PUBLIC DEBT MANAGEMENT & SUPERVISION

Federal Legislative List Part -II Section 8

PAKISTAN STUDY GROUP ON FEDERALISM

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SCOPING STUDY PAPERS
No-01/Dec-2015

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ACKNOWLEDGEMENTS

No words can thank God for bestowing an honour to the National Institute of Historical and Cultural Research (NIHCR) to host the valuable project of the Pakistan Study Group on Federalism (PSGF) was launched on October 27, 2014, jointly by the UNDP's project on Strengthening Participatory Federalism and Decentralization (SPFD), the (NIHCR), and the Council of Social Sciences (COSS) at the NIHCR, Quaid-i-Azam University, Islamabad. Since the idea of establishing the PSGF, indeed, belongs to Mr. Amjad Bhatti of the UNDP, so he entitles the first gratitude. Irrespective of any mid-course ebb and flow he always extended his unconditional support to the project for its successful accomplishment. All together, we are personally obliged to the Country Director, UNDP-Pakistan Mr. Marc-André Franche—a staunch supporter of citizen empowerment and institution building in Pakistan. In spite of all the vicissitudes in and with the project, he kept on supporting the PSGF for its smooth running. Mr. Daud Sharif, and Mr. Taimoor Javeed of UNDP, stood the next adherents in this regard. They both were personally involved to pull through the project from all its odds. Throughout the project activities a wholehearted support of Dr. Alia H. Khan, Dr. Zaman, Dr. Waheed, and Dr. Wiqar Ali Shah boosted it up.

The most technical job of communication and research was taken up by Miss Amina Sarwar. Her technical input and effective communication with the Council of Advisors, list of experts and the Steering Committee was commendable. Later on this task was resumed by Mr. Naseer Ahmed who steered it quite promptly towards its successful finishing. A constant guidance of Dr. Rahat Malik to them was infusing spirit to the project.

For making these publications possible we had to avail technical support of Mr. Munir Khawer Mr. Muhammad Saleem, and finally of Mr. Imran Zahid. Time to time assistance of Mr. Hazzor Bux Channa and Mr. Rao Tahir also made this endeavour possible. Managing the finances at multiple levels with the UNDP, COSS, NIHCR and finally maintaining the accounts of PSGF was quite a complicated job, which was efficiently done by Mr. Atlas Khan. His synchronization with a financial expert like Mr. Daud Sharif was really creditable. I personally thank all the team of NIHCR for their categorical support in every regard. At last but, not at all the least, I feel myself helpless to rightly acknowledge the love and affection of Prof. Dr. Eatzaz Ahmed who initially facilitated the signing of MoU with the UNDP and then always extended his patronage to the PSGF.

(Sajid Mahmood Awan)

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LIST OF ACRONYMS

ADB	Agricultural Development Bank
CCI	Council of Common Interest
DG	Director General
DLI	Disbursement Linked Indicators
DMIS	Debt Management Information system
DMFAS	Debt Management and Financial Analysis System
DMU	Debt Management Unit
DPCO	Debt Policy Coordination Office
DPS	Debt Policy Statement
EAD	Economic Affairs Division
FAAA	Foreign Aid Assignment Account
FDFDS	Finance Department and Foreign Debt Section
FLL	Federal Legislative List
FL2	Federal Legislative List-2
FRDLA	Fiscal Responsibility and Debt Limitation Act, 2005
GDP	Gross Domestic Product
HR	Human Rights
INTOSAI	International Organization of Supreme Audit Institutions
IMF	International Monetary Fund
IPC	Inter Provincial Coordination
ISSAI	International Structure of Supreme Audit Institutions
KP	Khyber Pakhtunkhwa
MTDMS	Medium Term Debt Management Strategy
NAM	New Accounting Model
NEC	National Economic Council
NFC	National Finance Commission
P&D	Planning and Development
PAP	Public Accounts of the Province
PCF	Provincial Consolidated Fund
PDM	Public Debt Management
PDMA	Public Debt Management Audit
PML-N	Pakistan Muslim League (Nawaz)
RAP	Revised Accounting Procedure
RFA	Revolving Fund Accounts
SNG	Sub-National Government
UNCTAD	United Nations Conference on Trade and Development
WB	World Bank
WBDSP	World Bank Debt Support Program

EXECUTIVE SUMMARY

The Scoping Study on federalism in Pakistan regarding the subject of "Supervision and Management of Public Debt" (Federal Legislative List Part II Section 8) is divided into five parts: Part one contains introduction, literature review, history, and an overview of debt stock and debt structure of Pakistan; Part two surrounds definitions of public debt and its management, principles, objectives and functions of the PDM, and how the PDM is premised and contingent upon the principles of provincial borrowing autonomy, economic and political principles of fiscal federalism; Part three covers detailed description and analysis of federal and constitutional arrangements of the PDM; Part four deals with an overview of the provincial PDM frameworks and describes and analyses the PDM arrangements in the Punjab, KP, Balochistan and Sindh, as well as some intergovernmental issues of the PDM; and, the Part five encloses conclusion, policy challenges and recommendations.

1. HISTORICAL APPRAISAL OF DEBT STOCK AND THE DEBT STRUCTURE IN PAKISTAN

1.1 Introduction

The Public Debt Management (PDM) is not only a third-world issue rather it indeed is their serious concern. Debt and its management is a global issue; rich and poor, developed and developing countries all face challenges of debt and debt management by respective levels of their governments. However, debt management in the third world has been of grave concern. This was taken up quite late as a political issue involving broader political concerns demanding political consensus. Legislation and institutional mechanisms were introduced and adopted by the third world countries during late 1990s, starting from different debt reform programmes of the IMF and the WB, the UNCTAD and the Commonwealth who have been major contributors in terms of inspiration, finance, technical and institutional support for debt management reforms in the developing world.

The public debt is as political as technical, within the framework of federal relations of center and federating units. The public debt is a domain full of choices and alternatives, risks and costs, packaged advantages and disadvantages, complex decision making, volatile financial environments and incentive structures. All these factors make public debt domain full of challenges and opportunities for the creditors and borrowers, debt managers and policy makers, and the nation, its federating units and public at large, being beneficiary or affected in the long run. Thus, it calls for broader participation and consensus as well as for transparency and accountability of public debt policy and institutions.

1.2 Literature Review

The foundations for fiscal federalism which also provide insights for federal arrangements of public debt management are inspired from Oates (1972, 1994), Rodden (2004), and Banting *et.al*. (1994), etc. Moreover, literature on Sub-National Governments (SNGs) borrowing and finance as Garci-Mila *et.al.*(2001), Singh and Plekhanov (2005), Stegarescu (2013), Vulovic (2010), etc. was quite useful. The Sub-National Government borrowing in federalism has also been undertaken by some other researchers as impact of fiscal decentralization on fiscal stability. Such studies include: "Fiscal Decentralization and Macroeconomic Stability: The Experience of Large Developing and Transition Economies" by Fukasaku and De Mello (1998) and *Costs of SGN Borrowing and Need for SNG Fiscal Discipline* by Ter-Minassian (1997), and the IMF/WB's advisory and policy literature on independent debt management, autonomous from monetary policy, particularly the WB *Revised Guidelines for Public Debt Management* (2014), and the UNCTAD studies etc.

All this literature has been a substantial source of major debt management reforms reflected in adoption of debt related legislation, independent debt management offices and specialist staff (independent from Finance Ministry and State Banks) and the UNCTAD's DMIS (Debt Management Information System) adopted by EAD in Pakistan, etc. has been the outcomes and thrust of debt management reforms in countries like Pakistan. Eric Togo (2007) talking about a sovereign Asset and Liability Management (ALM) framework proposed for integrating debt management with macroeconomic framework of analysis. Barro (1999) considered the effect of debt management on tax, Tobin (1963) on macroeconomic stabilization, Missale (2000) on deficit stabilization and Calvo and Guidotti (1990) in consistent monetary policy. Eatzaz Ahmed (2011) highlights issues in public debt management in Pakistan and that how the absence of effective debt management can exacerbate debt crisis situation. The researchers have also been grappling with the definition, the meanings and quantifying the debt and related fiscal concepts and the research results therefore differ.

1.3 Methodology

A series of interviews was conducted by the researcher himself to interview the debt management government officials, policy makers and the persons sitting at the helm of affairs. Number of official records was consulted as primary source of research. Apart from it, different reports, working papers, journal articles and distinguished lectures were also thoroughly reviewed and referred as secondary sources to support the central argument of the study. The researcher has exploited both qualitative as well quantitative research techniques to approach the fundamental facts on the subject. The study by default was of empirical in nature however, the rational logic was also applied for normative explanation of the subjective reality. This does not mean at all that objectivity of the study was ever compromised. With an application of all these diversified approaches the study turned out to be empirico-rational in its construction.

