

8. SPECIFIC ISSUES

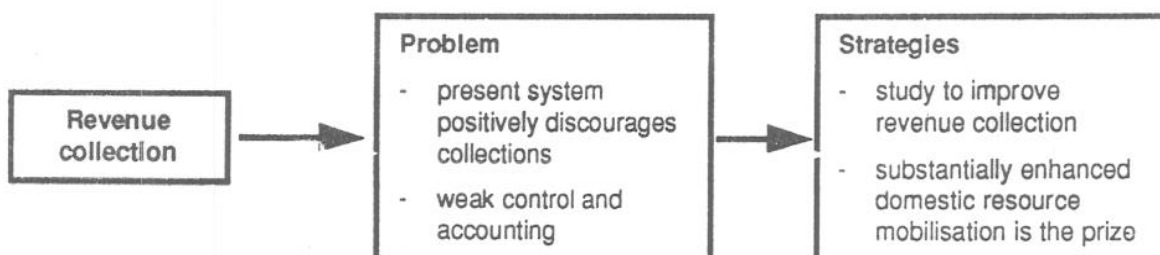
8.1. Introduction

8.1.1. This section deals with certain specific issues raised by CORBEC that were considered to need special attention and explanation as part of the overall major strategies. In the order in which they were mentioned in the Inception Report, these concern:-

- (i) Lack of control over revenue receipts;
- (ii) The absence of information and transparency regarding food operations;
- (iii) Problems related to foreign project aid and development expenditure;
- (iv) Whether certain Autonomous Bodies' borrowings should be treated as Public Debt in the accounts of the Government;
- (v) Weaknesses in the systems of on-lending and equity participation for Autonomous Bodies;
- (vi) A system for monitoring and approving guarantees; and
- (vii) Banking and cash management.

8.1.2. The individual sections deal with a brief over-view of the current position and problems that exist followed by a summary of the issues and the proposed strategies for improvements.

8.2. Revenue Receipts



8.2.1. Virtually all revenue receipts, excepting those of Railway, Post, Telegraph and Telephone, Forest, Foreign Loans and Grants are accounted for initially at District and Thana offices after being paid into a branch of the Bangladesh Bank or its agent the Sonali Bank.

8.2.2. The Bangladesh Treasury Rules and the Subsidiary Rules lay down the procedures for booking receipts in Government's accounts. However, when the task of receiving monies due to the Government was passed to the Bangladesh Bank and designated branches of Sonali Bank, many of the provisions, especially those relating to Treasuries, became obsolete because Treasuries as they were then known ceased to exist. Nevertheless, the Rules do state that all monies received on account of Revenue shall without undue delay be paid in full to the Treasury or into the Bank and shall be included in the Government Account. Because of the reference to Bank these provisions are still relevant as are others when interpreted properly to present circumstances.

8.2.3. Under the Revenue Account there are currently 69 main heads of receipt of which 18 are tax revenues and the rest non-tax revenues. The main categories of tax revenues are taxes on income and profits, taxes on property and capital transfers, and taxes on goods and services.

8.2.4. There are two principal methods by which Government collects monies from the public. These are payment direct to the Bangladesh Bank, or a designated Sonali Bank which replaced the former Treasuries for this purpose, and payment direct to a Government office or department authorised to receive the monies and then later deposit them to the bank.

8.2.5. Set out below is a brief summary of weaknesses that have been observed:-

- (i) There is no consistency in the method of accountability for receipts. Different authorities administering different types of revenue receipts follow different procedures. For some types of receipts subsidiary records are kept and these provide a means of producing reports for both reconciliation purposes and for management information. However in most cases this does not happen.
- (ii) There is an absence of reconciliation between the authorities administering the source of receipt and the accounts offices keeping the initial accounts. For example, in respect of the Ministry of Forest there is actually a form, ref. no 66, which should be sent for reconciliation purposes at the end of each month by the Accounts Officers to the relevant sectoral officer responsible for ensuring monies due are collected. This system does not appear to be used very often and Accounts Officers' claim that the sector officer should come to them to do the reconciliation. More often than not, reconciliation does not take place.
- (iii) In some instances the payer not only has to write out the chalan, the term for receipt, but also take it to an office for verification before payment is made at the bank. This is not only a nuisance but also time consuming. In fact there is not even consistency in the number of copies of the chalan needed. In practice it appears to vary from 2 to 4 even though the treasury rules generally state what should be done in given circumstances.
- (iv) The accounting offices are unable to verify the collecting banks reported figures, mainly because of the absence of reconciliation and no pre-verification.
- (v) There are frequent instances where Government's pre-printed chalans are not used and the payers have to provide their own stencilled or photo-copied versions. It was claimed that this is because of the unavailability of the standard forms.
- (vi) There appears to be an ignorance about the existing rules for the booking of Government receipts. Moreover with the creation of District and Thana Accounts Offices the rules are both obsolete and confusing.

Proposed solutions

8.2.6. Initially, a complete detailed review of all types of receipts being collected and accounted for at District and Thana offices is needed to establish where standardisation and uniformity can be achieved, especially with regard to responsibility for collection, the methods of payment to be used, what subsidiary accounting records should be kept and how reconciliation can best be achieved. At the same time decisions should be made about how best to produce relevant accounts that can be used by the managers at various levels who should have the responsibility for monitoring and controlling collections. Comparisons of actuals with estimates should be incorporated on all management accounting returns.

8.2.7. In carrying out this review special attention should be given to the following points:-

- (i) Without causing further inconvenience to the paying public consideration should be given to the extent to which Departments can be made responsible for collecting their own revenues and depositing those monies with the banks, as do the Tahsildars for land revenue. This would minimise the occasions on which the payer would have to make out his own chalan, help reduce mis-allocations in coding and facilitate reconciliation work;
- (ii) For standard fees and charges, where the above is not possible without inconvenience to the payer, the use of standard pre-printed forms should be considered as well as the provision of carbon paper, or even carbon backed forms;
- (iii) Investigation into the possible use of receipting machines is also recommended, provided satisfactory maintenance facilities can be assured; and

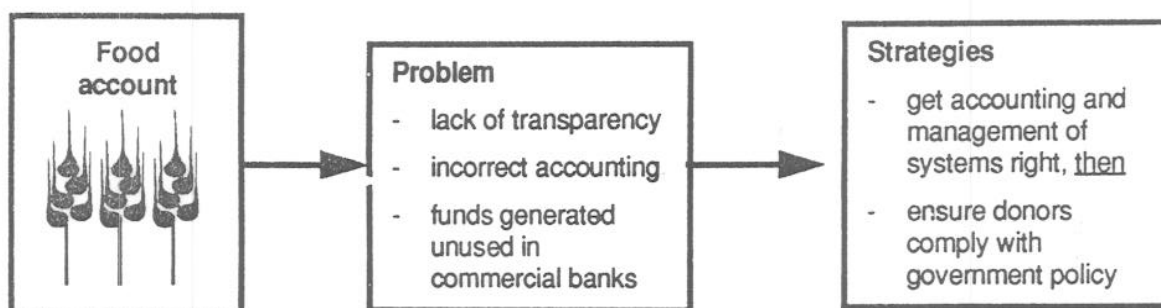
(iv) Effective systems of reconciliation.

