



Islamic Republic of Pakistan

**KHYBER PAKHTUNKHWA REVENUE MOBILIZATION AND PUBLIC RESOURCE
MANAGEMENT
(P162302)**

Fiduciary Systems Assessment

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ABBREVIATIONS AND ACRONYMS

ACA	Anti-Corruption Investigating Agency
ACE	Anti-Corruption Establishment
ACG	Anti-Corruption Guidelines
AGP	Auditor General of Pakistan
APPM	Accounting Policies and Procedures Manual
BER	Budget Execution Report
BP/OP	Bank Procedure/Operational Policy
CGA	Controller General of Accounts
CoA	Chart of Accounts
COFOG	Classification of the Functions of Government
DA	Designated Account
DAO	District Administrative Office
DFID	U.K. Department for International Development
DLI	Disbursement-Linked Indicator
ETNCD	Excise, Taxation, and Narcotics Control Department
FIA	Federal Investigating Agency
FM	Financial Management
FMIU	Financial Management Information Unit
FSA	Fiduciary Systems Assessment
GFS	Government Finance Statistics
GIZ	German Agency for International Cooperation (<i>Deutsche Gesellschaft für Internationale Zusammenarbeit</i>)
GoKP	Government of Khyber Pakhtunkhwa
IFR	Interim Financial Report
IPF	Investment Project Financing
IPSAS	International Public Sector Accounting Standards
IT	Information Technology
KP	Khyber Pakhtunkhwa
KPITB	Khyber Pakhtunkhwa Information Technology Board
KPPRA	Khyber Pakhtunkhwa Public Procurement Regulatory Authority
KPRA	Khyber Pakhtunkhwa Revenue Authority
MIS	Management Information System
MTBF	Medium-Term Budgetary Framework
MTEF	Medium-Term Expenditure Framework
MTFF	Medium-Term Fiscal Framework
NAB	National Accountability Bureau
NAM	New Accounting Model
NBP	National Bank of Pakistan
NFMIS	National Financial Management Information System
PAP	Program Action Plan

PCU	Project Coordination Unit
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PFMRS	Public Financial Management Reform Strategy
PIFRA	Project to Improve Financial Reporting and Auditing
PforR	Program-for-Results
QR	Quick Response
SBP	State Bank of Pakistan
SOP	Standard Operation Procedures
ST&IT	Science Technology and Information Technology
TA	Technical Assistance
TOR	Terms of Reference
TSA	Treasury Single Account
UIPT	Urban Immoveable Property Tax
USAID	U.S. Agency for International Development



Introduction

- 1. A Fiduciary Systems Assessment (FSA) of the Program was undertaken in accordance with World Bank Procedure/Operational Policy (BP/OP) 9.0 Program-for-Results (PforR) financing and using the PforR Guidance Note (June 30, 2017).** The assessment reviewed the fiduciary arrangements relevant to the Program in the Project Coordination Unit (PCU) established in the Finance Department, selected implementing agencies of the Government of Khyber Pakhtunkhwa (GoKP) (Finance Department, Planning and Development Department, and Excise, Taxation, and Narcotics Control Department [ETNCD]), including Khyber Pakhtunkhwa Revenue Authority (KPRA), and Khyber Pakhtunkhwa Information Technology Board (KPITB), which is an autonomous body, to determine whether these implementing agencies provide reasonable assurance that the Program financing proceeds will be used for intended purposes with due attention to the principles of economy, efficiency, effectiveness, transparency, and accountability.
- 2. The existing country systems are reasonably sufficient for the Program and the overall fiduciary risk is Substantial.** Implementing agencies have sufficient sanctioned positions for the budget and accounting staff to manage existing workload. There are however insufficient qualified accounting staff. Despite reasonable assurance of fiduciary safeguards, there are several residual risks to address. These measures build on those identified in the 2017 PEFA assessment. Based on the assessment, it is essential that the fiduciary-related activities listed in the Program Action Plan (PAP) are carried out to mitigate the identified risks. These measures are reinforced by relevant Disbursement-linked Indicators (DLIs) that will be monitored during Program implementation.
- 3. The legal and institutional structure for fraud and corruption prevention is satisfactory.** At the provincial level, Khyber Pakhtunkhwa (KP) Anti-Corruption Establishment (ACE) Rules of 1999 provide the legal framework for fraud and corruption. Any citizen can complain against any official to the ACE. Khyber Pakhtunkhwa the Government Servants (Efficiency and Discipline) Rules 2011 were promulgated under the authority vested in section 26 of the Khyber Pakhtunkhwa Civil Servants Act 1973 (Khyber Pakhtunkhwa Act No. XVIII of 1973). These rules govern internal accountability arrangements. The KP Right to Information Act 2013 provides for citizens' access to information in government departments.
- 4. The fiduciary risks identified in this document are consistent with the KP PEFA assessment report published in 2017.** The financial management (FM) element of the assessment identified certain capacity shortages and control weaknesses in the implementing entities. Challenges exist with respect to developing adequate FM professional capacity to manage financial matters for a program, especially given that it is the first PforR operation to be implemented by the GoKP. Vacant positions in FM in the proposed PCU need to be filled as well as an effective internal audit function established and gradually rolled out to cover the GoKP. Similarly, there would be an urgent need to enhance the professional capacity to effectively manage the procurement function in the PCU. On interim basis, the terms of references (TORs) of any of the existing procurement staff working on World Bank-funded projects could be enhanced to support the PCU in initial procurement action specifically for the technical assistance (TA) component. The Program will be subject to annual audit by the Auditor General of Pakistan (AGP) as the Supreme Audit Institution of the country. Audited Program financial statements shall be furnished to the World Bank within nine months of the end of each fiscal year.



5. **The GoKP transacts its business through a Treasury Single Account (TSA).** The Finance Department provides reliable information on commitment ceilings to the spending units through periodic releases of funds; however, spending units cannot initiate the procurement process until funds are released. Although in the last two years, these releases have happened periodically without significant delays, this sometimes results in non-utilization of budget amounts if the procurement process could not be completed before the close of the financial year.

