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**Public Financial Management Reform in the Middle East and North Africa:  
An Overview of Regional Experience**

**Part I  
Overview and Summary**

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## **Abstract**

This report surveys the experience of Middle East and North Africa countries on the topic of public financial management reform. Drawing upon a variety of sources, including Public Expenditure and Financial Accountability (PEFA) assessments, Country Financial Accountability Assessments, Public Expenditure Reviews, and other documents and reports—and augmented as necessary by interviews with leading reformers—the report seeks to address several major questions. How do MENA countries compare with other comparable countries at similar levels of development with regard to their PFM systems and practices? What has been the substantive content and thrust of PFM reforms in MENA over the last decade? Where have these reforms done well, and where have they struggled? What were the key ingredients for success or failure? Are there lessons in how these reforms were implemented that will be of value to other countries and the donor community?

## Abbreviations

ACCT	Treasury Central Accounting Unit (Algeria)
AfDB	African Development Bank
AFMIS	Accounting-based Financial Management System
AGES	Automated Government Expenditure System
AP	Autorisations de Programme
ARABOSAI	Arab Organization of Supreme Audit Institutions
ASOSAI	Asian Organization of Supreme Audit Institutions
BCC	Budget Call Circular
BdL	Central Bank of Lebanon
BSA	Board of Supreme Audit (Iraq)
BSMP	Budget System Modernization Project (Algeria)
CACI	Central Inspection Agency (Syria)
CAO	Compliance Advisor Ombudsman
CBE	Central Bank of Egypt
CBI	Central Bank of Iraq
CBY	Central Bank of Yemen
CDR	Council for Development and Reconstruction
CFAA	Country Financial Accountability Assessment
CGED	General Control of Expenditures Commitment
CGSP	Public Services Audit Office (Tunisia)
CIB	Central Inspection Board (Lebanon)
CMU	Cash Management Unit
CNED	National Fund of Equipment for Development
CoA	Chart of Accounts (Jordan)/Court of Accounts (Lebanon)
COCA	Central Organization of Control and Audit (Yemen)
COFC	Central Organization for Financial Control (Syria)
COFOG	Classification of the Functions of Government
COG	Central Government
COI	Commission of Integrity (Iraq)
COR	Council of Representatives (Iraq)
CP	Credits de Paiement
CPA	Coalition Provisional Authority (Iraq)
CPAR	Country Procurement Assessment Report
CPI	Corruption Perception Index
CPIA	Country Policy and Institutional Assessment
CSMP	Civil Service Modernization Project (Yemen)
CST	Central Sales Tax
DA	Algerian Dinar
DB	Budget Directorate
DFID	Department for International Development (United Kingdom)
DGCP	General Directorate for Public Accounting (Tunisia)
DMFAS	Debt Management Financial Analysis System
DPL	Development Policy Loan
DPM	Deputy Prime Minister
DPPR	Development Plan for Poverty Reduction

DPR	Detailed Project Report
EC	European Commission
EdL	Electricité du Liban
EFMIS	Emergency Fiscal Management Reform Implementation Support
ESW	Economic and Sector Work
EU	European Union
FAD	Fiscal Affairs Department
FE	Forward Estimate
FMIS	Financial Management Information Systems
FRR	Revenue Regulation Fund (Algeria)
FY	Fiscal Year
GBD	General Budget Directorate (Jordan)
GBO	Budget Management by Objectives (Tunisia)
GCC	Gulf Cooperation Council
GCF	Financial Audit Office (Tunisia)
GDDS	Government Data Dissemination Standard
GDP	Gross Domestic Product
GFSM	Government Finance Statistics Manual
GFMIS	Government Financial Management Information System
GFS/COFOG	Government Finance Statistics/ Classification of the Function of Government
GID	Integrated Expenditure Control System
GoE	Government of Egypt
GoI	Government of Iraq
GoJ	Government of Jordan
GoL	Government of Lebanon
GoY	Government of Yemen
GPC	General Party Congress (Yemen)
GTZ	German Technical Cooperation
GU	Governmental Unit
HCCAF	High Commission for Administrative and Financial Audit (Tunisia)
HIPC	Heavily Indebted Poor Countries
HRC	Higher Relief Commission (Lebanon)
ICI	International Compact for Iraq
ICR	Implementation Completion Report
ICRG	International Country Risk Guide
ID	Iraqi Dinar
IDA	International Development Association
IDF	Institutional Development Fund
IFMCA	Institutional Financial Management Capacity Assessments
IFMIS	Iraq Financial Management Information System
IGF	Inspectorate- General of Finance
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standards
ISDT	Income and Sales Tax Department

ITD	Income Tax Department
ITF	Iraq Trust Fund
JD	Jordan Dinar
KRG	Kurdistan Regional Government (Iraq)
LOLF	Loi Organique Relative aux Lois de Finances (Morocco)
LTO	Large Taxpayer Office
MDCI	Ministry of Development and International Cooperation (Tunisia)
MDG	Millennium Development Goals
MED	Ministry of Economic Development
MEF	Ministry of Economy and Finance (Morocco)
MENA	Middle East and North Africa
MMSP	Ministry of Public Sector Modernization (Morocco)
MOF	Ministry of Finance
MOH	Ministry of Health
MOLA	Ministry of Local Administration (Yemen)
MOP	Ministry of Panning
MOPDC	Ministry of Planning and Development Cooperation (Iraq)
MOPIC	Ministry of Planning and International Cooperation
MSAD	Ministry of State of Administrative Development (Egypt)
MTEF	Medium Term Expenditure Framework
MTFF	Medium Term Fiscal Framework
MTO	Medium Taxpayer Office
NGO	Non-Government Organization
NFTI	National Fiscal Training Institute
NRA	National Reform Agenda
NSSF	National Social Security Fund
OBL	Organic Budget Law
ODPM	Office of the Deputy Prime Minister
OECD	Organization for Economic Cooperation and Development
OPM	Office of the Prime Minister
PA	Palestinian Authority
PAL	Public Accounting Law (Lebanon)
PARL	Public Administration Reform Loan
PARP	Public Administration Reform Program
PCSC	Complementary Plan for Support to Growth (Algeria)
PDD	Public Debt Department
PEFA	Public Expenditure and Financial Accountability
PEIA	Public Expenditure and Institutional Assessment
PEM-TA	Public Expenditure Management - Technical Assistance
PER	Public Expenditure Review
PFM	Public Financial Management
PFMAU	Public Financial Management Advisory Unit
PIF	Palestinian Investment Fund
PIU	Project Implementation Unit

PLC	Palestinian Legislative Council
PPP	Purchasing Power Parity
PRDP	Preparation of a Development Plan
PSA	Production Share Agreement
PSR	Public Sector Reform
ROB	Results-Oriented Budgeting
ROSC	Report on the Observance of Standards and Codes
SAACB	State Audit and Administrative Control Bureau (West Bank & Gaza)
SAI	Supreme Audit Institutions
SDDS	Special Data Dissemination Standards
SIGIR	Special Inspector General for Iraqi Reconstruction
SOE	State Owned Enterprise
SONATRACH	Société Nationale pour la Recherche, la Production, le Transport, la Transformation, et la Commercialisation des Hydrocarbures s.p.a. (Algeria)
SNG	Sub-National Government
SPC	Special Planning Commission (Syria)
STA	Special Treasury Account
STD	Sales Tax Department
SU	Spending Units
TGR	Kingdom General Treasury (Morocco)
TSA	Treasury Single Account (Egypt)
UNCAC	United Nations Convention Against Corruption
UNDP	United Nations Development Program
U.S.AID	United States Agency for International Development
VAT	Value Added Tax
WBG	West Bank & Gaza
WGI	World Governance Indicators
YER	Yemeni Riyal

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## Table of Contents

<b>Acknowledgements .....</b>	<b>i</b>
<b>Executive Summary .....</b>	<b>ii</b>
<b>Chapter 1 .....</b>	<b>1</b>
<b>Introduction: Public Financial Management Reform in MENA and Beyond .....</b>	<b>1</b>
The Importance of Public Financial Management .....	1
Beyond MENA: The Lessons from Global Experience .....	2
What is “MENA”? Selecting the Countries for this Study .....	3
Using the PEFA Ranking to Evaluate PFM in MENA .....	5
Where MENA has Ranked Consistently Higher .....	8
MENA Country Templates and Case Studies on PFM Reform .....	11
<b>Chapter 2 The Substance of Public Financial Management Reform: What Reforms are Needed and Which are Working? .....</b>	<b>13</b>
1. Strategic Budgeting .....	14
Macro-Fiscal Capacity .....	14
Medium Term Perspective .....	15
Budget Integration to Improve Resource Allocation .....	16
2. Budget Preparation .....	18
Broadening Budget Coverage .....	18
Improving Budget Transparency and Classification .....	19
3. Resource Management .....	21
Treasury Operations .....	21
Reforms in Tax and Customs Administration .....	23
Procurement Reform .....	24
4. Internal Control and Audit .....	25
Developing Expenditure Controls .....	25
Strengthening Internal Audit .....	27
5. Accounting and Reporting .....	29
Accounting Policy Reforms .....	29
Introducing a Performance Focus to the Budget .....	30
6. External Accountability .....	32
Strengthening External Audit .....	32
<b>Chapter 3 Implementing Reforms in Public Financial Management: An Emerging Set of Promising Practices in MENA? .....</b>	<b>34</b>
How Important is Implementation to the Success of MENA’s PFM Reforms? .....	34
Lesson 1: Know the Value—and Limitations—of Political Economy Analysis .....	37
Lesson 2: PFM Reform as Means and Not Ends .....	39
Lesson 3: Context Matters, so Swim with the Current .....	39

Lesson 4: The Wisdom of “Muddling Through”—Grand Strategy versus Incremental Change.....	41
Lesson 5: Establish Basic Systems before Contemplating More Advanced Reforms...	42
Lesson 6: When Possible, Keep Reforms Quick, Simple and Mutually Reinforcing ...	44
Lesson 7: Be Wary of Large Financial Management Information Systems .....	46
Lesson 8: Internal Challenges: Leadership, Coordination, Skills and Incentives.....	48
Lesson 9: External Stakeholders—Useful, but Don’t Count on Them .....	52
Lesson 10: Lessons for Donors: Be More Strategic, Selective, Modest and Flexible ...	53
<b>Appendix.....</b>	<b>58</b>

## **TABLES**

Table 1: Breakdown of Successful and Challenging PFM Reforms in MENA .....	ix
Table 2: Basic Statistics on MENA Countries Selected for PFM Analysis .....	4
Table 3: PEFA Scores for the MENA Countries in the Study.....	10
Table 4: Relevant PEFA Scores for Strategic Budgeting .....	14
Table 5: Relevant PEFA Scores for Budget Preparation .....	18
Table 6: Relevant PEFA Scores for Resource Management .....	21
Table 7: Relevant PEFA Scores for Scope of Budget .....	25
Table 8: Relevant PEFA Scores for Accounting and Reporting.....	29
Table 9: Relevant PEFA Scores External Accountability .....	32
Table 10: Breakdown of Successful and Challenging PFM Reforms in MENA .....	35
Table 11: Donor Support for PFM Reforms in MENA .....	54

Table A. 1 MENA PEFA Averages Compared With World Averages For Comparable Countries.....	58
Table A. 2 MENA Country Scores on Individual PEFA Criteria.....	59

## **FIGURES**

Figure 1: MENA PEFA Averages Compared to Global PEFA Averages for Comparable Low Middle Income Countries.....	iv
Figure 2: Reforms at Different Stages of the Budget Cycle .....	v
Figure 3: MENA PEFA Averages Compared to Global PEFA Averages for Comparable Low Middle Income Countries .....	7
Figure 4: Reforms at Different Stages of the Budget Cycle .....	13

## **BOXES**

Box 1: Ten Principles of Implementation for PFM Reforms in MENA.....	x
Box 2: Ten Principles of Implementation for PFM Reforms in MENA.....	37
Box 3: History of the Iraq IFMIS System.....	47



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Mark E. Ahern

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# Executive Summary

## Introduction

One of the most important functions governments perform is that of mobilizing and deploying financial resources to achieve their objectives. According to the most recent World Bank data, governments throughout the Middle East and North Africa (MENA) region spent approximately \$407 billion dollars in 2007 in delivering their policy, regulatory and service functions. The way in which this money is spent has huge implications for their broader development trajectory. For example, a one percent efficiency gain in Egypt's budget for 2009 would yield \$637 million dollars—enough resources to build 40,000 schools, pave 4,500 kilometers of highway, or recruit an additional 600,000 doctors. It is therefore not surprising that issues of public financial management, or PFM, have been at the heart of governance reform programs in virtually all of the countries in the region.

For governments to perform their spending function well, their PFM practices should meet certain well-established criteria. Government spending should be affordable, in that it takes place within a framework that ensures expenditure is consistent with monetary and fiscal policy objectives and sustainable in the long term. Governments should optimize the allocation of public resources between different sectors and expenditure categories in a way that reflects their policy priorities, including sustainable growth as well as human and social development. Such expenditure should be efficient, in that it maximizes output for a given set of inputs, and effective, in that it supports the successful realization of the government's goals. It should also be transparent; conducted in accordance with the relevant laws and regulations; and undertaken with appropriate checks and balances to ensure financial probity.

While such objectives are relatively straightforward, their realization can be anything but. In many MENA countries, PFM reforms have been on the agenda for a decade or more. This report seeks to reflect upon this experience to date and better understand the nature of the PFM challenges confronting these countries. This study surveys these reforms across ten Arab countries: Algeria, Egypt, Iraq, Jordan, Lebanon, Morocco, Syria, Tunisia, the West Bank and Gaza and Yemen. They were selected partly because they are places where the Bank has been heavily engaged on PFM issues and been able to gather a wealth of comparative information. They also represent an interesting cross-section of administrative traditions and different levels of development. At the high end, in 2007 Lebanon had a GDP per capita of \$6,017 and a life expectancy of 72 years, whereas at the other end of the spectrum, these figures stand at \$973 and 62 years for Yemen. Lebanon has around 38.3 internet users per 1,000 citizens, as opposed to only .9 for Iraq. Taken together, these countries are home to over two thirds of MENA's population and nearly one third of its GDP. Many of the findings from this analysis will be of relevance to other MENA countries as well.

Turning to the substance of PFM reforms, the study considers to what extent these countries dealing are with common problems stemming from similar administrative traditions and comparable levels of development, or unique challenges grounded within their own particular historical or bureaucratic experience. The analysis also seeks to understand the type of PFM reforms that have been implemented across the region in the last decade, including where these reforms have gone well, where they have not, and why. Beyond these questions, the study seeks to see if any broader conclusions can be drawn regarding the way in which these reforms have been implemented and how that has affected their success (or lack thereof). Are there tactical lessons about what works best during implementation from which future reformers can benefit? In what ways do broader political economy considerations shape and influence the challenge of PFM reform in MENA?

To review PFM reform across MENA, it is necessary to utilize a common approach to structure the analysis. In recent years, the Public Expenditure and Financial Accountability (PEFA) framework has become the most recognized and widely accepted tool for assessing the status of a given country's PFM system. This set of twenty eight (28) high level indicators measures performance against best practice in developed and developing countries and allows progress to be tracked over time. The indicators analyze performance in the six core areas of public financial management spanning the budget process: (1) credibility of the budget; (2) comprehensiveness and transparency; (3) policy-based budgeting; (4) predictability and control in budget execution; (5) accounting, recording, and reporting; and (6) external audit. The central government is the main area of focus, along with issues relating to the overall scrutiny of public finances. Activities of public enterprises and sub-national levels of government are not addressed directly.

While the PEFA indicators provide a point assessment of the PFM system for a particular country, the focus of this study is on the reforms to the system and what progress is being made as a result of these reforms. To gain this insight, the PEFA analysis has been augmented by a series of country chapters that are provided in Volume 2. These chapters were drafted along a common template to provide a more detailed picture of the PFM reform efforts in the countries of this study. These assessments have also sought to go beyond the “what” of PFM reform—where the analysis is organized around the six core PEFA areas—to capture some of the “how” and “why” of reform. This touches upon both strategies for implementation and broader political economy issues within a given country. These chapters have relied heavily upon desk studies of existing Bank and Fund documents, such as PERs, CFAAs, CPARs, IMF Fiscal ROSCs, as well as a variety of project-related documents.

In two cases of particularly interesting and far-reaching reform in MENA, the analysis relies on more detailed case studies. The first is Salam Fayyad's PFM reforms, which were implemented during his first tenure as Minister of Finance in the West Bank & Gaza from 2002 to 2005. The second are the reforms in tax and customs implemented in Egypt since 2005 under the tenure of Youssef Boutros Ghali. These reforms are singled out both because they were substantial in scope and are widely perceived to have made a material improvement to the existing systems.

### **MENA PFM Practices Compared Against Global Averages**

Figure 1 below provides the summary results for the six PEFA exercises that have been completed for countries in the study. Assessments for the WBG and Syria were completed in 2006; Jordan in 2007; Iraq and Yemen in 2008; and Morocco in 2009.<sup>1</sup> A PEFA analysis is currently underway in Tunisia, but has not been finalized. PEFA reviews have yet to be conducted for two other countries in this study: Algeria and Lebanon. The PEFA alpha scale has been converted to a numeric scale ranging from 0 to 4 to assist with comparisons, where 4 is the highest rating.

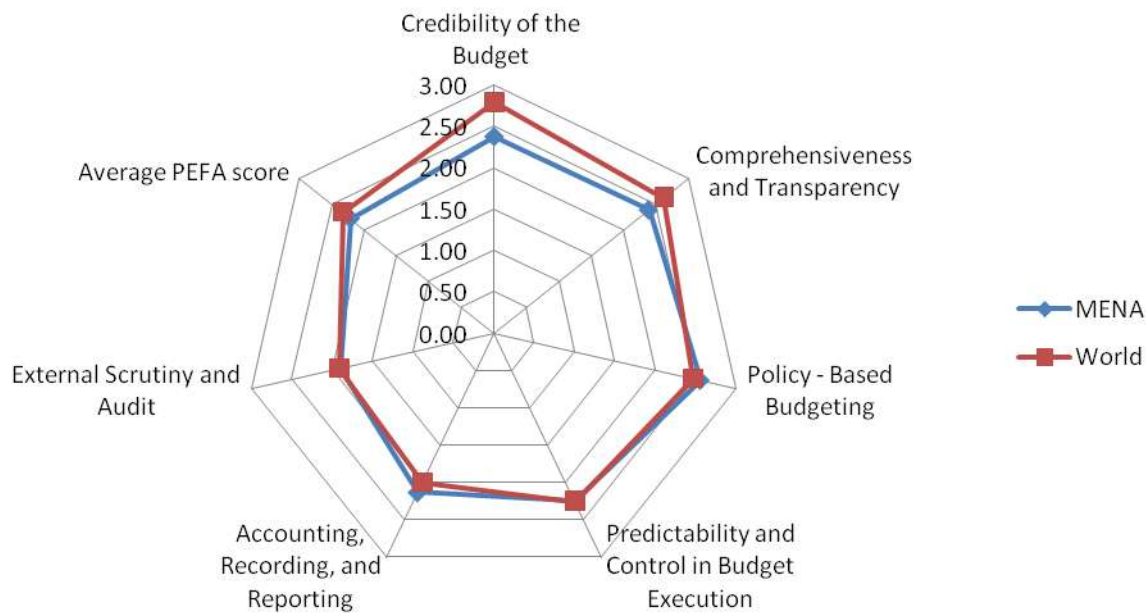
A comparative analysis was conducted as to where MENA countries stood vis-à-vis other countries at similar levels of development, in this case 19 lower middle income countries with GDPs from \$936 to \$3,075 per capita in 2007 who had recently completed a PFEA assessment. (Among the list of comparators were three countries from Africa; three from Latin America and the Caribbean; six from East Asia and the Pacific; and seven from Europe and Central Asia.)<sup>2</sup> The results are presented below.

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<sup>1</sup> Although a PEFA was presented for Egypt in October 2009, it remains preliminary, as the Government has not endorsed a number of the findings.

<sup>2</sup> The countries incorporated into this analysis include Congo Brazzaville, Lesotho, Swaziland, Dominican Republic, Paraguay, Peru, Indonesia, Samoa, Timor Leste, Tonga, Tuvalu, Vanuatu, Albania, Armenia, Azerbaijan, Kosovo, FYR Macedonia, Moldova and Ukraine.

**Figure 1: MENA PEFA Averages Compared to Global PEFA Averages for Comparable Low Middle Income Countries**



At an aggregate level, MENA's PFM systems are roughly comparable to those of other countries at similar income levels. As a whole, the region tends to fare a bit better on accounting, recording and reporting and a bit worse on credibility of the budget. Among the countries covered in this study, the highest ranked countries in aggregated PEFA rankings are Morocco and Jordan. They both have overall average scores of about B (2.87). On the lower end of the scale, West Bank and Gaza (WBG) and Iraq have PEFA Assessments that would average around a C- (1.5 to 1.6), although the formal PEFA assessments do not include minus (-) rankings. In terms of average scores for the six main categories, the tightest scores (i.e. the lowest standard deviation) were around credibility of the budget, indicating commonality among MENA countries on this dimension, whereas the largest average discrepancies were found in the area of budget comprehensiveness and transparency.

### The Substantive Reform Agenda

This section is structured around 13 common categories of PFM reform grouped under six stages of the Budget cycle. The selection of categories follows that used by Matt Andrews in an earlier study using PEFA data; however the categories have been adapted to reflect common reform activity in the MENA region.<sup>3</sup> Figure 2 sets out the different stages in the budget cycle and the reform categories considered at each stage

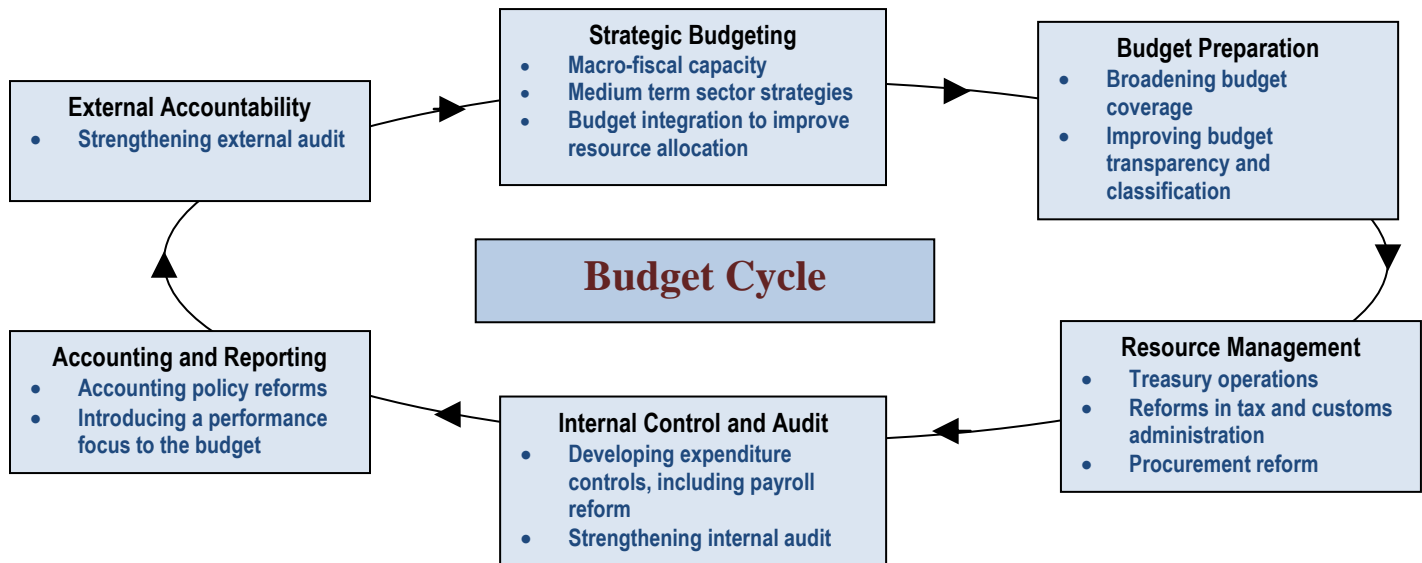
The choice of reform categories involved a number of compromises, and several important reforms that have close links to PFM (e.g. civil service reforms) are not considered. Determining whether to create separate categories for some wide-ranging reforms was also an issue. In particular, two common reforms—Medium Term Expenditure Frameworks (MTEFs) and treasury reforms—often cover a number of the above categories. These reforms are considered in their component parts during

<sup>3</sup> Andrews, *PFM in Africa, Where are We, How Did We Get There, and Where Should We Go?* See the following webpage: <http://www.resultsfordevelopment.org/sites/default/files/resources/PEFA-in-Africa-pdf.pdf>.

the discussion. Conversely, reforms in budget transparency that occur at a variety of stages in the budget cycle (for example budget documentation, in year financial reporting, and end of year financial statements) are considered in a single category.

For each of the six stages of the budget cycle, the relevant PEFA scores are first reported, followed by an assessment of each of the reform areas relevant to this stage. For each reform area, the report briefly sets out the underlying objective of this type of reform before reviewing experience in different MENA countries. It then provides an assessment of what has worked and what has proven to be more challenging.

**Figure 2: Reforms at Different Stages of the Budget Cycle**



## 1. Strategic Budgeting

**Macro-fiscal Capacity and Budget Sustainability.** Having a unit in the Ministry of Finance to provide macroeconomic and fiscal (macro-fiscal) policy advice is important for good aggregate fiscal management. The Ministries of Finance in the region have traditionally not had this capacity but, in recent years, a number of countries have established units to provide macro-fiscal advice. The work is analytically demanding and attracting suitable staff within standard civil service contracts has proven to be a challenge. In view of this, many of the units initially focused on monitoring taxes and preparing monthly reports on budget execution. However, as they have increased their capacity, they have become more involved in budget preparation through developing a fiscal framework for the budget—although the link between these frameworks and the final budget is still not strong.

**Focusing on Medium Term Expenditures at the Sectoral Level.** In fiscal management, the cost of a policy in the next year is not always a good indication of the costs over time. To better manage the budget, a number of countries in the MENA region are attempting to develop “forward estimates” of expenditures at the sectoral level as part of Medium Term Expenditure Framework (MTEF) reforms. The reform is extremely resource intensive and, to date, the results have been disappointing. Often, the work has been carried out through pilot projects in various sectors with limited ownership from the Ministry of Finance. As a result, the estimates remain an analytical exercise which is not used in preparing the budget. Another weakness is that the analysis focuses only on project expenditures and

insufficient attention is paid to recurrent expenditures, which generally form the bulk of the budget. While the argument for developing sector based forward estimates to provide a medium term perspective is compelling, this is a major reform and should only be initiated once more basic improvements to the PFM system have been completed.

***Budget Integration to Improve Efficiency of Expenditure.*** All countries in the region continue to have elements of dual budgeting, with separate arrangements for deciding the allocations for operating and capital expenditures. These arrangements impede efforts to get the best value for money from expenditures, as they risk gaps or duplication of expenditure; inconsistent expenditures; and the wrong mix of expenditures both in aggregate and at the level of activities. While some progress has been made to integrate the presentation of the budget, efforts to integrate other elements of budget management have largely been elusive. In countries with a separate planning ministry managing the capital budget, institutional resistance to consolidating budget management in the Ministry of Finance has been a particular problem. Where consolidation of budget management within the Ministry of Finance does occur, one of the main challenges is to ensure that the Ministry has the necessary analytical capacity to oversee the capital budget. For this reason, the transition needs to be carefully planned.