8.2.8. The role of the Bangladesh Bank and its agent, the Sonali Bank, in the collection of receipts should be reconsidered in the light of the above findings. Particular attention is needed to the introduction of a method of verifying and reconciling the monthly figures being supplied by the Sonali Bank through the Bangladesh Bank with those of the central accounts.

8.2.9. The use of pilot projects for any changes should be considered as essential. When final changes have been decided upon the revised systems will need to be specified in a modern loose leaf accounting manual.

Recommendation

51 A Revenue Collection Study should be carried out with the objective of identifying improvements to procedures, the extent to which Departments could be made responsible for their revenue collection, and enhancing domestic resource mobilisation

8.3. Food Operations

8.3.1. Government's recently outlined food policies include the improvement of public domestic procurement and distribution operations, adequate incentives for growers, the phasing out of subsidies, except for targeted distribution programmes, and the removal of the restrictions on private food grain imports, storage and inter district trade. It is through the Directorate of Food that food aid is received, distributed and sold. This includes sales to produce the counterpart funds to be used for development purposes.

8.3.2. For many years the lack of information and transparency regarding food operations have been a cause for concern. The accounting system is said to follow the budgeting system which itself does not even highlight clearly such essential items as operating costs, stock losses and subsidies.

8.3.3. Whilst the Food Directorate keeps the subsidiary accounting records for food operations the entries recorded in the Government's accounts are done either by the Chief Accounts Officer of the Ministry or the Controller General of Accounts. For the food operations the main accounting entries are all recorded through the Consolidated Fund as capital Expenditure (Non-Development) using a main code denoting the Food Trading Account.

(Md. Habibur Rahman)

Joint Secretary,
Finance Division

Ministry of Finance
Government of Bangladesh

8.3.4. The accounting operations are complicated both by the inclusion in the budget and accounts of the food trading operations as non-development capital expenditure and by the differing requirements of donor agencies, especially where counterpart funds have to be created for development purposes. For example, the locally generated counterpart funds from the sale proceeds of food and commodity receipts under the current United States Aid Programme, PL 480 Title III have to be placed with a commercial bank, namely American Express, whereas under the previous agreement they were deposited in a special account with the Bangladesh Bank. In most cases where counterpart funds have been created they cannot be automatically utilised for development without further reference back to the donor agency for approval.

8.3.5. The recommended changes from the Food and Agriculture Organisation's study of subsidiary accounts systems are now being implemented but this does not appear to have addressed the interface of the accounts with the presentation of food operation either in the budget or the central accounts. As a result the desired transparency is unlikely to be achieved.

8.3.6. Major problems surrounding these accounts include:

- (i) The accounting entries being made for certain consignments, when counterpart funds have to be created for development purposes, result in the state trading food account being in effect wrongly charged twice, the account being debited when the consignment is received and then having sale proceeds netted from receipts for a transfer to deposit. This also results in two credits for each consignment, one as grants received and the other as funds on deposit.
- (ii) When projects are approved for financing from counterpart funds, entries are being made in the accounts that result in the project codes being credited wrongly with the amounts approved.
- (iii) Though a commissioned report from consultants Price Waterhouse recommended there was no need for the opening of a separate special interest bearing deposit account with a commercial bank for USAID counterpart funds, exactly the opposite has occurred. At the 31.12.92., the equivalent of almost US \$60 million was sitting on deposit with the American Express Bank whilst the Government was borrowing locally to finance its operations.
- (iv) A decision still has to be made about the correct accounting entry to be made for monies deposited with the American Express Bank.
- (v) The lack of transparency and the absence of any published form of trading and profit and loss account and balance sheet showing write-offs, subsidies, stocks and profits or losses.

Solutions

8.3.7. The first step recommended in relation to reforms of the food operations in the accounts of the Government should be to operate it outside the Consolidated Fund. This could be done either by making the Food operations the responsibility of an Autonomous Body or operating the account on a trading basis as a memorandum account under the Public Account of the Government. At this stage the latter treatment is recommended.

8.3.8. The net result in the Revenue Account would be the recording of simple entries to show either the surplus or deficiency attributable each year. A memorandum trading account would give in both the budget and accounts the cost of such items as Government subsidies and stock losses. The following is an example of the format. This could also incorporate quantities where appropriate so as to give more meaningful management information.

STATE TRADING FOOD ACCOUNT			
Sales and Recoveries (including food for works, subsidies etc)	Taka	Taka	Taka
			2,277,00,00
Deduct value of sales being:-			
Opening stock		500,00,00	
Cost of Sales			
Foreign aided imports	971,84,00		
Own resource imports	420,97,00		
Internal procurement	<u>882.15.00</u>	2274,96,00	
Stock surpluses during year		<u>5.00.00</u>	
		2,779,96,00	
Less			
Stock losses during year	20,00,00		
Value of closing stock	<u>525.00.00</u>		
		<u>545.00.00</u>	<u>2,234.00.00</u>
Gross surplus/deficit from trading			43,00,00
Deduct			
Operational costs		370,00,00	
Debt charges		<u>35.00.00</u>	<u>405.00.00</u>
Net surplus /deficit to be transferred to revenue account			-362,00,00

8.3.9. Where the food account is to be used for the creation of counterpart funds for development purposes, a standard accounting system should be established incorporating the following requirements:

- (i) Counterpart funds should be maintained, initially, in special bank accounts with the Bangladesh Bank and in the accounts of the Government be shown in Deposit Accounts under the Public Account;
- (ii) As the counterpart funds are approved for the financing of development projects or programmes they should be transferred from the appropriate Deposit Account to the Revenue Account as Grants received.
- (iii) When the use of the funds is agreed with the donor, a Government Order or Warrant should be issued to the spending agency giving the expenditure code to be used and the method by which expenditure is to be incurred.

