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INTRODUCTION

1. The purport of this assessment of accounting and auditing in the public sector is to help in implementing a highly effective public financial management (PFM) through better quality accounting and public audit processes. It is envisaged to provide greater stimulus for more cost-effective outcomes of government spending. The specific objectives are (a) to provide the country's accounting and audit authorities and other interested stakeholders with a common well-founded knowledge as to where local practices stand in accordance with the internationally developed standards of financial reporting and audit; (b) to assess the prevailing variances; (c) to chalk out methods to reduce the variances; and (d) to provide a continuing basis for measuring improvements.

2. Information on national standards and practices for accounting, financial reporting, and auditing in the government budget sector and in the state-owned enterprise sector were collected through diagnostic questionnaires that were completed in conjunction with country authorities. The diagnostic questionnaires incorporate the principles contained in the public sector accounting and auditing standards promulgated by the International Organization of Supreme Audit Institutions (INTOSAI) and International Federation of Accountants (IFAC). The responses in these questionnaires have been further explored through discussions by a World Bank team with country authorities. These discussions included examination of accounts and audit reports and working papers to explore the quality of the processes and the products. Annex A further explains the methodology used for the study.

3. The analysis in this report has been conducted in the light of the strong measures being taken in the Kingdom of Bhutan to reform the accounting and auditing processes. New laws on public finance and auditing are in an advanced stage of preparation or are before the legislature. Steps are already being taken in the Department of Budget, the Department of Finance, and the Royal Audit Authority (RAA) to modernize their practices and make better use of information technology and communications.

4. The World Bank and other donors have been involved in assisting the Royal Government of Bhutan in these endeavors. A coordinated effort to prepare a roadmap for comprehensive PFM upgrading is being developed between the donors and the Government. The Country Financial Accountability Assessment (CFAA) completed in February 2002, identified financial human resource development as one of the priority areas. The CFAA recommended that the Government develop an integrated plan to improve financial accountability including:



- Adopting international accounting standards in major public enterprises;
 - Implementing professional leadership in accounting and financial management;
 - Implementing a fully integrated, computerized government accounting system;
 - Drafting new acts on public financial management and combating corruption;
 - Strengthening the Royal Institute of Management (RIM); and
 - Providing training for finance, accounting, and internal audit staff in line ministries and other government agencies, heads of administration and finance divisions, and other managers.
5. The Royal University of Bhutan and its institutions are increasing the attention given to training in accounting and establishing revised and upgraded curricula and courses. Assessment of training needs have been carried out to help in the creation of their medium-term development plans.
6. Annex B provides a summary of international accounting and auditing standards referred to, in this study. Annex C and D provide national accounting and auditing legislation, respectively. Annex E includes a description of the benefits of accrual accounting. The Supplementary Table of Standards and Gaps shows the present position for each component of the existing standards, and the options for improvements that would bring closer conformance with the international standards.