## **2. Budget Preparation**

***Broadening Budget Scope and Coverage.*** Ensuring broad budget coverage is important to make the budget effective both as a tool for fiscal control and allocating resources to the highest priority area. It is also important to ensure that there is effective accountability for public expenditure. Limitations in the scope of the budget are a general problem in the region as reflected in low PEFA scores for unreported government expenditure. The technical demands of this reform are not significant and good progress has been made where there is sufficient political commitment. However, there are strong incentives for those with expenditures outside the budget to resist the change, and a strategic approach needs to be taken to the reform that anticipates the likely resistance from these interests.

***Improving Budget Transparency and Classification.*** Better information on budgeted expenditures can play an important role in building the credibility of the government's fiscal policy with the public, parliament and external financiers. Reforming the budget classification is an important component of this broader objective. Many countries in the region have taken steps to improve the transparency of the budget documents, update the budget classification, and introduce in-year budget reporting. These efforts have been among the most successful PFM reforms. One of the factors behind this success is that the reforms are seen as technical in nature and thus less susceptible to opposition from vested interests. The reforms also tend to rely on a small team of staff in the Ministry of Finance, which makes them better placed in an environment where the civil service has limited capacity. Moreover, once introduced the reforms have tended to become part of the fabric of the system and this has made them more enduring.

## **3. Resource Management**

***Developing Treasury Operations.*** A well functioning treasury system can minimize the government's net borrowing costs and reduce exposure to the risk of bank default. A number of the countries in the region have embarked on treasury reforms to improve cash management by establishing a treasury single account (TSA) at the central bank. While progress has been made, the coverage of the TSA is often not complete because the Ministry of Finance has not had the authority to consolidate some balances. A number of countries have set up units to prepare and maintain a cash plan, which can assist in aligning the borrowing and investment activity with the government's cash needs. However, too often the cash plans are not being actively used in cash management. Few countries have taken steps to improve debt management systems as part of treasury reforms.

**Reforms in Revenue Administration: Tax and Customs.** By improving the administration of the tax system, a government can increase the revenues it collects while enhancing the fairness of the system and reducing the cost of doing business for taxpayers. In general, MENA countries have made much better progress with tax administration reform than they have with expenditure management reforms. One reason for this is that Ministers of Finance have taken an active interest in the reforms as they are driven by a need to both increase revenues and improve the environment for doing business. Another factor is that tax administration is a distinct function within government and it has been possible to provide performance incentives to the staff of the tax authority that could not be applied generally across the public sector. One unhelpful consequence of this tactic has been that some of the better staff have moved to tax administration from expenditure roles within government, exacerbating existing capacity problems in these areas. For this reason, caution should be exercised in deciding whether to introduce incentives for tax administration in isolation.

**Procurement Reform.** The way in which the purchase of goods and services is controlled through the procurement process can help the government to minimize collusion and other corrupt practices. Improvements to the procurement procedures can therefore lower the cost of government expenditures. The procurement systems in the region are weak. Reforms have been attempted in a number of countries but the timescales for these reforms have been extended and the outcomes have been disappointing. The reforms often touch on areas of significant corruption and therefore can pose a threat to particular interests, which have strong incentives to delay or divert the process. The failure to make progress in large part reflects an unwillingness to confront these special interests.

#### **4. Internal Control and Audit**

**Developing Expenditure Controls.** Effective expenditure controls are important to support aggregate fiscal control, ensure that the allocation of resources reflected in the budget is followed, and that the government does not pay more than it needs to for goods and services. Because of the link to the transaction cycle, the controls are an important element in addressing corruption associated with government expenditure. The countries in the region tend to have extensive and time-consuming control systems (often evidenced by multiple approval signatures), but as evidenced in the PEFA assessments, these systems are not effective. Two key problems are that the overlaying controls diffuse accountability, and that they often only apply at the payment point rather than when expenditure is committed. Despite the problems being faced in the region, there have been relatively few attempts to streamline and strengthen the general control procedures. Progress has been made by some countries in payroll management, but this is uneven. The overall impression is that where there is a failure to make progress with improving expenditure controls, it is mainly due to a lack of genuine interest in the reforms from the authorities.

**Strengthening Internal Audit.** Internal audit aims at providing the executive with assurance of the quality of the financial management systems—in particular the implementation of financial controls and the management of risks.<sup>4</sup> Most countries in the region have weak internal audit functions reflecting problems in both the scope of audit activity, and conflicts of interest where the auditor is also part of the control function. Internal audit has in general not been given a high priority for reform in part because it is an advanced PFM reform. But resistance to change can also come from existing auditors who are reluctant to be removed from the transaction control process when this is a source of corruption.

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<sup>4</sup> While internal audit can also provide comment on the value for money of expenditures, this is not generally a core function.

## 5. Accounting and Reporting

**Accounting Policy Reforms.** Accounting reforms can improve the reliability with which expenditures and cash balances are controlled, monitored and reported. Where accounting policies are aligned with international standards, there can be increased confidence in the integrity of the financial information presented. Experience with the reform of accounting systems in the region has been mixed. While most countries now operate double entry systems, there has been limited success in reforming accounting methodologies towards a consistent use of cash or accruals, as well as in applying international accounting standards. Because accounting reforms affect the work of many employees throughout the public sector, a strong commitment from the senior staff in the Ministry of Finance is essential if they are to be successfully introduced.

**Introducing a Performance Focus to the Budget.** The traditional input based budget does not provide policy makers with information on what goods, services, or policies are being financed by government expenditure. The idea of focusing on performance has been around for some time, and there is considerable interest in this reform from countries in the region. However, the successes to date are limited and the timeframe for the reform is proving to be extended. The reform is difficult in part because it relies on having many other elements of the PFM system operating at a reasonable standard. For this reason, even where the reform proceeds, every effort should be made to avoid conceptually sophisticated approaches and to ensure that the approach can be supported by the accounting systems.

## 6. External Accountability

**Strengthening External Audit.** External audit provides parliament with assurance on the adherence to financial laws, the reliability of the financial statements, and value for money in government expenditure. As such, it provides an essential discipline on the financial management of the executive. The PEFA assessments indicate that the external audit functions of countries in the region have a range of weaknesses characterized by a strong focus on transactions rather than systems, as well as conflicts of interest where the auditor is part of the ex-ante control system. In spite of the weaknesses in the audit bodies, there have been relatively few efforts to reform the external audit function, in part reflecting the relatively minor role played by parliaments in many countries in the region. While the focus of external audit is on providing assurance to parliament, the presence of an effective audit body can also support reforms in budget execution, by encouraging more discipline in the accounting practices. However, the success of efforts to build the capacity of the audit body will ultimately depend on whether the parliament is prepared to utilize the auditor's report.

### **Implementing Public Financial Management Reforms in MENA: An Emerging Set of Promising Practices?**

Summarizing the discussion above, the following table breaks MENA's experience with PFM reform down along three dimensions. The first category is reforms that have typically been more successful, in that a number of MENA countries have been able to implement them effectively and achieve concrete, independently verifiable improvements. The third category is comprised of reforms that have been historically been more challenging, difficult and problematic. It does not mean that they have been impossible to implement, and some MENA countries may have been able to put in place certain elements of these reforms. But this is not common. The "mixed" category represents an area where generalizations across the region are difficult to make and the results are often more unique to a given country.



**Table 1: Breakdown of Successful and Challenging PFM Reforms in MENA**

Successful PFM Reforms	Mixed	Challenging PFM Reforms
<ul style="list-style-type: none"> <li>• Improving budget classification</li> <li>• Improving budget transparency</li> <li>• Reforms in tax and customs</li> </ul>	<ul style="list-style-type: none"> <li>• Enhance macro-fiscal capacity</li> <li>• Budget integration</li> <li>• Streamlining ex-ante control processes</li> <li>• Commitment control</li> <li>• Payroll management</li> <li>• Treasury operations</li> <li>• Reform of accounting systems</li> <li>• Internal and external audit</li> </ul>	<ul style="list-style-type: none"> <li>• Medium term sector strategies</li> <li>• Improving budget scope and coverage</li> <li>• Introducing performance into the budget</li> <li>• Procurement reforms</li> <li>• Large information technology projects</li> </ul>

The PFM reforms that have been particularly successful in MENA fall into two types: efforts to improve budget transparency and classification, and the reform of revenues, particularly tax and customs. Ironically, these represent two very different reforms. The first are relatively straightforward and technocratic in nature. An existing body of accepted practice exists to reform economic classification, such as in the form of the IMF's GFSM 2001, and there are incentives to align accounts along standard international practice to facilitate the production of comparable fiscal and economic data. While there may be some resistance to such reforms stemming from basic bureaucratic inertia, no fundamental interests are challenged or mandates threatened. Once implementation is complete, the reform becomes part of the fabric of the system and endures.

This is not true for reforms in tax and customs, where the stakes are much higher. Revenue agencies are often among the entities in government where problems of corruption are most pronounced, since their function places them in a position to extract rents from both firms and the general public. Efforts to restructure and reorganize such functions often encounter fierce resistance from both those on the inside and some on the outside. Yet if the challenges are great, the gains are often significant as well. For governments facing significant fiscal deficits, it is often more politically palatable to raise revenues—difficult as that may be—than to engage in painful cuts in expenditure. Such reforms are therefore able to garner the requisite high-level political support to see them through in spite of considerable opposition.

Unfortunately, on the other side of the spectrum are a host of reforms that are neither particularly easy to implement nor which bring the promise of substantial fiscal gains, at least in the short-term. Some, such as improving the scope and comprehensiveness of the budget, are not technically difficult to implement. However, as noted above, unless significant political capital is invested in overcoming bureaucratic resistance, these reforms are unlikely to move forward. Other reforms, such as the development of MTEFs and greater performance orientation into the budget, are often both technically demanding and run up against powerful vested interests. In many cases, their successful implementation may depend upon underlying systems, procedures and practices being in place that may not exist. It is therefore not surprising that their implementation is frequently delayed or halted. A variety of lessons have emerged from the individual case studies and the more detailed assessments of reforms in the WBG and Egypt. They are summarized below as the “Ten Principles of Implementation” for PFM reforms in MENA.

### Box 1: Ten Principles of Implementation for PFM Reforms in MENA

1. Know the value—and limitations—of political economy analysis
2. PFM reform as means and not ends
3. Context matters, so swim with the current
4. The wisdom of “muddling through”— grand strategy versus incremental change
5. Establish basic systems before contemplating more advanced reforms
6. Whenever possible, keep reforms quick, simple and mutually reinforcing
7. Be wary of large financial management information systems
8. Internal challenges: leadership, coordination, skills and incentives
9. External stakeholders—useful, but don’t count on them
10. Lessons for donors: be more strategic, selective, modest and flexible

***Lesson 1: Know the Value—and Limitations—of Political Economy Analysis.*** In many areas of governance and public administration reform including PFM, there has been a rush to embrace the discipline of political economy analysis (PEA) over the last decade. The field is still evolving and precise definitions are elusive, but at its core PEA analysis embodies the important observation that political and bureaucratic factors matter. Would be reformers should not mechanistically seek to transfer approaches and practices that work well in one setting to other very different institutional contexts.

Yet beyond this basic and sensible warning, the PEA literature has relatively little to contribute when it seeks to address the most important questions in any reform initiative: what should be done, when does it need to happen, who should do it and how. Each reform experience is unique and endogenous to a particular time and country, as well as to an individual set of political, bureaucratic, institutional and personal dynamics. PEA may be valuable in highlighting constraints or identifying potential supporters, and it can help to inform decisions about what is to be done. But the trajectories of the most successful reforms in MENA bear little resemblance to the type of recommendations that a typical donor-supported PEA would generate. PEA is not a substitute for solid strategic decision-making, and even less for astute tactical maneuvering during implementation. More is likely to be gained by investing in greater tactical flexibility, in terms of field-based governance advisors and public sector specialists who can provide real-time advice and assistance in high risk, high engagement settings, than in trying to perform more rigorous political and bureaucratic analysis up-front.

***Lesson 2: PFM Reform as Means and Not Ends.*** PFM reforms arise from a number of different motives, ranging from the need to respond to an emergency to individual ministers seeking to make a career for themselves as reformers. In the MENA region, the most far-reaching reforms were implemented in response to an acute fiscal crisis and the need to fundamentally restructure tax practices to attract foreign investment. Under these circumstances, PFM reforms were effective in large part because they promised to be a solution—or at least part of the solution—to a broader set of problems. As such, senior political leaders were willing to push them through in the face of considerable resistance. Reforms that were implemented because they are consistent with emerging international best practice have typically lacked the staying power to overcome entrenched opposition.

***Lesson 3: Context Matters, so Swim with the Current.*** A corollary of the observation that reforms are a means and not an end in themselves is the point that context matters. As noted above, two of the most far-reaching PFM reforms took place against a backdrop of an acute

financial crisis, which gave them profile and visibility. However, major reform agendas can stretch over years, whereas the political and economic conditions that give rise to them are typically subject to much shorter time horizons. If reforms are largely technical in nature, have a solid rationale behind them are supported by well-positioned champions within the relevant ministries, and if they avoid alienating powerful constituencies, then under most circumstances they can probably stay “under the radar screen” and survive the shifting political, economic and administrative sands. Lebanon was able to implement some important reforms in payroll management, for example, even in the midst of a chronic political crisis and the absence of a functioning parliament.

But Lebanon’s experience is also instructive, in that when these reforms have needed to move beyond the realm of what could be implemented by a Ministry of Finance decree and required broader cabinet or parliamentary approval, they have stalled. There are no examples of more far-reaching PFM reforms that came to fruition if the broader political context was not supportive. Nor are there examples of where senior officials were able to isolate and protect major PFM reforms from major shifts in the broader political climate. Put succinctly, an ebbing tide grounds all large boats—regardless of how well they are designed or the skill and determination of the captain.

***Lesson 4: The Wisdom of “Muddling Through”—Grand Strategy versus Incremental Change.*** To what extent are MENA PFM reform agendas driven by an overarching strategic framework or integrated plan, versus a more flexible and improvised approach that seeks to take advantage of opportunities when they emerge? The answer is not entirely straightforward. On the one hand, MENA does not suffer from an absence of strategic plans for upgrading systems and procedures. Furthermore, there have been examples of when countries would have benefited from adopting a more comprehensive approach to PFM reform. The lack of a more comprehensive approach can be particularly problematic in the development of integrated financial management information systems, for example.

Yet while such reform strategies can be valuable as a statement of intent, communicating priorities, securing donor support or providing political cover for a given set of activities, their role in actually shaping successful reforms can be modest. The development of such plans is no guarantee that they will be implemented expeditiously. In many MENA countries, roll-out has taken much longer than expected, with a number of components being dropped or modified along the way. Nor are such plans a prerequisite for success. Salam Fayyad adopted a flexible view to West Bank & Gaza’s PFM reforms, recognizing that he could not determine *a priori* the sequencing of reforms or expect to have control over the entire process. Fayyad describes his approach as being, “patient, deliberate, methodical, and opportunistic, looking for an opening here and there.” His approach was informed by a clear set of priorities, but utilized tactical flexibility in terms of the sequencing and timing of reforms. Aspects of Egypt’s tax reforms evolved in much the same way.

***Lesson 5: Establish Basic Systems Before Contemplating More Advanced Reforms.*** The temptation is often irresistible for governments and international advisors to strive for quantum improvements in performance by adopting some cutting-edge practices from OECD countries in a developing country context. More often than not, the result has been a litany of dashed expectations and failed reforms. In response, the Bank’s *Public Expenditure Management Handbook* (1998) emphasizes the importance of “getting the basics” right before moving on to tackle more advance reforms.

The PFM reform experience within MENA largely bears this out. This has been particularly true with regard to two sets of initiatives that have been among the more technically advanced to be implemented to the region: the move to a Medium Term Expenditure Framework and the effort to introduce greater performance orientation into the budget process. As noted above, both have shown themselves to be complicated and problematic to implement, in part because their realization has relied upon a number of preconditions to be in place before they can be effective, and in part because other senior officials have been generally unwilling to allow themselves to be bound by such initiatives.

***Lesson 6: When Possible, Keep Reforms Quick, Simple and Mutually Reinforcing.*** It is an accepted article of faith that major PFM reforms are difficult, complex undertakings that require years or sometimes decades to fully come to fruition. Laws and regulations must be drafted; longstanding practices restructured; political and administrative cultures changed; institutions built and capacities strengthened. To attempt such undertakings quickly, so the argument goes, is a recipe for poorly thought through implementation and eventual failure.

As with many managerial maxims, there is some truth to this contention. PFM reforms in a number of MENA countries, such as introducing MTEFs or greater performance orientation into the budget, do take a long time to implement. Yet there are also cases where reforms can be implemented quite quickly when the requisite political will exists. Reforms dedicated to expanding the scope and comprehensiveness and transparency of the budget, for example, can be implemented within weeks or months if the proper political will is in place. Furthermore, some of the more effective reforms were deliberately implemented with haste. Salam Fayyad wanted to generate confidence in the reform agenda by taking specific, quick steps that made an impression. He felt, rightly as it turned out, that reform would become more difficult with time. Otherwise, as has happened far too often in MENA, reform can become “business as usual” and lose any sense of priority or urgency.

A related question is whether to pilot reforms or roll them out whole. In MENA, pilot PFM reforms have been implemented in a wide variety of contexts. The answer to this question is highly contextual. On the positive side, pilots—particularly when combined with rigorous monitoring—provide an opportunity to gain valuable experience in identifying potential problems that could plague a set of PFM reforms and rectifying them before too much damage is done. This is particularly important when the roll-out is likely to be time-consuming and expensive, as is the case with large IT systems. However, in the absence of firm commitment to proceed with a given set of reforms, pilots can often become an excuse for delay and inaction. Sometimes it is preferable to roll out reforms broadly and accept that there will be challenges during the early stages of implementation. Pilots also tend to do better in administrations with a history of experimentation and innovation than those with fixed traditions embedded in a strong legal framework.

***Lesson 7: Be Wary of Large Financial Management Information Systems.*** An integrated financial management information system (IFMIS) can offer great benefits for a variety of PFM activities, especially budget execution. All countries in the region have made some effort to introduce computerized systems to support PFM. In general, two different strategies have been adopted: (1) develop a “sophisticated” fully integrated IFMIS; or (2) use a simple customized IT system to support budget execution. While there are some small successes to date, most of the “sophisticated” projects have struggled to meet their implementation milestones, budgets and promised functionality. When things go wrong, such IT failures can be extraordinarily costly, as was illustrated with the recent failure of a \$30 million FMIS system in Iraq. A number of problems have undermined these large projects, but two

important concerns are weak project management arrangements and inadequate commitment and/or engagement of staff of the Ministry of Finance to the reform. Would-be reformers looking to import sophisticated IT solutions should proceed with caution in both MENA and elsewhere.

The second approach has been to develop simple computerized systems with limited functionality to help support budget execution. The systems are usually customized to fit the specific needs of the budget execution system of the country. They tend to have much lower initial development costs, and provided their objectives remain minimal, they may also be an efficient way of exposing officials only familiar with paper based operations to the potential of a future IFMIS. However, there are limitations to this approach. First, because the systems are developed to order, they often do not include standard functionality that has proven useful in other systems. Second, the systems tend to be less flexible in dealing with new user requirements than off the shelf systems. While the initial cost of the system may not be high, these costs increase over time as the system is reconfigured for new developments. For these reasons, the use of a simple system should be seen as a short term solution with the eventual aim of moving to an integrated system.

***Lesson 8: Internal Challenges: Leadership, Coordination and Incentives.*** MENA's reform experience holds a number of important lessons as to how such reforms should be structured and organized. The most far reaching and successful reforms within MENA have been driven by powerful ministers of finance, whose role is pivotal in the process. Both Salam Fayyad in the West Bank & Gaza and Youssef Boutros Ghali in Egypt brought a combination of impressive technical expertise and a solid technical of the issues, along with considerable political and managerial savvy and sheer determination.

There is a wide array of stakeholders in any PFM reform initiative, including ministries, agencies, departments, sub-national entities, and state owned enterprises. The quality of coordination between these agencies and the MOF varies both within and between countries, but it is frequently problematic and occasionally dysfunctional. To cope with such problems, several countries have established inter-agency task forces and other mechanisms to facilitate coordination. Their structure and membership can vary without unduly compromising their prospects for success. More problematic is the fact that, while such coordinating bodies can be relatively easy to establish, in a number of cases they end up meeting only infrequently thus compromising the quality of implementation.

MENA countries have adopted a variety of approaches to gain access to the requisite expertise. Some have relied heavily upon project implementation units staffed largely by external experts, whereas others have sought to keep these reforms in-house. While each approach has its strengths and weaknesses, some general lessons have emerged. The first is that technically skilled and managerially adept leadership is required at the project management level—and such leaders need to be fully empowered—or the reforms are unlikely to succeed. Second, capacity constraints at the team level are often not taken seriously enough in designing reforms. Efforts to work around a lack of capacity by relying too heavily upon external experts or local staff recruited specifically for the task are a Faustian bargain; they need to be carefully planned and managed with a clear exit strategy in mind. Finally, MENA governments have often chronically under-invested in the careful monitoring of reforms.

***Lesson 9: External Stakeholders—Useful, but Don't Count on Them.*** As a general rule, the Executive Branch is extremely powerful throughout MENA. Other stakeholders—be they

legislative or judicial branches, various civil society organizations, academics, think tanks, or the private sector—operate at a distinct disadvantage when it comes to influencing political and administrative decision-making. This is particularly true with regard to PFM reform, which is often viewed as a narrow, specialized and technocratic field.

Throughout the region, parliaments have been growing in influence but still typically lack the staff and committee structures that would allow them to provide detailed scrutiny to budget proposals. In a number of countries, their ability to revise or change budgets presented by the executive is limited, and the information they receive can be partial and fragmented. Their follow-up in areas such as audit reports is variable. With a few notable exceptions, they have typically not been a strong force for PFM reform, and some have even advocated approaches antithetical to sound PFM practice. If parliament's influence has been modest, that of the public has been virtually nonexistent. A few NGOs and think tanks may have pressed for greater budgetary openness and transparency, but there is no evidence that they have had any real influence over the shape or content of PFM reform programs to date.

***Lesson 10: Lessons for Donors: Be More Strategic, Selective, Modest and Flexible.*** The donor community has been heavily although unevenly engaged in providing support to public financial management reforms throughout the MENA region. According to the OECD DAC database, approximately ten MENA countries received donor assistance for PFM reforms during the period from 2003 to 2007, with the lion's share going to Iraq, Morocco and Jordan. Other recipients included Algeria, Egypt, Lebanon, Syria, Tunisia, West Bank and Gaza, and Yemen. Total funding for PFM was around \$459 million during this five year period. The average was \$92 million, with considerable variation between years. While the data probably provides a rough proxy for relative levels of donor engagement, these figures reflect budget support operations with a PFM focus rather than dedicated resources for PFM reform. The latter is likely to be much more modest, probably averaging in the \$1 to \$5 million dollar range per country annually after adjusting for the odd major IT project. The bottom line is that PFM reform in MENA is not an area where the donor community has over-invested.

Many donor-supported reforms have been too ambitious, overstating the amount of political and bureaucratic support for reform; not fully aware of the role of legacy systems and whether the necessary preconditions were in place; and in general trying to do too much within too limited a period of time and without the required capacity. Donor modalities need to be developed to better respond to the dynamic nature of the PFM reform process. There is a role for the traditional project management framework when the reforms are large and enduring (and the sums involved substantial), which is designed to successfully manage a broad and diverse agenda and ensure appropriate accountability. But lengthy appraisal, consultant selection and mobilization procedures often result in delays and lost opportunities. As was noted in Lesson 4 above, the more successful PMF reforms tend to involve “strategic opportunism”—seizing upon opportunities rapidly as they emerge within a broader framework of clearly articulated priorities.

To exploit such opportunities as and when they occur, donors need to augment their traditional approaches with small, rapidly disbursing, carefully targeted aid. To do this will require several preconditions: (1) accurate, up to date knowledge of the situation on the ground, including the evolving political and bureaucratic dynamics; (2) talented, advisors who have technical skills, political and managerial savvy, and the trust of senior officials; (3) a well-articulated framework of PFM priorities; and (4) small amounts of discretionary resources that can be utilized quickly and flexibly to help facilitate implementation.

# Chapter 1

## Introduction:

### Public Financial Management Reform in MENA and Beyond

*In the early stages of the state, taxes are light in their incidence, but fetch in a large revenue...As time passes and kings succeed each other, they lose their tribal habits in favor of more civilized ones. Their needs and exigencies grow...owing to the luxury in which they have been brought up. Hence they impose fresh taxes on their subjects... sharply raise the rate of old taxes to increase their yield...But the effects on business of this rise in taxation make themselves felt. For business men are soon discouraged by the comparison of their profits with the burden of their taxes...Consequently production falls off, and with it the yield of taxation.*

-- Ibn Khaldun (1332-1406) --

### The Importance of Public Financial Management

One of the most important functions that governments perform is mobilizing financial resources and deploying them to achieve their objectives. According to the most recent World Bank data, governments throughout the Middle East and North Africa (MENA) region spent approximately \$407 billion dollars in 2007 in delivering their policy, regulatory and service functions. The way in which this money is spent has huge implications for their broader development trajectory. For example, a one percent efficiency gain in Egypt's budget for 2009 would yield US\$637 million dollars—enough resources to build 40,000 schools, pave 4,500 kilometers of highway, or recruit an additional 600,000 doctors. It is therefore not surprising that issues of public financial management, or PFM, have been at the heart of governance reform programs in virtually all of the countries in the region.

In the BBC parody of government life, *Yes Minister*, the consummate British bureaucrat, Sir Humphrey Appleby, once wryly observed: "the Treasury does not work out what it needs and then thinks how to raise the money. It pitches for as much as it can get away with and then thinks how to spend it." While such thinking has not been entirely banished from public sectors around the globe, the PFM agenda has moved quite a bit since this episode first aired in January 1986. Over the past two decades, there has been relentless pressure in both developed and developing countries to improve the quality of public expenditure and generate more value for money from government operations.

For governments to perform their spending function well, their PFM practices should meet certain well-established criteria. Government spending should be affordable, in that it takes place within a macroeconomic framework which ensures that the level of spending is consistent with the government's monetary and fiscal policy objectives and is sustainable in the long term. Governments should optimize the allocation of public resources between different sectors and expenditure categories in a way that reflects their policy priorities, including sustainable growth as well as human and social development. Such expenditure should be efficient, in that it maximizes output for a given set of inputs, and effective, in that it supports the successful realization of the government's goals. It should also be transparent; conducted in accordance with the relevant laws and regulations; and undertaken with appropriate checks and balances to ensure financial probity.

In many MENA countries, PFM reforms have been on the agenda for a decade or more. Some are seeking to implement basic financial management and information systems that will ensure resources are spent in a timely fashion for the purposes intended. Others are pursuing changes that will allow for greater efficiency and predictability in spending, along with an enhanced focus on performance and value for money. Many are dealing with issues such as enhancing transparency, ensuring adequate internal and external audit, or expanding the scope and comprehensiveness of the budget.

This report seeks to reflect upon this experience and better understand the nature of the PFM challenges confronting the countries of the MENA region. Turning to the substance of these reforms, it asks where are they performing well and where are they struggling? To what extent are these countries dealing with common problems stemming from similar administrative traditions and comparable levels of development, or unique challenges grounded within their own particular historical or bureaucratic experience? The analysis also seeks to understand the type of PFM reforms that have been implemented across the region in the last decade, including where these reforms have gone well, where they have not, and why.

Beyond these questions, the study seeks to see if any broader conclusions can be drawn regarding the way in which these reforms have been implemented and how that has affected their success (or lack thereof). How do broader political economy considerations shape and influence the challenge of PFM reform in MENA? Are there tactical lessons about what works best during implementation from which future reformers can benefit?

