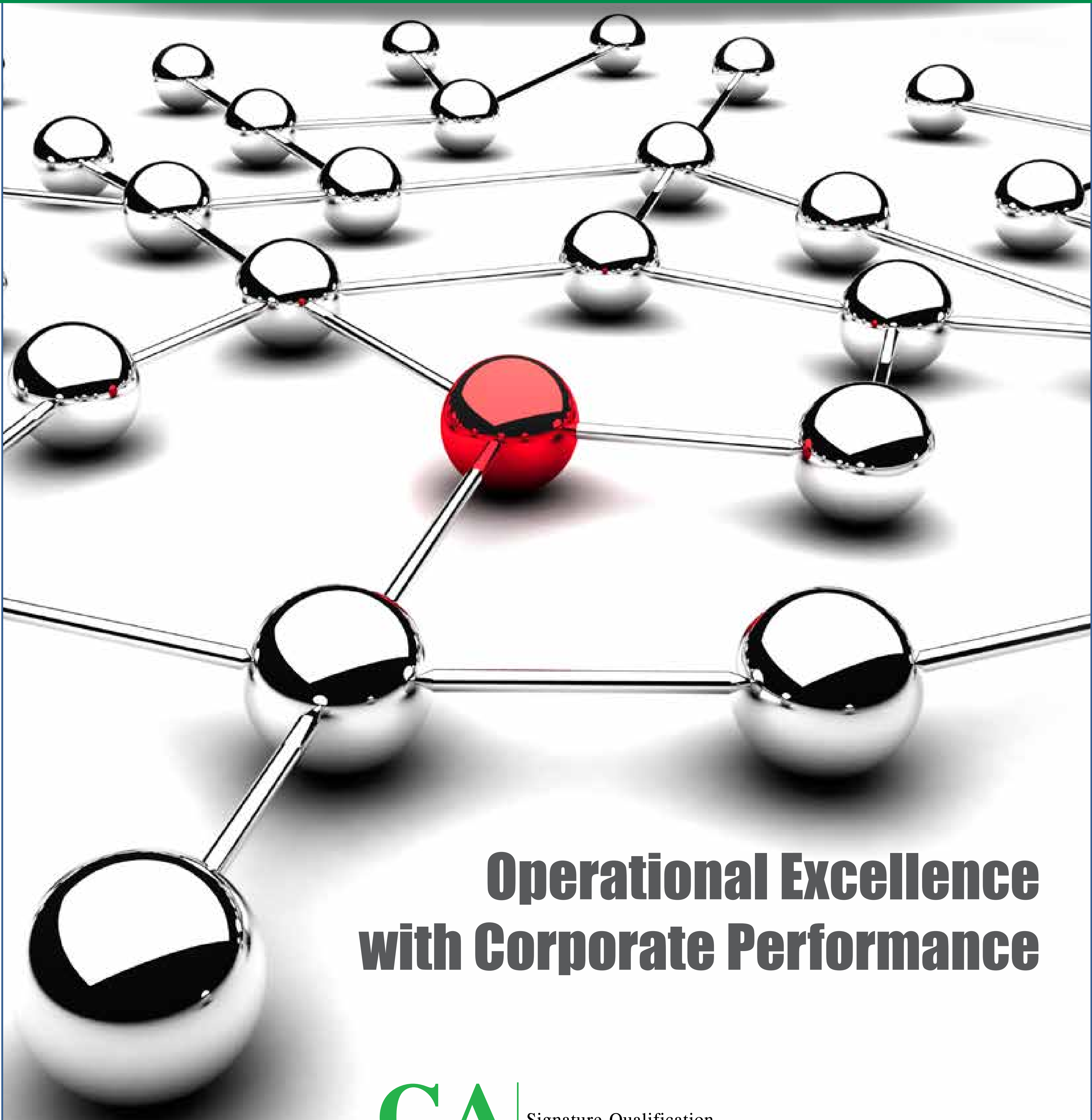
THE PAKISTAN ACCOUNTANT

Apr-Jun 2014

Magazine of The Institute of Chartered Accountants of Pakistan



Operational Excellence with Corporate Performance

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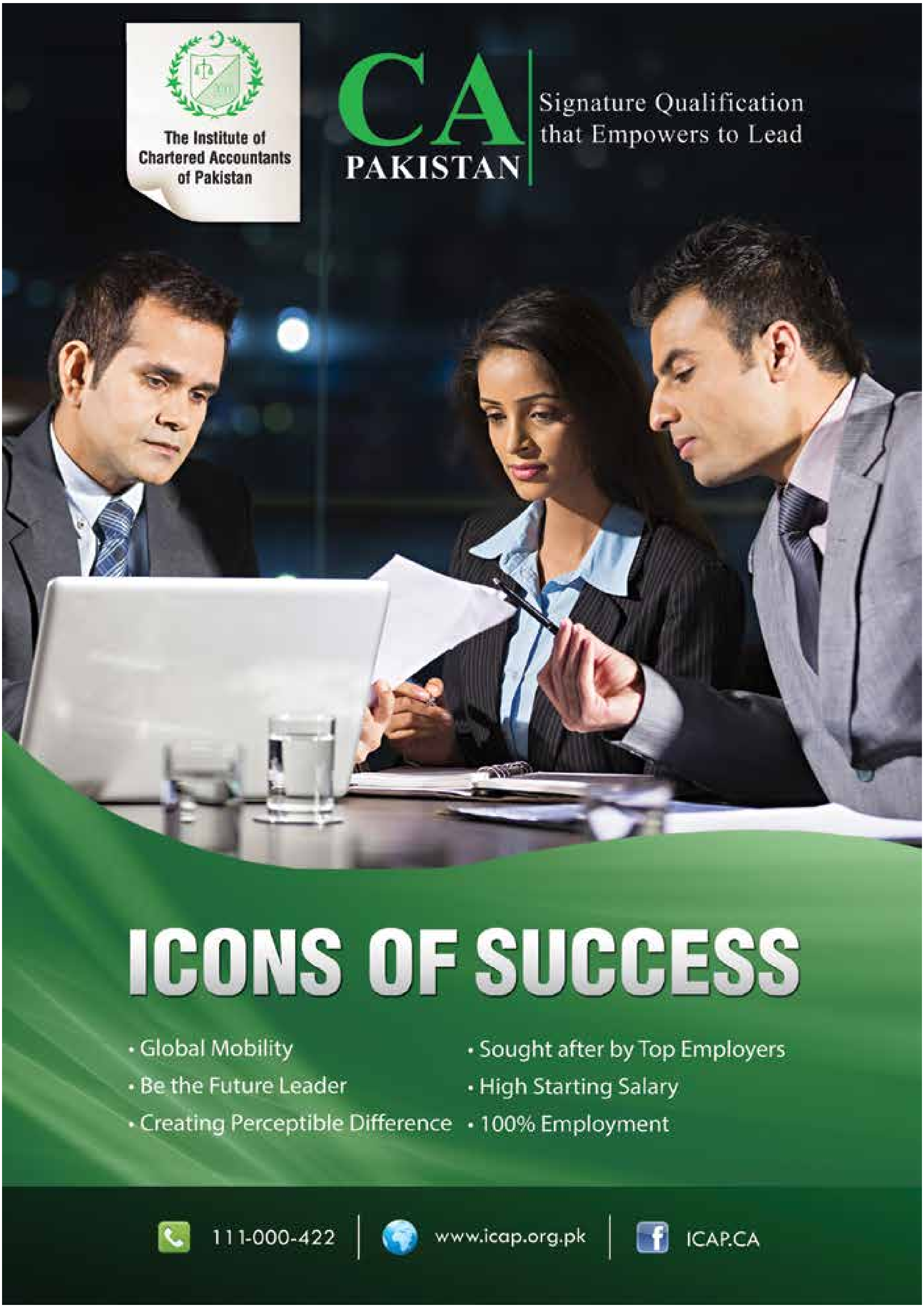
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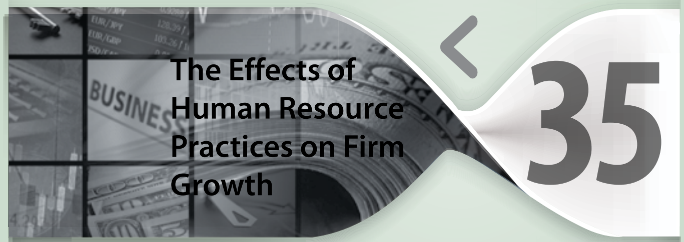

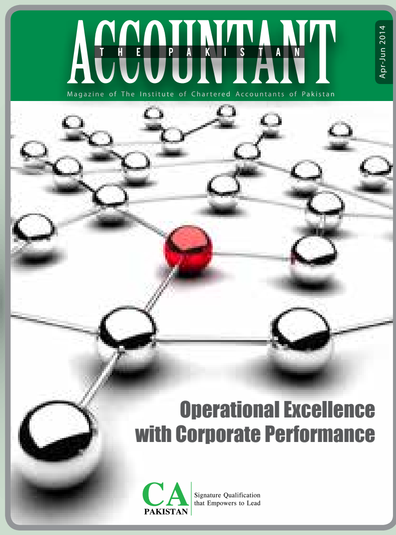

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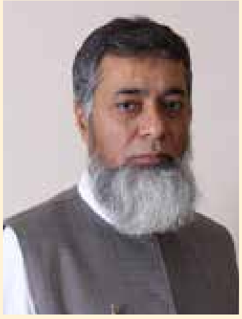


Editor's Letter

"Excellence is an art won by training and habituation. We do not act rightly because we have virtue or excellence, but we rather have those because we have acted rightly. We are what we repeatedly do. Excellence, then, is not an act but a habit."

–Aristotle

Though he was probably speaking to artists, craftsmen and students, Aristotle could have been talking to today's accountants when he wrote those words 2,300 years ago. Industry accountants aspire to the same ambitious goals as Aristotle's listeners. They want their businesses to run safely and more efficiently: to demonstrate operational excellence. But aspirations are not enough; excellence is a habit that results from millions of small acts, performed every day by tens of thousands of employees.

Unlike Aristotle's audience, however, a company cannot simply decide to get better. Because they are large, complex organizations, companies demand a systemic approach to improvement: an operational excellence management system (OEMS), a set of rules that describe how a company is going to operate in order to achieve operational excellence. The best examples are focused, simple and relentlessly applied.

Striving to achieve operational excellence is one of the most important contributors to an organization's sustainable performance and growth. Companies that reach for a higher level of operational excellence reap numerous benefits -- a systemic, evolving and effective approach to business operations; a continually productive and innovative workforce; and an organization that consistently realizes sustainable growth and increasing valuation.

Accountants play important roles in helping the organization achieve and sustain operational excellence. The road is not an easy one, but the accountants have the relationships with the senior management to push for sustained improvements. They also have access to secured information data as well as market conditions, to create a strong case for change and help implementations succeed. Accountants are in an optimal position to monitor performance changes so that stakeholders can see how operational excellence initiatives translate into improved financial results. Today, the quest for operational excellence becomes a part of high level business strategy that is linked to an organisation's journey to high performance.

M. Sharif Tabani, FCA

President's Page

Operational excellence has its origins in industries such as the automotive, banking, computer, pharmaceutical etc. where price and cost competition had led to greater customer-centricity, process efficiency and innovation — which leads to various process improvement approaches such as Six Sigma and Lean Management. These are extremely critical in industries facing extreme competitive pressures resulting in low-margins. In order to remain competitive, markets require holistic and sustainable solutions to rationalize investment budgets, reduce their operating costs, and boost operational efficiency.

Operational excellence approaches were invented to implement a culture of continuous improvement. These improvements are supported by proven analytical tools and working methods that enable measurable and significant development by increasing efficiency, quality and customer satisfaction.

The challenges of today's competitive times is re-building the image of the business operations and making it a global example for growth. The key to re-shaping the future strategy is transparency, consistency and good corporate governance.

The Accounting profession has proved its mantle in handling complex challenges and surmounting the hurdles faced by the economy time and again. The profession has evolved with its multi-faceted roles in the true sense 'Learning from the past and Building the Future'. Chartered Accountants with their unique blend of technical knowledge, foresightedness, methodology and command over processes reap true, meaningful, personal and professional satisfaction from their experiences and are undoubtedly the ones who lead the business in adapting to whatever changes lie ahead.

Ultimately, there is no one-size-fits-all strategy to achieving operational excellence. Each company must assess its own operating environment, strengths and weaknesses. Operational excellence does not mean improving upon all weaknesses, but rather identifying a few key activities and ensuring they are executed flawlessly. Attaining operational excellence is an often overlooked way to gain competitive advantage over competitors.

Naeem Akhtar Sheikh, FCA

Join the Discourse

This issue's topic is:

"Every job is a self-portrait of those who did it. Autograph your work with quality." Quality only happens when you care enough to do your best…what do you think?

Muhammad Hamid, ACA (R-6850)
Karachi

As the old saying goes, "a man is known by the company he keeps". I would change this a bit by saying that "a man is known by the quality of work he does". In today's fast changing world we have to respond very quickly to change in order to keep ourselves IN in the competition and get the desired market share. Therefore, be sure that whatever we do it should be done in the fastest and least expensive way without compromising the quality. What do I mean by quality? I don't believe quality work to be 100% accurate. As applied in accounting the concept of "materiality" should also be applied to our work i.e., a task completed efficiently with material accuracy will deliver the desired results. Quality in cost budget is the need of the day so as standardization. Therefore, standard formats and procedures with relevant controls should be used to ensure that most of our work is done efficiently while maintaining the value.

Muhammad Ali, ACA (R-6930)
Faisalabad

It is vital for survival and growth of every organization to have profound commitment to developing a quality consciousness which is communicated to its all stakeholders including employees through their vision, mission statements and various strategies like Total Quality Management (TQM) & Quality Assurance (QA) strategy. Employee performance has been increasingly related not only to the efficient but also the effective use of available resources while ensuring compliance of quality standards. Quality consciousness organizations document a quality manual that states the quality management system of the organization and establishes a documented quality plan setting out the specific quality practice, resources required and the sequence of activities relevant to particular product. Some manufacturing organizations have also developed 'Back Track Systems' in order to trace back any process defect to the process owner in order to achieve zero defect level.

Humayun Habib, ACA (R-5111)
Johor Bahru, Malaysia

Recently I read in HBR companies that turn employees' struggle into growth opportunities are discovering a new kind of competitive advantage. To an extent that we ourselves are only beginning to appreciate , most people at work , even in high-performing organizations, divert considerable energy every day to a second job that no one has hired them to do; preserving their reputations, putting their best selves forward, and hiding their inadequacies from others and themselves. We believe this is the single biggest cause of wasted resources in nearly every company today.

Shafiq Ahmed, ACA (R-4421)
Muscat

Professional competence, integrity and due care are the hall mark of any profession as it is evident from the code of ethics for professional accountants by IFAC. Nevertheless, quality of work drives from an unrelenting attitude to continued learning and professional development. The work of the accountants and its products are a source of information and decision making to a wide spectrum of users. The best products are normally thought to have derived from compliance with the standard minimum requirements and operating procedures, however, continued professional development, use of technology as well as continuous effort for objective based value addition are equally pivotal to the quality of an accountant's work and its products. The advent of the latest technological advancements has significantly cut down the cost of resources enabling the accountants to focus more on quality driven efforts matching with ever growing requirements of the entrepreneurs and other users. The professional accountants affiliated with recognized accounting bodies have added pressures from the regulators and other monitoring authorities who act as deterrent for them to maintain the quality of the work and meet minimum compliance requirements.

Abdus Slam, ACA (R-7627)
Faislabad

Quality objective - State of being free from deficiencies, Freeing work from deficiencies does not mean covering mistakes rather eliminating them through care.

Achieving Quality - Quality does not happen instantaneously but it's being created. To achieve quality in work requires "Quality Care".

Quality care - It exists when you follow "Better than before approach". It means to adopt a cyclic approach----errors/problems----correction/solution-----improvement -----Quality. Cycle recurs again. It means not being complacent with your existing performance but careful in finding ways to insert improvements in the work.

Munir Muhammad Shafi, ACA (R-7432)
Karachi

The word Professionalism is a multidimensional terminology. Many precious traits like Knowledge, skills, determination, honesty and hard work etc. grace this word with its true essence. The display of Professionalism at work eventually leads to the quality generated from every output produced with the sincere effort of an individual. In the field of Accounting and Finance, the quality is basically linked with transparency in financial reporting, compliance with regulatory requirements, productive analysis to help decision making that enhances shareholder's value and a good display of ethics at work. All these milestones cannot be achieved without a real display of 'Professionalism' at work. The role of an accountant has now been evolved far more than a mere number cruncher. A finance professional is now even expected to diligently assist in key strategic decision making that enhances Shareholder's value. A good display of dynamic and proactive approach is required to produce the required quality and embark with professional excellence.

Fawad Hassan, ACA (R-7108)
Islamabad

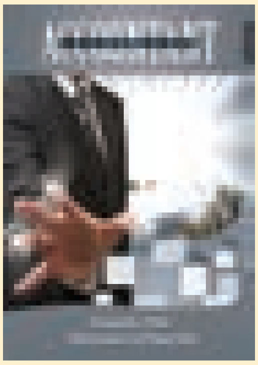
World is competitive, and it has been this way since inception. Its basic human instinct to acknowledge and respond to competition going around. It's not surprising that in corporate world, everyone is striving to be the best and irreplaceable. Quality Output can make you the finest arrow of quiver.

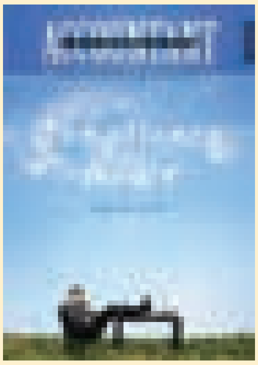
"ABILITY" and **"WILLINGNESS"** are traits which can be pronounced as pre-requisites for a quality output.
Beware of instances which can blunt any of these attributes.

