the onset of the 2007-2009 economic crisis. The emergence of the term reflected recognition of the increased importance of entities and activities structured outside the regular banking system that perform bank-like functions.

During the financial crisis, liquidity support from the government enabled banks to avoid selling their holdings of certain assets at the bottom of the market. But that support wasn't available to the SBS. Although most areas of shadow banking appear to be on the mend, the segments most closely linked to mortgage lending,

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such as residential mortgage-backed securities (MBSs), remain depressed. It is not clear how the SBS will end up participating in the housing market until the future of the government-sponsored enterprises is clear and new bank mortgage-lending guidelines are in place.

Banks sought different means for moving credit risks off their balance-sheets, aiming at increasing the volume of operations without the need to put aside the capital coefficients required by the Basel Agreements. They did this in various ways, for example: by acquiring protection against credit risks on the derivatives markets; by issuing credit securities whose return is dependent on the amortization paid by borrowers; and by creating various Special Investment Vehicles (SIVs). However, they were only able to do it because other agents were willing to take as the counterparty of such operations, namely to take risks for a return which seemed very high at the time. These agents were part of the global SBS that is a set of institutions which operated as banks without being banks, raising resources in the short term, operating with very high leverage and investing in long-term illiquid assets. Unlike banks, however, these institutions were loosely regulated and supervised, they did not have reserves of capital, they had no access to deposit insurance, to the rediscount operations or to the last resort credit lines of central banks. As a result, they were highly vulnerable both to an investors' run (withdrawal of resources or mistrust of short-term markets) and to asset imbalance (devaluation of assets as compared to liabilities).

As mentioned above, the economic crisis can be linked to



the obvious result of the vulnerability of the SBS. In traditional banking, the vulnerability originates in a run by the bank's depositors. In securitized banking, the run comes from the deposit end (the providers of wholesale funding to the shadow banks). The two markets in which such runs are most likely are the repo market and the commercial paper market. The evidence on runs in the markets for wholesale funding demonstrated the parallel between traditional bank runs by depositors in the banking panics prior to crisis and the recent panic in credit markets that relied on wholesale funding. As wholesale funding dried up for troubled shadow banks, they were forced to sell off assets in order to meet liquidity demands of investors. Such a fire sale of assets lowered the prices of assets on similar collateral throughout the market, raising the cost of funding for healthy shadow banks harshly.

This trend was first pointed out for the repo market in a series of papers that are summarized in work by Gary Gorton (an

American economist who was a central figure in the study of the global financial crisis of 2007–2009). In the interdealer repo market, a run occurred primarily through increased haircuts on the securities posted as collateral. In the case of some securities, especially those backed by troubled mortgage loans, the haircuts were close to 100 percent which was implying that these assets were no longer eligible for repo transactions. An increase in the haircuts on the repo implies an increased demand for collateral on the same loan or, conversely, a reduction in the supply of funds for a given amount of collateral. Since the supply of collateral in the entire SBS was fixed over the short run, this meant that there was a significant liquidity crunch (shortfall in the supply of funds) and a steep rise in the cost of funding through repo transactions.

In the case of funding through money market mutual funds (MMMFs), the panic was witnessed in two major shocks to the commercial paper market in 2007–2008. The first shock came

around July-August 2007 with the collapse of certain financial entities that had invested heavily in subprime mortgages. This led investors to question the quality of even highly rated ABCP. As a result, the spread of ABCP over the federal funds rate increased from 10 percent (before the shock) to 150 percent (after the shock). The second and more severe shock occurred with the collapse of Lehman Brothers in September 2008. This led to a direct default on commercial paper issued by Lehman Brothers, \$785 million of which was held by the Reserve Primary Fund (one of the largest MMMFs), with more than \$65 billion in assets. Needless to say, the news of exposure triggered a run on this fund and quickly spread to other MMMFs. To cope up with the run on MMMFs, the U.S. Treasury announced a temporary deposit insurance covering all money market instruments only three days after the collapse of Lehman.

## G20 Summit in Paris and its resolution

In the summit on 9th October 2011 of G20 in Paris the SBS was critically reviewed and agreed by all participants upon some aspects. The summit was encompassed with some Principles and Recommendations to support the system, those are:

### Principles:

- The SBS is an important part of the global economy as long as the benefits are derived from specialization and competitive advantage (and not from regulatory arbitrage);
- The financial system can only be effective if there is clarity as to where risk in the system resides;
- Once clarity has been

achieved, it should be determined whether the capital that ultimately supports credit creation is appropriately sourced;

- Following on from the above, there is no need for regulation as long as the underwriters and participants in those markets are the only bearers of that risk (no backstop by the tax payer); and
- Regulation should be required only in instances where the risk and ultimate liability may be transferred to the tax payer.

### Recommendations:

- Implement a policy of non-governmental bailouts for activities outside the regulated area. This means that underwriters have to understand that they bear the full risk and must therefore identify and communicate those risks in the various unregulated financial markets;
- Base regulatory activities in the area where the tax payer is at risk on functions rather than institutions;
- Accelerate and implement reforms, in particular related to money market funds. Specifically, clarify that the risk resides with investors, consider a substantive change regarding the concept of 'net asset value (NAV)', and the introduction of a liquidity redemption fee designed to remove the incentive to be the first out of the fund; and
- Establish a voluntary compliance framework that would facilitate transparency and foster the system in regards to the unregulated SBS.

## Regulations exist and underway for SBS

In 2010 an Act was passed in the

USA called "the Dodd-Frank Act", and made provisions to regulating the SBS. As per that Act the Federal Reserve would have the power to regulate all institutions of systemic importance, for example. Other provisions include registration requirements for hedge funds which have assets totaling more than USD150 million and a requirement for the bulk of over-the-counter derivatives trades to go through exchanges and clearing houses.

According to, Mark Carney (Chairman of the FSB): "The global watchdog might introduce direct regulation of the shadow banking system to tackle the risks moving into this unregulated sector from the heavily supervised mainstream banking sector". He also said in November 2011, "Regulating the shadow banking industry would be a top priority for the board in the coming months". The recommendations for G20 leaders on regulating shadow banks are due to be finalized by the end of 2012. USA and the European Union are already approving rules to increase regulation of areas like securitization and money market funds.

German Chancellor Angela Merkel proposed to indirectly regulate the SBS prior to imposing direct regulation on institutions such as hedge funds and money-market funds that have traditionally been outside the scope of financial supervision. She recently said in a news conference, "In a first step to generate more transparency, the proposal for indirect regulation certainly makes sense and as a next step, direct regulation must come". Her comments have come after Otmar Issing (the former chief economist of the European Central Bank who is the chairman of a working group on financial market architecture) presented a report to

the government. In that report, he lobbied for indirect regulation of the shadow banking sector as a preliminary step because there is currently no chance for reaching an international agreement for a direct regulation. He said, "With indirect regulation, banks would have to make public their business activities with hedge funds, helping to identify risks that such transactions have. This indirect regulation is nothing but a huge step forward amid the risks that exist in the banking sector due to their connections with the shadow banking system. This is a basis from where we can take the next step".

Banks across Europe could be forced to hold lower levels of capital under fresh European Union (EU) law in the coming months. If the draft paper from the EU becomes legislation, the shadow banking could play a vital role in the region's economic recovery as it continues to struggle with the impact of its debt crisis.

### Demerits and Risks of SBS

Since shadow banks do not take deposits, they are subject to less regulation than traditional banks. They can therefore increase the rewards they get from investments by leveraging up much more than traditional banks and this can lead to risks mounting in the financial system. Unregulated shadow institutions can be used to evade the strictly regulated mainstream banking system and therefore avoid rules designed to prevent financial crises.

Intermediating credit through non-bank channels can have advantages, for example by providing an alternative source of funding and liquidity. However, as the recent financial crisis has shown, the SBS can also be a

source of systemic risk both directly and through its interconnected relation with the regular banking system. It can also create opportunities for arbitrage that might undermine stricter bank regulation and lead to a build-up of additional leverage and risks in the overall financial system.

### Regulatory problems and possible solutions for SBS

#### Problems:

- Many attribute the expansion of the current crisis from the U.S. housing market to the global financial system to the actions, insufficient regulation, and eventual collapse of the SBS.
- By using shadow banking mechanisms, such as structured investment vehicles (SIVs), collateralized debt obligations (CDOs), and credit default swaps (CDSs) to purchase, finance, and insure MBSs, many investment banks and other financial institutions were able to make these high-risk transactions off of their balance sheets and free from most regulations, which typically applied only to on-balance sheet transactions.
- By using special entities that made up the SBS, financial institutions were able to make higher risk transactions and investments, not only because these high-risk transactions were hidden from normal accounting exposure and regulation, but also because these entities were not subject to the same risk-reducing minimum reserve requirements as were the commercial banks and other institutions, which in most cases were the parent institutions of the shadow banking entities in question.

#### Possible Solution:

- Many in the financial community have called for the implementation, both at national and international levels, of minimum reserve requirements for all institutions and entities involved in the purchase of MBSs, the production of commercial paper, etc.
- Such requirements would reduce the level of risk involved with purchase and trading of high-risk securities, like MBSs.
- Economists and regulators have also suggested the following changes to regulation of shadow banking activities:
  1. more aggressive oversight and regulation of the risk management activities of all institutions and entities, both on- and off-balance sheet;
  2. elimination of over-the-counter trading of CDSs and development of a monitored international clearing house to facilitate such trades; and
  3. increased national and international disclosure requirements for financial institutions.

### Stance of IASB and FASB on SBS

London based International Accounting Standards Board (IASB) and USA based Financial Accounting Standards Board (FASB) both are responsible for setting accounting standards. Both have issued several Standards called IAS/IFRS and US GAAP respectively and those are mandated, adopted and followed by the Capital market, Financial Statement preparers, auditors,

investors and users alike across the globe. These two private and independent organizations are also monitoring, involving and advising for the SBS.