1.4 Historical Appraisal of Statutory Debt

The practice of statutory debt ceiling and limitation started in the US in 1917 with the Second Liberty Bond Act, 1917 which evolved into general debt limit in 1939 (Austin, D. Andrew & Levit, Mindy R., 1993) and played role in federal borrowing, congressional oversight and the legislative process (Linda K. Kowalcky and Lance T. LeLoup, 1993). Hoogduin *et. al.* (2010) have traced evolution of public debt management and its objectives in the macroeconomic policies of 1960’s and 1970’s in Europe. This was spurred by the developments in financial markets as liberalization and deregulation.

On Independence, Governor General Muhammad Ali Jinnah sent an emissary to the US for financial support for Pakistan. The external as well as domestic debt became predominant in the development decade of 1960s in Pakistan. Many attempts to rein in the public debt have been made previously to donor-sponsored debt reform as the working and report of Debt Reduction and Management Committee (Government of Pakistan, 2001) reveals powers of borrowing were part of the Constitutions of Pakistan, for both the federal as well as provincial governments.

However, legislation related to financial responsibility and debt limitation, providing broader framework for debt management, was introduced in 2005 under the Financial Responsibility and Debt Limitation Act, 2005. Such legislation in India was introduced through the Fiscal Responsibility and Budget Management Act, 2003. Similar legislations were introduced during the same period in many developing countries as part of debt management reform programmes by the international development agencies.

1.5 History of Debt Management Reforms

Major advisory services by the international agencies are provided by the UNCTAD/DMFS and the WB Debt Management Advisory Services. Many third world countries have adopted debt management reform proposed by these agencies. A structured and sequential proposal of debt management reform is provided in their advisory reports, and particularly in *WB Guidelines for Public Debt Management* (2001), regularly revised and the recent most revised version dates 2014. When faced with the challenge of information on external debt in its first technical assistance programme on debt, the UNCTAD developed initial version of computer based Debt Management and Financial Analysis System (DMFAS) in 1981 which evolved the web-based version in 2009.

The DMFAS by UNCTAD, the Debt Management Programme of the Commonwealth Secretariat as well as the Debt Management Support Programme of the World Bank have helped developing countries improve debt management, particularly developing mechanisms for collection of statistics on complete public debt profile, for improved decision and policy making (Ugo, 2008). The WB launched a pilot project of debt management reform covering 12 countries including Pakistan in 2002 (World Bank, 2007). The EAD and the SP introduced debt management related reforms with the technical assistance of ADB (Ahmed, 2011). Though the reform programmes include the Public Debt Management Audit (PDMA), as the INTOSAI Development Initiative launched in 2008 in collaboration with the UNCTAD, however, the PDM in Pakistan remains long distance away from this stage.

1.6 Analysis of Debt Stock and Debt Structure

The Debt Policy Statement 2014-15, issued by the Debt Policy Coordination Office and required to be submitted to the legislature, has presented the following picture of Pakistan’s public debt. According to the *Auditing Public Debt Management 2011*, the public debt in Pakistan was recorded at Rs. 16,235 billion as at the end of September 2014, registering an increase of Rs. 239 billion or 1.5 percent during the first quarter of 2014-15. External public debt decreased by US$ 1.4 billion during first quarter of 2014-15 and recorded at US $50 billion. Revenue deficit was recorded at Rs. 173 billion or 0.7 percent of GDP in 2013-14 and needs to be brought to nil as required under the FRDL Act, 2005. The Debt Policy Coordination Office (DPCO), Debt Policy Report also provides that “Public debt to GDP ratio recorded a decline…and stood at 63 percent at the end of 2013-14”. It expresses government’s commitment to reduce public debt to GDP ratio and bring it to below 60 percent as prescribed in the FRDL Act, 2005. Provinces are indebted to the federal government by 800 billion rupees.

Pakistan's public debt has two components i.e. domestic and international. Domestic public debt includes bonds and bank loans. Bonds form direct borrowing by government from public and come in a variety of bonds (as saving and other financial certificates, including Sukuk, etc.); bank loans are arranged by the State Bank of Pakistan for the federal government for domestic debt and financial market particularly banking sector.

International borrowing also comes in two forms i.e. commercial loans and financial assistance. Commercial loans from international banks are arranged by the Finance Division through its External Finance Wing. This borrowing is arranged at international commercial rates. This also includes the introduction of the Eurobonds, attracting international retail creditors, besides borrowing from international banks.

Borrowing in the form of financial assistance is arranged by the Economic Affairs Division, from multilateral and bilateral donors; this form of borrowing is taken at subsidized rates. Financial assistance related borrowing comes in mainly three forms: development assistance, policy loans and budgetary support. Development assistance is arranged for development projects and is also termed as project loans; it is negotiated according to the project and disbursed according to the achievement of project phases, as provided in the DLIs (the Disbursement Linked Indicators), which are part of the project and therefore also of the debt negotiations.

Policy loans (or programme loans as they are termed otherwise) are aimed at development and improvement in any target sector as education or communication, but not specific activity of the project; instead multiple activities and projects can be taken up by the respective sector. The disbursements are linked to the given targets of the sector or policy area or programme in that specific sector/policy area; the disbursement linked targets are supposed to be achieved within specific period of time, from one year to five years.

The third form of financial assistance borrowing is budgetary support: it is aimed at macro-stabilization; most of the IMF loans are targeted at budgetary support, with broader macro-economic targets, such as against deficit or inflation, or to improve current account position and easing the balance of payment problems.

2. ESSENTIAL PRINCIPLES OF FISCAL FEDERALISM AND THE PDM

2.1 Definition of Public Debt and Public Debt Management

Public debt is commonly defined as an obligation of a government entity, including a national government, a political subdivision and government controlled bodies. According to the ISSAI 5421, *Guidance on the Definition and Disclosure of Public Debt*, the public debt can include liabilities or other commitments incurred directly by public bodies, like:

- Central government, or federal government, depending on the manner of political organization in a country;
- State, provincial, municipal, regional and other local government or authorities;
- Owned and controlled public corporations and enterprises;
- Other entities that are considered to be of a public *quasi*-nature;
- Liabilities or other commitments incurred by public bodies on behalf of private corporations or other entities.

As most of literature on debt has been concerned about "external" public debt, definitions, meanings and measures of public debt have been skewed from perspective of the dichotomy of external-domestic public debt. Though the scholarly debate continues, yet the current scope of the definition of public debt not only includes the principle amounts owed to creditors (domestic or foreign), but also all liabilities, risks, externalities and other vulnerabilities, ensuing from the politics and practice of public debt.

Definition of public debt management has also been attempted from different perspectives. The *IMF Guidelines* (2014) define public debt management as following:

> Public debt management is the process of establishing and executing a strategy for managing the government's debt in order to raise the required amount of funding at the lowest possible cost over the medium to long run, consistent with a prudent degree of risk. It should also meet any other public debt management goals the government may have set, such as developing and maintaining an efficient market for government securities.

The *IMF Guidelines* (2014) on public debt management contain following areas of debt management framework: legislative framework; debt management strategy; policy coordination and oversight; organizational structure; staff capacity; debt recording and reporting; operational risk management; audit and compliance.

The objectives and functions of public debt management have been provided and examined from different perspectives and include, among others, macroeconomic stabilization, cost and risk minimizing, tax smoothing and deficit stabilization. *Debt Policy Statement* issued by the DPCO (Ministry of Finance, 2015) provides objectives as to develop a viable and stable debt portfolio, mitigating risks of refinancing, exchange rate fluctuations and debt accumulation.

2.2 Principles, Objectives and Functions of PDM

The PDM frameworks also need to be based on some principles which have emerged through the PDM projects with international best practices as evolved over time in developed and developing countries. They include among other: independence, specialization, incentive structure, transparency, accountability, competitiveness, debt discipline and debt harmonization,

Independent debt management can be a basic requirement and starting point for provincial debt management independence from Finance Ministry or at least rest of the monetary management of the Finance Ministry, and independence in reporting to the legislature, etc. This independence needs to be ensured through legislation, organizational and operational framework at the provincial as well as the federal levels. Debt audit may also need to be incorporated in transparency and accountability regime with its reporting to the provincial and national legislatures.