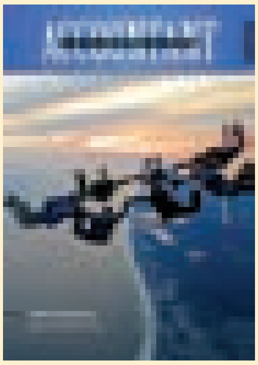
What impairs **ABILITY**? …..Of course, carelessness would be a stock answer, cope it !!! Secondly, knowing nitty-gritty of a task may not be enough, if you know how to do a job by yourself, learn to get it done through your vice also, especially when you are working somewhere at middle or top levels of hierarchy. Understand assignments, delegate them, keep follow up and supervise.

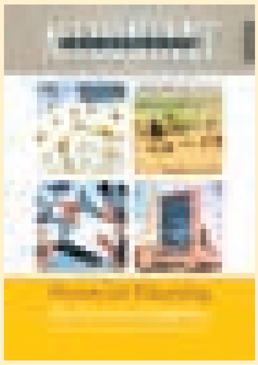
How **WILLINGNESS** is blunted? You think you are a marathon worker but your efforts are not acknowledged. Your peers get appreciation despite the fact that you work more than anyone else. Workplace has become a place of depression…… Refresh yourself and understand the difference between efficiency and effectiveness. You may be efficient but may not be effective !!! Admit your weaknesses, as it is the first step towards excellence.

THE PAKISTAN ACCOUNTANT NEEDS YOU









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Possible Categories

- Auditing and Accounting
- Value addition to SMP, SME
- Corporate Law and Governance
- Islamic Finance
- Sustainability and Social Accounting
- Banking
- Taxation
- Risk Management
- Information Technology
- Economy
- Business Management
- Human Resource
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Articles received after the due date will be used for the successive issues upon approval of the Publications committee.

Members are requested to send in their articles at the earliest at any of the emails below:
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Thank you

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Enabling Insight towards the Challenges in Business Operational Performance

Zeeshan Iqbal

Operational performance has become widely recognized and accepted as a critical success element for companies. It is best described as the level at which all business units in an organization work together to achieve core business goals. Unlocking operational performance requires the proliferation of transformational initiatives, motivated by development, maturation and affordability of innovative solutions that allow businesses to transform, compete and succeed.

There are two primacies i.e. Revenue and Profit growth which were steadily displayed up in all reports of the business. So, by what means do we ensure that our profits are rising while staying focused on attaining revenue growth? This is where excellence in business operations becomes critical.

Operational Excellence is an attitude of guidance, collaboration and problem solving resulting in constant improvement throughout the organization by focusing on the needs of the customer, empowering employees, and enhancing prevailing activities in the process. When people, processes and systems in a business are operating at 100% efficiency and productivity, excellence becomes a given business goals and priorities no longer remain a wish-list. This should be an easy to achieve state in a perfect domain, in the end why would anybody not want his organization to succeed or why would systems and process not work at 100% efficiency?

There is no. of obstacles inside the organization that bound companies from attaining operational excellence and that includes.

Structural Silos (or Absence of Alliance)

Constant enhancement can only happen and be sustainable when there is a well-coordinated isometrics that combines discrete steps into a joint effort. This is very challenging to do if each part in an organization acts individually and does not take into account how and where other parts can contribute to their development plans. When everybody take part and act as a team to build and act on one strategy that has a common goal and clear accountability for the steps necessary to achieve that, operational policies would be so much easier to implement.

year out of balance. Too often, these procedures are performed in a top-down way with no tying-in of the strategic goals to the implementation steps. It is quite normal for the employee to lose focus and direction when they can't visualize exactly how they are contributing to the company's high level goals. Whether it be an annual or a quarterly exercise, strong guidelines for planning and execution of the procedures goes a long way to ensure that you retain sufficient control over where and how operations needs to focus on during the period to meet the business goals.

Outdated Systems and Technology

Putting off investments in new IT infrastructure may save money in the short term, but sticking with older technology may hurt a company's credibility with employees and customers. Usually performance management systems and spreadsheet-based processes engage managers in endless detail and consume more of their time trying to shuffle between systems and sheets and integrate the output of multiple systems. Managers spend most of the time (80%) getting the systems to work and the remaining time (20%) on actually executing on the information. Companies should get their technology updated to best support their business objectives as it is a good investment and worth every penny in the long run – as it frees up the resources to spend more time on analysis and execution.

These major barriers as concluded are not the sole ones that cannot be overcome with a little focus and a lot of effort. Smart employees support with the right tools, realistic planning, and the desire to catalyze positive change across the organization, it is possible to make significant developments to accelerate the journey towards operational excellence.

Absence of Granular Information

As we know that information in raw form of data is not knowledge but is the first necessary phase towards intelligence. Sometimes organization's financial systems crunch revenues and costs into kinds that work well for the company's financial reporting but are not granular enough for competent operations management. Unawareness in employees about tasks is a big barrier to do any kind of accurate performance management. Conflict in information leads to incorrect planning and it arise due to various data sources and non-transparency in information sharing. For any successful plan, annual data and knowledge management strategy is a must that depends on trends and analysis.

Lack of commitment from the Senior Management

Except the others, this one part needs full support from the senior management in terms of consistency in direction setting and the will to enforce the much needed discipline. The tasks that are commonly not well-aligned to the overall business goals – for example, sales runs after revenue growth and does not care about profitable growth, finance pushes for bottom-line at the cost of top line improvement, delivery gives meeting milestones priority over costs. Business primacies need to be powerful, strong and steady throughout the organization to create a culture where responsibility for performance is pervasive, accountable, and aligned.

Poor Planning for Success

Improper procedure for the basic building blocks of planning, budgeting and forecasting, made the entire

A Second Check on Operational Efficiencies of a Company

Muhammad Adeel Sarfraz, ACA

The concept of Internal Auditing evolved after World War II with the progress of management science. After emersion of ENRON case in 2001, global corporate environment significantly moved towards strict compliance and monitoring of business operations before getting too late to cry over spilled milk. To overcome the risk of business failure in Pakistan, Securities and Exchange Commission of Pakistan (SECP) issued Code of Corporate Governance (Code) in 2002 for regulating and monitoring various corporate matters. Among other significant matters, the Code specifically regulated listed companies to establish a separate and independent Internal Audit (IA) function, whose head shall have access to the chair of the Audit Committee. Despite complying the regulations, IA has yet to be evolved in its true spirit. Internal Auditing can be defined as:

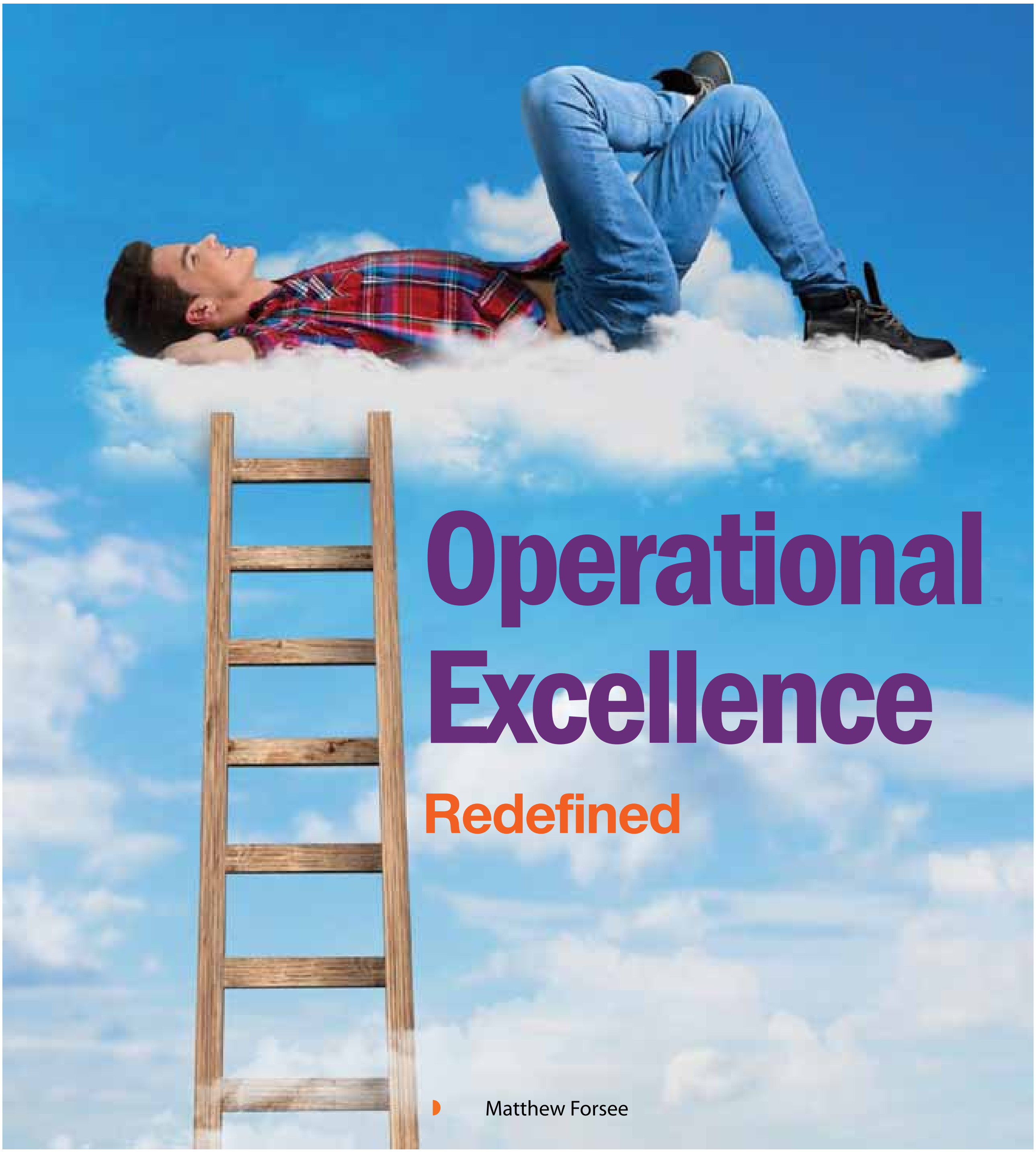
IA helps an organization accomplish its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Internal auditors are not responsible for the execution of company activities; rather they advise management and the Board of Directors regarding how to better execute their responsibilities. However, targeted department/process owner has a common perception of not sharing their information in full with IA, due to the *misunderstanding* that the more information IA receive, the more it get opportunities of raising concerns about their operations. Therefore, the information coming out of the department is very limited; which is creating a gap in working environment and thus encouraging inefficiencies in the organization, as a whole.

IA is said to be eyes and ears (probably the only *official* one) of the senior management of the company. Their prime objectives include to highlight control weaknesses in the company and to report the same to company directors through Audit Committee. The audited department is too busy in daily operations that at times, they might overlook some of the weaknesses. There may be some unwritten policies and procedures, which should be brought down to black 'n white. Now here comes in the role of IA; the identifier of loop holes and control weaknesses. IA also highlights the areas which need some improvement/refinement in it. Along with leading the department, the head has highest priority for eliminating all the possible high level risks. Once all high risks are secured within the department, department heads then go to mitigate medium risks, while not compromising on high risks. Usually, HoDs, don't get time to come to risks categorized as low. IA looks for all types of risks (H/M/L) in a particular process. Due to a good performance by HoDs, mostly high and somewhat medium risks are already well covered; whereas, the remaining medium and low risks are identified and highlighted usually by IA. Nevertheless, a second eyed review is required, in order to help concerned department, to identify process risks and mitigations thereof. It is also a possibility that a certain process doesn't have any unaddressed risk, in which case IA should not go into unnecessary details just to raise audit observations. IA also has to look for those medium/low level risks which, in combination, may lead to high level risks.

On the other side of story, IA is the representative of senior management of a company towards middle/ lower management. Its duty of IA to report risky areas which could possibly impede the overall objectives of the company. IA should keep its eyes and ears open within and outside the organization to identify any such risks. The audit plan should not entirely depend on random selection, rather a carefully identified risk based areas should be targeted. Internal auditing professional standards require the function to evaluate the effectiveness of the organization's Risk management activities. The audit plan should also consider location based risks such as cash handling and disposal process on plant sites, audit for marketing techniques and consolidation & reconciliation of disbursed processed at head office et cetera. Based on a risk assessment of the organization, internal auditors, management and Boards determine where to focus internal auditing efforts.

In order to excel in industry and attain organizational goals, every department has to support other departments while not compromising its own goals. Every department works hard to achieve their objectives within time; and so does the IA. An audited department should realize that a process will never reach for perfection; but there will always be a room for improvement. And IA is there to *help your department* to achieve your departmental goals, in more efficient and controlled manner. It is the coherence and coordination of all the departments that helps in accomplishing overall objectives of an organization.



Operational Excellence

Redefined

Matthew Forsee

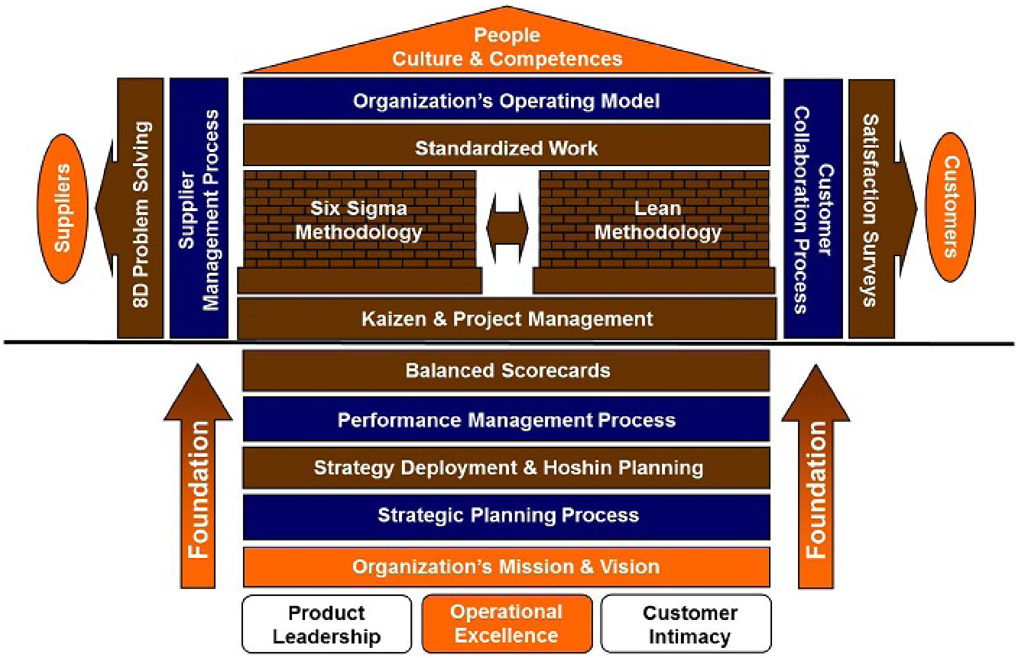
Operational excellence is about five things: driving innovation; managing talent; improving customer retention; ensuring strategy aligns with tactics; and determining optimal enterprise velocity. Operational excellence is a mindset, not a tool that helps increase profitability, productivity, retention, and innovation.

In a faster, more inter-connected world, organizations can't expect to use the same strategies and continue to be successful. Customers, businesses, supply chains, and the skills required to thrive are all changing. You need to change as well.

In business, Operational excellence is all about consistent execution; when you combine that with excellent strategy, you will be able to achieve the performance you want. It means that you are more consistent than your competitors. It means that customers can rely on you, employees perform consistently (and understand why they are doing so) and that your leadership team is consistent in tone and strategy.

When you get the results you desire, operational excellence will always be a part of that equation. The other piece of the puzzle is reduced risk. Consistent results naturally reduce risk, and, in turn, the costs of doing business. Operational excellence will save you money to make you more money. Operational excellence, then, can create more excellence, profits and growth for your business.

Naturally, the definition and shape of operational excellence can change over the course of time as your culture shifts, technology is updated, and marketplace trends and needs change. That means your leadership team has to stay on top of operational excellence and consistent results. You may need to revise how operational excellence looks for your business next year or the year after, but the equation should always include consistency in execution to reduce risks and costs. This will all add up to reliable results and increased profits.



While operational excellence alone won't get your business where you want to go, it will contribute to culture, business improvements, leadership and real results.

Organizations pursuing an Operational Excellence differentiation strategy are able to deliver a combination of quality, price, and ease of purchase and service that no other organization in their market or industry can match.

Achieving Operational Excellence requires the successful implementation of a Business Execution System that effectively and seamlessly integrates the following four building blocks: Strategy Deployment, Performance Management, Process Excellence, and High Performance Work Teams.

First, Operational Excellence organizations follow a well-defined Strategy and Operational Planning & Deployment Process that ensures collaboration and alignment among the different parts of the organization and effectively links strategic and operational objectives, initiatives and execution. Strategy Mapping and Hoshin Planning provide this systematic and collaborative planning, execution, and review process.

Second, Operational Excellence organizations are able to translate strategic or operational objectives and initiatives into measurable success indicators and ensure alignment among the different levels and parts of the organization. The Balanced Scorecard Methodology provides a Performance Management framework to ensure alignment of an organization towards common objectives and goals.

Third, Operational Excellence organizations are process-centered organizations that have well designed, efficient, and effective management, value chain, and support processes to deliver best-in-class products and services consistently. Process Excellence concepts, methods and tools, including Six Sigma Methodology, Lean Management Methodology, 8D Problem Solving Process, and Business Process Improvement, are core competences and utilized at all levels of the organization.

Fourth, Operational Excellence can only be achieved and sustained with the right attitude, the right mindset, and the right competencies. Operational Excellence organizations continuously strive to increase the engagement and empowerment of their employees through strong values, guiding principles, leadership development, coaching, and continuous competence development.

The House of Operational Excellence provides a high-level framework for an integrated Business Execution System for Operational Excellence organizations.

Conclusion

For companies finance, accounting, and other critical business functions, operational excellence in their strategy is a "must have" for the predictable, consistent delivery of a high-quality operation. This requirement, combined with the opportunity to leverage the investments to accelerate business transformation, makes careful scrutiny of the operational sophistication, practices, investments, and quality of resources more important than ever. Optimized, compliant, and resilient business processes that maintain secure and well-protected information assets significantly reduce legal exposure and the possibility of negative impact to reputation and brand. They also lead to improvements in cost, customer satisfaction, and productivity.