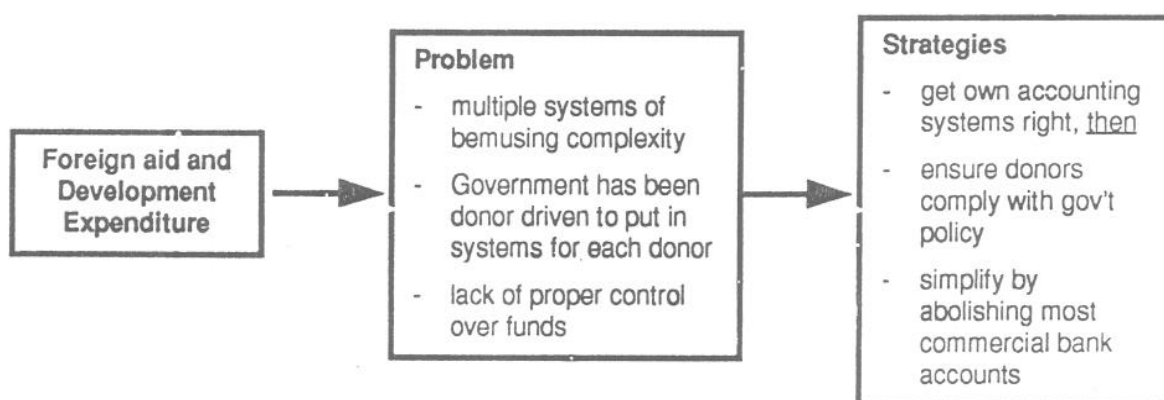
8.3.10. Again, as with project aid and development expenditure, it could well take time to achieve these changes. Hence, it is recommended that Government should set out its policies and long term objectives with regard to these matters. The reasons for these changes should be explained fully to the involved aid agencies and their support in implementing them should be sought.

Recommendation

52. Food trading accounts should be maintained on a commercial accrual basis as memorandum trading account so as to provide the desired transparency, with only net receipts or payments being shown in the Revenue Account.

53. Counterpart funds should be maintained in special accounts with the Bangladesh Bank.

8.4. Foreign Aid and Development Expenditure



Foreign Aid

8.4.1. Foreign loans and grants that are paid to the Government should be received by the Bangladesh Bank and be shown in the Government's accounts as receipts to the Consolidated Fund, thus meeting constitutional requirements.

8.4.2. All such receipts by the Bangladesh Bank should be notified to the Controller General of Accounts by way of a daily clearance memorandum, which is used to record the transaction in the accounts. However, in certain instances this is no longer happening, especially where ad hoc arrangements have been made to speed up the disbursement of monies to project implementing agencies. In these case the monies are being transferred through the Bangladesh Bank to the spending agencies without being put through the Government's bank accounts. Not only is this irregular but it has resulted in the absence of proper timely accounting entries.

8.4.3. Direct payments for goods and services, including technical assistance, by donor and lending agencies are not being entered in the accounts of the Government. These (if they can be ascertained) are entered in the Government accounts by book transaction at a subsequent stage. Advices of direct payments for goods supplied are generally sent to the project implementing agencies to be recorded in the expenditure statements of the projects. However, that does not mean that they will be recorded as receipts to the Government. It would appear that only if they are reported to the Economic Relations Division of the Ministry of Finance or the Controller General of Accounts that an accounting entry recording the receipt may be made.

8.4.4. Other problems include:

- (i) No reconciliation with the Economic Relations Division which monitors all foreign aid which is particularly important for future verification of debt charges;

- (ii) Some counterpart fund aid monies being recorded twice in the accounts as receipts, initially as grants and then as deposits.

Development Expenditure

8.4.5. Accounting for expenditure from foreign aid to the satisfaction of Government is complicated by the differing requirements of the donor and lending agencies. Also, depending on the type of funding, grant or loan, and whether the money is paid in advance or is reimbursable the procedures for recording expenditure vary considerably.

8.4.6. Furthermore, for various reasons ad hoc funding arrangements have been introduced that do not always satisfy Government's expenditure accounting needs. In some cases these have aggravated the problem of producing accurate and meaningful accounts. It has been claimed that cumbersome disbursement procedures have caused project implementation delays and thus such arrangements are necessary.

8.4.7. The major weakness is the inability to record in the accounts on an accurate and timely basis the actual expenditures being incurred on development projects. Contributing factors to this include:

- (i) The introduction of systems to speed up disbursement procedures, whereby the actual disbursement of monies to projects' commercial bank accounts are accounted for centrally as expenditures.
- (ii) The Chief Accounting Officers in Ministries, who should be responsible for making the initial accounting entries in the books of Government and controlling project expenditure are being by-passed, especially where foreign aid financing is concerned. This means that the Principal Accounting Officer, who has the ultimate responsibility for the correctness of project accounts is also being by-passed. Thus there is no means of enforcing effective financial and management control.
- (iii) The use, for projects, of commercial bank accounts outside the Government's main cash accounts with the Bangladesh Bank. There is little or no control over expenditures being met therefrom.
- (iv) The accountants engaged in keeping the subsidiary accounts for the projects are in many cases lacking formal training in accounting and knowledge of donor requirements. Also, they do not have manuals of operation.
- (v) An unnecessary work load is being placed upon implementing agencies accounting staff by the collection of monitoring data in differing formats by different offices. Time would be better spent concentrating on the production of accurate and meaningful accounts that would satisfy both Government's needs as well as those needs of the aid donors.

8.4.8. As with other areas of accounting, apart from the deficiencies in recording expenditure on a timely basis, there is a complete absence of effective budgetary control. For management purposes the comparison on a regular basis of actual expenditure as against approved budgets and cash flow forecasting simply does not exist.

Solutions

8.4.9. As far as project aid and development expenditure are concerned certain radical changes are recommended. These are that:

- (i) all grant and loan aid receipts should be paid to the Government through its central accounts with the Bangladesh Bank and the use of other bank accounts by individual Ministries for the receipt and transfer of these funds should cease.

