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Report No: 57116-PK

PROJECT PAPER

ON A

PROPOSED RESTRUCTURING AND ADDITIONAL CREDIT

IN THE AMOUNT OF SDR 15.6 MILLION
(US$ 24.5 MILLION EQUIVALENT)

TO THE

ISLAMIC REPUBLIC OF PAKISTAN

FOR A

SECOND IMPROVEMENT TO FINANCIAL REPORTING AND AUDITING (PIFRA II) PROJECT

JANUARY 14, 2011

Financial Management Unit (SARFM)
Pakistan
South Asia Region

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CURRENCY EQUIVALENTS

(Exchange Rate Effective October 31, 2010)

Currency Unit	=	Pakistan rupee
SDR0.636217	=	US$1
US$	=	SDR 1.57179

FISCAL YEAR
July 1 – June 30

ABBREVIATIONS AND ACRONYMS

ACL	Audit Command Language
ADB	Asian Development Bank
AF	Additional Financing
AG	Accountant General
AGP	Auditor General of Pakistan
AGPR	Accountant General of Pakistan Revenue
AJK	Azad Jammu and Kashmir
AMIS	Audit Management Information System
CAATs	Computer Assisted Audit Techniques
CFAA	Country Financial Accountability Assessment
CFAO	Chief Finance and Accounts Officer
CGA	Controller General of Accounts
DAGP	Department of the Auditor General of Pakistan
DAO	District Accounts Office
DBA	Database Administration
DDO	Drawing and Disbursement Officer
DfID	Department for International Development (UK)
DNA	Damages and Needs Assessment
EA	Environmental Assessment
EAD	Economic Affairs Department
EDO	Executive District Officer
FABS	Finance & Budgeting Systems
FAM	Financial Audit Manual
FATA	Federally Administrated Tribal Areas
FBR	Federal Board of Revenue
FD	Finance Department
FRDL	Fiscal Responsibility and Debt Limitation (Act)
GIFMIS	Government Integrated Financial Management Information Systems
GoP	Government of Pakistan
GPF	General Provident Fund
IDA	International Development Association
IPSAS	International Public Sector Accounting Standards
ISACA	Information Systems Audit Control Association
IUFRs	Interim Unaudited Financial Reports
KP	Khyber Pakhtunkhwa
M & E	Monitoring and Evaluation
MoF	Ministry of Finance
MTBF	Medium Term Budget Framework
NAM	New Accounting Model
NBP	National Bank of Pakistan
NOL	No Objection Letter
OAG	Office of Auditor General
OAGP	Office of Auditor General of Pakistan
ORAF	Operational Risk Assessment Framework
PAAS	Pakistan Audit and Accounts Service
PAC	Public Accounts Committee
PAD	Project Appraisal Document
PAO	Principal Accounting Officer
PDOs	Project Development Objectives
PEFA	Public Expenditure and Financial Accountability
PETS	Public Expenditure Tracking System
PFM	Public Financial Management
PFO	Pakistan Fiscal Operations
PI	Performance Indicator
PIFRA	Project to Improve Financial Reporting and Auditing
PKR	Pakistan Rupee
PLA	Personal Ledger Account
PMU	Project Management Unit
PRSP	Poverty Reduction Strategy Paper
PSLM	Pakistan Social and Living Standard Measurement
SAP CC	SAP Competency Center
SBA	Stand-by Arrangement
SBP	State Bank of Pakistan
TARP	Tax Administration Reform Project
UNDP	United Nations Development Program
WAN	Wider Area Network

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ISLAMIC REPUBLIC OF PAKISTAN

ADDITIONAL FINANCING FOR THE SECOND IMPROVEMENT TO FINANCIAL REPORTING AND AUDITING PROJECT

Project Data Sheet

Project Paper

Annexes

PAKISTAN

SECOND IMPROVEMENT TO FINANCIAL REPORTING AND AUDITING PROJECT

RESTRUCTURING AND ADDITIONAL FINANCING DATA SHEET

Basic Information (Original Project)	
Project ID: P076872	Project Name: Second Improvement to Financial Reporting and Auditing Project
Team Leader: Aman Trana	Expected Closing Date: June 30, 2011
Environmental category: B	Lending Instrument: Specific Investment Loan

Basic Information (Additional Financing)	
Date: November 13, 2010 Country Director: Rachid Benmessaoud Sector Manager/Director: Jennifer K. Thomson	Team Leader: Aman Trana Sectors: Sub-national government administration (53%); Central government administration (45%); Banking (2%) Themes: Public expenditure, financial management and procurement (50%); Standards and financial reporting (25%); Administrative and civil service reform (25%)
Project ID: P122635	Environmental category: B
Lending Instrument: Specific Investment Loan	Additional Financing Type: Restructuring

Project Financing Data

[ ] Loan [X] Credit [ ] Grant [ ] Guarantee [ ] Other:

For Loans/Credits/Others:
Total Bank financing (US$m.): 24.50
Proposed terms:

Financing Plan (US$m)

Source	Local	Foreign	Total
BORROWER/RECIPIENT	3.86	0.00	3.86
International Development Association (IDA)	24.50	0.00	24.50
Total:	28.36	0.00	28.36

Borrower: Islamic Republic of Pakistan
Responsible Agency: PIFRA Directorate under the Office of Auditor General of Pakistan
House No. 745, Main Ibn-e-Sina Road, Double Road, Sector G-11/2
Islamabad, Pakistan
Tel: (92-51) 926-7166; pd@pifra.gov.pk

Estimated disbursements (Bank FY/US$m)

FY	2012	2013							
Annual	14.00	10.50							
Cumulative	14.00	24.50							

Project implementation period: Start July 1, 2011 End: June 30, 2013
Expected effectiveness date: July 1, 2011
Expected closing date: June 30, 2013

Does the project require any exceptions from Bank policies? (See para 31)	[X]Yes [ ]No
Have these been approved by Bank management? (See para 31)	[X]Yes [ ]No

Does the project include any critical risks rated "substantial" or "high"?	[ ]Yes [X] No

Project development objective:
Overall project development objectives under Additional Financing remain unchanged from PIFRA II, namely to: (a) build capacity to improve accuracy, comprehensiveness, reliability, and timeliness of financial and fiscal reporting at all levels of government; (b) improve public financial management, accountability, and transparency; (c) enhance the capacity of public sector managers to use credible financial information for better and informed decision-making; and (d) facilitate oversight of the use of public monies, and increase the national and international credibility of government's financial statements and assurance processes. The main additional element during the Additional Financing period will be to emphasize transition and ownership of the IT systems to the relevant government agencies (i.e., AG, MoF, and CGA).

Project description:
Additional Financing will allow deepening of reforms that have been successfully established under PIFRA II and a phased transition to substantial incorporation of the system under GoP line agencies. It will, inter alia: (i) provide interim support for continued operation and maintenance of the Financial Accounting and Budgeting System (FABS) and full development of the Audit Management Information System (AMIS); (ii) address some continuing issues that impede the full realization of fiscal and financial management outcomes from the IT systems; and (iii) build capacity of the MoF, CGA, and AGs to apply the IT platforms to key areas of PFM reform and further integrate the processes of fiscal policy, budget preparation, and financial management.

Additional Financing will comprise three main components, aligned with the PIFRA II structure: (i) Financial Accounting and Budgeting System (FABS) - MoF/CGA; (ii) Audit; and (iii) Project Management. Component 1 is centrally concerned with the continued operation and maintenance of FABS, capacity building and transfer of responsibility to the MoF and CGA. Component 2 provides additional resources to establish AMIS initiated under PIFRA II and to transition system and performance audit practices fully to the OAGP. Project management will be maintained to oversee all project operations and promote transition arrangements.

Safeguard policies triggered?	Yes	No
Environmental Assessment (OP/BP 4.01)	[X]	[ ]
Natural Habitats (OP/BP 4.04)	[ ]	[X]
Forests (OP/BP 4.36)	[ ]	[X]
Pest Management (OP 4.09)	[ ]	[X]
Physical Cultural Resources (OP/BP 4.11)	[ ]	[X]
Indigenous Peoples (OP/BP 4.10)	[ ]	[X]
Involuntary Resettlement (OP/BP 4.12)	[ ]	[X]
Safety of Dams (OP/BP 4.37)	[ ]	[X]
Projects on International Waters (OP/BP 7.50)	[ ]	[X]
Projects in Disputed Areas (OP/BP 7.60)	[X]	[ ]

Disclaimer: "A part of the proposed project will be carried out in Azad Jammu Kashmir, an area over which Pakistan and India have been in dispute since 1947. By financing the credit, IDA does not intend to make any judgment as to the legal or other status of the disputed territory or to prejudice the final determination of the parties claim."

I. INTRODUCTION

1. This Project Paper seeks the approval of the Executive Directors to provide an additional credit in Special Drawing Rights in an amount equivalent to US$ 24.5 million to the Islamic Republic of Pakistan for the Second Improvement to Financial Reporting and Auditing Project (PIFRA II; P076872; Credit No. 4109-PAK) and also to extend the closing date of the original project from June 30, 2011 to June 30, 2013 (coterminous with the closing date of the Additional Financing operation).

2. The proposed Additional Financing would help finance activities associated with deepening the reforms that have been successfully established under PIFRA II and also allow for a phased transition to substantial incorporation of the system under Government of Pakistan (GoP) line agencies. Additional Financing will, inter alia, (i) provide essential interim support for the continued operation and maintenance of the Financial Accounting and Budgeting System – FABS; and the consolidation of the audit function including the full development of the Audit Management Information System (AMIS); (ii) address some continuing issues that impede the full realization of fiscal and financial management outcomes from the IT based financial management and auditing systems developed under PIFRA; and (iii) build capacity of the MoF, Controller General of Accounts (CGA), and Office of the Auditor General of Pakistan (OAGP) to apply the automated information systems to key areas of PFM reform and further integrate the processes of fiscal policy, budget preparation, and financial management.

3. No changes are proposed to project objectives, but a restructuring of the component activities as well as a refinement of the institutional implementation arrangements is envisaged. In addition, the proposed operation entails invoking the Country Financing Parameters for Pakistan by allowing for 100% financing of project activities during the extended life of the project. The closing date for the Additional Financing operation would be June 30, 2013.

II. BACKGROUND AND RATIONALE FOR ADDITIONAL FINANCING

4. The original PIFRA II credit was approved by the Board on September 6, 2005 in the sum of US$ 84 million with the GoP providing counterpart funding of US$ 9 million. The Project became effective on November 8, 2005, with an original closing date of December 31, 2010, which has been extended to June 30, 2011.

5. The Project's development objectives, which will remain unchanged during the Additional Financing operation, are to: (a) build capacity to improve accuracy, comprehensiveness, reliability, and timeliness of financial and fiscal reporting at all levels of government; (b) improve public financial management, accountability, and transparency; (c) enhance the capacity of public sector managers to use credible financial information for better and informed decision-making; and (d) facilitate oversight of the use of public monies, and increase the national and international credibility of government's financial statements and assurance processes.

6. The **principal development outcomes** anticipated from the project include improved capacity in financial resource management, budgeting, expenditure control and accountability at national, provincial and district levels. The **higher level outcome**

indicators are: (a) transparent and effective fiscal administration supported through MTBF and integrated financial management system; (b) effective and transparent financial reporting, control, and audit through timely submission of reliable and comprehensive financial statements that are audited on time using international standards; (c) effectively tracked and managed poverty- reducing spending through reliable and timely PRSP reports; (d) effective corruption and inefficiency reducing measures related to accounts and budget control applied through effective monitoring of the use of systems functionality, bill tracking, and issuance of checks; (e) stable FABS operations and maintenance support in GoP established through implementation of data warehouse, disaster recovery, and information security plan; and (f) adequate number of staff trained in MoF, line ministries/departments, and CGA to manage and apply systems to fiscal and financial management.

7. **Implementation status of existing project**: Implementation support and supervision performance ratings have been fully satisfactory, both for Development Objectives and Implementation Progress, throughout the Project implementation period. The Project has no unresolved fiduciary, environmental, social, or other safeguards problems, and compliance with the Credit covenants is satisfactory. There are no prior actions necessary under the Additional Financing operation, including the extension of the original project.

8. **PIFRA II accomplishments**. PIFRA has established an accounting, reporting and audit system that covers core government entities at the federal, provincial, and district level. These achievements place Pakistan at the forefront of Public Financial Management (PFM) reform in the South Asia region and Pakistan is the only country in the region where SAP has been implemented successfully on such a large scale in the public sector. Specifically, PIFRA II has enabled timely and reliable reporting of accounts and audit certification of financial statements that are submitted to the legislature within 8 months after the financial year-end (previously 24-28 months). Transparency has improved due to the strengthening of internal controls and by enabling stakeholders to generate timely reports through the system. Accounting and payment processes that were adopted under the new system have made it possible to ensure accuracy, completeness, reliability, and timeliness of accounts. Further, system-generated monthly and quarterly fiscal reports have made possible timely macro-economic review and analysis by policy makers.

9. The GFMIS implemented under PIFRA is now used by the federal, provincial and district governments to:[1] (i) prepare and compile the annual budget estimates and fulfill associated reporting requirements; (ii) exercise ex-ante budgetary control on allocations and enable processing of all government expenditure and receipt transactions; (iii) make payments (currently by check) against bank accounts where government appropriated funds are held; (iv) prepare the payroll for some 1.9 million government employees across all levels of government; (v) make pension calculations and improve timeliness of payments to all government pensioners; (vii) maintain the General Provident Fund liability accounting for all government employees; and (viii) prepare periodic budget execution and fiscal reports for all stakeholders, including the MoF/ provincial Finance Departments/ line ministries and departments.

[1] Except defense and railway services.

10. **Disbursements:** As of October 31, 2010, US$ 61.37 million equivalent were disbursed under the IDA Credit (72% of the total amount) and the remaining undisbursed balance under the project has been fully committed. The disbursement rate slowed, particularly in the final year of implementation, primarily because of the delay in completing certain high-value and complicated procurements. Specifically, procurements related to the SAP software upgrade (US$ 5 million), purchase of new servers (US$ 5 million) and the AMIS software (US$ 2 million), and the completion of civil works (US$ 2 million). However, most of these procurements are in an advanced stage and are expected to be finalized within the next few months. The completion of these procurements, along with the spending associated with other amounts committed, would account for about 60% of the remaining PIFRA II funds and also act as a catalyst for a the spending envisaged under Additional Financing.

11. Consistency with the CAS and CPS: The Bank Group's **Country Partnership Strategy (CPS) 2010-2013,** the successor to the CAS (2006-09), is aimed at helping Pakistan address some of its major institutional, policy and financing constraints, and sustain high economic growth rates, manage conflict, and improve human development. The four pillars of the CPS focus on: (i) strengthening economic governance; (ii) improving human development and social protection; (iii) bettering infrastructure to support growth; and (iv) enhancing security and reducing the risk of conflict. The proposed Additional Financing is directly linked to and aligned with the first pillar. The Additional Financing is equally aligned with th**e Pakistan Poverty Reduction Strategy Paper II for 2009-2011**, specifically Pillar 9 – Governance for a Just and Fair System, which includes the public financial management sector. PIFRA II and the Additional Financing operation will make government more accountable and its processes transparent and thereby contribute to the government's development agenda. In increasing transparency in public finance management, the Bank, together with key development partners in Pakistan, would be seen as a credible partner that can engage in the PFM sector, and support reforms within a wider country context. The Bank is considered as having comparative advantage to engage with the GoP in PFM reforms, supported through the PIFRA. The Additional Financing will be completed within three years of the closing date of the original project, PIFRA II, as required under OP/BP 13.20.

12. **Rationale for Additional Financing and Extension of PIFRA II.** The proposal for Additional Financing and extension of the existing Project is in response to the Government of Pakistan's requests dated March 17, 2010 and August 3, 2010, respectively to scale up and consolidate the reforms already realized in the implementation of the PIFRA delivered activities.