This report is divided into two volumes. The first volume summarizes the results and presents the conclusions of this analysis. The second provides the individual country case studies and templates upon which many of these conclusions are based.

### **Beyond MENA: The Lessons from Global Experience**

The MENA PFM reforms have not taken place in a vacuum. Throughout the globe, a variety of reforms have been implemented over the past two to three decades under the general rubric of “New Public Management.” The scope and content of these reforms has varied, but they have generally included providing greater responsibility and control over inputs to managers in exchange for greater accountability for outputs; moving to a multiyear framework in budget execution linked to realistic fiscal policy and revenue estimates; shifting from cash accounting to accrual accounting; and moving from compliance auditing to performance auditing, among others. Many of these reforms were introduced in OECD countries and then migrated to MENA and other developing countries in varying degrees—or at least attempts were made to transpose them. Against these trends, an opposing “getting the basics right” school emerged that emphasized the need for essential systems to be in place and functioning well before moving on to advanced reforms. PFM reforms in MENA and elsewhere have tended to reflect elements of both approaches—the desire to adopt more “cutting edge” practices across a range of fields and sub-fields, such as introducing more performance orientation, Medium Term Expenditure Frameworks (MTEFs), and financial management information systems, as well as the need to ensure that the essential prerequisites are in place first.

Issues of public finance reform have been at the core of the World Bank’s work on governance for over two decades. A recent survey of support for public sector reform by the Bank’s Independent Evaluation Group (IEG) reviewed the Bank’s work on PFM issues



throughout the globe.<sup>5</sup> The report noted that between 1990 and 2006 the Bank approved 467 lending projects with significant public sector reform components. Of these, public financial management was by far the most common theme, comprising 81 percent of the public sector projects approved during this period. PFM work was also heavily represented in Bank analytical and advisory activities and institutional development grants. Furthermore, the Bank's work on PFM issues has increased sharply since the 1990s.

The IEG report concluded that the Bank's increased PFM lending and analytical work can be linked with encouraging PFM improvements among borrowers, usefully adapting PFM tools from other jurisdictions and carrying out effective monitoring with robust assessment tools, such as PEFA.<sup>6</sup> However, progress has been uneven. The report argued that Bank performance might have achieved greater success with deeper institutional and governance analysis, greater attention to addressing basic systems before moving to advanced PFM tools and techniques, and more Bank support and flexibility in working to improve country procurement systems. It also noted that some specific reforms, such as moving to a MTEF, have been successful in some contexts but challenging in many others.

Other assessments have sounded similar themes, arguing for both a widening and a deepening of reforms to engage a broader set of stakeholders while simultaneously underscoring the need for more attention to domestic politics and established practices and institutions.<sup>7</sup> They have argued that PFM reform is a long-term endeavor, in which failure is often attributed more to implementation than the technical aspects of the program. Reforms such as MTEFs and expenditure controls have tended to move forward slowly, as have those involving large computerized information systems and the reform of audit institutions.

This analysis will argue that in a number of important areas, such findings are consistent with the experience of PFM reform in MENA. In particular, MENA countries have struggled to implement many of the PFM reforms that have been problematic elsewhere. Yet there are also important points of divergence, particularly with regard to the prescriptions for implementation. It may be that MENA poses some unique challenges that are not present elsewhere. Or it may be that our understanding of how such reforms are actually implemented in many countries around the globe needs to be further refined.

### **What is "MENA"? Selecting the Countries for this Study**

At a broader level, the question of how to define the Middle East and North Africa region is a thorny one that raises a host of complex and occasionally contentious issues. The definition utilized in this analysis is a strictly bureaucratic one. The World Bank's Middle East and North Africa (MENA) region consists of 19 countries, stretching from Morocco in the west to Oman and Iran in the east. It includes Djibouti but not Mauritania or Sudan. As of 2007 (the most recent year for which statistics are available), average GNI per capita across the region is around \$2,795, a figure that places it roughly in the company of East Asia and the Pacific (\$2,190). It is well below Europe and Central Asia (\$6,013) and Latin America and the Caribbean (\$5,888), but ahead of South Asia (\$879) and Sub-Saharan Africa (\$966).

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<sup>5</sup> World Bank, *Public Sector Reform: What Works and Why?* 2008.

<sup>6</sup> Ibid, p.51.

<sup>7</sup> Carole and Nico Pretorius, *Public Financial Management Reform Literature, United Kingdom Department for International Development Evaluation Working Paper*, 2009.

**Table 2: Basic Statistics on MENA Countries Selected for PFM Analysis**

		GDP		GDP	Life Exp.	Internet use	
Country	Population	(US\$ mil.)	per capita	at Birth	Literacy	per capita	
1 Algeria	33,858,168	\$136,034	\$4,018	72	70		10
2 Egypt	80,060,540	\$130,473	\$1,630	70	71		15
3 Iraq	29,947,491	\$62,000	\$2,070	68	74		1
4 Jordan	5,718,855	\$17,005	\$2,974	72	90		21
5 Lebanon	4,162,450	\$25,047	\$6,017	72	87		38.3
6 Morocco	31,224,136	\$75,226	\$2,373	71	52		21
7 Syria	20,082,697	\$40,549	\$2,019	74	80		17
8 Tunisia	10,225,400	\$35,020	\$3,425	74	74		17
9 WBG	3,832,185	\$4,016	\$1,048	73	92		9
10 Yemen	22,269,306	\$21,658	\$973	62	59		1

**Total**                      **241,381,228**                      **\$547,029**

**% of MENA**                      **67.9%**                      **31.5%**

Source: World DataBank: <http://databank.worldbank.org/ddp/home.do?Step=3&id=4> Source: All data is for 2007 or most recent year available.

This study surveys PFM reforms across a range of ten countries in the Middle East and North African (MENA) region: Algeria, Egypt, Iraq, Jordan, Lebanon, Morocco, Syria, Tunisia, the West Bank and Gaza and Yemen. They were selected partly because they represent countries where the Bank has been heavily engaged on PFM issues and been able to gather a wealth of comparative information (although Syria is an example of a country where a diagnostic has been performed but the engagement has been more limited). They also represent an interesting cross-section of administrative traditions and different levels of development. Table 1.1 above captures a number of characteristics for each country, ranging from GDP per capita to literacy and life expectancy rates to internet penetration. At the high end, Lebanon has a GDP per capita of \$6,017 and a life expectancy of 72 years, whereas at the other end of the spectrum, these figures stand at \$973 and 62 years for Yemen. Jordan has around 38.3 internet users per 100 citizens, as opposed to only .9 for Iraq. Taken together, these countries are home to over 70 percent of MENA's population and just under a third of its GDP. Many of the findings from this analysis will be of relevance to other MENA countries as well.

To differing degrees, the largest group of countries shares a French colonial heritage, including Morocco, Algeria, Tunisia, Lebanon and Syria. The French colonial administration left behind a functioning bureaucracy and well-defined legal framework. In these countries, as in many other civil code jurisdictions, the law plays a prominent role in many facets of public administration, including PFM. Egypt, Jordan, West Bank and Gaza, Iraq and, to a lesser extent, Yemen experienced varying degrees of British colonization. This was more deeply rooted in the former People's Democratic Republic of Yemen (also known as South Yemen), where Aden was colonized from 1839 to 1967, and in Egypt, which was colonized from 1882 to 1923. As with French colonization, the most lasting legacy has tended to be the civil administration and the legal background. As late as the fall of Saddam Hussein in Iraq, for example, the budget director in the Ministry of Finance relied on manuals and regulations dating from the British era.

While these countries come from disparate legal and administrative backgrounds, they share a number of features in common. Their Arabic language and Islamic heritage support a shared sense of identity. Most achieved independence around the same time, and in a number of cases their constitutions and legal frameworks were derived from similar sources. Their public sectors tend to be large and expensive, reflecting the need to absorb excess employment, as well as the statist or dirigiste principles that encapsulated the prevailing wisdom during their political formation in the 1940s and 1950s. Political movements such as pan-Arabism, and political parties, such as the Ba'ath, often had cross-border connections, as did many of the royal families through ties of blood and marriage. All of these factors have reinforced a sense of collective identity.

Beyond these cultural and historical linkages, there are numerous integrative institutions that reinforce this sense of collective character within the MENA region. The most prominent is the Arab League, or to give it its correct title, the League of Arab States, which has 22 members. While the Arab League typically deals with broader political issues, it has on occasion addressed the “good governance” agenda as well through forums such as the Alexandria Declaration in May 2004. While focusing mostly on legal and political reforms, the declaration also contained references to minimizing bureaucracy and increasing government efficiency, as well as encouraging privatization programs and passing laws that would obligate authorities to produce economic data and make it available and easily accessible. Of more specific interest to PFM reform agenda are groups such as the Arab Organization of Supreme Audit Institutions (ARABOSAI), a regional group of INTOSAI with 21 members.<sup>8</sup> The UNDP and OECD’s MENA Initiative on Governance and Investment for Development has recently began establishing a network of senior budget officials patterned after similar networks in Central and Eastern Europe. These organizations promote good practice among members and hold regular meetings to discuss issues of mutual interest.

### **Using the PEFA Ranking to Evaluate PFM in MENA**

To review PFM reform across MENA, it is necessary to utilize a common framework of analysis. In recent years, the Public Expenditure and Financial Accountability (PEFA) framework has become the most recognized and widely accepted tool for assessing the status of a given country’s PFM system. This set of twenty eight (28) high level indicators measures performance against best practice in developed and developing countries and allows progress to be tracked over time. An additional three indicators are used to track donor practices in heavily aid dependent settings.

The indicators analyze performance in the six core areas of public financial management spanning the budget process: (1) credibility of the budget; (2) comprehensiveness and transparency; (3) policy-based budgeting; (4) predictability and control in budget execution; (5) accounting, recording, and reporting; and (6) external audit. The central government is the main area of focus, along with issues relating to the overall scrutiny of public finances. Activities of public enterprises and sub-national levels of government are not addressed directly.

PEFA was not initially developed to facilitate cross country comparisons, but it is increasingly being used for this purpose. Paolo de Renzio, for example, recently compared the results of 57 PEFA assessments conducted prior to August 2007, including three from the MENA region (Jordan, Syria and the West Bank and Gaza).<sup>9</sup> Although at that point, the MENA sample was too small to draw any robust conclusions, de Renzio highlighted several interesting findings, including the large variation between average scores, the tendency for rankings to fall off as one progresses from budget

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<sup>8</sup> See <http://www.arabosai.org/en/index.asp>

<sup>9</sup> Paolo de Renzio, *What do PEFA Assessments tell us about PFM Reforms across Countries? Overseas Development Institute Working Paper No. 302*, 2009.

formulation through implementation to audit and accountability, and the utility in focusing on more narrow comparisons across certain sub-sets of countries.

Table 1.2 provides the summary results for the six PEFA assessments that have been completed for countries in the study. Assessments for the WBG and Syria were completed in 2006; Jordan in 2007; Iraq and Yemen in 2008; and Morocco in 2009.<sup>10</sup> A PEFA analysis is currently underway in Tunisia, but has not been finalized. It has yet to be conducted for two other countries in this study: Algeria and Lebanon. The PEFA alpha scale has been converted to a numeric scale ranging from 0 to 4 to assist with comparisons, where 4 is the highest rating. It should be noted that, while all PEFA assessments use the same framework, the scores reflect the judgment of the assessment team. Therefore undue weight should not be given to small differences across countries. Furthermore, PEFA is a tool that is applied to all countries—both developed and developing—which may also have an impact upon the MENA rankings.

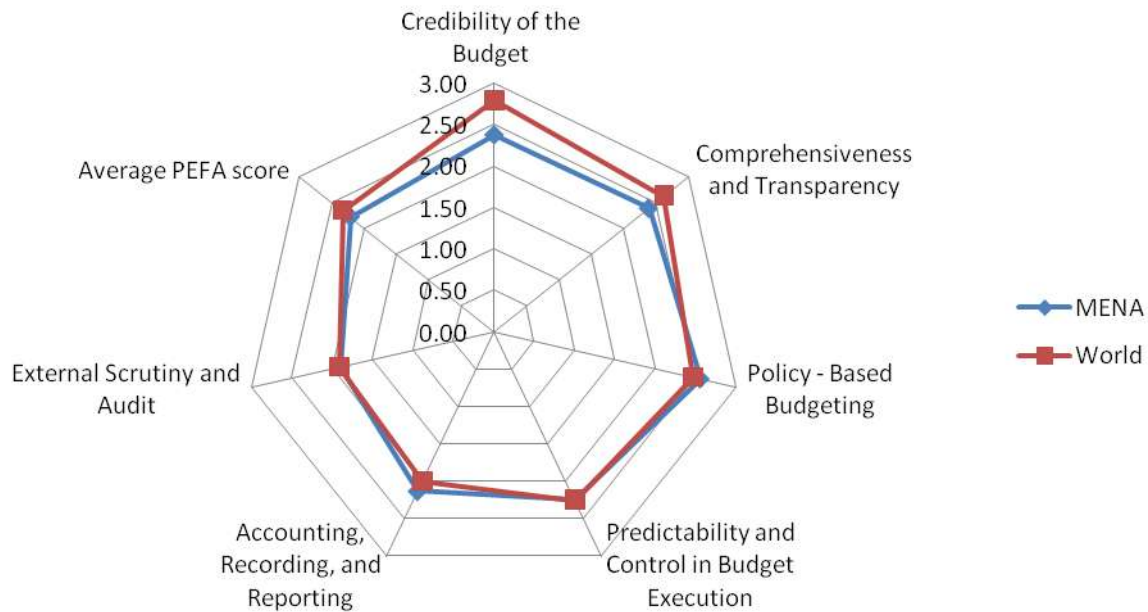
A comparative analysis was conducted as to where MENA countries stood vis-à-vis other countries at similar levels of development, in this case 19 lower middle income countries with GDPs from \$936 to \$3,075 per capita in 2007 who had recently completed PFEA assessment. (Among the list of comparators were three countries from Africa; three from Latin America and the Caribbean; six from East Asia and the Pacific; and seven from Europe and Central Asia.)<sup>11</sup> The results are presented in Figure 3.

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<sup>10</sup> Although a PEFA was presented for Egypt in October 2009, it remains preliminary, as the Government has not endorsed a number of the findings.

<sup>11</sup> The countries incorporated into this analysis include Congo Brazzaville, Lesotho, Swaziland, Dominican Republic, Paraguay, Peru, Indonesia, Samoa, Timor Leste, Tonga, Tuvalu, Vanuatu, Albania, Armenia, Azerbaijan, Kosovo, FYR Macedonia, Moldova and Ukraine.

**Figure 3: MENA PEFA Averages Compared to Global PEFA Averages for Comparable Low Middle Income Countries**



At an aggregate level, MENA's PFM systems are roughly comparable to those of other countries at similar income levels. As a whole, the region tends to do a bit better on accounting, recording and reporting, and a bit worse on credibility of the budget. (See the Appendix for a more detailed breakdown.)

Among the countries covered in this study, the highest ranked countries in aggregated PEFA rankings are Morocco and Jordan. They both have overall average scores of about B (2.87). On the lower end of the scale, West Bank and Gaza (WBG) and Iraq have PEFA Assessments that would average around a C- (1.5 to 1.6), although the formal PEFA assessments do not include minus (-) rankings. In terms of average scores for the six main categories, the tightest scores (i.e. the lowest standard deviation) were around credibility of the budget, indicating commonality among MENA countries on this dimension, whereas the largest average discrepancies were found in the area of budget comprehensiveness and transparency.

It is also interesting to note that there is a fairly high correlation between PEFA scores along various dimensions and the World Bank Institute's World Governance Indicators for controlling corruption in MENA (which, in turn, are tightly correlated with Transparency International's corruption rankings). The  $R^2$  value is around .92 and the correlation coefficient is .86, indicating that states that do well on PEFA also tend to do well on controlling corruption. However, given the small sample size, it is more difficult to make judgments about causality even though the  $R^2$  values and correlation coefficients are relatively high.

Though there is a large range in the overall country averages for the PEFA assessment, it is clear that the region as a whole has progressed in some areas more than others. This is best assessed at the level of sub-category because of the variability of scores within each category.

## **Where MENA has Ranked Consistently Higher**

When reviewing the MENA region's individual PEFA scores, four dimensions stand out as areas of strength. They include aggregate revenue outturns compared to the original approved budget; the comprehensiveness of information included in budget document; the orderliness and participation in the budget process; and the transparency of taxpayer obligations and liabilities. Each is discussed in greater detail below.

***Aggregate Revenue Outturn Compared to Original Approved Budget.*** Most countries scored solid A's (4.0) in this subcategory, which is part of the section "Credibility of the Budget." The exceptions were WBG and Syria, which both scored a B (3.0). This indicates that the countries were meeting, or exceeding, the forecast future revenue flows and therefore could be confident about financing the budget. Over-achieving the revenue projection often occurs where conservative assumptions are used—particularly when projecting petroleum revenues. While the PEFA system does not penalize countries that exceed the revenue projections included in the budget, it should be noted that this outcome can lead to a problems where the "excess" revenue is distributed as part of a supplementary budget during the year. This is the sub-category with the lowest standard deviation among all 28 indicators, indicating the tightest clustering among countries.

***Comprehensiveness of Information Included in Budget Documentation.*** This sub-category falls within the section, "Comprehensiveness and Transparency." A number of countries scored A's (4.0) in this subcategory, but the average was reduced by very low scores for Syria and Iraq, which both scored a D (1.0). The scores suggest that the countries who have taken an interest in the issue have made good progress.

***Orderliness and Participation in the Budget Process.*** Most countries scored well in this subcategory, which is in the section "Policy Based Budgeting." Yemen and Morocco stood out with A's (4.0), while the main exception was Iraq with a C (2.0). This indicates that budgets are generally prepared on time and follow a well defined process—although it makes no comment about the quality of the budget that is prepared.

***Transparency of Taxpayer Obligations and Liabilities.*** This subcategory, which is in the section "Predictability and Control of Budget Execution," was an area in which the region did particularly well (scores of A's and B's for all countries).

## **Where MENA has Ranked Consistently Lower**

There are a number of elements of the PEFA where the scores are consistently weak. They include the composition of expenditure outturns compared to the original approved budget; the effectiveness of internal audit; the quality and timeliness of annual financial statements; and external scrutiny and audit.

***Composition of Expenditure Outturns Compared to Original Approved Budget.*** This subcategory is in the section "Credibility of the Budget" and received poor rankings. All countries scored a C (2.0), with the exception of Syria and Jordan which both scored D's (1.0). The low scores could reflect a number of problems. Either there are weaknesses in the budget that result in inappropriate allocations, or there are inadequate controls exerted during budget execution. This was the sub-category with the highest standard deviation, indicating the greatest discrepancy between countries.

***Effectiveness of Internal Audit.*** This subcategory is within the section, "Predictability and Control in Budget Execution," and was consistently low throughout the region. The MENA countries scored between a C+ (2.33) and D (1.0). The subcategory, "Competition, Value for Money and Controls in

Procurement,” is another area requiring improvement, with low scores for all countries other than Morocco and Jordan, which had B’s (3.0).

***Quality and Timeliness of Annual Financial Statements.*** This subcategory is part of the section, “Accounting, Recording, and Reporting,” and had modest rankings throughout the region (between C+ and D+, or 2.33 and 1.33). The low score could reflect poor quality accounting systems, or the low importance attached to the external audit function.

***External Scrutiny and Audit.*** This category of the PEFA assessment had the lowest average scores. The subcategories, “Scope, Nature and Follow-up of External Audit” and “Legislative Scrutiny of External Audit Reports” ranked low in every MENA country, ranging from a score of C+ to D. The exception was Yemen, which scored a B+ in “Scope, Nature, and Follow-up of External Audit.” This reflects weaknesses in both the capacity of the external audit body and of the legislative body charged with follow up on the reports that are prepared, as well as the general preeminence of the executive vis-à-vis the legislative branches

Table 3: PEFA Scores for the MENA Countries in the Study

		Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Credibility of the Budget	Aggregate expenditure out-turn compared to original approved budget	NA	NA	1.00	4.00	NA	4.00	2.00	NA	3.00	1.00	<b>2.50</b>
	Composition of expenditure out-turn compared to original approved budget	NA	NA	2.00	1.00	NA	2.00	1.00	NA	2.00	2.00	<b>1.67</b>
	Aggregate revenue out-turn compared to original approved budget	NA	NA	4.00	4.00	NA	4.00	3.00	NA	3.00	4.00	<b>3.67</b>
	Stock and monitoring of expenditure payment arrears	NA	NA	1.00	1.00	NA	2.33	NA	NA	1.33	-	<b>1.42</b>
	<b>Average score for Credibility of the Budget</b>			<b>2.00</b>	<b>2.50</b>		<b>3.08</b>	<b>2.00</b>		<b>2.33</b>	<b>2.33</b>	<b>2.37</b>
Comprehensiveness and Transparency	Classification of the budget	NA	NA	2.00	4.00	NA	4.00	1.00	NA	1.00	2.00	<b>2.33</b>
	Comprehensiveness of information included in budget documentation	NA	NA	1.00	4.00	NA	3.00	1.00	NA	3.00	4.00	<b>2.67</b>
	Extent of unreported government operations	NA	NA	1.33	3.00	NA	2.33	2.00	NA	2.33	3.33	<b>2.39</b>
	Transparency of Inter-Governmental Fiscal Relations	NA	NA	1.00	3.33	NA	2.00	2.33	NA	1.33	4.00	<b>2.33</b>
	Oversight of aggregate fiscal risk from other public sector entities	NA	NA	1.00	3.33	NA	3.00	2.00	NA	1.33	2.00	<b>2.11</b>
	Public Access to key fiscal information	NA	NA	1.00	3.00	NA	4.00	1.00	NA	2.00	2.00	<b>2.17</b>
	<b>Average score for Comprehensiveness and Transparency</b>			<b>1.22</b>	<b>3.44</b>		<b>3.06</b>	<b>1.56</b>		<b>1.83</b>	<b>2.89</b>	<b>2.33</b>
Policy-Based Budgeting	Orderliness and participation in the annual budget process	NA	NA	2.00	3.33	NA	4.00	3.33	NA	2.33	4.00	<b>3.17</b>
	Multi-year perspective in fiscal planning, expenditure policy and budgeting	NA	NA	1.33	3.33	NA	2.33	1.33	NA	1.00	3.00	<b>2.05</b>
	<b>Average score for Policy - Based Budgeting</b>			<b>1.67</b>	<b>3.33</b>		<b>3.17</b>	<b>2.33</b>		<b>1.67</b>	<b>3.50</b>	<b>2.61</b>
Predictability and Control in Budget Execution	Transparency of taxpayer obligations and liabilities	NA	NA	3.00	3.00	NA	4.00	NA	NA	NA	3.00	<b>3.25</b>
	Effectiveness of measures for taxpayer registration and tax assessment	NA	NA	2.00	2.33	NA	3.33	NA	NA	NA	3.00	<b>2.67</b>
	Effectiveness in collection of tax payments	NA	NA	1.33	3.00	NA	3.33	NA	NA	NA	1.33	<b>2.25</b>
	Predictability in the availability of funds for commitment of expenditures	NA	NA	2.33	4.00	NA	2.33	1.33	NA	1.33	1.33	<b>2.11</b>
	Recording and management of cash balances, debt and guarantees	NA	NA	2.00	3.33	NA	4.00	2.33	NA	2.00	3.33	<b>2.83</b>
	Effectiveness of payroll controls	NA	NA	1.33	3.00	NA	3.33	1.33	NA	2.33	1.33	<b>2.11</b>
	Competition, value for money and controls in procurement	NA	NA	1.33	3.00	NA	3.00	1.00	NA	NA	1.33	<b>1.93</b>
	Effectiveness of internal controls for non-salary expenditure	NA	NA	1.33	3.00	NA	2.33	3.33	NA	1.33	1.33	<b>2.11</b>
	Effectiveness of internal audit	NA	NA	1.33	2.00	NA	2.33	2.33	NA	2.00	1.33	<b>1.89</b>
	<b>Average score for Predictability and Control in Budget Execution</b>			<b>1.78</b>	<b>2.96</b>		<b>3.11</b>	<b>1.94</b>		<b>1.80</b>	<b>1.92</b>	<b>2.25</b>



		Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
<b>Accounting, Recording, &amp; Reporting</b>	Timeliness and regularity of accounts reconciliation	NA	NA	2.33	3.33	NA	4.00	3.00	NA	2.00	3.00	<b>2.94</b>
	Availability of information on resources received by service delivery units	NA	NA	1.00	1.00	NA	3.00	2.00	NA	1.00	3.00	<b>1.83</b>
	Quality and timeliness of in-year budget reports	NA	NA	1.33	2.00	NA	3.33	1.33	NA	3.00	1.33	<b>2.05</b>
	Quality and timeliness of annual financial statements	NA	NA	1.33	2.00	NA	1.33	2.00	NA	1.33	2.33	<b>1.72</b>
	<b>Average score for Accounting, Recording, and Reporting</b>			<b>1.50</b>	<b>2.08</b>		<b>2.92</b>	<b>2.08</b>		<b>1.83</b>	<b>2.42</b>	<b>2.14</b>
<b>External Scrutiny &amp; Audit</b>	Scope, nature and follow-up of external audit	NA	NA	-	2.00	NA	1.33	2.33	NA	1.00	3.33	<b>2.00</b>
	Legislative scrutiny of the annual budget law	NA	NA	1.00	4.00	NA	3.33	2.33	NA	2.33	2.33	<b>2.55</b>
	Legislative scrutiny of external audit reports	NA	NA	1.00	2.00	NA	1.33	1.33	NA	1.00	1.33	<b>1.33</b>
	<b>Average score for External Scrutiny and Audit</b>			<b>1.00</b>	<b>2.67</b>		<b>2.00</b>	<b>2.00</b>		<b>1.44</b>	<b>2.33</b>	<b>1.91</b>
	<b>Average PEFA score per Country</b>			<b>1.58</b>	<b>2.87</b>		<b>2.87</b>	<b>1.92</b>		<b>1.64</b>	<b>2.42</b>	<b>2.22</b>
Standard 4.0 Scale:												
A (highest)												
A-												
B+												
B												
B-												
C+												
C												
C-												
D+												
D												
D- (lowest)												
Bolded numbers (not underlined) indicate scorings represent an average of the scores for the dimensions making up that indicator, all others												

## MENA Country Templates and Case Studies on PFM Reform

While the PEFA data provides an important overview, it tells only part of the story. Future PEFA exercises will allow for benchmarking progress, but the exercise is relatively new in the region and currently they provide a one-time snapshot of the quality of PFM practices within a given country. To gain a more comprehensive and dynamic picture, this analysis has been augmented by a series of country chapters, which are provided in Volume 2. These chapters were drafted along a common template and have sought to utilize a modified PEFA framework to provide a more nuanced picture of the PFM reform efforts in the countries of this study. These assessments have also sought to go beyond the “what” of PFM reform and capture some of the “how” and “why” behind the reforms, touching upon both strategies for implementation and broader political economy issues within a given country.

In two cases of particularly interesting and far-reaching reform in MENA, the analysis relies on more detailed case studies. The first is Salam Fayyad's PFM reforms, which were implemented during his first tenure as Minister of Finance in West Bank & Gaza from 2002 to 2005. The second are the reforms in tax policy and administration that have been implemented in Egypt since 2004 under the tenure of Youssef Boutros Ghali.<sup>12</sup> These reforms are singled out both because they were substantial in scope and are widely perceived to be the most successful of their type within the MENA region. They are the subject of more detailed World Bank case studies being developed through a joint case writing program between the Bank and the Dubai School of Government.<sup>13</sup>

Finally, it is worth stating that the PEFA scores do not in themselves provide a guide to the relative priority that should be given to reform activity. They are an important indicator but the assessment of priorities requires a fuller analysis. For example, if a country has sizable expenditure arrears then it may be more important to raise a score from 2 to 3 in this indicator than to improve a score of 1 in another area. Similarly, a low score on the transparency of inter-government relations will have different implications for a country with a highly decentralized system from one that is dominated by the central government.