Program Design and Expenditure Framework

The Government Program

6. **The overall government program is estimated to cost PKR 43,776 million (US\$330 million) during 2019–2023.** The following key entities are implementing the GoKP Program: the Finance Department, ETNCD, Planning and Development Department, Revenue and Estate Department, and Science Technology and Information Technology (ST&IT). The entities cover the full scope of core functions and activities needed to deliver the government’s program. The World Bank’s IDA resources (US\$118 million) will constitute 36 percent of the overall financing requirement to implement the government’s program (Table 1). The Program includes a separate disbursing TA implemented as an Investment Project Financing (IPF) for a total of US\$18 million. Funding for the Program will be provided through the GoKP’s annual budget and the Program funds will flow through the treasury system. Detailed program cost breakdown for the government program is shown in Tables 3–7.

Table 1: Summary of the GoKP Program Cost and Financing Sources

Source	Amount (US\$, millions)	% of Total
GoKP	212	64
IDA	118	36
Other development partners	—	—
Total	330	100

The Program (PforR) Boundary and Expenditure Framework

7. **The Program (PforR) is derived from the six policy areas of the Public Financial Management Reform Strategy (PFMRS).** The proposed Program comprises a modest selection of key elements of the GoKP’s PFMRS identified from each of the six policy areas. The selection of the areas which the Program will support is based on the GoKP’s own prioritization, the potential for high impact, and the World Bank’s own potential to add the most value in terms of technical expertise and sharing of international good practices in revenue mobilization and public resource management. These areas also expand specific areas of engagement under other World Bank operations, notably the Governance and Policy Project and support from other development partners, for example, the U.K. Department for International Development (DFID), German Agency for International Cooperation (*Deutsche Gesellschaft für Internationale Zusammenarbeit*, GIZ), and U.S. Agency for International Development (USAID). Implementation of the government program primarily requires compensation of staff, operating expenses of the five implementing entities, as well as repairs and maintenance costs. These, together, constitute recurrent spending of the entities.



8. **The Program Expenditure Framework is defined as the total estimated recurrent spending by the five entities implementing the PFMRs.** The expenditure boundary for the Program is, therefore, defined as the total estimated recurrent spending by these five entities over the Program duration of 2019–2023. The expenditures are derived from the GoKP’s three-year Medium-Term Expenditure Framework (MTEF) projections plus two forward years. The government expenditure lines affected by these recurrent spending are employee-related expenses, retirement benefits, operating expenses, and repairs and maintenance. This equates to US\$157 million and will be financed through an IDA credit of US\$100 million (Table 2). The Program is a modest part of the GoKP’s broader effort to improve public financial management (PFM). The Program will incentivize the GoKP at various stages of implementing the PFMRs and provide support for accelerating these reforms in the implementation period. The recurrent expenditures under the five agencies, namely the Finance Department, ETNCD, Planning and Development Department, Revenue and Estate Department, and ST&IT, will be used to determine if the overall expenditure at the Program closure is equal to or less than the total IDA financing for the Program. Detailed breakdown of the Program Expenditure Framework is shown in Tables 7 and 8.

9. **The Program will use normal budget procedures of the GoKP.** These procedures are well defined, and expenditures are tracked using the New Accounting Model (NAM) Chart of Accounts (CoA). The budgeting of the Program expenditures will constitute part of the government budgeting process. The funds for the Program will be appropriated from both current and development sides of the provincial budget.

Table 2: Summary of the Program (PforR) Expenditure Framework and Sources

Source	Amount (US\$ millions)	% of Total
GoKP	57	36
IDA (PforR)	100	64
Other development partners	—	—
Total	157	100

Table 3: Overall GoKP Program Cost by Department (PKR millions)

Department	FY18–19	FY19–20	FY20–21	FY21–22	FY22–23	TOTAL
ETNCD (including KPRA)*	1,339	1,425	1,372	1,455	1,560	7,151
Finance	3,676	4,003	4,426	4,944	2,051	19,100
Planning and Development	2,820	1,364	645	519	545	5,893
Revenue and Estate	1,884	1,824	1,909	1,857	1,694	9,168
ST&IT (KPITB)	515	440	470	502	537	2,464
Grand Total	10,234	9,056	8,822	9,277	6,387	43,776



Table 4: Overall GoKP Program Cost by Department (US\$ millions)

Department	FY18–19	FY19–20	FY20–21	FY21–22	FY22–23	TOTAL
ETNCD	10.10	10.75	10.35	10.97	11.77	53.94
Finance	27.73	30.20	33.40	37.31	15.48	144.12
Planning and Development	21.28	10.29	4.87	3.92	4.11	44.47
Revenue and Estate	14.22	13.76	14.41	14.01	12.79	69.19
ST&IT (KPITB)	3.89	3.32	3.55	3.79	4.05	18.60
Total	77.22	68.33	66.57	70.00	48.20	330.32

Note: Exchange Rate: US\$1 = PKR 132.50 (as of November 2, 2018).

Table 5: Overall Government program, by Object Description (PKR millions), per FY

Major Object Description	FY18–19	FY19–20	FY20–21	FY21–22	FY22–23	Total
A01: Employee-related expenses	2,529	2,584	2,644	2,707	2,771	13,235
A02: Project pre-investment analysis	—	—	—	—	—	—
A03: Operating expenses	1,088	1,218	1,364	1,527	1,682	6,879
A04: Employee retirement benefits	70	78	87	98	109	442
A05: Grants, subsidies/write-off loans	508	569	637	713	799	3,226
A06: Transfers	74	82	92	103	116	467
A09: Physical assets	57	64	72	80	90	363
A13: Repairs and maintenance	36	40	45	50	56	227
A14: Development/Capital	5,872	4,421	3,880	3,998	765	18,936
Total (PKR, millions)	10,234	9,056	8,821	9,276	6,388	43,775
Total (US\$, millions)	77.23	68.34	66.58	70.01	48.21	330.37

Note: Exchange Rate: US\$1 = PKR 132.50 (as of November 2, 2018).