13. While PIFRA II's performance has been satisfactory, extension of the original project's closing date to June 2013 is needed to allow critical activities (see para. 10) to be completed. For example, PIFRA is currently engaged in several activities under the FABS component for which PIFRA II resources have already been committed. These include: (i) upgrade of SAP software;[2] (ii) design, procurement and implementation of an Information Security/Disaster Recovery Management System; (iii) upgrade of servers at the Center and

[2] PIFRA needs to upgrade its software to the latest version to avoid exorbitant annual maintenance charges and also to provide additional functionality directly required for the public sector (i.e., MTBF support).

provinces and replacement of old workstations; and (iv) establishment of a data warehouse facility. Extension of the closing date to June 2013 would allow these activities to be completed and PIFRA II resources will continue to be available for completion of these tasks.

14. The Additional Financing operation will ensure that arrangements are made for sustaining the continued operation of the mission critical systems developed under PIFRA and, perhaps more importantly, that the day-to-day operations of the agencies responsible for the Government's Financial Accounting and Budgeting operations are not put in jeopardy after project closure. Such an outcome would pose a significant reputational risk for the Bank. The information systems also need to be rolled out to line ministries/ departments and key spending units. An important objective of extending the system will be to enable full implementation of commitment accounting, as well as to support output-based budgeting currently being implemented under the MTBF program.

III. PROPOSED PROJECT CHANGES

15. Under Additional Financing, the Project's overall development objectives and scope will remain unchanged from PIFRA II. However, there will be a realignment of the Project components and accordingly the institutional arrangements to better address implementation necessities as well as strengthen stakeholder coordination.

Revised Project Components

16. PIFRA II included 4 components, namely: Component 1 - Financial Accounting and Budgeting System (FABS); Component 2 - Capacity Building and Upgrading of CGA; Component 3 - Capacity Building and Upgrading of OAGP; and Component 4 - Project Management.

17. Instead of 4 components as under the original project, Additional Financing will comprise three main components, aligned with the PIFRA II structure: (i) Financial Accounting and Budgeting System—MoF/CGA (Component 1); (ii) Audit (Component 2); and (iii) Project Management (Component 3). Component 1 under Additional Financing will unify the original components 1 and 2 into an integrated whole since the MoF/CGA will take over the FABS operations and maintenance during the Additional Financing period. Component 2 of Additional Financing provides additional resources to further strengthen the external audit function through the establishment of an Audit Management Information System (AMIS) initiated under PIFRA II and also allow the OAGP to fully transition to systems and performance audit practices. Project management will be maintained to oversee all project operations and promote transition arrangements. Annex 3 provides a detailed description of the linkages of the original PIFRA II components to the three components as redefined under Additional Financing.

A. Component 1: Financial Accounting and Budgeting Systems (FABS) – MoF/CGA (US$ 19.40 million). This component will ensure the continuing support for operation of the systems, strengthen the capacity of FABS to produce fiscal reports, integrate FABS with the MTBF, and link both systems to overall PFM reforms. The component would also establish a firmer relationship between budgeting and accounting and allow the MoF to use the SAP based system as a platform for further PFM reforms.

The bulk of the Additional Financing will be absorbed by this component and the major items that will require financing over the next two years relate to: (i) the maintenance costs of the hardware elements of the country-wide network set up to implement the FABS system and the replacement upgrade costs of some elements of this network; (ii) the annual license fees for the application and systems software and costs associated with software upgrades; (iii) the costs associated with operation of the FABS network, including telecommunications costs, arrangements to ensure adequate power supply at the various FABS sites, special stationary, etc.; and (iv) the costs associated with the operations of the SAP Competency Center and financing the salaries of consultants/ specialists and ongoing training activities. Component 1 will comprise four sub-components as discussed below.

i. **Sub-component 1.1: Continued Operation and Maintenance of FABS.** With most of the sites productive, the emphasis is now on: (i) deepening reforms by ensuring that core systems functionalities (i.e., budgeting, accounting, payroll, GPF, and pensions) available in the system are implemented fully and uniformly at all levels of Government; (ii) improving the comprehensiveness, accuracy and timeliness of the data being entered into the system and of the reports and financial statements produced by the system and ensuring their ready availability for the Financial Managers at the federal, provincial and district levels, including the Principal Accounting Officers (PAOs) in line ministries and departments; and (iii) ensuring that transaction processing is implemented as was intended and in a manner that optimizes systems use, eliminates redundant business processes such as maintenance of manual ledgers and registers, and follows standard accounting and data management and control practices.

ii. **Sub-component 1.2: CGA Capacity Development and Transition Plan.** A transition phase is necessary to allow critical expertise to be enhanced in the office of the CGA. SAP Competency Center units servicing sites in Islamabad HQ and the provinces, now stationed in PIFRA-FABS, will be streamlined and transferred to the CGA. The CGA will establish a Quality Assurance Cell to review system functionality and performance. A short-term (around 3 month) international consultancy will prepare an organizational and functional plan for IT set-up required to maintain and operate FABS in the CGA, and appropriate local consultants will be hired to guide its implementation. In addition, the CGA will play a key role in overseeing and the Chief Financial and Accounting Officers (CFAO) function and training its staff. The sub-component, whose implementation would be closely coordinated with the MoF activities as relating to the role of the CFAOs, provides for recruitment of an international consultant who would provide assistance to the CGA to define this role and to establish a training program (which will include short-term local/foreign training for both CGA staff and CFAOs).

iii. **Sub-component 1.3: Fiscal Reporting on General Government.** Financial and fiscal reporting has been substantially improved under PIFRA II and the PAD benchmarks have been substantially achieved. A few issues remain to be addressed (particularly that of timely entry of transactions sanctioned by Federal MoF/Provincial Finance Departments into the system), but early in the Additional Financing period, quarterly production of the federal Pakistan Fiscal Operations (PFO) report through the system should be feasible. Once the principles are fully tested, consolidation of federal and provincial accounts in a general government PFO should be achieved by end-2010/11. The

CGA and AG Pakistan Revenues would perform all of the technical work to produce the fiscal reports.

iv. **Sub-component 1.4: FABS Support to MTBF Implementation.** The MTBF has now been rolled out to all ministries and the 2010/11 budget was presented to the parliament in both the traditional White Book (demand for grants) form and in the Green Book (MTBF) format. Integration of the MTBF on the SAP platform, which has been delayed pending acquisition of the SAP upgrade from its current version to ECC06, will give greater assurance of data integrity and will link budget preparation and budget execution more closely. The upgraded version will be financed under PIFRA II and should be available by end-FY 2011. The target should be to establish preparation of the MTBF based 2012/13 budget on SAP, and configuration should be initiated as soon as practicable after the software upgrade is acquired. Provision is made under FABS for enhancement of systems related to MTBF. Issues of capacity building and transition of functional responsibility fully to the MoF/CGA under sub-components 2-4 are discussed in greater detail in Annex 4.

B. Component 2: Audit (US$ 4.67 million). Overall, this component has met its basic objectives of conducting the audits using modern audit techniques and presenting the audited accounts to the legislature within 12 months of the close of the fiscal year. However, some activities under the Project are not yet fully realized and are critical in order to ensure that its objectives are fully met. The Quality Management Framework has been finalized and requires support of consultants for timely implementation. The consultants hired for developing and implementing Information Systems (IS) Audit guidelines have completed their ground work and the field testing of the audit methodology is underway. Completion of these initiatives will enable the OAGP to adopt Information Systems Audit Control Association (ISACA) standards. Training of sufficient number of PAAS officers to sustainably conduct all activities of the audit without the support of consultants is another critical activity. There is also a need for structural reform in audit planning, execution and reporting to allow the OAGP to achieve improved ratings under the PEFA framework, as well as in the conduct of procurement audits and reporting of systemic issues of government wide practices on budgeting, revenue generation, status of internal control and internal audit activities. These activities are planned to be completed alongside the implementation of the Audit Management Information System (AMIS). The funds under the Audit component will primarily be spent on recurrent costs associated with AMIS, engagement of local consultants to provide assistance with the strengthening of regularity, certification and performance audits, as well as the purchase and maintenance of laptops, printers, network equipment, etc.

C. Component 3: Project Management (US$ 0.43 million). The overall performance of the Project Management Unit (PMU) has been satisfactory. The Project management team would need to remain intact during the two-year transition phase and the unit would be strengthened under Additional Financing to allow for improved reporting of monitoring indicators to the various technical and steering committees. Other cross-cutting activities supported under the aegis of the PMU shall continue under Additional Financing to enhance the value of improved coordination under the revised institutional and implementation arrangements. Project management costs will largely include costs for technical consultants (i.e., procurement, internal audit, etc.) and some minor equipment upgrades and cross-cutting activities like M&E, training, and change management and coordination.

18. **Project Costs and Component Financing.** The funding required under Additional Financing is US$ 24.5 million. The table below is a cost allocation for both the extension of the existing project and the Additional Financing period. See Annex 7 for a detailed breakdown.

Sr.	Component	Original Cost as per PC-I	MidTerm Review Update	Expenditure Up to September 2010	Remaining Commitments	Revised Cost PIFRA-II	FY 2012	FY 2013	Total	Revised Cost with Addl Fin
		(US$ Million)								
1	FABS + MoF/CGA	58.00	56.72	42.70	20.42	63.12	11.17	8.23	19.40	82.52
2	Audit	19.55	16.22	12.20	5.58	17.78	2.61	2.07	4.68	22.46
3	Project Management	6.45	12.28	2.30	0.80	3.10	0.22	0.21	0.42	3.52
	Total Cost	**84.000**	**85.220**	**57.200**	**26.800**	**84.000**	**14.000**	**10.510**	**24.500**	**108.500**

Revised Institutional Implementation Arrangements

19. With a view to enhancing ownership of project deliverables, the institutional and implementation arrangements proposed under Additional Financing will vary from those designed under the original PIFRA II. The design of the new institutional arrangements takes cognizance of the need to establish a transitional arrangement for moving both the implementation and closer supervision of activities related to the FABS component to the MoF. Annex 6 provides a detailed description of the institutional and implementation arrangements under Additional Financing.

20. The maturing of FABS during the original project implementation now allows stronger action to integrate its operations within the MoF/CGA. As a key user of system information and manager of budget authority, the MoF will play a central role in operations related to budget management and reporting. Technical responsibility for the FABS component and its future operation will, however, rest with the CGA, with appropriate involvement of the AGs. The implementation and supervision of the Audit component will continue to be anchored under the OAGP to conform to the requirements of independence of the audit function and the statutory nature of the office. Project management, while retaining its existing structure and function as well as its current overall reporting arrangements, will service both the Audit and FABS components. Project management will continue to coordinate the execution of the project closely with the responsible agencies and no change is envisaged in its existing responsibilities.

21. The institutional structure of the original PIFRA II will be strengthened by establishing 2 separate and distinct Component Steering Committees – one responsible for Audit and the other responsible for FABS. The Audit component committee will be chaired by the Auditor General and the FABS component shall be chaired by the Finance Secretary, MoF. These two committees will be responsible for overseeing the project components' implementation within their agreed policy framework, reviewing key implementation strategies, providing strategic high-level directions, and reviewing overall implementation progress. For each of the two component committees, there shall be a

Technical Committee to oversee the day-today technical aspects of the components' implementation.

22. The institutional arrangements for Additional Financing also make provision for a two-person high-level strategic committee, comprising the Auditor General and the Finance Secretary, MoF. This committee will reinforce collaboration and enable resolution of major issues impacting either of the two components (Audit and FABS) or from interaction between them.

23. **Procurement**. The majority of outstanding procurements will utilize PIFRA II funds carried forward to the extension period (see para 10). Under Additional Financing, the major procurements would relate to replacement hardware elements for the FABS network, the recurrent costs to ensure continued and stable operation of this network, acquisition of a system for archiving records at the office of the CGA, establishing a data warehouse, purchase of software and additional SAP licenses, and purchase of laptops, printers, generators, etc.

24. In line with Bank policy, all procurements under the original project that are yet to be initiated and those under Additional Financing will be governed by the Bank's May 2004 Procurement Guidelines, revised October 2006 and May 2010, and Consultant Guidelines May 2004 as revised in May 2010. Readiness of the activities to be funded by the Additional Financing is articulated in the procurement plans. Due diligence will be carried out on the original project to identify contracts in the approved procurement plan yet to be initiated. Thresholds for prior review by the Bank, as well as the procurement methods to be applied, will remain the same as those in the current DCA.

25. A summary of the procurement plan envisaged under Additional Financing is presented in the table below:

#	Category	Method							Total (#)	Estimated Cost in PKR (M)	Estimated cost in U$$ (M)
		ICB	NCB	NS	QCBS	CQS	SSS	Other			
1	**Works**	0	1	1	0	0	0	0	2	72.25	0.85
2	**Goods**	6	2	0	0	0	0	0	8	563.125	6.625
3	**Consulting Services (Firms)**	0	0	0	1	0	0	0	1	29.75	0.35
4	**Individual Consultants**	0	0	0	0	0	0	0	0	0	0
Total		**6**	**3**	**1**	**1**	**0**	**0**	**0**	**11**	**665.125**	**7.825**

26. **Financial Management**. An assessment of the financial management arrangements in place for the original Project was done based on which the overall FM risk is considered Moderate. Staffing, budgeting, accounting, internal controls, financial reporting and audit arrangements in place were found satisfactory. PIFRA II is a successful pilot in the use of the national accounting system (FABS) for accounting and reporting of foreign-funded projects. The Additional Financing has been established as a separate project in the AGPR server and the same processes and procedures will be followed. There are no outstanding audit reports or ineligible expenditures under the original credit. PIFRA does not implement any other Bank projects.

27. **Disbursements** for the Additional Financing will be report-based. Interim Un-audited Financial Reports will be submitted to the Bank within 45 days of the end of each calendar quarter. Format and content of these IUFRs will be agreed during Negotiations. Funds will be disbursed to a segregated designated account in US Dollars on the basis of cash forecasts provided in quarterly IUFRs. The Additional Financing would be disbursed in a period of around two years. The allocation of Credit proceeds by disbursement category will be made as indicated below.

Category	**Amount of Credit (expressed in USD)**	**Percentage of Expenditures to be Financed**
Goods, Works, Consultants' services, Training and Incremental Operating Costs	24,500,000	100%
TOTAL AMOUNT	**24,500,000**	

IDA financing is inclusive of import duties and taxes.

28. **Designated Account**: In accordance with agreed procedures for operation and maintenance of the Designated Accounts, circulated by the Government of Pakistan, from time to time, a Segregated Designated Account (DA) in US Dollars, will be established for the Additional financing for receipt of funds from the Bank. On a quarterly basis, the IDA will front-load funds in the DA keeping in view the forecast cash requirements for the following two quarters. The funds provided into the DA would be used to meet Bank's eligible share of financing of expenditures. The DA will be operated by joint signatories.

29. **Incremental Operating Costs**: Incremental operating costs will cover incremental staff salaries, per diem and fringe benefits, rent, office supplies, utilities, conveyance, travel and boarding/lodging allowances, operating and maintenance expenditures of office equipment and vehicles, bank charges, insurance, advertising, media projections, newspaper subscriptions, periodicals, printing and stationary costs incurred for the purposes of the Additional Financing, but excluding salaries of the Recipient's civil servants.

30. Based on our assessment, the financial management arrangements for the Additional Financing are considered satisfactory and there is sufficient assurance that the requirements of OP 10.02 will be met. The implementing entity will ensure that the Bank's guidelines on Preventing and Combating Fraud and Corruption in Bank Financed Projects are followed.