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<sup>12</sup> The analysis of Salam Fayyad's reforms is captured in Nithya Nagarajan, *Reforms in Public Financial Management: West Bank & Gaza*, and Nithya Nagarajan, *Egypt: Overhaul of Tax Policy and Administration*, (World Bank and Dubai School of Government: *MENA Governance Case Program*, 2010). Egypt's reforms in tax administration are captured in a *Doing Business* case study by Rita Ramalho, *Adding a Million Taxpayers* (World Bank: *Doing Business*, 2008).

<sup>13</sup> Since 2005, the World Bank has been working with the Dubai School of Government to identify and draft cases on indigenous examples of governance and public sector reform drawn from throughout the MENA region. These cases will be published in a book, *Governance Reform in the Middle East and North Africa: The Lessons from Experience* (forthcoming).

## Chapter 2

### The Substance of Public Financial Management Reform: What Reforms are Needed and Which are Working?

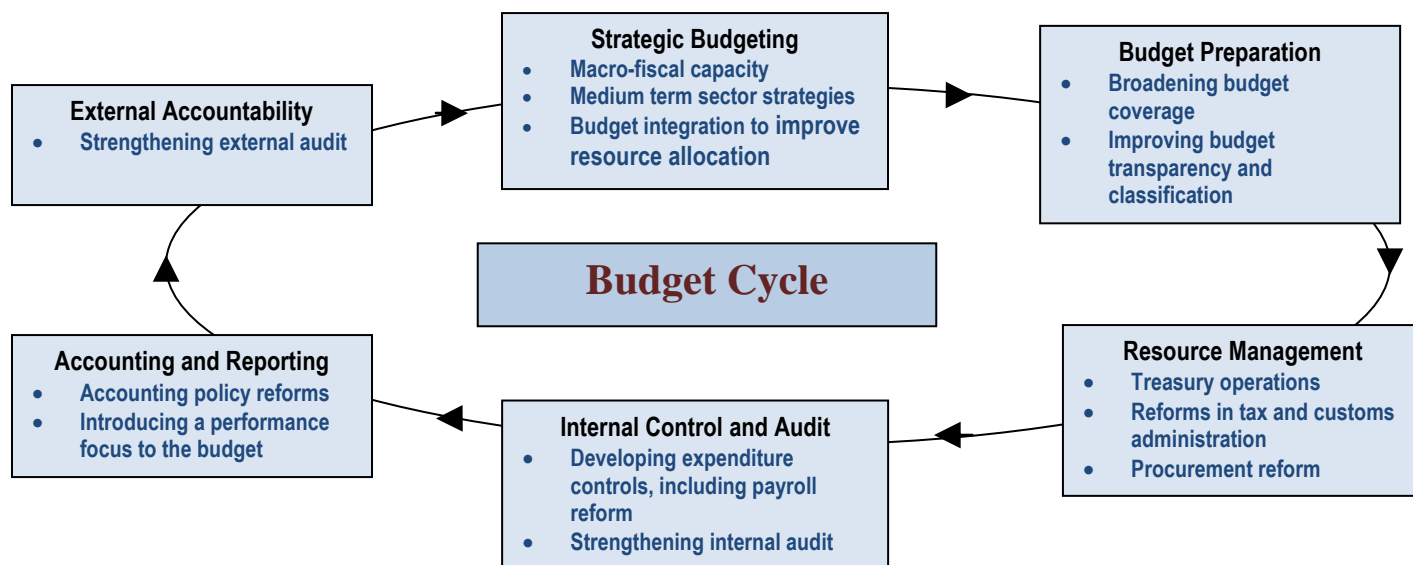
*In warfare everything is simple.  
But the simple is often quite difficult.*

-- Karl von Clauswitz –

Although Clauswitz's famous dictum focuses on a more elemental field of human endeavour, it could easily apply to the discipline of public financial management. At one level, the goals of PFM are obvious and straightforward. Spend money efficiently within an envelope that is affordable and sustainable, in accordance with established procedures, on activities that will maximize a country's long-term development potential. But while the objectives are simple, their realization is typically anything but.

This section reviews the main PFM reforms being pursued by countries in the region. The aim is to highlight which reforms are making progress (and which are not), as well as to set out some of the technical issues associated with the reforms. The analysis draws from the country case studies in Volume 2 and is structured around some common categories of PFM reform. The selection of categories follows the work of Andrews,<sup>14</sup> who assesses reforms at six different stages of the budget cycle. However the categories have been adapted to reflect common reform activity in the MENA region. Figure 4 sets out the different stages in the budget cycle and the reform categories considered at each stage.

**Figure 4: Reforms at Different Stages of the Budget Cycle**



<sup>14</sup> Andrews, *PFM in Africa: Where Are We, How Did We Get There, and Where Should We Go?* Transparency and Accountability Project, the Brookings Institute and the World Bank. See the following webpage: <http://www.resultsfordevelopment.org/sites/default/files/resources/PFM-in-Africa-pdf.pdf>.

The choice of reform categories involved a number of compromises and several important reforms that have close links to PFM are not considered. For example, tax and expenditure policy reforms, and civil service reforms are often closely associated with the reform of the PFM system. However, these reform areas are not included in the PEFA framework and including them in the study would have extended the analysis.

Determining whether to create separate categories for some wide-ranging reforms was also an issue. In particular, two common reforms—Medium Term Expenditure Frameworks (MTEFs) and treasury reforms—often cover a number of the above categories. These reforms are considered in their component parts during the discussion. In particular, components of MTEF are considered under both macro fiscal capacity and medium term expenditures, while components of treasury reforms are considered under treasury operations, expenditure controls and accounting policy reforms. A similar situation applies with the reform of the legislative framework for PFM. Rather than consider legislative issues as a separate component, legislative reforms are included where relevant in the different categories. Conversely reforms in budget transparency that occur at a variety of stages in the budget cycle (for example budget documentation, in year financial reporting, and end of year financial statements) are considered in a single category.

For each of the six stages of the budget cycle the relevant PEFA scores are first reported, followed by an assessment of each of the reform areas relevant to this stage. For each reform area, the report sets out briefly the underlying objective of this type of reform before reviewing experience in different MENA countries. It then provides an assessment of what has worked and what has proven to be more challenging.

## 1. Strategic Budgeting

**Table 4: Relevant PEFA Scores for Strategic Budgeting**

	Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Multi-year perspective in fiscal planning, expenditure policy and budgeting	NA	NA	1.33	3.33	NA	2.33	1.33	NA	1.00	2.33	<u>1.94</u>
Aggregate expenditure out-turn compared to original approved budget	NA	NA	1.00	4.00	NA	4.00	2.00	NA	3.00	1.00	<u>2.50</u>
Aggregate revenue out-turn compared to original approved budget	NA	NA	4.00	4.00	NA	4.00	3.00	NA	3.00	4.00	<u>3.67</u>

## Macro-Fiscal Capacity

**Why is the Reform Important?** Having a unit in the Ministry of Finance to provide macroeconomic and fiscal (macro-fiscal) policy advice is important for good aggregate fiscal management. A key task of the unit would be to assist in developing a medium term fiscal framework (MTFF) for the preparation of the budget. The aim of an MTFF is to guide the preparation of the budget so that fiscal policy is consistent with the government's monetary and exchange rate policies and debt levels are kept sustainable. The unit can also monitor progress with budget execution and advise whether a change to the budget stance is warranted during the year.

**What is Happening in the Region?** The Ministries of Finance in the region have traditionally not had a strong macro-fiscal capacity. To the extent that this capacity existed within government, it was

within the planning ministry. It tended to focus on contributing to planning activities, such as a five year plan, or general economic forecasting.

In recent years Jordan, Egypt, Lebanon and Yemen have started to develop some capacity in the Ministry of Finance to provide macro-fiscal advice.<sup>15</sup> Initially, many of these units focused on monitoring taxes, and the work was geared towards preparing monthly reports on budget execution. These monthly reports tended to be exercises in data dissemination rather than analysis, but the generation of these reports has proven to be a useful tool to develop capacity in the units. The units have been less active in providing policy advice on fiscal management. This capability can be expected to expand as the capacity of the unit improves and more ministers look for this advice.

As the units increase their capacity, they have become more involved in budget preparation through developing an MTFF. In many countries, the links between the MTFF and the final budget is still not strong, and this will require further development before the reform can be considered successful.

To carry out their role effectively, these units need to recruit staff with good analytical skills. The public sector pay and conditions make it difficult to attract such staff. It is therefore not surprising that in some countries (e.g. Egypt and Lebanon), the officials working on these issues are not serving under standard public sector terms and conditions. Even with these contracts, there will be a challenge to retain staff as they develop experience.

Where it has not been possible to recruit staff on special contracts, it has been necessary to tailor the work of the unit to the capabilities of the staff available. In particular, as discussed above, where staff have limited economic forecasting skills, the units have given priority to fiscal reporting and forecasting. The unit has relied on other institutions (such as the central bank) for the relevant macroeconomic data.

**Assessment.** The establishment of a macro-fiscal unit has become important, as Ministries of Finance have attempted to develop a MTFF to guide the preparation of the budget. The work is analytically demanding, and attracting suitable staff within standard civil service contracts has proven to be a challenge. By initially focusing on fiscal forecasting, many units have made progress in preparing an MTFF, although the link between this and the preparation of the budget needs to improve.

## **Medium Term Perspective**

**Why is the Reform Important?** In fiscal management, the cost of a policy in the next year is not always a good indication of its costs over time. For example, capital expenditures on a new school in one year can lead to a need for additional operating expenditure in the future. Similarly, some expenditure is driven by demographic movements that can change substantially over time. While the legal focus is on the annual budget, it is recognized that governments need to understand and make provision for the expenditure implications of policies in the coming years (typically the next three years).<sup>16</sup> To be implemented effectively, this requires a “bottom up” assessment of the medium term cost of existing policy—or “forward estimates”—often as part of a Medium Term Expenditure Framework (MTEF) reform.<sup>17</sup>

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<sup>15</sup> Although in Lebanon’s case, it was led by consultants outside the Ministry of Finance.

<sup>16</sup> Taking a medium term perspective also helps avoid ad hoc and across the board expenditure cuts when fiscal adjustment is required, as it recognizes the value of targeted savings that take time to bear fruit.

<sup>17</sup> The term MTEF is generally used to refer to a group of budget reforms—including the development of a Medium Term Fiscal Framework (MTFF), which is considered as part of the macro-fiscal section above.

***What is Happening in the Region?*** A number of countries in the MENA region are attempting to develop forward estimates as part of MTEF reforms, but none has a functioning system at present. The work has generally been carried out through pilot projects in various sectors. This is the approach that is being followed in Jordan and Lebanon. The PEFA assessments indicate that the lack of a medium term focus continues to be a major weakness in the region.

The development of sectoral forward estimates as part of an MTEF is a very resource intensive reform. Countries with limited capacity for reform might well decide not to embark on this initiative—an approach taken by Iraq. Even Jordan has faced delay with the reform because senior management has been distracted by the other PFM reforms taking place.

One of the challenges with this reform has been ensuring that it is integrated with the core budget preparation process. In Morocco and Tunisia, which were the first countries in the region to attempt to develop medium term forward estimates, the exercise remains separate from the budget itself and is viewed more positively by sector ministries than the Ministry of Finance. Although the forward estimates beyond the budget year are not legally binding, they do provide sectoral ministries with additional confidence of future resources. Conversely, some Ministries of Finance view the forward estimates with suspicion—taking the view that they restrict the “flexibility” with which the Ministry of Finance can manage budget preparation in the future. This is a concern of the budget directorate in Morocco, which has avoided implementing the reforms fully because it fears being tied by the forward expenditure estimates.

Another challenge with the preparation of forward estimates is ensuring that they focus on both the recurrent and capital budgets. In countries where the two budgets are not well-integrated, this does not always happen. In Jordan, for example, the focus of the estimates is on projects and not sufficiently on recurrent expenditures. Identifying the future recurrent implications of current capital expenditure is one of the more important elements of forward estimates, but it is also important to identify changes in recurrent expenditure needs that are not directly linked to projects.

***Assessment.*** The argument for developing sector based forward estimates to provide a medium term perspective is compelling, but this is a major reform and should only be initiated once more basic improvements to the PFM system have been completed. While there is merit in starting the reform by working with pilot sectors, it is critical that the Ministry of Finance is supportive and committed to using the output in budget preparation. It is also important that the forward estimates include recurrent expenditures as well as projects in order to have a comprehensive picture.

## **Budget Integration to Improve Resource Allocation**

***Why is the Reform Important?*** By integrating the management of operating and capital expenditures in the budget, the quality of government expenditure can be improved. In dual budgeting systems, there are often inconsistencies between the two budgets. For example, insufficient resources may be made available to maintain investments once they are complete. More generally, with a dual approach to budgeting, the link between policy interventions and the budget is weakened. High level allocations for the investment or operating budgets are more important in determining the final budget allocations than an assessment of the right mix of operating and capital expenditures for the sector.<sup>18</sup>

***What is Happening in the Region?*** All countries in the region inherited systems of budget management that separated recurrent expenditure from capital expenditure, and many continue to have

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<sup>18</sup> While the term capital budget is used in this report, the non-recurrent budget is variously referred to as the capital, investment, or development budget by countries in the region.

separate ministries managing the two budgets. In addition to the separation of responsibility for budget management at the central institutions, there is generally further fragmentation at the level of line ministries with separate finance and planning departments responsible for the two budgets. Although the dual budgeting system is a legacy from the colonial powers, it is ironic that neither Britain nor France currently operates a dual budget.

In several countries in the region, noticeably the Maghreb countries and more recently Syria, the management of the two budgets is under the Ministry of Finance. However, even with this institutional integration, the Ministry of Finance operates separate processes in preparing the two budgets. Algeria integrated the management of the two budgets within sectoral units in the budget department in 2008, in an attempt to unify the processes.

While it is possible that budget integration could be achieved without consolidating budget management in one ministry, in practice the transaction costs of managing this transition have proven to be an impediment to effective integration. Jordan is one of a number of countries in the region that has received on-going advice from the IMF and the World Bank to consolidate budget management within the Ministry of Finance to assist integration. While the advice appears to be accepted at a technical level, no change has occurred. In Lebanon, some argue that integrating the capital budget within the Ministry of Finance would concentrate too much power under one minister. At present, the capital budget is managed by a separate agency reporting to the Prime Minister. In these circumstances, unless there is a strong political will to overcome institutional resistance, efforts to achieve budget integration are unlikely to be successful.

One of the key challenges when shifting institutional responsibility for the management of the capital budget to the Ministry of Finance is to develop the necessary analytical capacity in the relevant MOF staff. In general, Ministries of Finance have tended to manage the recurrent budget through incremental changes to the prior period budget. Planning ministries have often developed a broader range of project appraisal skills and are more experienced at assessing how projects fit with sectoral strategies. The different capacity of the two institutions has been one reason why some donors have favored maintaining their relationship with the Ministry of Planning for donor financed capital expenditures. The reform in Syria presents an interesting case study. When the management of the investment budget in Syria was transferred from the State Planning Commission to the Ministry of Finance, it was expected that many of the staff would be transferred as well. In practice, many of the staff were reluctant to leave the State Planning Commission, and this left the Ministry of Finance poorly equipped to manage its new responsibilities. In view of this, the Budget Department established a specialist unit to manage the investment budget. So while budget management has been consolidated at the Ministry of Finance, the procedures for the two budgets remain distinct.

While integration of budget management has proven difficult in the region, some of the countries have taken steps to integrate the presentation of the two budgets. For example, Algeria now has a unified budget presentation. The West Bank and Gaza also presented its 2009 budget on an integrated basis. This can be a useful first step towards more substantive budget integration.

The issue of budget integration will become more pressing as countries move to introduce a performance focus to budget management. It is an anathema to performance budgeting to have processes for managing the preparation of the budget based on the nature of the expenditure inputs. The same applies to the separation of management between planning and finance departments within a line ministry. In a performance budgeting environment, it will ultimately be important to reduce restrictions on the use of inputs, which would make the budget split redundant. Moreover, it will be important to have a single process for monitoring the sectoral ministry as part of the accountability framework.



**Assessment.** All countries in the region continue to have elements of dual budgeting. While some progress has been made to integrate the presentation of the budget, efforts to integrate other elements of budget management have largely been elusive. In countries with a separate planning ministry managing the capital budget, institutional resistance to consolidating the budget management processes has been a particular problem. Where consolidation of budget management within the Ministry of Finance does occur, one of the main challenges is to ensure that the Ministry has the necessary analytical capacity to oversee the capital budget. For this reason, the transition needs to be carefully planned.

## 2. Budget Preparation

**Table 5: Relevant PEFA Scores for Budget Preparation**

	Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Orderliness and participation in the annual budget process	NA	NA	2.00	3.33	NA	4.00	3.33	NA	2.33	4.00	<u>3.17</u>
Classification of the budget	NA	NA	2.00	4.00	NA	4.00	1.00	NA	1.00	2.00	<u>2.33</u>
Comprehensiveness of information included in budget documentation	NA	NA	1.00	4.00	NA	3.00	1.00	NA	3.00	4.00	<u>2.67</u>
Transparency of Inter-Governmental Fiscal Relations	NA	NA	1.00	3.33	NA	2.00	2.33	NA	1.33	4.00	<u>2.33</u>
Public Access to key fiscal information	NA	NA	1.00	3.00	NA	4.00	1.00	NA	2.00	2.00	<u>2.17</u>
Quality and timeliness of in-year budget reports	NA	NA	1.33	2.00	NA	3.33	1.33	NA	3.00	1.33	<u>2.05</u>
Quality and timeliness of annual financial statements	NA	NA	1.33	2.00	NA	1.33	2.00	NA	1.33	2.33	<u>1.72</u>

### Broadening Budget Coverage

**Why is the Reform Important?** There are two key reasons for ensuring that the scope of the budget is broad. First, the budget is the main mechanism for accountability—of both the executive to parliament as well as within the executive. Because alternative accountability mechanisms are often not put in place, extra-budgetary expenditures are not subject to adequate oversight. In addition, the budget is the main instrument for fiscal management. When expenditure takes place outside the budget, it undermines the budget’s effectiveness as a mechanism for fiscal control and a process for allocating resources to the government’s highest priority areas.

**What is Happening in the Region?** Limitations in the scope of the budget are a general problem in the region. In Algeria and Morocco, the budget is fragmented with numerous special treasury accounts outside the general budget—although in the case of Morocco, there is disclosure of the fiscal information relating to these special accounts in the budget documents. In Egypt, significant third party revenues and unused budget allocations have been used for extra-budgetary expenditure, while in Lebanon the coverage of projects financed by foreign donors has not been adequately captured in the budget. Although the PEFA assessments do not address this issue directly, the low scores for unreported government expenditure support the view that this is an area of weakness.

One of the challenges in extending the scope of the budget is that there are strong incentives for those benefiting from the current arrangements to resist the change. In Egypt, the Ministry of Finance attempted to rein in extra-budgetary expenditures as part of its treasury reform. While significant



balances were initially brought back to the Central Bank of Egypt, these were kept separate from the government's main bank accounts, and the procedures for the management of the expenditures were not amended. Some of the balances later returned to commercial banks—effectively unwinding the initiative, although the IMF has recently reported that the reform is on track.

In Lebanon, the coverage of foreign financed projects in the budget was considered a delicate political issue, as the current arrangement gives the Prime Minister considerable influence over these expenditures. In 2007, a budget law was drafted allowing for the integration of the largest extra-budgetary entities into the budget—although this was only to the extent of the aggregate flows. However, the law is yet to pass. It failed to address the extra-budgetary expenditure of other large entities, such as those providing health services; family allowances and pensions; and financing to the country's 927 municipalities.

The technical demands of extending budget scope and coverage are not significant, and good progress can be made where there is the political commitment. For example, in Jordan, a number of steps have been taken to extend the coverage of the budget, and the PEFA assessment indicates that only a small proportion of total expenditures are not covered. However, there needs to be a strategic approach taken to these reforms which anticipates the likely resistance from vested interests.

**Assessment.** Improving budget coverage is important to promote accountability for government expenditure and to support the effective allocation of resources. While the technical demands are not significant, improving the coverage of the budget has proven to be difficult for many countries in the region. There are strong vested interests in the existing arrangements, and this is a reform that requires firm political commitment if it is to be successful.

### **Improving Budget Transparency and Classification**

**Why is the Reform Important?** The need for better information on budgeted expenditures is one element of a general trend towards improved budget transparency in developed countries. This reflects the view that greater transparency in budget documents can play an important role in building the credibility of the government's fiscal policy with the public, parliament and external financiers. Reforming the budget classification is an important component of this broader objective. Traditional budget classifications have tended to mix expenditures of different economic nature, and it was often difficult to obtain a clear understanding of what was happening with the government's accounts.

**What is Happening in the Region?** Many countries in the region are reforming the economic classification used in the budget to align with the classification used in the IMF's Government Financial Statistics (GFS) 2001.<sup>19</sup> This change has recently been made in Egypt, Yemen and Iraq, while Tunisia is developing a new classification for use in 2015. Morocco has a budget classification that is broadly consistent with GFS, while Lebanon has had a classification aligned with the earlier GFS 1986 since the late 1990s. Both Algeria and Syria have developed a new economic classification based on the GFS 2001 but have yet to implement it. The improvements in economic classification are reflected in relatively high PEFA scores for the quality of budget classification for a number of countries.

While many of the above countries focused solely on the economic classification, Jordan has taken a more comprehensive approach and developed a new chart of accounts as part of its GFMIS project.

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<sup>19</sup> While the GFS 2001 is an accrual system, these countries are generally using the classification while following cash based accounting.

This includes a revised economic classification in line with GFS 2001, along with new administrative, functional, fund and geographic classifications.

There are reports that the changes to the economic classification have substantially improved the quality of fiscal information in some countries. The benefits of changes to the administrative classification are not as obvious, but are also important as they can improve the accountability for budget allocations. As the administrative classification is also often used to approximate the purpose of expenditure (function), it can be very important in improving the quality of information for policy-makers.

It has been common for those providing technical assistance in the PFM area (particularly the IMF) to help countries prepare a new economic classification. Once the classification is updated, its use tends to become embedded within the PFM system and the reform becomes enduring and self-sustaining. However, a major investment is required to train staff during the transition. In Iraq, the training on the new classification system was viewed by some as inadequate, and this has reduced the quality of information produced.

In addition to reforming the budget classification, many MENA countries have taken steps to improve the transparency of budget reporting. One sign of these improvements is that the *Open Budget Index* recently improved Egypt's ranking from near the bottom (a rating of "provides scant to no information") towards the middle ("provides some information")—a significant improvement from 2006 to 2008.<sup>20</sup> Tunisia prepares well documented and easy to understand budget documents, although only with a one year horizon. Jordan's budget documents meet almost all information benchmarks required by transparent practice, one omission being a list of financial assets. In Morocco and Algeria, the documents are extensive, although there are important gaps and the information is not always user friendly. For example, in Algeria there is a lot of general information but no fiscal balance, no information on public corporations and no information on contingent liabilities. Yemen, Iraq, and West Bank and Gaza have also increased the information content of their budget documents—again with some gaps.

Another important initiative has been to provide monthly reports on budget execution during the year. This is now happening in Morocco, Egypt, Jordan, West Bank and Gaza and Lebanon. These reports are generally posted on the relevant Ministry of Finance website. The PEFA scores for this subcategory reflect some progress in this area, although the overall performance is mixed.

There are some specific features of this reform that have helped to make it successful. First, the preparation of the information is generally carried out by a small number of staff within the Ministry of Finance. As such, it is easier for technical assistance to initiate the work and for these changes to be maintained. Second, as the reports are prepared on a frequent cycle, they become part of the routine of the relevant staff. In West Bank and Gaza, it has become a source of pride for the Ministry of Finance staff that the reports are always prepared by the 15<sup>th</sup> of the following month—which is reflected in their relatively high PEFA score. Finally, while increased transparency can be a powerful tool, there are likely to be fewer vested interests opposed to the presentation of specific information.

**Assessment.** There has in general been good progress in improving the quality of budget classification and the transparency of budget documents. After initial technical assistance, the budget classification reforms in particular have been enduring once the change was introduced. Similarly, monthly reporting and improvements to the transparency of budget documents has often been enduring. This is in part because the reforms rely on a small team of staff in the Ministry of Finance for

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<sup>20</sup> See <http://www.openbudgetindex.org/>.

implementation, which makes them better placed to succeed in an environment where the civil service has limited capacity. Moreover, because the reforms are considered technical, they have tended to meet less opposition from vested interests than many other PFM reforms.

### 3. Resource Management

**Table 6: Relevant PEFA Scores for Resource Management**

	Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Predictability in the availability of funds for commitment of expenditures	NA	NA	2.33	4.00	NA	2.33	1.33	NA	1.33	1.33	<u>2.11</u>
Recording and management of cash balances, debt and guarantees	NA	NA	2.00	3.33	NA	4.00	2.33	NA	2.00	3.33	<u>2.83</u>
Transparency of taxpayer obligations and liabilities	NA	NA	3.00	3.00	NA	4.00	NA	NA	NA	3.00	<u>3.25</u>
Effectiveness of measures for taxpayer registration and tax assessment	NA	NA	2.00	2.33	NA	3.33	NA	NA	NA	3.00	<u>2.67</u>
Effectiveness in collection of tax payments	NA	NA	1.33	3.00	NA	3.33	NA	NA	NA	1.33	<u>2.25</u>
Competition, value for money and controls in procurement	NA	NA	1.33	3.00	NA	3.00	1.00	NA	NA	1.33	<u>1.93</u>

### Treasury Operations

**Why is the Reform Important?** A well functioning treasury system can reduce the cost and risk of government operations.<sup>21</sup> In particular, it can improve cash management and minimize the government's net borrowing costs. By consolidating cash holdings, it can also reduce the government's exposure to the risk of bank default.

**What is Happening in the Region?** A number of the countries in the region have embarked on treasury reforms to improve cash management. While progress has been made, the reforms have not always been implemented as originally envisaged.

In general, the reforms have involved establishing a treasury single account (TSA) at the central bank, with a series of transaction accounts holding "zero balances" at commercial banks. This arrangement allows cash to be consolidated in an account at the central bank while utilizing commercial banks for branch network operations. When fully developed, the reforms involve active cash planning to understand the cash needs of the government so that the consolidated cash balances can be managed on a daily basis. Although the reform should also be associated with steps to improve debt management, few countries in the region have made progress in this area.

Improving cash management by moving towards a TSA has been part of the reform agenda in Iraq since at least 2005. In that year, a joint World Bank/IMF mission recommended, as a medium-term reform (that is, by the end of 2006) that progress towards TSA should be made, subject to

<sup>21</sup> Treasury reforms are often used to refer to a range of PFM reforms relating to budget execution. These can include cash management, expenditure control and accounting reforms (often in an improved IT environment). In this section, the focus is on cash management reforms.

improvements in the payments and banking systems.<sup>22</sup> Progress has been limited and, in 2008, the IMF reported that the GoI did not yet operate a TSA and continued to hold large idle balances outside the main treasury account.