About the Author:
Matthew Forsee provides leadership for the Shared Services Initiative and the Operational Excellence Initiatives for a private entity. He serves as the point of contact for the entity and is responsible for overall project coordination.

Non Finance for Finance Professionals

Waqas Latif, ACA

Introduction

Finance for Non Finance Professionals is not a new term these days as one can find many luring training brochures on the subject. Further, understandability of financial information and financial awareness among non finance professionals is on the rise in recent years. Now, non finance managers' wants to understand the meaning and sense, the likes of balance sheet, profit and loss account and cash flow statement makes because of the importance and implications of business decisions on top and bottom line figures in the financial statements in which stakeholders are profoundly interested in.

Although, non finance professionals are moving ahead with great zeal for better understanding about financial statements, costing, budgeting, forex and taxation matters, but quite unfortunately finance professionals are still stuck up with the core role of controlling and monitoring the financial vaults of companies with a meager focus of what is happening around the vault in the larger scheme of things in and around the Company.

Infact, not much has been emphasized about non finance knowledge and understandability for finance professionals. But, with the radical shift in ways businesses are run these days. Finance professionals are considered as key contributor in all major business decisions. Now management wants finance to translate their key decisions in terms of quantifiable commercial and financial benefits. Therefore, it is important that the role of finance and accounts department also embody the role of business finance and administration and act as an overall advisor or facilitator to the business.

HIS Model

Although, it would be very difficult to outline major non finance areas which finance professionals should be aware of, still considering various researches and contemporary trends, following three areas could be considered as major knowledge arsenal for finance professionals embodied in HIS model.

The model will be explained in reverse order considering the importance of area in question.

Strategic Planning

In a survey carried out by Deloitte CFO Signals™ in their 2012 fourth quarter periodical, it was discussed, which capabilities would CFOs most likely to improve and the results were not surprising at all. CFOs are obviously quite satisfied with the competencies in key areas like corporate finance, treasury, and audit, but they want to improve in areas that support finance's increasingly strategic role i.e. strategic planning.

According to Paul Mandell, CEO and co-founder of the Consero Group, "The CFO is increasingly being called upon to weigh in on much more strategic decisions involving the company, including everything from transactions to providing assessments of emerging

markets and analyses that go far beyond looking at the

**Deloitte CFO Signals™ survey, fourth quarter 2012*

books and determining whether there will be enough cash to support investment."

Considering the importance of strategic planning from above examples, now the question arises, what knowledge should finance people have about strategic planning and how that knowledge could be used to effectively contribute to the strategic planning process. The details are as follows:

- **Strategic Planning Process**
  Strategic Planning is among the most widely used term and a lot has been written on the subject which is also being used in business. So, there is nothing new about the term. Strategic Planning records a series of unique decisions, the organization has made with respect to its future strategy and goals. It embodies decisions relating to Business Portfolios, Value Chain, Product Mix, Geographies, Customers, Segments, Acquisitions and Alliances etc. A good strategic planning process is one which facilitates the creation of a superior strategy and ensures sustainable growth considering all the risks and external factors.

- **Misconceptions about Strategic Planning process**
  Often the following statements are seen as strategies for businesses:

  - Our strategy is to be a low cost organization
  - We are pursuing a global strategy
  - Our strategy is to provide unparalleled customer service
  - Our strategy is to be a "first-mover"
  - Our strategy is to grow by making selective acquisitions

  The only thing common in the above is that none of them is a "strategy"!

  (Source– Academy of Management Executives 2001 Vol. 15)

  The above statements are merely an articulation of statement of intent of what is important for organization? Which organization doesn't want to lower its costs? Who doesn't want to offer great customer service? Wouldn't your competitors in the same industry say similar things about their intent? The point here is, these are things that would need to be done regardless of the strategy. The above may be very critical for an organization, but they are not "strategic".

  (Source: Ivey Business Journal September / October 2013)

  Secondly, strategic planning should be seen as an iterative process which should be continuously evolved and adopted with any compelling changes in external environment.

  How to effectively contribute in Strategic Planning Process

  Finance professionals by virtue of their knowledge and experience can play a key role in every phase of the strategic planning process. For example they can contribute:

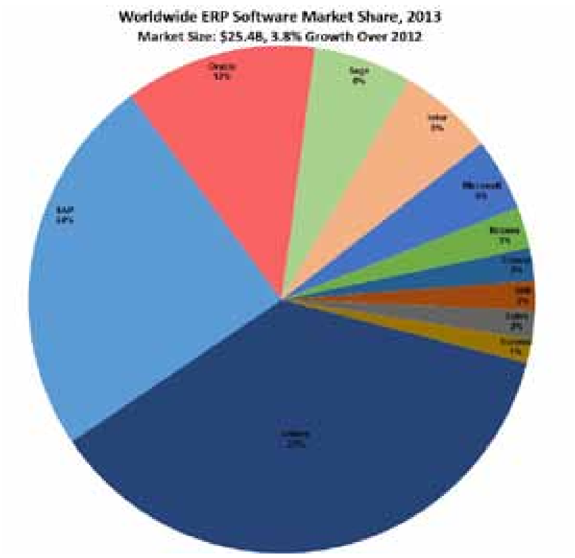
  - By providing important financial information and expertise to the development of the strategic plan by shedding light on organization's financial capacity to deal with risks related to its strategic objectives.
  - By providing external environmental analysis, internal resource analysis and risk analysis about financial and capital markets and associated risks in achieving its strategies.
  - In establishing guidelines and procedures for strategic planning process etc.

Information Technology (IT)

The pervasive use of Information Technology in every aspect of business including internal operations of organization and transactions and with core technologies becoming better, faster, cheaper and easier to use, IT has posted a new challenge to every profession contributing towards organization growth and success.

According to a survey by Internal Data Corporation, non-IT business executives spend 20 % of their time thinking about IT. Therefore, to remain oblivion about this area of business means wasting 20% of your valuable time. Further, there is an immense pressure on businesses to automate processes, to turn to paper less environments where all monitoring and controlling is being done through embedded controls in system and with gross sophistication in analyzing data through data mining and other contemporary methods, finance professionals need to be aware of knowledge of IT to effectively discharge their duties. Following are some of the areas which finance people should be aware of about IT:

- **Enterprise Resource Planning (ERP)**
  According to Gartner's ERP Market Share Update published on May 5, 2014, the worldwide ERP software market stands at $25.4B in 2013. The market share of major ERP players worldwide are as follows:



**Source: Gartner's ERP Market Share Update*

This enormous size of ERP market clearly exhibits its importance to every business these days. Often, Finance people are involved in implementation of these ERPs. Infact, finance has a key role to play in its implementation as the notion goes for every Information System "garbage in, garbage out". So, it is important that accurate data is being inputted with processing of data ensuring compliance to laws and regulations to have desired results as output/information. Also, with rapid changes in taxation laws, it is important that related changes are timely made to the system to ensure adherence to laws.

- **Audit Software**
  The use of IT in audit has clearly revolutionized the whole audit profession. Initially, IT was mainly used as a documentation tool. However, these days audit softwares drive the whole audit process to deliver quality audits while ensuring efficiency and covering all related audit risks. Therefore, now a days, it has become a key requirement for every finance professional in practice to be able to use and understand the workability of these softwares so to be able to deliver quality audits. Not only that, now professional in practice needs to continuously evolved audit methodologies using information technology to ensure compliance with auditing standards and delivering customers expectations of timely completion of audits without compromising its effectiveness.

- **Importance data Integrity, confidentiality and loss protection**
  In a contemporary business world, data is as valuable as money itself. Therefore, protecting its integrity, confidentiality and protecting it from loss is of paramount importance. Out of all types of information organization carries and stores, financial information occupies the most prominent position. With finance professionals as guardians for financial information of the Company ,

  it is important that they are well aware about how to keep its integrity, confidentiality and protect from loss and have a robust backup plan in case of any disaster to Information System.

Human Resource (HR)

People represent the most important aspect of any organization, they are the reasons organizations hit the pinnacle of growth and success and they are often responsible of its dismal downfall. Although, the area of human resource is quite vast, however, there are three important areas which finance professionals should be aware of. The details of which are as follows:

- **Partnering with HR department**
  An Economist Intelligence Unit of The Economist

carried out a research program in 2012 titled *"CFO perspectives How HR can take on a bigger role in driving growth"* the paper discussed in detail about the friction which exists between Finance and HR and its implication and how a more productive relationship can contribute to the benefit of the Company.

Finance professionals need to understand a fact that they usually deals with numbers which are quite measurable and tangible. However, the role of HR is more art than science as quoted by Lucy Dimes, CEO for the UK and Ireland, Alcatel-Lucent. So, finance needs to understand HR perspective for longer-term programmes without having a quantifiable ROI.

Further, the CFO and the head of HR are the only people, along with the CEO, who have an overview of the whole organization and the leadership capability within it (Simon Henry, CFO, Royal Dutch Shell). Therefore, it is important for Finance and HR to collectively endeavor for overall quality and capabilities of staff, their learning and development while ensuring lucrative incentives so that people remain engaged and motivated and perform to the highest level of their capabilities.

- **Cost of Labour (wages, salaries and bonuses)**

According to a research carried out by Duke University CFO Magazine, 2008 which outlines CFO's top concerns, it turns out that Human Resource was second major expense outlay for Organizations.

Further, According to a US Bureau of Labor Statistics study, average spending on salaries as a percentage of operating expense in the US ranges from 18% in retail and wholesale trade to 52% in healthcare services and that excludes spending on training, induction and other employee expenditures.

Following matters should be considered while controlling the cost of labour by finance:

- Performance based incentives, flexible staffing and maintaining employee sponsored health care plans etc.
- Laying off low performing employees instead of blind lay off as cost saving measures and invest to attract the best candidates.
- Wise investment in succession planning and training of staff.

- **Managing Finance Department's workforce**
Often, CFO has been considered as hardliner captain of Finance Department as compared to other departmental heads. Further, CFO heads one of the most qualified workforce in the Company including chartered and certified accountants. Therefore, it is pertinent that in order engage and retain highly qualified people, effective management of finance workforce should be made through engagement culture and maintaining better employee relationship.

Conclusion
The role of Finance professionals has increased many folds with the radical shift in the global economy in the last few years. Now, the new business setup requires finance people to be equipped with not only core financial expertise but also to be able to contribute at a much larger level to other business decisions for overall growth and prosperity of the business.

GOVERNANCE AND TAXATION

Syed Anees Hassan, ACA

Taxation should be conceived and implemented on a larger scale and not with narrow minded approach and for one person's benefit or other's. **Tax is simply a charge, person pays to government for governance** (governance is consideration). Hopefully I didn't oversimplified it!

Government earns by some two main sources one is through Taxation and the other is through Non taxation (e.g., business). Possible main sources of taxation are:

- Income earned by people of governorate
- Entrance and Exit points of governorate
- Use of infrastructure and other assets of government by its people

All the income earned by government has only **one just primary purpose** and that is governance. Government makes governance by managing its affairs, development of its geography and making every possible step for well being of its people in both material and ethical arenas. **The concept of taxation arises from the very concept of government.** As individuals want the government and for this desire they have it, so they have to fund it as well. People want to be governed in best possible way.

Factually government has just one source of income and that is taxation. Other sources like businesses or else are not factual income for governments. A government is run and known for the taxation it collects and its consumption. Otherwise, there is no need for it! It is a **key indicator of government performance. Government's business is governance not money making!** Government may facilitate different ventures through public private partnership in specific businesses but later on government should disinvest its share in it. It does not mean that there is an un-checked market – un-checked market is not considered as governance! (let's leave this topic for some other time)

Taxation is used for all matters pertaining to governance like governmental functional running, development of nation, development of infrastructure, feeding the poor and needy, tackling emergencies, maintenance and development of armed forces, providing of health facilities, providing education to its nation, development of technical and scientific research, development of ethical and moral values, development and facilitation of new research and markets, providing best environment to its people, safety of its nation, law and order, police, justice, law making, ensure employment of its people (by creating such environment where jobs will generate) etc.

Yes! In my view health and education should be free of charge for all people. The uninterrupted supply of other necessities of life at very affordable rates is government's duty under governance model.

Taxation is an **economic cum strategic substance** rather than any other. Taxation is a tool to strategically build the economy and keep economic activity on and protect the local businesses and individuals. Taxation policies could also affect international arenas.

Taxes could be imposed in following two broad ways:

- Direct – this includes income tax, customs, infrastructure tax etc
- Indirect – this includes general sales tax etc.

Here I must agree that few businesses which are basically not for money making but actually part of governance (so actually not businesses) should rests with the government (by business here I mean entity operating for increasing wealth only). For example:

- Railways – a very Important strategic asset
- Special airline – or a division in air force maintained for civilian use
- Special road transportation units
- Heavy mechanical and technical industries of governance nature
- Arm industry
- Scientific research and industries etc.

One of the major role taxation plays in governance is achievement of the prime objective of well being of people and that is **harmonizing the distribution of income** and restricts the collection of wealth in few hands. If in a society there is immense gap between income groups that means the taxation system there is pathetic.

Let's go here with a simple example. Here are brief facts:

Total income of country	**PKR**	**1,000,000**
Total population of country	No.	100,000
Total working population of country	No.	55,000
Children & Teenagers	No.	25,000
Old citizens	No.	5,000
Un-employed	No.	5,000
Non working adult population	No.	10,000
Per Capita	PKR	10
Income per working person	PKR	18

The breakup of total income is:

Income from 10,000 (Group A)	PKR	650,000
Income from 45,000 (Group B)	PKR	350,000

From this we arrive at that there is a huge per person gap between two groups income.

Per working person income in A group	PKR	65
Per working person income in B group	PKR	8
Difference between two groups	PKR	57

Let's have a more detailed picture of this population breakup:

	Group A	**Group B**	**Total**
Working Class	10,000	45,000	55,000
Children & Teenagers	4,545	20,455	25,000
Old citizens	909	4,091	5,000
Un-employed (seeking jobs)	909	4,091	5,000
Non working adult population	1,818	8,182	10,000
Total	18,181	81,818	100,000
Percentage of population	18	82	

Now we assume that proportionately tax will be imposed on two income groups. 40% tax will be imposed on Group A and 2% on the other one. Now see the new picture:

	Group A	Group B	Total
Income (PKR)	650,000	350,000	1,000,000
Tax Rate (%)	40	2	
Tax (PKR)	260,000	7,000	267,000
Net Income retained (PKR)	390,000	343,000	733,000

Few striking facts to be noted are that about 27% of overall income has been taken by government (legally!) while the tax rate for two groups was different. The income at disposal of the rest of population was 73%.

	Group A	Group B	Government
Percentage of Total Income before tax	65	35	-
Percentage of Total Income after tax	39	34	27

Total disposable income with group A is 39% (w.r.t. total income) while with group B it is 34% - see how the difference changed from 65:35 to 39:34:27. This shows that the total wealth contained in two groups has now very less difference between each other. However, due to the number of person's variation, per person disposable income varied.

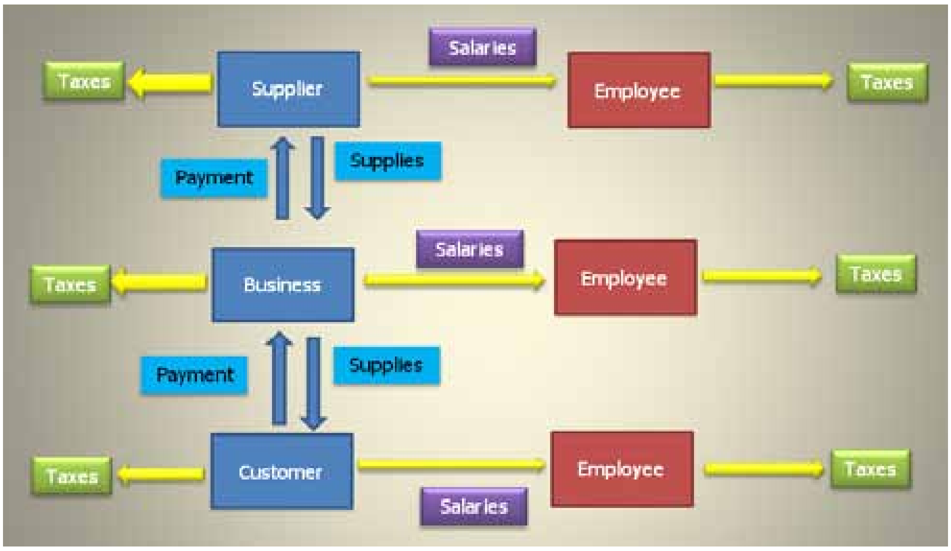
	Group A	**Group B**	**Total**
Per working person income before tax (PKR)	65	8	18
Per person income before tax (PKR)	36	4	10
Per working person income after tax	39	8	13
Per person income after tax	21	4	7

Before and after tax per person income is almost unchanged for group B but has significant impact on group A. With respect to before tax income the distribution is 65 and 35 while with respect to after tax disposable income of PKR 733,000 the distribution is 53 and 47 – see here the decrease and increase of 12% in the two groups.

The government has all in all of 27% of total income for its affairs. We assume here that per person requirement for its necessities and reasonable living is PKR 2. On this premise PKR 2 could be saved by group B persons totaling to PKR 163,636. While group A per person could save up to PKR 11 (being fond of luxury) totaling to PKR 199,991. Therefore this total PKR 363,627 or less than this could be saved and reinvested in the system. If saved and reinvested it will again generate a cycle of economic activity leading to more tax collection. If government is in need of any portion of this saving, it can take the saving from people but not in shape of additional tax which will wipe their saving capacity and morale. Government should collect it in courteous manner like investment schemes or loans etc. Let people have a reasonable share of their own incomes!