31. In case of IDA, there are nine projects in Pakistan which have not refunded or provided documentation on the use of Designated Accounts/Special Accounts (DA/SA) after the deadline of two months after the end of the "grace period" (i.e., the "lapsed loan" date, normally six months after the Closing Date). Under Bank policy (OP12.00, disbursement para 12), failure to refund unused Designated Accounts/Special Accounts balances results in the Bank not permitting the use of DA under new loans/credits. Management endorsement for a waiver of the requirements of OP12.00 has been secured

for a period of 12 months ending on October 31, 2011 to allow for continued use of DAs for loans and credits to Pakistan. It is hereby requested that the waiver be confirmed by the Board for this Additional Financing.

32. It should be noted that the Bank's Executive Directors on November 17, 2009 approved revisions to its Policy on Access to Information, which included new requirements related to the disclosure of audited financial statements for its projects. The new requirement are in effect from July 1, 2010 and apply to operations for which the invitation to negotiate is issued on or after July 1, 2010.

33. **Safeguards (Environment and Social)*:*** The Additional Financing will not entail any new civil works beyond renovations to existing government offices that will house the computers. There are therefore no safeguard policies to be triggered by the Additional Financing although the Category for the original project was, at mid-term, upgraded from 'C' to 'B' due to inclusion of renovation/construction works in project scope. To comply with the Bank's OP 4.01, PIFRA completed an Environmental Assessment (EA) study in June 2010 that addressed the potential negative impacts associated with the PIFRA II construction activities.

34. The EA, in addition to identifying the mitigation measures to offset the potential negative impacts, also includes an Environmental Management Plan (EMP). The EMP comprises environmental mitigation and monitoring plans, which define the mitigation and monitoring actions, assign responsibilities, and describe methodologies for these actions. The EMP also specifies the environmental awareness raising and training requirements to be fulfilled by PIFRA to improve the environmental performance of the construction works.

35. PIFRA will ensure compliance with the EA and EMP for: (i) any remaining construction works; (ii) renovations of existing offices; and (iii) usage of the facilities constructed under the project. In compliance with the EMP, PIFRA will also commission an environmental audit of the buildings constructed under the project to identify any negative environmental impact and to determine the measures to mitigate these impact through a thorough monitoring framework for any such impacts.

Project Benefits and Risks

36. Successful implementation of the PIFRA II-AF project will have far-reaching benefits for GoP fiscal and financial management. Achieving these objectives will, in turn, help improve economic performance and social welfare. The potential for timely, effective fiscal and financial reporting has already been well established under PIFRA II. The Additional Financing operation will provide the opportunity to fully realize these benefits and build up management capacity for the GoP to sustain the system in the future. As a successful PFM project, PIFRA will significantly reduce operational risks arising from sector investment projects and management of public funds (partly reflected by the substantial increase in recoveries reported by the OAGP for 2009).[3] The main risks for a

[3] Total cash recoveries made possible due to the information available to the auditors from the FABS, in the calendar year 2009 amounted to PKR 19 billion compared with a baseline of only PKR 5 billion in prior years. It is not, however, to be expected that such a level of recoveries would be sustained; the impact of

PFM project are generally not an increase in fiduciary risk, but rather that fiduciary risks are not sufficiently reduced because the Project objectives may not be fully realized.

37. An analysis of operational risks and mitigating measures are presented in the Operational Risk Assessment Framework (Annex 2), which puts the overall operational risk rating as “Medium-I” (i.e., high impact/low likelihood)”.[4] This assessment reflects a high level of country risk balanced against generally low project risks and “Medium-I” implementing agency-related risks.

38. Country-level risks are very high because of the weak macro-economic situation, which has been further compounded by the recent disastrous floods. Inevitably, this situation will make it difficult for the GoP to provide the needed resources to build up its fiscal and financial management capacity. At the same time, the GoP and all DPs should recognize the key long-term role that will be played by the country-wide IFMIS that is being put in place under PIFRA. A continuing build-up of fiscal and financial management capacity is essential to equip the GoP to address future fiscal management and natural disaster response challenges.

39. Project risks of themselves are assessed as being relatively low. The satisfactory progress made by PIFRA II against the original PAD benchmarks is evidence of an effective design and strong project management. It is recognized, however, in the AF design that more effort has to be made to build up management capacity in the CGA. The key aim in this regard is to ensure that the financial management and IT skills now resident in the PIFRA II project team are effectively transferred to the CGA and AGs. It is also evident that the FD has not been sufficiently involved in ensuring that FABS reporting is sufficiently geared to fiscal policy setting and management.

40. To some extent, the lack of in-depth involvement of the MoF is a consequence of the necessarily heavy emphasis on transaction processing in the early stages of implementing a GIFMIS. Initially, financial and fiscal reporting quality will be low until system coverage is complete and data entry processes are fully bedded down. PIFRA is now, however, at the stage where data entry is generally sound and reconciliation processes are sufficiently in place to ensure a progressive improvement in data quality standards. Therefore, system-generated financial and fiscal reports can begin to transform fiscal and financial decision-making processes. Technically, there are relatively few issues to be resolved. The governance arrangements under Additional Financing should ensure full involvement of the MoF in making effective use of FABS reporting functionality for fiscal management.

41. The ORAF assesses implementing agency risks as being generally “Medium-I” (i.e., high impact/low likelihood). Much of the responsibility for ensuring a capacity build-up in the MoF/ FD, CGA/AGs, and OAG, however, will lie with the GoP and these agencies. The Additional Financing design emphasizes the following aspects to assist GoP agencies to meet this responsibility: training of CGA, MoF/ FD, line ministry, and OAG

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improved auditing in subsequent years could be expected instead to reduce the level of financial irregularities—an equally or even more important benefit.

[4] Rating of risks on a four-point scale – Low (low impact/low likelihood); ML (low impact/high likelihood); MI (high impact/low likelihood); and High (high impact/high likelihood).

management and staff; reviews of critical business processes; a strengthened governance structure that should ensure full involvement of the MoF/ FD; and regular M&E reporting to the Bank and Project Steering Committees on the status of all project objectives—as well as progressive transfer of M&E functionality to the CGA to promote sustainable system management. A high level of support for the Additional Financing proposal has been indicated by most of the federal and provincial agencies. It will be important for the overall success of the project that the new governance structure takes up project implementation in a fully coordinated way to achieve the essential transfer of management skills.

Annex 1: Revised Results Framework and Monitoring Indicators

1. The monitoring and evaluation framework that will continue to be used for PIFRA II Additional Financing is shown in the three tables below. Table 1.1 shows the results framework in standard Bank format. The framework remains based on the PIFRA II PDOs; the original indicators are refined somewhat to reflect experience during project implementation with more emphasis in the Additional Financing stage on transfer of management skills and ownership. Table 1.2 shows how these indicators will be assessed and milestones to be achieved during the implementation period, including the final outcome and intermediate outcome values planned by the end of the project. This table also includes baseline values at the beginning of PIFRA II and just prior to inception of Additional Financing. These demonstrate that all of the key outcomes defined in PIFRA II have been substantially achieved by the end of the original project financing.. The purpose of the Additional Financing is to ensure that the functionality now in place and in use can be managed and sustained by the GoP over the long-term.

2. The above-mentioned tables provide a clear quantitative picture of the progress of implementation of PIFRA II. M&E for the PIFRA project has, however, involved much more detailed analysis and discussion during Bank project reviews. Detailed quantitative and qualitative reviews of progress must be undertaken within the year to identify and discuss issues and bottlenecks that may arise and impede achievement of targeted outcomes. This work is done by the PIFRA II M&E unit in consultation with all GoP agencies involved in PIFRA-related activities. The issues raised are discussed by project management and Bank review missions and resulting recommendations become action points for subsequent reviews. Table 1.3 both illustrates the progress made to date and the nature of the discussions carried out during project reviews.

3. An important aim of the Additional Financing project management component will be to complete transfer of these key M&E skills to the relevant units of the MoF, CGA, and the OAG by 2012.

Table 1.1: Results Framework and Monitoring

PIFRA II Additional Financing

PDO	Project Outcome Indicators[5]		Use of Project Outcome Information	
Current (from PAD)	Current	Proposed	Current	Proposed
The project will (1) build capacity to improve the accuracy, comprehensiveness, reliability, and timeliness of intra-year and year-end government financial reports, at Federal and Provincial levels, and initiate the process at District and sub-District levels, thereby strengthening the financial accountability cycle; (2) directly support the GoP's commitment to improved public financial management, accountability, and transparency; (3) enhance the capacity of public sector managers to use credible financial information for better and informed decision making, and (4) facilitate public oversight of the use of public monies, and increase the national and international credibility of Governments' financial statements and assurance processes.	1. Effective and transparent fiscal administration *(MTBF in place and FABS-supported)*	No Change	Indicators show the extent to which system outputs are (a) reliable and (b) applied to fiscal management	No Change
	2. Effective and transparent financial reporting, control, and audit *(timely, reliable submission of financial statements and timely audit)*	No Change	Timeliness and certification of accounts indicates effectiveness of financial controls. System allows CAATs and performance-based audit	No Change
	3. Effectively tracked and managed poverty reducing spending *(timely reliable PRSP reports*	No Change	System tracking of PRSP sectors improves efficiency of PRSP reporting and enables improved audit of service delivery	No Change
	4. Effective corruption & inefficiency reducing measures related to accounts and budget control applied (*system monitoring of use of functionality, bill-tracking, issuance of checks)*	No Change	System tracking of application of functionality identifies procedural failures, reduces discretion, and encourages efficiency of system operations.	No Change

[5] Indicators remain consistent with PAD objectives, but incorporate further definition of outcomes and measurement as a result of experience during project implementation.

		5. Establish stable FABS operations and maintenance support in GoP (*implement a data warehouse, an Information security and Disaster recovery plan)*.	No Change	Achieving critical system benchmarks, plus training and continued monitoring and evaluation by the M&E cell of PIFRA and transfer of M&E techniques to CGA and MoF, will help ensure transfer of responsibility fully to the GoP to sustain system operations and maintenance after the end of the PIFRA II-AF project. Numbers of trained key management and operational staff will indicate extent of GoP operational capacity.	No Change
		6. Adequate numbers of trained staff in MoF and CGA to manage and apply system to fiscal and financial management *(trained MoF, CGA, and line ministry CFAOs)*	No Change		
Intermediate Outcomes[1]		**Intermediate Outcome Indicators**		**Use of Intermediate Outcome Monitoring**	
Current	Proposed	Current	Proposed	Current	Proposed
Component 1: FABS-MoF/CGA					
1. Effective reconciliation of accounts for fiscal reporting and. planning	No Change	1.1 Discrepancies between monetary survey credit and government fiscal deficit (for 2004/05 = 1.2% of GDP).	No Change	Identification of causes of discrepancies and their elimination will give assurance of data reliability for both fiscal and financial reporting.	No Change
		1.2 Issue of reliable, timely budget execution reports (BERs) to PAOs	No Change	Timely reports on actual versus budget increases PAOs accountability and control of spending	No Change
2. Accurate, comprehensive, and timely reports, based on international standards of accounting and internal control.	No Change	2.1 Application of IPSAS accounting standards	No Change	Adherence to IPSAS improves quality and transparency of financial statements.	No Change
		2.2.Implementation of commitment accounting	No Change	Commitment records improve control and helps avoid arrears.	No Change

3. System functionality tracking for improved efficiency and reduced discretion	No Change	3.1 Bills passed within 3 days (%)	No Change	Increased efficiency and accountability of AG staff.	No Change
		3.2 All cheques issued by system	No Change	Reduction in discretion and improved efficiency.	No Change
4. Achieve comprehensive data entry to FABS	No Change	4.1 Comprehensive data entry coverage (% expenditure & receipts)	No Change	Assurance of reliability and sustainability of system data management	No Change
		4.2 Interfaces with SBP/NBP, NBR & EAD established	No Change		
Component 2 Audit					
5. Effective and timely audit of government accounts using international standards of auditing.	No Change	5.1Application of modern audit practices	No Change	Improves efficiency and relevance of audit.	No Change
		5.2 Performance audit of policy-linked programs (such as poverty reduction)	No Change	Improves policy accountability of government.	No Change
		5.3 Implementation of AMIS	No Change	Improves efficiency and consistency of audit practices	No Change
		5.4 Training of PAAS staff to replace consultants	No Change	Achieves ownership and sustainability of audit practices	No Change
Component 3 Project Management					
6. Management skills transfer	No Change	6.1 Transfer of M&E and Change Management skills to CGA/OAG	No Change	Strengthens MoF, CGA, and OAG management skills and builds sustainability	No Change

Table 1.2 Arrangements for results monitoring

Project Outcome Indicators		Baselines		Target Values		Data Collection and Reporting		
		June 2005 Original	**October 2010 (At Appraisal)**	**2011**	**2012**	**Frequency and Reports**	**Data Collection Instruments**	**Responsibility for Data Collection**
Current	Proposed							
1. Effective and transparent fiscal administration *(MTBF in place and FABS-supported)*	No Change	Pilot MTBF implementation underway for 5 federal ministries	Fully rolled out MTBF. No FABS configuration	FABS config-ured	FABS support of MTBF	Annual	Periodic survey[6]	MoF M&E Unit
2. Effective and trans-parent financial report-ing, control, and audit *(timely, reliable financial statements submission and timely audit)*	No Change	Accounts submitted to OAG 3-4 months after due date. OAG accounts 15 months or more after year-end. Quality poor	Accounts to OAG 2 months after year-end; OAG accounts submitted within 12 months of year-end. Quality improved	OAG certification and audit report within 8 months	OAG certification and audit report within 6 months	Annual	Periodic survey	OAG CGA
3. Effectively tracked and managed poverty reducing spending *(timely reliable PRSP reports*	No Change	All PRSP reports prepared manually with no data assurance	System produces PRSP reports; data entry to be further improved	System-gen. PRSP report. PETS initiated	System reports; PETS established	Annual	Periodic survey	CGA PRSP Sect't
4. Effective corruption & inefficiency reducing measures related to accounts and budget control applied (*system monitoring of use of functionality, bills and issuance of cheque etc)*	No Change	Manual issuance of checks & no systematic review of workflow practices	FABS issues checks and provides regular reports on bill-tracking and other uses of system functionality.	System reports established as routine.	System reporting fully under CGA and regular OAG audit.	Annual	Periodic survey	CGA M&E OAG

[6] The M&E Unit of PIFRA II-AF will be responsible for regular monitoring and surveys, and reporting to project management, Bank missions, and project steering committees. Progressively responsibilities for M&E will be taken over by the CGA and OAG to ensure sustainability after AF completion.