In Jordan, while many of the bank accounts were initially consolidated at the central bank, a number of accounts were not consolidated and outside the capital Amman, positive cash balances continued to be held at commercial banks. After some delay, it appears that agreement has now been reached to consolidate most of these balances—although in spite of this, a recent IMF/World Bank report noted that government deposits with commercial banks had recently increased. Lebanon also consolidated some balances at the central bank, but a number of important accounts were kept separate and the balances in these accounts were not available to meet cash needs. These limitations were not in general technical but more to do with whether the Ministry of Finance had the authority to consolidate the balances.

As discussed earlier, a similar issue arose in Egypt. The Ministry of Finance attempted to close a large number of accounts at commercial banks in order to consolidate the government's cash balances. However, facing vested interest from the “owner” of the account, the balances were kept separate within the central bank and eventually many returned to commercial bank accounts. The IMF has recently reported a fresh initiative by the Ministry of Finance on this reform.

In Yemen, it was proposed to establish a treasury in the Ministry of Finance to assume many of the budget execution functions at present carried out by the central bank. The reform has not progressed, in part because it was dependent on the implementation of the new information system (AFMIS), which has taken far longer than initially anticipated to make fully operational. More generally, there was limited enthusiasm from the Ministry of Finance for the reform and considerable unease from the central bank, which at present has 80 percent of its staff involved in supporting the budget execution function.

The use of cash plans for active cash management is at an early stage for countries in the region. Good progress has been made with cash planning in Jordan, but this remains a “research exercise” and cash management is still mainly through cash rationing. In Lebanon, cash rationing is still being used on a daily basis by the Ministry of Finance to decide which bills to clear. A start has been made to prepare a cash plan to guide budget execution, but there has been reluctance to involve line ministries in the preparation of the plan, which limits its status and has raised questions about whether the Ministry of Finance is truly interested in making this reform.

Cash constraints are also a significant problem in the West Bank and Gaza. However, there is an interest in moving to a more systematic arrangement and a cash plan was developed for 2009 with input from line ministries. The reform is in its early stages, and the cash plan is not yet being used to assist cash management.

It is worth mentioning that in countries with cash rationing in effect, the Ministry of Finance has considerable influence. It is therefore not uncommon to find the MOF less than enthusiastic about moving to a more systematic cash management system.

With treasury reforms there are a number of technical challenges, and a lot to learn from the experiences of other countries. For this reason, it is valuable to have technical assistance to support the reform. However, a greater need is to have solid commitment from staff within the Ministry of

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<sup>22</sup> In fact, the Financial Management Law (CPA Order 93 of 2004) requires that all receipts shall be credited to a Treasury Consolidated Account and paid into the Treasury Single Account, and all payments shall be debited to the Treasury Consolidated Account and withdrawn from the Treasury Single Account.

Finance for the reform. While other PFM reforms can be managed by a small team within the Ministry of Finance, these reforms affect many administrative employees throughout the public sector. Unless there is strong leadership from senior staff at the Ministry of Finance, the changes are difficult to implement successfully.

**Assessment.** While some progress has been made on treasury reforms in the region, this remains work in progress. Although a TSA has been established in many countries, the coverage is often not complete because the Ministry of Finance has not had the authority to consolidate some balances. A number of countries have set up units to prepare and maintain a cash plan, which can assist in aligning the borrowing and investment activity with the government's cash needs. However, too often the cash plans are not being actively used in cash management. Few countries have taken steps to improve debt management systems as part of treasury reforms.

### **Reforms in Tax and Customs Administration**

**Why is the Reform Important?** The collection of tax and customs revenues involves a number of challenges. Although the government collects tax by exerting its coercive power, this will meet strong resistance from taxpayers if the system is not perceived to be fair and efficient.<sup>23</sup> By improving the administration of the tax system, government can increase the revenues it collects consistent with the applicable laws, while enhancing the fairness of the system and reducing the compliance costs for taxpayers. The latter is important, as complying with the tax system can be a high cost of doing business.

**What is Happening in the Region?** In general, the MENA countries have made much better progress with tax administration reform than they have with expenditure reforms. Historically, countries in the MENA region have had a low tax to GDP ratio and inefficient tax systems that gave considerable discretion to the tax inspectors. Many countries are now interested in increasing the taxes collected—pressed to do so in some cases by the prospect of declining oil revenues. In light of this objective, a number of Ministers of Finance have taken an active interest in reforms to improve tax policy and administration. An additional motivation has been to improve the business environment.

There are some impressive achievements in tax administration reform from the region. Egypt has made considerable progress from a low starting point, and a 2008 IMF report noted a variety of important accomplishments. They include: (1) the successful implementation of self-assessment for income tax; (2) the creation of the Egyptian Tax Authority, as a vehicle for tax administration modernization; and (3) the establishment of a large taxpayer center and a pilot medium-size taxpayer center in Cairo. These reforms are at an early stage but the progress to date is impressive.

Jordan amalgamated the income and sales tax units into a new tax authority, and more recently it has made a number of changes so that the tax system provides an attractive and stimulating environment for local and international investors. In this regard, they conducted a comprehensive review of tax regimes to simplify and reduce their number to a minimum and consolidated the legislation. Morocco is considered to have a good tax system with a clear legal basis. A single taxpayer identification number is under development, and performance criteria for tax audits have been adopted. The introduction of large and medium taxpayer offices as “one stop shops” for taxpayers has also been adopted in Lebanon and Algeria, while Yemen has also introduced a system of self assessment for large companies.

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<sup>23</sup> This analysis focuses on the administration of general government taxes and duties related to income, trade and consumption etc. Where countries rely on revenues from petroleum or other natural resources, a different set of challenges apply.

It is interesting that more progress seems to be made on revenue administration issues than on expenditure administration. There are a number of possible explanations. One interesting observation is that it has been possible in some countries to provide real incentives to staff of the tax authority as part of the reforms. In particular:

- While in the past, tax administration was often just another department in the Ministry of Finance, many of the reforms have set up a separate tax authority or at least introduced separate administrative arrangements for the tax department. In Lebanon, this approach has allowed otherwise restrictive civil service wage rates to be bypassed. Being a tax official is a sought after job within the administration. Syria is also putting emphasis on this approach as part of its tax reforms.
- A number of countries in the region have also established bonus arrangements to provide tax collectors with an additional incentive. Tunisia attributed part of a recent increase in its tax collections to changes to the bonus structure.

Providing incentives for staff has been more difficult for expenditure reforms because of the wider implications for government administration. These incentives have had a positive effect in helping establish a new culture for tax administration. On the other hand, such arrangements have led some of the better staff to move from expenditure roles within government, exacerbating existing capacity problems in these areas. For this reason, caution should be exercised in deciding whether to adopt the approach.

**Assessment.** Tax administration reforms have in general been more successful than expenditure reforms in the MENA region. In part, this is because Ministers of Finance have taken an active interest in the reforms. However, tax administration is also a distinct function within government and it has been possible to support reforms by introducing separate administrative arrangements to provide stronger incentives for staff. One unhelpful consequence of this tactic has been that some of the better staff have moved to tax administration from expenditure roles within government, exacerbating existing capacity problems in these areas. For this reason, caution should be exercised in deciding whether to introduce incentives for tax administration in isolation.

## **Procurement Reform**

**Why is the Reform Important?** The way in which the purchase of goods and services is controlled through the procurement process can help the government to minimize collusion, kick-backs and other corrupt practices. Improvements to procurement procedures can therefore lower the cost of government expenditures.

**What is Happening in the Region?** As can be seen in the PEFA scores, many MENA countries have weak procurement systems. Yemen provides a good example of the type of problems that exist. The external audit body has commented that the procurement system is rife with fake competition, abuse of contract variations with subsequent project overruns, non transparent tender evaluations, an all too frequent resort to direct procurement methods, and the use of “slicing” to bypass procurement and authorization thresholds.

Procurement reforms are being discussed in a number of countries, usually on the back of a new procurement law. This is the approach being followed in Yemen and West Bank and Gaza. A new law has also been drafted in Lebanon, but is awaiting approval by the Council of Ministers before it can be submitted to parliament. In all cases the new laws include:

- Establishing an independent public procurement agency under the new procurement law;

- Preparing standard bidding documents based on the new law; and
- Preparing a user's manual and guidelines.

Procurement reforms have taken time to implement. Yemen has been working on the reform for over five years and has been actively supported first by the World Bank, and more recently with training by U.S. AID. Syria developed a new law in 2005, but this contained a number of weaknesses and the World Bank is now supporting work to revise the law. The delays stem from a variety of factors, but an important element is the strong opposition to reform from individuals and institutions benefiting from the existing system. In many cases, this is due to significant elements of corruption in the government procurement system.

**Assessment.** The quality of procurement systems in the region is weak. Reforms have been attempted in a range of countries, but the timescales for these reforms have been extended and the outcomes have been disappointing. The reforms often touch on areas of significant corruption and therefore can pose a threat to particular interests which have strong incentive to delay or divert the process. The failure to make progress in large part reflects an unwillingness to confront these special interests.

#### 4. Internal Control and Audit

**Table 7: Relevant PEFA Scores for Scope of Budget**

	Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Composition of expenditure out-turn compared to original approved budget	NA	NA	2.00	1.00	NA	2.00	1.00	NA	2.00	2.00	<u>1.67</u>
Stock and monitoring of expenditure payment arrears	NA	NA	1.00	1.00	NA	2.33	NA	NA	1.33	-	<u>1.42</u>
Effectiveness of payroll controls	NA	NA	1.33	3.00	NA	3.33	1.33	NA	2.33	1.33	<u>2.11</u>
Effectiveness of internal controls for non-salary expenditure	NA	NA	1.33	3.00	NA	2.33	3.33	NA	1.33	1.33	<u>2.11</u>
Effectiveness of internal audit	NA	NA	1.33	2.00	NA	2.33	2.33	NA	2.00	1.33	<u>1.89</u>

#### Developing Expenditure Controls

**Why is the Reform Important?** It is an obvious point, but effective expenditure controls are important to ensure that expenditures remain within the budget allocations and support aggregate fiscal control; as well as that the budget's role in allocating resources to sectoral expenditures occurs in a timely manner at the lowest cost, and that any changes in circumstances during the year can be accommodated. In addition to general expenditure controls, there are specific requirements to manage effectively the payroll procurement process. Because of the link to the transaction cycle, the controls are an important element in addressing corruption associated with government expenditure.

**What is Happening in the Region?** The countries in the region tend to have extensive and time-consuming control systems, but these systems are often not effective. As can be seen in the PEFA scores, controls on payrolls and non-salary expenditures, as well as the management of arrears, are all

areas of weakness. The composition of the outturn also differs greatly from the approved budget in all countries.

In order to improve the quality of expenditure control, reform proposals are being made to:

- Streamline the control processes and clarify accountability;
- Apply controls at the point of commitment; and
- Improve the quality of controls on procurement and payroll.

It is common practice in the region to have multiple signatures associated with the clearance of each transaction. Where there are numerous signatories to a given expenditure, it is often not clear who is ultimately responsible and hence accountable for misuse. This can be problematic within one institution, but in countries like Lebanon, Syria, Jordan and Morocco the problem is exacerbated by having a range of different agencies involved in the ex-ante control process. In addition to weakening accountability, the procedures can become a major impediment to the government's ability to conduct business. In a number of countries (notably Iraq), the delays caused by heavy control procedures are said to explain delays in capital projects. Moreover, in Lebanon, the problem is used as a rationale for managing capital projects outside the government system.

Despite the problems being faced in the region, there have been relatively few attempts to date to streamline the control procedures. Morocco has embarked on a reform of the organization of its ex-ante control system. In 2006, the separate bodies that control payment orders and commitments were merged. In 2007, cumbersome virement rules were revised to provide greater flexibility to ministries. This has already resulted in improvement in the timeliness of budget execution. It is also planned that "ministerial treasuries" will perform a simplified modernized ex-ante control, which will be based on risk assessments and the size of the transactions. However, few of these treasuries have been established. There have been proposals to streamline the ex-ante controls system in Lebanon, but the latest reform action plan makes only a marginal mention of this initiative. The lack of focus on this issue is in part a reflection that the need for reform is not accepted. However, it is also recognition that the reform would be challenging, given it would involve changing the roles of some institutions.<sup>24</sup>

Cash rationing and the build-up of arrears is a major problem for many of the countries in the region. Lebanon, West Bank and Gaza, Yemen and to a lesser extent Egypt and Jordan have identified problems with expenditure arrears.<sup>25</sup> While many of the problems stem from the poor quality of budget preparation, there are opportunities to better manage the problem if expenditure controls are exercised at the point of expenditure commitment. At present, many countries implement the expenditure controls at the point of payment, by which time the liability has been created and the only question is when payment will be made. In Lebanon, there is an additional complication posed by the violation of the annuality principle in the regular budget.

To address the arrears problem, Morocco has introduced a system of commitment controls, although the draft PEFA assessment suggests that the system is not yet working effectively. West Bank and Gaza is in the early stages of introducing commitment controls in conjunction with the new accounting system. The recent IMF/World Bank mission to Jordan has recommended that

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<sup>24</sup> This can be particularly problematic where there are known to be side payments for staff associated with the expenditure control process.

<sup>25</sup> In Algeria, funds release is not timely and arrears do develop, but the petroleum revenues have been available to finance any arrears that emerge.



commitment controls also be a feature of the financial management system being developed. On the other hand, while a commitment control feature is part of the software specifications in the Yemen financial management information system, this functionality has not yet been designed or activated. Although it is possible to implement commitment controls in the absence of computerization, all the reforms to date are progressing as a component of an IT project.

The PEFA scores suggest that, in relative terms, the management of payrolls is in better shape than other expenditure controls. Both Jordan and Morocco have solid scores in managing the payroll. Progress on a more limited basis has been made in Lebanon. Overall payroll controls in Egypt are fairly effective as payroll audits are carried out, though they are not comprehensive. Lebanon's computerization of payroll and pension management in the 1990s was a major achievement. In 2006, the MOF introduced direct computerized bank payment to public sector employees, which has also allowed a reduction in the number of ghost workers.

Payroll reform is a particular priority in West Bank and Gaza and Yemen—although the problem in each country is different. In Yemen, the problem is one of ghost workers and double dippers, while in West Bank and Gaza, it is the lack of budget discipline in the recruitment process. In West Bank and Gaza, payroll controls have improved substantially in 2007 and 2008. They provide more assurance on the integrity of an item that in the 2009 budget constitutes more than 60 percent of recurrent expenditure. In particular, the payroll system is now connected with the accounting system of the MOF, and a separate financial controllers department reviews the payroll on a monthly basis.

In Yemen, a civil service project started in 1998 which included the establishment of a clean personnel database by 2001. The project was restarted in 2005 with a re-visitation of the clean up exercise (principally of double dippers and ghosts) through a new database that includes biometric control data. However, the clean up exercise currently covers around 70 percent of all Government employees and does not include a significant portion of the ministries of Defense and Internal Affairs. There is a consensus among knowledgeable observers that the former is likely to be particularly problematic in terms of ghost workers and double-dippers. Furthermore, the biometric system is not as yet closely linked to the payroll, which does not allow it to function as intended.

**Assessment.** The quality of expenditure controls in all forms is poor for countries in the region. Despite the problems being faced, there have been few attempts to date to streamline and strengthen the expenditure control procedures. Where the reforms involve institutional changes, they have proven particularly challenging. Progress has been made by some countries in payroll management, but this is uneven. The overall impression is that where there is a failure to make progress, it is mainly due to a lack of genuine interest in the reforms.

### **Strengthening Internal Audit**

**Why is the Reform Important?** Internal audit aims at providing the executive with assurance of the quality of the financial management systems—in particular the implementation of financial controls and the management of risks.<sup>26</sup> Depending on the system of control in place, this could be assurance to the Ministry of Finance or to the senior management of the line ministry.

**What is Happening in the Region?** The PEFA assessments indicate that the internal audit function is poorly developed in most countries in the region, with Morocco being one of the few countries to have a relatively positive PEFA assessment. Many of the weaknesses are similar to those found with the

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<sup>26</sup> While internal audit can also provide comment on the value for money of expenditures, this is not generally a core function.

external audit bodies and relate to problems of the scope of work carried out, concerns about conflict of interest, and institutional clarity.

In many countries, the internal audit function has a strong transaction focus, and aims to identify cases of mismanagement or a failure to follow procedures rather than looking at the adequacy of the overall systems. This is often a feature where the function has emerged from a Soviet style inspection service. The internal audit in Syria is an example of this, and the relatively strong PEFA assessment for Syria reflects the extensive control which is applied through this system rather than the adequacy of the scope of its activities. In countries such as Lebanon and Jordan, internal audit is part of the ex- ante control process. This compromises the auditor's independence, as any assessment is a comment on the auditor's own work. Institutional clarity is a particular problem in Tunisia where there are several internal audit bodies, with one reporting to the Prime Minister and another to the Minister of Finance.<sup>27</sup> The institutions have similar roles although the latter extends further into value for money issues.

There have been relatively few efforts to reform the internal audit functions in the region—in part reflecting the view that internal audit is an advanced reform. It is certainly more recognized where countries adopt a performance budgeting approach and there is a greater focus on the accountability of line ministries. This creates a demand from managers for assurance on the systems they are managing. However, it is possible that resistance to a change in role is also coming from auditors where involvement in the transaction control process is a source of corruption or influence.

One interesting example of internal audit reform is in West Bank and Gaza. Since 2004 the Ministry of Finance has been building an internal audit functions with support from the European Union. The function has been providing the Minister of Finance with assurance of the financial management systems both within the Ministry and throughout the core public sector. The reform has closely followed international norms for internal audit activity. In view of the Ministry of Finance's objective of devolving responsibility for financial management to the line ministries, the plan is for the internal audit function to also be transferred.

**Assessment.** Most countries in the region have weak internal audit functions reflecting problems in both the scope of audit activity, and conflicts of interest where the auditor is also part of the control function. Internal audit has in general not been given a high priority for reform in part because it is considered an advanced PFM reform. But resistance to change can also come from existing auditors who are reluctant to be removed from the transaction control process when this is a source of corruption.

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<sup>27</sup> A third body has a particular focus on public property issues.

## 5. Accounting and Reporting

**Table 8: Relevant PEFA Scores for Accounting and Reporting**

	Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Timeliness and regularity of accounts reconciliation	NA	NA	2.33	3.33	NA	4.00	3.00	NA	2.00	3.00	2.94
Oversight of aggregate fiscal risk from other public sector entities	NA	NA	1.00	3.33	NA	3.00	2.00	NA	1.33	4.00	2.44
Extent of unreported government operations	NA	NA	1.33	3.00	NA	2.33	2.00	NA	2.33	3.33	2.39
Availability of information on resources received by service delivery units	NA	NA	1.00	1.00	NA	3.00	2.00	NA	1.00	3.00	1.83

### Accounting Policy Reforms

**Why is the Reform Important?** Accounting policy reforms can improve the reliability with which expenditures and cash balances are controlled, monitored and reported.<sup>28</sup> Where accounting policies are aligned with international standards, there can be increased confidence in the integrity of the financial information presented.

**What is Happening in the Region?** Accounting systems in general are not well developed in the region, and there is a mixed record of reform. In Syria, the accounting system still operates on a single entry basis. This makes the system more prone to error, as there is not a ready reconciliation between the flows and stocks. A recent European Union project endeavored to introduce double entry accounting through a new IFMIS system, but this has not been successful.

There are extensive delays in preparing the final accounts in Morocco and Tunisia that reduce the quality of the accounting systems. In both countries, the final accounts are not completed until two years after the end of the financial period.

In Egypt, the accounting system is on a double-entry basis but has a mix of cash and accrual concepts that complicates interpretation of the accounts. The IMF recommended that a pure cash based system be adopted as part of a medium term transition to accrual accounting, but in spite of considerable TA the system has not been reformed. The IMF has recently commented that accrual accounts “of questionable utility” persist, as well as a variety of memorandum accounts. On a more positive note, PEFA scores indicate that account reconciliations are generally conducted on a timely basis. While this indicates adequate processes within the accounting departments, it does not provide assurance on the quality of the accounting framework.

Jordan appears to have made the most progress with accounting reforms. It is now about to adopt the International Public Sector Accounting Standard (IPSAS) as part of the reform project that includes the implementation of a GFMIS.

<sup>28</sup> In this section the focus is on accounting methodology and standards.

As with treasury reforms, there are a number of technical challenges with accounting reforms and there is much to learn from the experience of other countries. For this reason, it is valuable to have technical assistance to support the reform. However, given that the reform affects the work of a large number of civil servants, the main need is to have solid commitment from senior staff within the Ministry of Finance for the reform. This is particularly the case where the existing practices have been in place for an extended time and the accounting staff in the country have considerable human capital attached to knowing these practices.

**Assessment.** Experience with the reform of accounting systems has been mixed. While most countries operate double entry systems, there has been limited success in reforming accounting methodologies towards a consistent use of cash or accruals, let alone applying international accounting standards. A challenge with accounting reforms is that they affect the work of many employees throughout the public sector, and a strong commitment from the senior staff in the Ministry of Finance is essential if the reform is to be successful.

### **Introducing a Performance Focus to the Budget**

**Why is the Reform Important?** The traditional input based budget does not provide policy makers with information on what goods, services, or policies are being financed by government expenditure. In the absence of this information, attempting to ensure the efficiency and effectiveness of expenditure is a challenging task. The aim with a performance focused budget is to aggregate inputs that are used to deliver a particular group of activities. Often the reform is associated with some relaxation of input controls and, in the more advanced applications, with the introduction of an accountability framework based on performance.

**What is Happening in the Region?** The idea of focusing on performance has been around for some time, but in the last twenty years many OECD countries have reformed their budgets to introduce a more explicit performance focus. Such reforms have been given different labels—with program, output, or results oriented budgeting being among the most common.

In view of the broader global trend towards improved effectiveness in public administration, there is considerable interest from countries in the region in introducing a performance focus to the budget. The earliest efforts were made by Jordan, which started its results oriented budgeting reform in 1998. In recent years, a number of other countries have started to work on pilots for program based budgets, including Morocco, Algeria, Tunisia, Lebanon, and Syria.

The Jordanian experience is particularly instructive. The first efforts were supported by the German aid agency GTZ and continued from 1998 to 2004. They were ultimately considered too ambitious and had little impact. Since then, an approach has been piloted in the Ministry of Education and is being extended to other ministries. Initially, there appeared to be little ownership of this initiative by the General Budget Directorate of the MOF, but this is no longer the case. A recent review by the IMF/World Bank noted that progress has been made. However, it also commented that the reform has not yet delivered the benefits that were expected. One reason identified is that the lack of some basic elements of the PFM system (e.g. commitment controls) has tended to negate the progress with this more advanced reform.

Morocco has also been working on performance budgeting reforms for a number of years. The World Bank provided assistance to the government to develop a performance budgeting approach, based on pilots in a number of ministries. However, while some performance budget documents were drafted, government support for this exercise was weak and the initiative has not been pursued after these initial drafts. More recently, the MTEF reform is being used to develop more performance focus. A

methodology was developed in 2006 and work on the MTEFs has continued, but to date the budget is an input based document.

Tunisia has four results based budgeting pilots underway with support of the World Bank, but it is taking a measured approach to the reform. The intention is to include the pilot ministry information as an annex to the 2011 budget. A similar path is being followed by Syria, although it expects to include some material on its two pilots in the 2010 budget. A European Union project financed training and study tours for staff in the Syrian Ministry of Finance over a number of years, but there was no reform to the budget as a result of this initiative. The latest developments are taking place in a low key fashion with the support of the IMF. In Algeria, a pilot program budgeting was carried out in FY07. It was not repeated in 2008 but is expected to resume in 2009. Full adoption of program budgeting and management is planned for the budget in 2012, if the new organic budget framework law is adapted by parliament in time.

In West Bank and Gaza, a pilot approach was rejected and all ministries were asked to develop programs to establish a link between the budget and the government's reform plan.<sup>29</sup> The program structure was used for presentation purposes in the 2009 budget, although it will be refined in future years. One of the motivations for this reform has been to demonstrate that budget support from donors is being used as planned.

The slow progress on introducing a performance based approach is in large part because it is necessary to have many of the basic elements of the PFM system in place before it can work effectively. Often these weaknesses are only fully recognized when work on a pilot begins. A number of prominent examples of the challenges facing reforms in this area are:

- In Syria, the work with pilot ministries revealed that—in addition to the standard dual budgeting problem—a large portion of sectoral expenditure (say in education or agriculture) is fragmented between the relevant sector ministry and the Ministry of Local Administration. Unless this institutional fragmentation can be addressed, it will hamper the efforts to make program budgeting effective.
- In West Bank and Gaza, it was recognized that the accounting systems need to be adapted to allow programs to be monitored during the execution of the budget. While chart of accounts changes are manageable, the accounting system will not be able to manage complex cost allocations. This will mean that some of the programs initially defined will need to be simplified to meet the capacity of the accounting system.

Another challenge is to avoid the reform becoming an information collation exercise, which loses sight of the objectives. When fully developed, a program structure can involve a range of sub-programs and activities. Combined with associated performance indicators, the information demands can be extensive. This might make sense in a well developed budget system where skilled staff are able to effectively use the information. However, in an environment where there are capacity constraints in both preparing and using the information, the data collation process can become an end in itself, undermining the reform. This was a criticism of initial work on results oriented budgeting in Jordan. Also, the budget documents in Morocco include hundreds of input or output indicators, but little attention is paid to them. The government intends to improve these performance indicators, including reducing their number.

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<sup>29</sup> Palestinian National Authority, *The Palestinian Reform and Development Plan (PRDP)*, 2008.

Finally, it is worth noting that Egypt, Yemen and Iraq have decided not to start work on a performance focused approach to budgeting at this point. In Iraq in particular, this reflects recognition that there are more fundamental reforms deserving priority.

**Assessment.** There is considerable interest from MENA countries in introducing a performance focused approach to budgeting. However, the successes are limited to date and the timeframe for the reform is proving to be extended. This reform is complicated and difficult—in part because it relies on having many other elements of the PFM system functioning at a reasonable standard. For this reason, even where the reform proceeds, every effort should be made to avoid conceptually sophisticated approaches and to ensure that the approach can be supported by the accounting systems.

## 6. External Accountability

**Table 9: Relevant PEFA Scores External Accountability**

	Algeria	Egypt	Iraq	Jordan	Lebanon	Morocco	Syria	Tunisia	West Bank & Gaza	Yemen	Average score
Scope, nature and follow-up of external audit	NA	NA	-	2.00	NA	1.33	2.33	NA	1.00	3.33	<u>2.00</u>
Legislative scrutiny of the annual budget law	NA	NA	1.00	4.00	NA	3.33	2.33	NA	2.33	2.33	<u>2.55</u>
Legislative scrutiny of external audit reports	NA	NA	1.00	2.00	NA	1.33	1.33	NA	1.00	1.33	<u>1.33</u>

### Strengthening External Audit

**Why is the Reform Important?** External audit provides parliament with assurance on the adherence to financial laws, the reliability of the financial statements, and value for money in government expenditure. As such, it provides an essential discipline on the financial management of the executive.

**What is Happening in the Region?** The PEFA assessments indicate that the external audit functions of countries in the region have a range of weaknesses. Egypt is an extreme example as the activities of the Central Audit Organization, which is Egypt's Supreme Audit Institution, are shrouded in secrecy. In Algeria, the last published annual report from the National Audit Court was in 1996-97, and its reports are not now publicly available despite an apparent requirement that they be published in full or in part in the Official Gazette.