- (ii) The Controller General of Accounts be made responsible for making the accounting entries for these receipts in the books of the Government and notifying other interested offices such as the External Resources Division.
- (iii) A policy should be established, in conjunction with donor agencies, with regard to direct payments by donors and lending agencies to meet the Government's need to receive relevant data to record these transactions. Once established the reporting requirements should be set out clearly in the related agreements.
- (iv) The use of separate commercial bank accounts for holding counterpart funds should cease.
- (v) Other than for Autonomous Bodies implementing directly development projects, the use of separate commercial bank accounts for development expenditure should cease.

(note that the references to separate bank accounts in (i), (iv) and (v) all refer to different issues, indicating the complexity of the systems that have been allowed to develop

Is it still in existence?

- (vi) For monies being released to Autonomous bodies, in respect of development projects, consideration should be given to the introduction of an imprest system under which the replenishment of funds is dependent upon receipt of satisfactory accounts for the money spent.
- (vii) Systems should be established whereby the Chief Accounts Officers of the Ministries are responsible for recording the accounting entries for development aided project expenditure as it occurs.
- (viii) A system has to be established to capture in the accounts interest earned on any commercial bank accounts operating in the name of the Government.
- (ix) Formal training be given for all accounting staff involved with development expenditure, especially those keeping subsidiary records.
- (x) As and when changes are made, new manuals of instruction will be introduced.

8.4.10. Whilst it is accepted that all the changes could not be achieved at once, it is advisable that the long term objectives and related policies should nevertheless be firmly established as a priority, so that the aid agencies and others who may have an interest can have no doubt about the intentions of the Government.

8.4.11. As there may be resistance from the aid agencies involved, especially those which have been instrumental in the introduction of ad hoc arrangements to overcome accounting weaknesses, the Government should have early discussions with them on these matters and convince them that standardised procedures and resulting up to date accounts are in the long term best interests of all parties concerned. It should also be noted that recent studies indicate disbursement of funds is not a major problem in project implementation, and the departmentalisation process recommended above will itself improve the efficiency of the Government accounting system in disbursing funds.

8.4.12. The changes envisaged should be introduced on a systematic basis with a small team of accounting experts dealing with each aspect and each Ministry one at a time.

8.4.13. We would be much less concerned that a monetised value of technical assistance appears in the accounts. If this information is required at all, it could be covered simply by a summary memorandum statement in the accounts.

Recommendation

54 The Government should initiate a major policy change in the system of handling donor funds, by insisting that they are all dealt with through Government accounts at the Bangladesh Bank, and by agreeing procedures to capture all project expenditure transactions.

8.5. Autonomous Bodies and Public Debt, On-Lending and Equity Participation

Public Debt

8.5.1. Public debt includes only borrowing by the Government, even though the monitoring by the Bangladesh Bank shows net public borrowing after taking into account certain non-commercial public sector agencies positions with commercial banks. CORBEC, however, questions whether such debts should be included because the loans are raised on the basis of public policy, some agencies fail to meet their repayments resulting in the liability being passed to Government, the crowding out effect of borrowings by these bodies on the credit available to the private sector as the public sector has preferential access to credit facilities from the commercial banks and Government is unable to assess quickly the future budgetary impact of the loans.

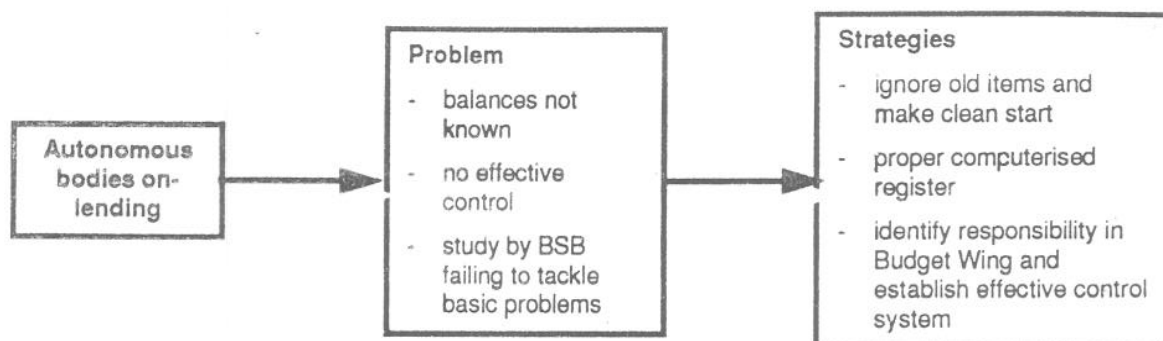
8.5.2. The effects of these loans on the credit facilities available to the private sector could not be ascertained but it was felt that there is no current problem as in some cases commercial banks do actually have an excess of funds available for lending. However, clearly this position could change.

8.5.3. There is a conflict between on the one hand the need for information for public financial management, and on the other hand the line of separation that has been drawn by making certain activities into Autonomous Bodies. Whilst for budgeting and cash management purposes any possibility of a future charge on the Government needs to be known, such loans would not be accounted for as part of Public Debt. In Bangladesh this is where the problems arise as there is no reliable system in existence that would enable the Government to monitor and assess any contingent liability on such loans, details are not specifically kept by the Government and the extent of any liabilities already taken over could not be established with accuracy.

8.5.4. Technically, the borrowings are not part of the public (i.e. government) debt. Therefore they should be excluded. However, they are within what is usually defined as the Public Sector Borrowing Requirement (PSBR), and indication of all borrowings by public sector bodies. Therefore, a memorandum summary of the position could be included with the budget, highlighting the contingent liabilities that could in practice become actual liabilities. It should be noted that whilst Government may feel a certain amount of responsibility for such debts there is in fact no commitment to do so unless a Government Guarantee exists.

Recommendation

55 It is neither desirable or necessary to include in the accounts of the Government as Public Debt the direct borrowings of Autonomous Bodies. However, a memorandum summary could be incorporated for information.

On-Lending

8.5.5. In Bangladesh donors frequently lend funds to Government for projects which are operated through Autonomous Bodies. Such funds are "on-lent" to such bodies. The on-lending of funds to Autonomous Bodies is dealt with by the Development Wing of the Finance Division. Whilst a booklet has been produced showing standard terms and conditions to be applied for these agreements, when not covered by a main agreement, there does not appear to be in existence any fully documented system about either the terms of such on-lending or the records that should be kept.