In view of the complex and dynamic nature of the financial and debt markets around the world, specialized staff with background educational and professional experience in debt management for renowned corporate or public sector need to be leading the debt offices, with a mix of bureaucratic and specialist staff manning the organization’s strategic and everyday matters. Enabling incentive structure can only attract competitive professionals in the debt management office from highly lucrative and competitive financial and debt market domestically as well as internationally.

Since early 80s, the UNCTAD and other development agencies have successfully been evolving and implementing the debt management information systems in developed as well as developing countries which has also been adopted and implemented in Pakistan by the EAD for the management of external debt raised by the federal government. Such information systems are not only pre-requisite for an effective debt management, but also for effective reporting system for legislature as well as for policy making, and fulfillment of the requirements of transparency and consequently accountability. Such information systems are also basis for debt crisis prevention. Ugo Panizza (2008) concludes on his analysis of developing countries public debt concerns: “crisis prevention requires detailed and prompt information on debt”.

The cost of borrowing is a significant indicator and criteria of an effective PDM. Domestic short term borrowing has traditionally been more costly than international medium and long term borrowing. Within domestic debt market, competition and choice amongst alternative debt instruments may be more a political choice rather than technical and revenue demand driven. Such practices and choices will shape and influence effective debt management in provinces causing concerns of transparency and accountability.

An effective provincial PDM can provide for provincial debt discipline, as provinces are going to fare without previous experience the complex, dynamic and even chaotic debt and financial markets. Monitoring and evaluation mechanisms for debt sustainability and prevention from debt default can be ensured through placing appropriate mechanisms for PDM.

The federal government bears the responsibility of debt harmonization at national level through appropriate intervention of standards in provincial borrowing and through a variety of fiscal and financial incentives and instruments so that debt structure, level and cost etc. pertaining to provinces are managed in harmonized fashion by the federal government, ensuring debt sustainability as well as accountability of provincial borrowing autonomy and national debt management. Debt stock, portfolio, composition and repayment schedules — all will affect the challenge of debt harmonization and eventually may influence the evolving federal fiscal relationship (Garci-Mila, *et. al.*, 2001).

2.3 Provincial Borrowing Autonomy and PDM

Most of the federations provide for Sub-National Government or provincial borrowing autonomy. The Constitution of Pakistan, 1973 also provides for the provincial borrowing autonomy under its Article 167, which says:

> **Borrowing by the Provincial Government.—**(1) Subject to the provisions of this Article, the executive authority of a Province extends to borrowing upon the security of the Provincial Consolidated Fund within such limits, if any, as may from time to time be fixed by Act of the Provincial Assembly, and to the giving of guarantee within such limits, if any, as may be so fixed.
>
> (2) The Federal Government may, subject to such conditions, if any, as it may think fit to impose, make loans to, or, so long as any limits fixed under Article 166 are not exceeded give guarantees in respect of loans raised by any Province, and any sums required for the purpose of making loans to a Province shall be charged upon the Federal Consolidated Fund.
>
> (3) A Province may not, without the consent of the Federal Government, raise any loans if there is still outstanding any part of a loan made to the Province by the Federal Government or in respect of which guarantee has been given by the Federal Government; and consent under this clause may be granted subject to such conditions, if any, as the Federal Government may think fit to impose.
>
> [(4) A Province may raise domestic or international loan, or give guarantees on the security of the Provincial Consolidated Fund within such limits and subject to such conditions as may be specified by the National Economic Council.]

Clause 4 has been added through the 18th Amendment in 2010, to make the provincial borrowing autonomy workable, which could not be operationalized even after its provision by the 1973 Constitution. Relation of clause 1 and clause 4 then can be understood in this background, making the provincial borrowing autonomy restricted, limited and dependent upon interprovincial arrangements with the federal government through the National Economic Council. Above all, since the Article 167 was not operationalized independently by the provinces previously, it made or kept the need for an autonomous provincial debt management regime also dormant and in infancy. Moreover, the relation of clause 4 and clause 1 will also come into interplay as the spirit of the clause 1 provides broader provincial borrowing autonomy as compared to the clause 4, but appear to be retained by the drafters and Parliamentarians of the 18th Amendment for future engagement of effective and broader provincial borrowing autonomy. This requires, *inter alia*, the development of an effective and independent provincial debt regime, with its own organizational and incentive structures, information and debt data systems, reporting and policy-making mechanisms.

Development of international and domestic debt and financial markets has made borrowing autonomy and its effective management possible and a federal choice in growing numbers of the federal states. Previously, debt and financial market were mostly controlled and responsive to the national central governments. With the growing complexity, dynamism, and diversity in the debt and financial markets, products and instruments have dramatically transformed public finance at lower levels of government not only a likelihood, but rather a pre-requisite for devolution of financial participation as well as financial responsibility. As loaning to all tiers of governments is accessible, available and manageable, provincial borrowing autonomy has evolved from a legal constitutional fiction to an everyday fact.

Though decentralization of debt (as part of revenue raising/revenue mobilization), have been seen in the framework of borrowing autonomy as revenue autonomy (Tanzi, 2008), but the borrowing autonomy is closely linked with the PDM. In the absence of effective PDM, provinces fail even in the limited borrowing autonomy, leading eventually to their estranged relations with the federal government and loss of trust in their financial and fiscal capability. As borrowing autonomy directly implicates transparency and accountability, the PDM provides basis and framework ensuring effective presence of these two principles.

It has been argued that unpredictability and transfer dependence of federal grants and transfers can be reduced by the provincial borrowing autonomy. Higher federal transfers result in lower provincial accountability (vertical fiscal imbalance). Moreover, just the “level” of debt a province is allowed to raise is not true reflection of borrowing autonomy; instead regulatory framework and capacity to raise and manage debt also influence borrowing autonomy of the provinces (Rodden, 2004). As Amertya Sen (1999) would have it: autonomy is about capacity and choice. This raises the issue of federal commitment principle in case of debt default by the provincial governments. It is argued that Intergovernmental “competition” in competitive borrowing calls for its effective management and stringent debt discipline. Besides intergovernmental and inter-regional competition (or otherwise cartelization), regional and ideological variations may also cause the changing cost of borrowing for different provinces, as some province may experience peculiar political and economic circumstances such as law and order situation, low or high levels of conflict, regime instability at provincial level, GDP levels. These all factors may escalate the costs of borrowing and impact the federal commitments, against debt default by the provinces (Benton, 2013).

2.4 Over-Borrowing, Debt Default and PDM

Provinces may start projects which later on demand raised costs; the causes may be natural disasters, security threats and law and order situation, regime changes, changes in international political and economic scenario, etc. This raises the issues of federal government commitment and bailout (Seitz, 1999): fiscal and borrowing autonomy of sub-national governments is contingent upon financial responsibility and federal government's commitment against any bailout to the default provincial government.

Besides US and other federations, the case of German government in bailing its sub-national government out is an interesting study. Data from comparative political studies suggest frequent bailouts of the provincial government in such circumstances by the federal government, not only for the reason the primary rather sole responsibility of the federal government owing to its sovereign guarantee, but also because of the pressures of judiciary, media and political groups (Stegarescu, 2013). In Pakistan, this can cause even exacerbated competition amongst the provinces on one side resulting in political willingness for financial recklessness and irresponsibility and therefore default as a chain reaction, besides political and fiscal tensions and struggles between the federal government and the defaulting province.

2.5 Fiscal Federalism and PDM

Federalism is a process, a process of federal-provincial relations, growing and evolving. So are fiscal federal arrangements. Ultimate end and purpose of federal fiscal arrangements is the welfare of each individual (Tanzi, 2008). All such federal arrangements are ultimately aimed at reaching out to that individual and ensure its welfare. Economic principles of fiscal federalism which most economists put forward for their analysis and empirical study can also be viewed from the perspective of PDM.

Fiscal efficiency is the core principle and the PDM is also aimed at achieving this, as it makes borrowing safer and cheaper, against being riskier and costlier (Panizza, 2008). Reducing debt costs, risks and other vulnerabilities and negative externalities is the prime target of PDM. Equity principle can be introduced through greater provincial borrowing autonomy and broader participation and consensus in debt policy and decision making of the regions and provinces.

The principle of creation and sustenance of national economic union is also linked with the PDM: both are premised on debt and fiscal discipline through effective regulation of debt and financial markets, reform and technical support of the provincial debt regimes and maintenance of fiscal and debt regime standards for provincial as well as federal governments within the constitutional arrangements and norms.