In early 2008, the USA SEC and the President's Working Group on Financial Markets asked FASB to act quickly to review and reform the rules governing the accounting for securitizations and special-purpose entities (SPEs). The goal was to improve the accounting and overall transparency by eliminating abuses, thereby creating a system of "sound securitization," and also help restore confidence in the reporting of our financial institutions.

In November 2010 Seoul Summit, following the completion of the new capital standards for banks (Basel III), the G20 leaders warned of a potential that regulatory gaps may emerge in the SBS. They therefore requested that the FSB in collaboration with other international standard setting bodies to develop recommendations to strengthen the oversight and regulation of the SBS.

## **Crux**

From all above discussions it can be concluded that, a run on its funds is as much a real risk for a shadow bank as it is for a normal bank and could have devastating consequences for the global financial system because the two sectors are so closely linked. Therefore, the SBS and the traditional banking can be viewed as a parallel system and complement to each other, not the substitute. The challenges going forward are to tie together the benefits and mitigate the risks and redundancies of such a parallel banking system.

One of the reasons for the current worldwide economic crisis is a lack of transparency in the global financial system. This is the end product of a half century of creating and expanding a shadow financial structure comprising tax havens, secrecy jurisdictions, disguised corporations, anonymous trust accounts, and fake foundations. Also included in this system, are trade mispricing mechanisms, money laundering techniques, and gaps left in western laws that facilitate the movement of corrupt, criminal, and commercially tax-evading money across borders. Some estimates suggest that as much as half of global trade and capital movements pass through this SBS.

The consequences of this cloudy structure and the money it moves are now clear:

- In developed countries: credit has dried up in large part due to the difficulty of appraising the quality of assets held by financial institutions that operate partially or wholly within this solid system that includes almost all major U.S. and European banks, and
- In developing countries: an estimated \$1 trillion a year of illegally generated money is shifted abroad through this system, constituting the most damaging economic condition hurting the poor, undermining poverty alleviation and delaying sustainable growth.

The Task Force on Financial Integrity and Economic Development urges the G-20 to focus on substantially improving transparency in the global financial system. Thus far in discussions and commentaries, greater emphasis has been given to strengthening regulation within the existing

structure. While some regulatory improvements are certainly needed, it seems, this emphasis is misguided. Far greater benefit can arise by significantly curtailing the SBS that is clearly at the root of the economic crisis all the countries are facing.

While some analysts have asserted that the SBS is redundant and inefficient, it is not difficult to see the benefits of securitized banking. Securitization allows for risk diversification across borrowers, products and geographic location. In addition, it exploits benefits of both scale and scope in segmenting the different activities of credit intermediation, thereby reducing costs. Moreover, by providing a variety of securities with varying risk and maturity, it provides financial institutions opportunities to better manage their portfolios than would be possible under traditional banking.

Finally, and contrary to popular belief, this form of banking increases transparency and disclosure because banks now sell assets that would otherwise be hosted on their balance sheets. Enhancing supervision and regulation of the SBS in areas where systemic risk and regulatory arbitrage concerns are inadequately addressed is therefore important.

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***The Author is Financial Controller  
Sothorn Region, The Coca Cola Bottling  
Company of Saudi Arabia***

# Reforms in Public Sector Accounting : Pakistan Perspective

Masud Muzaffar



## Background of Public Sector Accounting System in Pakistan

Pakistan inherited an accounting system devised by the British. This system had been basically designed to suit the colonial interests of a foreign power. Time and events made this system obsolete, primarily because the system was manually based and was not geared to produce timely reports, and further since economic development of the country and welfare of the masses had assumed greater significance for the government, thereby enlarging the scope of operations of the public sector, traditional system had become inadequate to produce comprehensive & meaningful financial reports.

## Basic Shortcomings of the old system

- Manually based: It was a manual based system therefore was unable to produce comprehensive reports in a reasonable time.
- Lack of conformity with international Generally Accepted Accounting Principles.
- Lack of information between budgetary and accounting data for financial reporting.

- Failure to provide financial analysis in the reports and resultant lack of meaningful information.
- Non-comprehensive Chart of Accounts.

## Important and basic principles of Government Accounting (legacy system) were:-

- Period of Account: Transactions were recorded which took place during a financial year (from 1st July of a calendar year to 30th June of the next calendar year).
- Cash basis of accounts: with some exceptions of book adjustments the transactions in the government accounts represented the actual cash receipts and disbursements during a particular financial year as distinguished from amounts due to or by the government during the same period.
- Main divisions of accounts: The main divisions of accounts were revenue, capital, debt and remittance.
- Classification of Accounts: Major, minor & detailed heads of accounts were used while recording government transactions.
- Refund of Revenues: Refund of revenues as a general rule was taken as a reduction of revenue receipts



under the major head concerned.

- Capitalization of expenditure: The system was not based on purely professional lines to enable capitalization of expenditure.
- Balance to Balance

In conformity with the overall reforms process, and this being a continuous task, initiated by the Government of Pakistan like economic reforms, corporate governance reforms and judicial reforms - financial reforms were also initiated. As a part of financial reforms a Project to Improve Financial Reporting & Auditing (PIFRA) was introduced, with the financial & technical support of the World Bank. As a warm up to the formal launch of the project in 1996, a diagnostic study to assess the then prevalent system was conducted from 1993-96, again with the support of World Bank. First phase of this project was completed on 31st December, 2005. From 1st January 2006 second phase (PIFRA-II) started, which was completed on 30th June, 2011. Thereafter a two year process of consolidation of the reforms started.

### **Components of the Reforms Project**

**Components of the reforms process are as follows:-**

- Government Accounting & Financial Reporting
- Change management & human resources
- Auditing
- Training
- Administration
- Other policy support

### **Objectives of the Reforms Project**

**Objectives of the reforms project were as follows:-**

- Adoption and implementation of best business practices
- Modernization of Government Audit Procedures
- Adoption of Internationally Accepted Accounting and Auditing Standards
- Improvement of Financial Accounting and Information systems.
- Tighter Internal Controls.
- Building staff capabilities.

**Main Goals:**

- To modernize Cash Based Accounting System

“ AS A CONTINUATION OF THE REFORMS PROCESS, PAKISTAN HAS THROUGH A PHASED PROGRAM STARTED THE ADOPTION OF IPSAS. AS FIRST STEP, SINCE FINANCIAL YEAR 2006-2007 THE FINANCIAL STATEMENTS OF ALL ACCOUNTANTS GENERAL (NATIONAL AS WELL AS SUB-NATIONAL) ARE BEING PREPARED UNDER CASH BASIS IPSAS. CURRENTLY THE FINANCIAL STATEMENTS BLEND THE REPORTING FORMATS UNDER NAM AND IPSAS CASH BASIS BY REPORTING CASH FLOWS STATEMENT(IPSAS-2) OVER AND ABOVE THE REQUIREMENTS OF CASH BASIS IPSAS, AND FOCUS ON BUDGETARY COMPLIANCE FOR THE FINANCIAL YEAR AS PER PROCEDURE LAID DOWN IN THE CONSTITUTION.”

- To bring transparency and Public Accountability in Financial Reporting
- To improve budgetary controls
- To provide timely and accurate information to the stakeholders

## Separation of Accounting and Auditing Functions

Before discussing in slight details the features of the new accounting system, it would be pertinent here to mention a significant landmark achieved in the process of financial reporting and auditing reforms; this had been the separation of Accounting & Auditing functions.

Prior to the year 2001 the Auditing and Accounting functions were combined in the office of the Auditor General of Pakistan. This caused a conflict of interest situation and was against the International Best Practices. Though partial separation was achieved at working level in the year 1988, yet concentration of functions at the top level did not effectively achieve the basic purpose of separation. In the year 2001, through two separate legislations known as Auditor General's (Functions, Powers and Terms and Conditions of Service) Ordinance, 2001 and Controller General of Accounts (Appointment, Functions and Powers) Ordinance, 2001, Auditor General of Pakistan was relieved from the responsibility of maintenance of Accounts, though under the Constitution of Islamic Republic of Pakistan he continues to retain the prerogative of prescribing, with the approval of the President of Pakistan, the Forms, Principles and Methods according to which the Accounts of the Federation and Provinces are to be kept.

Separate office of Controller

General of Accounts was created for the maintenance of Accounts of Federation, all the Provinces & Districts. Auditor General in turn certifies these accounts & along-with his reports submits them to the President and respective Governors for causing them to be laid before the respective Legislature. Though some progress is still required to be achieved for the administrative independence of the Controller General of Accounts, yet functional separation of Accounts & Audit and introduction of system of certification of Accounts is a significant movement towards achievement of International Best Practices.

## Basic Features of the reformed Accounting System

The reforms process has introduced the New Accounting Model (NAM). NAM has been developed with the help of international consultants and involvement of all stakeholders and is consistent with international standards. NAM is codified in seven volumes of manuals and has replaced the old codes – some of which dated back to Victorian period. Its implementation involves a comprehensive process re-engineering while making the accounting consistent with international best practice and includes a powerful classification scheme geared to modern financial management needs. Country wide adoption of NAM will ensure common standards and uniformity of accounting information. A fully computerized Accounting network has been established in the office of CGA, AGPR, Provincial AGs, Federal and Provincial Finance Departments & most of the District Accounts Offices (DAOs), while remaining DAOs are in the process

of being covered by the system.

NAM caters for Modified Cash Accounting, Commitment Accounting, Assets Accounting, Revised Chart of Accounts, and Double Entry Book Keeping.

All above is ensured through revised Chart of Accounts and would eventually lead to complete transformation to full Accrual Accounting.