5. Establish stable FABS operations and maintenance support in GoP (*implement a data warehouse, an Information security and Disaster recovery plan).*	No Change	FABS operated only at pilot level at commencement of PIFRA II. Most transactions were carried out manually	FABS is now used across the country to prepare and compile the Annual Budget Estimates and process all government expenditure (including payroll) and receipts transactions	SAP upgrade to ECC06; Server upgrade; Data ware-house and security and disaster plan to be fully implemented	All Sites on full work flow (e.g. KP and Balochistan)[7]; FABS support Unit established under the CGA for ongoing maintenance and support.	Annual	Periodic survey	CGA M&E
6. Adequate numbers of trained staff in MoF and CGA to manage and apply system to fiscal and financial management *(trained MoF, CGA, and line ministry CFAOs)*	No Change	Very few staff trained in systems operation or new work practices.	All operational staff of CGA/AG and DDOs trained in work practices at all levels of gov't. Few trained in overall systems operations and management.	Professional training: 20 senior, including operation, staff ; 20 CFAOs	20 senior, including operation staff; 20 CFAOs	Annual	Periodic survey	MoF CGA M&E Unit

[7] Subject to improvement in law and order situation

Intermediate Outcome Indicators		**Baselines**		**Target Values**		**Data Collection and Reporting**		
		May 2005 Original	**October 2010 (At Appraisal)**	**2011**	**2012**	**Frequency and Reports**	**Data Collection Instruments**	**Responsibility for Data Collection**
Current	Proposed							
Component 1: FABS-MoF/CGA								
1. Effective reconciliation of accounts for fiscal reporting and planning								
1.1 Discrepancies between monetary survey credit and government fiscal deficit (for 2004/05 = 1.2% of GDP).	No Change	1.1 Estimated statistical discrepancy 2004/5 -1.2% GDP	<0.5 GDP	Full reconcilia tion	Full reconcili ation	Annual	Periodic survey	MoF M&E Unit
1.2 Issue of reliable, timely budget execution reports (BERs) to PAOs	No Change	No BERS—civil accounts only	90 % coverage of BERs—further data improvements needed	100 %	100% & full commit ment records	Annual	Periodic survey	CGA
2. Accurate, comprehensive, and timely reports, based on international standards of accounting and internal control.								
2.1 Application of IPSAS accounting standards	No Change	Financial statements did not comply with IPSAS.	Financial statements at federal and provincial level now comply with IPSAS as regards cash-basis systems	Progress on impleme nting fixed asset module	Progress on implem-enting other aspects of accruals —part of long-term roadmap	Annual	Periodic survey	CGA OAG
2.2 Implementation of commitment accounting	No Change	No commitments recording	Commitment recording above PKR 0.5m introduced	Impleme ntation of commit ment accounts for all major	Full commit-ment accountin g and reporting	Annual	Periodic survey	CGA

				projects, including those paid thru Assign-ment Accounts				
3. System functionality tracking for improved efficiency and reduced discretion								
3.1 Bills passed within 3 days (%)	No Change	No bill-tracking	Tracking in place at all levels. 12-30 percent bills paid within 3 days	50 %	80%	Annual	Periodic survey	CGA M&E Unit
3.2 All cheques issued by system/direct vendor payment	No Change	Manual issuance of cheques	All cheques issued by system	Direct payments to 70 % of vendors	Direct payments to all vendors	Annual	Periodic survey	
4. Achieve comprehensive data entry to FABS								
4.1 Comprehensive data entry coverage (% expenditure & receipts)	No Change	Coverage of projects, SAEs, foreign-financed transactions, and MoF transactions incomplete or non-timely	All but a few transactions are now covered by the system at object-level, and on time.	100%	100%	Annual	Periodic survey	CGA M&E Unit
4.2 Interfaces with SBP/NBP, NBR & EAD established	No Change	No interfaces with key revenue and financing systems	Interfaces with NBR and SBP near complete. EAD improved but to be initiated	All interfaces in place	As for 2011	Annual	Periodic survey	CGA M&E Unit
Component 2 Audit								
5. Effective and timely audit of government accounts using international standards of auditing.								
5.1 Application of modern audit practices	No Change	Manual, transactions sample-based audit. No staff trained in Financial Audit Manual (FAM) or CAATS. Few with professional degrees	CAATS and risk-based techniques now widely applied (18 performance audits completed—all gov't levels). Staff now trained in FAM (2787 vs target of 1750);	Quality Control Framework effectively operational and used for	Second cycle, Quality Control Framework effectively operatio	Annual	Periodic survey	OAG M&E Unit

			CAATS (1458/1200); foreign training for degrees (30/30); local training for degrees (161/109).	the FY09-10 audit. IS Audit on job training for FAOs' staff. Incorporation of QMF, IS Audit and AMIS into regularity audit practices.	nal and used for the FY10-11 audit. IS Audit on job training for FAOs' staff. Incorporation of QMF, IS Audit and AMIS into regularity audit practices			
5.2 Performance audit of policy-linked programs (such as poverty reduction)	No Change	Few policy-oriented audits.	A range of poverty-linked programs now subject to audit.	Development of Performance Audit Manual. Revision and development of guidelines.	Training of 30 PAAS officers on performance audit and supervision of 3 audits by the consultant.	Annual	Periodic survey	OAG M&E Unit
5.3 Implementation of AMIS	No Change	No formal audit management information system (AMIS	Substantial delays in design and tendering for AMIS	Acquisition of software and prelimina	Roll-out to key sites	Annual	Periodic survey	OAG M&E Unit

				ry pilot				
5.4 Training of PAAS staff to replace consultants	No Change	During transaction roll-out-a heavy reliance on consultants.	PAAS playing increasing role—but still dependent on consultants.	Phased reduction of consultants, reducing total number from 50-54 to 36-40. PAAS officers trained on FAM, Performance and IS Audit	Only Audit experts and few supervisors to be reatained till project end. Additional 25 PAAS officers trained on FAM, Performance and IS Audit	Annual	Periodic survey	OAG M&E Unit
Component 3 Project Management								
6. Management skills transfer								
6.1 Transfer of M&E and change management skills to CGA/OAG	No change	Limited skills transfer in transactions roll-out phase of PIFRA II	Awareness of M&E and CM heightened, but little formal skills transfer	Joint work with MoF/CGA/OAG and PIFRA team	Full take-over of M&E and CM functions by GoP	Annual	Periodic survey	MoF CGA OAG PIFRA

Table 1.3 PIFRA II Outcome Assessment: July 2010

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
Effective and Transparent Fiscal Management					
1. Effective reconcile-iation of accounts	**1.1** Aggregate CGA/SBP reconciliation	Continuing very large discrepancies between monetary survey credit to general government and fiscal deficit were experienced. Shown in Pakistan Fiscal Operations (PFO) report on MoF website. Derived by manual adjustment to AGPR data (Estimated discrepancy 2004/5 -1.2% GDP). Reports on reconciliation at each level of government are considered by federal and provincial Fiscal Monitoring Committees (FMCs). However, FMCs were relatively inactive at PIFRA II inception, and follow-up on issues was limited.	**1.1** Statistical discrepancy over the past 3 quarters of PFO has ranged from 0.025-0.01 % GDP. All areas contributing to the discrepancy have been identified and are being addressed as part of the process of system generation of federal level PFO accounts. FMCs have been revitalized but appear less necessary as system reconciliation and interfaces are established. CGA should take over main function of ensuring reconciliation at all levels of government. .	Proper recording of accounting entries according to NAM to enable federal unidentified expenditures to be reduced to no more than 0.5% of total expenditure by end-FY2009	Improved reliability of data for macro-economic management and achievement of MDGs.
	1.2 FBR/AGPR/ Bank interface	No interface to facilitate reconciliation between AGPR, FBR treasuries, SBP/NBP, or EAD	**Interfacing AGPR-SAP with SBP, NBR, and EAD**: (i)Good progress has been made in establishing an interface between AGPR and NBR. Interface being tested (ii)Manual reconciliation has been relatively successfully established to reconcile EAD and AGPR data on foreign financed projects. An AGPR/EAD (DMFAS) interface should be feasible, but has not yet been implemented. (iii) The SBP has agreed to provide data as per fields defined by PIFRA to facilitate reconciliation of fiscal and monetary accounts, but has not yet provided a portal nor current data.	Full reconciliation at federal and provincial levels by FY 2009, using PIFRA interfaces with SBP/NBP/CBR/Planning	
	1.3 Audit of reconciliation	Reconciliation mentioned as an issue for some agencies, but not addressed as a systemic issue	OAG have conducted two data sufficiency audits of the FABS (for 2006/7 and 2008/9 accounts), that, among other things, review data entry and reconciliation processes. Such system reviews will become part of OAG's regular audit practice.	Not specified, but important element of	

[8] Assessment of situation at end of PIFRA I.

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
				OAG oversight of GoP-wide accounting issues.	
2. Fiscal Responsibility and Debt Limitation Law (FRDL) and Macro-fiscal Manage-ment	**2.1** SAP-generated macro-fiscal reports	Capacity for systems-generated macro-fiscal reports not available. Reports compiled manually by MoF from CGA, SBP, and EAD data two months after the end of the quarter. No fully reconciled PFO is prepared based on year-end final data.	The COA has now been full mapped to the GFSM-2001economic classification and can generate Pakistan Fiscal Operations (PFO) reports at the federal level. Some remaining data entry issues (particularly timely entry of MoF-sanctioned transfers and improvement of project reporting) have to be overcome to allow timely reconciliation.	Not specified, but important area of interaction between accounts and fiscal policy.	Reliable reports monitoring fiscal balance and debt used as basis for economic policy and for statutory fiscal reports.
	2.2 Recon-ciliation of foreign debt and aid flows with AGPR/ AGs	Limited coordination of debt management and accounting systems. Debt records maintained by DMFAS and AGPR not consistent. Reconciliation of debt and foreign aid transactions between EAD and SBP does take place regularly and data are given to AGPR/CGA. Comprehensive transactions reconciliation with AGPR is not in place, however, as some transactions (third party payments) do not pass through AGPR accounts and are not brought promptly to account in line with Finance Division requirements.	Completion of interfaces (see 1.2 above) will greatly facilitate reconciliation—and addressing the underlying issues has already contributed to improved reconciliation. Reconciliation of data on federal projects is one of the main remaining problems because of late and incomplete submission of payments schedules (without inclusion of third-party payments		
3. Implem-entation of MTBF	**3.1** Federal Ministries MTBF/ SAP program budgeting progress	<u>Federal level</u>: Pilot MTBF implementation underway for 5 federal ministries in phase 1. Phase 2, emphasizing top-down ceilings for ministries, underway from December 2006. No use of PIFRA facilities proved possible during phase 1.	**3.1**. MTBF has been fully rolled out to all ministries and the budget preparation process consolidated: (i) a single budget circular to all ministries covering revenue budget, development budget, and MTBF; (ii) MTBF (Green Book) presented to parliament at same time as Demand for Grants (White Book) estimates (iii) a Budget Strategy Paper covering macroeconomic strategy reviewed by Cabinet as part of budget preparations. Forward estimates (indicative ceilings) for 2010-2013 were presented as part of the 2010/11 budget. These will need to be reviewed in light of recent budget cuts.	Federal budgets for FY 08 and beyond prepared under MTBF principles.	Accountable forward projections of the budget will increase capacity of federal and provincial governments to direct fiscal policy and

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
			PIFRA has been configured to apply the MTBF output-oriented budget classification and incorporate this in the COA, but the SAP upgrade is essential to establish a user-friendly budget preparation module in the system. FABS support to MTBF is factored into the PIFRA II-AF project extending PIFRA II to end-2012.		improve transparency.
	3.2 Provincial MTBF/ SAP program budgeting progress	Limited work in provinces, with no coordination with federal efforts.	**3.2** Punjab Province is developing its MTBF and has been liaising with the Federal MTBF on technical issues. Some work is being initiated at KP. Once the functionality developed by PIFRA has been proved at the federal government level, it should, in principle be equally applicable to provinces.		
Effective and Transparent Financial Reporting, Control, and Audit					
4. Timely monthly budget execution reports to MoF and PAOs	**4.1** Federal/ Provincial/ District reporting	Federal and provincial monthly civil accounts are prepared from 15-21 days after month-end. Data neither comprehensive nor reliable. Format of reports limited to actual spending without budget data and do not allow PAOs to check status of budget execution against authorization	**4.1** AGPR and all the four AGs are generating budget execution reports (BERs). Provincial BERs are increasingly moving to real-time accounting for some SAEs—all cheques for provincial Works and Forests (other than KP Forests, which is resisting change) are entered in the system through DAOs (without pre-audit) which allows recording of expenditure by object at time of actual spending. Federal projects operate through assignment accounts and neither project directors nor the federal MoF wish to change procedures to achieve real-time recording of expenditure. Accounting in Balochistan remains problematic for many districts because of capacity constraints.	Budget execution reports available within 4 weeks of month-end by 2007. Accurate, timely, and comprehensive statements used for decision-	Improved capacity of policy-makers to review and adjust policies in line with current situation.

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
	4.2 Sub-district reporting	1. The principle of applying a NAM-compliant system was agreed but no coordinated action to promote implementation. 2. Some assessments of TMA financial management needs have been done, but a full survey is not widely available	Overall the situation has improved substantially from the baseline position. Timeliness has not yet improved but will do so when data entry issues are resolved. Availability of comparisons with budget data and more reliable expenditure data have greatly improved information available to PAOs. Budgeting in KP TMAs has been converted to COA. Similarly, the accounts in Punjab were converted to COA through mapping with old COC. Floods have delayed decision of provinces regarding restructuring of TMAs therefore FABS has not yet been extended to TMAs.	making by PAOs and the MoF, by 2008	
5 Strengthen-ing internal controls	**5.1** Financial controller appointments and internal control plan	Internal control recognized as weak (2004 CFAA). In 2005, 15 Chief Audit Officers (CAOs) appointed, but support and management integration not in place. An Internal Audit Manual was prepared in 2002, but not printed or distributed	**5.1** Following a range of discussions and workshops held over the past few years, Cabinet has recently made a decision to phase out the MoF Financial Advisor posts and empower PAOs to manage ministry budgets with the assistance of CFAOs who will be appointed to each ministry. A considerable amount of work will be required under the proposed AF to ensure that this change effectively strengthens financial control. It is envisaged that, as early as possible, an international consultant will be hired to review the scope of work and degree of support required for the PAOs and CFAOs to carry out their duties. The MoF instructions in the *System of Financial Control and Budgeting, September, 2006* will need revision and extensive training of CFAOs and support officers will be required. CFAOs are expected to have duties related to MTBF service delivery management as well as financial control functions.	Preparation of internal control manuals and Auditor General's annual report on internal controls.	Improvement of internal control and audit essential to fiscal management and an important input to external audit.