8.5.6. The procedure for the execution of on-lending agreements, which are actually known as Subsidiary Loan Agreements, depends on the provisions of project proformas, external credit agreement terms and whether any standard terms and conditions set by the Government can be applied. Thus the terms and conditions for subsidiary loan agreements can vary considerable especially if specified in a main loan agreement with a foreign lender. Under the standard terms established by the Government, the interest rates at present vary between 7.5% and 11.5% depending on the purpose of the loan. The higher rates are charged for commercial types of projects generating income and the lower rates for the non-commercial type of programme and organisation.

8.5.7. For the Government the Subsidiary Loan Agreements are usually signed by the Joint Secretary of the Development Wing after being approved either by the Joint Secretary or the Additional Secretary. Approval by the Secretary, Minister or Cabinet is not sought and was not considered necessary as the terms and conditions have already been established either by the main Development Credit Agreement or by Government's standard terms and conditions.

8.5.8. When a Subsidiary Loan Agreement is executed it should be entered into a register which records full details that can be used for future budgeting and accounting control purposes. This is not being done, but a simple data base on computer would achieve the desired register.

8.5.9. No standard format has been used for reconciling and agreeing with the borrowers the amounts outstanding and on many occasions, because of the absence of records, the Government has had to rely on what the borrowers claimed were the amounts due.

8.5.10. The Government has already recognised the serious deficiency concerning the absence of proper reliable records for Subsidiary Loan Agreements and engaged the Bangladesh Shilpa Bank to carry out a special project to rectify this. The tasks involve not only devising a new procedural manual but also setting up reliable computerised records. However, this project is already behind schedule because it is dependent on the borrowers for data. Also, it is only addressing the reconstruction of records up to 1991, so until the new system is devised, which at the moment appears to have low priority, the problems persist.

(Md. Habibur Rahman)
Joint Secretary,
Finance Division
Ministry of Finance
Govt. of Bangladesh

8.5.11. The budget estimates for the annual repayments are not even initiated by the Development Wing. The Budget Wing prepares these and in the absence of reliable records they are frequently simply based on previous year's figures. This leads to the unusual situation where a substantial provision is made each year in the budget for non-payment of the estimated amounts. There is no inbuilt system in the Development Wing that checks to ensure all repayments of interest and principal are received, recorded and properly accounted for.

8.5.12. Because of problems in getting Autonomous Bodies to make timely payments of amounts due under the agreements, efforts were made to deduct unpaid monies from the fourth quarter's release of development funds allocated to projects. This practice was not considered acceptable by the project implementing agencies and led not only to reconciliation problems but also unnecessary delays in the implementation of projects which were totally unrelated to the unpaid debt charges.

8.5.13. There are still many problems because of the lack of any system for the processing, recording, budgeting and accounting in connection with on-lending and subsidiary loan agreements and what has been done so far by the Bangladesh Shilpa is not going to alleviate the situation.

8.5.14. The Government's strategy to establish standard terms and conditions for the on-lending of funds, received from foreign donors and agencies, makes administrative sense provided there is no resulting hidden subsidy, especially to the commercial type of public enterprises.

Solutions

8.5.15. It is recommended that, other than when on-lending terms and conditions are specified in the original loan agreement with the Government, the standard terms be applied but with the provision that for commercial types of public enterprises the conditions be no softer than those applicable to the original loan.

8.5.16. Government's strategy should also be to ensure that the standard terms and conditions are reviewed at least once a year, perhaps as part of the budget procedure, to ensure they are kept in line with policies of the Government concerning interest rates generally.

8.5.17. Whilst the final outcome of the Bangladesh Shilpa Bank's project to establish up to date records and procedures for these subsidiary loan agreements is not yet known, preliminary indications are that it is not achieving its original objectives. It is having great difficulty in reconstructing the records and in getting information from the Autonomous Bodies. Nevertheless, it is essential that the strategy for reforms now being considered should decide who is to be responsible for the management of on-lending, including budgeting and accounting. The Development Wing of the Finance Division has the responsibility for processing these agreements and, therefore, it is suggested that it also be made completely responsible for the management of all aspects of this work.

8.5.18. The project involving the Bangladesh Shilpa Bank has so far failed to set up any system for the recording of subsidiary loan agreements for on-lending and is proceeding extremely slowly in reconstructing reliable data. Hence, it is still a priority that a system for recording all new agreements and loans be devised and implemented without delay.

Recommendation

56 All on-lending to autonomous bodies should be subject to standard terms and conditions, other than when these are specified in the original loan conditions by donors. The standard conditions should be reviewed at least annually.

57 The present Shilpa Bank project should be re-directed to focus on developing a system for monitoring and controlling all on-lending. Where existing loans cannot be identified they should be ignored.

Equity Participation

8.5.19. The decision on equity participation, for both commercial and non-commercial Autonomous Bodies is taken by the Autonomous Bodies Wing of the Finance Division. In practice this may be in the form of direct investment in share capital or the conversion of loans into equity. This Wing deals also with cash grants and subsidies.

8.5.20. Equity participation should be approved through normal revenue budgetary allocations. However, there are occasions when this procedure is not followed and outstanding loans which the autonomous bodies are unable to meet are turned into equity finance. Approval for this is done at officer level without being reported to the Parliament.

8.5.21. Proposals for equity participation should be subjected to thorough examination by the Autonomous Bodies Wing with scrutiny of cash flow prospects and profitability. Decisions are taken on the merit of each case. When loans are converted onto equity there is a guideline that the debt equity ratio should be below the 60: 40 level except for the Power Development Corporation where it has been relaxed to 40:60.

8.5.22. The main problem with equity participation is that there is no consistency in the system of appraisal and approval, particularly when outstanding loan debt is simply converted into equity instead of being shown in the budget as a subsidy to the organisation concerned because it is unable to meet its current liabilities. The latter system is preferable as it is more transparent, specifically highlighting problems which otherwise would go unnoticed except to those directly involved with the approval process.

Solutions

8.5.23. The strategy for equity participation should be simple in that outstanding subsidiary loan charges should not be converted into equity. Applications for equity should be dealt with under the procedures established for development projects and any need for subsidies should be considered accordingly under the revenue budget. These two items should not be confused and should be shown separately and clearly in both the budget and accounts.

8.5.24. Whilst on-lending comes under the Development Wing, equity participation is dealt with by the Autonomous Bodies Wing. There would certainly be a case for combining these responsibilities under the same Section, namely the Development Wing, leaving the Autonomous Bodies Wing to concentrate on its monitoring procedures.

Recommendation

68 Loans to Autonomous Bodies should not be converted to equity. Where new equity is issued, it should be treated as an investment.