Affordability in federal fiscal and financial arrangements is also critical principle and criterion and developed mechanisms of the PDM can help prevent riskier and costlier debt arrangements, which can threaten smooth and growing inter-provincial federal relations. Flexibility principle has also been considered by some researcher in the context of fiscal federalism and also relates to the PDM, as debt policy and decision makers are exposed to developed and diverse instruments of debt market (both domestic and external), they are also faced with the challenges of volatility and trade-offs amongst debt instrument choices.

The principle of accountability also cannot be over-emphasized in relation to the PDM. Competitive instead of cartelized borrowing can be ensured through legal and political requirement of debt reporting (to creditors, legislature, federating units, civil society and public at large), debt auditing by the supreme audit institutions and by providing clear levels and means of accountability. At present, dilemmas of the PDM accountability is that there are no federal mechanisms of accountability and public debt audit—for the debt structure, its level and costs and provincial demand-debt relations etc. in the present legislative and legal framework, except one time submission of Debt Policy Statement by DPCO (an office of the Finance Ministry), before national legislature, even that in highly technical jargon of the debt and financial market, with limited independent source of comparative data analysis on Pakistan’s debt from third sources for the legislature.

2.6 Political Principles of Fiscal Federalism and PDM

In addition to the economic principles of fiscal federalism, political principles of federalism also equally relate and concern the PDM framework: participation, consensus, fiscal autonomy to lower levels of government, predictability to provincial finance, debt discipline, borrowing cost competitiveness vs. debt cartelization, risk management, default management etc. are critical for the design of PDM framework in provinces and inter-provincial forums without which effective coordination, long term harmonization and trust cannot be expected from evolving fiscal autonomous relations of a federation.

PARTICIPATION: Democracy is about greater and effective participation of the citizens or voters, and it is organized through participation mechanisms of representative institutions. Federalism provides the possibility of participation of regions and populations through different levels and tiers of government. Fiscal and borrowing autonomy provides opportunity to the provincial and local representatives and decision makers to become part of the efforts of financing governments at provincial and local level. Such participation breeds transparency, accountability, consensual decision making and a strong sense of collective equity and fairness.

Further, it helps developing a culture of participatory fiscal and financial governance. Consensual decision making reduces strains and stresses of regional absence and distrust in the fiscal decision making, thus lowering the cost and risks of decisions, and their enforcement. Greater fiscal autonomy at lower levels of government provides opportunity to manage regional affairs not only in spending and revenue mobilization spheres, but also in borrowing, thus prompting the process of financial responsibility and accountability.

Unpredictability in providing finance to the budgetary spending and development projects in case of complete dependence on the federal government transfers can cost more and have greater risks than raising own taxes and debt domestically and internationally. It in turn helps improve predictability of the public finance for the provinces. It also helps in reducing transfer dependence, particularly in the case of Pakistan where emergencies and exigencies of its peculiar geo-strategic existence and development dilemmas, provide federal government grounds for diversion of committed resources, affecting provincial development schedules and plans and thus causing regional and provincial discontent.

Debt discipline is the essential principle for the continued trust, commitment, and fiscal sustainability of the whole federation. Default of one province not only places the federal government in trouble of bailout and increased cost of borrowing, but also may create strenuous fiscal struggle amongst the provinces themselves, by creating spiral of fiscal irresponsibility and *en bloc* default of the rest of the provinces. Prevention of fiscal and financial crisis can only be ensured through debt and fiscal discipline.

The case of competitive vs. cartelized borrowing in relation to the provincial PDM is also interesting. Provinces may compete for low cost borrowing or otherwise may also cartelize amongst themselves for high cost borrowing, evading debt audit and accountability, thus eventually burdening the national exchequer, even if not defaulting *en bloc*. Here, the analysis of Freitag and Vatter (2008: 272-294) is equally enlightening:

> From a theoretical point of view, decentralization and federalism can be associated with both an expansive and a dampening effect on government debt. On the one hand, decentralized structures have been argued to lead to a reduction of debt due to inherent competition between the member states and the multitude of veto positions which restrict public intervention. On the other hand, decentralization has been claimed to contribute to an increase of public debt as it involves expensive functional and organizational duplications as well as cost-intensive, often debt-financed, compromise solutions between a large number of actors that operate in an uncoordinated and contradictory way.

DEBT RISK MANAGEMENT: Volatility, complexity and diversity of debt and financial markets, and their products and instruments place provincial public debt management at a medium to high risk in financial and fiscal terms. Managing possible and potential risks of the public debt by embedding appropriate mechanism in the legal and institutional frameworks will be a priority of the public debt decision makers in the province.

DEBT DEFAULT MANAGEMENT: Developing mechanisms to deal, control and limit provincial debt defaults may be too early to talk and discuss in the case of federal fiscal arrangements in Pakistan, yet not too far-fetched. Debt default is not only a possibility but a reality in many federal polities, providing for some form and level of provincial borrowing autonomy. The public debt carries its own vulnerabilities, externalities and risks and these vulnerabilities and risks may turn into default, causing either ensuing federal-provincial (and even interprovincial) fiscal struggles, even if not leading to inter-provincial level default in a country. Appropriate mechanisms for debt default management need to be incorporated and placed in the legislative, legal, organizational and operational frameworks of the debt management in a province.

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3. FEDERAL GOVERNMENT AND CONSTITUTIONAL FRAMEWORK OF PDM

3.1 Federal Government Arrangements of Public Debt Management in Pakistan

A review of federal public debt management is made below to grapple with the present and existing scenario with reference to the 18th Amendment. This section will see as to how do laws, institutions, rules and practices (established through pre-18th Amendment arrangements) evade constitutional spirit and norms and in which direction they need to be steered and redesigned. So the pre-18th Amendment arrangements of federal government for public debt management in Pakistan were as follows:

i. **THE FISCAL RESPONSIBILITY AND DEBT LIMITATION (FRDL) ACT, 2005:**

This law was introduced as part of Government of Pakistan's attempt to reform fiscal and debt management, with initiative and technical support of international development donor agencies. It provides a centralized and specialized debt management framework. Though this law was introduced prior to the 18th Amendment, it neither covered the domain of the provincial borrowing autonomy enshrined in the 1973 Constitution of Pakistan, nor did it envisage any such possibility of inter-provincial supervision and control of national/federal debt management. Though it provides for transparency and semblance of accountability before the legislature; yet accountability to the interprovincial forum (like CCI) is still absent, despite lapse of 5 years to the 18th Amendment providing "Public Debt Management and Supervision" to be subject of the CCI being part of FLL Part II. The FRDL Act, 2005 is aimed at debt management being exclusive domain of the federal government. The Act provides for Debt Policy Coordination Office, which is part of the federal Finance Ministry so is technically less independent of monetary and fiscal policy frameworks under the control of the Ministry. Above all, debt data remains outside the control of this Office, which is the basic instrument of debt policy and decision making as well as of transparency and accountability.

ii. **FINANCE DIVISION:**

It regulates foreign commercial loans as well as domestic borrowing, alongwith the State Bank of Pakistan. Being arm of the federal government finances and financial arrangements, it dominates the national debt policy and decision making and carries over-whelming and predominant role in national debt regime. The CCI allowed it, in its meeting in 2011, to continue its borrowing policies and practices as it had been doing in the past, thereby sanctifying its centralized and exclusivist control of national debt regime.

iii. **STATISTICAL DIVISION:**

The General Statistics (Reorganization) Act, 2011 created the Pakistan Bureau of Statistics, repealing previous related laws and merging all related organizations; consequently, providing vast legal powers to the Bureau. Four members were to be taken to represent provinces, on the recommendations of provinces. Particularly, this law on statistics empowered and made the Bureau responsible for two major areas of statistical activity contributing to the assessment of GDP (whether national or provincial): population census and agriculture census. But owing to political exigencies this law could not be implemented effectively and substantially. This lack and absence of two major areas of censuses caused greater problems, distrust and tensions amongst federating units regarding the authenticity and accuracy of GDP assessment by the federal government, and even of the provincial GDP calculations by the provincial governments, while GDP is the sole basis and criteria for debt accumulation and allocation amongst federating units.

iv. EAD MANUAL:

It provides the Re-Lending Policy framework for the provinces intending for any sort of foreign financial assistance. The manual was updated till 2008, but attached Office Memorandum dates the Economic Affairs Division (EAD) lending practice to the year 1997; changes in the practice and procedure brought about later on are not reflected in the manual. Re-lending policy is a part of this manual which also needs to be revised besides the rest of the manual.

v. DEBT POLICY COORDINATION OFFICE (DPCO):