With some countries, the weaknesses relate to institutional problems, with many external audit bodies reporting to the President or King instead of solely to the parliament.<sup>30</sup> In many countries, the audit function has a strong transaction focus, with the aim of identifying cases of mismanagement or a failure to follow procedures rather than looking at the adequacy of the overall systems. In countries such as Lebanon and Jordan, external audit is involved in ex-ante control, compromising the auditor's independence. In Tunisia, a good quality external audit is carried out by the Court of Accounts and the INTOSAI standards on autonomy, scope and quality are met. However the value of audit work is limited by the fact that it is only partially published, the public accounts may be some two years old by

<sup>30</sup> Whether joint reporting is in practice a problem depends on whether the arrangements compromise the willingness of the auditor to raise concerns or problems.

the time the settlement law is considered by parliament and by the lack of any formal parliamentary hearing on the report by the Court of Accounts on this act. A similar situation applies in Morocco.

In spite of the weaknesses in the external audit bodies, there appear to have been relatively few efforts to reform the external audit functions. Given the relatively limited role played by the parliament in most of the countries in the region, it is not surprising that there is limited demand by the parliament for support in holding the executive to account. This is reflected in the very low PEFA scores for legislative scrutiny of audit reports for all countries in the study.

Although there are proposals for future reform in Jordan and Lebanon, the three countries with the most experience with audit reforms to date are Iraq, West Bank Gaza and Yemen. They have had mixed experiences. In Iraq, the reform involved introducing a new inspector general function based on the U.S. model. A number of PFM experts believe that this reform has not been successful, as the new function is not well understood and is not integrated with the existing oversight institutions. The change has also exacerbated existing capacity problems.

In West Bank and Gaza, a new audit body was established in 2005. However, in light of the prevailing political instability during that period, the capacity building process restarted in 2007. It has received little technical assistance from donors to date, but a major capacity building project is about to start financed by the European Union. Alongside this project, the external audit is being guided by the Auditor General of Norway for the audit of the 2008 financial statements. This would be the first audit of financial statements since 2003. The audit is not complete, but the early indications are that working through a “live” audit will be a very productive capacity building exercise. The presence of the Norwegians has also provided the external audit with needed credibility in its discussions with the Ministry of Finance. The extensive effort made by the Ministry to document and support the 2008 accounts has also confirmed the vital role that an external review can play in ensuring discipline in the financial management function. Without the possibility of external review a range of sloppy—if not unethical—practices can easily develop.

In Yemen, the external audit body has received support from GTZ for a number of years. Since 2007, the body can be seen to be having a real influence, with active consideration of its report by the parliament. Before then little progress was apparent. Although the project has been active since 2005, the reform towards an institution meeting INTOSAI standards is still work in progress. For example, only now has a draft audit bill been completed and forwarded to the President to address (among other things) the independence of the external audit agency.

**Assessment.** Most countries in the region have weak external audit functions, in part reflecting the relatively minor role played by parliaments in many countries in the region. While the focus of external audit is on providing assurance to parliament, the presence of an effective audit body can also support reforms in budget execution by encouraging more discipline in the accounting practices. However, ultimately the success of efforts to build the capacity of the audit body will depend on whether the parliament is prepared to utilize the auditor’s report.

### **Chapter 3**

## **Implementing Reforms in Public Financial Management: An Emerging Set of Promising Practices in MENA?**

*One of the lessons of public finance reform is that people do not 'eat' reform,  
people cannot relate to reform. So what is important is to look for ways  
to make people actually feel the difference.*

-- Salam Fayyad --

At one level, it is an admittedly artificial exercise to separate the content of reforms from their implementation, for the two are inextricably linked. The nature of the reforms being implemented will inevitably influence the pace and timing of change, the size of the effort, and the actors engaged in it. Yet the science (or art) of management has also long-realized that the way in which reforms are implemented can have an important impact upon their realization. This chapter seeks to review the lessons that have been learned from a decade or more of trying to implement PFM reform in MENA to understand if there are obvious pitfalls to be avoided or approaches that will elevate the prospects for success. It also seeks to better understand the various political and bureaucratic dynamics surrounding these changes.

### **How Important is Implementation to the Success of MENA's PFM Reforms?**

Before proceeding, it is important to better understand the role of implementation in contributing to successful PFM reforms. As Table 10 indicates, not all reforms are created equal. This table breaks the MENA experience with PFM reform down along three dimensions. The first category are reforms that have typically been "more successful," in that a number of MENA countries have been able to implement them effectively and achieve concrete, independently verifiable improvements. The third category, "challenging PFM reforms," is comprised of reforms that have shown themselves historically to be more difficult and problematic. It does not mean that they have been impossible to implement, and some MENA countries may have been able to put in place certain elements of these reforms. But this is not common. The "mixed" category represents an area where generalizations across the region are difficult to make and the results are often more specific and unique to a given country.



**Table 10: Breakdown of Successful and Challenging PFM Reforms in MENA**

Successful PFM Reforms	Mixed	Challenging PFM Reforms
<ul style="list-style-type: none"><li>• Improving budget classification</li><li>• Improving budget transparency</li><li>• Reforms in tax and customs</li></ul>	<ul style="list-style-type: none"><li>• Enhance macro-fiscal capacity</li><li>• Budget integration</li><li>• Streamlining ex-ante control processes</li><li>• Commitment control</li><li>• Payroll management</li><li>• Treasury operations</li><li>• Reform of accounting systems</li><li>• Internal and external audit</li></ul>	<ul style="list-style-type: none"><li>• Medium term sector strategies</li><li>• Improving budget scope and coverage</li><li>• Introducing performance into the budget</li><li>• Procurement reforms</li><li>• Large information technology projects</li></ul>

Two types of PFM reforms have been particularly successful in MENA: efforts to improve budget transparency and classification, and revenue related reforms, particularly those involving the reform of tax and customs. Ironically, these represent two very different types of reforms. The first are relatively straightforward and technocratic in nature. An existing body of accepted practice exists to reform economic classification, in the form of the IMF's GFSM 2001, and there are incentives to align accounts along standard international practice to facilitate the production of comparable fiscal and economic data. While there may be some resistance to such reforms stemming from basic bureaucratic inertia, no fundamental interests are challenged or mandates threatened. Once implementation is complete, the reform becomes part of the fabric of the system and endures. It is therefore not surprising that many MENA governments have been able to take this step.

This is not true for revenue consolidation or reforms in tax and customs, where the stakes are much higher. Revenue agencies are often among the entities in government where problems of corruption are most pronounced, since their function places them in a position to extract rents from both firms and the general public in exchange for a variety of favors. Efforts to restructure and reorganize such functions often encounter fierce resistance from both those on the inside (who benefit from informal payments) and some on the outside (who have learned to work around the current system and use it to their advantage). Such reforms are not for the timid or hesitant.

Yet if the challenges are great, the gains are often significant as well. For governments facing significant fiscal deficits, it is often more politically palatable to raise revenues—difficult as that may be—than to engage in painful cuts in expenditure. In Lebanon, for example, reforms in tax policy and administration were initiated since the 1990s because it was the largest single source of revenue for the government. A combination of tax and customs reforms, including moving to a VAT, was able to increase government revenue by \$1.88 billion between 1997 and 2003, or from 11 to 16 percent of GDP. In Egypt, reforms in tax policy and administration implemented in 2005 and beyond brought over 1 million new taxpayers into the system and increased income tax revenue from 7 to 9 percent of GDP. Beyond the promise of new revenue, such reforms are often initiated to remove obstacles to increased private investment. For all of these reasons, such reforms are able to garner the requisite high-level political support to see them through in spite of considerable opposition.

Unfortunately, on the other side of the spectrum are a host of reforms that are neither particularly easy to implement nor which bring the promise of substantial fiscal gains, at least in the short-term. Some, such as improving the scope and comprehensiveness of the budget, are not technically difficult to

implement. Progress has been made in a number of settings, such as Jordan and the West Bank & Gaza. However, the political hurdles are considerable, as many powerful entrenched interests often prefer to remain off-budget. Unless significant political capital is invested in overcoming such resistance, these reforms are unlikely to move forward.

Other reforms, such as the development of MTEFs, introducing large IT projects and integrating more performance information into the budget, are often both technically demanding and run up against powerful vested interests. In many cases, their successful implementation may depend upon underlying systems, procedures and practices being in place that may not exist. It is therefore not surprising that their implementation is frequently delayed or halted. As one assessment of PFM reforms in Yemen noted with refreshing candor, “for the Finance Minister or the National Public Financial Management [Reform] Coordinator, only those set of reforms which can bring instant recognition and resources to the government are of priority...reforms which are painstaking and long-term without immediate benefits take a back seat.”<sup>31</sup>

Under such circumstances, it may be tempting to conclude that—in the final calculation—it is the nature of the reforms themselves as much as the way they are implemented that is responsible for their ultimate success or failure. In the words of Egypt’s Minister of Finance, Youssef Boutros Ghali, “it is easy to change laws—it is hard to change the attitudes of those who implement them.”<sup>32</sup> Reforms that are largely technical in nature will be easier to implement; those that are technically demanding and rely upon certain preconditions to be in place will be more difficult. Reforms that do not alienate powerful constituencies will be easier to implement; those that cross fundamental political and bureaucratic interests will be more difficult. Reforms that have a high payoff in terms of tangible, concrete returns in the near term will be easier to implement; those whose benefits are more distant or ephemeral will not be.

While there is certainly truth in this contention, reality is more complex and nuanced. Considerations of political will, leadership talent, the broader authorizing environment, and internal capacity (to name but a few) can shape and modify reform agendas in ways that confound simple predictions. Few would have anticipated that Salam Fayyad, for example, would have enjoyed the success that he has in reforming West Bank & Gaza’s PFM practices. His initial focus on consolidating banking arrangements, strengthening expenditure controls and budget reforms—while desperately needed—would not have been areas that held great promise for far-reaching improvements on an *a priori* basis. In a similar fashion, one would have expected that some of the higher income countries with more effective administrations would have been able to make greater progress towards strengthening internal and external audit than has been the case so far. There are a few cases where poorly designed interventions have been made to work through sheer dogged determination, albeit often with compromises in timing, cost and functionality. There are far more in which reforms that were generally sound and appropriate floundered through poor implementation.

Box 2 summarizes some of the key lessons from MENA reforms that have emerged from this analysis, including both the individual case studies and the more detailed assessments of reform experience in the WBG and Egypt. Although efforts have been made to make them as rigorous as possible, they are admittedly more qualitative than quantitative. As noted above, these principles are not intended to provide a comprehensive review of all of the lessons from this experience—only to highlight some of the more interesting and relevant ones for future reformers and those who support them. Each will be discussed in greater detail below.

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<sup>31</sup> Arya, *Chapter 10: Yemen*, in Vol. 2, p. 139.

<sup>32</sup> Author interview, *H.E. Youssef Boutros Ghali*, 2009.

## Box 2: Ten Principles of Implementation for PFM Reforms in MENA

1. Know the value—and limitations—of political economy analysis
2. PFM reform as means and not ends
3. Context matters, so swim with the current
4. The wisdom of “muddling through”—grand strategy versus incremental change
5. Establish basic systems before contemplating more advanced reforms
6. Whenever possible, keep reforms quick, simple and mutually reinforcing
7. Be wary of large financial management information systems
8. Internal challenges: leadership, coordination, skills and incentives
9. External stakeholders—useful, but don’t count on them
10. On the value of synergy, or all good things go together

### Lesson 1: Know the Value—and Limitations—of Political Economy Analysis

In many areas of governance and public administration reform including PFM, there has been a rush to embrace the discipline of political economy analysis (PEA) over the last decade. Definitions as to exactly what PEA is may vary as the field is still evolving, but one in-common usage notes that it is concerned with the interaction of political and economic processes in a society: the distribution of power and wealth between different groups and individuals, and the processes that create, sustain and transform these relationships over time.<sup>33</sup> There are a variety of competing approaches to conducting PEA, including the World Bank’s Institutional Governance Reports (IGRs) and Expected Utility Stakeholder Models; DFID’s Drivers of Change analysis; as well as other more general types of stakeholder assessment and analysis. At their core, all of these approaches share a common belief that—in the words of the Bank’s 2008 IEG study—the performance of both PFM and other reforms would be better if it were informed by deeper institutional and governance analysis.<sup>34</sup>

At one level, the logic of this position is unassailable. The history of PFM reform is littered with examples where far-reaching reforms were introduced without a careful assessment of the underlying political and institutional environment in which they were being implemented, often in the hope that reforms which had shown themselves to be effective in one country or administrative context could be easily grafted on to another. Few experienced practitioners would argue with the cautionary notes struck by the PEA literature, or the premise that greater upstream analysis of what is politically or administratively feasible will pay downstream dividends when it comes to implementation.

Yet beyond these basic warnings, the PEA literature has relatively little to contribute when it seeks to address the most important questions in any reform initiative: what should be done, when it needs to happen, who should do it and how. The reason is found at the core of the more sophisticated assessments of this discipline. Each reform experience is unique and endogenous to a particular time and country, as well as to an individual set of political, bureaucratic, institutional and personal dynamics. PEA analysis may do an effective job of highlighting constraints or identifying potential supporters. It can help to inform decisions about what is to be done. But it is not going to substitute for solid strategic decision-making, and even less for astute tactical maneuvering in implementation. These will remain highly contextual and contingent upon a host of factors that are fluid, dynamic and idiosyncratic.

<sup>33</sup> Collinson, cited in the *OECD DAC discussion of political economy analysis*. See [http://www.oecd.org/document/8/0,2340,en\\_2649\\_34565\\_37957768\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/8/0,2340,en_2649_34565_37957768_1_1_1_1,00.html)

<sup>34</sup> See IEG, *Public Sector Reform: What Works and Why*, p. 51.

When PEA strays from its descriptive role and seeks to develop more general prescriptive principles for guiding actual reform efforts, the resulting precepts are often rather tepid and generic. Reformers are urged to look for windows of opportunity, pluck “low hanging fruit,” worry about incentives, forge coalitions with like-minded groups in government and civil society, know that leadership matters, and to co-opt opponents through negotiation or by disseminating information about the nature and content of the reforms.

Such admonitions are not necessarily foolish or wrong. However, measured against a careful review of how the more far-reaching PFM reforms in MENA were actually accomplished, they often appear detached, debatable and even a bit Pollyannaish. Serious PFM reform involves moving aggressively to overturn a dysfunctional status quo and establish a new institutional order. Those who benefit from the existing system will resist these efforts, at times tenaciously. (At one point during Salam Fayyad’s tenure at the Ministry of Finance, rival Palestinian security forces actually confronted each other over efforts to reform the General Personnel Council.) More often than not, traditional interests win, or at least manage to fight the reforms to a draw. Examples of far-reaching PFM reforms in the region are relatively few and far-between.

When such reforms do emerge, the trajectory they follow is typically not what your standard PEA would predict. In light of the high degree of political fragmentation within the PA and the extensive authority centralized under President Arafat, few would have suggested that Salam Fayyad begin his reform agenda with consolidating banking arrangements. The fiscal logic behind such a move was obvious, but it was by no means clear that he would have the mandate and political authority to pull it off. In a similar fashion, Boutros-Ghali noted that political and administrative calculations didn’t change his perception of what needed to be done, but they did influence the timing. Beginning his reform agenda with the always thorny issue of tax and customs reform was a risky move politically, yet such institutions had to be reformed to achieve Egypt’s broader national goals. As one of his key advisors noted, “on the reform of tax policy, he may have been constantly probing and adjusting his priorities in light of what was politically feasible. But on the administrative side, we knew what needed to be done and we just had to go do it.”<sup>35</sup>

Furthermore, the tactics used by all sides—including the reformers—can be ruthless. Some reforms may be the product of extensive coalitions and careful consultations. Others are rammed through quickly with little debate or discussion. (Salam Fayyad argued that a key component of his reform strategy was to move quickly and keep his opposition off balance.) Adversaries are more often than not isolated, cut-out of the action and eventually forced out of government rather than being won over by gentle persuasion. Claims are made about the benefits of reform and accomplishments achieved that, in retrospect, are inflated or exaggerated. Feints and diversions are employed to befuddle adversaries. (Youssef Boutros Ghali once argued that reformers should, “open five fronts, knowing that you will only succeed on two.”) Difficult tradeoffs are made, in which reformers settle for half a loaf instead of none or focus their limited political capital on a few important gains with the knowledge that some very dysfunctional policies and practices will continue elsewhere for the indefinite future.

The objective is not to question the ethics or efficacy of these reforms, about which reasonable and well-intentioned observers could differ. It is simply to make the point that the implementation of far-reaching PFM reforms in MENA is a complex and difficult task whose success is highly dependent upon a variety of contextual factors, not the least of which is the ability of those championing these reforms to manage the political and bureaucratic process effectively. PEA plays a role in underscoring

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<sup>35</sup> Author interview, *H.E. Youssef Boutros Ghali, Ashraf Gamal El-Din, Gamil Ezzat and Ayhmed Monkez Shaker, Egyptian Tax Authority*, 2009.

the fundamentally political nature of these changes, as well as in identifying the likely sources of support and resistance, and in that it provides a useful service. But more is probably to be gained by investing in greater tactical flexibility, in terms of field-based governance advisors and public sector specialists who can provide real-time advice and assistance in high risk, high engagement settings, than in trying to assume that more rigorous political analysis up-front will answer these questions.

## **Lesson 2: PFM Reform as Means and Not Ends**

PFM reforms arise from a number of different motives. They can be implemented in response to a particular fiscal problem or crisis, typically a growing deficit and the need to raise revenues, curb expenditures or use existing resources more efficiently. They can be implemented as part of a political agenda to ensure better service delivery. They can be pursued at the request of donors or in the hope of improved regional integration. They can also be championed for idiosyncratic reasons, such as ministers or officials seeking to make a career for themselves as reformers. None of these motives are mutually exclusive, and often two or more could come into play.

In the MENA region, the most far-reaching reforms in West Bank & Gaza and Egypt were implemented in response to an acute fiscal crisis—compounded by a severe economic contraction in the case of the West Bank and Gaza. By the spring of 2002, the Government of Israel was withholding clearance revenues, which represented nearly two-thirds of PA revenues. Arab donors had cut their contributions by around half. The international community had expressed serious reservations about President Arafat’s stewardship over PA finances and was threatening to withhold desperately needed funds for budget support. In 2004, Egypt confronted a budget deficit of 40 billion pounds (approximately \$7.2 billion), or 8.3 percent of GDP. Around 8.3 million Egyptians were in the informal sector, or 37 percent of the workforce, which provided significant untapped potential for broadening the tax base. Another powerful factor in Egypt was the imperative of enhancing the country’s ability to attract much-needed private investment.

Under these circumstances, PFM reforms were effective in large part because they promised to be a solution—or at least part of the solution—to a broader set of fiscal and growth-related problems. As such, senior political leadership was deeply invested in the reforms and was able to push for them strongly, even though the way forward would be difficult and they were likely to encounter entrenched resistance.

Other reforms that were targeted at enhancing performance or modernizing antiquated procedures to make them more in line with emerging best practice have typically not fared as well. Their implementation has been slower at least in part because a general lack of urgency has made it easier to defer difficult choices and avoid tackling entrenched interests. While senior officials often like the notion of pursuing “cutting edge” reforms, such motivations are not enough by themselves to galvanize a serious reform effort. Reforms that rely upon them tend to dissipate once their champion leaves office.

## **Lesson 3: Context Matters, so Swim with the Current**

A corollary of the point that reforms are a means and not an end in themselves is the point that context matters. As noted above, two of the most far-reaching PFM reforms took place against a backdrop of acute financial crisis. Under these circumstances, reformers were able to gain additional support through associating their efforts with desired national ends. They were also allowed considerably more latitude in devising solutions than they would have otherwise enjoyed.

However, like the Almighty, context can both giveth and taketh away. Major reform agendas can stretch over years, whereas the political and economic conditions that give rise to them are typically

subject to much shorter time horizons. Pressures towards reform that are felt acutely during times of crisis can dissipate if oil prices rise or other activities take place that distract reformers. The experience of Jordan's *National Agenda* offers a case in point. The government articulated a fairly far-reaching governance reform agenda, including a variety of PFM reforms. However, the hotel bombings in Amman in November 2005 led to a shift in the political center of gravity in which security concerns came to predominate. Although the reform agenda remained, efforts to implement it were slowed down to avoid alienating important traditional constituencies during a period of heightened national tension.

In a similar fashion, as the political contest between Fatah and Hamas intensified in 2005, much of the momentum behind the PA's PFM reform agenda was dissipated. In Algeria, the broader political environment has hindered the reforms. Priorities on the political agenda after the terrorism period, and the general lack of political and technical commitment, explain lack of progress from 2001 to 2005. Lebanon's PFM reform agenda has also been repeatedly suspended by political unrest. A PFM reform program started in 2005 was suspended after the conflict with Israel in 2006, and another PFM reform program presented at the International Donor Conference in Paris in 2007 has been similarly held captive to the ongoing political unrest in that country.

In many parts of the world, the willingness to implement major public sector reforms is often linked to the electoral cycle. It is greatest immediately after an election, particularly if the incoming party is given a mandate for change. It drops considerably in the run-up to an election, partly because senior officials are caught up with the demands of campaigning and have less time for administrative issues, and partly because they are anxious to avoid taking decisions that could alienate powerful constituencies just before going to the polls. Although elections are a factor in a handful of MENA countries such as Morocco, Lebanon, the WBG, Yemen and Kuwait, as a general principle this dynamic is weaker and more muted in MENA for the obvious reason that elections themselves are typically less important.

Of more relevance are cabinet reshufflings. Their impact upon PFM reform agendas can be extraordinarily difficult to predict, but at a minimum such changes are disruptive and can reduce the incentive to support reforms with long gestation periods. This is particularly true in countries where cabinet turnover is more frequent, such as Jordan, where the average life span of a government between 1999 and 2007 was six to eight months. During this period, the Hashemite Kingdom has witnessed no fewer than eight Ministers of Public Sector Development portfolio and five Ministers of Finance. The implications for reform were spelled out in the words of one former civil servant:

It took three months to convince a new minister about our objectives, mandate, and by the time the person understood, he left. So much of our efforts were directed to educating ministers. Ministers knew that their tenure was short lived and that they would not stay for more than one year, and it affected the program greatly. They were interested in short term wins instead of longer term reforms and seeing the process in a holistic manner.<sup>36</sup>

Syria provides an interesting study in contrasts. Over the past five years, the two key reformers for PFM (the Deputy Prime Minister and the Minister of Finance) have had continuity in their positions, which has helped to facilitate Syria's reform efforts. However the broader geopolitical developments in the period have exerted tremendous pressure on Syria and diverted some attention of the key political figures.

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<sup>36</sup> Nagarajan, *Cabinet Decision Support Reforms: The Case of Jordan* World Bank and Dubai School of Government Case Study 2009-01 (forthcoming), p. 22.

It is difficult to determine if context is a definitive factor affecting PFM reform in MENA or merely an important one. If reforms are largely technical in nature, have a solid rationale behind them, are supported by well-positioned champions within the relevant ministries, and if they avoid alienating powerful constituencies, then under most circumstances they can probably stay “under the radar screen” and survive the shifting political, economic and administrative sands. Lebanon was able to implement some important reforms in payroll management, for example, even in the midst of a chronic political crisis and the absence of a functioning parliament.

But Lebanon’s experience is also instructive, in that when these reforms have needed to move beyond the realm of what could be implemented by a Ministry of Finance decree and required broader cabinet or parliamentary approval, they have stalled. There are no examples of more far-reaching PFM reforms that came to fruition if the broader political context was not supportive. Nor are there examples of where senior officials were able to isolate and protect major PFM reforms from major shifts in the broader political climate. Put succinctly, an ebbing tide grounds all large boats—regardless of how well they are designed or the skill and determination of the captain.

#### **Lesson 4: The Wisdom of “Muddling Through”—Grand Strategy versus Incremental Change**

To what extent are MENA PFM reform agendas driven by an overarching strategic framework or integrated plan, versus a more flexible and improvised approach that seeks to take advantage of opportunities when they emerge?

The answer is not entirely straightforward. On the one hand, MENA does not suffer from an absence of strategic plans for upgrading systems and procedures. Algeria drafted a PFM reform strategy in 2007, which has yet to be formally approved, although its Organic Budget Law articulates the directions of reform. In a similar fashion, Egypt has drafted a PFM strategy in 2008 which is currently under consideration by the MOF. Jordan had a Strategy for Financial Reform from 2004-2007 that was also embedded in broader national reform plans, including the *National Agenda*. In Morocco, PFM reforms have been embedded with the Governments Public Administration Reform Program of 2003. In Tunisia, a PFM reform program is being implemented and improving the use of resources as component of the Strategy for the Development of the Public Service 2007-11. The Bank has been assisting the Tunisians in drafting a budget reform master plan in 2008, which has not yet been formally approved but was used by the government in negotiating budget support from the EU. The Palestinians have clarified their intentions for PFM reform in a variety of documents, such as *Building a Palestinian State: Towards Peace and Prosperity*, which was presented to donors in Paris in December 2007. Yemen’s PFM reform strategy was approved by Cabinet in 2005 and has also been supported by the donor community.

Furthermore, there have been examples of when countries would have benefited from adopting a more comprehensive approach to PFM reform. Egypt has attempted a wide range of PFM reforms, for example. However, beyond the realm of tax and customs, progress has generally tended to be patchy and of limited duration. Until recently, there has been no overarching strategic framework within which reforms have been planned, prioritized, sequenced, costed, evaluated for feasibility and monitored. In a similar fashion, prior to 2008, Iraq’s management of the PFM reform process has suffered from the absence of any overall vision, strategy or prioritized and logically sequenced action plan. For example, the many capacity building workshops that have been run in and outside Iraq have provided participants with new knowledge and skills, but this training has tended to be ad-hoc and provided without the benefit of a more comprehensive framework for staff development, which in turn should be grounded in a careful assessment of the functions that the various ministries should be performing and the skills required to do them well. The lack of a more comprehensive approach can

be particularly problematic in the development of integrated financial management information systems, as will be discussed in greater detail below.

Such reform strategies can be valuable as a statement of intent, or for communicating priorities, securing donor support, or providing political cover for a given set of activities. Yet their role in actually shaping successful reforms can be modest. The development of such plans is no guarantee that they will be implemented expeditiously. In many MENA countries, roll-out has taken much longer than expected, with a number of components being dropped or modified along the way.

Nor are such plans a prerequisite for success. Egypt's far-reaching reforms in tax and customs were initiated in 2004, yet its broader plan for PFM reform is still under review. Senior officials repeatedly emphasized the probing and opportunistic nature of these reforms, while underscoring that the general strategic direction was clear. Salam Fayyad adopted a flexible view to West Bank & Gaza's PFM reforms, recognizing that he could not determine *a priori* the sequencing of reforms or expect to have control over the entire process.

He explains:

The context in which you are operating has to be kept in mind all the time. It's not easy. You are working within a system of deeply entrenched habits—not good ones—so you basically have one of two choices. Either to come in and say, 'this is what I want to do. Either it's done, or I'm out,' which is what everyone was expecting, or maybe even banking on. Or, you could be opportunistic: do what you can, as soon as you can do it, wherever you can do it. I chose the latter way...But, at all times have clarity as to what is important and what is not too important.<sup>37</sup>

Fayyad describes his approach as being, "patient, deliberate, methodical, and opportunistic, looking for an opening here and there." It was informed by a clear set of priorities. He began by focusing on the major structural problems related to revenue and expenditure management, treasury systems and the budget, which he described as "elements without which you cannot have a well functioning public finance system." But he combined this strategic orientation with tactical flexibility in terms of the sequencing and timing of reforms. His Deputy Finance Minister, Jihad al Wazir, notes that the actual sequencing of the WBG's PFM reform agenda was heavily influenced by political dynamics, and based on doing "what you can get done at the time."