Table 6: Program (PforR) Program Boundaries (PKR, millions)

Major Object Description	FY18–19	FY19–20	FY20–21	FY21–22	FY22–23	Total
A01: Employee-related expenses	2,529	2,584	2,644	2,707	2,771	13,235
A03: Operating expenses	1,088	1,218	1,364	1,527	1,682	6,879
A04: Employee retirement benefits	70	78	87	98	109	442
A13: Repairs and maintenance	36	40	45	50	56	227
Total	3,723	3,920	4,140	4,382	4,618	20,783

Note: Exchange Rate: US\$1 = PKR 132.50 (as of November 2, 2018).

Table 7: Program (PforR) Program Boundaries (US\$, millions)

Major Object Description	FY18–19	FY19–20	FY20–21	FY21–22	FY22–23	Total
A01: Employee-related expenses	19.1	19.5	20.0	20.4	20.9	99.9
A03: Operating expenses	8.2	9.2	10.3	11.5	12.7	51.9
A04: Employee retirement benefits	0.5	0.6	0.7	0.7	0.8	3.3
A13: Repairs and maintenance	0.3	0.3	0.3	0.4	0.4	1.7
Total	28.1	29.6	31.3	33	34.8	156.8

Note: Exchange Rate: US\$1 = PKR 132.50 (as of November 2, 2018).



Institutional and Legal Framework for Financial Management

Country Issues Related to Public Financial Management System

10. **Pakistan has a three-tier governance infrastructure for PFM that operates through the federal, provincial, and district government(s).** The Finance Ministry/Department and the line ministries/departments at the federal and provincial levels have well-defined roles and responsibilities for budget formulation and execution. The Controller General of Accounts (CGA), a representative of the federal government, through its associated offices across the country, preaudits the transactions, makes payments, and thereafter, prepares financial statements. The AGP, being the Supreme Audit Institution of the country, is bestowed by the Constitution to conduct audit of federal, provincial, and district government entities. The KP PEFA was carried out in 2017 report, a follow-up of the 2007 PEFA. The PEFA confirmed the results of the Public Financial Management and Accountability Assessment of Federal Government (2012). Both assessments noted significant progress as a result of ongoing reforms for improving the PFM system in the country.

11. **The budget formulation and execution is based on administrative, economic, and subnational classification using government finance statistics (GFS)/United Nations Classification of the Functions of Government (COFOG).** Transfers from the federal government to the provincial governments are transparent and governed by rules settled under the Constitution. Accounting and financial reporting have been automated at the federal, provincial, and district levels through the nationwide implementation of the National Financial Management Information System (NFMIS) using the SAP application with a uniform CoA.¹ Connectivity is in place for all line ministries/departments to monitor budget execution on a real-time basis. Fiscal reports and the CoA used by the federal and provincial governments are the same. The NFMIS produces fiscal reports within two months from the end of fiscal year-end. The report indicates that local and foreign debt are properly recorded, reconciled, and reported.

12. **Payroll is backed by personnel files containing all information pertaining to payroll master data.** Changes to payroll information in the NFMIS are fully supported by the relevant documentation. The GoKP has introduced Medium-Term Budgetary Framework (MTBF) reforms focusing on introduction of multiyear planning and budgeting preparation for at least three years on a rolling basis. The MTBF reforms will help the provincial government in prioritizing its expenditures. Accounting system of the provincial government provides complete and reliable information about resources received by the Finance Department, Planning and Development Department, ETNCD, Board of Revenue, and their respective field offices. Financial statements of the federal and provincial governments are being prepared under cash basis of accounting and are aligned with the format given by the International Public Sector Accounting Standards (IPSAS) 'cash basis'. Annual audits reports of the GoKP for FY13–14 to FY16–17 have not been received by the KP Provincial Assembly. The progress on transparency through public availability of financial information is also noteworthy.

13. **The assessment identified certain areas for improvement to achieve better PFM outcomes.** For improved budget credibility, the government needs to institutionalize the MTBF. For better expenditure control, the commitment accounting functionality available within the NFMIS needs to be utilized. The

¹ International Monetary Fund - Government Financial Statistics Manual 1986.



GoKP also needs to develop and implement an effective internal audit function with regular reporting for follow-up management actions, and continuing efforts are needed to improve effectiveness of tax collection and the management of cash balances affecting the predictability of availability of funds.

Budgeting and Planning

14. The budgeting of the Program expenditures will constitute part of the GoKP budgeting process.

The funds for the Program will be appropriated from both the current and development provincial budgets. The GoKP has a well-defined budgeting process and introduced output-based budgeting on pilot basis in 2011 which was extended to all the line departments and further reforms are under way to introduce modern practices in financial planning and budgeting. It has also taken measures to link policy planning to budgeting, improving transparency, and fostering accountability. The Medium-Term Fiscal Framework (MTFF) and MTBF provides three-year estimates by administrative, economic, and functional classification.

15. Although the MTBF has been introduced, the current (recurrent) budget managed by the Finance Department and the development (investment) budget by the Planning and Development Department remain separate streams.

During the budget formulation stage, the development budget is presented in a single line rather than the expenditure categories according to the CoA. The information provision in MTFF is quite robust; however, the application in terms of performance evaluation of the service delivery departments based on information provided, needs attention. The Monitoring and Evaluation (M&E) Directorate (within the Planning and Development Department) provides monitoring reports while impact evaluation studies have been piloted recently funded by development partners. All the participating departments follow the Budget Call Circular and Annual Development Program guidelines issued by the Finance Department and the Planning and Development Department, respectively.

16. The budgetary creditability of the GoKP, as indicated by 2017 GoKP PEFA, shows an improvement regarding the extent of deviation on the aggregate level for revenue and expenditure outturns.