8.6. Guarantees*Background*

8.6.1. CORBEC expressed concern about the extent to which the Government is required to give guarantees for both domestic and foreign loans because under the Constitution whenever a payment has to be made by the Government for either a guarantee or a counter guarantee the expenditure is automatically charged to the consolidated fund, regardless of whether any budgetary provision has been made. It is, however a practice which is standard in most countries.

8.6.2. The most usual requirement for Guarantees are those in respect of loans contracted by Autonomous Bodies. Also, on rare occasions Guarantees are given for foreign loans to the private sector when the overseas lender has made it a condition of the loan. Another variation is that the Bangladesh Bank as the Central Bank of the country is frequently asked to guarantee the repayment of loans in foreign currency when required and these are always covered by counter guarantees by the Government.

8.6.3. Whilst Article 81(1)(b) of the Constitution gives a definition of a Money Bill which includes a Bill dealing with "the borrowing of money or the giving of a guarantee by the Government, or the amendment of any law relating to the financial obligations of the Government", as far as could be ascertained there is no legal requirement for such a bill to be enacted for guarantees, which is an anomalous situation.

Existing Procedures

8.6.4. Where a guarantee is being sought, application has to be made to the Autonomous Bodies Wing in the Finance Division of the Ministry of Finance.

8.6.5. If after examination the giving of the guarantee is to be recommended it is sent to the Finance Secretary for formal approval. There are occasions, however, whereby the approval of a higher authority, such as the Minister for Finance or the Cabinet, is needed. Examples are hard term commercial loans, which have to go before Cabinet, and guarantees for large loans where policy issues are involved which could be put to Parliament, e.g. aircraft for the Bangladesh national airline. When approved, the guarantee is given formally by the Joint Secretary (Budget)

8.6.6. All guarantees given should be recorded in a formal Guarantees Register kept in the Budget Wing of the Finance Division.

Weakness of Present System

8.6.7. There does not appear to be any formal documented procedure to meet the present day needs for the giving of Government Guarantees.

8.6.8. There is no reliable method of establishing what guarantees have been given by the Government as no guarantees register appears to exist for the period prior to the financial year 1984/85. Until such a reliable record can be created, the extent of the Government's contingent liabilities for guarantees given and outstanding would be difficult to assess, even though the position should be highlighted in both the budget and the accounts at least as a memorandum note.

8.6.9. Whilst under the Constitution any payments made under a guarantee are an automatic charge on the Consolidated Fund, there is no formal method in existence whereby Parliament approves guarantees given. In many countries this is done by publishing certain details of guarantees given as statutory instruments and then laying them on the table at Parliament for approval.

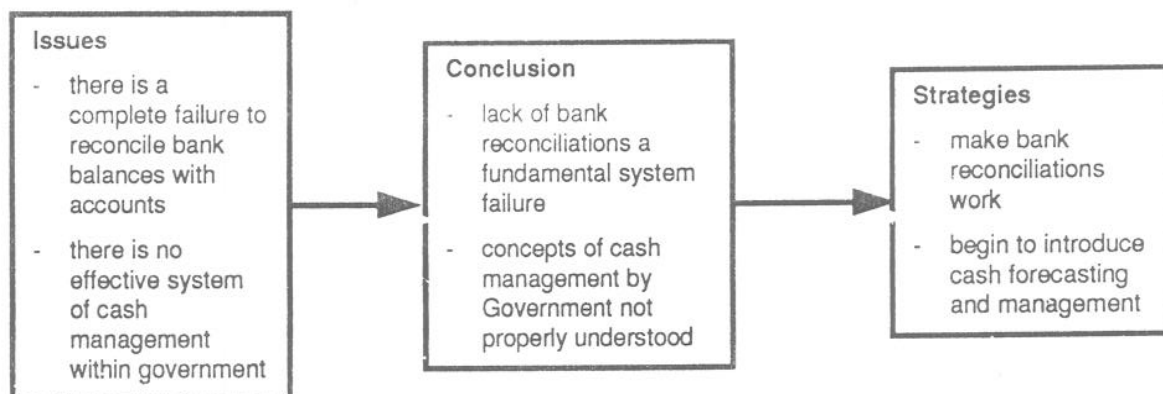
Solutions

8.6.10. Because of the absence of reliable records and a properly documented system, the strategy for Guarantees should be to firstly establish a comprehensive up to date guarantees register within the Development Wing of the Finance Division and then formally document the procedure that is to apply for the giving of such guarantees, including the promulgation of an appropriate statutory instrument for Parliament's endorsement or approval. Under existing legislation this should be a Monetary Bill which can be enacted under provisions contained in the Constitution.

Recommendation

59 The loan guarantee register should be brought up to date, procedures documented, and guarantees made the subject of a statutory instrument.

8.7. Banking Arrangements and Cash Management



Introduction

8.7.1. An important aspect of financial management and expenditure control is banking and cash management, especially the latter which is making projections of resource availability during the year and matching the use of funds to those resources. If cash management is ineffective, the Government may have to resort to short term borrowing. In addition, if there are funds outside the Government's control, there may be a need to borrow to meet short term deficits, even though there are large balances in bank accounts outside the Government system.

8.7.2. This section of the report will look firstly at the Government's banking arrangements and then at the aspects of cash management.

Banking Arrangements

8.7.3. The Bangladesh Bank, the Central Bank of the country, acts as the Government's bank and custodian of its monies. Its functions on behalf of the Government include the collection of receipts, making payments, remittances of cash between accounts and the first lender to the Government to meet any cash shortfall.

8.7.4. It has branches in just 7 places throughout the country and where there is no branch, the Sonali Bank acts as its agent and performs the necessary treasury functions. In the Government's bank accounts there is no differentiation between Consolidated Fund balances and Public Account balances. The entire cash balance with the Bangladesh Bank is treated as one. However, for the convenience of accounting, the Government's transactions are recorded in 29 main accounts, including 20 allocated for the specific transactions of Chief Accounts Officers and 6 sub-accounts. The special accounts for counterpart food aid funds are treated as sub-accounts in the bank.

8.7.5. However, outside this system are the commercial bank accounts held by development project implementing agencies, some of which such as SAFE meaning special account in foreign exchange and CONTASA meaning convertible Taka special account the Government has been encouraged to open by aid donors to speed up the use of funds, bank accounts held in Districts for such purposes as land acquisition, accounts operated by Chief Accounts Officers through which project aid monies are passed to project bank accounts, the USAID deposit account with the American Express Bank and more recently, imprest and revolving fund accounts set up by certain aid donors with the Bangladesh Bank but outside of Government's bank accounts.