In the final analysis, the optimal approach is likely to be one of "strategic opportunism." Such an approach would combine careful upstream analysis of the major strengths and weaknesses confronting a given PFM system, perhaps drawing upon a variety of analytic tools such as PEFA, PERs, CFAAs, CPARs, Fiscal ROSCs and the like, in forming a clear set of strategic objectives. But it would realize that there is an inherently organic nature to reform that makes it unlikely to proceed in a rational, linear fashion. Within MENA, the most effective reformers are those who have been strategic in recognizing and selecting appropriate windows of opportunity, while being flexible and opportunistic in exploiting them.

## **Lesson 5: Establish Basic Systems before Contemplating More Advanced Reforms**

The temptation is often irresistible for governments and international advisors to strive for quantum improvements in performance by adopting some cutting-edge practices from OECD countries into a developing country context. More often than not, the result has been a litany of dashed expectations and failed reforms. In response, the Bank's *Public Expenditure Management Handbook* (1998)

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<sup>37</sup> Fayyad, *Transcript*, 2008.



emphasizes the importance of “getting the basics” right before moving on to tackle more advance reforms. Drawing upon earlier work by Alan Schick and others, a number of precepts have been laid for doing so.<sup>38</sup> This list includes:

- Foster an environment that supports and demands performance before introducing performance or outcome budgeting;
- Control inputs before seeking to control outputs;
- Account for cash before accounting for accruals;
- Establish external controls before introducing internal control;
- Establish internal control before introducing managerial accountability;
- Operate a reliable accounting system before installing an integrated financial management system;
- Budget for work to be done before budgeting for results to be achieved;
- Enforce formal contracts in the market sector before introducing performance contracts in the public sector;
- Have effective financial auditing before moving to performance auditing; and
- Adopt and implement predictable budgets before insisting that managers efficiently use the resources entrusted to them;

The PFM reform experience within MENA largely bears this out. This has been particularly true with regard to two sets of initiatives that have been among the more technically advanced to be implemented to the region: the move to a Medium Term Expenditure Framework, and the effort to introduce greater performance orientation into the budget process. Both have shown themselves to be complicated and problematic to implement, in part because their realization has relied upon a number of preconditions to be in place before they can be effective, and in part because senior officials have been generally unwilling to allow themselves to be bound by such initiatives.

As the discussion in Chapter 2 indicates, a number of countries in MENA have sought to implement MTEFs, including Algeria, Jordan, Lebanon, Morocco and Tunisia. None have implemented such a system in its entirety. Jordan has probably made the most progress in implementing several components of an effective MTEF, although these reforms are still in their early stages. Other countries have made significantly less progress. Lebanon’s MTEF is only a general guidance to sectors communicated in the budget circular in the form of an overall budget ceiling. The MTEF is operational only as a pilot project in the Ministry of Education, and even there it only sets ceilings in terms of overall expenditure. In Morocco, an MTEF methodological guide was developed on preparing sector MTEFs in 2006. This guide has been approved and transmitted officially to line ministries by circular of the Prime Minister in 2007. In 2008, nine sector/ministry MTEFs were prepared, and MTEFs for five additional ministries are now underway. However integration with the budget has yet to be achieved and, at the moment, preparation of the budget remains input based with little explicit discussion of policies and priorities.

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<sup>38</sup> See *Public Expenditure Management Handbook*, p. 8.

In a similar fashion, reforms to introduce a greater focus on performance into the budget have often taken a long time to implement and been hindered by the lack of underlying conditions, such as a well-functioning accounting system that can yield accurate cost data. Such efforts can be prone to delays and interruptions. With regard to Algeria, for example, the performance budgeting pilots were stopped for one year by the MOF, and real ownership of the MTEF and performance budgeting pilots by the line ministries may be questionable. Jordan has also begun experimenting with some elements of performance budgeting, although the effort is still in its infancy with pilots being carried out in a few ministries. An earlier performance budgeting initiative assisted by GTZ Germany from 1999 to 2004 was regarded as being too ambitious and had little impact.

In some respects, a more interesting question is whether it makes sense to hold out objectives such as MTEFs and performance budgeting as a distant goal in the hope of gaining traction on some important but more pedestrian reforms, such as improving budget classification or upgrading the ability of the accounting system to provide more accurate cost data. A case could be made that embedding these smaller and “less glamorous” reforms in a broader objective will give them greater visibility and cohesiveness than they would otherwise enjoy. While such an approach cannot be ruled out entirely, MENA’s experience demonstrates that—while it may help with the initial “marketing” of the reform package—it is not a recipe for long-term success. It is better to set modest, measureable objectives and achieve them than goals that, with the passage of time, appear more and more ambitious and unrealistic.

#### **Lesson 6: When Possible, Keep Reforms Quick, Simple and Mutually Reinforcing**

It is an accepted article of faith among many officials and development practitioners that major PFM reforms are difficult, complex undertakings that require years or sometimes decades to fully reach fruition. Laws and regulations must be drafted; longstanding practices restructured; political and administrative cultures changed; institutions built and capacities strengthened. To attempt such undertakings quickly, so the argument goes, is a recipe for poorly thought through implementation and eventual failure.

As with many managerial maxims, there is some truth to these contentions. PFM reforms in a number of MENA countries, such as introducing MTEFs or greater performance orientation into the budget, introducing major IT systems, improving the quality of expenditure controls, or strengthening internal and external audit capacity do take a long time to implement. Algeria’s Budget System Modernization Project began in 2001 and was finally closed in 2009 after its objectives had been significantly scaled down. Morocco’s PFM reform agenda has been moving forward gradually since 2003. Reforms in West Bank & Gaza have been underway since 2002.

Yet there are also cases where reforms can be implemented quite quickly when the requisite political will exists. Reforms in expanding the scope and comprehensiveness of the budget, for example, can be implemented within weeks or months if the proper political will is in place. Reforms in improving budget transparency can also be implemented within no more than a month or two.

Furthermore, some of the more effective reforms were deliberately implemented with haste. Salam Fayyad wanted to generate confidence in the reform agenda by taking specific, quick steps that made an impression. He explains, “I have learned about the need to move fast, and make an impression. It gets more difficult with time, not easier. You need to use your success as a stepping stone. Success breeds success. If you say ‘give me time, I will assess,’ that is the wrong approach. You need to immediately begin to make an impression.”<sup>39</sup> These sentiments were echoed by Youssef Boutros

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<sup>39</sup> Nithya Nagarajan *interview with Prime Minister Salam Fayyad*, 2007.

Ghali, who notes, “the faster you move, the less resistance you will encounter, because it takes time for your opposition to organize and mobilize.”<sup>40</sup>

The reality of MENA’s experience is that many PFM reform efforts, including those of both Fayyad and Boutros Ghali, tend to follow an uneven trajectory. Periods of reform and progress are offset by intervals of limited activity and little forward movement. Sometimes, these periods of inactivity can be extensive. (Relatively little happened in Algeria’s PFM reform effort, for example, for nearly five years.) Admonitions to move with haste can help maintain momentum and push agendas forward. Otherwise, as has happened far too often in MENA, reform can become “business as usual” and lose any sense of priority or urgency.

***The Use of Pilots.*** A related question is whether to pilot reforms or roll them out whole. In MENA, pilot PFM reforms have been implemented in a wide variety of contexts. Algeria piloted some reforms in program budgeting but then discontinued the exercise. Egypt piloted the creation of a medium-size taxpayer unit in Cairo and the introduction of reduced ex-ante controls over virement in three governorates. Jordan piloted a results-based budgeting exercise in the education sector. Lebanon has piloted the introduction of internal audit within the Ministry of Finance. Morocco has also sought to pilot performance budgeting in a number of ministries. In the 2010 budget, Syria piloted the introduction of a program structure that integrated recurrent and investment budgets in two pilot ministries. Tunisia is piloting program budgeting in four ministries. Information systems have been piloted in a number of countries, including Jordan and Yemen.

The jury is still out regarding the effectiveness of pilots. Not surprisingly, the answer to this question is likely to be highly contextual and dependent upon both the nature of the reform and the institutional context in which it is being rolled out. On the positive side, pilots—particularly when combined with rigorous monitoring—provide an opportunity to gain valuable experience in identifying potential problems that could plague a particular set of PFM reforms and rectifying them before too much damage is done. This is particularly important when the roll-out is likely to be time-consuming and expensive, as is the case with large IT systems.

However, in the absence of firm commitment to proceed with a particular set of reforms, pilots can often become an opportunity for delay and inaction. Line departments in many MENA countries are often unenthusiastic about pilots, preferring to adopt a “wait and see” approach rather than invest time and energy implementing new approaches that may ultimately not be implemented. It is interesting to note that, after initially intending to pilot the introduction of the MTEF in specified ministries, Jordan’s General Budget Department decided to roll out forward estimates and performance indicators to all ministries rather than starting with a number of pilots. They did so with the understanding that it will take time to build depth in the process and bring about more fundamental changes in budget planning processes, but the effort was worthwhile and needed to proceed regardless. Furthermore, pilots tend to do better in administrations with a history of experimentation and innovation than those with fixed traditions embedded in a strong legal framework. In the Algerian context, for example, it can be easier to implement top down reforms based on laws and regulations rather than those that involve studies and pilots.

***The Value of “Virtuous Circles.”*** Finally, certain sets of reforms can foster “virtuous circles” and positive feedback loops, whereas others require constant effort. Budget classification is an example of the former, and it is not surprising that it has been one of the more effective reforms of its type in MENA. While it requires effort in overcoming institutional inertia and capacity building, once these skills have been obtained, it becomes easier each year to prepare and implement the budget with the

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<sup>40</sup> Author interview, H.E. Youssef Boutros Ghali, 2009.

new classification scheme. Other examples are reforms to the payment processes, payroll procedures, and monthly reporting. Once introduced, these procedures have continued. Even when there was a break in monthly reporting in the WBG during the Hamas period, for example, such reforms were reinitiated without too much difficulty.

### **Lesson 7: Be Wary of Large Financial Management Information Systems**

An integrated financial management information system (IFMIS) can offer great benefits for all PFM activities, especially budget execution. Such systems can facilitate timely and accurate reporting of budget execution; allow internal controls to be exercised through the IFMIS, and therefore support more consistent compliance; and allow central agencies to oversee budget execution by line ministries, therefore facilitating the devolution of responsibility to front line managers while retaining information at the center. All countries in the region have made some effort to introduce computerized systems to support PFM. In general, two different strategies have been taken towards this reform. These are to develop either: (1) a “sophisticated” fully integrated IFMIS; or (2) a simple customized IT system to support budget execution. While there are some small successes to date, the “sophisticated” projects have been problematic.

The fully integrated IFMIS approach has been followed by Yemen, Iraq, Egypt, Syria and more recently Jordan. Although the first efforts started in Yemen in 2003, as of 2010 none of the systems are fully operational. The Jordanian GFMIS—which was financed from local resources—appears to be best placed for successful implementation. In contrast to the other projects, the Jordanian GFMIS appears to have followed sound project management procedures and had active involvement from staff in the Ministry of Finance.

At the other end of the spectrum were efforts by U.S AID and a U.S. consulting firm, Bearing Point, to implement a Freebalance system in Iraq. As the discussion in Box 3 indicates, work began in implementing this system in 2003. After spending nearly \$30 million in developing the system, U.S.AID suspended work on the project in June 2007 and eventually signed an MOU with the Ministry of Finance handing over full ownership. While efforts continue to implement the system, recent assessments indicate that it is being used only for a modest number of government transactions.

### Box 3: History of the Iraq IFMIS System

In 2003, the Coalition Provisional Authority (CPA) instructed U.S.AID to begin implementation of the Iraq Financial Management Information System (IFMIS) through a contract implemented by the consulting firm BearingPoint. This task was undertaken to modernize Iraq's public financial management systems within a cash accounting framework. It was a key component of Iraq's stand-by agreement with the IMF.

By June 2007, the IFMIS had been rolled out in 132 spending units (SU) nationwide. According to Bearing Point and the MOF, these 132 SUs collectively accounted for over 80 percent of GOI expenditures. Work on the IFMIS was terminated by USAID following the abduction of five Bearing Point consultants in May 2007 at the MOF, as well as due to difficulties in aligning the system to the needs of the Iraqi government.

On January 14, 2008, U.S.AID and the Ministry of Finance (MOF) signed a Memorandum of Understanding (MOU), which gave impetus for USAID to restart the program by outlining an agreement to cooperatively identify and resolve technical issues and transfer full ownership of the IFMIS to the MOF. While USAID may continue to offer limited technical assistance to the MOF to operate, maintain and update the system, the MOF will assume full ownership of the computer hardware and software.

However, questions remain about the extent to which the system is truly being utilized. As of January 2009, eleven pilot SUs have been using IFMIS for less than five months and entered an average of less than 10 percent of total monthly transactions during the period of July to November 2008.<sup>41</sup> A World Bank assessment of this experience noted that it had been plagued by a number of problems, including:

- Unsatisfactory project supervision and contract management arrangements;
- Lack of support for and recognition of Project Management Teams;
- Insufficient or inappropriate incentives to promote the Government's PFM reform agenda;
- Inadequate consultative, coordination and co-financing arrangements to support high levels of ownership, effective partnerships and high degrees of commitment from key stakeholders;
- Poor FMIS design and more specifically the planning process to set the FMIS implementation strategy; and
- The absence of a medium-term PFM reform program that informs the prioritization and sequencing of specific PFM reform measures including development and roll-out of an FMIS.

While the Iraq project used an off-the-shelf package, the Yemen project was customized to meet local demands. Neither is considered to be particularly successful, although the Yemen system is likely to meet the basic functionality required by the government. In Syria, the IFMIS was developed as part of an EU project with limited involvement of line staff in the Ministry of Finance. The system was completed in 2008, but there is no indication from the Ministry of Finance that it is ready to be used. In Egypt two separate systems (AGES and IFMIS) were being developed in parallel by different teams. While the IMF recommended that the AGES project be discontinued, for some time the IFMIS was also not promising. However, a number of the problems appear to have been addressed, and recent assessments by the IMF suggest that the development of a new computerized financial management information system, under a project being managed by Booz Allen, is well on track.

The second approach has been to develop simple computerized systems with limited functionality to help support budget execution. The systems are usually customized to fit the specific needs of the budget execution system of the country. This approach was followed by Lebanon in the late 1990s and the system is still in place. More recently in West Bank and Gaza a simple system was developed, which in the space of four months went from concept to managing payments.

The use of a simple system has advantages—especially in cases such as West Bank and Gaza, where a new budget execution system was needed at short order. They tend to have much lower initial

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<sup>41</sup> This discussion is adapted from U.S. AID, *Iraq Financial Management Information System Assessment*, (January 2009), [http://pdf.usaid.gov/pdf\\_docs/PNADO270.pdf](http://pdf.usaid.gov/pdf_docs/PNADO270.pdf).

development costs and, provided their objectives remain minimal, they may also be an efficient way of exposing officials only familiar with paper based operations to the potential of a future IFMIS. However, there are limitations to the approach. First, because the systems are developed to order, they often do not include standard functionality that has proven to be useful in other systems. Second, the systems tend to be less flexible in dealing with new user requirements than off the shelf systems. This is a problem with the Lebanese system, where changes to the budget procedures can require substantial reprogramming of the IT system. While the initial cost of the system may not have been high, these costs increase over time as the system is reconfigured for new developments. For these reasons, the use of a simple system should be seen as a short term solution, with the eventual aim of moving to a fully integrated system. As with any short term solution, it is important to avoid overinvesting in developments that will eventually be superseded.

In summary, all countries in the region have been undertaking some IT investment to support the PFM system, but the record of the large projects in particular is not successful. There are a number of problems that have undermined these large projects, but two important concerns are: (1) weak project management arrangements; and (2) inadequate commitment and/or engagement of staff of the Ministry of Finance to the reform. The alternative of developing a simple non-integrated system to order has been successful in some countries in the short term. In general this approach makes sense as a step towards eventually developing an IFMIS, but not as a long term solution in its own right.

It should be noted that MENA's experience with FMIS is hardly unique. In both the public and private sectors, the implementation of large IT systems has often been problematic. In one study, fully 75 percent of IT systems implemented in the United States failed to fully deliver in terms of their time, cost or projected functionality. Other studies have cited similar failure rates. The reasons for this lack of success are many. On the design side, they include insufficient analysis of the business case; poor definition of project scope and objectives; insufficient time allotted and over-optimistic planning. Project management issues include insufficient backing from senior executives; a lack of authority or decision-making ability in the team; poor collaboration and communication; and inadequate tracking and reporting. Even under the best of circumstances, large IT systems can be complex and difficult to implement. A World Bank study in 2003, for example, noted that a review of Bank FMIS projects took on average over seven years to complete with an average cost of \$12.3 million. Thus the problems that large IT systems encounter in MENA are more likely to reflect the difficulties inherent in implementing such systems anywhere, particularly in low capacity environments, rather than any special technical or administrative challenges unique to the region.

## **Lesson 8: Internal Challenges: Leadership, Coordination, Skills and Incentives**

MENA's reform experience holds a number of important lessons as to how such reforms should be structured and organized. This section addresses several key themes, including: (1) the stature and status of key reformers; (2) the coordination of PFM reforms within government; (3) how reform units and project management units have been structured; (4) their staffing and skills mix; and (5) the role of the chief executive. Each is discussed in detail below.

***Stature and Status of Key Reformers.*** It is axiomatic in the literature of public management that reforms need to have a champion. It is therefore not surprising that many of the most far reaching PFM reforms within MENA have been driven by powerful ministers of finance, who play a uniquely important role in taking the PFM reform agenda forward. There is, quite simply put, no more important position for advancing this agenda in the region.

In this regard, the experience of Salam Fayyad in the West Bank & Gaza and Youssef Boutros Ghali in Egypt is particularly instructive. Both men brought a combination of impressive expertise and solid

technical understanding of the issues. Their backgrounds are remarkably similar—both have Ph.D.s in economics and spent time in the International Monetary Fund before assuming their duties. Beyond technical knowledge, they brought managerial talent and dynamism, along with a clear vision as to what needed to be done and considerable political savvy. Perhaps most importantly, they brought sheer determination. As Boutros Ghali notes, “you need to be fixated—single minded—and repeat yourself over and over again until it happens.”<sup>42</sup>

Egypt’s experience is also instructive, in that major reforms cannot be implemented by the Minister alone. Boutros Ghali argued that he could not do a tenth of what was needed. He needed a group of like-minded reformers around him, around 50 in his estimation, to help take the reforms in tax and customs forward. Part of their responsibility was to provide the necessary technical expertise when needed; part of it was to oversee the implementation of various dimensions of the reform agenda; and part was to monitor if actions were being taken as promised. The question of how to best balance external and internal expertise is a thorny one that will be addressed in greater detail below. However, in the view of Minister Boutros Ghali, such a cadre of committed in-house allies was essential, as one should not underestimate the tenacity of resistance to major reforms from the rank and file bureaucracy.

***Coordination of PFM Reforms within Government.*** While national legal and institutional frameworks differ at their core, PFM reforms center upon the Ministry of Finance. The MOF has clear responsibility for the recurrent budget in all of the countries in this study, and MOF staff seconded to line departments play an essential role in authorizing expenditure. The extent to which the MOF dominates the budget and expenditure process may vary. In a few administrative contexts, the MOF is clearly the dominant player in most aspects of public financial management; in others, it has historically played more of an instrumental role in facilitating and monitoring decisions taken elsewhere. Jordan is unique in that responsibility for formulating the recurrent budget has been given to a quasi-independent agency, the General Budget Directorate, with a weak reporting relationship with the Ministry of Finance. Regardless of these arrangements, the MOF occupies a pivotal position in the reform of public finances, and no PFM reforms in MENA have been able to move forward unless the ministry is fully on board and committed.

Most countries also have powerful Ministries of Planning who look after the capital budget. In a number of countries, such as Jordan, WBG and Yemen, the Ministry of Planning is responsible for issues of donor coordination. However, a few (such as Egypt) have given this function to other agencies, such as the Ministry of International Cooperation. Many also have various supreme audit agencies or *cour des comptes* who play a role in ex-post (and occasionally ex-ante) audit and approval. Beyond the immediate core actors, there are a wide array of public sector participants and stakeholders in the budget process, including ministries, agencies, departments, commissions, deconcentrated and sub-national entities, and state owned enterprises.

The quality of coordination between these agencies and the MOF varies both within and between countries, but it is frequently problematic and occasionally dysfunctional. Iraq serves as an example of the latter. One of the most significant challenges facing the GoI is to improve the integration of the capital and recurrent budgeting processes. Bank analysis of the Iraqi PFM system found that reforming these arrangements will be challenging owing to the traditional rivalry between the two ministries, the political allegiances of the respective ministers and the need to ensure no loss of face on the part of either ministry. A 2006 assessment of Algeria’s PFM reforms also noted lack of inter-agency coordination and a failure to adequately engage with line ministries as a reason behind their limited success. Even in countries such as Jordan, the institutional fragmentation of the budget process

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<sup>42</sup> Author interview, H.E. Youssef Boutros Ghali, 2009.

between the MOF, MOP, General Budget Directorate and the Prime Minister's office had been an obstacle to the formation of a unified view of budget reform and has compounded the problems of identifying a champion of the reform process and ensuring effective leadership from the MOF. A joint Bank-Fund team reviewing the reform experience in 2004 suggested that the main constraints on the effective design and implementation of an ambitious budget reform program were weak leadership, institutional fragmentation and weak reform management capacity.<sup>43</sup>

To cope with such problems, a number of countries have established inter-agency task forces to facilitate the coordination of PFM reforms. Yemen, for example, has vested overall responsibility for implementation in a Ministerial PFM Reform Committee, which meets annually and is responsible for the implementation of the strategy and achievement of the desired reform outcomes.<sup>44</sup> A PFM Reform Task Force headed by the Deputy Minister of Finance in Charge of Budget has been set up which is responsible for overseeing the implementation of the reforms, along with a number of technical committees that have responsibility for specific PFM Reform activities, such as the Committee on Functional Classification.

Unfortunately, while such coordinating bodies can be relatively easy to establish, in a number of cases they end up meeting only infrequently, thus compromising the quality of implementation.

The various MENA country templates underscore that the position of the broader public sector, and particularly line departments, government agencies and state owned enterprises, will vary depending upon the nature of the issue at stake. As a general rule, line departments have been supportive of changes, such as increased virement, that give them greater control over and discretion in the use of resources. They are resistant to changes that create new obligations or could reduce their influence and power, such as eliminating extra budgetary funds. However, the views within such agencies are seldom monolithic. When Salam Fayyad instituted a process of paying the salaries of security services by direct deposit into Bank accounts, many of senior security officers resisted this effort. However, it proved to be quite popular with the rank and file security personnel.

One area where progress could be made throughout MENA is in the expansion of inter-agency coordination mechanisms at the working level. Throughout the region, most decisions tend to flow up to the minister, which can lead to delays and the compartmentalization of information. Within a given ministry, the minister is also typically the focal point for coordination, and interaction across the different departments can be limited. In most reforms, effective internal communication appears to be a problem. The World Bank's 2008 CFAA on Egypt comments that, "information on the MOF initiatives to improve PFM is not adequately communicated to ministries and their staff."<sup>45</sup>

***How Reform Units and Project Management Units have been Structured.*** MENA countries have adopted a variety of approaches to managing PFM reforms on a day-to-day basis and gaining access to the requisite expertise. Some governments have relied heavily upon project implementation units staffed largely by external experts, including Algeria, Lebanon and Yemen. Others have sought to keep these reforms in-house, either by asking existing officials to take them forward as part of their ongoing responsibilities or by setting up dedicated reform units. While each approach has its relative strengths and weaknesses, some general lessons have emerged.

The first is that technically skilled and managerially adept leadership is required at the project management level—and such leaders need to be fully empowered—or the reforms are unlikely to

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<sup>43</sup> World Bank/IMF, *Jordan Work Program for Consolidating Budget Management Reforms*, 2004.

<sup>44</sup> The Committee is made up of the Minister and Vice Minister of Finance, the Minister of Planning, the Minister for Civil Service, the Minister for Local Authorities and the Governor of the Central Bank.

<sup>45</sup> World Bank, *Egypt: Country Financial Management Accountability Assessment*, 2008.



succeed. In Algeria, for example, there was no director of the General Budget Directorate for several years, only an acting director. Reforms did not move forward during that period. In Egypt, one of the factors that contributed to the slow progress in GFMIS implementation was the absence of a full-time project manager and support staff; at other times, project managers were appointed without appropriately delegated authority. Iraq has shown that problems can occur during implementation as a result of limited authority and resources being delegated to program managers. Too often, decisions have to be referred up the hierarchy in a way that stifles initiative and provides little incentive to managers, which undermines ownership of and commitment to the reforms.

Second, to some degree, organizational structures and reporting relationships can be flexible and tailored to the unique institutional circumstances and challenges at hand (as well as the available budget). A minimalist approach often involves one or two experts embedded as advisors within a ministry. While their modest capacity limits the reforms they can support, such experts can be valuable in providing real-time advice and assistance and in serving as brokers for bringing in additional expertise as necessary. For more substantial reforms, the typical structure involves a committee at the ministerial or deputy-minister level to provide oversight and political support; a working group at the technical level to coordinate the work, and—depending upon the size of the reform agenda—various sub-groups dealing with particular topics that report up to the technical committee. The technical committee itself is usually staffed by a secretariat consisting of local and international experts.

Numerous variations on these models exist, and a number have been quite effective. Egypt's project management arrangements for tax administration evolved considerably without noticeably impacting the pace of implementation. This may be because the quality of personal relationships among the key players matters greatly. A suboptimal project management structure can be made to work if there is good will and trust among the relevant players, whereas even a well-designed structure will fail if the participants refuse to cooperate.

***Staffing and Skills Mix.*** Capacity constraints at the team level are often not taken seriously enough in designing reforms. Even governments with relatively strong capacity among mid-level managers and at the working level, such as Jordan, have struggled when the PFM reform agendas have become too broad and demanding. The resources required to implement reforms have often been inadequate or not sustained, as other more pressing matters have captured the attention of key officials.

Efforts to work around a lack of capacity by relying heavily upon external experts or local staff recruited specifically for the task are a Faustian bargain. Egypt also demonstrates a particularly interesting approach to the challenge of bringing in talented staff to help with the reform effort. The Minister has surrounded himself with a group of “outsiders,” some of whom have been brought in from the private sector while others came from other parts of government. This group provides a specialist cadre that runs parallel to the traditional administration and is much better paid (in this case, by international donors). In a similar fashion, both Lebanon and Yemen have utilized donor funds to recruit external experts at salaries as much as ten times that of local staff to provide badly needed expertise.

Unfortunately, this has created a dichotomy between donor and government financed staff, with the risk that the latter—often very experienced—feel marginalized and lack motivation. It can also lead to a backlash, particularly when such reforms are perceived to be driven by expatriates who do not adequately understand local conditions or may be trying to “impose” a donor-driven agenda. Some ministers, such as Boutros Ghali, have sought to address these concerns by keeping external technical advisors in the background and away from line department staff. While reliance upon imported expertise may be the only way to gain access to the requisite skills and knowledge necessary to

implement certain PFM reforms, it is a short-term approach and should be implemented only with a medium term exit strategy in mind.

***Monitoring the PFM Reform Agenda.*** MENA governments have often chronically under-invested in the careful monitoring of reforms. In Morocco, for example, there is a PFM reform subdivision within the budget directorate of the MEF. The deputy director of budget supervises, among other divisions, this sub-division. However, there does not appear to be any systematic monitoring of the reforms by government. The same is true in Lebanon, where a unit financed by UNDP is in place with a mandate to assist the MOF with the implementation of PFM reforms. However, there is no monitoring system in place to report on progress or delays. Even in cases where formal mechanisms existed, such as in Syria, they are often not utilized.