However, no progress has been observed on the introduction of measures to prepare and record consolidated expenditure payment arrears which provide an outlook of unsettled expenditure obligations of the government. However, while reviewing the budget utilization report of the Program implementing entities, low utilization rates were noted for the KPITB, ETNCD, and the Board of Revenue. The discussion with the relevant parties revealed that the main reasons are stemming from the overestimation of budget figures.

17. For the Program, the implementing agencies are yet to initiate the planning process for detailed implementation plan and cost estimates to be finalized.

It is imperative for the Program's success that the implementing agencies finalize and obtain approved implementation plans before the close of FY18–19. The PCU will prepare annual budgets based on their work plans. The budgets will follow applicable government/entity budgeting guideline and will be reflected in the government systems indicating the budget sanctions for the fiscal year.



Table 8: Development Budget Utilization (%)

Budget Entity	FY16–17	FY17–18
Finance Department	30	90
Planning and Development Department	19	27
Revenue and Estate Department	35	98
ETNCD (including KPRA)	15	26
Local government	81	75
KPITB	71	25

Fraud and Corruption

Legal and Institutional Context

18. **In Pakistan, there is an established anti-corruption framework comprising enabling legislation, anti-corruption investigating agencies (ACAs), and a dedicated anti-corruption court system.** Enabling anti-corruption legislation dates as far back as 1860. At the federal level, the Federal Investigation Agency (FIA) has its roots in the Special Police Establishment created in 1942 to investigate corruption in the Supplies and Procurement Department of the Government of India. In 1999, the National Accountability Bureau (NAB) was established to investigate major corruption cases; in 2010, the Competition Commission of Pakistan was established as a watchdog to fight anti-competitive practices, including collusion in procurement, in the private sector. All the four provinces have ACEs. Additionally, there are single-mandate and general-mandate ombudsmen both at the federal and provincial levels.

19. **After the inception of the Special Police Establishment at the center and ACE at the provincial levels, the ACE West Pakistan was reorganized in June 1956.** To provide procedural modalities, constitution, functions, duties, and powers, the West Pakistan Anti-Corruption Ordinance, was promulgated in 1961. According to this ordinance, the director was designated to be the head of this Establishment in each province, assisted by sufficient number of assistant directors crimes/legal and technical officers. The other codal formalities for prosecution of cases are governed by Criminal Law Amendment Act 1958. In the same pattern, the provincial ACE was established in erstwhile North West Frontier Province (renamed Khyber Pakhtunkhwa) in 1971. During 1999, the GoKP replaced the West Pakistan ACE Rules 1965 by KP ACE Rules 1999, notified vide No. SOS-III(S&GAD)4(6)/98, dated December 15, 1999. This Establishment performs its functions within the abovementioned legal framework.

20. **Any citizen can complain against any official to the ACE.** Complaints are received simultaneously at the headquarters, regional, and district levels. However, as a precautionary measure, a Standard Operation Procedures (SOP) has been designed to ascertain the identity of the complainant or informer and genuineness of the complaint/information. This is to eliminate the element of blackmailing of public servants and to entertain only genuine complaints. According to the SOPs, the assistant director (Complaint) after hearing the complainants, recommends the initiation of an enquiry or forwards this to the departments concerned, or files the complaints as baseless, devoid of evidence/beyond jurisdiction, and so on.

21. **In 2011, the Khyber Pakhtunkhwa Government Servants (Efficiency and Discipline) Rules 2011 were promulgated under the authority vested in section 26 of the Khyber Pakhtunkhwa Civil Servants**



Act 1973 (Khyber Pakhtunkhwa Act No. XVIII of 1973). On the administrative side, these Rules govern internal accountability arrangements. Officials can be penalized if charged with corruption or even with the reputation of being corrupt. Penalties range from fines to dismissal from service. Appeals against the administrative order are heard under the Service Tribunals Act 1974 before the KP Services Tribunal. The Office of the Ombudsman provides a forum for the protection of people’s rights against maladministration and corrupt practices by public servants.

22. **The KP Right to Information Act 2013 was passed by the provincial legislature with the objective to ensure the access of citizens to information in government departments and thus create a transparent and corruption-free environment conducive for the growth of democracy.** The Right to Information Act together with KP Prevention of Conflict of Interest Act 2016, whereby clear conflict of interest and related post-employment principles for public office holders, have been established to prevent and minimize the possibility of conflicts arising between the private interests and public duties of public office holders in the province. They represent one of KP's most critical achievements in the fight against corruption. Under the provisions of the Right to Information Act, any citizen may request information from a ‘public body’ which is required to reply expeditiously or within 15 days. The Act also requires every public authority to computerize their records for wide dissemination and to proactively publish certain categories of information for easy citizen access. The establishment of an independent Information Commission will also help fight corruption. The Commission will deliver decisions instructing the government, courts, universities, police, and departments on how to share information of public interest. The protection of whistleblower under section 30 is a noteworthy provision.

Application of Anti-Corruption Guidelines Under the Program

23. **The GoKP’s anti-corruption framework has all the essential ingredients to address corruption issues related to the Program.** The implementing agencies of the Program are all governed by the civil and criminal administrative arrangements described earlier. In addition, the borrower will implement the Program in accordance with the provisions of the Anti-Corruption Guidelines (ACG) applicable to PforR operations. The modalities for implementing the ACG include the following:

- (a) All fraud and corruption complaints will be aggregated through three mechanisms. First, a management information system (MIS) is to be maintained by the executing agency/implementing agencies for administrative discipline and efficiency inquiries, including any procurement corruption charges related to the Program. Second, the ACE already aggregates and categorizes all complaints. Third, the Secretary Finance will process, through the relevant administrative authorities, any Program-related procurement corruption complaints that may be received.
- (b) The Office of the Secretary Finance will be the GoKP’s focal office for the purposes of ACG application. It will also aggregate Program-related procurement corruption complaints by monitoring the MIS of administrative inquiries and by maintaining liaison with the ACE.
- (c) The GoKP will undertake investigations, criminal and administrative, under the Program, of all material and credible allegations of fraud and corruption and keep the World Bank abreast of their progress and findings and make the conclusions public.