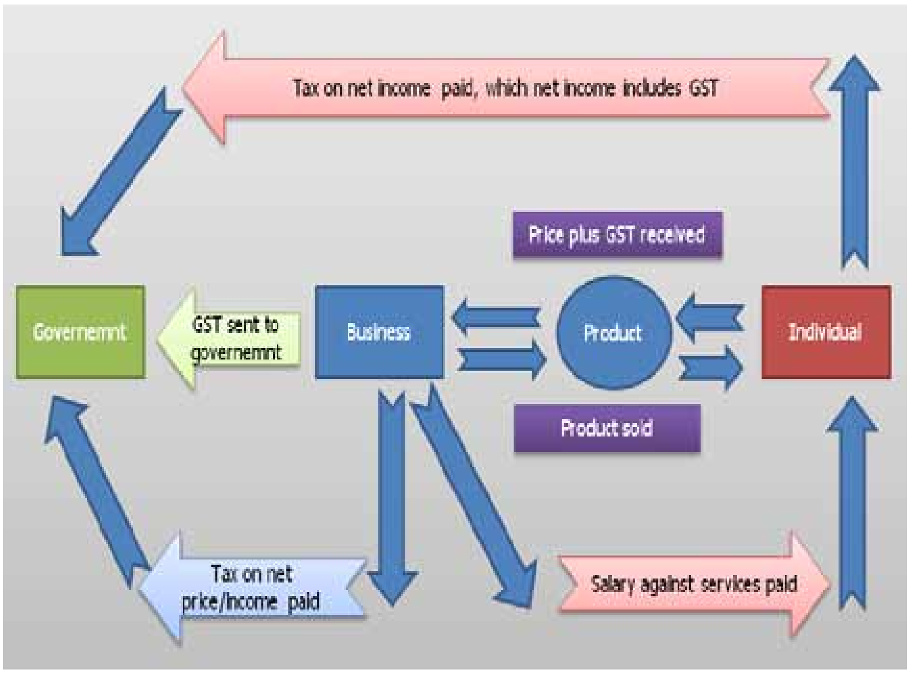
On the other hand, what government collects as tax is ultimately in use of individuals of that governorate in shape of welfare, security etc. Therefore, we can say **tax is not depriving one of one's income; rather it is payment for some most important consideration.**

This example is a very simple description just to get a point. The real economic situations are complex and involve multidimensional reviews having lots of variables and fixed components and statistical analysis. God willing more complex transactions could be discussed later on some time.



Let's move to another important factor in taxation and that is to understand that ultimately individual is the holder of income and bearer of expense. Establishment of businesses is a source/platform/stimulus for economic activity and employment. **Individual-whether entrepreneur or employee etc. is the ultimate holder of income and liable to tax**. All other taxes and levies are intermediary/non-final with but ultimate effect on individual.

On this premise, **business tax should be lower than the individual tax,** provided individual income should be enough for spending a reasonable life with all necessities. However, there should be a total cap of overall taxes (direct and indirect) imposed in the system. **Let the businesses grow and get more taxes from individuals!**



Indirect tax should be lower as its affect is same across all income groups. While direct taxes rates should be high and proportionate. Infrastructure taxes are direct somehow. Taxes imposed at geographical boundaries at entrances and exits are generally termed as customs. Customs have impact on businesses but its ultimate impact is on individual in the shape of high/low product or service price. Customs along-with other tax measures are important tool to protect local businesses as well. Withholding of taxes at sources could be a technique but its purpose be understood. At source with-holding of tax (either direct or indirect) is to be used, ideally, as a documentation tool and as indication for a person's income and expenses which could be used as corroborating evidence. Otherwise, if full tax is deducted at source then it will relieve people of sensing a responsibility to own and deposit their tax returns by their own. **Taxation is an agent which develops sense of responsibility among citizens and fastens the bonds between individual and government (state) and among citizens themselves.** Therefore, like other indirect taxes, withholding tax rate should be minimal and certainly it is adjustable. Those withholding taxes which are termed as final tax for a person should be in very restrictive and particular in cases.

On the basis of above narrated, individual's income simply looks like:

Individual's income	PKR xxxxx
Goods and services purchased (inclusive of customs and other taxes impact)	(PKR xxxxx)
Indirect taxes paid on purchasing	(PKR xxxxx)

Net Income	PKR xxxxx
Income tax	(PKR xxxxx)
Retained Income or Saving	PKR xxxxx

Here we can see that an individual is not taxed just once but at many stages. Therefore, **overall capping of tax is necessary.** It is also highly recommended for smooth running of economy that **tax laws should be straight forward and without ambiguities.** Tax matters resolving mechanism should be fast enough. Tax machinery should be sincere, ethical and professional.

Zero tolerance is advisable for tax fraud or mis-declaration. Its reason is simple because it equals hindrance in governance. Besides, it is untoward thing that one wants government in ones inner-self and then after having it deceive it and break its promises.

There is no room in ideal and fair society for disproportionate distribution of income. It's not the case that one earned more so he should have more and more and that one is not responsible for why another one has not earned more. It could be alternatively argued what such steps have been taken or have not been taken by the society as a whole (including those earning more) that let not earn others earn more. It is basically against the concept of society. Society is termed as one unit – hand cannot say to shoulder as why shoulder has taken more or vice versa and that hand is not responsible for shoulder's low capacity or vice versa – all have to work in unity. If it is supposed that one is to let live at its own, than the concept of government is nothing but a waste. People by themselves desire for government that's why government is there. No human can escape this phenomenon as it is in its very inner-self nature. See the people living in jungles, even they form a government led by their tribal leader.

However, the one who has more is not completely deprived of its income. One should be left with enough spare portion for one's effort for earning more. Only a certain portion of one's income goes to government on the premise that government funds have to be provided on proportionate basis in return for governance and safety.

Nevertheless, the concept of let the richer become more rich is neither appropriate nor justifiable. Government is there to maintain a balance in society. Concentration of wealth in one or few hands could be curbed by government by use of various means including the most powerful of them is tax (let's do not discuss the concentration of wealth here and will discuss sometime later).

In short, taxation is a tool in the hands of governors for governance for strategic cum economic purposes. It is source for achieving society objects of well being. Taxation policies of a governorate depict the culture and nature of a society as whole and sincerity of government. Taxation policies should be made with far-sightedness and strategic objectives. Taxation should be understood in essence; it is not a mere revenue collection phenomenon, it is a regulatory-strategic phenomenon. Taxation is not a burden; it is against consideration and a tool of governance.

I accept that in above few lines it is not possible to sum up the whole story. It is just an effort to hint out at few points and there are numerous issues related to this topic which are not discussed here.

Hostility of Alternative Corporate Tax

Section 113C of Income Tax Ordinance, 2001

Ellahi Bukhsh Qureshi

The Federal Budget 2014 has introduced a new concept of taxation called Alternative Corporate Tax (ACT) by inserting section 113C under the Income Tax Ordinance, 2001. Globally this had already been recognized in the legislation of many countries including USA and also under Indian Income Tax Law.

The intention of the legislature is asserted that this implication is introduced in-order to discourage tax avoidance by companies with the means of perpetual declaration of losses or low income under tax base i.e. after admissible/inadmissible adjustments. It is further emphasized that the said new tax is introduced to facilitate the companies genuinely involved in losses or low income for some period of time.

The introduction of this new concept on one hand aims to increase revenue and on the other hand has engulfed corporate taxpayers with ambiguity, as they cannot reach to ascertain correct tax liability unless an attempt is exercised to go through preparation of two different kinds of tax calculations. Had the intention of the lawmaker been to increase tax revenue, it could have simply done so by enhancing the rate of minimum tax u/s 113 of the Ordinance.

Moreover, it is further by hook and crook applied with retroactive effect from tax year 2014. The section ACT enlightens that the tax payable by the company shall be higher of the Corporate Tax or Alternative Corporate Tax, by completely brushing aside whatever Income Tax Law saying about payment of tax (in technical term it is said as notwithstanding anything contained in the Ordinance). The CT and ACT terms mentioned are defined by the law as under:

Corporate Tax (CT)

Under lexicon of the law, the term is defined as total tax payable by the company, including minimum tax and final taxes but excludes tax under section 8 (tax on dividends, tax on certain payments to non-resident on shipping & air transport income) and any tax payable due to non-compliance of withholding taxes u/s 161 and 162 as well as default surcharge / penalty.

Alternative Corporate Tax (ACT)

ACT means the tax at the rate of 17% of accounting income. For the purpose of ACT, accounting income is defined to mean profit before tax as declared in financial statements for the tax year excluding;

- Share of income under equity method from associate recognition.
- Exempt income
- Capital gains on sale of securities
- Imports under FTR
- Dividend Income
- Supplies and Contracts under FTR
- Export related income under FTR
- Income from Prizes and Winnings
- Brokerage and Commission Income
- Income enjoying tax credit u/s 65D and 65E (industrial undertaking)
- Income enjoying tax credit u/s 100C i.e. NPO's as defined under the said section introduced in Finance Act, 2014.

- Income of the company eligible to reduction of corporate tax rate at 20% under clause 18A of Part-II of Second Schedule introduced in Finance Act, 2014. The said reduction of normal tax rate is subject to conditions specified in the said clause.

The new concept further dictates that expenses should be apportioned between Normal Tax Structure and Final Tax Regime income in order to calculate accurate accounting income. After having determined accounting income under ACT concept and CT, the higher shall be payable by the company for the respective tax year. Where ACT is higher than CT, the excess shall be carried forward for 10 immediately succeeding tax years.

This new concept also elucidate the method as to how carry forward of excess ACT over normal CT be evaluated in addition to clarify that corporate taxpayer shall not be prejudiced or deprived from the entitlement of carry forward of minimum tax as already on statute book through provision to section 113(2)(c). Therefore, this exercise would be burdensome as both sections 113(2)(c) [Minimum Tax] and 113C [Alternative Corporate Tax] shall implicate parallel which will compel a corporate taxpayer to maintain vigilant record of two different of adjustments, one u/s 113(2)(c) and another u/s 113C.

Since excess would be deferred tax assets, therefore, this portion appears to have been omitted to incorporate u/s 147 of the Ordinance to recoup deferred tax liability of the corporate taxpayer which is mandatory in four quarters under a tax year.

Keeping in view of elaboration of law and interpretational assessment on all technical vacuums at grass root level, following 3 examples are produced here in below to comprehend the complexity /methodology of carried forward of excess ACT or CT:

SCENARIO NO: 1		**Alternate Corporate Tax @ 17%**	**Corporate tax**		**Excess to be c/f**	
			Normal Tax @ 34%	**Minimum Tax @ 1%**	5 Years u/s 113(2)(c)	10 Years u/s 113C
		A	**B**		**C**	**D**
Turnover	120,000			1,200	1,200	1,200
Accounting Income	7,500	1,275				1,275
Taxable profit for the tax year 2014	800		272		272	
		1,275	**272**	**1,200**	**928**	**75**

As apparent from the above, the ACT here exceeds the CT (Normal and Minimum Tax) and hence shall be payable by law in this case on one hand and on the other hand, significantly Minimum Tax also exceeds Normal Tax and hence the difference shall also be carried forward under proviso to section 113(2)(c). In addition, the difference between the ACT and Minimum Tax shall further be required to be carried forward u/s 113C. The above scenario results into carry forward of excess of ACT over CT amounting to Rs. 75/- over a period of 10 years and excess of Minimum Tax over Normal tax amounting to Rs.928/- for a period of 5 years.

SCENARIO NO: 2		**Alternate Corporate Tax @ 17%**	**Corporate tax**		**Excess to be c/f**	
			Normal Tax @ 34%	**Minimum Tax @ 1%**	5 Years u/s 113(2)(c)	10 Years u/s 113C
		A	**B**		**C**	**D** A-B
Turnover	120,000			1,200		
Accounting Income	10,000	1,700				1,700
Taxable profit for the tax year 2014	4,700		1,598			1,598
		1,700	**1,598**	**1,200**		**102**

In this example ACT here exceeds both Minimum and Normal Tax and therefore residual excess will be traveling to carry forward u/s 113C. However, since Normal Tax is higher than Minimum Tax, therefore, no excess amount arises under proviso to section 113(2)(c). The outcome of this scenario results in amount of Rs.102/- available for carry forward being excess of ACT and CT for a period of 10 years.

SCENARIO NO: 3		**Alternate Corporate Tax @ 17%**	**Corporate tax**		**Excess to be c/f**	
			Normal Tax @ 34%	**Minimum Tax @ 1%**	5 Years u/s 113(2)(c)	10 Years u/s 113C
		A	**B**		**C**	**D**
Turnover	120,000			1,200	N/A	N/A
Accounting Income	5,890	1,001				
Taxable profit for the tax year 2014	3,824		1,300			
		1,001	**1,300**	**1,200**	**-**	**-**

This example manifests Normal Tax implication since it exceeds both Minimum Tax and ACT and therefore shall be payable by law as one unit in this case. The above scenario results into no eventuality of carry forward of excess amount in both cases, since normal tax is higher than both ACT and Minimum Tax.

In nutshell, mechanism of both sections 113 and 113C shall have to be implemented side by side, for which separate record shall have to be maintained for the amount of deferred tax assets available for carry forward under both sections. Below notified industries are absolved from the purview of this new tax mechanism;

a) Insurance Business

b) Business engaged in production and exploration of Petroleum

c) Business engaged in exploration and extraction of mineral deposits

d) Banking Company

A glaring panorama obviously manifests that our tax wizard sitting in Ministry of Finance have blindly introduced this new spell from importing theme from USA and INDIA without adjudging repercussions when our tax policy has not been consistent where after every year significant changes militates through Acts and Notifications which annihilates impact of established history of an enterprise.

Let's put ourselves in the shoes of the Government with the intentions of increasing revenue in the interest of National Exchequer. Section 113 has indeed some intrinsic loopholes with which companies avoid or condense the tax payable under the said section. Section 113 has an exception where a company declares gross loss before set off of depreciation and other inadmissible expenses. On the same footing, section 113C ceases to provide the exception. One of the ways of tax avoidance which a company could pursue in the case of section 113 is declaring gross loss which they are left out in the case of section 113C. The other one is provisions and incomes rather notional or actual which are avoided from falling under the definition of "turnover" as defined under section 113. For the sake of understanding, let's take an example of brokerage industry. The common revenues earned by brokerage houses include Commission, Dividend, Capital Gain and Re-measurement of Securities at fair value which is a notional value in the financial statements disclosed under the compliance of IAS 39 of International Financial Reporting Standards. For the purpose of section 113, turnover of brokers only include Commission Income, which insignificantly covers less than 30% of the total revenue in the industry. So this scapegoat for brokers, though legal, curtails the efficaciousness of Minimum Tax.

The nutshell of above elaboration clearly explicates that the new concept could not be said to be a significant effort of the Ministry of Finance to increase in revenue rather is an exercise of futility to place corporate tax payers under double jeopardy. The aforesaid amendment has raised overwhelming tax calculations and workings along with enhanced record maintenance and complicating assessments, whereas the purpose could have been achieved by bringing proper amendments in section 113 in order to curtail lacunas which are exploited by the taxpayers or alternatively, the whole section 113 could have been replaced by this new section 113C. By doing so the purpose desired could have attained not at the cost of over-whelming practices and calculations resulting into complexities envisaged at each stage of assessments under the Ordinance.

Pakistan is a Tax Heaven for Foreigners

Syed Imtiaz Abbas Hussain, FCA

Government of Islamic Republic of Pakistan always endeavour to create environment conducive for foreigners for their comforts and satisfaction through applying soft, simple, relax and straight terms and conditions and exemptions and tax concessions in the Income tax, Sales tax & excise duty (VAT Mode) and other income related laws for foreigners.

Income tax

In Income Tax Laws, non-resident foreign taxpayers may be (a) an individual, whose stay in Pakistan is less than 183 days in a tax year, (b) a Firm / Association of persons, if the control and management of their affairs is not situated wholly or partly in Pakistan at any time in the tax year, and (c) a Company, which is not incorporated or formed by or under any law in force in Pakistan, and the control and management of their affairs are not situated wholly in Pakistan at any time in the tax year.

1. The non-resident foreigners are not taxed in Pakistan for their foreign source income;

2. The following Pakistan source income of non-resident foreigners are subjected to special concessional rate of income tax , which are deducted as a final tax, and the non-resident foreigners are not required to file Income Tax Return for such income but to just furnish a statement to the Commissioner of Inland Revenue to that effect:

2.1 Income Tax at 6% on gross amount of (a) a contract under a construction, assembly or installation project in Pakistan, including (b) a contract for the supply of supervisory activities in relation to such project, and (c) a contract for advertisement services rendered by TV Satellite Channels (Section 152 (1A) and (1B) of and (Clause 41, Part IV of Second Schedule attached to) the Income Tax ordinance 2001;

2.2 Income Tax at 5% on gross amount of insurance premium or re-insurance premium (Section 152 (1AA) and (1BB) of Income Tax Ordinance 2001);

2.3 Income Tax at 8% on gross amount of shipping income for the carriage of passengers, livestock, mail or goods embarked in Pakistan (income receive in or outside Pakistan) or embarked outside Pakistan (income receive in Pakistan) from carrying on the business of operating ships as the owner or charterer (Section 7 and 8 of Income Tax Ordinance 2001);

2.4 Income Tax at 3% on gross amount of air transport income for the carriage of passengers, livestock, mail or goods embarked in Pakistan (income receive in or outside Pakistan) or embarked outside Pakistan (income receive in Pakistan) from carrying on the business of operating aircraft as the owner or charterer (Section 7 and 8 of Income Tax Ordinance 2001);

2.5 Income Tax at 15% shall be deducted from the gross amount paid on royalty or fee for technical services to non-resident foreigner (Section 6 and 8 of Income Tax Ordinance 2001);

3. The non-resident foreigners are not necessarily required to be in Pakistan for income tax purpose as they are allow to have any person in Pakistan as

their representative under section 172 and 173 of the Income tax ordinance 2001.