Its functions and responsibilities have been outlined in the FRDL Act, 2005. They include: preparation of debt reduction path, evaluation and guidance on borrowing strategies, monitoring and proposing ways to contain borrowing costs, analyzing and providing management framework against foreign exchange risks, providing information on public debt (domestic, external, government guarantees), preparing debt policy statement with trend identification, working on debt reduction path and suggesting adjustments, leadership on debt data and compliance, maintaining centralized, updated and electronic debt data. The DPCO organization includes three directors, two being professionals of debt and financial market; one of them is taken as Director General. Provincial debt regimes and inter-provincial participation is not provided in the design of this national debt regime.

vi. DEBT POLICY STATEMENT (DPS):

The FRDL Act, 2005 necessitates the DPCO to submit some policy statements to the legislature every year; the DPS being one of them, as disclosure and analysis or situation report on public debt. This is a part of the Global Debt Management Reform Programmes. Despite the CCI decision to oversee the “broader” debt policy in 2011, the DPS was directly submitted by DPCO to the legislature. The language of the report was highly technical; and the public debt appeared as national issue, instead of federal issue with federating units separately discussed and analyzed.

vii. MEDIUM-TERM DEBT MANAGEMENT STRATEGY (MTDMS) 2013/4-2017/8:

The MTDMS was also issued by the DPCO as per the requirement of the FRDLA, 2005 (and also part of the World Bank debt reform agenda). As is the case of DPS, public debt is a federal domain in the broader framework outlined by MTDMS. It does not provide for any guidance or parameters for the debt management strategies which may be adopted by the provinces. It is, in its spirit and contours, a national strategy.

3.2 Constitutional Arrangements for PDM: Council of Common Interests and National Economic Council

3.2.1 CCI and PDM

Created through the Constitution of Pakistan 1973, the Council of Common Interests was aimed at providing enhanced inter-provincial coordination, dispute resolution and participatory management (Zahid, 2013). Eighteenth Amendment to the 1973 Constitution added 10 subjects to the Federal Legislative List Part-II (Article 154 of the 1973 Constitution of Pakistan); greater space was added into the competence of the Council of Common Interests (CCI) in formulating and regulating policies pertaining to the subjects of the List. This included “Supervision and Management of Public Debt.” This subject has been introduced in the Constitution for the first time. Article 154 of the 1973 Constitution provides the function of the CCI that “the Council shall formulate and regulate policies in relation to matters in Part II of the Federal Legislative List and shall exercise supervision and control over related institutions”. Hence, the CCI responsibilities regarding “Supervision and Management of Public Debt” include: i) formulation and regulation of policies; ii) supervision and management of related institutions.

Scope and jurisdiction of the CCI extends to the supervision and management of public debt; this means that competence of the CCI encompasses: i) debt related policy formulation and regulation and, ii) supervision and control of debt related institutions. This necessitated fundamental transformation in debt regime of Pakistan. As a constitutional requirement, the CCI was required to lead the federal debt policy and debt institutions, transforming both from centralized executive activity to inter-provincial highly coordinated and consensual responsibility. The constitution required the CCI to provide with a federal/inter-provincial and participatory governance framework for debt policy and debt institutions, particularly when viewed from a perspective of devolved governmental functions, more development and service delivery related subjects were transferred to the provinces and therefore, the financing needs were expected to be not only being generated from the provinces but also being articulated from these provinces, instead of the federal government. This required massive and fundamental transformation in the way government had been financing its activities in centralized and exclusive manner, unaccountable to the provinces and unresponsive to the provincial demands and needs.

Historically, the borrowing had been the jurisdiction and domain of the federal government despite the concept and provision of the provincial borrowing autonomy in Article 167 of the 1973 Constitution. The federal government with its borrowing power, given through Article 166 of the Constitution, had been exclusive and unaccountable authority in borrowing for the country — for all tiers and levels of government, for public enterprises and for every project and programme. This activity was conducted through the federal Ministry of Finance. The debt policy was sole domain of the federal executive authority. The role of Finance Ministry grew in its overwhelming presence and ascendancy in the aftermath of the financial crises of 1990s and close collaboration with the World Bank and the IMF for programmes of macroeconomic stabilization, with dwindling of the role of Planning Division.

The Financial Responsibility and Debt Limitation Act, 2005 attempted to introduce transparency and accountability in the federal debt regime; debt emerged as a political issue, beside technical one: a political issue which concerns not only the stakeholders (borrowers and creditors and mediating agencies), but also the recurrent financial regional and global crises made it a concern of the public at large, besides the federating units of Pakistan. Internationally, the development agencies took up projects of debt regime reform, which included debt data and information systems, debt limitation legislation and incorporated the concepts of financial prudence and responsibility by the executive authorities engaged in debt negotiations and repayments, as well as the precepts of transparency and accountability before the legislatures and the public at large. The Act created Debt Policy Coordination Office (DPCO) with functions and objectives of developing debt reduction path, borrowing strategies, borrowing cost and risk evaluation, preparation and submission of debt policy statement to the legislature and maintenance of the centralized and updated record. In addition to this, the Rules of Business of the Federal Government provide that the function and responsibility of the EAD is to manage and supervise all matters related to the foreign financial assistance (i.e. external debt management), while Finance Ministry looks after external finance (commercial loans from international banks and other financial institutions) as well as domestic debt (from financial institutions as banks, national saving, etc. whether raised directly by the DPCO through auction process or arranged through the State Bank of Pakistan).

The 18th Amendment offered an opportunity to revisit the federal arrangements of centralized, executive controlled and exclusivist debt regime. The moment of transformation was however evaded. In 2010, the World Bank declined to further negotiate for loans immediately after the 18th Amendment as it considered that approval of CCI was mandatory constitutionally being authority for debt policy and regulation. The issue was taken up by the Finance Ministry with the CCI in its meeting on August 27, 2011 and reported in Case No. CCI. 4/4/2011 titled as "Public Debt Management and Supervision Policy". The Minutes state as follows:

> He (the Finance Secretary) stated that this entry in Part II (Public Debt Management and Supervision) of the Federal Legislative List and consequent exercise of jurisdiction by the Council of Common Interests needs to be clearly understood because in the presence of other constitutional provisions dealing with the subject of government borrowing and debt, there may be confusion that could create operational problems in the management of government business in the context of government borrowing and raising of debt (CCI, 2011: 8-9).

This ground provided the Finance Secretary an opportunity to relieve the burden of the CCI, as the minutes further provide: "…placing each proposal before the Council will not only overburden the Council but also hinder the borrowing process". Therefore, the Finance Secretary forwarded the proposed role and function for the CCI in the following words: "… the

Council of Common Interests would oversee the overall policy for debt management and supervision within the broad parameters imposed through legislative actions of Parliament" (CCI, 2011:9). He did neither provide the constitutional and legal sources of confusion, nor proposed any framework for "overall" policy and the "broad" parameters; nor even was provided any time-frame for such blanket approval of CCI for continuing the pre-18th Amendment executive control of debt management, against the letter and spirit of the constitution. Neither the CCI annual reports reveal the issue being taken up afterwards, nor placing of supervisory mechanism, as was proposed and agreed by the participants of CCI Meeting.

The CCI decided, as provided in the Minutes, that: i) The transactional business of federal government with respect to borrowing from domestic and foreign sources would continue as in the past; ii) The overall debt management policy will be approved by the Council of Common Interests within the parameters imposed by Parliament; iii) The Council of Common Interests will be regularly briefed on the progress of implementation of the approved policy; iv) The Council of Common Interests will also be briefed regularly on the overall state of public debt and its analysis from the perspectives of debt sustainability, cost of debt, sources of debt and efficient management of debt; and v) the policy statement containing objectives, scope, present position of domestic and external debt and medium term macro-economic framework proposed in different borrowing options, subject to consultation with the provinces.

As aspired by the Parliament through its 18th Amendment, the CCI could not emerge as a leader and as a forum of participation and consensus for inter-provincial as well as federal debt policy and institutions. As a result of the decision, neither debt policy is approved by the CCI in any format and template, nor the CCI is shown as a debt policy forum or a channel through which DPCO's Debt Policy Statement is presented before the legislature. Above all, even if the decisions of the above said meeting still left some scope of the CCI in leading debt policy and institutions in a reformed federal manner, its capability to undertake such leadership role could not have matched the expectations. The FRDL Act, 2005 and functions of the DPCO which require amendments in light of the above decisions making DPCO and debt policy and debt institutions, *broadly and within parameters*, responsive to the CCI.