## Chart of Accounts

An essential feature of NAM is the new Chart of Accounts. Chart of Accounts provides the structure by which accounting transactions are coded and thus used in financial reporting. The chart of accounts structure consists of elements that each represents a "view" or "dimension" of financial information considered useful for financial reporting

**The chart of Accounts contains five elements. These are as follows:-**

- Entity
- Object
- Fund
- Function
- Project

**Entity:** The entity element enables reporting of transactions by the organizational structure or in other words the organizational unit, which is creating transaction. The use of the entity element is mandatory for all accounting transactions. It includes:

- Government
- Ministry
- Division / Department
- Attached Department
- District
- DDO

**Object:** The Object element

enables the collection and classification of transactions into expenditure and receipts and also to facilitate recording of financial information according to accounting elements. The use of the object is mandatory for all accounting transactions. It includes:

- A0000 Expenditure
- B0000 Tax Receipts
- C0000 Non-Tax receipts
- E0000 Capital receipts
- F0000 Fixed Assets
- G0000 Liabilities
- H0000 Equity

**Fund:** It is the pool of money from which budgetary allocation is made (e.g. Consolidated Fund / Public Account. To indicate "fund" is mandatory for all accounting transactions. It includes:

- Grant No. Public Account /

Consolidated Fund

- Source - Capital / Revenue
- Sub- Fund- Voted, Charged, Current, Development

**Project Element:**

The Project element enables transactions to be aggregated and reported at a project level (generally equivalent to 'sub-grant' level in the project development budget). The Project element consists of the project number, which is identified by four numeric characters. Each Project will have a unique project number.

**Function:** The Function element provides reporting of transactions by economic function and program. The function code is mandatory for transactions relating to expenditure. It includes:

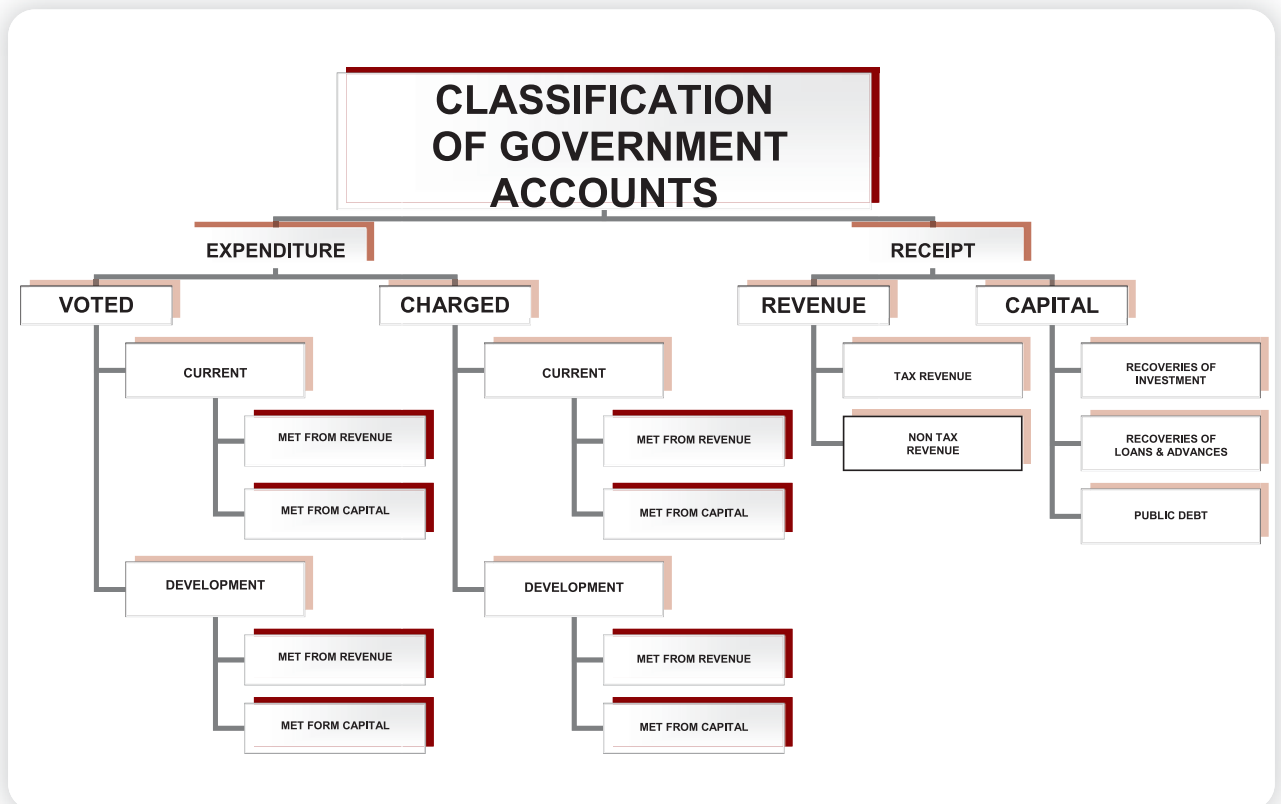
- Major Function

- Minor Function
- Detailed Function
- Sub-Detailed Function
- Program

**NAM is based on Modified Cash Basis of Accounting, in so far as it provides for:-**

- Commitment Accounting
- Accounting for Assets & Liabilities
- Double Entry Booking

**Commitment Accounting:** Commitment could be defined as an obligation to make a future payment, and arises when an entity issues a legally binding purchase order or enters into a contract for acquisition of goods and services. Commitment Accounting introduced w.e.f. December, 2009 has the following main features:-



- Commitments only of significant values are to be recorded. Presently the threshold of recording commitments is Rs. 500,000/-.
- Commitments are to be booked against the funds available under a particular budget head.
- All outstanding commitments, at the close of the financial year would be reversed.
- Expenditures are to be reported on the main body of Accounts on a cash basis, and then adjusted for outstanding commitments at the end of the reporting period.

## Accounting policies for recording Commitments

Following Accounting Policies govern the recording of commitments:-

- Commitments are used to control large and non-regular expenditures against appropriation;
- A purchase contract and order has been placed;
- The officer in accordance with the Delegation of Financial Powers has authorized the commitment;
- Once a commitment is entered into and approved by the delegated authority it must be recorded by the DDO;
- Commitments shall only be raised for those expenditures expected to be paid for in the current financial year.
- A commitment, once recorded, must not be reversed unless:
  - Payment has been made, or
  - The purchase order or other legally binding contract has been cancelled and approved.
- At the close of the financial year all outstanding commitments made during that year are duly scrutinized by the AG /MOF for allowing for the

reinstatement of valid commitments in the next year;

- Commitments which are not renewed are cancelled.

## Main Features of Commitment

- A process leading to Accrual based accounting
- A process envisioning better Budgetary Control
- A new concept dealing with "Memorandum" accounting and
- A method confined to contingency payments only (excluding pay, pension, GPF or staff advances)

## Accounting for Fixed Assets

Assets are Economic Resources which are owned by a business and are expected to benefit future operations.

Accounting of Assets: Under modified cash basis an asset is recognized when:

- It is probable that the future economic benefits will occur;
- The asset possesses a cost or other value that can be measured reliably.

## Accounting of Liabilities

Under modified cash basis a liability is recognized when:

- It is probable that the future sacrifice of economic benefits will be required;
- The amount of the liability can be measured reliably.
- The major classes of liability to be reported in the balance sheet under the modified cash accounting model are as follows:
  - Public debt
  - Deferred liabilities
  - Current liabilities

## Recognition of Revenues

A revenue item is recognized when:

- It is probable that the increase of future economic benefits related to the increase in assets and/or decrease in liabilities will occur;
- The increase in future economic benefits related to the increase in assets and / or decrease in liabilities can be measured reliably;
- Receipts are accounted on a cash basis;
- Financial reports then show expected receipts as a note.

## Recognition of Expenses

An expense is recognized when:

- It is probable that the decrease in future economic benefits related to the reduction in assets and / or increases in liabilities will occur;
- The decrease in future economic benefits can be measured reliably;
- All revenues and all expenditure are shown on a gross basis.

## Recognition of Equity

Unless otherwise specified, the Government of Pakistan is the sole holder of the residual value of all accounting entities.

- The Government of Pakistan has two distinct roles within the modified cash model. The first is as the owner of all accounting entities, the second is as the funder of services. This distinction is important in determining the entity/ Government relationship.

## Movement towards full Accrual Accounting

NAM is geared to transformation to full Accrual Accounting. Accrual Accounting has following major benefits.

- Support better accountability and provide better information for decisions on investments and management of assets and liabilities.
- Provide more meaningful and comprehensive information to fully cost the goods and services provided by the organization.
- Provide better information for choices between different options with respect to service delivery.
- Reduce scope to report expenses that may never occur such as un-liquidated obligations.
- Provide a better basis for evaluating an organization's performance in terms of resource management.
- Better support results based management.
- Improve consistency, comparability and reliability of financial statements which strengthens overall confidence in the financial information for both external and internal users

## Performance of Accounting Functions

Under the Controller General of Accounts (Appointment, Functions and Powers) Ordinance, 2001 the Controller General of Accounts is responsible through offices sub-ordinate to him – to maintain the Accounts of Federation, all the Provinces & Districts, yet some organizations are entrusted with the job of maintaining their own accounts (though under the overall supervision of the Controller

General of Accounts). These organizations known as self accounting entities, are as follows:-

- National Savings Organization;
- Pakistan Mint;
- Pakistan Public Works Department;
- Ministry of Foreign Affairs;
- Geological Survey of Pakistan;
- Pakistan Railways;
- Forest Department;
- Ministry of Defence.

The system provides for comprehensive models of payroll, GP Fund, staff expenses and pensions. With these models fully in place the erstwhile complaints regarding missing GP fund credits and delay in the final payment of GP fund as well as pensions have been substantially reduced. In fact it is now possible to generate the pension payment order on the same day the pension papers are received in an accounts office.