4. The following Pakistan source income of non-resident foreigners are not subjected to income tax as they are totally exempted:

4.1 Agricultural income which includes (a) any rent or revenue derived from land which is situated in Pakistan and is used for agricultural purposes, (b) any income derived from such land, and (c) any income derived from any building which is on or in the immediate vicinity of such land (Section 41 of Income Tax Ordinance 2001);

4.2 The income of an individual shall be exempt from income tax entitled to privileges under the Diplomatic and Consular Privileges Act 1972 or under the United Nations (Privileges and Immunities) Act 1948 to the extent provided for in those Act. (Section 42 of Income Tax Ordinance 2001);

4.3 Any salary received by a foreign citizen employee of a foreign government as remuneration for services rendered to such government shall be exempt from income tax. (Section 43 of Income Tax Ordinance 2001);

4.4 Any Pakistan source income which Pakistan is not permitted to tax under a tax treaty shall be exempt from income tax. (Section 44 (1) of Income Tax ordinance 2001);

4.5 Any salary received by a foreign citizen employee shall be exempt from income tax as per an Aid Agreement, whose salary paid out of funds or grants released as aid to Pakistan. (Section 44 (2) of Income Tax ordinance 2001);

4.6 Any income received by a foreign citizen person engaged as a contractor, consultant or expert on a project in Pakistan shall be exempt from income tax as per a bilateral or multilateral technical assistance Agreement, such income is paid out of funds or grants in accordance with the said agreement. (Section 44 (3) of Income Tax ordinance 2001);

4.7 Any profit received on a security issued by a resident person shall be exempt from income tax, where the security was widely issued by the resident person outside Pakistan for the purpose of raising a loan outside Pakistan for use in a business carried on in Pakistan and the profit was paid outside Pakistan. (Section 46 of Income Tax ordinance 2001);

4.8 Any income of a foreign national (company, firm or association of persons) or any other non-resident person from profit on moneys borrowed under a loan agreement or in respect of foreign currency instrument approved by the federal Government is exempt from total income (Clause 75 , Part I of Second Schedule attached to the Income Tax ordinance 2001);

4.9 Any income received by a taxpayer from a corporate agricultural enterprise, distributed as dividend out of its income from agriculture (Clause 105B, Part I of Second Schedule attached to the Income Tax ordinance 2001);

4.10 Any amount received on encashment of Special US Dollar Bond issued under the Special US Dollar Bonds Rules, 1998 (Clause 135, Part I of Second Schedule attached to the Income Tax ordinance 2001);

4.11 Any income from investment in OGDCL exchangeable bonds issued by the Federal Government (Clause 135A, Part I of Second Schedule attached to the Income Tax ordinance 2001);

5. Other special concession and relieves in income tax to non-resident foreigners includes the following:

5.1 The income tax at 10% instead of 20% to be deducted under Section 152 (2) in respect of payments from profit on debts from debt instruments, Government securities including treasury bills and Pakistan Investment Bonds, which shall be final tax as well, and the investments are exclusively made through a Special Rupee Convertible Account maintained with a bank in Pakistan (Clause 5A, Part II of Second Schedule attached to the Income Tax ordinance 2001);

5.2 Deduction of income tax at 20% under Section 152 (2) shall not apply in respect of payments to foreign news agencies, syndicate service and non-resident contributors, who have no permanent establishment in Pakistan. (Clause 41B, Part IV of Second Schedule attached to the Income Tax ordinance 2001);

5.3 The provisions of Section 113 (Minimum Income Tax) and Section 151 (tax deducted at source from profit on debts) shall not apply in respect of receipts from Pak Rupees denominated Government and Corporate securities and redeemable capital, where the investments are made exclusively from foreign exchange remitted into Pakistan through a Special Convertible Rupee Account maintained with a bank in Pakistan. (Clause 19, Part IV of Second Schedule attached to the Income Tax ordinance 2001);

5.4 The non-resident foreigner shall not be required to furnish Income Tax return if his only Pakistan source income is from owns immovable property with a land area of 250 square yards or more or owns any flat / apartment (Section 115 (3) of the Income Tax ordinance 2001);

When the non-resident maintains permanent establishment in Pakistan, then their income will be subjected to income tax applicable to resident taxpayers and may also enjoy deductions subject to some terms and conditions. (Section 101, 105 and 152 of Income Tax Ordinance 2001 and Rules 17 to 19 of Income Tax Rules 2002)

Sales Tax (VAT Mode)

In Pakistan General Sales Tax (GST) is being maintained at VAT Mode as a result input tax paid is recovered against output tax received on supplies and services, and accordingly there will be almost no burden of sales tax on business people as burden of sales tax goes to end consumers who need to pay sales tax without recovery.

In Pakistan sales tax on goods are subjected to sales tax Laws maintained by Federal Government and charge at 17% except in some cases increased / reduced rates are allowed, and sales tax on services are subjected to sales tax Laws maintained by Provincial Government and charge at 16% except in some cases increased or reduced rates are allowed.

Under the Sales tax Laws, foreigners enjoy exemptions, concession and relief as under:

The following goods charged to sales tax at Zero rate. (Section 4 of Sales Tax Act 1990 and Fifth Schedule attached thereto):

Goods exported out of Pakistan;

Supply of goods to diplomats, diplomatic missions, privileged persons and privileged organizations;

Supplies to duty free shops;

Supplies of raw materials, components and goods for further manufacture of goods in the Export Processing Zones;

Supplies of such Pakistani plant and machinery to the export processing Zones and to petroleum and gas sector Exploration and Production companies, their contractors and sub-contractors as may be specified by the Federal Government;

Supplies made to exporters under the Duty and Tax Remission Rules 2001;

Imports or supplies made to Gawadar Special Economic Zones excluding vehicles.

The supply of following goods or import of goods shall be exempt from sales tax. (Section 13 of Sales Tax Act 1990 and Sixth Schedule attached thereto):

Gold and Silver in un-worked condition;

Incinerators of disposal of waste management, motorized sweepers and snow ploughs;

Goods imported by various agencies of the United Nations, diplomats, diplomatic missions, privileged persons and privileged organizations;

Import of articles of household and personal effects including vehicles and also the goods for donation to projects established in Pakistan, imported by any Rulers of Gulf Shaikhdoms who is in possession of residential accommodation in Pakistan and goods including vehicles by the United Arab Emirates dignitaries for their personal use and for donation to welfare projects established in Pakistan;

Educational, scientific and cultural material imported from a country signatory to UNESCO Agreement or a country signatory to bilateral commodity exchange agreement with Pakistan;

Personal wearing apparel and bonafide baggage imported by overseas Pakistanis and tourists;

Goods and services purchased by non-resident entrepreneurs and in trade fairs and exhibitions subject to reciprocity;

Supplies made by cottage industry and retailers whose annual turnover from supplies, whether taxable or otherwise, made in any tax period during the last twelve months ending any tax period does not exceed rupees five million;

Supply of fixed assets against which input tax adjustment is not available;

Foodstuff and other eatables prepared in the flight kitchens and supplied for consumption on-board in local flights;

Agricultural produce of Pakistan, not subjected to any further process of manufacture.

Conclusion

Hassle free systems and procedures and a lot of exemptions, concessions and relief in tax regime in Pakistan encourages foreigners and overseas Pakistanis to invest in Pakistan, which is evidenced by the fact that Direct Foreign Investment (DFI) has shoot up many folds under the present Government as economic indicators are positive. Apart from these advantages, other economic benefits one can avail in Pakistan includes: availability of skilled and cheap labour, high rate of return on investments and savings, relaxed foreign exchange rules, low rate accommodations, cheap food, rich mineral deposits and government extra-care for foreigners etc.

The author is a fellow member of The Institute of Chartered Accountants of Pakistan and has experienced of 25 years in different capacities as Head of Finance & Accounts, Audit Partner, Management and business Consultant, Professional Examiner and contributes in Journals and newspapers.

Addressing Internal Audit Reports

A Balanced Approach

Muhammad Imran, ACA

Debacles an internal audit function faces in volatile environment, probable reactions from audit committee in response to audit report. How a veteran Non-Executive member of the Audit Committee can augment Internal Audit function and ensure its continuity and usefulness

Board of Directors is accountable for overall performance of the company. Code of Corporate Governance requires delegation of core business functions to different committees. Audit committee is entrusted to govern internal audit function of the company and establish internal controls for smooth functioning of business operations and making them free from surprises. In SME's or family owned unlisted enterprises, normally a single active member is performing multiple functions like acting as Chairman, Chief Executive and sole active member of the audit committee because of the absence of non-executive director in audit committee, all reports are addressed to him/her, consequently auditor has to report snags and glitches in functions and business processes to the gentleman who is actually the process owner of those functions/ processes. First of all auditors are reluctant to report such anomalies which place them in head-on position with the CEO, secondly if auditor tries to do so, the bashing response from executive impede him to make second attempt. In such environment, internal audit function remains volatile till composition of the audit committee is reformed.

In comparatively structured business setups which are following guidelines of Code of Corporate Governance by putting non-executive directors. Internal audit department is supposed to follow audit plan and prepare audit reports on different business functions which are submitted to audit committee for their review and actions. This the time when internal auditor and process owners have to face different reactions from audit committee, for empirical analysis these reactions can be categorized into two broad groups which are actually two extreme ends. It doesn't mean that all the reactions of the audit committees can be absolutely positioned on said extreme poles but study shows that most of the companies pass through these phases in their life cycle before attaining maturity.

In first type of response audit committee is acting as report collection and archiving Centre i.e. no active participation in the internal audit function, possible reasons are committee lack capacity to interfere or the other possibility is committee is concern about business operations but committee members feel that auditor and process owners will sort-out the conflicting issues mutually and they will come up with mutual strategy as committee participation will single-out one of the party. Process owners usually blames that auditors are living in ideal world and recommendations are unrealistic, as they are standing away from real world problems. Committee is also unwilling to own any Upcoming fiasco due to following auditor recommendations. On the other hand if committee starts annulling auditors' point of view committee members will be blamed being lacking neutrality. So they prefer to play a role of silent spectator to keep both stakeholders motivated and parallel running of both functions and to safeguard their impartiality without sharing burden of any unforeseen fall back from both stakeholders.

In second type of response committee overreacts on audit points by thinking that they have to take action on each of the audit point and at least one head to be chopped off as a response to each audit report, as either process owners are circumventing internal controls or they are negligent in performance of their duties so the stiff actions against process owner is the only solution for complying with auditor recommendations, this is another extreme end which even sometimes put a sensible auditor in an awkward situation who is actually the owner of those reports i.e. reaction is more than needed. Audit points by nature can be categorized in any of the following:

- Audit points requiring rectifications of mistakes.
- Audit points requiring changes or improvement in business processes.
- Audit points guiding process owners to avoid certain types of mistakes in future.
- Audit points highlighting or identifying frauds or potential areas of frauds.
- Audit points challenging business policies and strategies.
- Audit points highlighting weaknesses in internal controls.
- Audit points highlighting weaknesses in system controls.

So in case of many of the points process owner may not be directly responsible or there may be a shared responsibility in some of the cases, some of the audit points are because of following flawed policies/ processes or due to establish practices or weaknesses in system controls.

So the audit committees taking extreme stances often aggrandize 'Management vs. Auditor' conflicts. These conflicts grow up and cause hurdles in business operations. One of the reasons of extraordinary hype of conflict is that unlike public sector organizations which have many forums like service tribunals, courts to conciliate their grievances or giving them opportunity of being heard, private sector organizations lack this luxury. In such circumstances, audit committee becomes unable to depict visible improvements in business operations. Then BOD has to make their choice which is most of the time is suspension of internal audit function and disbanding audit committee because firing process owners means discontinuation of business operations, which is not an option. Auditor and audit committee becomes a soft target, after some time another team is created and the same story continues.

Now what is supposed to be the rational reaction of the audit committee? A balanced approach to disseminate a very calculated response keeping in view the weight and nature of the audit points, and to further act as mediator between internal audit department and process owners, by making appropriate action plans on auditor recommendations duly supported by a follow up system to ensure compliance to the auditor recommendations in letter and spirit, this is the only solution for business improvement and long continuity of both of the functions i.e. management and internal audit. This problem can largely overcome by introducing seasoned non-executive directors in audit committee. It will help in sorting out internal conflicts so that both stakeholders can strive to conserve their focus on improvements in internal controls, system controls, business processes.

What are the Future Prospects of the Global LNG Industry?

Saeed A. Chughtai

"It is said that something as small as the flutter of butterfly's wings can ultimately cause a typhoon half way across the world[1] " - Chaos Theory. In evaluating any future prospect, this statement becomes all the more important. It is thus more productive to determine the boundaries of our analysis and identify the stakeholders.

LNG is obtained by freezing the Natural gas at temperatures as low as -256° Fahrenheit (-161° Centigrade Approx). The condensation process results in reduction of volume that is almost 600 times smaller than the original gaseous volume[2]. This makes LNG highly portable and capable of being transported over long distances duly addressing the operational issues associated with pipeline transportation. The effective large volume also makes it economically viable. The sellers thus can benefit from supply arbitrage.

Traditionally the LNG business was very straight forward. It essentially involved Long Term contracts, with take or pay clauses between the Buyer and Seller. The supply was executed through dedicated contracted LNG ships[3]. The LNG business has now taken lime light due to geopolitical impediments, security of supply issues, cost of transportation, line losses and inadequate transport system pipelines associated with Natural Gas. In Pakistan the fast depletion of existing reservoirs has prompted consumers / consumption centres to look towards other alternatives like LNG.

Alot of effort and research has gone in, to gauge the future prospects of the industry The LNG business is capital intensive and money has been poured in to enhance the facilities both at the manufacturing and receiving ends. The prices of LNG have been especially volatile since the 2008 International Financial crash[4]. The high gas prices in 2008 fuelled interest of the investors. This in turn led to an evolution in the LNG markets prompting structural changes. A huge influx of investment in LNG projects resulted in under capacity utilization further shadowed in 2014 by relatively depressed oil price owing to US Shale Oil discoveries coming on line. The danger of over supply and resultant dampening of prices exists. New. sites are being discovered, Iraq with the third largest reserves of Natural gas is racing to get its facilities operational. On the other hand Nuclear power generation is now being viewed with contempt after the Fukushima I Nuclear Power Plant disaster in 2011. Japan and Germany are now moving away from Nuclear power to LNG and renewable sources[5]. Future is difficult to predict, but what can be said with certainty is that LNG business has its own set of challenges.

Global LNG Markets

The Global LNG Market can be categorized as under[6].

- The North East Asia (Japan, Korea, Taiwan, etc.)
- Europe (United Kingdom, Spain, France Belgium)
- United States
- Emerging Economies (India, Pakistan, Africa etc)[7]

The North East Asia:

Demand Trends

This market has traditionally been the major market for the LNG industry. The close proximity of the region to the producing regions and lower cost of the product has increased dependence of the regional economies on LNG. The LNG demand of the region can be categorised to be relatively inelastic as compared to other regions.

Major Suppliers

This market has been essentially supplied gas form the suppliers in the Middle East. Some of the demand has also been met from indigenous production.

Pricing Mechanism

Business in this market has essentially been conducted through fixed trading routes under long term contracts. This has been the practice as recent as the beginning of this century, however during 2005 to 2008 demand in USA and Europe increased, the suppliers thus resorted to short term contracts on FOB basis. After 2008, technological advancements and shale Oil & gas discoveries led to USA being a potential major supplier, consequently the long term contracts have seen a revival.

Overview

The region has been the traditional focus of the industry. As the economies of the region tend to mature, the growth in demand also tends to stabilise at the current levels.

Europe

Demand Trends

The economies of the region are quite mature with very stable growth rates. The demand for LNG however originates from the demand and supply gap in the natural gas. Demand centres of the market are in UK, Spain, France and Belgium.

Major Suppliers

The Region has been meeting its requirements primarily through gas imports from Russia and to a certain extent from indigenous production. After having reached oil peak the local Natural Gas production is in the decline, thus prompting a gap between demand and supply. UK has now moved from a net exporter to Net importer of gas. Supplies from Russia have been disrupted without much notice due to disputes over transit tariffs with Ukraine. This has raised serious concern over security of supply.

The Continental Europe almost entirely depends on imported supplies. A portion of which is supplied through pipelines from Algeria. The political upheaval in Ukraine has heightened security of supply concerns in Europe.

Pricing Mechanism

The pricing of LNG is more responsive to the market forces as compared to the North East Asian Market. The region has three trading points with varying degrees of liberalization and liquidity. Efforts are being made by the European Union to model these trading points on the same lines as that of US. A brief description of the three is given below.

a) National Balancing point in UK. This trading point is more structured and closer to the US model (Henry Hub). The pricing mechanism is more responsive to market forces in the price determination. This is essentially because the gas infrastructure in UK is also quite developed.

b) The Zeeburge Market is a virtual trading Hub, structured to some extent on the lines of NBP. However the trading activity on the hub is restricted to the movements through the UK – Belgium interconnector, and accordingly the prices are traded at a premium or discount on the NBP price, depending on the flow of gas to or from UK.

c) The TTF prices on the other hand are highly correlated to the Dutch and Belgian gas pipeline import prices. These prices are based on the long term indexation parameters i.e. the heating oil and residual fuel with a time lag. Most of the times the TTF prices would be linked to the prices in NBP – Zeeburge, however in period of extraordinary Demand and Supply variation / disassociation may occur.

Overview

A lot of infra structure development work has been carried out in Europe .New terminals have been commissioned and storage capacity is being enhanced. All this development work has been carried out inspite of the fact that capacity utilization in main land Europe has not exceeded 60 %. In UK however it has been almost 70 %.

United States

Demand Trends

After having attained oil peak, the US has moved to develop its Shale Oil and Shale gas production. The technological advancements, particularly by USA has helped it bridge the supply demand gap, inspite of the large size of the US economy. It is has been estimated that US would emerge as a major exporter of LNG.

Major Suppliers

New discoveries have been made in the West Pacific and a major portion of the US demand is being met by these nations. (Tobago, Trinidad). A reasonable portion of the US LNG needs were traditionally met from the Middle East imports. Previously supplies to US were also made from Northern Africa, however there is a change of focus and most of the supplies from North Africa have been directed towards Europe.

Pricing Mechanism

The Henry Hub in USA is the most advanced and developed trading hub for LNG . The prices are essentially determined by the interaction of market forces and gas to gas competition. The US also has a futures market dealing with LNG situated at Louisiana called "Henry Hub". This adds depth and liquidity to the US market.

Overview

In 2010 the US was expected to account for 50 % of the global LNG market. In USA the major uses of LNG can be categorized into three:

1) Power Generation
2) Industrial consumption and
3) Private Domestic Consumption.