Though the CCI was created by the 1973 Constitution, its rules of procedure and practice were however framed in 1991 and revised only in 2010. It remained un-functional and unutilized forum, owing to many interventions in the Constitution and political changes: it was put in abeyance in 1977 by the martial law and its federal spirit changed with the 8thAmendment in 1985; while it was given *quasi*-presidential form in 2003 through the 17th Amendment. In 37 years' span from 1973 to 2010 up till the introduction of the 18th Amendment, only eleven meetings of the CCI were held; while only after that, 16 meetings have been held till August 31, 2015 (CCI is required to meet at least once in ninety days): it met thrice in 2010, four times in 2011, thrice in 2012, thrice in 2013, twice in 2014 and once in 2015. Independent Secretariat has also plagued the capability issue of the CCI.

Nevertheless, the Prime Minister of Pakistan made the CCI and the IPC independent of the Cabinet Division and allocated them to IPC Division, the summary of the independent secretariat of the CCI had reportedly been returned to the IPC Division by the PM without making any advance on the subject. This also has adversely affected any leading role and initiative by the CCI regarding the development of the PDM framework in the provinces, as inter-provincial concern, focusing and emphasizing concepts of financial and fiscal prudence and responsibility as well as standards in the debt reform organizations in the provinces. Provincial governments have themselves not looked back to their concurrence to the proposal of the Finance Secretary which provided ground for the CCI decision as discussed above. The public debt management and supervision appears to be a low priority subject for those leading provincial/inter-provincial federal relations, which may hamper the development of fiscal federal arrangements towards effective provincial autonomy and participation in critical fiscal decisions, such as public debt.

This does not mean that provinces are completely blacked out from debt policy and institutions. Provincial participation and engagement with the EAD debt processing (both debt negotiation as well as debt repayment) are regular phenomena. Through the Re-Lending Policy of EAD provided in EAD Manual and its office instructions: debt arrangements for the provinces from donors (multilateral/bilateral) aimed at loans including both project and programme loans; participation of provincial departments (finance, P&D, concerned department as Education) is pre-requisite of borrowing process in each loan. Besides this, provincial participation in debt policy is also ensured through their contribution for the Debt Policy Statement, required to be submitted to the legislature annually on the occasion of Annual Budget of the Federal Government. However, provinces have not been able to evolve any informal mechanism to make the Federal Government accountable or responsive regarding the critical nature of debt policy and its highly centralized debt institutions.

The Federal Government failed to provide for enabling environment for the development of provincial PDM. So far there have never been any support to provinces for debt related and particularly debt management related legislation, drafting of rules and procedures, establishment of new and independent debt management organizations with debt specialists, capacity building of debt staff, and introduction and implementation of debt management related information, reporting and risk management system. The DG and the DPCO were unaware of constitution or unwilling to consider constitutional requirements related to the PDM as an FL2 subject. He was also unwilling to take initiative and extend technical support to provinces in the PDM.

Federal/Provincial Debt Conferences could have been potential mechanism of making debt policy inclusive and consensual from the very scratch i.e. before initiating debt arrangements with creditors and donors for the upcoming financial year; such debt conferences could have been held annually before the budget, or else even bi-annually, as one to formulate the annual debt policy and other in mid of the year to evaluate and assess the progress of the on-going debt policy. But there is not any such mechanism evolved yet, either from the Federal

Government, or from the CCI and the provincial governments. There is no other measure/effort taken or mechanism adopted for the provincial engagements and their participation in policy making regarding debt decisions by the Federal Government This requires the evolution of annual debt policy as political debate, independent of other fiscal and financial policy areas, besides extending the debt politics beyond the corridors of executive offices, and bringing it to the forum of Parliament. Some third world countries have laws regulating every debt arrangement with creditors and donors, up to a particular amount or percentage of GDP, by bringing it to the domain of the approval of the Parliament, and not even the forum like the CCI, which makes many prospective debt arrangements being disapproved by the Parliament and thus curbing imprudent and irresponsible financing practices of the executive authorities, and also making the debt management more inclusive, participatory and consensual.

Provinces could develop their own mechanism of inter-provincial decision making in their respective jurisdiction and domains of FL2 Subjects. Though available in the form of CCI, yet informal conferences on budget and finance related matters are held in federalist countries like Canada. Debt is a joint and shared responsibility for many reasons: debt management is provincial subject; major spending subjects are responsibility of provinces; in absence of formalized provincial arrangements for the PDM, informal and intergovernmental fiscal conferences can help provinces develop their arguments and concerns in more articulate and convincing ways. But the provincial governments also have not taken any joint measure, mechanism and effort to make federal government’s debt decision more aligned with demands and needs of the provinces.

An analysis of the debt stock accumulated during 2011-2015 and the PDM shows that eighty percent of the PML-N government taken debt domestically and internationally meant for macro-stabilization and was raised in the name of water and sanitation or similar infrastructure development claims. Since the professed purpose was basically the domain of provinces and provinces already were in fiscal surplus in those subjects, the debt raised hitherto mainly lacked federal demand and for that reason any need for consensus.

3.2.2 NEC and PDM

The National Economic Council (NEC) was created originally in the 1956 Constitution along with the National Finance Commission (NFC) and continued through the 1962 and 1973 Constitutions. Basic task of the NEC in the 1956 Constitution was to review the overall economic position and formulate plans for financial, commercial and economic policies. This task continued in the 1962 Constitution. After insertion of clause 4 of the Article 167 of the Constitution of Pakistan 1973, the NEC has got a very crucial and critical role in setting and determining limits of provincial borrowing whether domestic or international. The NEC has therefore become central to the PDM, as not only debt quota determining office, rather coordinating with provinces and the Federal Government in the process of determining the provincial debt limit. The NEC has recently allocated provincial debt quota or debt ceilings, aimed at raising domestic debt, for the first time, through its decision in the meeting held on

June 1, 2015, on the summary sent to it by the CCI as it decided in its meeting on March 18, 2015. The Finance Ministry has communicated this NEC decision through its letter (Debt Policy and Coordination Office' letter dated June 16, 2015) which states that:

> i)-the federal government will continue to assist provinces to receive support from development partners such as the World Bank, the Asian Development Bank and bilateral sources. Since these loans are contracted by the federal government, they are counted in the federal indebtedness, and no additional burden on overall debt/GDP is entailed;
>
> ii)-despite limitations of available fiscal space, a symbolic start of allowing provincial borrowings should be started. Accordingly, provinces are allowed a domestic borrowing limit of 0.5% of GDP (or Rs.153 billion) after excluding domestic loans of Rs.40.4 billion owed to the Federal Government. This will mean a net limit of Rs.112.6 billion
>
> iii)-The limit specified in (ii) will be distributed among the provinces as per their relative share in the divisible pool which is as under:

TABLE: PROVENCIAL BORROWING LIMIT AS PER THEIR SHARE

Provincial Debt Limit Rs. in billion					
Area	Punjab	Sindh	KPK	Balochistan	Total
Net Available Limit	61.75	20.05	16.88	13.91	112.59

However, no framework for the NEC has yet been outlined for its operations under Article 167(4) of the Constitution of Pakistan 1973, which determined the role of the NEC through the 18th Amendment. It appears that practice and precedent are considered sufficient as substitute of such framework.

4. PROVINCIAL PDM FRAMEWORKS AND INTERGOVERNMENTAL DEBT POLITICS

4.1 Overview of the Existing Provincial PDM Framework

The Provincial Debt Management regime has continued to be traditional in its organization and has remained largely without reform, except the initiation of debt management reform programme in Sindh government by the World Bank starting in 2014. The reform initiative is expected to move to the rest of the provinces as well, and the World Bank's technical assistance is focused on advising the provincial governments for hiring, organizing, capacity building of the staff and debt data management. Still much work is required to be done by the provincial governments at their own initiative and pace.

All the provincial governments need to work out some critical areas for an effective debt management framework such as legislation and legal framework, organizational design with specialist staff and market based incentive structure and work environment, determining and notifying rules and roles, building capacity of the existing and newly hired staff, implementing and developing debt database and debt management and financial analysis system for effective reporting, transparency and accountability before legislatures, supreme audit institutions and the public at large. But none of these can be developed and sustained in the absence of a Federal Government and its debt management framework to provide harmonization of the provincial debt management, let alone the absence of Council of Common Interests for over-arching role in collaborating and synergizing the efforts of provincial debt management frameworks, besides providing for debt management standards and norms to help evolve national outlook in debt management.