## Exempt Entities

Accounts of following entities do not form part of Government Accounts. These entities, fully responsible for maintaining their accounts, are:-

- Water and Power Development Authority;
- Oil and Gas Development Authority;
- National Highways Authority;
- National Mass Transit Authority; and
- All Government Corporations, listed companies and other entities required to prepare reports under the Companies law.

## Budget Preparation and Execution

Budget preparation and execution is a crucial element of the financial

management system. The Project to Improve Financial Reporting fully caters for preparation of budget and its execution through the system. It provides for funds availability check which does not allow any payment in excess of the available budget and hence is a very effective tool for expenditure controls.

## Auditing

The reforms project also encompasses the Auditing activity. For this purpose a new Risk based Audit manual known as Financial Audit Manual along with sectoral guidelines has been developed. Coupled with the Audit Management Information System this would comprehensively update the audit system and thus further strengthen the system of transparent and institutional accountability.

## IPSAS Implementation Status in Pakistan

As a continuation of the reforms process, Pakistan has through a phased program started the adoption of IPSAS. As first step, since Financial year 2006-2007 the Financial Statements of all Accountants General (National as well as Sub-national) are being prepared under Cash Basis IPSAS. Currently the financial statements blend the reporting formats under NAM and IPSAS cash Basis by reporting Cash Flows Statement (IPSAS-2) over and above the requirements of Cash Basis IPSAS, and focus on budgetary compliance for the financial year as per procedure laid down in the Constitution.

Note: The attached annexure shows the details of IPSAS requirement and its implementation status in Pakistan.

<i>Financial Statements</i>			
1.3.4	An entity should prepare and present general purpose financial statements which include the following components:	Financial Statements for the year ended June 30, 2009	<i>Complied</i>
	(a) A statement of cash receipts and payments which:	Statement of Cash Receipts & Payments	<i>Complied</i>
	(i) Recognizes all cash receipts, cash payments and cash balances controlled by the entity; and	do	<i>Complied</i>
	(ii) Separately identifies payments made by third parties on behalf of the entity.	do	<i>Partially Complied</i>
	(b) Accounting policies and explanatory notes; and	Notes to the Financial Statements	<i>Complied</i>
	(c) When the entity makes publicly available its approved budget, a comparison of budget and actual amounts either as a separate additional financial statement or as a budget column in the statement of cash receipts and payment.	1 - Statement of Comparison of Actual Amounts by Function 2 - Statement of Comparison of Actual Amounts by Department	<i>Complied</i>
<i>Information to be Presented in the Statement of Cash Receipts and Payments</i>			
1.3.12	The statement of cash receipts and payments should present the following amounts for the reporting period:	Statement of Cash Receipts & Payments	<i>Complied</i>
	(a) Total cash receipts of the entity showing separately a sub-classification of total cash receipts using a classification basis appropriate to the entity's operations;	Statement of Cash Receipts & Payments	<i>Complied</i>
	(b) Total cash payments of the entity showing separately a subclassification of total cash payments using a classification basis appropriate to the entity's operations; and	Statement of Cash Receipts & Payments	<i>Complied</i>
	(c) Beginning and closing cash balances of the entity.	Statement of Cash Receipts & Payments	<i>Complied</i>
1.3.13	Total cash receipts and total cash payments, and cash receipts and cash payments for each sub-classification of cash receipt and payment, should be reported on a gross basis, except that cash receipts and payments may be reported on a net basis when:	Statement of Cash Receipts & Payments	<i>Complied</i>
	(a) They arise from transactions which the entity administers on behalf of other parties and which are recognized in the statement of cash receipts and payments; or	Statement of Cash Receipts & Payments	<i>Complied</i>
	(b) They are for items in which the turnover is quick, the amounts are large, and the maturities are short.	Statement of Cash Receipts & Payments	<i>Complied</i>
1.3.14	Line items, headings and sub-totals should be presented in the statement of cash receipts and payments when such presentation is necessary to present fairly the entity's cash receipts, cash payments and cash balances.	Statement of Cash Receipts & Payments	<i>Complied</i>

<i>Payments by third parties on behalf of the entity</i>			
1.3.24	Where, during a reporting period, a third party directly settles the obligations of an entity or purchases goods and services for the benefit of the entity, the entity should disclose in separate columns on the face of the statement of cash receipts and payments:	<u>Statement of Cash Receipts &amp; Payments</u> Please note that due to non availability of information the figures are not presented. Furthermore, the non availability of information was discussed with the Finance Department	<i>Partially Complied</i>
	(a) Total payments made by third parties which are part of the economic entity to which the reporting entity belongs, showing separately a subclassification of the sources and uses of total payments using a classification basis appropriate to the entity's operations; and	<u>Statement of Cash Receipts &amp; Payments</u> Please note that due to non availability of information the figures are not presented. Furthermore, the non availability of information was discussed with the Finance Department	<i>Partially Complied</i>
	(b) Total payments made by third parties which are not part of the economic entity to which the reporting entity belongs, showing separately a subclassification of the sources and uses of total payments using a classification basis appropriate to the entity's operation. Such disclosure should only be made when during the reporting period the entity has been formally advised by the third party or the recipient that such payment has been made or has otherwise verified the payment.	<u>Statement of Cash Receipts &amp; Payments</u> Please note that due to non availability of information the figures are not presented. Furthermore, the non availability of information was discussed with the Finance Department	<i>Partially Complied</i>
<i>Accounting Policies and Explanatory Notes</i>			
1.3.30	The notes to the financial statements of an entity should:	Notes to the Financial Statements	<i>Complied</i>
	(a) Present information about the basis of preparation of the financial statements and the specific accounting policies selected and applied for significant transactions and other events; and	Notes to the Financial Statements <i>Note # 1 - 7</i>	<i>Complied</i>
	(b) Provide additional information which is not presented on the face of the financial statements but is necessary for a fair presentation of the entity's cash receipts, cash payments and cash balances.	Notes to the Financial Statements. <i>Note # 8 - 31</i>	<i>Complied</i>
1.3.31	Notes to the financial statements should be presented in a systematic manner. Each item on the face of the statement of cash receipts and payments and other financial statements should be cross referenced to any related information in the notes.	Notes to the Financial Statements <i>Note # 1 - 31</i>	<i>Complied</i>

<i>Reporting Period</i>			
1.4.1	The general purpose financial statements should be presented at least annually. When, in exceptional circumstances, an entity's reporting date changes and the annual financial statements are presented for a period longer or shorter than one year, an entity should disclose in addition to the period covered by the financial statements:	The Reporting Period ranges from July 1, 2008 to June 30, 2009	Complied
	(a) The reason(s) for a period other than one year being used; and	The Reporting Period ranges from July 1, 2008 to June 30, 2009	N/A
	(b) the fact that comparative amounts may not be comparable.	The Reporting Period ranges from July 1, 2008 to June 30, 2009	N/A
<i>Timeliness</i>			
1.4.4	The usefulness of the financial statements are impaired if they are not made available to users within a reasonable period after the reporting date. An entity should be in a position to issue its financial statements within six months of the reporting date, although a timeframe of no more than three months is strongly encouraged. Ongoing factors such as the complexity of an entity's operations are not sufficient reason for failing to report on a timely basis. More specific deadlines are dealt with by legislation and regulations in many jurisdictions.	The dead line for submission of Financial statements decided by CGA was August 31, 2009. Which is 2 months after the end of Financial Year.	Complied
<i>Authorization Date</i>			
1.4.5	An entity should disclose the date when the financial statements were authorized for issue and who gave that authorization. If another body has the power to amend the financial statements after issuance, the entity should disclose that fact.	Notes to the Financial Statements	Complied
<i>Comparative Information</i>			
1.4.16	Unless a provision of this Standard permits or requires otherwise, comparative information should be disclosed in respect of the previous period for all numerical information required by this Standard to be disclosed in the financial statements, except in respect of the financial statements for the reporting period to which this Standard is first applied. Comparative information should be included in narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.	A - Statement of Cash Receipts & Payments B - Statement of Comparison of Actual Amounts by Function C - Statement of Comparison of Actual Amounts by Department D - Notes to the Financial Statements	Complied

<i>Identification of Financial Statements</i>			
1.4.23	Each component of the financial statements should be clearly identified. In addition, the following information should be prominently displayed and repeated when it is necessary for a proper understanding of the information presented:	<i>Following captions have been used:</i> A - Statement of Cash Receipts & Payments B - Statement of Comparison of Actual Amounts by Function C - Statement of Comparison of Actual Amounts by Department D - Notes to the Financial Statements	<i>Complied</i>
	(a) The name of the reporting entity or other means of identification;	Name of The Concerned Govt is mentioned of its respective Financial Statements	<i>Complied</i>
	(b) Whether the financial statements cover the individual entity or the economic entity;	Name of The Concerned Govt is mentioned of its respective Financial Statements	<i>Complied</i>
	(c) The reporting date or the period covered by the financial statements, whichever is appropriate to the related component of the financial statements;	Year ended June 30, 2009 has been used.	<i>Complied</i>
	(d) The reporting currency; and	Pakistan Rupee disclosed in notes to the Financial Statements	<i>Complied</i>
	(e) The level of precision used in the presentation of figures in the financial statements.	Disclosed in notes to the Financial Statements	<i>Complied</i>

*The Author is a Senior Fellow Member of ICMAP.*

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# Modernization of accountability in public sector of Bangladesh from the perspective of global standards

S. M. Rafiqul Islam ACA



## Introduction

Accountability is not a simple concept. It is a critical element of representative democratic government. Today, every conscious citizen of Bangladesh is demanding clearer and greater accountability for the way the government spending their tax money and uses its authority. That's why traditional view and practice of accountability are challenged in a public sector where the focus is on getting results, where the government engages in partnering arrangements with local government and with outside organizations to deliver public policy, and where managers are encouraged to innovate and take reasonable risks.