Bank Reconciliation

8.7.6. It is the Controller General of Accounts who has the task of reconciling the Government account with the Bangladesh Bank. Whilst daily returns are received from the Bangladesh bank no checking is done on these. The monthly return is used for the basis of reconciliation and verification of the Government account balances.

8.7.7. The cash balance shown by the Bangladesh Bank is apparently always found to be lower than the figure shown in the compiled account of the Government by an amount generally in the range of about 90 to 200 crore. Each month the Controller General of Accounts notes in the register that "the bank is showing a less figure" but there is no analysis of the difference and no further explanation is recorded. For the month of July 1992 the difference was actually just in excess of 527 crore which is more than five billion taka. The explanation given was that the differences occur because approximately the last 10 days monthly figures from the Sonali Bank and the Bangladesh Bank are not included in their monthly statements. This is despite the fact the monthly statement from the Bangladesh Bank is generally about 2 months late, which should give adequate time to ensure that it is correct and meaningful. The differences are apparently not drawn to the attention of the Finance Division.

8.7.8. A cursory check of the amounts shown by the central accounts section of the Bangladesh Bank with the accompanying advice for direct payments and receipts is done every month to ensure the correctness of the figures but there is no reconciliation back to the originating authority. It would also appear that of the 458 branch offices of Sonali Bank, test checks with the respective accounts offices on the balances shown for 20 of these are carried out each month but no reconciliation of the difference is undertaken.

Reconciliation Weaknesses

8.7.9. The main problem is that a complete and proper bank reconciliation is not being carried out by the Controller General of Accounts Office as it should be. In accordance with Article 272 of the Account Code, Volume IV the Controller General of Accounts should furnish a certificate that the cash balance with the Bangladesh Bank has been checked and reconciled with the books of the Government. However, whilst certifying the annual account of 1991/92 the Controller has recorded an unreconciled difference of Tk 340.84 crores for which no satisfactory explanation has been given.

8.7.10. Ancillary problems include:

- (i) The subordinate offices involved with the bank reconciliation process do not appear to attach much importance to this extremely vital area of accounting work;
- (ii) No manual exists for the procedures to be followed for a system which has become much more complicated with the advent of the decentralisation of accounts and the rapid expansion of Government activities;
- (iii) There is little effective verification being done on the correctness of revenue receipts paid into the banks;
- (iv) The non-inclusion of transactions in the month end statements prepared by both the Sonali Bank and some Regional Accounts Offices as well as the lateness of submissions make the cash balance reports of the Bangladesh Bank and the Government unreliable.

8.7.11. The accounts maintained in commercial banks and the new imprest accounts at the Bangladesh Bank, all in the name of the Government, are excluded from the reconciliation process.

Adequacy of banking system

8.7.12. Concern has been expressed to us as to whether the banking system would be able to cope with its side of the reconciliation requirements, even if all of the problems on the Government accounting side were resolved. We could not answer this question, as we have not had access to the accounting system of the banks. However, the Sonali Bank is itself receiving very substantial assistance to upgrade its systems, and therefore it would seem appropriate to assume that by the time the Government system is upgraded, the issue of the bank capability will have been addressed.

Importance of Cash Management

8.7.13. Apart from the absence of proper bank reconciliation, cash management in Bangladesh, including cash flow forecasting, appears to be ignored. The table below summarises the issues.

Table 15: cash management

Why cash management is ignored	<ol style="list-style-type: none"> 1 Government departments and spending agencies experience no cost of funds, and hence no benefits, or conversely costs, for managing funds well or badly; 2 the main focus of budget execution is on the release of funds, and the actual spending of money is not well co-ordinated with apportionment of budget appropriations; 3 the main focus of Government accounting is on the propriety of expenditure, not the efficiency of fund utilisation.
Why it is important	<ol style="list-style-type: none"> 1 impact on public sector borrowing requirement - bad cash management can increase need for temporary borrowing 2 there is a real interest cost or benefit to Government 3 important for Fund stabilisation programmes (not relevant in Bangladesh)
The four components of effective cash management	<ol style="list-style-type: none"> 1 Cash flow forecasts, profiling over the year the timing of cash inflows and outflows 2 cash inflow control - measures to accelerate flow of receipts 3 cash outflow control - management of timing of disbursements 4 bank balance management - keeping balances in subsidiary bank accounts to a minimum

8.7.14. There is no phasing in the allocation of revenue funds (see Section 3 on budgets). Although development funds are released in a somewhat phased manner, a large proportion are channelled through separate bank accounts over which the Government has limited or no control.

8.7.15. Ineffective cash management could mean that the Government will have to resort to short term borrowing to meet temporary deficits. It should also be borne in mind that the cost of financing a deficit, either short or long term, can have a significant impact on resources available for other purposes. Borrowing costs money and to do so unnecessarily is simply a waste. The following paragraphs describe responsibilities for cash management in Bangladesh, including short term debt management.

Cash Management and Ways and Means

8.7.16. It is the Ways and Means Section of the Finance Division, Ministry of Finance, that has the responsibility for cash management. In order to carry out its function effectively, it should initially establish from the budget what deficit will have to be financed during the year and then by preparing cash flow projections, in conjunction with the Bangladesh Bank, the Government's banker, be able to work out how to minimise any borrowing costs. This is not being done.

8.7.17. It would appear that the Ways and Means does not at any time use cash flow projections to work out from the annual budget what the Government's borrowing requirements are likely to be over the year. There is no cash flow forecasting and thus no system of achieving control through a payment plan based on the estimated cash requirements of the disbursement officers. The allocation and disbursement of funds for development purposes is controlled on a quarterly basis but with little regard, until the final quarter, of any actual cash flow.