- (d) The GoKP will provide the World Bank with reports annually or more frequently as warranted, reporting allegations of fraud and corruption under the Program received and registered, as well as related investigations and, as needed, the actions taken. Reciprocally, if the World Bank finds evidence of corrupt practices, the World Bank will, to the extent consistent with World Bank policy, refer the case to the GoKP for investigation under the relevant criminal and civil laws.
- (e) If the World Bank determines to conduct an administrative review into allegations or other indications of fraud and corruption in connection with the Program, conducted alone, together or in parallel with the government investigation, the GoKP will cooperate fully with representatives of the World Bank and take all appropriate measures to ensure the full cooperation of relevant persons and entities subject to the government jurisdiction in such investigation, including in each case, allowing the World Bank to meet with relevant persons and to inspect all of their relevant accounts, records, and other documents and have them audited by or on behalf of the World Bank. If the World Bank finds evidence of corrupt practices, the World Bank will refer the case to the GoKP for investigation under the relevant criminal and civil laws. The World Bank may, however, debar private individuals and firms on its own.
- (f) The World Bank's right to investigate or conduct review does not extend to criminal investigations, which is the exclusive jurisdiction of the GoKP.
- (g) The GoKP will ensure that any person or entity debarred or suspended by the World Bank is not awarded a contract under or otherwise allowed to participate in the Program during the period of such debarment or suspension.
- (h) The bidding documents will serve as bidders' source of information regarding the applicability of the ACG to the Program. Compliance will be verified through the Program's annual audits.

Fiduciary Capacity

24. **A fiduciary assessment was conducted of the Finance Department, Planning and Development Department, ETNCD, including the KPRA and KPITB.** The implementing agencies have sufficient sanctioned positions for the budget and accounting staff to manage the existing workload. As for the TA component, a PCU will be formed to manage the component and to coordinate the work of the implementing entities under the PforR. It is envisaged that a qualified procurement specialist, internal auditor in addition to one senior financial officer, and one accountant will be appointed to work in the PCU with other technical and monitoring team. The implementing agencies of the Program will have their required dedicated and qualified FM and procurement specialists so that financial reporting and procurement plans/processes are streamlined. It would also be helpful to draw FM and procurement specialists from the pool of civil servants that are currently undergoing FM and procurement certification program under the parallel World Bank-financed Governance and Policy Program.

25. **The recommended mitigating measures according to Table 11 are anticipated to build experience and skills that will outlast the Program itself and spill over into improved FM in KP.** The



measures are focused to prioritize the key themes highlighted in the 2017 PEFA assessment and to bolster/strengthen capacity in these areas under this Program.

26. **The use of Project to Improve Financial Reporting and Auditing (PIFRA) Integrated Financial Management Information System in producing program-level financial statements will also benefit FM in the province and the lessons learned will bolster the use of the system going forward.** In this regard and as agreed with the Finance Department, a separate fund code and object codes will be created for the Program by which the program-related receipts and expenditures could be captured.

Accounting and Reporting

27. **It was observed by the KP 2017 PEFA that the government has sound accounting, recording, and reporting procedures in place.** The GoKP has adopted the budget classification, accounting, and reporting framework of the Government of Pakistan. The Provincial Auditor General Office, an extension of the CGA, provides the accounting and financial reporting support to the GoKP. The Provincial Auditor General Office is supported by the District Administrative Office (DAOs). However, as highlighted, a significant amount of public funds lies in commercial banks outside of the TSA—one of the main issues in cash management the proposed Program seeks to address.

28. **The NFMIS connectivity, which allows easy access to information on budgetary resources available and consumed, has been provided to all the line departments with the exception of the ETNCD and KPRA which use manual systems internally,** but payments are authorized by the Accountant General Khyber Pakhtunkhwa. Accounting across the implementing agencies relates to the recording of the financial transactions pertaining to purchases and disposal of fixed assets, services and supplies, payroll, advances to employees and vendors, payments to contractors under development works, including tax withholding from payments and day-to-day operational expenses through petty cash transactions.

29. **Each implementing agency will maintain its own books of accounts for the program-related activities on a cash basis, using the government’s accounting policies and procedures, which also include a GFS-compliant CoA collectively called the NAM.** The accounting and reporting of each implementing agency uses the SAP system implemented under the PIFRA Project and carry out monthly expenditure reconciliation, as part of the monthly Budget Execution Report (BER) process with the Accountant General Khyber Pakhtunkhwa.

30. **The Financial Management Information Unit (FMIU) established in the Finance Department is responsible for electronic processing of data (budget, releases, accounts, rules, receipts, and others).** The information retrieved/accessed instantly facilitates decision making and brings efficiency and transparency in FM. The Unit has established a province-wide network between the Finance Department, 26 District Finance Departments, and major line departments. The provincial and districts’ budgets are available online. Releases are also online, and expenditure is updated online. Budget and expenditure are monitored in real time. The FMIU is also responsible for the compilation and printing of the following budget-related books in financial year.

31. **The KPITB, as an autonomous body, maintains its own accounting system, which is off-the-shelf.** The system was assessed and found satisfactory in conducting accounting and reporting transactions. As for the KPRA, it does not have access to SAP and uses manual records to record transactions. It is



recommended though that the KPRA and KPITB are connected to the SAP system to harmonize the accounting and reporting of the program.

32. **The PCU, as the coordination agency, will be responsible for recording the transactions pertaining to the TA component.** The PCU will also prepare and submit to the World Bank biannual interim financial reports (IFRs) for the TA component. The PCU will also be responsible for coordinating the timely annual audit of the program-level annual financial statements that will be shared with the World Bank. The program-level reporting will require close coordination between the PCU and the implementing departments.