According to NASA,

*"Public administration accountability involves the means by which public*

*agencies and their workers manage the diverse expectations generated within and outside the organization."*

Therefore, high standards of public governance are the essential foundation for achieving sustainable economic growth and social cohesion. Without high standards, there can be no confidence in the integrity of public institutions or indeed in the value of democratic processes in promoting and protecting the interests and well-being of citizens.

## The Elements of Accountability

Accountability is a relationship based on obligations to demonstrate, review, and take responsibility for performance, both the results achieved in light of agreed expectations and the means used.

<b>A relationship</b>	Accountability involves two (or more) parties in a relationship that features certain obligations.
<b>Obligations</b>	All parties in an accountability relationship have obligations that imply responsibilities and consequences. In addition to the obligations inherent in the relationship (to demonstrate, review, and take responsibility), others can come from outside (such as legal, professional, contractual, and hierarchic obligations) and from an internalized sense of integrity.
<b>Demonstrate</b>	Demonstrating performance involves proactively reporting what results have been achieved and the appropriateness of the means used; it requires honesty, openness, and transparency. In a hierarchic relationship, this obligation is on the subordinate party.
<b>Review</b>	Review involves analyzing and reflecting on the reported results and the means used, and then taking appropriate action. Each party has an obligation to review. Those accounting should review to learn what is working and what is not, and should adjust their activities accordingly. Those holding to account should direct or call for any needed change. If performance is good, this could simply mean reconfirming current activities or could entail individual rewards. If performance is weak, corrective action would be expected. Review and adjustment of unacceptable performance might involve sanctions on individuals. Review can also result in revising expectations or adjusting other elements of the accountability relationship.
<b>Take responsibility</b>	Taking responsibility emphasizes answering for and accepting responsibility for what has or has not been accomplished and for the means used in the effort.
<b>Results</b>	A key focus in accountability is on the results (outputs and outcomes) accomplished or not accomplished.
<b>Agreed expectations</b>	The agreed expectations stem from either a formal or informal agreement on what is to be accomplished. In a hierarchic situation, one would expect a degree of discussion between the two parties as to what is reasonable and feasible, placing an obligation on the superior party to be clear about what is expected.
<b>In light of</b>	This emphasizes that performance is comparative. One is called on to compare what was accomplished with what was expected. Effective accountability requires disclosure: setting out beforehand what is expected and then reporting against those expectations. It also requires learning: looking in light of the expectations at what was accomplished or not, and what has been learned that will improve future performance.
<b>The means used</b>	How one delivers public services, uses authority, and handles public money are more than means of achieving results: they are ends in themselves, important reflections of public sector values and ethics. It is expected that the means used treat people fairly, are undertaken with propriety, and reflect good stewardship—that is, provide best value for money and respect the environment.

Source: 2002 December Report of the Auditor General of Canada



**ACCOUNTABILITY FRAMEWORK IS AN ESSENTIAL BEGINNING FOR EFFECTIVE ACCOUNTABILITY. ITS IMPORTANCE IS OFTEN REFLECTED IN DOCUMENTS THAT OUTLINE SPECIFIC ARRANGEMENTS FOR ACCOUNTABILITY. DOCUMENTING THESE ARRANGEMENTS HELPS ENSURE A ROBUST ACCOUNTABILITY RELATIONSHIP; ONE THAT SETS OUT A BASIS FOR ASSESSMENT AND THAT DOES NOT CHANGE IF INDIVIDUALS IN THE ARRANGEMENT ARE CHANGED.**



## The Accountability Process

A widely circulated slogan “Placing the Public's Money Beyond Parliament's Reach”.

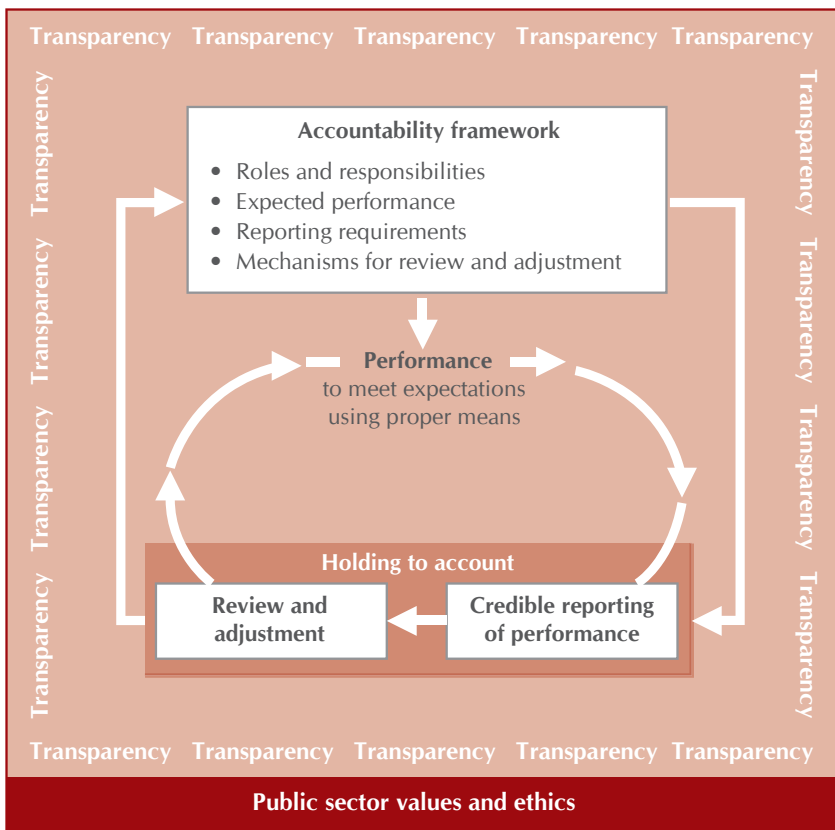
Keeping this view in mind the accountability process should be formulated depending on the principles of effective accountability. In applying these principles, two aspects of the accountability process need to be considered:

- The accountability framework. Is there an appropriate accountability framework in place to support strong accountability relationships?
- Holding to account. Are effective reporting, review, and adjustment occurring?

Accountability framework is an essential beginning for effective accountability. Its importance is often reflected in documents that outline specific arrangements for accountability. Documenting these arrangements helps ensure a robust accountability relationship; one that sets out a basis for assessment

and that does not change if individuals in the arrangement are changed. As shown in the following Exhibit, a good

accountability framework has four elements, which are based on the principles of effective accountability.



Source: 2002 December Report of the Auditor General of Canada

<b>Clear roles and responsibilities</b>	The roles and responsibilities of the parties in the accountability relationship should be well understood and agreed upon.
<b>Clear performance expectations</b>	The objectives pursued, the accomplishments expected, and the operating constraints to be respected (including means used) should be explicit, understood, and agreed upon.
<b>Balanced expectations and capacities</b>	Performance expectations should be clearly linked to and balanced with each party's capacity (authorities, skills, and resources) to deliver.
<b>Credible reporting</b>	Credible and timely information should be reported to demonstrate what has been achieved, whether the means used were appropriate, and what has been learned.
<b>Reasonable review and adjustment</b>	Fair and informed review and feedback on performance should be carried out by the parties, achievements and difficulties recognized, appropriate corrections made, and appropriate consequences for individuals carried out.

**Public sector values and ethics**, such as fairness, honesty, probity, integrity, and fidelity to the public trust, underlie any accountability process. Without a shared understanding of these basic values by the parties involved, an accountability process is unlikely to be effective. Public sector managers and their partners who deliver public services for the government should actively promote and enforce a corporate culture of high ethical standards and public sector values. The more those delivering public functions have internalized a sense of responsibility for observing public sector values and ethics, the less those values and ethics need to be formalized in accountability arrangements.

### Relationships within the Accountability Systems:

Demands for a client focus, more responsiveness from the bureaucracy and the personal responsibility of managers are changing the system of accountability of the public service and, indeed, the relationship between government and citizen.... civil servants work for the government, and in democratic governments it is assumed that they work at least indirectly for all citizens.

Under the bureaucratic system, expectations are managed through a hierarchical arrangement based on supervisory relationships; the legal accountability system manages agency expectations through a contractual relationship; the professional system relies on deference to expertise; while the political accountability system promotes responsiveness to constituents as the central means of managing the multiple expectations. Such relationships within accountability systems are shown by the following Table.

	Type of Accountability System	Analogous Relationship (Controller/Administrator)	Basis of Relationship
1	Bureaucratic	Superior/Subordinate	Supervision
2	Legal	Lawmaker/law executor/Principal/Agent	Fiduciary
3	Professional	Layperson/expert	Deference to expertise
4	Political	Constituent/representative	Responsiveness to constituents

Source: *Public Administration Review, USA (May/June 1987)*

### Ensuring Public Sector Integrity and Accountability

An OECD (Organization for Economic Co-operation and Development) organized a seminar in its 50th anniversary in Paris in April 2011 where experts on integrity and public governance and internal and external audit professionals came together to share their experiences, debate

ways to address public sector integrity and accountability, and identify best practices. In that seminar the following recommendations provided to enhance the public sector's contribution in the public administration's risk management, control and governance processes to the prevention, detection, and reporting of fraud and corruption.

1. Internal audit's reporting lines to the highest authority within the ministry contribute to its independence. To be independent, internal audit must report administratively to the minister or to the immediate deputy. Such a reporting line should be mandatory and formalized in the internal audit mandate. An independent audit committee, reporting to the highest authority in the ministry, should also exist. Its mandate should clearly cover the monitoring of risk exposures, particularly those relating to fraud and corruption. In addition, such an audit committee should be kept periodically informed of cases of fraud and corruption. Lastly, most of its members should be recruited from outside the ministry and, where possible, from outside the public administration. Internal audit should have close ties with the audit committee
2. In cases where internal audit and investigation functions are separate, there should be a clear mandate for each function. They should work together to coordinate rules and policies aimed at avoiding duplication, have regular meetings to coordinate work programs and results (including the communication of annual reports), and participate in joint training/awareness-raising activities with regard to the risks of

fraud and corruption and fraud-combating process (detection, investigation, improvement through the experience gained, and reporting).