8.7.18. In conjunction with the Bangladesh Bank, which under the Bangladesh Bank Order of 1972 has been given the responsibility of managing public debt and issuing new loans on behalf of the Government, the Ways and Means Section on advice and information received uses the under mentioned main local sources in order to meet deficit financing:-

- (i) What are called Ways and Means Advances, which is the term given to the Government's first line of borrowing which is given automatically by the Bangladesh Bank in the form of an overdraft facility. This advance is made on a daily basis up to a maximum of Tk 20 crore and does not need any prior approval from the Ways and Means Wing as Government has a standing agreement for this arrangement;
- (ii) Until recently for amounts above Taka 20 crore, 91 day Treasury Bills were tendered for by the commercial banks. The authority for these issues was given by the Minister for Finance on the advice of the Ways and Means Section which in turn acts primarily on the recommendation of the Bangladesh Bank. However, under recent changes the Bangladesh Bank issues to itself, without Finance Division approval, Treasury Bills at pre-determined rates for amounts above 20 crore. These are held by the Bangladesh Bank, but may be offered for tender to commercial banks at the discretion of the Bangladesh Bank. This is in effect another form of ways and means advance, but without any ceiling or prior approval requirement. It should be noted that the Debt Management Board, recently set up by the Government, is considering the public issue of treasury bills; and
- (iii) Government Bonds for longer term borrowing. These are issued as and when required and are open to all. These have a fixed maturity period and fixed rate of interest. There does not appear to be any set procedure for deciding the amount of an issue. The Ways and Means Section makes the recommendation to the Secretary, Finance Division. Again the Bangladesh Bank is very much involved in making the original recommendation.

8.7.19. Other local sources of borrowing available on a temporary basis include Prize bonds, Wage Earner's Development Bonds and various deposits held under the Public Account.

Other Related Cash Management Problems

8.7.20. The problems of cash and debt management are compounded by the lack of control and forecasting of on-lending liabilities and repayments of autonomous bodies which are dealt with elsewhere in this report.

8.7.21. In addition the Government has no means of monitoring the magnitude of cash balances being held in its name outside the main cash accounts with the Bangladesh Bank. In the financial year for 1991/92 the Government paid interest of Tk 202.71 crores on special treasury bills whilst at the same time an estimated amount of Tk 1117.91 crores was being held in one form or another with commercial banks. Also, very large cash balances, totalling Tk 4343.68 crores, were being held by public enterprises and this figure would include unspent balances of funds released for development projects.

8.7.22. There is not enough emphasis being placed on the importance of cash management and the benefits it can bring when carried out effectively. In this respect the direct link between cash management and its effects on debt management seem to have been forgotten. None of this is helped by certain aid donors disbursing funds direct to project commercial bank accounts without being put through the Government's bank accounts with the Bangladesh Bank.

Solution

8.7.23. As far as banking and cash management are concerned the strategy for the main thrust of the reforms programme should be to:-

- (i) Minimise the number of commercial bank accounts being operated in the name of the Government;
- (ii) Ensure that all monies held in bank accounts in the name of the Government are accounted for as such and not as disbursements as at present. This would mean including these balances in monthly reconciliations;
- (iii) Insist that all monies paid to the Government by aid donors and lending agencies are channelled through the cash Accounts held with the Bangladesh Bank;
- (iv) Introduce a proper comprehensive system of bank reconciliation that is carried out promptly at the end of each month with all differences being explained and recorded;
- (v) Within the Ways and Means Section of the Finance Division of the Ministry of Finance be given more importance to cash management and its inter-relationship with debt management including the introduction of cash flow projections as part of budgetary procedures;
- (vi) Establish a proper system for the raising of local loans in conjunction with cash management responsibilities including a procedure for formal approval by Parliament.

Recommendation

60 Minimise or eliminate the number of commercial banks holding government monies, and insist donors channel funds through the Bangladesh Bank.

61 Action should be taken to ensure that all bank reconciliations are properly and promptly carried out at the end of each month with all differences explained and recorded.

62 Initiate actions in Ways and Means Section to give more importance to cash management.

8.7.24. To achieve these ends it is important that aid agencies are fully appraised of the Government's objectives and that they be encouraged to support the endeavours to successfully bring about these reforms. The long term benefits should be seen as more important than temporary methods of expediency to overcome short term problems.

8.8. Summary of strategies

No.	Strategy	Comment
20	Revenue Collections Undertake a study to identify mechanisms for improving revenue collection procedures	(1) there is a need for more uniformity and simplicity in the systems of collecting and accounting for Government revenue receipts; (2) the question of whether Departments should be made responsible for collecting their own receipts; and (3) the need for effective reconciliation procedures both internally and with the collecting banks
21	Food operations Introduce proper accounting procedures, and ensure all funds banked in accounts with Bangladesh Bank	(1) the question of whether the state trading food account operations be treated as part of the Consolidated Fund; (2) the need to establish correct and simple accounting entries for dealing with the creation and use of counterpart funds arising from food aid; and (3) the need to open deposit accounts with commercial banks for food aid counterpart fund
22	Foreign aid and Development Expenditure Improved procedures putting transactions through special accounts with Bangladesh Bank, stopping most commercial bank accounts, and improving accounting procedures including revised procedures for carrying over unused funds at the end of the financial year	(1) foreign aid monies from donors are being passed through the Bangladesh Bank to the spending project agencies without being put through the Government's accounts with the Bank; (2) a problem of the absence of accounting entries recording direct payments for goods and services, including technical assistance, by donor and lending agencies; (3) there are differing accounting procedures, that do not satisfy the Government's needs for development expenditure financed by foreign aid, resulting from ad hoc arrangements introduced for the disbursement of these funds; (4) the unnecessary use of commercial bank accounts for development projects resulting in the lack of expenditure control; and (5) the absence of budgetary control in relation to development projects.
23	Autonomous bodies on-lending and equity participation Establish a system for recording and monitoring all on-lending in the Development Wing of Finance Division responsible.	(1) the issue of whether it is necessary to include the borrowings of non-commercial autonomous bodies in the budget and accounts of the Government as public debt or whether a simple monitoring system will suffice; (2) action is needed to establish an interim system for processing, recording, budgeting and accounting in respect of on-lending subsidiary loan agreements; (3) there is a need for the development of a system for equity participation that is consistent, transparent in the budget and does not allow the giving of hidden subsidies by converting outstanding loans into equity

24	Guarantees Establish a comprehensive register and implement parliamentary approval procedures	(1) there is a need for a fully documented system for approving, recording and monitoring guarantees; and (2) it is essential to recreate the guarantees register for outstanding guarantees given prior to 1984/85.
25	Banking and cash management Make reconciliation procedures work, avoid unnecessary use of commercial bank accounts, initiate cash management procedures	(1) monies is being held in commercial bank accounts instead of in Government's accounts with the Bangladesh Bank; (2) there is an absence of proper bank reconciliation; and (3) there is a lack of cash flow forecasting and effective cash management.