The US has had the most developed and extensive infrastructure and industry. There are a number of players operating at each point of the LNG supply chain. A lot of infra structure development work has also been carried out in USA. Almost 4000 KM of LNG pipelines have been laid. Three new LNG terminals have been established and storage capacity increased. All this development work has been carried out inspite of the fact that capacity utilization in USA has not been more than 40%. The Shale Oil & Gas potential has now made USA a potential major supplier.

Emerging Economies

Demand Trends

The emerging economies have high economic growth rates along with large population. The need for energy in these economies is great, and shall be increasing at a very fast pace.

Major Suppliers

The major suppliers to the market is essentially the middle east. However new discoveries are being made in these emerging economies and an increasing respectable portion of the demand is being met through indigenous sources.

Pricing Mechanism

At the present the pricing mechanism in this market segment is more reflective of trends, witnessed in other markets, essentially in East Asia.

Overview

The influence of this market, at the moment, is not significant, however things would change as these economies develop.

Analysis of the Interdependencies and Evalution in the Global Market

a) Market Players:

The LNG business has undergone massive changes over the years. As late as the beginning of this centaury the business was mainly focussed on North East Asian Markets, comprising Japan, Korea(s) Taiwan. The supplies mainly originated from the Middle East.

The European and US markets are now becoming a player in the industry primarily because in case of Europe the indigenous production of oil fuels and natural gas has been declining, while in case of USA technological advancements has made it less reliant on imports. There is a widening gap between demand and supply, shifting of roles. Europe in addition has supply security issues due to uncertainty and mismanagement on natural gas from Russia.

The price of LNG has been quite low as compared to the oil fuel and thus the emerging economies are more encouraged to look towards the LNG for meeting there needs for energy.

b) Pricing Mechanism:

The increased demand of LNG has induced refinement in the pricing mechanism. LNG Futures are now being traded adding depth and liquidity to the market. These developments are essentially taking place in the US and European market.

The North Eastern Asian market has also had to react to the developments in the other markets. Prices in this market are now reverting back to long term contracts from the short stint of short term contracts and on FOB basis.

c) LNG Prices:

The Prices of LNG have increased by almost 60%, since 2000. Recently the prices have dropped, but they still remain higher than the 2005 mark.

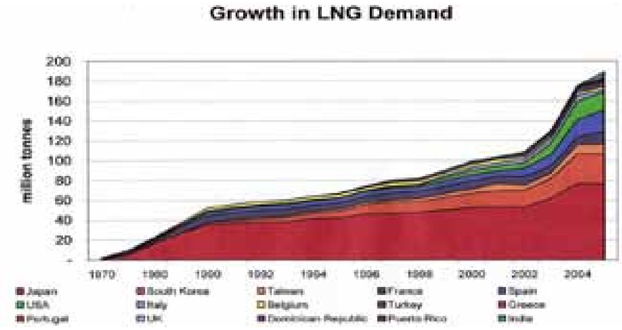
Oil to Natural Gas Ratio Drops to Three and a Half Year Low – Bespoke February 20, 2014

d) Investments in LNG:

The widening gap between demand and supply and the resultant increase in prices have prompted the Middle

Eastern and the Western Pacific Nations to invest heavily in the exploitation of resources and improving infrastructure for export of gas. The European and US in turn have also improved there infrastructure and continue to invest in it.

Expert Reviews for the Future



Culled from Foss, M., Introduction to LNG, Centre for Energy Economics, January 2006

Triangulation and Critical Review

The importance of the LNG business cannot be overlooked. It is an emerging industry. A lot of investment has been made in the support infrastructure.

Analytical Review of the LNG Industry

NEW DISCOVERIES
(Specially in Emerging Economies)
- Iraq
- Venezuela
- Brazil
- Kazakhstan
- USA – Shale Oil & Gas

THE SUPPLIERS
- LNG Terminals
- Pipelines
- LNG Cargo Ships
- Regasifications Plants
- Plant Manufacturing facilities
- E & P Companies

THE INDUSTRY
- Middle East & Africa (Qatar, Algeria, Egypt)
- Iran
- East Pacific Nations
- North Sea
- Indigenous Local Production

THE BUYERS
- Europe
- East Asia
- China & India
- Emerging Economies

(Electricity, Oil Refining, Industrial, & Residential)

THE COMPETITORS
- Russia & North Europe Pipeline N Gas supplies
- Nuclear Power
- Alternative / Renewable Energy

- International Environmental Conventions.
- US Energy Policy`

Future Prospects

The LNG is an emerging industry. Trading in this commodity is increasingly been structured and organised to make it responsive to market forces. Inspite of increase in its price it has remained very competitive to the oil prices.

However efforts are being made to tap the reservoirs of Iraq. Brazil and Venezuela are investing in the development of there infrastructures.

The electricity production is the major user of the LNG, particularly accounting for almost 50 % of the demand. The recent US initiative to encourage use of nuclear power for electricity may cast a shadow on the LNG demand.

Conclusion

It is difficult to conclude and make a prediction, but it can be said that LNG industry inspite of the challenges ahead of it would be a force to reckon with. The Short term prospects remain bright.

Current Review

After having established the mechanism and dynamics we shall evaluate the industry by using the analytical tools suggested by Micheal Porter. The figure above is the grouping of the industry in respective arenas.

Previously higher prices of the LNG business were witnessed due to the weaker bargaining position of the buyers. This has now reversed due to potential over supply in the Market.

There has been some restriction to the entry of new competitors to the industry. The war in Iraq, underdeveloped infrastructure in Brazil & Venezuela and inaccessibility to the market by Kazakhstan has been the barriers to entry.

The erratic pipeline supplies by Russia and lacking management has only manifested in the weakness on part of the competitors.

The costs of renewable energy sources and environmental concerns on Nuclear power have also contributed to the weakness in competition.

In the medium term there is a danger of over supply, but there is a strong possibility that the demand and supply gap would persist.

1. Gleick J, (1987). Chaos : Making a new Sciences, Newyork; Viking
2. See Foss, M., Energy Economic Research at the Bureau of Economic Geology, ' INTRODUCTION TO LNG', January 2007 pp. 7-8. At http://www.naturalgas.org/lng/lng.asp (Last visited March 1, 2010)
3. An Industry view- Challenges for project financing LNG, Project Finance International Yearbook, 2002. p. 32
4. Kimberly Amadeo, How Crude Oil Prices Affect Gas Prices, About.com – US Economy. 2014
5. EIA Report, Natural Gas Review 2011 , April 2012
6. Cris Holmes, World LNG, Oil & Gas Journal, April 9, 2007
7. EIA Report, Natural Gas Review 2008 , April 2009

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2014-15

Keep FBR People Away and See the Miracle

Zeeshan Aslam
FCA, FCCA, CIA, FPA

Budget is to be presented in June but the question remains there "is it the only budget presented and thereafter government will not change taxes?" The answer is no there will be changes to the electricity prices, fuel prices, gas prices, grocery and moreover government will have to change certain budget measures based on pressure group and ultimately the looser will be the poor and lower middle class families who cannot cope up with the inflationary pressures and they are subject to indirect and direct taxes, who will prepare their house budget? Or should we keep them vulnerable to irrational tax measures, that may resulted in suicides of the families, corruption and increased crime rates.

Other question, are businessmen afraid to pay taxes and the answer from most is no infect they want to pay taxes but they are afraid of FBR people and they may be in trouble if they declare their taxes correctly since and ultimately they have to settle cases through corrupt practices.

Why not make things simple, there shouldn't be any relief to any person, industry and all should be taxed but the main success factor is to keep "FBR PEOPLE AWAY FROM DIRECT CONTACT WITH TAX PAYERS". So I may suggest as follows:

1. Reduce indirect tax rate and it should be levied on all sectors and products (however export related sectors may be kept zero).
2. Any amount deposited in business accounts of companies, AOPs, business individuals shall be subject to 2% withholding and bank should be deposited by bank in the FBR and the tax so withheld shall be minimum tax.
3. The Chartered Accountants firms (other than auditor of the companies) should compute and certify that calculations are accurate along with the tax return of these individuals. All of the chartered accountant firms quality should be reviewed by ICAP to make sure that they certified correctly.
4. The withholding by companies under various sections including 153 and others should be abolished and let these companies do their business and banks at the time of deposit as mentioned before should withheld and deposit.
5. Retailers should be given special cash machines/soft wares linked with FBR computers in order to record and issue receipt and daily collections should be deposited in their bank accounts and at that time they should also be subject, as explained before, to withholding tax by bank of 2%. The retailers who will not implement FBR soft wares, should be subject to total audit without any distinction and extra tax may be levied.
6. Banks should obtain certificate from their clients about source of their income and if not given than their accounts should be blocked. Also banks should be asked to make it mandatory that each year their clients should submit their returns by December and if not submitted than they may block customer accounts. Also banks should be audited by chartered accountants firms (other than their auditors) to give certificate and effective implementation of this measure.

If we rationalize our system and have professional people in FBR and good governance may improve the system without difficulty.

The Effects of Human Resource Practices on Firm Growth

Donald Bowen

Although the connection between firm growth and labour is well documented in economics literature, only recently the link between human resources (HR) and firm growth has attracted the interest of researchers. This study aims to assess the extent, if any, to which, specific HR practices may contribute to firm growth. We review a rich literature on the links between firm performance and the following HR practices: (1) job security (2) selective hiring, (3) self-managed teams (4) compensation policy, (5) extensive training, and (6) information sharing. We surveyed HR managers and recorded their perceptions about the links between HR practices and firm growth. Results demonstrated that compensation policy was the strongest predictor of sales growth. Results provide overall support for all HR practices except of job security. Eventually, selecting, training, and rewarding employees as well as giving them the power to decide for the benefit of their firm, contribute significantly to firm growth.

Introduction

The extent to which, if any, human resource management (HRM) impacts on organizational performance has emerged as the central research question in the personnel/HRM field. Although this indicate that some human resources practices may have a positive effect on organizational performance, most scholars suggest that more conceptual and empirical work is required. For the moment, although Human resources (HR) are considered as the most valuable asset in an organization, they make a difference only for a few organisations. The link between human resources (HR) and firm growth is well documented in classic economic theory. Overwhelming evidence suggests growth is driven by specialization and division of labour in the processes of generation and attraction/development of technological opportunities. However, at the firm level of analysis, only recently the link between human capital and growth has attracted the interest of researchers.

Firm growth is often seen as an indication of market acceptance and firm success. Growth is considered as a top strategic priority for most firms yet only few companies achieve growth and ever fewer in maintaining in. Assuming, that firm growth involves more purposeful work and strategic decision making than leaving it to random and chance events, the present study addresses: How do human resource management practices contribute to firm growth?

A growing body of empirical research has examined the effect of certain HRM practices on firm performance. Although there is a long list of best HR practices that can affect either independently or collectively on the organizational performance, results are hard to interpret. In order to determine any effects of HR practices on firm growth, we choose to examine HR practices initially proposed by Pfeffer (1998) which according to the literature, can be expected to influence the firm performance. In his seminal work, Pfeffer (1998) proposed the following seven HRM practices: (1) employment security (2) selective hiring, (3) self-managed teams and decentralization of decision making (4) comparatively high compensation contingent on organizational performance, (5) extensive training, (6) reduced status distinctions and barriers, including dress, language, office arrangements, and wage differences across levels, and (7) extensive sharing of financial and performance information throughout the organization. The following sections will develop hypotheses concerning the relationship between HRM practices and firm growth.

Compensation Policy

Performance-based compensation is the dominant HR practice that firms use to evaluate and reward employees' efforts. Evidently, performance-based compensation has a positive effect upon employee and organizational performance. However, there is scarce evidence on the effects of compensation policy of firm growth. Empirical studies on the relationship between performance-related pay and company performance have generally found a positive relationship, but a growing body of empirical evidence suggests that it is not just pay level that matters, but pay structure as well. Barringer et al. (2005) conducted a quantitative content analysis of the narrative descriptions of 50 rapid-growth firms and a comparison group of 50 slow-growth companies. Results demonstrated that employee incentives differentiated the rapid-growth from the slow-growth firms. Firms that were eager to achieve rapid-growth provided their employees financial incentives and stock options as part of their compensation packages. In doing so, firms managed to elicit high levels of performance from employees, provide employees the feeling that they have an ownership interest in the firm, attract and retain high-quality employees, and shift a portion of a firm's business risk to the employees. Performance-based compensation is the single strongest predictor of firm performance. Both performance-based compensation and merit-based promotion can be viewed as ingredients in organizational incentive systems that encourage individual performance and retention. Employee turnover can significantly slow revenue growth, particularly in knowledge-intensive industries (Baron and Hannan, 2002). Given that much of the tacit knowledge resides within employees, significant turnover poses a threat to firm performance and its future growth potential. With high turnover rates, firm growth flees away along with leaving managers who often become employers of rival firms or establish themselves rival firms.

Therefore, we propose this hypothesis:
Hypothesis 1: Compensation Policy is positively related to firm growth

Decentralization & Self-managed teams

More and more, employees are required to work in teams, make joint decisions, and undertake common initiatives in order to meet the objectives of their team and organization. Self-managed teams can affect firm growth in two ways: Firstly, a surplus of junior managers in a firm may create and support dynamics of firm growth. The growth stage is perhaps the most dynamic stage of a firm's life cycle. As the business expands, new levels of management are added. Decision-making becomes more decentralized, middle managers gain authority and self-managed teams proliferate as the firm adds more and more projects and customers.

Secondly, teamwork and decentralization of decision making promotes employee commitment participation and create a sense of attachment, thus indirectly affecting firm performance. Several studies identified self-managed teams and decentralization as important high-performance HRM practices (Pfeffer, 1998; Wagner, 1994; Yeatts and Hyten, 1998; Singer and Duvall, 2000). Decentralised teams have a positive effect on two dimensions of the performance, time and flexibility. The role of human resource practices in creating organizational competitive advantage and found that top management team social networks (practices such as mentoring, incentives, etc.) mediated the relationship between HR practices and firm performance.

Firms with large teams performed better and firms with dominant CEOs performed worse in a turbulent environment than in a stable one. A company with micro level of centralisation is a receptive environment for self-managed teams. In a study of differential outcomes of team structures for workers, supervisors, and middle managers in a large unionized telecommunications company, Batt (2004) found that participation in self-managed teams is associated with significantly higher levels of employment security, and satisfaction for workers and the opposite for supervisors.

Therefore, we propose this hypothesis:
Hypothesis 2: Decentralisation is positively related to firm growth.

Information Sharing

Sharing of information may have a dual effect: Firstly, it conveys employees the right meaning that the company trusts them. Secondly, in order to make informed decision, employees should have access to critical information. Communicating performance data on a routine basis throughout the year help employees to improve and develop. Employees presumably want to be good at their jobs, but if they never receive any performance feedback, they may perceive to have a satisfactory performance when in fact they do not. Furthermore, information sharing fosters organizational transparency which reduces turnover and forges synergistic working relationship among employees.

Information sharing is not a widespread HR practice as someone might have expected it to be. Many companies are vulnerable to share critical information with their employees because in this way employees become more powerful and companies may loose control of them (Pfeffer, 1998). Furthermore, information sharing always involves the danger of leaking important information to competitors. In a study of Fortune 1,000 largest manufacturing and service companies on high performance practices, Lawler et al. (1995) found information sharing to correlate to firm performance but results are inconclusive.

Therefore, we propose this hypothesis:
Hypothesis 3: Sharing of information is positively related to firm growth.

Selective Hiring

This practice can ensure that the right people, with the desirable characteristics and knowledge, are in the right place, so that they fit in the culture and the climate of the organization. Moreover, pinpointing the rights employees would decrease the cost of employees' education and development. Selective hiring is a key practice that creates profits. HR practices of high performance companies found that attracting and selecting the right employees increase the employee productivity, boost organizational performance, and contribute in reducing turnover. Hiring standards reflect not only organizations' skill requirements but also the preferences of various groups for such standards and their ability to enforce these preferences. An effective hiring process ensures the presence of employees with the right qualifications, leading to production of quality products and consequently in increase of economic performance. Cardon and Stevens (2004) pointed out that for small companies recruiting is often problematic. This can be due to several reasons such as limited financial and material resources and jobs with unclear boundaries responsibilities, which decreases their potential to hire qualified candidates.

Therefore, we propose this hypothesis:
Hypothesis 4: Selective hiring is positively related to firm growth.

Training and Development

Training and development may be related to firm performance in many ways. Firstly, training programmes increase the firm specificity of employee skills, which, it turn, increases employee productivity and reduces job dissatisfaction that results in employee turnover. Secondly, training and developing internal personnel reduces the cost and risk of selecting, hiring, and internalising people from external labour markets, which again increases employee productivity and reduces turnover. Training and development like job security requires a certain degree of reciprocity: A company that train and develop systematically its employees advocates them that their market value develops more favourably than in other firms. This increases employees' productivity, commitment, and lowers turnover. Companies may also assist their employees in career planning. In doing so, companies encourage employees to take more responsibility for their own development, including the development of skills viewed as significant in the company. Barringer et al. (2005) compared rapid-growth and slow-growth firms and found that rapid-growth firms depend heavily on the abilities and efforts of their employees to maintain their growth-oriented strategies. The fast-growth firms used training programs to achieve their objectives and emphasized employee development to a significantly greater extent than their slow-growth counterparts. Therefore, training and employee development practices are more common in rapid-growth firms than slow growth ones. Michie and Quinn (2001) investigated the relationships between UK firms' use of flexible work practices and corporate performance and suggested that low levels of training are negatively correlated with corporate performance.

Therefore, we propose this hypothesis:
Hypothesis 5: The extent of training and development will be positively related to firm growth.