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
	5.2 Review and audit of internal control .	From 2004-5, all AGP reports to the President and provincial governors make high-level comments in a separate chapter on internal controls. Reports indicate systemic weaknesses and recommend steps to be taken by PAOs, but greater depth of systemic analysis is required	**5.2**. There are now extensive audit comments on financial control, although until there is a systemic overhaul, these have continued to focus on individual weaknesses. The FY 2007-08 Audit report of Federal government focused on foreign debt reconciliation, proposed a need assessment to be carried out by government for all significant loans, policy for recovery of relent loans, foreign debt hedging required, grants disbursements required, internal audit department /staff at EAD required.		
	5.3 Personal Ledger Account (PLA) numbers & controls	PLAs present problems of control and scope for discretion. As of June 2005, there were a total of 2714 PLAs (including 770 non lapsable). Total PLA receipts for 2004-5 were PKR 103.3 billion (60.8 at federal level) and payments PKR 110 billion (68.6 federal). Controls were exercised by restricting permission to open accounts, but these did not give effective control and caused complications for reconciliation of accounts (see 1.1 above)	**5.3** PLAs are largely not used at federal level, but SAEs, such as Pakistan Public Works Department, continue to use PLAs. As noted above, however, assignment accounts continue to present problems with regard to comprehensive and timely recording and reporting.		
	5.4 Project accounting and reporting	Control over development projects was limited prior to PIFRA II by the practice of issuing single-line appropriations for many major development projects	The project accounting system of SAP is now activated in all federal HQ and regional offices, and at all provincial HQ and DAOs (except for Balochistan DAO offices). Object-wise classification of project expenditures is in place at all of the above (except Balochistan district). However, most large development projects at federal level use		

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
			Assignment Accounts due to which project accounting remains incomplete.		
6. Timely, reliable end-of-year financial statements	**6.1** Federal Provincial and District accounts	In 2004-05 (see Annex V) there was a 3-4 month lag between due date (7 months after year-end) and actual submission of accounts by respective AGs to OAG and, correspondingly, accounts were certified 15 months or more after year-end by the OAG.	The 2008/9 federal and provincial accounts were submitted by all AGs around end-August 2009 (2-3 months before the due date). Delays were experienced, however, for submission of district accounts by Balochistan, KP, and Sindh. Federal and provincial (including AJK) financial statements were certified and audit reports issued by OAG within 8 months of year-end. Some district accounts (Sindh, KP, and Balochistan) continue to experience delays. It is anticipated that these times will further improve as data entry issues are resolved. District governments in Balochistan have been abolished since July 2010.	Audited accounts presented to the legislature within 12 months of the end of the fiscal year by FY 2008.	This standard is a basic element of fiscal and financial accountability.
7. Imple-mentation of financial reporting including adoption &implement ation of internat-ional accounting standards	**7.1** Commit-ment accounting	Policy is to progressively implement international standards (IPSAS). NAM, although mainly cash, embodies capacity for commitments and essential asset and liability accounts.	**7.1** The CGA has issued instructions on mandatory recording of commitments, to the PAOs. Any purchase of asset valuing Rs 500,000 and above shall be recorded as commitment through commitment Advice Form 4-C. Claims shall be not be entertained if the instructions are not fulfilled from 1 July 2009.Commitments are now being recorded at provincial and district level. Federal project directors are not yet recording commitments. CFAOs will play a major role in ensuring commitment recording as part of financial control.	Not specified beyond NAM	A progressive move toward implementation of IPSAS will provide a sounder base for fiscal and financial decisions.
	7.2 Fixed assets module	Fixed Asset module not activated	Preliminary steps are being taken to establish inventory control, but full use of fixed assets accounting is seen as a long-term objective in the context of eventual adoption of accrual accounting. A road map toward accrual accounting will be prepared before the Dec. 2010, but its implementation will be over a long period.		
	7.3 IPSAS Financial Reporting &	No IPSAS-consistent statements were initiated under PIFRA I.	Financial statements at federal and provincial level now comply with IPSAS as regards cash-basis systems		

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
	Long-term plans				
8. Effective audit of government accounts		Preparation of manuals and field guides initiated during PIFRA 1. Limited numbers of staff had received SAP or CAATs-related training.. No performance, risk-based, or system-based audit practice had been established.	Extensive training of OAG staff has been carried out by July 2010on application of the Financial Audit Manual (FAM) (2787 vs target of 1750); CAATS (1458/1200); foreign training for degrees (30/30); local training for degrees (161/109). FABS has facilitated CAATs audit to replace manual transactions audit—greatly increasing efficiency and timeliness of audit. A range of special audits (at request of parliament or government), performance audits, and project audits are now carried out at all levels of government. Certification and regularity audit are being progressively linked in time to ensure overall accountability.	Modern auditing practices are used to audit all districts and self-accounting entities audited by 2007 and provincial and federal by 2008.	More effective and efficient auditing practices will enhance accountability.
Indicators of Poverty Reduction					
9. Tracking poverty reducing spending	**9.1** Data reliability assurance	The PRSP Secretariat prepared manual reports drawn from the civil accounts and subject to data limitations of the manual AGPR/CGA accounts.	System-generated PRSP reports are being produced by FABS, but data entry problems (outlined above) have to be resolved to improve reliability. Further investigation of service delivery in vertically integrated programs is required.	Not specified.	Improved reliability of data combined with assurance of effectiveness of spending would enhance credibility of poverty reduction efforts.
	9.2 PRSP surveys on effectiveness of spending.	Regular surveys of the impact of spending rely on the Pakistan Integrated Households Survey (PIHS), and through use of a Core Welfare Indicator Questionnaire (CWIQ) in a new data series the Pakistan Social and Living Standard Measurement (PSLM). Issues of service delivery through the budget were not systematically addressed.	PRSP have initiated a joint program with UNDP which will include some work on a public expenditure tracking system (PETS)		
	9.3 Audit of PRSP programs	Some audit observations are made for instance, on the mismanagement of Khushal Pakistan Program. However, no explicit emphasis was given to the PRSP in the audit program or in audit reports.	Poverty reduction programs are now regularly subject to performance audit.		

Indicator Area and Implementation Indicators		Baseline Assessment[8]	Implementation Progress Assessment (July 2010)	PAD Indicative Benchmark	Outcome Impact
Indicators of Reduction of Inefficiencies and Corruption					
10. Corruption-reducing measures related to accounts and budget control .	**10.1** Transaction processing time	Prior to PIFRA II, transaction processing times were governed by Government Finance Rules, which set a benchmark of 14 days. Some manual data on transaction processing was maintained, but no reliable estimates of average processing time was available	Following CGA instructions and DAO training, the bill-tracking system is functional at Provincial AGs and the AGPR as well as most DAOs. The system is helping to identify slow payments and reduce overall payment delays.	Not specified.	Improvements in processing and removal of discretion will reduce opportunities for corruption.
	10.2 Reduced discretion: -payroll -suppliers -cheques -PLAs & other discretionary accounts	No scope for system-based payment or system issuance of cheques. PLA treatment, as described, provides opportunities for discretion and is weakly controlled.	System issuance of cheques is now applied at federal, provincial, and district level (apart from some districts in KP and Balochistan on nonworkflow sites). System reports can track and verify system check issuance. PLAs are largely being eliminated or measures taken to track expenditures in real time.		
	10.3 Risk-based audit	Audit was traditional and transaction-based prior to PIFRA II. While fraud cases were uncovered during routine audit and certain corruption sensitive areas identified and reported (such as contract management and alteration of contract TORs post-contract), the lack of a systems and risk-based approach meant that it had limited impact and was less visible	**10.3** Audit plans and audit techniques are now substantially formulated on the basis of a formal risk assessment.		

Annex 2: Operational Risk Assessment Framework (ORAF)

Project Development Objective

Project's development objectives are to: (a) build capacity to improve accuracy, comprehensiveness, reliability, and timeliness of financial and fiscal reporting at all levels of government; (b) improve public financial management, accountability, and transparency; (c) enhance the capacity of public sector managers to use credible financial information for better and informed decision-making; and (d) facilitate oversight of the use of public monies, and increase the national and international credibility of government's financial statements and assurance processes

PDO Level Results Indicators:	1. Effective and transparent fiscal administration *(MTBF in place and FABS-supported)*
	2. Effective and transparent financial reporting, control, and audit *(timely, reliable financial statements submission and timely audit)*
	3. Effectively tracked and managed poverty reducing spending *(timely reliable PRSP reports)*
	4. Effective corruption & inefficiency-reducing measures related to accounts and budget control applied (*system monitoring of use of functionality, bills and issuance of cheques etc)*
	5. Establish stable FABS operations and maintenance support in GoP (*implement a data warehouse, an Information security and Disaster recovery plan*).
	6. Adequate numbers of trained staff in MoF and CGA to manage and apply system to fiscal and financial management *(trained MoF, CGA, and line ministry CFAOs)*

Risk Category	Risk Rating[9]	Risk Description	Proposed Mitigation Measure
Project Stakeholder Risks	Low	Reserved support by FD for implementation may limit progress in capacity building. Lack of donor support may limit progress in utilizing system for donor-funded projects, thereby reducing reliance on country system. Lack of public support may limit acceptance of the system.	Increasing involvement of the FD in implementation as an integral part of AF design should consolidate GoP support. Delivery of fiscal reports will underline utility of FABS to FD. Increased public/donor awareness of the project's objectives and accomplishments.
Implementing Agency Risks	MI	Management capacity, governance failures, the possibility of fraud and corruption pose the greatest risks. However, such risks are mitigated by the project design, which is specifically designed to improve management capacity and governance. In addition, emphasis is placed on monitoring systems and an independent audit by a private is carried out.	
Project Risks			
o Design	Low	Failure to provide counterpart staff for capacity development will impede project implementation	Trainings provided under the Project will enhance capacity.

[9] Rating of risks on a four-point scale – Low (low impact/low likelihood); ML (low impact/high likelihood); MI (high impact/low likelihood); and High (high impact/high likelihood).

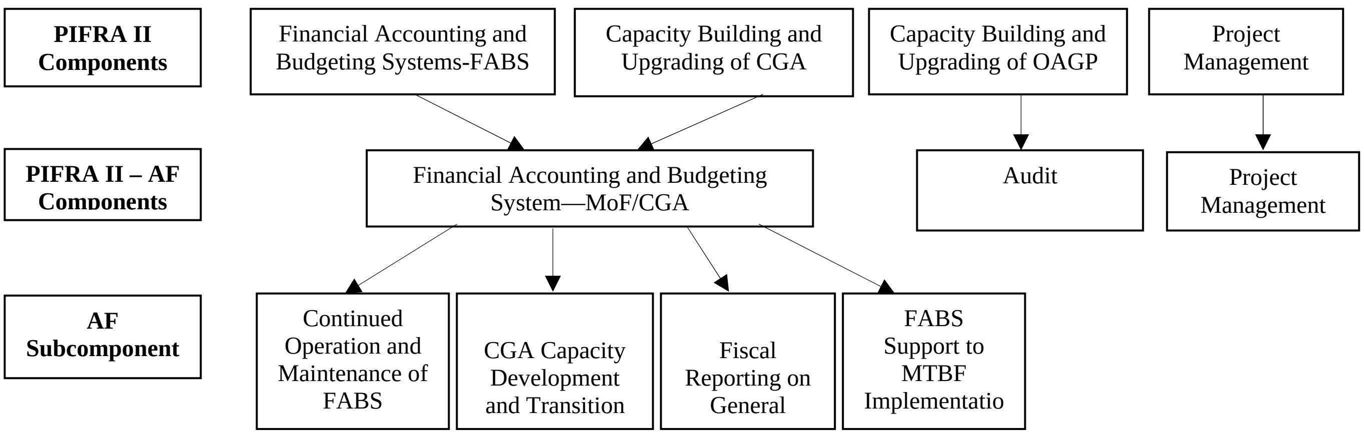
Risk Category	Risk Rating[9]	Risk Description	Proposed Mitigation Measure
o Social & Environmental	Low	Limited additional impact.	No additional measures needed
o Program & Donor	Low	Continuing close cooperation with the MTBF is important, and failure in this respect could reduce the impact of both projects.	Establishing capacity for SAP to provide full functionality for MTBF budgeting and reporting is a continuing objective fully incorporated in the project design.
o Delivery Quality	MI	Potential failures in different aspects of implementation could give rise to problems of data quality or failure to properly use system functionality.	A continuing emphasis on project management, M&E, and data adequacy reviews by the OAG should ensure that delivery quality is maintained and established sustainably for the future.

Overall Risk Rating at Preparation	Overall Risk Rating at Implementation	Comments
MI	MI	A MI risk rating is justified in part because of the substantial achievements already in place as a result of PIFRA I and II, the revised governance structure, and the emphasis on vigilant monitoring by project management as well as by the OAG. future.

Annex 3: Detailed Project Description

1. Under Additional Financing, the Project's overall development objectives and scope will remain unchanged from PIFRA II. However, there will be a realignment of the Project components and accordingly the institutional arrangements.

2. Additional Financing will comprise three main components, aligned with the PIFRA II structure: (i) Financial Accounting and Budgeting System—MoF/CGA; (ii) Audit; and (iii) Project Management. Component 1 is centrally concerned with the continued operation and maintenance of FABS, capacity building and transfer of responsibility to the MoF and CGA. Because the MoF/CGA will take over the FABS operations and maintenance during the AF period, it unifies the former PIFRA II components 1 and 2. Component 2 of AF provides additional resources to establish the Audit Management Information System (AMIS) initiated under PIFRA II and to transition system and performance audit practices fully to the OAGP. Project management will be maintained to oversee all project operations and promote transition arrangements.



COMPONENT 1: FINANCE AND BUDGETING SYSTEM (FABS)—MOF/CGA

3. The bulk of resources for this component are necessary to ensure continuing support for operation of the system, strengthen the capacity of FABS to produce fiscal reports, to integrate it with the MTBF, and to link both systems to overall PFM reforms. This component should establish a firmer relationship between budgeting and accounting and allow the MoF to use the SAP system as a platform for further PFM reform.

4. The following sections summarize the key activities to be undertaken in the four sub-components of Component 1. Further details of issues and actions to be undertaken to maintain and operate the system under sub-component 1 are given in Annex 4, and for issues of capacity building and transition of functional responsibility fully to the MoF/CGA under sub-components 2-4 in Annex 5.

Sub-component 1.1: Continued Operation and Maintenance of FABS

5. FABS is now used by the federal, provincial and district governments to: (i) prepare and compile the Annual Budget Estimates and fulfill associated reporting

requirements; (ii) exercise ex-ante budgetary control on and enable processing of all government expenditure and receipts transactions; (iii) implement commitment controls on contract amounts of PKR 0.5 million and above; (iv) make payments (currently by cheque) against bank accounts where Government funds are held; (v) prepare the payroll for some 1.9 million Employees across all levels of Government; (vi) make pension calculations for all Government pensioners; (vii) maintain the GPF accounting for all Government employees; and (viii) prepare periodic budget execution and fiscal reports for all stake holders, including the MoF, Provincial Finance Departments, and Line ministries and departments.

6. To date, FABS has been implemented at the federal Ministry of Finance, all provincial finance departments, the District EDOs (finance) and a number of line ministries and departments under each level of Government at the center and in the provinces. In addition, it has been implemented at the office of the CGA, the AGPR, all the provincial AGs, and all the provincial AGPR sub-offices. A total of 118 sites have been completed out of 143, which include all the District Accounts Offices (DAOs), AGs, AGPR sub-offices, federal and provincial treasury offices, and nearly half the TOs in Balochistan are expected to be converted to DAOs with complete workflow by September. Systems implementation is essentially complete at the Center, and in the provinces of Punjab, Sindh and Khyber Pakhtunkhwa (KP). It is in the process of being rolled out to all DAOs/TOs in Baluchistan. In addition, the system is also being extended to Azad Jammu-Kashmir (AJK) and payroll is run on the system in 7 out of 10 districts and accounts are prepared on FABS in 3 districts. Four Self Accounting entities (Ministry of Foreign Affairs, Pak PWD, Pakistan Post Office and Geological Survey) are connected to the network and prepare their accounts on FABS. The current site implementation status is provided in Annex II.

7. All the key participants in Government budgeting and accounting and auditing processes at the federal, provincial, district levels of Government have transitioned to and are critically dependent on these systems for their day to day operations and functioning.

FABS Activities to be Financed

8. With most of the sites productive, the emphasis is now on: (i) deepening reform by ensuring that core systems functionalities (i.e., budgeting, accounting, payroll, GPF, and pensions) available in the system are implemented fully and uniformly at all levels of Government; (ii) improving the comprehensiveness, accuracy and timeliness of the data being entered into the system and that of the reports and financial statements produced by the system and ensuring their ready availability for the Financial Managers at the federal, provincial and district levels, including the Principal Accounting Officers (PAOs) in line ministries and departments; and (iii) ensuring that transaction processing while using the system is implemented as was intended and in a manner that optimizes system use, eliminates redundant business processes such as maintenance of manual ledgers and registers, and follows standard accounting and data management and control practices.

9. In addition several activities under this component need to be completed to: (i) ensure the continued stability of the hardware/ software technology platforms and the

FABS network; (ii) implement interfaces with other Government systems such as the State and National Bank of Pakistan (SBP and NBP), and the FBR; (iii) improve the data analysis capabilities by implementing a data warehouse; (iv) implement a comprehensive information security and disaster recovery plan; and (v) provide FABS support to the MTBF process.

To Be Financed From Original PIFRA II

10. PIFRA is currently engaged in several activities under the FABS component that will spill over beyond the closing date. These include: (i) extension of the system to the remaining DAOs/TOs/EDOs in Baluchistan and AJK, and to large Tehsil Municipal Administrations (TMAs); (ii) completion of connectivity to Line Departments; (iii) extension to foreign funded projects; (iv) up-gradation of SAP software;[10] (v) design, procurement and implementation of an Information Security/Disaster Recovery Management System; (vi) upgrade of servers at the Center and provinces and replacement of old workstations; (vii) establishment of a data warehouse facility; (viii) implementation of support to the MTBF process for the Finance division; and (ix) establishment of an interface with SBP, NBP and FBR.