3. Internal and external audit should consider increasing the coordination of their activities to mitigate the risks of fraud and corruption.
4. Internal audit should play a key role in advocating the formalization of an internal control and risk management framework that goes beyond purely financial controls to encompass the control environment in the very broadest sense, and that incorporates a code of ethics and fraud and corruption prevention plans.
5. Internal audit should periodically evaluate the quality and effectiveness of the controls put in place by management to expressly address fraud and corruption risks.
6. Internal auditors should be required to have general internal audit skills, as well as specific qualifications so they can better assess, and better detect, fraud and corruption risks.

Source: *The Institute of Internal Auditors, USA*

## Service Delivery by Government Institutions

According to Swedish Appropriations Bill for FY 2003,

*“The long-term goal is that citizens and business, from a service perspective, perceive the public administration as one single 24/7-agency without disturbing boundaries between agencies. This entails e.g. that one case, as far as possible, demands only one contact with the administration, which calls for agency collaboration. It is, however, important that agency responsibilities do not become so blurred as to impair transparency and accountability.”*

For the improvement of public service delivery, Batho Pele developed some principles saying “The People first” which were accepted by the Minister of Public Service and Administration in South Africa. It can be argued that all attempts at serving communities should be checked against the principles of Batho Pele, which are:

- (1) Consultation. Citizens should be consulted about the quality of the services they receive.
- (2) Service standards. Communities should be informed what level and quality of service they will receive so that they know what to expect.
- (3) Access. All citizens should have equal access to the services they are entitled to.
- (4) Courtesy. All members of the community should be treated with courtesy and consideration.
- (5) Information. Communities should be given full and accurate information about the public services they are entitled to.
- (6) Openness and transparency. Citizens should be informed on how local authorities function and the information they are entitled to.

- (7) Redress and handling of complaints. If community members do not receive promised services they should be entitled to a full explanation and also to a speedy remedy.
- (8) Value for money. Services should be provided economically and efficiently in order to provide citizens with the principle of best value for money.

## Basic Normative Criteria for Effective and Efficient Public Service Delivery

A universally acceptable code of conduct is a necessary component for public officials to perform their activities ethically. In the table below, normative criteria are proposed as being suitable as a base for effective and efficient public service delivery to its populace on the local sphere that can be measured or evaluated.

VALUES	ATTITUDES	APTITUDES
➤ Integrity	➤ Transparency	➤ Knowledge
➤ Transparency	➤ Responsibility	➤ Acceptance & comprehension of the goals & functioning of the administrative institutions
➤ Publicity	➤ Quality awareness	➤ Leadership qualities
➤ Accountability	➤ Legibility	➤ Communication skills
➤ Equity	➤ Clarity	➤ Social skill
➤ Non-discrimination	➤ Simplicity	➤ Independence
➤ Quality	➤ Inquisitiveness	➤ Ability to use experience
➤ Professionalism	➤ Adaptability	➤ Ability to further education & training
➤ Reliability	➤ Listening ability	➤ Analytical capability
➤ General interest	➤ Involvement	➤ Sense of renewal
	➤ Speed	
	➤ Effectiveness	
	➤ Efficiency	

## Conclusion

In the democratic system, the people elect the government and the government must be held to account, in Parliament, for the way it uses public authority. Ministers are individually accountable to Parliament for their own actions and for all aspects of their departments' and agencies' activities. Ministers are also collectively accountable for the decisions taken by the Cabinet.

Officials should be accountable to their ministers for the operation of their organizations. Traditionally, they remain anonymous. They may be required to explain those operations to Parliament on behalf of their ministers, but they do not need to answer to Parliament.

Therefore, in our view, accountability within the government administration should serve the following three purposes:

- to control against the abuse or misuse of power;
- to provide assurance that activities were carried out as intended and with due regard for fairness, propriety, and good stewardship; and
- to encourage improved performance of programs and policies, through reporting on and learning from what works and what does not.

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*The Author is a Member of ICAB*



# Interpretation of Taxing Statutes and The Role of Professional Accountants

Shawkat Ali Waresi



The legislative intention laid down in taxing statute is to realise revenue for the state by imposing burden of tax on its subjects. But no tax can be imposed on the subject without words in the Act clearly showing intention to lay a burden upon them.<sup>1</sup> More precisely, a subject can not be taxed merely on the plea that he falls within the spirit of law: the language in which the said law is written must express in clear terms the intentions of the legislature.

In Bangladesh the language finally used in taxing statutes is the result of several operations. First, the National Board of Revenue puts the intention of the Government of Bangladesh in the form of guidelines. It is then sent to the Ministry of Law where the expert draftsman converts it into a bill consisting of sections, sub-sections, clauses and sub-clauses. The bill is then introduced by the Finance Minister in Parliament where the members of both the Treasury Bench and the Opposition apply their minds to the words in the bill and propose changes which are either accepted or rejected by the majority of the members of Parliament. The bill on being passed by Parliament is sent to the President. If the President assents to the bill, it is converted into an Act. Thus the above process shows that both the language and the intention of taxing

statute undergo a very close and careful scrutiny before its enactment.

A taxing statute is put to real test when it comes to be implemented. If any dispute arises in interpreting a section, or a part of it or even a phrase or a word, the judicial authorities, try to come to a correct decision on such dispute by the application of the rules of interpretation. One special feature of income tax law is that if any dispute arises in the interpretation of any provision of law, the parties involved are the state on the one hand and the subjects on the other, unlike in other laws where the dispute usually remains confined to two private parties.

Another significant feature of income tax law is that it deals with the subtle concepts of mercantile, financial and accounting nature. For the interpretation of the general laws like Muslim law, Hindu law or Contract law, general rules of interpretation are applied. These general rules, except in certain circumstances or for certain purposes, do not apply to income tax law because of its special character. When general rules of interpretation do not apply to income tax law, it becomes necessary to rely upon other aids for determining legislative intention.

Of the aids necessary for the interpretation of taxing statutes, pre-enactment history of the statute is important. The Statement of Objects and Reasons, Report of the Select Committee Proceeding, Statement by the Finance Minister on the introduction of the Bill, legislative debates, amendments proposed by the Opposition and the action of the legislature thereon in the course of parliamentary proceeding form the pre-enactment history of taxing statutes. Judicial authorities, however, do not unanimously admit the importance and apply the aid of the history of taxing statutes to the interpretation. The British law prescribes the rule that for the purpose of construing a statute, any history of legislation should not be looked into. 2 Following the principles of the British rule Supreme Court of India declined to assent to the proposition that the history of a statute might throw valuable light on the intention of the legislature. 3 The American view, on the other hand, is not same on the point. Legislative history as an aid to the interpretation of a statute is not rejected by the American judicial authorities. They hold the view that where the language of a statute is ambiguous or obscure it isn't unjustified to take external assistance for ascertaining the object of the provision. They admit that external assistance is necessary for ascertaining the object of the provision. They, however, hold that these external aids do not have the same force as the judicial pronouncements. External aids could be helpful only in ascertaining the legislative intention.4

Previous decisions of the High Courts and Supreme Court adopted by the judicial authorities in the interpretation of taxing statutes are the most reliable and dependable aids to construe the statutes of the similar kinds. But there are instances of divergent views held by the judicial authorities even on the identical question. So far as the construction of

the statute is concerned, the judicial interpretation is not always uniform. From the study of a number of tax decisions of the High courts and the Supreme Courts of Bangladesh, India and Pakistan, it appears that the judicial authorities are not only divided in their decisions but also prescribe principles of construction which are even opposed to one another.

A section of judicial authorities hold the view that a fiscal enactment should be construed strictly and whenever there is an ambiguity, the benefit of doubt should be given to the citizens. If two equally reasonable constructions are possible, the construction favorable to citizens should be preferred.5 They even go so far as to say that the income tax Act should receive a strict construction, that is, a construction in favour of the Crown. 6

The second section of judicial authorities hold that an interpretation which defeats the very object sought to be achieved by the legislature must, if possible, be avoided even though the language of the statute suffers from slight inexactitude.7 They further say that the view of strict contraction in favour of the subjects maybe applied in a country where the doctrine of laissez fair is the ruling principle of the economy of the state. But in a state where the doctrine of welfare economy is adopted, the taxing statute should be interpreted on the language used in the statute to see whether the Act of the legislature clearly shows the intention to lay a burden on the citizens. Once that intention is proved it is not open to speculate on what would be the fair and equitable mode of levying tax. In case of ambiguity the attempt of the Court should be guided by the principles of justice and fairness.8 The judicial authorities of this group also hold the view that even though a taxing statute is to be construed liberally and favorably to the subjects, equality and impartiality

“ A SECTION OF JUDICIAL AUTHORITIES HOLD THE VIEW THAT A FISCAL ENACTMENT SHOULD BE CONSTRUED STRICTLY AND WHENEVER THERE IS AN AMBIGUITY, THE BENEFIT OF DOUBT SHOULD BE GIVEN TO THE CITIZENS. IF TWO EQUALLY REASONABLE CONSTRUCTIONS ARE POSSIBLE, THE CONSTRUCTION FAVORABLE TO CITIZENS SHOULD BE PREFERRED. ”



in the incidence of taxation are also no less important. The statute should, therefore, be construed to promote the equality and impartiality.<sup>9</sup>

The third section of judicial authorities hold the view that while interpreting a taxing statute, if there is any substantial doubt, the provisions relating to imposition of tax, that is, charging sections, are to be construed in favour of the subjects. Machinery sections, on the other hand, are to be liberally construed. If the incidence of tax is clear, the machinery sections should be so construed as to make the realisation of the proper tax possible. They should not be construed in such a way so that the intention of the legislature is defeated and the realisation of revenue is prevented.<sup>10</sup>

Since income tax laws deal with the subtle concepts of mercantile, financial and accounting nature, a considerable degree of knowledge in these subjects is required to understand the meaning and intention of taxing statutes. Even a multi-disciplinary approach may be taken for a correct and rational

interpretation of some provisions of taxing statutes. Considering the nature of the fiscal law the importance and relevance of the professional accountants have been duly emphasised by the income tax laws of Bangladesh, India and Pakistan by assigning judicial roles to them.