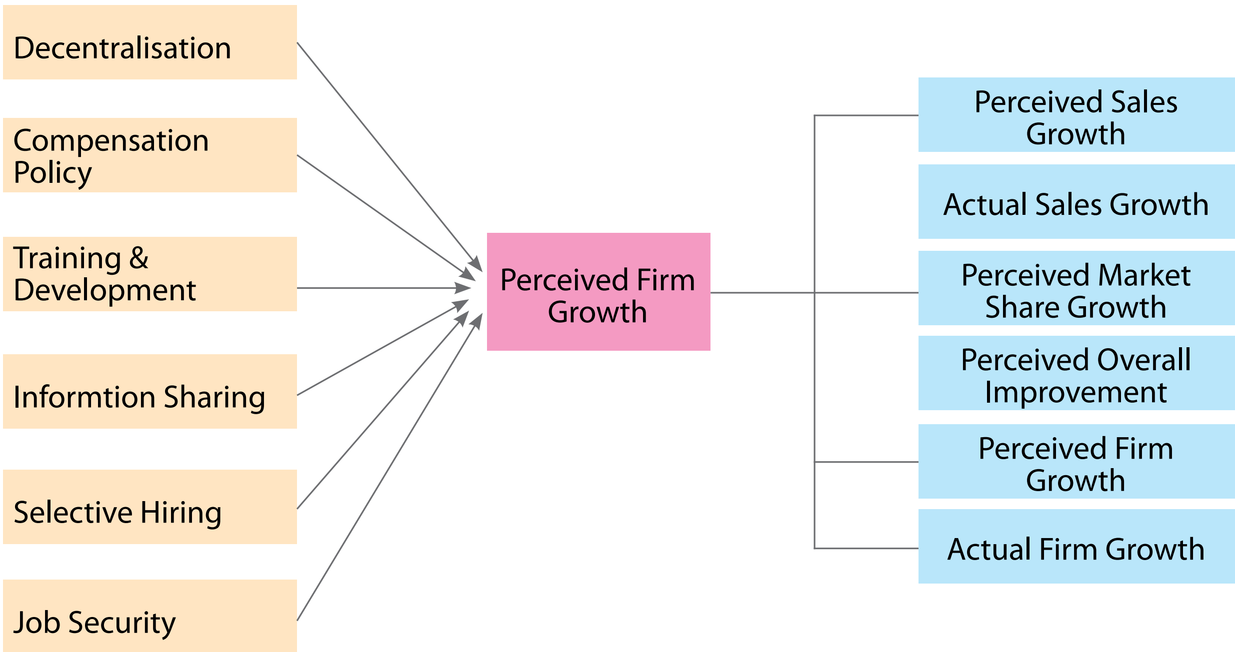
Job Security

Job security creates a climate of confidence among employees which cultivates their commitment on the company's workforce. Job security requires a certain degree of reciprocity: firstly, a company must signal a clear message that jobs are secure; then, employees believing that this is true, feel confident and commit themselves to expend extra effort for the company's benefit; finally, a company that have learnt that job security contributes to its performance, invests again in job security (Pfeffer, 1998). A conceptual model of the antecedents and consequences of job security was taken. Antecedents include worker characteristics, job characteristics, organizational change and job technology change. Consequences include psychological health, physical health, organizational withdrawal, unionisation activity, organizational commitment and job stress.

When companies do provide job security, then empirical evidence suggests that it has a positive effect on to firm performance. Following that job security impacts operational performance indirectly through organizational commitment. Kraimera et al. (2005) used psychological contract and social cognition theories to explore the role of full-time employees' perceived job security in explaining their reactions to the use of temporary workers by using a sample of 149 full-time employees who worked with temporaries. Results demonstrated that employees' perceived job security negatively related to their perceptions that temporaries pose a threat to their jobs. On the one hand, for those with high job security, there was a positive relationship between benefit perceptions and performance. On the other hand, for those with low job security, there was a negative relationship between threat perceptions and performance.

Therefore, we propose this hypothesis:
Hypothesis 6: The presence of job security is positively related to firm growth.

Figure 1 illustrates the associations between these hypotheses and relevant constructs.



METHOD

The sampling procedure and sample

While Figure 1 is a model of the firm performance, we choose to examine it as understood by the individuals who take decisions about firm performance. In doing so, we operationalize and measure individuals' perceptions of the model's variables in their work situations. In order to develop robust model linking HR practices and firm performance, we drew our sample from food companies operating in Greece for a minimum of five years. We included companies from the food processing and trading sub-sectors, excluding hospitality and retailing. In doing so, we aimed to increase the homogeneity of our population as we as decrease the necessary sample size to achieve robust validity of data analyses.

Testing the research hypotheses in a specific sector adds to the validity of the research design because managerial skills are to a large extent industry-specific. Furthermore, food industry is dealing with subsequent food crises and human resources are considered as a valuable asset to survive and maintain competitive advantage. In-depth interviews were conducted with key decision makers prior to designing a pre-test. The questionnaire was pre-tested with randomly selected firms. Based on the results of the pre-test instrument, the final questionnaire was refined. The respondents were mainly HR managers or, in same instances, the managing directors (MD) of the food firms.

In terms of the empirical research, we posted 372 questionnaires. We got 71 questionnaires, most of them answered by HR Managers (95%). We chose to include both HR and MD responses in the sample size although we recognize that there would be different perceptions about HR practices and organizational performance. The total response rate was 19.1%. To ensure that the respondents were comparable to non-respondents, analyses of variances were conducted between these groups. We also found no significant differences between HR managers and managing directors.

Statistical Analysis

SPSS v.10 on Windows XP was utilized for all analyses. We first had to reduce a large number of variables to a smaller set of components. Principal component analysis is a preferred method for this kind of study. We, then, used hierarchical regression in order to assess the effect of relation, if any, between HR practices and firm growth measures.

Principal component analysis with varimax rotation was conducted to assess the underlying structure for the nineteen HR practices questionnaire. Principal component analysis (PCA) involves a mathematical procedure that transforms a number of (possibly) correlated variables into a (smaller) number of uncorrelated variables called principal components. The first principal component accounts for as much of the variability in the data as possible, and each succeeding component accounts for as much of the remaining variability as possible. PCA helps with the latter. Having too many features often results in the problem having too many degrees of freedom leading to poor statistical coverage and thus poor generalization. The Varimax rotation is an orthogonal rotation applied to a truncated set of principal components. Its application is an attempt to obtain modes that are simple to interpret. Hierarchical regression models are well suited for this type of analysis. In hierarchical regression, the order of predictor entry, whether individual or in blocks, makes a difference in the results and conclusions. This allows examining the 'effects' of specific independent variables over and above one or more dependant variables.

Firm Growth

Respondents were asked to indicate their firm's growth as compared to the industry's average in these areas: perceived sales growth, perceived market share growth, perceived overall improvement and perceived firm growth. For perceived items, a 5-point scale ranging from bad (1) to very good (5) was used. Furthermore, we calculated actual sales growth, and actual firm growth based on the last 3- year firm performance. We calculated firm growth using sales and employee figures. Although we believe the perceived firm growth measures are appropriate, they have some limitations which should be discussed.

The first is that they are self-reported responses from HR managers, who may have a stake in seeing positive relationships between their decisions about personnel recruitment, training, development and compensation with achievement of firm's objectives.

Secondly, as in all self-reported studies, the possibility of common method variance should be addressed. When both the outcome measure (i.e. firm growth) and the six predictor variables (i.e. compensation policy, decentralisation), are self-reported on the same survey instrument, both measures share common methods variance. There are several techniques that can be used to minimise common method variance.

Third, management perceptions about concepts like firm growth and organisational performance may actually be more valid indicators than objective data such as profitability, market share and sales, since actual figures are directly related to a vast number of variables, such as trends in the economy, industry factors, and other environmental factors. Therefore, self-reported measures may, in some cases, represent more accurate descriptions than more objective measures. In the present study, since we are interested in the direction of causation between HR practices and firm effectiveness, the only people with the breadth and depth of knowledge to report adequately about these concepts are the HR managers or managing directors.

Finally, since we were interested in assessing the separate factors of a successful collaboration, we were limited in the number of objective measures that were available within the scope of this study. Because of the previously stated arguments, we concluded that the expert opinions of HR managers or managing directors would be valid and appropriate for this study. The results of data analysis should be acceptable if adequate controls are reported for the data.

DISCUSSION

The primary purpose of this study was to evaluate the impact of HR practices on firm growth. In summary, a review of existing literature finds that there are HR practices positively linked to organizational performance. Based on a comprehensive literature review, we hypothesised that the following HR practices are related to firm growth: (1) Compensation policy, (2) Decentralization & self-managed teams, (3) Information Sharing (4) Selective Hiring, (5) Training and Development and (6) Job Security. However, a review of literature pertaining to organizational performance shows that firm growth, an indication of market acceptance and firm success as well as a top priority of most companies, has been studied mostly as a latent variable of organisational performance.

Consequently, this paper argues that the selection of specific HR practices becomes a strategic decision. Therefore, HR managers should be able to report on the concrete results of specific HR practices on specific firm growth measures. Briefly, HR practices are linked to firm growth. The findings of the study lead to a number of interesting implications for HRM theorists and practitioners. The first (and rather obvious) implication can be derived from the evidence found that all HR practices are related to firm growth, a finding consistent with a variety of extant theories and studies,. Hence, firm growth as a strategic priority depends on human capital: selecting, developing, and rewarding the best people as well as revealing to them critical company information in order to make informed decisions which they are authorised to take.

Compensation policy was related to all perceived firm growth measures, being the strongest predictor of sales growth and the weakest of firm growth. Linking sales with compensation benefits can be an explanation of the high correlation between compensation policy and sales growth. Decentralisation and team working was significant factor of firm growth. Training and development was related to all firm growth measures but it showed higher correlation to overall firm performance improvement.

Information sharing has the inherent vulnerability that informed employees will become more powerful and companies may loose control of them. Even worse, information sharing involves the danger of leaking important information to competitors. On the other hand, information sharing tells employees that the company trusts them and thus gives them sensitive information to make informed decisions which will shape the future of the company. The findings demonstrate that information sharing does positively relate to firm growth. Information sharing was significantly correlated to sales growth, firm growth, and overall firm performance improvement. Respondents did not perceive that job security was an important HR practice. This finding can be attributed to the fact that most respondents were HR managers who might be reluctant to report an insecure job environment in their company's workplace. The findings as a whole suggest that a positive relationship exists between the extent to which companies implement HR practices and firm growth achievements. This overall result corroborates previous empirical studies on the links between HRM and firm performance. These findings provide tentative support of the contention that HR practices can create a competitive advantage.

Future research could clarify the causal relationship between HR practices and firm performance. Another research stream is examining HR practices in sets in order to assess their collective effect. The conceptual basis of further research can be extended. An interesting avenue for future research is the market-based competitive advantage approach, which declares that the market determines who is competitive or not. The market-based approach can provide another theoretical basis than resource-based view of competitive advantage, in order to examine the effect of HR practices on firm performance.

A series of limitations bounds the findings, conclusions, and implications of this study. The most obvious limitations of this study stem from the sample used and the measures employed. We examined a small set of HR practices that seem to have an effect on firm growth in Greek food industry. This study focused on established firms with more than 5 years of operation. However, the stage of a firm's lifecycle, either growth, mature, decline or revival stage can be an important factor in applying specific HR practices. Another limitation of the findings is the use of self-report questionnaires to collect data on all measures. This limits our ability to draw conclusions about the causal nature of the relationships between HR practices and firm growth. In a future study there would be of great value to see how different HR and MD responses are. These limitations suggest that the interpretation of research findings need to be cautious they also indicate a number of potentially fruitfully avenues for future research. Except from testing the research hypotheses in other settings and environments, the combined effect of HR practices, and which practice works better with another one is yet another open question. A large quantitative survey could also control for mediating and/or moderating variables between human resource management and firm performance.

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Professional Skepticism

Striking the Right Balance

Ayesha Arif, ACA

Global economies continue to experience a prolonged period of economic uncertainties and with that comes associated challenges for firms and participants in capital markets. The public places value on the independent financial statement audit because it enhances the degree of confidence of intended users in the financial statements. A high-quality audit features the exercise of professional judgment by the auditor and, importantly, a mindset that includes professional skepticism throughout the planning and performance of the audit. Against this backdrop, the value of an independent audit is heightened as it enhances the degree of user confidence in financial reports.

Many entities today face difficult economic conditions that give rise to financial reporting challenges such as the assessment of going concern, the determination of fair values and the choice of approach to accounting estimates. Furthermore, today's financial reporting requirements seek to address information that is ever more relevant to users. As a result of this challenging environment, more judgment and increased subjectivity is involved in management's accounting and reporting decisions. These developments highlight the importance of auditors exhibiting a skeptical mindset, especially in areas of financial reporting that are complex or involve estimation. Of course professional skepticism has become a topic du jour within the auditing profession in recent years. International Standard on Auditing (ISAs) define professional skepticism as "an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence". The Auditing Standards explicitly require the auditor to plan and perform an audit with professional skepticism recognizing that circumstances may exist that causes the financial report to be materially misstated. Professional skepticism is fundamentally a mindset. A skeptical mindset drives auditor behavior to adopt a questioning approach when considering information and in forming conclusions. In this regard, professional skepticism is inseparably linked to the fundamental ethical principles of objectivity and auditor independence.

Professional skepticism is a characteristic of a high quality audit and is closely related to professional judgment. Professional skepticism is an inescapable element in the exercise of professional judgment. The continuous application of the critical thinking process results in the application of professional skepticism. Professional skepticism is the hallmark of a good auditor and, when auditors combine awareness of traps and biases with professional skepticism, it elevates the quality of the professional judgments. Professional skepticism also includes a critical assessment of audit evidence, which comprises both information that supports and corroborates management's assertions, and any information that contradicts such assertions. Applying professional skepticism in this regard means questioning and considering the sufficiency and appropriateness of audit evidence obtained in the light of the circumstances.

The application of an appropriate degree of professional skepticism is a crucial skill for auditors. Unless auditors are prepared to challenge management's assertions they will not act as a deterrence to fraud nor be able to confirm, with confidence, that a company's financial statements give a true and fair view. The need for professional skepticism in an audit cannot be overemphasized. Skepticism is an essential attitude that enhances the auditor's ability to exercise professional judgment in identifying and responding to conditions that may indicate possible misstatement. Professional skepticism includes a critical assessment of audit evidence. It also means remaining alert for evidence that contradicts other audit evidence or that brings into question the reliability of information obtained from management and those charged with governance. The consistent application of professional skepticism is imperative for auditors to draw appropriate conclusions in the conduct of their work.

However, skepticism can be taken too far; challenging everything in a well-run company will slow down the publication of its financial statements and risk unnecessary costs. The definition of professional skepticism suggests that skepticism influences the scope of the work, helps the auditor evaluate audit findings and ultimately conclude whether sufficient appropriate audit evidence has been obtained to enable a 'true and fair view' opinion to be expressed on an entity's financial statements. It is widely acknowledged that a skeptical attitude of mind is essential if an audit is to be rigorous and performed with due professional care; however, auditing literature is less forthcoming about the degree of skepticism to be applied in practice. The degree of skepticism to be applied is important because it influences both the effectiveness and the efficiency of an audit. Too little skepticism endangers audit effectiveness; too much risks unnecessary cost. Achieving the right balance is vital. While the auditor cannot be expected to disregard past experience with management and those charged with governance, a belief that they are honest and have integrity does not relieve the auditor of the need to maintain professional skepticism or be satisfied with less than persuasive audit evidence when obtaining reasonable assurance. Unless audit inquiries are to be pursued without regard to cost or time, in practice there must be a limit on the degree to which auditors inquire about particular issues and the extent of audit procedures performed. This thinking probably underlies the famous judicial view that an auditor should be 'a watchdog not a bloodhound'.

Initially, auditors approach an audit without a strong predisposition to believe that either the financial information is misstated or that management is other than honest and candid. Through the process of gathering audit evidence, auditors may obtain information that suggests that the financial information could be misstated. In this situation auditors become more intense in their enquiries and seek to obtain more audit evidence to resolve issues, especially if they develop concerns about the veracity of the evidence or the integrity of those providing it. To understand the practical application of skepticism it may therefore be helpful to view it as being applied by auditors on a 'sliding scale' where the intensity of their scrutiny and challenge reflects both the auditor's initial mindset and their response to audit findings. Professional skepticism is applied largely by being alert. For example, being alert to audit evidence that contradicts other audit evidence obtained; or to information that brings into question the reliability of documents or responses to enquiries to be used as audit evidence. Further, it includes being alert to conditions that may indicate possible error or fraud, and to circumstances that suggest the need for audit procedures in addition to those required by the Auditing Standards.

When considering the auditor's initial mindset a distinction can be made between a neutral position (where the auditor does not assume either that the financial statements are misstated or that management is dishonest) and a more questioning approach that is sometimes referred to as 'presumptive doubt'. The auditor may accept records and documents as genuine unless the auditor has reason to believe the contrary. Nevertheless, the auditor is required to consider the reliability of information to be used as audit evidence.

What professional skepticism means in terms of the initial mindset that the auditor should have in undertaking an engagement? Contrast can be drawn between a "neutral" mindset, in which the auditor neither accepts management figures and explanations in an unquestioning way nor assumes that there is error or misstatement, and "presumptive doubt" where the auditor exhibits a heightened awareness of the risk that the figures could be affected by error or dishonesty. Auditors have sometimes been criticized for not applying sufficient professional skepticism, implying that more doubt would have led auditors to have investigated further or look for more persuasive evidence and to have avoided alleged failures as a result. However, greater doubt is not unambiguously a good thing as it may lead to unnecessary procedures, over-auditing and inefficiency. Recognizing that the initial mindset is largely a personal attribute, questions arise about whether all individuals are likely to have the same attitude of mind and, if not, what causes differences? Academics have identified a number of character traits that underlie auditor skepticism, including:

- Curiosity / having a questioning mind,
- Deferral of judgment / not jumping to premature conclusions,
- Understanding management behavior and motivations,
- Self-confidence, and
- Freedom of action.