11. Most of these elements have already been contracted for and PIFRA II resources committed to finance them. It is estimated that an amount of US$ 15.50 million and a period of two years would be required for completion of these tasks. Therefore, Bank extension of the closing date of the project to June 2013 would allow these activities to be completed and PIFRA II resources will continue to be available for completion of these tasks.

To Be Financed from Additional Financing

12. In addition to the above, PIFRA would require additional resources to ensure the continued operation and maintenance of FABS. The major items that will require financing over the next two years relate to: (i) the contracted maintenance costs of the hardware elements of the country-wide network set up to implement the FABS system and the replacement upgrade costs of some elements of this network; (ii) the contracted annual license fees for the application and systems software and costs associated with software upgrades; (iii) the costs associated with operation of the FABS network, including telecommunications costs, arrangements to ensure adequate power supply at the various FABS sites, special stationary, etc.; and (iv) the costs associated with the operations of the SAP CC and financing the salaries of consultants/ specialists and ongoing training activities.

13. **Post PIFRA FABS Organizational Arrangements.** It is necessary that the GoP makes appropriate arrangements to take over continued operation and maintenance of the FABS network after the project closes. Smooth operation of the system requires that the: (i) physical elements of the network are maintained on a day to day basis; (ii) software

[10] PIFRA needs to upgrade its software to the latest version ECC06 to avoid exorbitant annual maintenance charges and also to provide additional functionality directly required for the public sector (i.e., MTBF support).

elements, including the system databases are maintained to operate in an optimal fashion; and (iii) end users are responsible for functional aspects and for carrying out their work on the system (e.g., running the payroll, transaction processing, etc.).

14. The first two tasks will need to be performed by a central organization. Currently these tasks are carried out by the FABS directorate of PIFRA. During the course of the Additional Financing operation, the staff and resources of the FABS directorate should be transitioned to the Office of the CGA. The CGA is the preferred location of this function since it and its subordinate offices, including the AGs, are responsible for the bulk of the transaction processing that is carried out on the system. The tasks associated with the routine operation and maintenance of the system should therefore logically be its responsibility. However, for the CGA to be able to take over this function it will need to develop its capacity. This is discussed in greater detail in Annex III.

15. **Sub-component 1.2: CGA Capacity Development and Transition Plan.** Because of limited capacity in the CGA, a two year transition phase is necessary to allow critical expertise to be put in place. SAP CC units servicing Islamabad HQ and the provinces, now stationed in PIFRA-FABS, will be streamlined and transferred to the CGA. The CGA will establish a Quality Assurance Cell to review system functionality and performance. A short-term (around 3 month) international consultancy will prepare an organizational and functional plan for FABS IT set-up in the CGA, and appropriate local consultants will be hired to guide its implementation.

16. With the phase out of Finance Advisors (FAs), Chief Finance and Accounts Officers (CFAOs) will have major new responsibilities for financial control and budgeting. The CFAO role will require some redefinition to meet the requirements of both the functions taken over from the FAs and the implementation of the MTBF. The CGA will play a key role in overseeing the CFAO function and training the staff. It is proposed that an international consultant provide assistance to the CGA to define this role and to establish a training program (which will include short-term local/foreign training for both CGA staff and CFAOs). This work should be closely coordinated with MoF activities on the role of the CFAOs. Further assistance to CFAOs will be given by acquisition of a software/search engine to facilitate access to rules (MoF, Planning Commission, Establishment Division, etc.).

17. Another area where closer cooperation between the CGA and the MoF is required is in the area of commitment accounting. The CFAOs will play an important role in embedding commitment control into financial management practice. Recording of commitments is not yet satisfactory, in particular for federal projects under assignment accounts. Project directors are not recording commitments on the system and do not record their expenditures in real time, but rather through monthly schedules—often provided with substantial delays. Real time recording of expenditures in the provinces has been achieved both for projects and for self-accounting entities by requiring cheques to be endorsed and recorded by the DAOs prior to encashment. The NBP has co-operated by refusing to cash non-endorsed cheques. This process greatly simplifies bank reconciliation and enhances the accuracy and reliability of financial reports for the PAOs and finance departments. The

FD and CGA should develop a similar (or equally effective) procedure at the Federal level to enhance commitment control and financial reporting.

18. **Sub-component 1.3: Fiscal Reporting on General Government.** Financial and fiscal reporting has been substantially improved under PIFRA II and the PAD benchmarks have been substantially achieved. A few issues remain to be addressed (particularly that of timely entry of FD-sanctioned transactions into the system), but early in the AF period, quarterly production of the federal Pakistan Fiscal Operations (PFO) report through the system should be feasible. Once the principles are fully tested, consolidation of federal and provincial accounts in a general government PFO should be achieved by end-2010/11. The CGA/AGPR would perform all of the technical work to produce the fiscal reports, but the FD will have overall responsibility for the format, publication, and use of the PFO—as is currently the case. An additional consultancy will be required for this sub-component, particularly to consolidate provincial and federal accounts.

19. Some further measures are necessary to consolidate the PFO process. The MoF should take the lead, with the CGA/AGPR responsible for accounting and systems aspects. Technical assistance will be sought to establish and help implement a Chart of Accounts (COA) Review Unit with responsibility for reviewing the COA (see further discussion in Annex III). It is also desirable that the MoF review the present format of the published PFO and take steps to align it more closely with standard GFSM-2001 presentations. Since the present PFO is an important tool in any arrangements with the IMF, it may be appropriate to seek their comments on proposed changes—at least in relation to the present Stand-By Arrangement. Beyond this, the question of the entities included or excluded from general government warrants further examination. It is recommended that a review of the statistical classification of government entities be undertaken during the AF period. Such a review could involve a request to the IMF rather than AF resources.

20. PRSP reports represent another aspect of fiscal reporting at general government level requiring further consolidation during the AF period. The system has successfully generated reports covering all PRSP sectors, and the quality of PRSP reports should progressively improve. There are, however, some underlying problems with PRSP reports in that sector reports involving vertical government programs do not always represent expenditures at service delivery levels. A review of key service delivery programs, possibly incorporating some element of a public expenditure tracking survey (PETS) would help to further strengthen the PRSP reporting through the system. Consultancies to undertake such reviews will be conducted during the AF period and would be integrated with ongoing work of the PRSP Secretariat.

21. **Sub-component 1.4: FABS Support to MTBF Implementation.** The MTBF has now been rolled out to all ministries and the 2010/11 budget was presented to the parliament in both the traditional White Book (demand for grants) form and in the Green Book (MTBF) format. Integration of the MTBF on the SAP platform, which has been delayed pending acquisition of the SAP upgrade, will give greater assurance of data integrity and will link budget preparation and budget execution more closely. The upgrade version will be financed under PIFRA II and should be available by end-2010. The target should be to establish preparation of the 2012/13 budget on SAP, and configuration should

be initiated as soon as practicable after the software upgrade is acquired. Provision is made under FABS for enhancement of systems related to MTBF.

22. A fully integrated budget preparation and accounting system will be a very powerful financial management tool. However, given the relative inexperience of government managers—and the new CFAOs—in operating this tool, it is essential that sufficient skilled and experienced consultants are retained to support and train the GoP staff. DFID funding for this phase of the project ends in August 2011 and, consequently a decision has been made to reduce the number of IT staff and financial consultants starting from July 2011. Drawing down support at this stage may pose risks for the sustainability of budget and financial management reform. Alternative options should be explored with development partners to ensure continuity of MTBF implementation.

23. **Component 2: Audit.** Overall, this component has met its basic objectives of conducting the audits using modern audit techniques and presenting the audited accounts to the legislature within 12 months of the close of the fiscal year. Audits for the federal and provincial governments have been completed and audited financial statements along with audit reports submitted for presentation to the legislature within 8 months of the close of the fiscal year ending 30 June 2009. International Public Sector Accounting Standards (IPSAS)-compliant audited financial statements, along with audit reports of all district governments for the financial year 2008-09 were submitted to the Governors of the respective provinces within 11 months of the close of the fiscal year. These are significant achievements of PIFRA II considering that prior to the project the time lines for completion of audits ranged from 18 to 33 months.

24. The audit methodology has been improved by the use of the risk-based approach as compared with the largely voucher-driven audits conducted prior to the reforms introduced under PIFRA II. The OAGP now uses Computer Assisted Audit Techniques (CAATs) and EDP auditing tools to plan, select and perform procedures as a part of its audit execution. Quality of audit reporting has improved with increased focus on performance audits, as well as alignment of the results of regularity and certification audits. Audited financial statements have been made available to the general public by posting these on the CGA website.

25. There are however activities under the project that are not yet fully realized and are critical in order to ensure that the objectives of the project are fully realized. The Quality Management Framework has been finalized and requires support of consultants for timely implementation. The consultants hired for developing and implementing Information Systems (IS) Audit guidelines have completed their ground work and the field testing of the audit methodology is in hand. Completion of these initiatives will enable the OAGP to adopt ISACA standards. Training of sufficient number of PAAS officers to sustainably conduct all activities of the audit without the support of consultants is another critical activity. There is a need for structural reform in audit planning, execution and reporting to allow the OAGP to achieve improved ratings under the PEFA framework, as well as in the conduct of procurement audits and reporting of systemic issues of government wide practices on budgeting, revenue generation, status of internal control and internal audit

activities. These activities are planned to be completed through the implementation of the Audit Management Information System (AMIS).

26. Additional Financing and extension of the PIFRA project will provide the necessary space to consolidate the reforms already achieved, including capacity building and additional training of OAGP staff in financial, performance, and IS Audit, consultancies, enhanced procurement of EDP Auditing Tools, and other operational activities of the component.

27. The funds under the audit component will primarily be spent on AMIS related activities, which are capped at about US$ 2.0 million under PIFRA II. PIFRA needs to carefully review the funds available under PIFRA II and the allocation under the Additional Financing credit to assess whether the AMIS software as currently scoped is feasible. The Bank team reiterates that any NOL from the Bank is subject to the availability of adequate IDA resources and confirmation from the government that it will meet any shortfall in funds.

28. **Component 3: Project Management.** The overall performance of the Project Management Unit (PMU) has been satisfactory. The project management team should remain intact during the two-year transition phase and the unit should be strengthened under Additional Financing to allow for improved reporting of monitoring indicators to the various technical and steering committees. Other cross-cutting activities supported under the aegis of the PMU shall continue under Additional Financing to enhance the value of improved coordination under the revised institutional and implementation arrangements.

29. The Director of Outcome Monitoring and Evaluation (M&E) is now reporting to the Director of the Change Management Unit, rather than directly to the Project Director. The M&E work is crucial to informing the stakeholders and the Bank team of what is concretely being achieved on the ground and whether the project is meeting its developmental objectives. Therefore, M&E should report directly to the Project Director, and priority should be given to transitioning the application of robust M&E techniques to the CGA, MoF, and the OAGP during the extension period. Further, the M&E structure should be fully established with a Head whose experience and qualification are satisfactory to the Association.

Annex 4: Financial Accounting and Budgeting Systems (FABS)

1. The PIFRA I and II projects have implemented a group of systems for budget preparation, budget execution, accounting and fiscal reporting to be used at the federal, provincial and other levels of Government in Pakistan. These are the Financial Accounting and Budgeting Systems (FABS). FABS has been implemented using an internationally well known and widely used off the shelf application software package that was acquired by the GoP after international competitive bidding.

2. With the implementation of the FABS based GIFMIS, a repository of all Government expenditure and receipt transactions is now available to the Government audit organization to perform its audit functions. The audit organization has deployed a number of automated tools to perform their work, which includes Audit Command Language (ACL) and other software. This has made the national external audit system both timely and more effective as a result of the application of computer aided audit techniques (CAATs) and modern performance and systems-based audit.

3. All the key participants in Government budgeting and accounting and auditing processes at the federal, provincial, and district levels of Government have transitioned to and are critically dependent on these systems for their day to day operations and functioning.

4. The current site implementation status of FABS is as follows:

Area/ Province	Total Sites AM8	Pro-ductive Feb 2010	Pro-ductive July 2010	EDOs Actual/vs Productive Feb 2010	EDOs Actual vs Productive July 2010	Line Dept. Actual Vs Productive Feb 2010	Line Dept Actual Vs Productive July 2010
Federal	4	3	4			60/10	60/10
Gilgit/Baltistan (Northern Areas)	6	1	1			1/1	1/1
Punjab	38	39	39	36/36	36/36	42/42	42/42
Sindh	27	27	27	23/23	23/23	38/32	38/36
KPP	28	28	28	24/24	24/24	28/12	32/32
FATA	7	4	4				
Baluchistan	33	15	15	30/0		40/0	40/0
Total	**143**	**117**	**118**	**113/83**	**83/83**	**209/97**	**213/111**

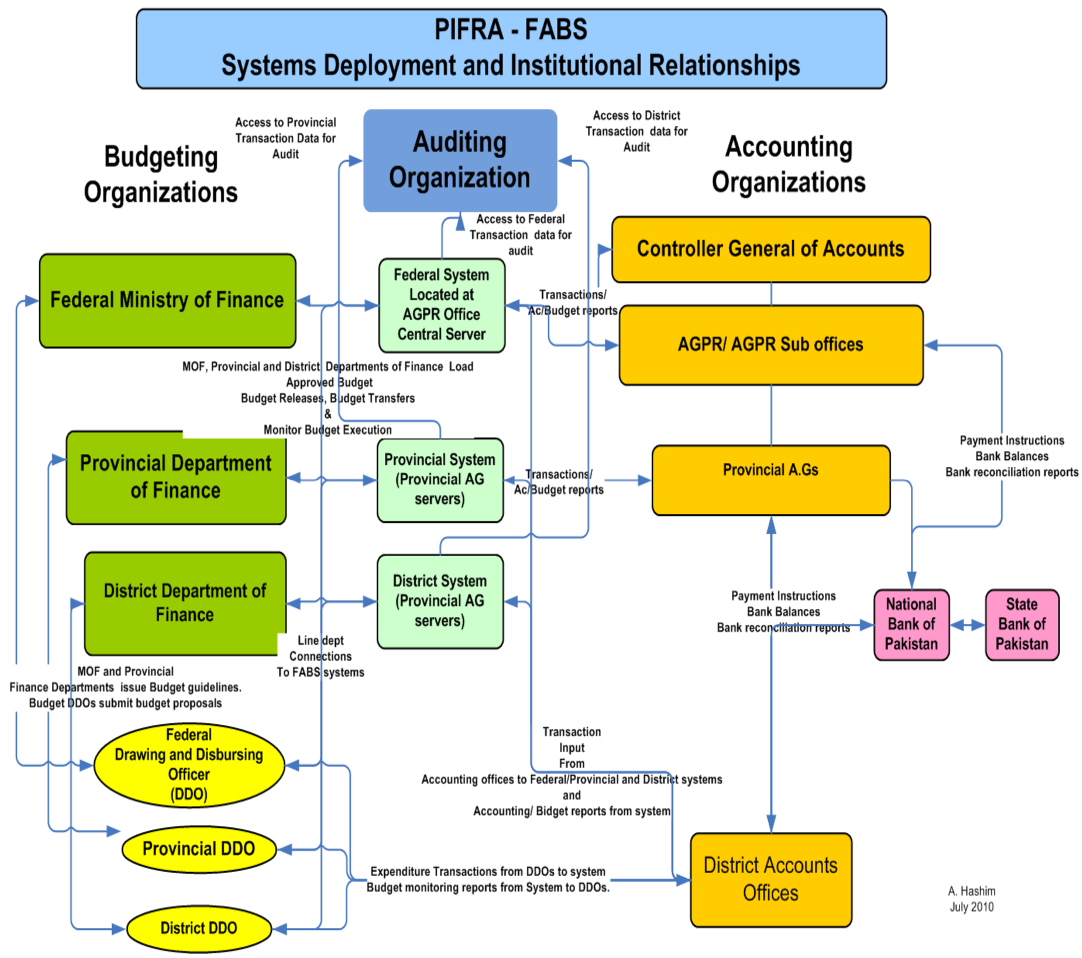
Systems Architecture

5. The system has been implemented in a partially distributed architecture:

- Federal Government budgeting and accounting transactions are carried out on a central server located in Islamabad.
- Provincial Government budgeting and accounting transactions are carried out on servers located in each of the provincial capitals, Lahore-Punjab, Karachi-Sindh, Peshawar- KP, and Quetta- Baluchistan.