Financial Reporting and Funds Flow and Disbursement Mechanism

33. **The IDA funds of the Program will be channeled to the GoKP Non-Food Account-1 through the State Bank of Pakistan (SBP) in accordance with the procedure notified by the Ministry of Finance (MoF) Government of Pakistan in August 2013.** Disbursement of Program funds will be made twice a year only upon achievement of the DLIs. Upon achievement of indicators, the PCU at the Finance Department of the GoKP will report to the World Bank and provide necessary evidence according to the legal agreements, as a justification that results for DLI(s) have been met. In the case of a scalable DLI, the amount to be disbursed will be determined in accordance with the formula set forth in the verification arrangement. A notification will be sent to the borrower to advise the amount to be disbursed against progress achieved toward the results of the scalable DLI. Disbursement requests will be submitted to the World Bank using the World Bank's standard disbursement forms signed jointly by authorized signatories. Details of the key disbursement issues will be spelled out in the Disbursement Letter. It is important to note that although PforR operations do not link disbursements to individual expenditure transactions, the aggregate disbursements under such operations should not exceed the total expenditures by the borrower under the Program over its implementation period. If by Program completion the financing disbursed exceeds the total amount of the Program expenditures, then the Finance Department of the GoKP is required to refund the difference to the World Bank.

34. **For the TA component, a Designated Account (DA) will be opened in U.S. dollars for the PCU.** This will be done in accordance with agreed procedures for Operation and Maintenance of the Revolving Fund/DA issued by the Finance Division, Ministry of Finance, Government of Pakistan to receive funds for the World Bank's eligible share of financing. The IDA funds will be disbursed to the DA in U.S. dollars using reporting disbursement method based on the submission of semester IFRs prepared by the PCU.

Procurement Systems Assessment

35. **Procurement regulatory reforms play a pivotal role in enhancing effectiveness of 'public investment management' in areas of capital expenditure.** This includes expenditure on physical infrastructure (for example, roads, and government buildings) and soft infrastructure (for example, human capital development, innovation support, and research and development). These in general facilitate strategic budget management and are an integral component of the overall PFM promoting value for money and transparency and aid in thwarting corruption. KP has witnessed regulatory governance activism in the past couple of years and as a result, the KP Provincial Assembly passed the Public Procurement Regulatory Authority bill on September 3, 2012, which became an Act on September 16, 2012, vide Notification No. PA/Khyber Pakhtunkhwa/Bill/2012/6059, dated September 20, 2012.



36. **The KP Public Procurement Regulatory Authority (KPPRA) has initiated many substantive measures to establish a procurement regulatory regime.** These arrangements contribute toward transparent, economic, efficient, traceable, and accountable procurements undertaken through public funds, incorporating fit-for-purpose procurement approaches. The procurement regulatory regime has been further strengthened by the removal of editorial conflicts, deficiencies, and inconsistencies and introducing some minor modifications in existing rules and, wherever possible, to render them more contextually relevant.

37. **Procurement planning is a key function in public sector organizations.** Its objective is to provide the line departments with continuity of inputs (procurements) to enable them to achieve strategic objectives. Within the framework of the annual procurement plan, this is the stage in the process when the objectives of making procurement are considered in relation to stakeholder needs and when a planned approach to the procurement is set out. Procurement-level plan could also involve cooperation with other procuring entities.

38. **Although the KPPRA presently hosts 168 procurement plans of different entities, the key issue is the lack of robust procurement planning framework.** It has to be understood that procurement regulation covers both recurrent and developmental expenditure and as such, the alignment with budget initiation and procurement planning is possible. The deficiencies in budget making impair the development of procurement plans. An annual procurement plan is also the first step in the procurement planning process. Ideally, the relationship that the procurement officers have with the user and budget departments should be so close that they are involved at an early stage of the budget cycle, where departments are identifying their needs in the respective budget year.

39. **Stakeholders, the Finance Department, and the procurement team work in isolation, unaware of each other’s needs.** Economies of scale are lost because the requirements of different areas would be processed separately. Resource scheduling becomes difficult. Periodic indicative notices would not be published as easily.

Institutional Arrangements

Staffing Arrangements

40. **The staffing requirements for each entity depends on the role which the entity is expected to play during the life of the Program.** Table 9 provides a brief assessment of the staffing requirements of the entities.

Table 9: Procurement Staffing Needs Assessment

Parameters	PCU-Finance Department	KPITB	Board of Revenue	KPRA	KPPRA	ETNCD
Is there sufficient expertise on the strategic plan implementation?	Yes	Yes	Yes	Yes	Yes	Limited
Is the staff strength adequate	Yes	Not relevant	Yes	Excess - 45 persons	Yes	Yes



Parameters	PCU-Finance Department	KPITB	Board of Revenue	KPRA	KPPRA	ETNCD
for current functions?				employed in accounts and finance		
Would additional staff be required to cater to PforR activities?	Yes. (a) Procurement specialists, (b) one contract administration specialist with information technology (IT) background, and (c) one FM specialist	(a) Procurement specialist and (b) one contract administration specialist with IT background	Procurement specialists; MS	(a) Procurement specialist and (b) one contract administration specialist with IT background	None	Procurement specialist
Will the staff require training and coaching during the Program?	Yes	Yes	Yes	Yes	Yes	Yes

Procurement Documentation

41. **Bids/proposals are consistently advertised in national daily newspapers and uploaded on the KPPRA websites and are easily accessible to potential bidders and consultants.** The following procurement documents are in use by the procuring entities in KP: Standard Bidding Documents for Procurement of Works (large contracts); Standard Bidding Documents for Procurement of Works (small contracts); Standard Bidding Documents for Procurement of Goods (large procurements); Standard Bidding Documents for Procurement of Goods (small procurements); and Standard Bidding Documents for Services containing instructions to bidders, (pre-)qualification, short-listing, and evaluation criteria.