Having said that the auditor cannot be expected to disregard past experience of the honesty and integrity of the entity's management and those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the auditor of the need to maintain professional skepticism or allow the auditor to be satisfied with less than persuasive audit evidence when obtaining reasonable assurance. Two particular areas that are likely to be relevant to the development and promotion of auditor skepticism are (a) recruitment, training and motivation / reward processes and (b) audit methodologies. Though it is not yet been concluded whether professional skepticism is an acquired skill or are largely innate, nevertheless, audit firms have acknowledged its importance and investing in the right people and developing the right processes to drive quality, through nurturing appropriate skeptical behavior through training. Further audit firms are responding by making their audit methodology more robust and responsive to growing concerns over recent years including development in auditing standards and regulatory arena. International Standards on Auditing (ISAs) explicitly recognize the fundamental importance of professional skepticism. Nevertheless, adopting and applying a skeptical mindset is ultimately a personal and professional responsibility to be embraced by every auditor. It is an integral part of the auditor's skill set and is closely interrelated to the fundamental concepts of auditor independence and professional judgment and contributes to audit quality. Professional skepticism facilitates the proper exercise of professional judgment in audit decisions such as audit strategies and detailed plans, the assessment of evidence, the evaluation of management's judgments and forming conclusions. Without professional skepticism, the auditor does not challenge nor remain alert to inconsistencies and circumstances that indicate actual or potential misstatements or fraud.

POWER CRY-SIS

Adil Farooq Qureshi

The name **'circular debt'** brings out the irony of continuous loop embedded in its nature. The total installed capacity for power generation at the end of FY 2012 was 24,412 MW, however only about 60% of it is utilized at the moment which makes up of 75% of total demand of 18,500-19,000 units. This resulted into 10-12 hours load shedding in urban areas and even worse situation in rural areas.

Circular debt is the amount of cash that is to be paid to the electricity producers (IPPs, GENCOs) by electricity distributors (DISCOs) and plagues the whole supply chain. The simplicity and complexity of power sector supply chain is that the entities involved have limited customers (1 in case of IPPs and GENCOs i.e., WAPDA) and limited suppliers (PSO, SNGPL / SSGCL). One weak link in the chain brings the whole system down as shown below:

Oil Producer(s) ➔ Oil Refinery(ies) ➔ Fuel Supplier (PSO, SNGPL / SSGCL) ➔ Electricity Producer (GENCOs, IPPs, Hydral plants) ➔ Electricity Distributor WAPDA (DISCOs) ➔ Consumer (domestic / industrial etc.)

Due to the limited number of parties involved in the supply chain, there is total dependency on the customer for generating cash flows from operations. Circular debt rose from Rs 84 billion at the end of FY 2005 to an estimated amount of Rs 537 billion at the end of Fiscal Year (FY) 2011. At the end of FY 2012 it was estimated to be Rs 872 billion representing approximately 4% of the national nominal Gross Domestic Product (GDP). Since their only customer WAPDA was delaying payments on electricity already delivered, IPPs resorted to bank borrowings to finance their working capital, which in turn resulted in exhaustion of banks' limits in terms of their risk exposure to the power sector. As the delay by WAPDA continued, it hampered the ability of IPPs to purchase oil and other raw material from suppliers resulting in under-utilization of available capacity.

Logically, the question arises: where did the circular debt come from? The explanation below is to simply make you understand the facts involved.

An average unit of electricity costs about the following w.r.t raw material used;

Raw Material	Rs / unit
Water	0.40 – 0.60
Gas	4-6
Furnace Oil	12-14
Diesel	17-19

and average price charged by WAPDA to consumers is Rs 7-9 / unit. How can you charge a product at Rs 8 which costs you around (say) Rs 15?! The comparison of costs of various raw materials and price of electricity shows that the cheaper resources were water and natural gas, which put WAPDA itself into profit. However, share of hydro power was about 31% of total generation in 2011, as compared to nearly 70% in the 1980s. Hydro power development suffered a slowdown due to controversies about major hydro power projects despite a large potential of hydro power in Pakistan. According to estimates, Pakistan has a hydro potential of about 60,000 MWs of which only 6,555 MW has been installed. Consequently, thermal power was relied upon. Initially, as natural gas was abundant and cheaper than oil, it was the preferred fuel for generation. However, a shortage of gas has resulted in a greater use of expensive furnace oil and high speed diesel oil. As a result, the cost of electricity has increased substantially. This issue is further exacerbated by the presence of corrupt practices and bad governance in the entities involved on the government end of the deal.

The interesting fact is that the price charged to ultimate consumer is fixed irrespective of the raw material used, however the cost varies w.r.t the raw material. The power purchase agreements (PPA) executed between WAPDA and IPPs provide that;

- Cost of raw material used will be billed to WAPDA based on a pre-determined heat rate (commonly known as plant efficiency)
- Cost of variable expenses to be billed to WAPDA based on pre-determined per unit rate
- Capacity charge to be billed to WAPDA even if zero units are produced by the IPP

Now when the consumer is charged for electricity as Rs 9 / unit (on average approx.) and the cost of that unit to DISCO is Rs 13 or Rs 18, how can WAPDA pay to GENCO or IPP in full? Or consider this, the IPP bills to WAPDA when no unit has been delivered due to PPA provision described above. The recovery losses of GENCOs also pose a big loss of revenue. As a result to fill this gap, the Government gave WAPDA subsidy amount. Since Government already faces budget deficit, this subsidy is financed by borrowing which further pressurizes the budget. Whether the power purchase agreement with IPPs / GENCOs contains flaws or the subsidy should not be borne by Government is a separate question. The former option is practically less probable since the IPPs involve foreign investments which were attracted based on guaranteed returns and the latter option is being implemented owing to compliance with IMF loan agreement covenants resulting in sharp electricity price hikes in the country.

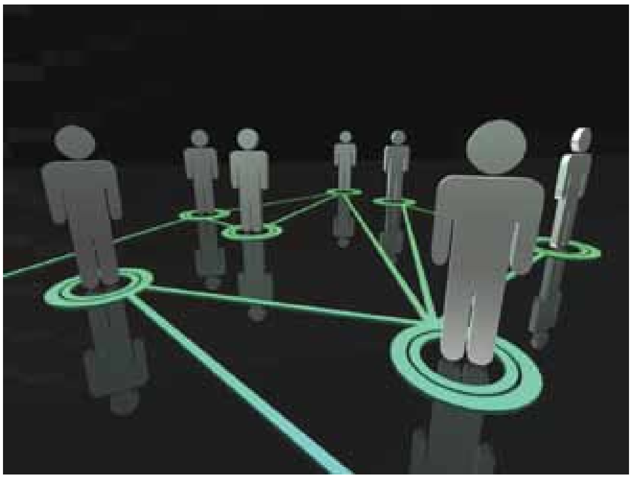
The common solutions being improvised by past and current governments are;

- One time payments of circular debt (as settled by present government in July 2013); and
- Attracting foreign investments in power sector.

Now what is surprising here that neither of these options are a solution to the core problem. Let's say today the government, somehow, clears all the outstanding balance of circular debt, what will happen then? Nothing, the debt will just build up again in a few months and we'll be facing the same load shedding. The present government settled Rs 460 billion in July 2013 (322 by cash, 138 by set-off) but Rs 43 billion was still pending at that time which has now grown to Rs 160 billion in just four months according to PakTribune.com.

The other solution being provided by government is rental power stations, more power generation plants. The only argument in its favor is that our existing plants are very old and their efficiency is less than 50%. But what is the need of new plants when there is already more capacity installed than needed at the moment!!! Further, the foreign investors fail to see the guaranteed returns in future, since they can provide the equity for fixed capital expenditure, however to earn the return on equity, the entity has to itself generate cash inflows for working capital. In the layman language, they can provide the investment in the plant, but are not going to bring their own oil and gas for generation. Further if the current scenario continues, how would WAPDA be able to pay the new plants when the existing ones are already considering invoking the sovereign guarantee provided for in PPAs.

In my opinion, long term solution is to positively make WAPDA a viable/profitable venture by curbing corruption and investing in generation of electricity from cheaper resources i.e., water and natural gas. Further the government should avoid agreements in future necessitating subsidy payment by government.



Economic Impacts of Riba (Interest) and the Remedy

Sami Ullah Khan

In Arabic language, Riba means usury, addition or growth. Historically, the Muslim jurists have held that any loan that involves an increase in repayments is forbidden, and as such, the Islamic state prohibits it. Muslim jurists have described two types of Riba; an increase in capital without any corresponding services provided and speculation, which is prohibited by the Qur'an, and commodity exchanges in unequal quantities, also prohibited in the Qur'an. The term Riba is not limited to money but also covers all the transactions whereby the debtor repays a certain quantity of goods in excess of those originally transacted, be it money, goods, any other tradable item or services; anything in excess of original agreed agreement is considered riba if items exchanged are of the same kind (such as gold for gold).

Realizing the importance of prohibition of Riba (interest) by Islamic laws, modern economists have also started evaluating its adverse impacts. Isolated implementation of a zero rate of interest was suggested by the Famous economist John Maynard Keynes, while Roy Harrod went on to proposes its total abolition. There is a growing number of modern day economists who are backing up the idea of a banking system without interest. Many corporate failures of the recent times have been tied up with the impact of higher rates of interest charged on their financing. The most feared impact of interest is its potential of limiting the borrowing capacity of the borrower crumbling under heavy interest, resulting in failure of his/her enterprise.

Another English economist Alfred Marshall in his principles of Economics (Book IV, Chapter XIX) puts it as, "the danger of not being able to renew his borrowings just at the time when he wants them more, puts him (the borrower) at a disadvantage relatively to those who use their own capital much greater than is represented by the mere interest on his borrowing. And the failure of this renewal may cause him to succumb to what would have been a passing misfortune if he had been using no capital, but his own".

Paying interest at higher rates has always been associated with the depression and crisis in trade. This however was mostly attributed to capitalism by the socialists. The fact is that interest is the greatest evil of capitalism and is the worst element of a capitalist economy itself. On the other hand, advocates of Islamic economy accept capitalism without interest thereby suggested eliminating its harmful impacts.

The Holy Prophet Muhammad (PBUH) has advised prohibition of seven harmful things and the third among these is interest, He stated,' Although interest brings increase, yet its end tends to scarcity'. The Holy Quran says, "That which ye give in interest in order that it may increase other peoples' wealth hath no increase with God; but that which ye give in Zakah, seeking God's countenance hath increases manifold" (Surah 30. Ar-Rum, Ayah 39).

Some notable economist including Arthur Pigou and Irving Fisher have conceded the negative impacts of interest in causing commercial and industrial crises. Islam favors the concept of joint stock companies and Arabs were the pioneered the establishment of these companies. Trade partnerships can be traced back to the days of Prophet Muhammad (PBUH) who himself had been the business partner of Hazrat Khadija (RA) who late became his wife. Modern days' phenomenon of purchase and sale of business shares are also evident from the Islamic history. Accordingly elimination of interest has been at the cornerstone of the basic objective of trade/economy in Islamic shariah in order to eliminate the likelihood of accumulation of wealth in the hands of a few thereby ensuing greater circulation of money and a wider distribution of wealth.

Broadly speaking major principles in Islamic economic model are (1) Zakat (i.e., the compulsory alms) (2) Islamic law of inheritance resulting in splitting the property of an individual into a number of shares given to his relations (3) The prohibition of interest which eliminates accumulation of wealth and this nips at the bud of capitalism. Sound economic system evolved by Islam is the only workable solution in solving the basic economic problems which are troubling the modern economies.

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Exploratory Testing

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"Everyone are born explorers, it's just that we learn how to do it better when it comes to testing software"

Introduction

Software testing is an integral part of software development life cycle. To improve the quality of software there are different testing approaches practiced over the years. Traditionally software testing is carried out by following scripted approach focusing on prior test design. So a holistic testing strategy should be in dire need which transcends test scripts to improve the quality of software. Majority of experts proposes a blended testing approach that combines exploratory with scripted testing to ensure consistent quality. Exploratory testing is an approach to test software where the tester does not require to follow a specific test design. But rather, exploratory testing should facilitate the tester in testing the complete system comprehensively.

Testing is potentially endless but an expert must introduce exploratory test techniques to identify defects early in the testing lifecycle. Experts stressed over on the implementation of a hybrid approach of exploratory and scripted testing that enhances the effectiveness of testing by combining the best of both worlds. Exploratory testing by experts is a way to conduct simultaneous learning, test design and execution of tests simultaneously. Other points towards exploratory testing enable constant evolution of tests easily. The ongoing tests might vary the conditions that initially exposed the problem, or they might explore possible side effects of the fix. The details of additional tests are not recorded in any test plan. The expert tester invents them as he starts working on it. The significance of exploration is an active, risk-focused investigation of the product. Rather than designing tests early, when the tester is just beginning to learn what the product is, how it can fail, and who will use it to do what, on what platforms.

Extracts from the History

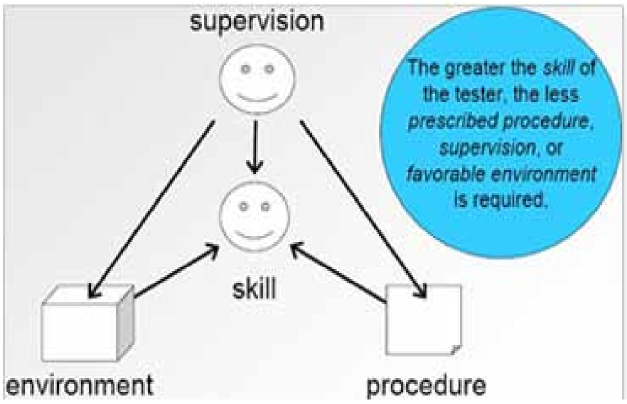
Exploratory testing is hardly new. The term was conceived by the software testing Guru Cem Kaner in 1983. In his classic bestselling book, Testing Computer Software (1988) he writes, "No matter how many test cases of how many types you've created, you will run out of formally planned tests. You can keep testing. Run new tests as you think of them, without spending much time preparing or explaining the tests. Trust your instincts." By discarding the approach of tester intuition and instinct as unscientific, immeasurable, and therefore unworthy, the exploratory testing approach has been continuously expanding since the last 25+ years. Kaner has recently updated the description as "Exploratory testing is simultaneous learning, test design, and test execution, with an emphasis on learning."

Scripted vs. Exploratory Testing

Scripted testing requires complete and detailed documentation. The tester writes out a detailed step by step perception of exploratory testing that has changed over time and now organizations have started developing a better understanding of it. The tester, sometimes the same person who wrote the test cases, and sometimes someone else who reads the test case, follows the instructions, reads the expected result from the document, and if what the tester observes the software to be doing at that point in time, corresponds, in the tester's opinion, to the what he understands to be what is written as the "expected result" in the document, then the test has passed. The tests that are being run have been scripted in advance. But in the real world it doesn't work this way, or at least, it shouldn't. Good testing is an intellectual activity that is something you do with your brain, comprising of not only the routine comparisons but also involves complex thoughts.

Exploratory testing does not rely on test cases documentation or to follow a specific test design prior to test execution. ET should rather help the expert tester in testing the complete system extensively. ET is done with a view that software is bound to have defects in it. The tester has to somehow identify these defects by using any possible combination of techniques. It is an optimized approach to find defects and less emphasis is made on test documentation.

The key difference between exploratory testing and scripted testing is the aspect of learning. ET needs a skilled expert tester, who is a competent critical thinker with advanced analytical skills and a creative imagination to be able to come up with a test, observe the results, decipher them, collect and consolidate data about the tests, formulate a hypothesis about the behavior of the software based on the data already collected, and think of new tests, on the spot, to check if the hypothesis is accurate. This can get quite complex, as new experiments often give unexpected and sometimes temporarily unexplainable results. A skilled tester with good exploration skills can get to the bottom of a complex testing issue by continuously refining his experiments and disproving his own hypotheses, all the while learning about the product. An effective software testing is a challenging intellectual activity, and at the same time is a very scientific and systematic experience.



Positive Aspects of Exploratory Testing

- Effectiveness of testing is directly related to tester's knowledge, experience and skills.
- ET is simultaneous learning of system under test, test design and execution.
- ET focuses on finding defects by exploration, instead of systematically producing test cases for later use.
- An ET tester uses all available information of target system under test. It includes any document i.e. user's manual, and marketing brochure. ET is guided by previously performed tests results and knowledge gained from them.
- ET does not define detailed test scripts; instead ET is exploration with general mission without following step by step instructions to complete the mission.

Negative Aspects of Exploratory Testing

- Management trust
- Industry or client lack of faith
- Coaching testers

Software testing can be very costly and is indeed a vast field so the accurate knowledge is crucial to ensure the quality of the software developed.

Conclusion / Wrap-up

Exploratory testing is an efficient and effective approach to testing software and has attracted a great deal of

interest in the software testing community. Exploratory approaches to testing live at one end of a continuum. While Scripted testing is pinning down a list of step-by-step actions to perform, each step paired with a extemporaneous condition to observe, is at the other end of the continuum. Scripted tests are designed by a senior expert tester, and given to a more junior tester to execute. Scripted approach is exorbitant and time-consuming, and seems likely to lead to in-attentional blindness. It also separates test design from test execution and result interpretation, and thereby lengthens and weakens the learning and feedback loops that would otherwise support and strengthen them. Critics annotates that ET is "unstructured", equating it with ad hoc testing or fooling around with the computer. If ET is fooling around with the computer, then forensic investigation is poking around inside a dead body.

Exploratory testing is not structured in the sense of following a prescribed, step-by-step list of instructions, since *that's not what structure means*. Structure, per the Oxford English Dictionary, termed as *"the arrangement of and relations between the parts or elements of something complex".* According to this definition, there is no reference to sequencing or to lists of instructions to follow. So, just as education, nutrition, driving automobile, juggling, child-rearing, and scientific revolutions are structured and have structure, ET is also structured. In fact, there are many other structures confederate with ET. Testers with ET experience might be more able to discover their blind spots or identify techniques that would not otherwise occur to them. Much work remains to be done before the impact of learning styles on ET is completely understood. Distinctive aspect needs to be explored comprehensively for connections. The aspects must be looked at in combination. Experimentation must be performed to validate the claims.

While exploring ET we found that there is a serious lack of research literature about ET but there is ample gray literature produced by different ET practitioners is available. Perception for ET has changed over time and now organizations have started developing a better understanding of it due to its Creativity, Interactive approach, Drive towards fast results, Concurrence of cognition and execution, De-emphasize archived testing materials.

There has been a recent empirical evaluation of influence of human personality on exploratory software testing (Shoaib et al., 2009) which described the relationship between human personality and the ability to become an exploratory tester. The results show positive relation between human personality traits and exploratory testing, and conclude that extrovert personality is more likely to be good ET testers in industry.