Professional accountants have a unique place in the legal framework of taxation. The Taxes Appellate Tribunal constituted under section 11 of the Income Tax Ordinance, 1984 consists of a President, a judicial member and an accountant member. Sub-section (3) of section 11 of the Ordinance provides that "A judicial member shall be a person who is or has been a District Judge" and sub-section (3) of section 11 of the said Ordinance also provides that "An accountant member shall be a person who is a Commissioner of Taxes or who has practiced professionally for a period of not less than eight years as a chartered accountant or a cost and management accountant." Under this provision of income tax law a chartered accountant or a cost and management accountant

when appointed as an accountant member enjoys the same legal authority as that of a District and Session Judge who is the highest judicial authority after the Judges of the Supreme Court, and a Commissioner of Taxes who is the highest income tax authority after the National Board of Revenue. It may be mentioned that the Taxes Appellate Tribunal is an appellate court under the Code of Civil Procedure (New India Life Assce & Co. Ltd Vs. C.I.T [1957]) 31 I.T.R.844). The decision of the Taxes Appellate Tribunal on the question of fact is final.

When a question of law arises out of the orders of the Taxes Appellate Tribunal the Commissioner of Taxes or the assessee may make a reference to the High Court Division of the Supreme Court. If even a question of fact decided by the Taxes Appellate Tribunal is referred to the High Court, the High Court may refuse to answer the question (Munshi Gulab Sing & Sons Vs. C.I.T.1949 I.T.R 66, 83)

The case relating to question of law referred to the High Court Division is heard by a bench of not less than two judges. The High Court decides the questions raised by the case and delivers a judgment containing the grounds on which the question is founded. What High Court in fact does is correct interpretation of the taxing statute. The question arises in this connection: is the bench interpreting the taxing statute competent enough?

The provision about the constitution of the bench of the High Court to hear and decide the case relating to question of law does not specify the qualification and experience of the judges of the bench as the provision about the constitution of the Taxes Appellate Tribunal does. It may be



mentioned in this connection that thousands of cases relating to income tax, VAT and customs remain undisposed of in the High Court for years together due mainly to shortage of judges with required qualification and experience in fiscal laws. According to Dhaka Law Report : "About 10,00 cases most of them pending for years together, still await disposal .The position is alarming for the reason that every week no fewer than 40 fresh cases are added to this staggering 10,000 while on an average hardly 10 such cases are disposed of in a week. This backlog of cases are there with orders of stay of realisation of the assessed government revenue...it was found that cases of government revenue remained inordinately stalled seriously affecting the government's budgetary calculations.....government revenue worth crores of taka continue to remain unrealised every week for indefinite period of time" [ 51 DLR (1999) ]. In the

national interest the Government should consider constitution of Revenue Bench consisting of professional accountants or appoint professional accountants in the bench constituted to hear the revenue cases. The professional accountants to be appointed as the judges of the Revenue Bench (or the existing bench) of the High Court must be the professional accountants who have worked for a specified period as the accountant member in the Taxes Appellate Tribunal.

In a welfare state income tax is imposed to realise a number of objectives. Of them, mobilisation of internal resources and attainment of greater degree of equality in the distribution of income are most important. Income tax laws should be rationally framed and carefully construed so that these two important purposes are achieved without doing injustice to the citizens or defeating the revenue. Recognising the importance of

professional accountants in the interpretation of taxing statutes, the professional accountants should be appointed as the judges of High Court bench constituted to hear the revenue case. It should be kept in mind that the theoretically most perfect tax system in the world may become a bad system if the intention expressed in the law is distorted.<sup>11</sup>

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## Syful Islam Assume Responsibility as President-ICAB for 2012

On 01 January 2012 Ms. Parveen Mahmud FCA, President, ICAB for 2011 formally hands over the responsibility of the presidency of the Institute to Mr. Md. Syful Islam FCA, President elect for the year 2012 in a simple ceremony organized by the Institute. The Secretary, ICAB Mr. N I Chowdhury FCA thanked both the outgoing and incoming Presidents and expected that 2012 will be another successful year like 2011. Mr. Md. Syful Islam FCA newly elected President of ICAB for 2012 spoke on the occasion and solicited cooperation from the employees like the previous year. He urged all to work for the Institute's development. Mr. Showkat Hossain FCA, Mr. Md. Abdus Salam FCA and Mr. Shahjahan Majumder FCA newly elected Vice Presidents of ICAB for 2012 also spoke on that occasion.



## President, CSE Made a Courtesy Call to President, ICAB



The President of Chittagong Exchange Commission (CSE) Mr. Al-Maruf Khan FCA paid a short visit to ICAB on 5 Jan 2012. He met President ICAB and discussed various issues related to the future prospect, challenges and improvement of the Chartered Accountancy Profession. He stressed the need to uphold the image of the profession. He emphasized on the development of the quality standard of audit and assurance services provided by the audit firms. He expressed his eagerness to cooperate the Institute in strengthening the process of the reporting framework in line with global standards according to IFAC requirements.

## DRC-ICAB Annual Picnic 2012

The Annual Picnic of ICAB was held on Friday 06 January 2012. It was a day full of joy and endless leisure for the picnickers who went to Zinda Park, Rugponj, Narayanganj, an area far from Dhaka to keep away from the monotonous routine of daily busy life. It was day of pleasure and play for near about 700 picnickers.

The Dhaka Regional Committee (DRC) of the Institute arranged the annual picnic. The picnic was declared opened by the President, ICAB.



## 75th SAFA Assembly and ICAI Conference

2-Member ICAB delegation led by Mr. Md. Syful Islam FCA, President, ICAB participated 75th SAFA Assembly meeting on 07 January 2012 at Trident Hotel, Chennai, India. The other Member of the of the ICAB delegation was Mr. Anwaruddin Chowdhury FCA. In the Assembly meeting, Mr. Muhammad Rafi FCMA, Vice President SAFA took over the SAFA Presidency for 2012 and Mr. Abdul Mannan FCMA of ICMAB elected the Vice President SAFA for 2012. ICAB delegation also joined the ICAI Conference titled "Accountancy Profession: Leveraging Emerging Challenges for Inclusive Growth" held on 6-8 January 2012 at Chennai Trade Center, India. On 08 January evening, Heads of SAFA member bodies participated a Panel discussion on the theme "Competency Building of SMEs in the Emerging Trade Order". As President ICAB, I was one of the Panel Speaker and discussed the Bangladesh perspective on the topic.



## ICAB Delegation Meets Commerce Minister



A delegation of the Institute of Chartered Accountants of Bangladesh (ICAB) made a courtesy call on Mr. Ghulam Muhammed Quader, Hon'ble Minister, Ministry of Commerce, GoB at his office on 12 January 2012. The ICAB delegation was led by Mr. Md. Syful Islam FCA, President-ICAB. Other members of the ICAB delegation were Mr Md Abdus Salam FCA, Vice President, Mr. Abbas Uddin Khan FCA, Mr. M. Farhad Hussain FCA, Council Members and Past Presidents, ICAB and Mr. N I Chowdhury FCA, Secretary-ICAB.

The ICAB delegation informed about the vital roles that ICAB is playing to improve the accounting and auditing standards, best practice in corporate management and governance, financial reporting standards and ethical issues.

ICAB delegation also met Mr. Md. Ghulam Hossain, Secretary, MoC and Mr Md Showkat Ali Waresi Joint Secretary, MOC and discussed various issues related to Chartered Accountants Profession.

## ICAB Delegation Meets BB Governor

A 4-member ICAB team led by Mr. Md. Syful Islam FCA, President, ICAB met with Dr. Atiur Rahman, Governor, Bangladesh Bank in his office on 18 January 2012. Other Members of the team were Mr. Md. Abdus Salam FCA, Vice President(E&T)-ICAB, Mr. M. Farhad Hussain FCA, Member Council & Past President ICAB and Mr. Masih Malik Chowdhury. In view of tremendous increase in operations banking and non-banking financial institutions the ICAB delegation represented that there should be more provision for appointment of Chartered Accountants in non-financial and financial institutions of all categories in order to ensure smooth application of accounting and auditing standards and standards of good governance. ICAB team drew attention to the Governor about some discrepancies on Bank Audit and Bank branch Audit. ICAB urged the Governor to use the expertise of ICAB on this matter. ICAB team also informed the Governor that ICAB is preparing a framework on "Banking Sector" which will be very helpful for banking sector. Governor assured all sorts of cooperation to ICAB in the coming days for strengthening the banking sector.



## 19th SAFA Board Meeting and ICAP Conference



2-Member ICAB delegation headed by Mr. Md. Syful Islam FCA, President, ICAB with Mr. Anwaruddin Chowdhury FCA, Member Council & Past President ICAB and Technical Advisor of SAFA Board participated 19th SAFA Board meeting and ICAP Concluding Golden Jubilee Conference titled “Testing times: Reflections on Present and Future” on 20-21 January 2011 at Lahore, Pakistan.

## Conference on “Stock Market and Economic Growth”

ICAB organized its first Members’ Conference on “Stock Market and Economic Growth” on Monday, 23 January 2012 organized by ICAB. In the Conference, Dr. Quazi Kholiquzzaman Ahmad, Chairman, Polli Karma Sahayak Foundation (PKSF) & Past President, Bangladesh Economic Association was present at the occasion as Chief Guest. Mr. Md. Shakil Rizvi, President, Dhaka Stock Exchange (DSE) Ltd. and Mr. Md. Al Maruf Khan FCA, President, Chittagong Stock Exchange (CSE) Ltd. were present at the Conference as Special Guests.