- Federal Government transactions related to Spending Units (SUs) located in the provinces are carried out on the provincial servers and this data is periodically uploaded to the Central server in Islamabad to get an overall comprehensive picture for the federal Government. This element of the architecture is being changed and after installation of a new upgraded central server in Islamabad (planned for later this year), all federal transactions across the country will be processed directly on this server. This will enable direct online access for all federal transactions and eliminate the necessity of periodically down-loading these transactions from provincial servers to be able to get a country wide picture.
- District government budgeting and accounting transactions are carried out on the respective provincial servers.

6. The systems architecture and the institutional interfaces with the systems are shown in the diagram below and details of how the various users of the system carry out their functional responsibilities using the system are described in Appendix I.



FABS Support Requirements

7. Smooth operation of the system requires:

- The physical elements of the network operate satisfactorily and are maintained on a day to day basis.
- The software elements, including system databases are maintained to operate in an optimal fashion.
- Routine tasks of systems, network and data base administration are carried out.
- System access is controlled so that end users are only able use authorized functions with regard to their specific areas.
- A robust information security and disaster recovery regime is implemented and the functions related to these aspects are performed regularly;
- A support team and help line is implemented to help end users in systems access and use.
- End users are responsible for functional aspects and for carrying out their work on the system, e.g. running the payroll, and other transaction processing and report writing tasks in their respective areas.

8. Since FABS is an integrated government-wide system with multiple users, the first 6 out of the 7 tasks will need to be performed by a central organization to maintain the integrity of the data bases and to ensure smooth and uninterrupted operation of the systems network. Currently these tasks are carried out by the FABS directorate of PIFRA through a SAP CC which is manned by local consultants paid by the project.

9. During the Additional Financing period, the staff and resources of the FABS directorate should be transferred to the Office of the CGA. The CGA would be the preferred location of this function since it and its subordinate offices, including the AGs are responsible for the bulk of the transaction processing that is carried out on the FABS system. The tasks associated with the routine operation and maintenance of the system should therefore logically be their responsibility. However, for the CGA to be able to take over this function it will need to develop its capacity to do so.

10. However, other end user groups outside the CGA organization, such as the MOF/Provincial FDs, Line departments / Ministries and subordinate organizations under the CGA, such as the AGPR/AGs/DAOs/ AGPR sub offices, would also need to have available to them a set of technical resources to address their day to day technical / operational requirements. At present, these resources are also provided through the FABS directorate of PIFRA. These resources could in the post-PIFRA period be posted out to these end user groups from the Central organization or could be hired directly by them.

11. The Government's plan to entrust the maintenance and support of the FABS to the Office of the CGA would accordingly necessitate the capacity of this unit to be enhanced. A capacity development plan will need to be developed to:

- Review the numbers, skills and deployment of the staff currently assigned these functions.
- Plan which of these functions could be transferred to regular CGA / government staff and which will need to be retained as consultants.
- Develop a skills development/ training plan for the unit.

Functional Responsibilities of the FABS Support Division in the Office of the CGA

12. The FABS support Division in the office of the CGA will have significant areas of responsibility for the management, control, operation and integrity of the applications and data, namely, system administration, database administration, applications technical support, network administration, operating systems and help desk administration. An explanation of the key functions and activities to be performed is given below.

13. **Systems Administration**: System Administrators shall be responsible for: setting up all user profiles and access rights on the production system; notifying all new users with their initial user-id's and passwords and advising them to change the passwords immediately; and maintaining the system access rights after receiving appropriate authorization, including disabling users, updating user access rights, and re-enabling users, manage security, concurrent processing, and other SAP administrative functions.

14. **Database Administration**: The Database Administrator shall have a technical background with thorough knowledge of the UNIX operating system, and SAP Database Administration (DBA background) with knowledge of clustered environments. Key responsibilities would include:

- Maintaining the various application environments and instances
- Creation of periodic backups
- Application of software patches
- Reporting Technical Action Requests to SAP
- Following troubleshooting paths
- Performing restores of a previous backup.
- Start-up/Shut down of the System
- Notify the implementation team and the user community of potential loss of service periods.

15. **SAP Application Development and Support**: An Application Developer is responsible for developing code and fixing bugs that are found during testing. The Application Developer will also be responsible for the design of user interfaces, reports, and any customization. The Application Developers will perform the following tasks:

- Development work including but not limited to export programs from the existing applications (HR & payroll, FI etc.)
- Developing reports required for all the functional modules
- Takeover and be responsible for the customizations developed by the Supplier and maintain these in Production.

16. **Network Administration**: The Network Administrators are responsible for the maintenance of the FABS network connectivity ensuring that all users have the required connections to the system access to production and training instances. The Network Administrator is responsible for the following:

- Performance of recurring operational tasks related to the support of the network infrastructure, including LANS, WANS, routers, servers and workstations.
- Maintenance of the communication infrastructure, access to the internet and the WAN resources when needed.
- Setting up and testing all users required connection and accesses to FABS Application Instances.

17. **UNIX Administration**: UNIX Administrators are responsible for the maintenance, support and upgrades of the operating software and utilities on which the Oracle Database and SAP applications reside. The UNIX Administration works in close collaboration with the Database Administration to ensure full applications availability and security to the end users. The UNIX Administrators is specifically responsible for the following:

- Managing File Systems
- Managing Users
- Network configuration
- Printer Management
- Managing and analyzing system resources
- Backup and recovery
- Managing and monitoring processes
- Development of UNIX scripts for management of specific tasks
- Disaster Recovery

18. **Help Desk Administration**: Help Desk personnel are either selected from the competent Super-Users or trained by the Super-Users to perform the Help-Desk activities. Help-desk personnel must be specialized by Module / Track. Help-desk supervisors shall have more multiple Module knowledge. Their role is to provide first line support to end-users as follows:

- Receiving and responding to end-user queries and requests.
- Receiving and logging end-user trouble-tickets (a report of a problem)
- Relaying resolutions of trouble-tickets to the originating end-user
- Establishing a knowledge base of FAQ's (Frequently asked questions) and their traditional troubleshooting and resolution paths.
- Escalating non-standard problems to second line support as to be outlined in the Helpdesk Strategy, logging, and receiving resolutions.
- Communicating circulars and changes to the system operation mode if/when needed.

Appendix I: FABS – Budget Preparation, Execution: Functional Responsibility and Systems Access

1. **Federal Government**. The MOF is responsible for compiling the Federal Budget on the basis of budget proposals received by them in response to the budget circular sent to the controlling spending ministries. After the budget has been approved by Parliament, it is loaded by the MOF in the main systems server in Islamabad.

2. In-year changes to this budget on account of budget revisions, virements that require MOF approval, and budget releases are also made by the MOF staff directly in the main systems server. The MOF also distributes the budget for the main line ministries to their subordinate spending units and enters the spending unit-wise (spending DDO wise) budget into the system. The MOF has a direct on-line connection with the main systems server to be able to do so. This version of the budget is used by the AGPR for controlling the budget execution for the federal budget during the year.

3. Since federal government payment transactions also take place in the provinces through federal government spending units located in the provinces, province-wise copies of the initial budget for the spending units located in each of the provinces are transferred electronically to the provincial servers located in each of the provinces and these copies are used to control the federal government budget execution for the federal government spending units located in the provinces. Sub-offices of the AGPR are located in each province and control budget execution for federal government SUs in the province.

4. The federal budget data from the provincial servers relating to the SUs located in the provinces is periodically uploaded to the Central server so that the federal Government can get a consolidated picture of the status of budget execution during the course of the year. As mentioned above, after the installation of the central federal server in Islamabad this will no longer be necessary and all federal transactions would be directly available for access at the central server.

5. Federal Government payment transactions at the Center are carried out on the main server in Islamabad and the AGPR is responsible for processing these transactions. Spending Units located in Islamabad bring their payment requests along with all necessary documentation to the AGPR office in Islamabad for processing. These include all payments including those for payroll. Federal Government payments for SUs located in the provinces are mainly carried out at sub-offices of the AGPR located in the provinces (for widely distributed SUs, these transactions are processed through the provincial DAOs. After the server upgrade, all federal transactions processing will also be carried out on the AGPR server. The DAOs will have an online connection to the Central server.

6. At present the AGPR produces the Budget execution reports for the Line Ministries and sends it to them each month. However, as on-line connections are completed from the line ministries to the main server during the course of the current year, the line ministries will have capability to produce these reports themselves on an as required basis. Once these connections are established, Line ministries will also use them to electronically send

their budget proposals at the start of the fiscal year (the NISs) to the MOF. They will also be able to enter commitment transactions in the system. Currently, the NISs are sent manually by the Spending Ministries to the MOF and the Commitment records are maintained at the Treasury offices (in the case of the federal government at the AGPR).

7. **Provincial and District Governments**. The respective Provincial Finance Departments are responsible for compiling the Provincial Budget on the basis of budget proposals received by them in response to the budget circulars sent to the line departments. After the iterative discussions with the line departments as part of the budget finalization process, these numbers are adjusted and the final budget prepared. After the budget has been approved by the provincial assembly, it is loaded by the FDs in the provincial servers located in each provincial capital. In a manner similar to that described above, the district government budget is prepared by the respective EDO Finance in consultation with the respective provincial finance Department on the provincial server.

8. In-year changes to this budget on account of budget revisions, virements that require FD approval, and budget releases are also made by the FD staff directly in the main systems server. The FD also distributes the budget for the main line departments to their subordinate spending units and enters the spending units-wise (spending DDO wise) budget into the system. The FD has a direct on-line connection to the Main Systems server to be able to do so. This version of the budget is used by the provincial AGs for controlling the budget execution for the federal budget during the year.

9. Provincial Government payment transactions throughout the province are carried out on the respective provincial servers and a network of DAOs in the province are responsible for these transactions. Spending Units bring their payment requests along with all necessary documentation to the respective DAO office for processing. These include all payments, including those for payroll. All transaction processing is carried out on the Provincial server located at the provincial capital. The DAOs have an online connection to the provincial server. A major portion of the District government budget is also transacted through the respective district accounts office (DAO) on the provincial server.

10. At present, the Provincial AG produces the budget execution reports for the provincial Line Departments and sends it to them each month. However, as on-line connections are completed from the line departments to the respective provincial servers during the course of the current year, the line departments will have capability to produce these reports themselves, as required. Once these connections are established Line departments will also use them to electronically send their budget proposals at the start of the fiscal year to the provincial Finance departments. They will also be able to enter commitment transactions in the system. At the moment the budget proposals are sent manually by the Spending line departments to the FDs and the Commitment records are maintained at the DAOs.

11. **Audit**: Both Federal and Provincial Audit departments have access to the accounting data in the main server to be able to perform their functions. They use computer assisted audit techniques and computer programs.

Annex 5: Key Issues and Actions to be taken in Transition of FABS to MoF/CGA

1. Details of the continuing operation and maintenance requirements of the FABS-based GIFMIS are covered in Annex II. This annex discusses the major issues to be addressed in building up capacity in the MoF and CGA to take over operations by end-2012. The activities to meet these needs will be carried out in the following sub-components:

- Sub-component 1.2: *CGA Capacity Development and Transition Plan*
- Sub-component 1.3: *Fiscal Reporting on General Government*
- Sub-component 1.4: *FABS Support to MTBF Implementation*

Sub-component 1.2: CGA Capacity Development and Transition Plan

2. As observed in the recent IMF review of PIFRA, the current capacity of the CGA is very limited in terms of taking on full technical responsibilities for the operation and maintenance of the system. The system has only recently been fully rolled out and PIFRA has been obliged to take the lead role in overseeing technical operations during the development phase. A two year transition phase is necessary to allow critical expertise to be put in place in the CGA. As described under component 1, SAP CC units servicing Islamabad HQ and the provinces, now stationed in PIFRA-FABS, will be streamlined and transferred to the CGA. The CGA lacks exposure to many of the functions that it will be responsible for, and external assistance will be needed to establish an appropriate structure for management and oversight of these functions. As well as SAP-CCs, the CGA will establish a Quality Assurance Cell that will apply many of the Monitoring and Evaluation processes used in PIFRA II to review system functionality and performance. Early in the AF period, a short-term (around 3 month) international consultancy will prepare an organizational and functional plan for the CGA, and appropriate local consultants will be hired to guide its implementation.

3. The Finance Advisor (FA) function of the MoF is to be phased out by mid-2011. Principal Accounting Officers (PAOs) and their Chief Financial and Accounting Officers (CFAOs) will therefore have major new responsibilities for financial control and budgeting. The CFAOs role will require some redefinition to meet the requirements both of functions taken over from the FAs, and the implementation of the MTBF. The CGA will play a key role in overseeing the CFAO function and training the staff. It is proposed that an international consultant provide assistance to the CGA to define this role (possibly initially on a pilot basis) and to establish a training program (which will include foreign training for both CGA staff and CFAOs). The Finance Division (FD) of the MoF has a key role in defining the functions of the CFAOs with respect both to financial control and budgeting under the MTBF (requiring some revision of the MoF *System of Financial Control and Budgeting*, 2006). It is essential that the FD and CGA coordinate closely in the CFAO development and training.

4. The system will of itself help CFAOs to exercise financial control since key procedures are embedded in the system and can be easily monitored. The system can be further enhanced by acquisition of a software/search engine to facilitate access to rules

(MoF, Planning Commission, Establishment Division etc). A consultancy would be needed to gather the rules, scan the images, and implement software to track/trace the rules through an appropriate search engine.

5. Another area where closer cooperation between the CGA and the MOF/FD is required is in the introduction of commitment accounting. Considerable effort is required by the CGA and AGs to familiarize and train accounting and administrative staff to integrate commitment recording and reporting in their work practices. The CFAOs will play an important role in embedding commitment control into financial management practice. A commitment column and an uncommitted balance column will be added to the budget execution reports (BERs) to ensure that commitments can be easily tracked. Recording of commitments is not yet satisfactory, however, in particular for Federal projects under assignment accounts. Project directors are not recording commitments on the system and do not record their expenditures in real time but rather through monthly schedules—often provided with substantial delays. Real time recording of expenditures in the provinces has been achieved both for projects and for self-accounting entities (SAEs) by requiring cheques to be endorsed and recorded by the DAOs prior to encashment. The NBP has co-operated by refusing to cash non-endorsed cheques. This process greatly simplifies bank reconciliation and enhances the accuracy and reliability of financial reports for the PAOs and finance departments. The FD and CGA should develop a similar (or equally effective) procedure at the Federal level to enhance commitment control and financial reporting.

6. The current CGA building has very limited space and there will be great difficulty in accommodating core staff to carry out the new functions. Some restructuring has been carried out to accommodate the HQ SAP-CC and to provide training space. It would be highly desirable for the GoP to provide additional funds for rental for some non-core functions as a short-term measure. In the long run, a new building for the CGA would be appropriate. However, these matters are beyond the scope of the PIFRA II-AF.