4.1.1 Provincial PDM in Punjab

Interviews of incumbent and ex-officers of the Finance and P&D departments as Additional Secretary Finance Punjab Kamran Rashid Khan, Zaighuam Abbas Baloch, ex-Deputy Secretary, Babur Rashid were conducted telephonically as well as during visit of the Punjab Secretariat, Lahore. The following offers a pen picture of the interviews and the data provided by the officers, mainly government publications on the issue.

White Paper on the Budget, 2015-16, Government of the Punjab reflects the debt stock of the Punjab Government to be Rs. 457, 982.885 million as on 30-06-2015; while domestic share in the total debt stock is Rs. 21,851.171 million and share of the foreign debt is Rs. 436,131.714 million (Government of the Punjab, 2016). The interviewees revealed that provincial governments have been getting three kinds of loans from the federal government: foreign, domestic and budgetary supports. The last ones are not repaid. For the first two, there is an agreement against each loan for three to five years period.

The provincial governments participate in the loan negotiation and loan repayment. Loan negotiations on the foreign borrowing for the provincial governments are conducted through

Economic Affairs Division (EAD), responsible for all foreign assistance related borrowing. With the approval of the Chief Minister of the Province, the provincial departments of Finance and Development, Planning and Development, concerned borrower department, Law Department organize for the loan negotiation, to be dealt and held by the EAD with development donors- multilateral or bilateral. Each department is responsible for its role in the negotiations. Law department is concerned with loan agreement; Finance department concerns the cost of borrowing; the concerned borrowing department deals with the project papers and its phasing attached with disbursement schedule or amortization schedule. The project papers include DLIs (Disbursement Linked Indicators) against the achievement of which disbursements are made by the donors. Therefore, agreed and disbursed amounts differ in almost all cases of borrowing.

There is finance agreement with amortization schedule and phasing in each case of borrowing; according to this, on reporting of the EAD, Federal Finance Ministry deducts a part of the principal and the cost of borrowing from the federal transfers to be made to the provinces. Loan related accounts are maintained according to Charts of Accounts in New Accounting Model (NAM) and the rules for the same have been provided in the Revised Accounting Procedure for Revolving Fund Accounts (Foreign Aid Assignment Account) issued by Finance Division on August 2, 2013. This provides accounting procedure at the national level for the foreign borrowing in different development projects and programmes.

The interviewees revealed that Loan Section in Finance Department and Foreign Debt Section in P&D departments supervise matters related to the borrowing through the Federal Finance Ministry. The P&D department coordinates for development finance with the EAD on behalf of the provincial government. The Loan Section is part of Resource Wing in provincial Finance department. It is responsible for managing provincial borrowing through the federal government. A section officer heads the Loan Section. The debt data is managed on individual MS Excel Sheets on PCs in the section. One page printouts are placed in the relevant files of the borrowing cases. Therefore, the data is neither consolidated nor reconciled, nor even is easily accessible for reporting and analysis, so is eventually unavailable for holistic policy and decision making process. Existing job description of the Loan Section includes foreign aid cases (their receipt monitoring, debt servicing, reconciliation with the EAD, borrowing related accounts), preparing related budget estimates, dealing with loans and advances to various agencies in the Province, loans and advances to financial/non-financial institutions, and even loans to government servants. This all is managed in a way which is very rudimentary, disorganized and individual based. The Punjab Government *Rules of Business, 2011* provide for Finance Department to be responsible for:

A- Legislative/Financial Management:- Management, Supervision and control of the Provincial Consolidated Fund and Public Accounts of the Province and matters connected therewith or ancillary thereto including but not limited to;

B- All loans and moneys received as repayment of loans:- Management, supervision and control of public debt;

C- Borrowing, lending, guarantees:-With the implementation of debt regime reform, it's clear objectives, roles and functions, rules of procedure and practice, mandatory reporting and planning, and parameters of performance evaluation and audit need to be the part of the reform process.

Reform of debt organization and management in the government of the Punjab is in the offing, and not a distant dream. On the one hand, the World Bank has taken up a project of debt management reform, initiating the process from Sindh government and to be extended to other provinces. The interviewees revealed that Punjab would be six months behind Sindh government's initiative of a reformed organization for managing debt, as the World Bank Debt Support Programme would roll out to the Punjab government soon.

Moreover, Punjab government officials are participating in the World Bank capacity building programme conducted in Sindh. On the other hand, the interviewees have also informed that the Chief Minister of the Punjab government has been given a presentation of the reformed Debt Management Unit, besides proposals for legislation and rules of procedure. However, the officers declined to share with the researcher any further detail of the summary sent to and the presentation made before the Chief Minister in this regard. This places hope in the process of reform of debt organization, independent from the Finance department and its traditional working and structure. Still, questions as to the proposed legislation regarding provincial debt regime of the Punjab government and the role of the federal government and its debt management and of the Council of Common Interests comes to fore for lack of substantial input and participation in the process of interprovincial debt governance framework.

4.1.2 Provincial PDM in KP

Interviews with the incumbent Additional Secretary Finance Department KP Mr. Kamran Rehman Khan and some ex-officers of the Finance Department were also conducted. The interviewees revealed that the reformed debt unit was in the offing, though existing one was working with manual registers for debt data purposes, and not even individual MS Excel Sheets on PCs. Additional Secretary shared the information that legislation was also in the pipeline for the reform debt regime in KP, yet the details or the main features of the same were not shared with the researcher.

4.1.3 Provincial PDM in Balochistan

Additional Secretary Pervez Nausherwani, DS Finance Lal Jan Jafar and some ex-officials were interviewed telephonically. They reported that though existing organizational structure of Resource Wing heading the Loan Section within the Finance Department continues working the matters of provincial borrowing in Balochistan, the section has worked tremendously regarding the loan repayments in recent years. According to them, the organizational structure, rules of procedure and practice, incentive structure and skill level continue to be the same as in KP or Punjab government. Interviews revealed that even though the World Bank has taken up the project of Debt Management Support Programme, the urgency and critical need for the debt management reform are only remotely sensed. Euphoria of provincial fiscal surplus and the achievement of significant loan repayment formed central themes of the interviewees' narratives.

4.1.4 Provincial PDM in Sindh

Interviews were conducted with Kher Muhammad Kalwat (Additional Secretary, Finance Department Sindh) and Kashif Sheikh (Financial Analyst). Mr. Kher Muhammad Kalwat revealed that the Sindh government has established a reformed organization for the debt management purposes, with the support and initiative of the technical assistance of the World Bank. The newly established Debt Management Unit (DMU) has organizational structure of Additional Secretary Resource Wing (Finance Department) heading one Special Financial Assistant who will supervise two Financial Assistants. The Financial and Special Financial Assistants have been hired for the special debt management tasks with relevant field specializations. In Sindh, Additional Secretary Resource Wing is supervised by Special Secretary (Budget). The whole organization is led by the Secretary Finance Sindh.

The interviewees revealed that the Debt Management Unit (DMU) was established with the technical support of the World Bank, which launched this project in 2014. The activities so far conducted in the project include establishment of new organization in the Sindh Government, hiring of specialist staff, training of staff (both newly hired and existing one). The DMU has started its work by collecting data concerning reconciliation of debts and related matters pertaining to the period up till June 30, 2015. Interviews revealed that at present, the debt data in Sindh government is being maintained on individual MS Excel Sheets for each year and each debt activity separately, specifying debt and interest of the year in particular activity or project. Though each debt has corresponding credit memo, still it does not specify as to which loan is it about and for what interest and commitment charges etc. The debt data is neither reconciled nor integrated, nor is easily accessible for reporting and analysis. Crucial policy and decision making components of reporting and analysis are, therefore, missing in the existing environment which DMU aims to reform. Resultantly, there is no possibility of debt and finance related advice and consultation based on debt related analysis in the present scenario.

Data base of the DMU is in the pipeline for development on the basis of this reconciliation of data, aiming to reform the present data and financial analysis and reporting situation. The DMU also aims at developing the borrowing plan particularly in the wake of allocation of debt ceilings to be raised, if required, by the Sindh government. The DMU also aims at working out and developing provincial debt strategy and policy. The officials of DMU hope that the Sindh Finance department and Planning and Development (P&D) Departments would consult the DMU in making decisions about loans, whether domestic borrowing or international through the EAD re-lending negotiated with development partners such as the World Bank and the Asian Development Bank etc. However, the interviewees revealed that not only there is no spade work so far done in the area of provincial legislation for a well thought out provincial debt regime, but also still there have not been officially notified rules of practice and procedure specifying roles and functions of the DMU staff and the DMU organization. Absence of legislative and legal framework is feared to dampen the development of debt governance regime in the province, even though Sindh government has by far the most advanced government in taking initiative towards the development of an independent and specialized debt management framework when compared with rest of the provinces.