42. **Timely and non-ambiguous clarifications to bidding/proposal documents are provided to all potential bidders in pre-bid meetings or pre-proposal conferences.** Mostly bidders attend in person—otherwise bidders send email/facsimiles which are responded to. The bid documents are made available to all interested bidders without prescribing any preconditions. However, there is room for simplification, enhancing transparency by creating links to key aspects of Regulations, including content on fraud and corruption and complaint management. These documents are largely drawn from bidding documents generally drafted by various international financial institutions. The KP’s regulatory activism, particularly related to procurement and contract management, is prototypical in Pakistan. It would be helpful to turn these regulatory provisions into actions through their incorporation in bidding documents



Review of Procurement Decisions and Resolution of Complaints

43. Complaints are reported to be rare; however, redress is provided through provisions of KPPRA-2012. The complaint management system has a formal structure. The grievance redress decisions are transparently published on the KPPRA website (<http://kppra.gov.pk/complaint-grivences/>).

Contract Management and Administration

44. Adequate mechanisms are in place for procurement and/or contract monitoring. The supplies and payments generally follow the time periods agreed in the contract agreement.

Table 10: Procurement Profiling for Program

Indicator	Expenditure	Cost (US\$)	Responsible Implementing Entity	Procurement Complexity	Risk
Database Integration in Tax Administration	2 blade servers (with required licensing; 1 data warehouse tool (with required licensing)	US\$1.5 to US\$2 million (approximately)	KPRA	M	M
Business processes for tax administration simplified and harmonized	No hardware and no services will be procured	0	KPRA	H	H
Cities with UIPT survey, valuation and digitized records	Services of a firm who will carry out the valuation	US\$4 million (approximately)	E&TD	M	H
TMAAs using NFMS to record transactions	SAP licenses, desktops, UPS, printers, connectivity and generators; training	US\$3 million (approximately)	Planning and Development Department supported by Finance Department	H	H

Note: H = High; M = Moderate.

Internal Controls and Internal Audits

45. **In KP, the accounting, reporting, and internal controls framework is supported with the following instruments:** Manual of Accounting Practices complemented with guidelines, handbook, and manuals for accounting and reporting; General Financial Rules; GoKP Rules of Business; Supplementary and Treasury Rules; Delegation of Financial Power Rules; Procedure for Assignment Account and Revolving Fund Accounts; KP Internal Audit Charter; and Public Procurement Rules, which will be observed for Program expenditure. Further, as stipulated in the Treasury rules and Accounting Policies and Procedures Manual (APPM), the National Bank of Pakistan (NBP) issues a daily return including the scroll and supporting evidence to the DAOs. For the DAO, the APPM stipulates daily checking of the bank scroll/return and monthly reconciliation of accounts. Moreover, segregation of duties has been comprehensively stipulated in General Financial Rules and APPM for authorization, recording, custody of assets, and reconciliation or audit. Most of these regulations were enacted a few decades ago and have undergone several revisions from time to time.



46. **Internal audit cells are established in the 11 line departments under the Internal Audit Charter, approved by the provincial cabinet.** Annual internal audit programs were developed with the assistance from a donor agency; however, lack of staff ability affected the implementation of the internal audit programs. The KP 2017 PEFA assessment reports that the controls are comprehensive, but issues remain with its application and same set of rules and regulations prevail; these are often excessive and mostly lead to operational delays. It has further been noted that the departmental internal audit teams do not work under clear ToR/work plan and are not qualified in the field of accountancy and auditing; they are mostly technical staff.

47. **The assessment of implementing agencies identified the following areas where internal controls need to be further improved:**

- Establishing an effective internal audit function that is either absent or is limited to preaudit.
- Improving reporting and reconciliation controls with periodic review by the senior management, which at present is an activity of the budget section of the implementing agencies.
- Strengthening asset management including asset coding, periodical physical verification, documentation of custodian's responsibilities for asset safeguard, and exercising strong controls over assets receipt and issuance. The KPITB, however, has a satisfactory inventory and asset management system with proper controls on the incoming and outgoing items as well as the Quick Response (QR) tagging system.
- Establishing a plan for periodic payroll audit across the Program.

Internal Auditing Arrangements for the Program

48. **The PAP will include several action points for the improvement of the nascent audit function in KP during the first two years.** During the first two years of the Program and until the action points mentioned earlier are implemented to render a reliable internal audit function, the Program will apply the same internal audit arrangements used for the KP Governance and Policy Project (through which a firm has been hired to carry out internal audit of the Project), which is financed by the World Bank through a Multi-Donor Trust Fund and has internal audit arrangements covering the Finance Department and the Planning and Development Department. The PAP actions include

- Hiring sufficient internal auditors who possess the relevant education background and experience in the internal audit cadre of KP in the implementing agencies; and
- Developing an annual internal audit plan based on the risk-based approach to review the controls of high-risk operations on quarterly basis and provide audit report and recommendations to the respective line departments and the Finance Department. The plan should also ensure that timely follow-up and advice are provided to the respective departments to address internal audit issues.



49. **For the PCU, a qualified senior financial officer (who will report to the PCU director) and one accountant will be appointed.** The accountant will be responsible for the preparation of the IFR for this component, which will also be reviewed by the financial office and approved by the PCU Program Director. It is advised that IFRs are generated through the SAP system as opposed to manual records.

Program External Audit

50. **The AGP adopted the Financial Audit Manual in 2006 (amended in 2010) that incorporates standards of International Standards of Supreme Audit Institutions.** In the KP 2017 PEFA assessment, the external audit function was rated 'D+' owing to low audit coverage. For the provincial government, the audit reports up to FY14–15 have been submitted to the legislature. The AGP has recently completed the audit of the implementing agencies up to FY16–17, and there are no significant audit observations that are unresolved or that have been reported to the Public Accounts Committee (PAC).

51. **Auditing arrangements of the Program.** The PCU will be responsible for coordinating with the implementing agencies for consolidating program financial statements. The audit of the Program's financial statements as well as the TA component will be carried out by the Department of AGP, acceptable to the World Bank. The auditor will express an opinion on the Program's annual financial statements and will also issue a management letter highlighting internal control, compliance, and other weaknesses. For each financial year, the AGP will audit the Program's financial statements and that will be submitted to the World Bank within nine months of the close of the financial year. The World Bank, in accordance with its Access to Information Policy, will request for public disclosure of the audit report.