Sub-component 1.3: Fiscal Reporting on General Government

7. Financial and fiscal reporting has been substantially improved under PIFRA II, and the PAD benchmarks have been substantially achieved. Both within-year reporting of the budget and end-of-year financial statements have been radically improved in terms of format, timeliness, and reliability. Budget execution reports (BERs) are circulated to all Federal and provincial PAOs 15-20 days after the end of the month (previously only civil accounts—without budget data were circulated). During the AF period, further improvements in timeliness and reliability of reports should be expected. Financial statements at all levels of government are now produced in IPSAS-compliant format for cash basis statements and are now being submitted for audit within 6 months of the end of the financial year. This achievement merits a PEFA-PI-25 rating of A compared with the baseline rating of C.

8. Substantial progress has been made in improving reconciliation processes and data entry. The discrepancies between the fiscal and monetary accounts, which were estimated to be more than 1.2 percent of GDP for the 2004/5 accounts are now contained to well

below the PAD benchmark of 0.5 percent, and the reasons for any remaining discrepancy are known and being remedied.

9. This level of progress has made it feasible to use FABS not only for standard financial reports but also to generate fiscal reports that are fully compatible with IMF GFSM-2001 standards. A full mapping of the NAM chart of accounts (COA), including all asset and liability accounts, to GFSM-2001 has been completed. The PIFRA team and the MoF are in the final stages of reconciling the federal government Pakistan Fiscal Operations (PFO) report with a GFS-compliant system generated report. A few issues remain to be addressed (particularly that of timely entry of FD-sanctioned transactions into the system), but early in the PFO period quarterly production of the federal PFO through the system should be feasible. Once the principles are fully tested, consolidation of federal and provincial accounts in a general government PFO should be achieved by end-2010/11. The CGA/AGPR would perform all of the technical work to produce the fiscal reports, but the FD will have overall responsibility for the format, publication, and use of the PFO—as is currently the case.

10. Some further measures are necessary to consolidate the PFO process. The FD should take the lead, with the CGA/AGPR responsible for accounting and systems aspects. The IMF has suggested the need to change the COA to attain full compliance with GFSM-2001. The compliance has been substantially achieved by the mapping exercise, but nonetheless there is a good case for seeking technical assistance to establish a COA Review Unit with responsibility for reviewing the COA. Such a unit would update, add explanatory notes to clarify elements of the current COA, review continuously, and, as appropriate, modify the classification. It would report periodically to a committee with representation from FD, CGA/AGs, line departments, and provinces.

11. It will also be desirable that the MoF review the present format of the published PFO and take steps to align it more closely with standard GFSM-2001 presentations. Since the present PFO is an important tool in any arrangements with the IMF, it may be appropriate to seek their comments on proposed changes—at least in relation to the present Stand-By Arrangement. Beyond this, the question of the entities included or excluded from general government warrants further examination. An entity such as the National Highways Authority, which is an autonomous agency but is mainly carrying out works as an agent of government, may, for statistical reporting purposes be properly included as part of general government. Such an approach would not imply any change in the legal status of the entity. It is recommended that a review of the statistical classification of government entities be undertaken during the AF period. Such a review could involve a request to the IMF rather than fund from AF resources.

12. PRSP reports represent another aspect of fiscal reporting at general government level requiring further consolidation during the AF period. The system has successfully generated reports covering all of the PRSP sectors, but data entry problems have meant that the PRSP Secretariat has not found the reports to be sufficiently reliable to date. These data problems are near to being overcome, and the quality of PRSP reports should progressively improve. There are, however, some underlying problems with PRSP reports in that sector reports involving vertical government programs do not always represent

expenditures at service delivery levels. In some cases, transfers to lower levels of government are recorded as expenditure, in others cheques may be deposited in bank accounts for subsequent distribution but recorded as expenditure in the accounts. A review of key service delivery programs, possibly incorporating some element of a public expenditure tracking survey (PETS) would help to further strengthen the PRSP reporting through the system. Consultancies to undertake such reviews are envisaged during the AF period. Such consultancies could be integrated with ongoing work of the PRSP Secretariat and coordinated with the AF.

Sub-component 1.4: FABS Support to MTBF Implementation

13. The MTBF has now been rolled out to all ministries and the 2010/11 budget was presented to the parliament in both the traditional White Book (demand for grants) form and in the Green Book (MTBF) format, which shows total revenue and development budget expenditures in relation to outcomes and outputs, each with associated performance indicators. Plans to integrate the GIFMIS and the MTBF have been delayed pending acquisition of a software upgrade (ECC06) and a Business Intelligence module that will facilitate configuration of SAP to accommodate the MTBF classification as an extension of the NAM COA. Integration of the MTBF on the SAP platform will give greater assurance of data integrity and will link budget preparation and budget execution more closely. MTBF configuration is feasible on the present SAP version, but its operation is much more user-friendly on the upgrade. The upgrade acquisition will be financed under PIFRA II and should be available by end-2010. The target should be to establish preparation of the 2012/13 budget on SAP. It would be very desirable to initiate the configuration as soon as practicable after the software upgrade is acquired. Provision is made under FABS for enhancement of systems related to MTBF.

14. A fully integrated budget preparation and accounting software will be a very powerful financial management tool. Given the relative inexperience of government managers—and the new CFAOs—in operating this tool, however, it is essential that sufficient skilled and experienced consultants are retained to support and train the GoP staff. DFID funding for this phase of the project ends in August 2011, and, consequently a decision has been made to reduce the number of IT staff and Financial Consultants starting from July 2011 and that the work would then be taken over by GoP staff. Drawing down support at this stage may pose risks for the sustainability of budget and financial management reform. Alternative options should be explored with development partners to ensure continuity of MTBF implementation.

Annex 6: Revised Institutional Arrangements

1. With a view to enhancing ownership of project deliverables, the institutional and implementation arrangements proposed under Additional Financing will vary from those designed under the original PIFRA II. The design of the new institutional arrangements recognize the need to establish a transitional arrangement for moving both the implementation and supervision of activities related to the FABS component to the MoF.

2. ***Responsibilities for project components:*** The implementation and supervision of the Audit component will continue to be anchored under the OAGP to conform to the requirements of independence of the audit function and the statutory nature of the office. The erstwhile separate component – Capacity Building of the Office of Controller General of Accounts (CGA) – will, under Additional Financing, be subsumed under the FABS component. The maturing of FABS during the original project implementation now allows stronger action to integrate its operations within the MoF/CGA. The revised arrangements do not imply any physical relocation of the systems themselves. FABS will continue to service a number of differing stakeholders, including the MoF, the Provincial Finance departments, District Governments (Accounting and Finance), AGPR and Provincial Accountants-General, Planning Commission and Provincial Planning and Development Departments, and Tehsil Municipal Administrations.

3. Technical responsibility for the FABS component and its future operation will, however, rest with the CGA, with appropriate involvement of the AGs. As a key user of system information and manager of budget authority, the MoF will play a central role in operations related to budget management and reporting. At the provincial level however, while the FDs will also play a central role in budget management and reporting, the Accountants- General will continue to report to the CGA. Project management, while retaining its existing structure and function as well as its current overall reporting arrangements, will service both the Audit and FABS components. Project management will continue to coordinate the execution of the project closely with the responsible agencies and no change is envisaged in its existing responsibilities.

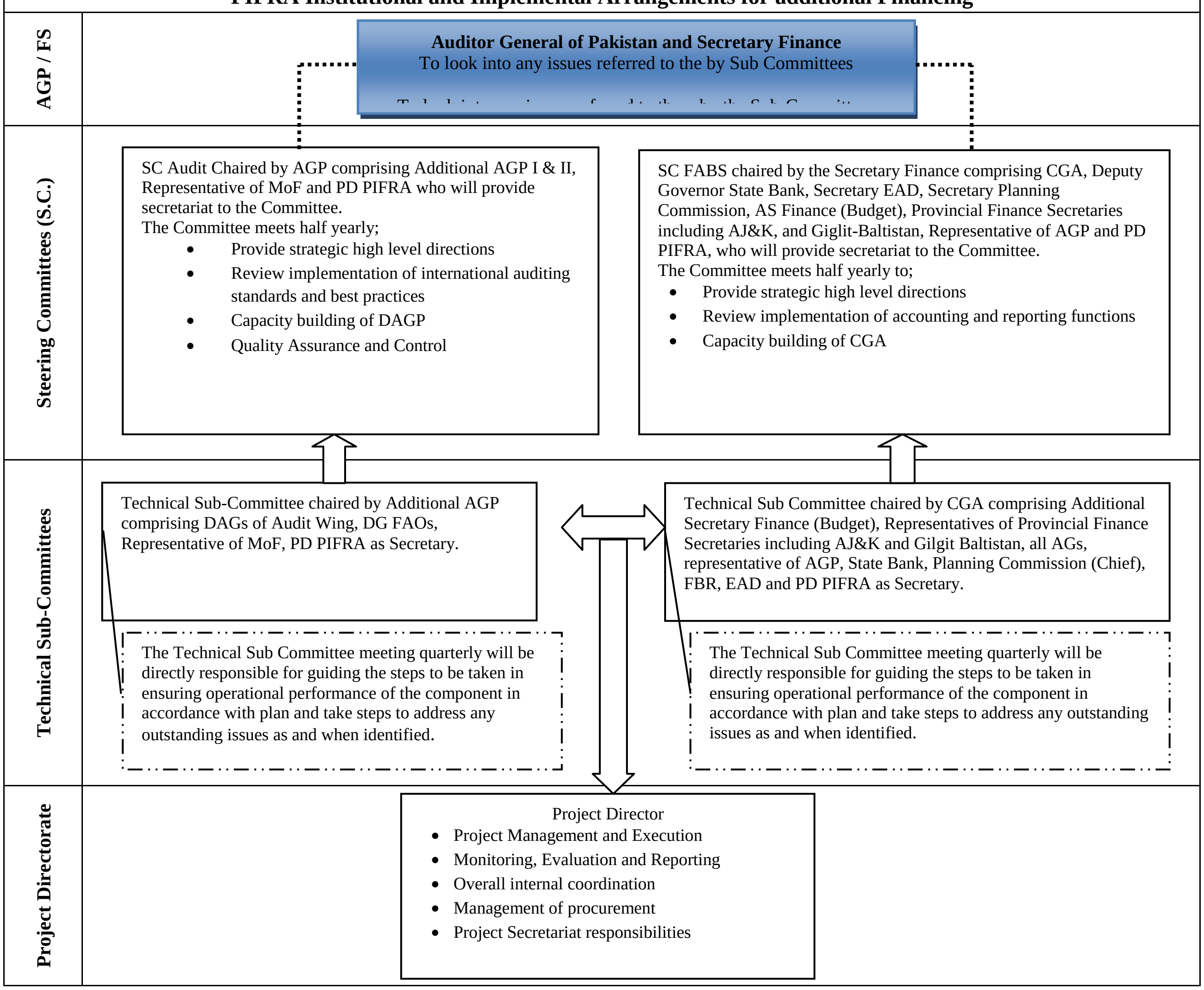
4. ***Steering Committees:*** Replacing the institutional arrangement structure of the original PIFRA II, there shall be 2 separate and distinct Component Steering Committees – one responsible for Audit and the other responsible for FABS. The Audit component committee will be chaired by the Auditor General and membership shall include officials as identified in the chart below. The FABS component shall be chaired by the Finance Secretary, MoF, with membership as highlighted in the chart below.

5. The two Component Steering Committees will meet at least once half-yearly, and will be responsible for overseeing the project components' implementation within their agreed policy framework, reviewing key implementation strategies, providing strategic high-level directions, and reviewing overall implementation progress. The PMU, through the Project Director, will provide the Committees, semi-annually, full information on project implementation progress, including achievement of milestones and any bottlenecks and slippages, plus an analysis of the implications of the current status for future achievement of benchmarks, and any other exception reports.

6. The institutional arrangements for Additional Financing also make provision for a two-person high-level strategic committee, comprising the Auditor General and the Finance Secretary, MoF. This committee will reinforce collaboration and enable resolution of any issues impacting either of the two component (Audit and FABS) Steering Committees.

7. For each of the two independent components, there shall be a Technical Committee to oversee the day-to-day technical aspects of the components' implementation. These Committees will report to their respective Steering Committees. The Technical Committee of the Audit component shall be chaired by the Additional Auditor General with membership as defined in the chart below, while the Technical Committee of FABS component will be chaired by the CGA. These two Technical Committees will meet at least quarterly and will be the first points of review of implementation performance of the respective components of the project, aside from internal reviews to be done by respective component chiefs. These subsidiary Committees have the direct responsibility for guiding the steps required in ensuring that progress in each component's implementation is in accordance with the plan and that steps are taken to address any outstanding issues.

PIFRA Institutional and Implemental Arrangements for additional Financing



Annex 7: Summary of Estimated Costs Under Additional Financing

	Additional Financing
	USD M
Component 1: FABS - MoF/CGA	
SAP Software Upgrade, Additional Licenses & Software	1.40
Purchase of Hardware for disaster recovery and new servers	0.50
SAP Licenses' fees/ Other Software Licenses	3.50
Maintenance of hardware/printers/ups/generators, etc	0.85
Server maintenance	1.20
Maintenance of PIFRA Sites-WAN Connectivity	1.30
Maintenance of PIFRA Sites-Diesel etc	1.00
Work stations/Laptop/printers/network equipment/ups/generators	2.35
Data Center/ Disaster Recovery Site - Civil Works	0.50
Vehicles	0.37
Data Warehouse (Consultancy)	0.50
Training	1.00
SAP CC Consultancies	1.40
CGA consultancies, software, training	1.86
Contingencies (@10 percent)	1.68
Total Component 1	**19.41**
Component 2: Audit	
Data Center -Civil Works	0.10
Recurrent Cost AMIS	0.87
Technical Assistance - Outsourcing Local Consultancies	1.30
Work stations/laptops/printers/network equipment/generators/maintenance	1.65
Training	0.36
Contingencies (@ 10 percent)	0.40
Total Component 2	**4.67**
Component 3: Project Management	**0.43**
Total IDA contribution	**24.50**
GoP contribution (salaries for civil servants, certain overhead costs)	**3.86**
Total	**28.36**

Annex 8: Revised Project Plan

1. The table below shows the timeline, milestones and end-points of all activities included in the FABS-MOF/CGA, as described in detail in the project paper and the related annexes.

Task Name	Start Date	End date
Project Plan PIFRA II and Extension - FABS - MOF / CGA	**01/11/2010**	**29/06/2013**
Project Plan PIFRA II - FABS - MOF / CGA	**01/11/2010**	**30/03/2013**
Interfaces	01/11/2010	30/03/2013
Data Ware House (DW)	01/01/2011	31/03/2012
Extension of FABS to Foreign Funded Projects	01/11/2010	29/09/2012
TMAs	01/01/2011	30/03/2013
Extension of FABS to AJK	01/11/2010	30/03/2013
DR\Server	16/11/2010	30/09/2011
Information Security and Management System	01/11/2010	31/05/2011
Support to MTBF	01/02/2011	30/03/2013
Software Upgrade	01/02/2011	30/03/2013
Strengthening of MOF Capacity and Fiscal Reporting	01/11/2010	29/09/2012
PRSP Reporting	01/01/2011	29/09/2012
PFO Reporting	01/11/2010	30/09/2011
Fiscal Reporting (Development of Reports and Training)	01/01/2011	31/03/2012
Road Map for Accrual Accounting	16/11/2010	31/12/2010
Review/update of NAM	01/02/2011	01/08/2011
CGA Component PIFRA II	**01/11/2010**	**30/03/2013**
Extension of FABS to FATA / Baluchistan	01/11/2010	30/03/2013
Archiving of Pension Records in AG Offices	01/12/2010	30/09/2011
Completion of Buildings (AG Sindh / AG Baluchistan)	01/11/2010	30/09/2011
Project Plan PIFRA II Extension - FABS - MOF / CGA	**01/07/2011**	**29/06/2013**
CGA - Capacity Development and Transition Plan	01/07/2011	29/06/2013
Automation of Rules & Regulations	04/07/2011	30/06/2012