4.2 Intergovernmental Debt Politics

Some issues can emerge as part of debt politics in the intergovernmental fiscal relations:

i. Debt Accountability: Debt accountability of the federal and provincial governments need to be brought in the debt legislation and rules and procedures related to debt management, as incentives for riskier and costlier debt raising by the debt managers and decision makers can neither be over-ruled nor even be over-emphasized. Debt defaults are not exceptions and decision makers of the debt regimes in developing countries cannot be complacent with the existing mechanisms available for ensuring debt discipline;
ii. Debt Distribution and Limitation: Delays in debt distribution and debt limitation have been experienced, as the Minutes of the 2011 CCI meeting on public debt management reveal that the provinces have been anxiously waiting for the distribution of debt limits and quotas, which only was finalized in June 2015 and no province has been able to raise even that allocation of debt, by the time this report was being finalized. Reasons may abound: provincial fiscal surplus as well as debt management organization;
iii. Transparency: Access to information on public debt will grow with particular reference to over secrecy and public and provincial demand for debt data. Transparency in raising exponential debt by the federal government particularly when the development and service delivery domains have been largely and overwhelmingly devolved to the provinces and the provincial debt demand has also not grown, in view of the small size of absorption capacity in development sectors as well as provincial fiscal surplus. The federal government is alleged by many quarters to be raising loans mostly for macroeconomic stabilization, but in the name and pretext of provincial development subject as water (irrigation, sanitation, etc.). Moreover, fiscal surplus myth has also been deplored by some, as surplus is reportedly created by the federal government which persuaded the provincial governments in the aftermath of the 7th NFC Award to invest fiscal and financial “surplus” in the federal government bonds. Transparency is an upcoming concern of federal debt politics;
iv. Cost of borrowing (short term borrowing vs. medium and long term borrowing);
v. Provincial debt competition, debt defaults and federal bailouts- commitment principle;
vi. Legislation, institutional and HR/staff capacity challenges of the provinces.

Under this whole scenario it becomes clear that all the provincial governments need to work out some critical areas for an effective debt management framework such as legislation and legal framework, organizational design with specialist staff and market based incentive structure and work environment, determining and notifying rules and roles, building capacity of the existing and newly hired staff, implementing and developing debt database and debt management and financial analysis system for effective reporting, transparency and accountability before legislatures, supreme audit institutions and the public at large. Only then the public debt can be managed and supervised properly, in a workable collaboration between the federal and provincial governments.

5. POLICY CHALLENGES, CONCLUSION AND POLICY RECOMMENDATIONS

5.1 Policy Challenges

1. Provinces to assess their regional/provincial GDPs as debt limits in FRDL Act, 2005 and the NEC provincial debt limits are GDP based. Problems and challenges faced in this respect include provincial assets, incomes transferred from one province to other, economic activities in one province while registration and recording in other provinces for different reasons (tax structure being one of them), etc.; the prime most need will be population and agriculture census which poses its own peculiar provincial challenges in terms of political as well as economic concerns of different groups in the provinces. Economists, coming from different political, ideological and geographical backgrounds, also differ on even the definitions, meanings and measures of public debt and GDP, the basis on which debt-fiscal space is measured and granted to the provinces for raising debt by the federal and provincial governments. The availability of data—accurate and trustworthy—for determination of the GDP and debt is also a source of concern for the provinces. The assessment of provincial and regional GDPs is not only a provincial challenge it is also a challenge for the federal government. It has to develop some institutional mechanisms, legal and operational framework, capacity building of the concerned organizations and their staff, and some standards and benchmarks based upon national and federal consensus in line with the international best practices.

2. Similarly, provinces also need to assess their revenue, prospects for effective revenue mobilization can influence and shape their policy and decision about debt according to revenue mobilization scheme of the NFC Awards. This poses serious challenge as provinces have neither been able to mobilize effectively their traditional tax base, rates and structures (such as property tax, tax on services, tax on agriculture income etc.), let alone developing tax strategy and policy for the domains and subject allocated to them through 18th Amendment. This area has also not witnessed serious attention of provincial governments, mainly as an outcome of the 7th NFC Award placing most provinces in surplus fiscal space. Introduction and implementation of provincial tax reform is perhaps one of the biggest challenges that the 18th Amendment has posed to the provinces and yet least attended and invested domain for the provinces. This is essential for effective, though limited, provincial fiscal autonomy in future. Failure of the provincial governments so far in this regard poses serious challenge to the effective and substantive development in the federal arrangements in Pakistan.

3. Provincial legislation is another challenge faced by independent debt raising effort. The federal legislation regarding debt and financial responsibility was enacted in 2005, prior to 18th Amendment. Even though provincial borrowing autonomy was already provided in the Constitution in its Article 167, yet the federal legislation did not presage the developments and political culture changing after 18th Amendment and 7th NFC Award. FRDL Act, 2005 continues to be central in its nature, as debt management devolved, provincial legislation for debt management as provincial subject as well as for organizing debt related activities once earmarked to provinces to raise debt domestically by themselves and within the province has become a political challenge. Besides legislation, there is a challenge of developing rules, practices and procedures developing manuals and operational dos and don’ts for raising debt domestically by the province.

4. Debt management reform at provincial level is political, economic, organizational as well as a technical challenge faced by the provinces. As so far only Sindh government has taken steps to introduce independent provincial debt management office, other provinces remain much behind in this respect even. But a broader level organizational change and institutional development call for comprehensive Debt Management Reform Programme in provinces. The federal government shares the responsibility with the provincial governments in lack of such reform programme and therefore can substantively contribute to develop such reform programme for provinces and with the support and demand of provinces taking the IPC/CCI in productive dialogue and engagement in carving out the reform agenda for provincial debt management reform. The federal government can also seek support of the interested donors having long expertise in public debt management reform in third world countries. Federal initiative, particularly, cannot be overlooked or obviated when NEC has earmarked the limits of debt to be raised by provinces domestically. Moreover, the complexity and dynamic nature of financial and debt markets world over, besides domestic debt market in Pakistan, the path-shaping role of the federal government becomes even more urgent and pre-requisite in providing ground for debt management reform to the provinces that are in their infancy of learning fiscal autonomy, though within a host of constraints and limitations. Absence and even apathy of the federal government’s path-shaping role in this regard, as exhibited by the senior officials of Finance Ministry, may negatively affect and even cause distortions and create financial risks, which may later on become liabilities for the federal government, as only the federal government bears the responsibility for sovereign guarantee for the loans raised and lent by the provincial governments. The CCI also needs to play its role in urging the federal government for taking initiative towards the development of debt management reform agenda.

5.2 Conclusion

The public debt is still being managed and supervised, not only primarily but predominantly, even if not exclusively, by the federal government. This arrangement has support and sanctity of the CCI through its 2011 decision. Though provinces lack willingness as well as capacity in steering the national debt management regime, let alone their own provincial PDM, the federal government is also lacking any initiative. Further, mentoring the role for development of a federal debt regime within which provincial and interprovincial players participate for a cause of influencing and shaping decisions regarding future debt policy. This requires federal driven financial and technical support programmes, besides the donor driven ones, for the development of inter-provincial PDM related legislation (with provincial laws as well as amending the federal fiscal responsibility and debt limitation law), debt data and reporting, debt management strategies and interprovincial transparency and accountability mechanisms.

The PDM can provide a fertile ground for more participatory and consensual decision and policy making in the evolving relations of the federation of Pakistan.

5.3 Policy Recommendations

1. Assess provincial GDPs by developing legal, institutional and operational framework.
2. Assess provincial revenues—structure, base, rates and enforcement, by introducing comprehensive tax reforms.
3. Introduction of provincial legislation, rules, procedure and operational framework and standards and manuals.
4. Provincial debt management reforms.
5. Debt advisory committees with specific scope and mandate—one based in each province and a broader one based in the CCI.
6. Broader public access to debt related data through annual debt analysis reports and studies.

List of Interviewees:

1. Ehtsham Rashid
2. Imranullah Khan
3. Sabz Amin
4. Anwar Sheikh
5. Amjad Farooq Bhatti
6. Zafrullah Khan
7. Kamran Rashid Khan
8. Dr. Parvez Nausherwani
9. Lal Jan Jafar
10. Kher Muhammad Kalwat
11. Kashif Sheikh
12. Zaighuam Abbas
13. Kamran Rehman Khan

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