Fiduciary Risks and Mitigation Measures

52. Based on the abovementioned reasons, the overall fiduciary risk assessed for this Program is classified as Substantial. Overall, the Fiduciary Assessment concludes that the examined program FM and procurement systems are adequate to provide reasonable assurance that the financing proceeds will be used for intended purposes, with due attention to the principles of economy, efficiency, effectiveness, transparency, and accountability, and for safeguarding program assets once the proposed mitigation measures have been implemented.



Table 11: FM and Procurement Risks and Mitigation Measures

Risk Area	Proposed Mitigation	Baseline	Risk Rating before Mitigation Measures	Mitigating Measures/Monitoring Benchmark	Risk Rating after Mitigation Measures
Planning and budgeting	<p>Implementation/budget plans for the Program with detailed costing and timelines developed by the implementing agencies</p> <p>Annual budget allocations for the Program made in accordance with the implementation plan</p>	<p>No plans available</p> <p>FY18–19 budget in preparation</p>	Substantial	<p>Implementation/budget plan approved by the respective secretaries/chairmen</p> <p>Procurement plans of implementing entities copied to the PCU Finance Department</p> <p>Allocation for the Program activities in the annual budget through budget appropriation FY18–19 budget and onward through annual development budget</p>	Moderate
Funds flow	Funds committed for the Program activities in annual budget released to the implementing entities in time	Nil	Moderate	Quarterly BERs	Moderate
FM capacity	<p>The FM units of the implementing agencies working at sanctioned strength</p> <p>Additional staff requirement for the PCU to be finalized and staff to be hired</p>	Vacancies in the PCU at the Finance Department to be filled	High	Qualified staff are appointed to manage FM activities by project negotiation.	Substantial
Accounting and reporting	Process of preparing Program-level financial reports and entities to be included in the reports to be finalized	Nil	Moderate	Program-level financial reporting arrangements will be the responsibility of the implementing entities and the PCU. Periodic Program-level financial reports will be prepared and reviewed by the PCU team and semiannual IFRs will be shared with the World Bank.	Moderate



Risk Area	Proposed Mitigation	Baseline	Risk Rating before Mitigation Measures	Mitigating Measures/Monitoring Benchmark	Risk Rating after Mitigation Measures
Internal controls	<p>Ensuring internal audit function has qualified staff, works according to an audit plan, and follows international standards</p> <p>Internal audit to prioritize reviews aimed at (a) improving reporting and reconciliation controls; (b) strengthening asset management</p>	<p>Nil</p> <p>Nil</p>	Substantial	<p>The PAP will include certain action points in this regard and interim arrangements will be in place.</p> <p>Qualified internal auditors will be appointed and conduct their work according to a clear annual risk-based plan for the implementing entities.</p>	Moderate
Program audit	Program external audits carried out on time	Nil	Moderate	Program audited financial statements available within six months after the close of the financial year	Moderate
Procurement					
Regulatory	Only principle-based exceptions resorted to for procurements related to the Program	Nil	Substantial	The World Bank will review reports of such expectations to reassess any mitigation measures.	Moderate
Oversight	Complaint Management System is consistently implemented	Most entities do have a compliance centered system in place	Moderate	Procurement complaint management system provides reasonable assurance to private sector per review	Low
Documentation	(a) Program-specific bidding documents for all the implementing entities under PforR until KPPRA completes its review and revamps and notifies Standard Bidding Documents and standard request for proposal SRFPs which the World Bank will eventually review and comment upon; (b) a Fiduciary SOP	(a) Some different versions are being used; (b) the entities are not administratively connected in most cases.	Moderate	(a) Bidding documents and SFRP uploaded on the publicly accessible websites of implementing entities within six months of Program effectiveness and; (b) fiduciary SOP shared with the World Bank within three months of Program effectiveness	Low



Risk Area	Proposed Mitigation	Baseline	Risk Rating before Mitigation Measures	Mitigating Measures/Monitoring Benchmark	Risk Rating after Mitigation Measures
	delineating roles and responsibilities of PCU and other entities may be developed and notified by the government.				
(a) Staffing (overall) (b) Staffing (specific)	(a) Recruitment of two procurement specialists and one contract administration specialist with IT background for the PCU (ideally a certified resource). (b) Rationalization of skillset to support public-private partnerships	(a) The PCU not yet in place (b) Very elementary capacity	Substantial	(a) To be done by negotiations (b) The PCU will assist relevant entities in engagement of a relevantly qualified and experienced staff for its nodal role under Public-Private Partnership Act	Moderate
Anti-corruption					
Complaints redressal	Secretary Finance to establish a program-level complaint registration and follow-up system.	Nil	Substantial	Complaints redressal established.	Moderate

Table 12: Procurement Staffing Profiles

Staffing	Board of Revenue	KPITB	KPPRA	KPRA	ETNCD	Finance Department
			<i>Administration</i>	<i>Director Administration</i>	<i>Administration</i>	<i>Administration</i>
1. Does the Agency have key staff with experience and a satisfactory track record in procurement in general and on donor-funded projects specifically?	No key procurement professional	Director Finance, Deputy Director Administration, and Assistant Director Procurement	No key procurement professional	Director - administration	No key procurement professional	No key procurement professional
2. Does the agency have or have access to contract management expertise and a track record of quality and timely delivery?	Not that much	Yes	Yes	Yes	Yes, to a greater extent	Not that much



Staffing	Board of Revenue	KPITB	KPPRA	KPRA	ETNCD	Finance Department
3. Does management ensure that staff take quality training for continuous skill development in procurement and contract management?	No	No	Yes	To some extent	No	No
4. Is there a published and known code of ethics that describes inappropriate behavior related to procurement?	No	Mentioned in the procurement manual	Yes	Yes	No	No
5. Are the staff selected on an open competitive basis and offered a competitive compensation that allows attracting high-caliber staff?	—	Open competitive process	Yes	Administration	No	Yes