Prof. Dr. Khawaja Amjad Saeed FCA, FCMA, Professor, Emeritus & Principal Hailey College of Banking & Finance, University of Punjab, Lahore, Pakistan attended the Conference as Guest of Honour.



While, Mr. Abbas Uddin Khan FCA, Member Council & Past President, ICAB and former member, Securities and Exchange Commission (SEC) conducted the session as Session Chairman. Mr. Masih Malik Chowdhury FCA, Council Member, ICAB & Senior Partner, Masih Muhith Haque & Co., Chartered Accountants presented the keynote paper.

Md. Syful Islam FCA, President, ICAB while giving his address of welcome at the Conference said that the context of present turmoil of economic standard of the country is timely to be discussed in such forum. The recent record of Stock Market is the focal point to the unpleasant economic trend of the country as the capital market going through a volatile and fragile situation. Therefore, a healthy, strong, and stable stock market is highly desirable.

## Conference on “An Alternative Financial System for Inclusive Growth and Sustainable Development”

Redesigning growth and making it more inclusive is crucial to global and sustainable development in the post crisis era, said the speakers in a Conference for the ICAB Members held on Monday, 06 February 2012 at 06-00 p.m. at ICAB Auditorium, organized by the Institute of Chartered Accountants of Bangladesh (ICAB) on “An Alternative Financial System for Inclusive Growth and Sustainable Development”

Dr. Atiur Rahman, Governor, Bangladesh Bank graced the occasion as Chief Guest.



Mr. Md. Humayun Kabir, Managing Director & CEO, Sonali Bank Ltd. and Mr. Mohammad Abdul Mannan, Managing Director, Islami Bank Bangladesh Ltd., were present at the Conference as Panel Speakers.

Mr. Anwaruddin Chowdhury FCA, Member Council & Past President, ICAB conducted the session as Session Chairman. Mr. Md. Abdus Salam FCA, Vice President, ICAB presented the keynote paper.

## Press Conference on ICAB-CAPA International Conference



Immediately before the ICAB-CAPA International Conference, the Institute of Chartered Accountants of Bangladesh (ICAB) organized a Press Conference on 21st February 2012 at Training Room, 6th floor, CA Bhaban. Mr. Md. Syful Islam FCA, President, ICAB presided over the conference. Vice Presidents, Council Members participated in the press conference.

Mr. Md. Syful Islam said that the present financial crisis, the demand for Public Sector Financial Management in respect of economic growth is very significant. In Bangladesh the Accounting and Auditing practices is based on Cash Basis Accounting, which is lagged behind the International Public Sector Accounting Practices and fails to report on Economic, Efficient and Effective use of public resources with proper accountability and transparency.

## CA Exams Result

The ICAB Professional Examinations November- December 2011 saw total number of 73 candidates who have cleared their final exams and are now eligible for Membership of ICAB. The members of the Editorial Board congratulate the successful candidates and wish them all success in their future Endeavours.

## ACCA Team Calls on ICAB President

A three member team comprising Ms. Lucia Real Martin, Director, Emerging Markets-Asia, Ms. Gillian Fawcett, Head of Public Sector and Ms. Mahua Rashid, Country Manager, ACCA Bangladesh called on the ICAB President, Mr. Md. Syful Islam FCA on 22 February 2012.

They discussed ways and means of supplementing the existing training facilities for ICAB students. The ACCA team also offered its assistance in providing support for Training the Trainers and other in sourced assistance for students in respect of preparation for various levels of professional examinations as well as for members intending to appear in the ICAEW professional examinations. The ACCA team also offered its assistance in providing support for Training the Trainers and other in sourced assistance.



ICAB President welcomed the visiting team members and outlined the current arrangements of ICAB in respect of training facilities for its students. She also expressed the strong determination of ICAB to provide high standard of training to its students.

The President was accompanied by Mr. Md. Abdus Salam FCA, Vice President, Mr. M. Farhad Hussain FCA, Council Member and Past President and Mr. N I Chowdhury FCA, Secretary, ICAB.

## Muhith Inaugurates the ICAB-CAPA International Conference



The Institute of Chartered Accountants of Bangladesh (ICAB) and the Confederation of Asian and Pacific Accountants (CAPA) jointly organised a high profile, full-day conference on 23 February 2012. The conference, titled "Strengthening Bangladesh Public Sector Accounting and Auditing - Global Reforms and The Way Forward", held at the Pan Pacific Sonargaon Hotel in Dhaka, Bangladesh.

A large number of foreign delegates from home and abroad attended the conference.

The Conference was inaugurated by the Honourable Finance Minister, Mr. Abul Maal Abdul Muhith MP. Mr. G. M. Quader, MP, Hon'ble Commerce Minister, GoB was present the occasion as Special Guest. Mr. Shafique Ahmed, Barrister-at-law, Hon'ble Minister for Law, Justice & Parliamentary Affairs, GoB was the Chief Guest in the Valedictory Session.

## ICAB Team Meets SEC Chairman

A 4-Member ICAB team headed by Mr. Md. Syful Islam FCA, President, ICAB had a courtesy call with Professor Dr. M. Khairul Hossain, Chairman of Securities and Exchange Commission (SEC) of Bangladesh in his office on 07 March 2012. Delegation team assured the Chairman that ICAB will extend all sorts of cooperation to SEC for ensuring the interest of the Capital Market investors. They also informed about the Members' Conference on Corporate Governance Guidelines. Chairman SEC also assured his all sorts of cooperation to ICAB in the coming days for strengthening the public confidence, transparency and accountability among the investors.

Others in delegation team were Mr. Md. Abdus Salam FCA, Vice President (E&T)-ICAB, Mr. N I Chowdhury FCA, Secretary ICAB and Dr. Mahfuzul Hoque, Director LPD-ICAB



## ICAB Team Attends SAFA Events and Cost Convention of ICWAI at New Delhi



A 4-Member ICAB delegation headed by Mr. Md. Syful Islam FCA, President, ICAB participated SAFA events during 12-15 March 2012 at New Delhi, India.

ICAB delegates attended the 20th SAFA Board meeting was held on 14 March 2012.

Earlier SAFA Board Meeting, two Committee meetings namely "SAFA Committee for Improvement, Transparency, Accountability and Governance (ITAG)" and "SAFA Committee on Harmonization of Fiscal and Tariff Regime" were held on 13 March 2012. Mr. Abbas Uddin Khan FCA, Member Council & Past President ICAB represented ICAB in the SAFA ITAG Committee meeting and Mr. Showkat Hossain FCA, Vice

President (T&R)-ICAB represented ICAB in the other Committee meeting.

ICAB delegates also participated the Inaugural Session of 53rd National Cost Convention titled "Sustainability Framework-Integrated Reporting, Imperative for CMAs" of ICWA India on 15 March 2012.

## ICAB Delegation Meets Commerce Minister

An ICAB delegation headed by Mr. Md. Syful Islam FCA, President, ICAB made a courtesy call on Mr. Ghulam Muhammed Quader, Hon'ble Minister, Ministry of Commerce, GoB at his office on 18 March 2012. Mr. Md Abdus Salam FCA, Vice President ICAB, Member Council & Past Presidents Mr. Sheikh A. Hafiz FCA, Mr. ASM Nayeem FCA, Mr. Abbas Uddin Khan FCA, Mr. M. Farhad Hussain FCA and Mr. N I Chowdhury FCA, Secretary-ICAB also accompanied the team. ICAB delegation discussed various concern related to accountants profession.



## Conference on "Demutualization of Stock Exchanges: Rationale, Practices and Road Map for Bangladesh"



The Institute of Chartered Accountants of Bangladesh (ICAB) organized a members' conference on "Demutualization of Stock Exchanges: Rationale, Country Practices and Road Map for Bangladesh" on 24 March 2012 at its auditorium.

Mr. Mohammed Farashuddin, former governor, Bangladesh Bank was the Chief Guest on the Conference. Mr. Md. Arif Khan FCMA, Member, Securities & Exchange Commission was present at the Conference as Special Guest while Mr. Md. Al Maruf Khan FCA, President, Chittagong Stock Exchange Ltd. was present as Panel Speaker. Mr. Jamaluddin Ahmed Ph.D, FCA, council member and former president, ICAB presented the keynote paper. The session of the conference was conducted by Mr. ASM Nayeem FCA, council member and former president, ICAB.

"The country will grow and the stock market will expand. So, there should be no reasons for the stockmarkets to lose their business because of demutualization", said Mr. Mohammed Farashuddin, former governor, Bangladesh Bank.

Delivering the address of welcome, Mr. Md. Syful Islam FCA, President, ICAB said that the demutualization of stock exchange is a recent experience in the economic world. Due to technological improvements and competitive environment changes, new opportunities alongside new threats have profound impact on stock markets. As an answer to these challenges, demutualization is a right step towards that.

## Conference on "Good Corporate Governance - a Tool for the Protection of Shareholder's Interest"



The Institute of Chartered Accountants of Bangladesh (ICAB) organized a Members' Conference on "Good Corporate Governance is a Tool for the Protection of Shareholder's Interest" on 31 March 2012 at ICAB auditorium.

Mr. Md. Abul Quasem, Deputy Governor, Bangladesh Bank was the Chief Guest at the Conference. Mr. Md. Matiul Islam FCA, Chairman, Industrial and Infrastructure Development Finance Company Ltd. (IIDFC) conducted the Session while, Mr. Akhter Matin Chaudhury FCA, Member Council presented the paper on the topic.

Mr. Md. Syful Islam FCA, President, ICAB delivered the address of welcome. Mr. Akhter Matin made few recommendations on proposed (draft) Corporate Governance Guidelines prepared by Securities and Exchange Commission of Bangladesh. As an important Stakeholders.

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