***Office of the Chief Executive.*** Perhaps one of the more interesting findings to come out of the MENA case studies is the relatively modest role played by leading political authorities, be they sheikhs, presidents or prime ministers, in supporting the PFM reform agenda. While it is difficult to conceive of such reforms going forward without their backing (or at least their implicit support), virtually no head of state sought to proactively advance these reforms. They did not get out in front of the issue by giving speeches, having regular meetings with teams working on various PFM reform agendas, or pushing reluctant or recalcitrant ministries to cooperate. At best, their efforts involved creating enough political space that champions at the ministerial level could advance the reforms and making favorable reference to the agenda in broader speeches before parliament and other venues about the government's overall strategy.

## **Lesson 9: External Stakeholders—Useful, but Don't Count on Them**

As a general rule, the Executive Branch is extraordinarily powerful throughout MENA. Other stakeholders—whether they are the legislative or judicial branches, various civil society organizations, academics, think tanks, private sector groups and the like—operate at a distinct disadvantage when it comes to influencing the process of political and administrative decision-making. This is particularly true with regard to PFM reform, which is often viewed as a narrow, specialized and technocratic field. This analysis focuses upon two sets of stakeholders who (in principle at least) could be able to influence PFM reform: (1) parliamentarians and legislative bodies; (2) civil society and the public. The role of a third group, donors and the international community, is discussed in the following section.

***Parliaments and Legislative Bodies.*** As the tables in the Appendix indicate, MENA averages a bit under the global mean for Lower Middle Income Countries regarding legislative coverage of audit reports, and a bit better for legislative scrutiny of the budget, with its average score being virtually identical. However, these averages mask considerable divergence between countries. Furthermore, MENA's aggregate rankings would fall significantly short of best practice in a broader global comparison. Throughout the region, parliaments operate at a major disadvantage vis-à-vis the executive branch on PFM issues. They typically lack the staff and committee structures that allow them to provide detailed scrutiny to budget proposals, and their follow-up in areas such as audit reports is variable. In a number of countries, their ability to revise or change budgets presented by the executive is limited, and the information they receive can be partial and fragmented.

As a general rule, parliaments have not been a strong force for PFM reform. In fact, at times the opposite has occurred. In Iraq, a major reform of the income tax regime was attempted in mid-2006. During parliamentary consideration, further retrograde changes were proposed with the opposite effect, and accordingly the package became stalled. Elsewhere, parliamentarians have generally been disinterested in PFM issues and reforms or preoccupied with other issues.

However, there are a few bright spots. Until its dissolution in 2006, the Public Accounts Committee of the Palestine Legislative Council played a proactive role in scrutinizing PA finances. In Egypt, there are encouraging signs of parliament becoming more active in its oversight role. Good examples have been provided by recent aggressive debates over the report of the Central Audit Organization and the changes made to the Government's 2007-08 budget proposals. Yemen has enjoyed vibrant parliamentary oversight of the government's budget estimates approval process. The Yemeni parliament appears to have been less engaged in monitoring actual expenditure achievements or of the quality of expenditure management, although again this appears to have changed for the better in recent years.

***Civil Society and the General Public.*** If parliament's influence over the PFM reform process has been modest, that of the public has been virtually nonexistent. A few NGOs and think tanks may have pressed for greater budgetary openness and transparency, but there is no evidence that they have had any real influence over the shape or content of PFM reform programs to date. In general, PFM reforms are too technical and too removed from their day-to-day experience for the public to form strong views about them, either pro or con.

Exceptions to the public's general detachment are PFM reforms that directly touch their livelihood and depend heavily upon citizen compliance. Egypt's tax and customs reforms are an excellent example. These reforms were generally popular, to the extent that they reduced the highest tax rate for corporations from 40 to 20 percent and for individuals from 32 to 20 percent. The Egyptian Government did embark on a fairly substantial consultation effort six months before the reforms were initiated, including both a number of roundtable discussions with various stakeholders and a media campaign. The implementation of these reforms may have been shaped in modest and incremental ways, such as the creation of a Large Taxpayer Center and pilot Medium-sized Taxpayer Center in Cairo. But there are clear limits to public influence. There has been no taxpayers' charter, and the Supreme Council of Taxes (a societal watchdog agency) has yet to be created.

Beyond tax and customs, public opinion may at best play a modest supporting role in two or three countries in the region. Concerns about widespread corruption within the PA, for example, may have generated some goodwill for Salam Fayyad's reforms in 2002. The promise of bringing tangible benefits to the local populace may have also influenced Fayyad's efforts to dismantle the monopolistic pricing structure of the Petroleum Corporation, which was cited in the epigram at the beginning of this chapter.

Unfortunately, even when successful, PFM reforms do not translate readily into political gains. In the January 2006 elections to the Palestine Legislative Council, Salam Fayyad's "Third Way Party" received 2.4 percent of the popular vote and won only two of the Council's 132 seats. There are examples when the public has actively opposed various aspects of the reform agenda, such as when Egyptian pharmacists called a nationwide strike and took to the street in protest against a decision by the Ministry of Finance to alter retroactively a previously agreed arrangement as a part of the tax reforms.

#### **Lesson 10: Lessons for Donors: Be More Strategic, Selective, Modest and Flexible**

The donor community has been heavily, although unevenly, engaged in providing support to public financial management reforms throughout the MENA region. Those most involved include the International Monetary Fund, the World Bank, the OECD, UNDP, and the European Union. A number of bilateral donors are also heavily engaged in providing support, including Britain's Department for International Development, the United States Agency for International

Development, the *Agence Française de Développement*, and the Dutch and Norwegian governments, among others.

A detailed assessment of the effectiveness of donor funding is beyond the scope of this exercise, which has focused more generally on the PFM reform challenges confronting the countries of the MENA region; the types of reforms being implemented; and which have shown promise to date and which have not. Nevertheless, a few conclusions emerge that may be valuable to donors active in this area. They are discussed below under three headings: (1) the nature and scope of donor engagement in MENA on PFM issues; (2) the substantive lessons for donors regarding PFM reform; and (3) modalities and processes.

**Table 11: Donor Support for PFM Reforms in MENA**

PFM - ODA Commitments (Current US\$ million)	2003	2004	2005	2006	2007	(Partial) Total per country	Annual Average
<b>Iraq</b>		0.04	..	137.61	40.20	177.85	35.57
<b>Morocco</b>			0.00	100.86	0.24	101.10	20.22
<b>Jordan</b>	0.01	2.38	0.04	25.48	58.51	86.42	17.28
<b>Tunisia</b>	0.43	0.48	0.13	..	41.39	42.43	8.49
<b>West Bank-Gaza</b>	11.54	2.62	4.12	1.35	3.10	22.73	4.55
<b>Syria</b>		9.94	0.39	..	0.00	10.33	2.07
<b>Egypt</b>		0.02	1.02	3.78	6.23	11.05	2.21
<b>Yemen</b>	0.19	0.04	1.86	..	3.99	6.08	1.22
<b>Algeria</b>			0.17	0.28	0.26	0.71	0.14
<b>Lebanon</b>					0.20	0.20	0.04
<b>Total for MENA</b>	<b>12.17</b>	<b>15.52</b>	<b>7.73</b>	<b>269.36</b>	<b>154.12</b>	<b>458.90</b>	<b>91.78</b>

Source: OECD DAC. Data are for the most recent years available.

***The Nature and Scope of Donor Engagement in MENA on PFM Issues.*** Table 3.2 provides a breakdown of average donor support for PFM issues by country drawn from the OECD DAC database. Approximately ten MENA countries received donor assistance for PFM reforms during the period from 2003 to 2007, with the lion's share going to Iraq, Morocco and Jordan. Other recipients included Algeria, Egypt, Lebanon, Syria, Tunisia, West Bank and Gaza, and Yemen. According to OECD DAC figures, total funding for PFM was around \$459 million during this five year period. The average was \$92 million, with considerable variation between years.

While the data probably provides a rough proxy for relative levels of donor engagement, care should be taken to not read too much into the findings, since some of these figures may reflect budget support with a PFM focus rather than dedicated resources for PFM reform. The latter is likely to be much more modest, probably averaging in the \$1 to \$5 million dollar range per country annually after adjusting for the odd major IT project, with some countries receiving substantially less. The bottom line is that PFM reform in MENA is not an area where the donor community has over-invested.

It is hard to make judgments regarding the effectiveness of this assistance. An effort to see if there was any statistical relationship between levels of donor aid for PFM and PEFA scores among recipients turned up virtually no correlation whatsoever (the  $R^2$  coefficient is 0.00).<sup>46</sup> The implications of this finding are unclear. It could mean that donors have not been effective in their support for PFM operations. Far more likely, it means that they allocate their assistance for PFM reform on criteria other than the underlying performance (or lack thereof) of the recipient country, as measured by the PEFA indicators.

In all likelihood, the influence of donors over the PFM reform process is more subtle and nuanced than can be captured by simple correlations. Donors can be a powerful impetus for change and reform, although their “persuasiveness” is closely aligned with a given country’s level of aid dependence. In countries such as Algeria and Syria, where donors have relatively little influence on government decision-making, domestic political and internal dynamics predominate. Donors can play a role in proffering advice and disseminating information, but governments enjoy great discretion over whether they choose to accept this advice or not. In settings such as the WBG and Yemen, where governments are heavily aid dependent, donors are able to play a more influential role in pressing for various reforms. A much less powerful but still important factor is the role of the international community. In the Maghreb, proximity to Europe and the pull of the European Union’s Neighborhood Policy and *acquis communautaire* have exerted some influence upon the PFM reform agendas in Morocco and Tunisia, as have the French budgetary reforms that have taken place since 2001.

It remains to be seen how the new generation of actionable indicators, such as PEFA, will have an impact upon the willingness of senior MENA officials to improve their PFM performance. On the positive side, it is clear that cross-country comparative indicators such as the World Bank’s *Doing Business* have played an important role in motivating senior officials in countries to undertake reforms aimed at strengthening their business environment. In Egypt, such improvements have been the source of considerable pride and have prompted progress towards reform in other areas, such as anticorruption. There is evidence that, in at least one MENA country, PEFA indicators may have played a comparable role. However, in some respects, PFM indicators such as PEFA are qualitatively different. The *Doing Business* indicators cater to a much larger constituency, including foreign and domestic investors and business associations. They are produced annually with an explicit comparative focus. PFM reforms tend to fall in the domain of specialists. PEFA was not explicitly set up with cross-country comparisons in mind, and the analyses are done much less frequently than once a year. For these reasons, they are unlikely to serve as a comparable motivating force for PFM reforms.

The experience of MENA countries indicates that donor engagement on PFM issues is a two-edged sword. On the positive side, the large number of countries with some type of donor supported PFM program bears witness to the considerable demand for donor resources and technical expertise on PFM issues. Beyond these countries, a number of others in the GCC and elsewhere are purchasing technical assistance from institutions such as the World Bank and IMF on a reimbursable basis—a “market test” that provides one of the best indications of country demand available. In addition to advice and assistance, donor engagement can be useful in “locking in” a particular reform program and generating publicity and obligations that domestic reformers can use to their advantage. Donors can also play a vital role in monitoring the implementation of various reform agendas that, as was noted above, is an area of chronic weakness in MENA. For all of these reasons, virtually no major PFM reform in MENA has been exclusively “home grown.”

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<sup>46</sup> Internal World Bank calculations. The authors are indebted to Hala Hanna of MNSD for this analysis. Looking over time, it will be interesting to observe whether repeat PEFA assessments indicate that donor involvement is having a positive effect on overall PFM performance.

But donors can also pursue their own agendas in ways that can occasionally complicate a given nation's PFM reform effort. The most prominent example is West Bank & Gaza, where donors invested considerable effort and energy from 2002 to 2005 in building up the Ministry of Finance as an alternative to the President's Office for managing the PA's finances, only to change course after Hamas was elected in January 2006 and support the President's Office, and then to switch back again in July 2007 after Fatah regained control of the West Bank. Fortunately, PA institutions were durable enough to withstand such pressures. But they did take a toll.

While the situation above is unique, it is far more common to encounter problems in fostering donor coordination in aid dependent environments, which can interfere with efforts to expand budget comprehensiveness or to integrate the recurrent and capital budgets. The PA has struggled with the superficial integration of public investment expenditures into the budget. The Ministries of Planning and Finance are co-signatories to all development projects financed by donors. But in practice, they have had limited engagement in the selection of projects, as donors often elected to engage directly with line ministries, other PA institutions and local governments. As a result, projects were not considered in a framework that accounted for future recurrent costs and debt servicing capacity, and the PA budget did not adequately reflect donor financed public investment.<sup>47</sup> Different donors also had conflicting expectations, demands and reporting requirements. While they called for PFM reforms since the 1990s, many donors were also under pressure to disburse to the PA and in practice and were willing to allow such reforms to take a back seat to more immediate priorities.<sup>48</sup>

***The Substantive Lessons for Donors on PFM Reform.*** Chapter 2 has addressed the substantive challenges of PFM reform in MENA at length, and its findings are summarized in Table 10. Their messages will not be repeated here. Suffice it to say that many donor-supported reforms have been too ambitious, overstating the amount of political and bureaucratic support for reform; not fully aware of the role of legacy systems and whether the necessary preconditions were in place; and in general trying to do too much within too limited a period of time and without the required capacity. At times, there is even a lack of understanding or consensus as to what reforms such as implementing a “medium term expenditure framework” or “introducing performance into the budget” will actually mean in practice. Donor programs can be far too comprehensive—seeking to solve too many problems at once—and would benefit from greater selectivity and prioritization.

There are two emerging issues that will shape donor approaches on PFM reform in the future. The first is growing use of PEFA exercises, which are likely to play a valuable role in improving the quality of donor assistance. There is considerable appetite within MENA countries for the use of PEFA assessments as a benchmarking tool, and the number of such exercises in the region is progressing steadily at a rate of two or three a year. Some GCC countries such as Kuwait are even willing to pay to have their PFM institutions and systems reviewed through the use of reimbursable technical assistance. This trend is a healthy one, in that the expanded use of PEFA will enlarge the amount of analytic work available to inform PFM reforms; help donors to better understand where the real issues and challenges are; and allow countries to monitor their performance over time, thus creating additional incentives to take PFM reforms forward. However, would be donors should also be wary in using PEFA exercises mechanistically to design reform strategies, lest they find themselves trying to “fill in the gaps.” Such motives, while understandable, may well result in developing reforms for areas where a given PEFA score is low but the demand for improving it is also weak and unsustainable. PEFA is not a substitute for careful strategic analysis and decision-making.

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<sup>47</sup> IMF, *West Bank and Gaza: Economic Performance in Conflict Situation*, op. cit., p.94

<sup>48</sup> Bank interview, Ghassan Khatib, May, June 2008; Bank interview with Dr. George Giacaman. 2007

The second trend is the increasing use of political economy analysis to illuminate public sector reform options, which is covered in the first lesson of this chapter. Few would dispute that political and bureaucratic dynamics can play a decisive role in the evolution of PFM reforms, and that a careful understanding of the issues involved would be invaluable to donors interested in supporting this work. The problem, put succinctly by a leading reformer in the region, is that donors “are typically not well-equipped to do it.”<sup>49</sup> By that, he meant that the process of PFM reform is a dynamic one requiring a great deal of insider knowledge and a lot of tactical real-time adjustments to changes in the prevailing political and bureaucratic winds. To the extent that donors will be able to capture this subtlety and nuance—whether it be through the use of embedded ministry advisors, knowledgeable local experts or some combination of both—their programs will be the better for it. However, if the exercise becomes static and routine, such as bringing in an external expert to draft a political economy report according to a standard template prior to the initiation of a major PFM reform, then much of its usefulness will be lost and the shelf life of the final product may be short.

***Modalities and Processes.*** In a similar fashion, donor modalities need to be developed to better respond to the dynamic nature of the PFM reform process. There is a role for the traditional project management framework when the reforms are large and enduring (and the sums involved substantial), which is designed to successfully manage a broad and diverse agenda and ensure appropriate accountability. But lengthy appraisal, consultant selection and mobilization procedures often result in delays and lost opportunities. As was noted in Lesson 4 above, the more successful PMF reforms tend to involve “strategic opportunism”—seizing upon opportunities rapidly as they emerge within a broader framework of clearly articulated priorities.

To exploit such opportunities as and when they occur, donors need to augment their traditional approaches with small, rapidly disbursing, carefully targeted aid. To do this will require several preconditions: (1) accurate, up to date knowledge of the situation on the ground, including the evolving political and bureaucratic dynamics; (2) talented, advisors who have technical skills, political and managerial savvy, and the trust of senior officials; (3) a well-articulated framework of PFM priorities; and (4) small amounts of discretionary resources that can be utilized quickly and flexibly to help facilitate implementation. Donor support can help create these essential preconditions.

While some donor-financed studies have been technically good, many were overwhelming in the quantity of recommendations provided, and there is often insufficient guidance on the prioritization and time sequencing of reform and on how to deal with institutional and capacity constraints. Furthermore, effective change management processes and skills have often been lacking.

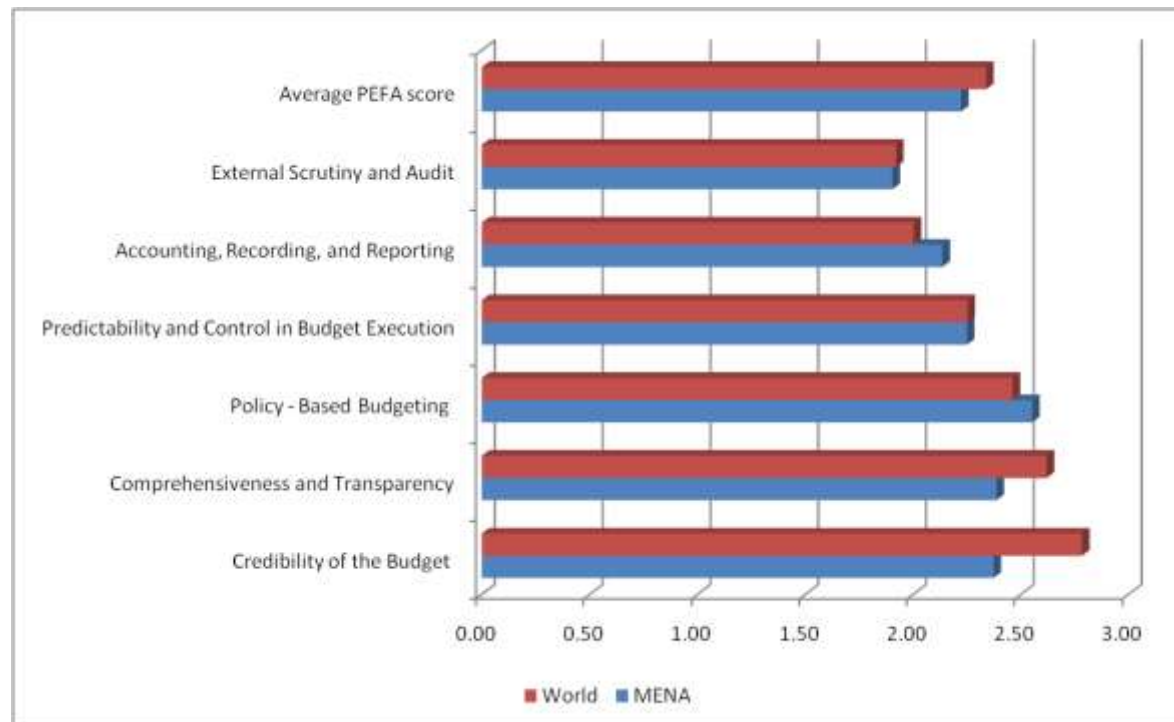
Finally, the legacy of partial and failed reforms in MENA indicates that there are times when the best strategy for donors may very well involve doing nothing. If the preconditions are not in place and there is limited will, capacity or political space for advancing PFM reform, then as indicated earlier, the most promising approach would be to focus on technocratic reforms, such as revising the budget classification. However, in many situations it may be difficult to proceed with even these modest programs. Such an approach runs contrary to the basic incentive systems at work in most donor agencies, where staff are encouraged to “make things happen” and weak PFM practices may be interfering with broader efforts to provide budget support. Yet in most cases, a poorly planned and executed set of PFM reforms is worse than none at all, in that it creates a barrier of resistance and cynicism that future reformers will need to overcome later.

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<sup>49</sup> Author interview, H.E. Youssef Boutros Ghali, 2009.

## Appendix

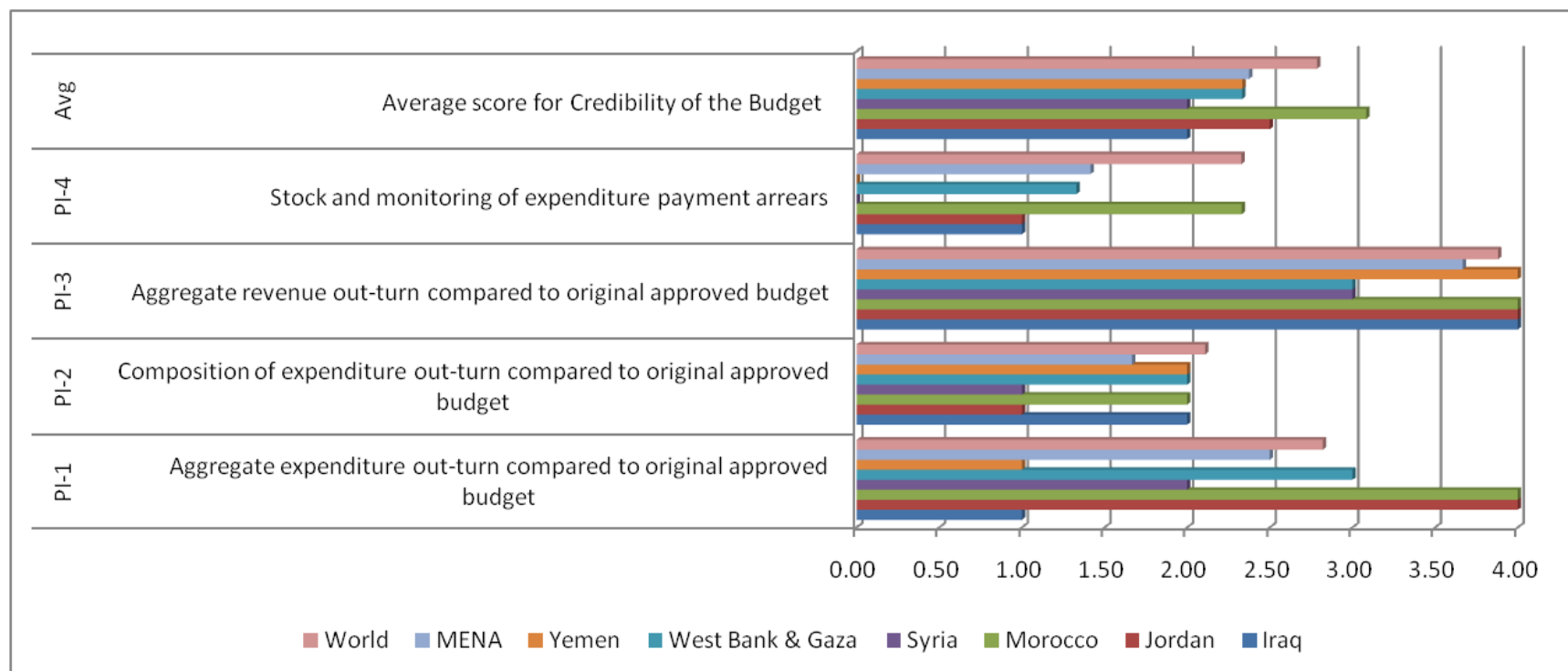
**Table A. 1**  
**MENA PEFA Averages Compared With World Averages**  
**For Comparable Countries**



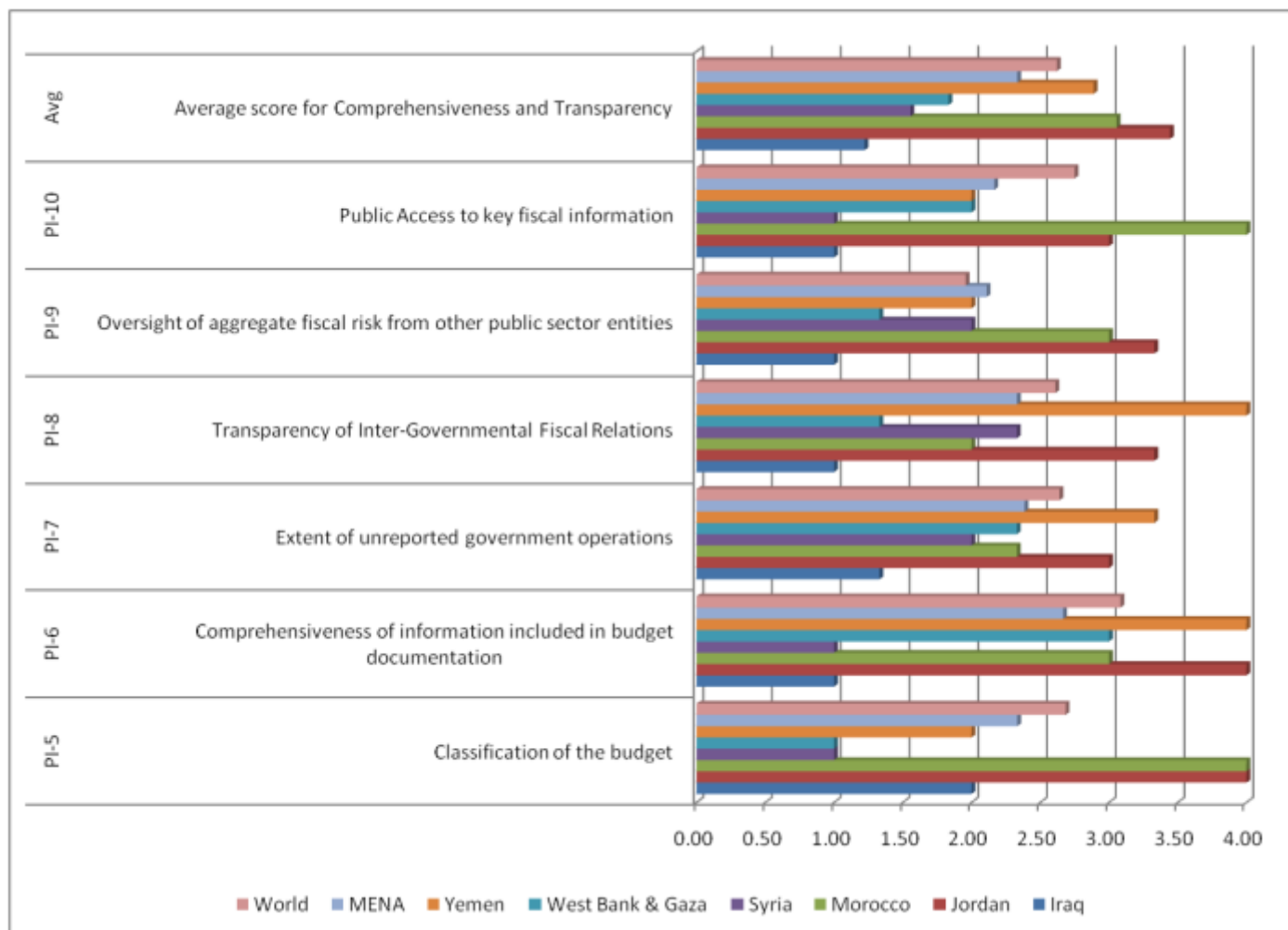


**Table A. 2**  
**MENA Country Scores on Individual PEFA Criteria**

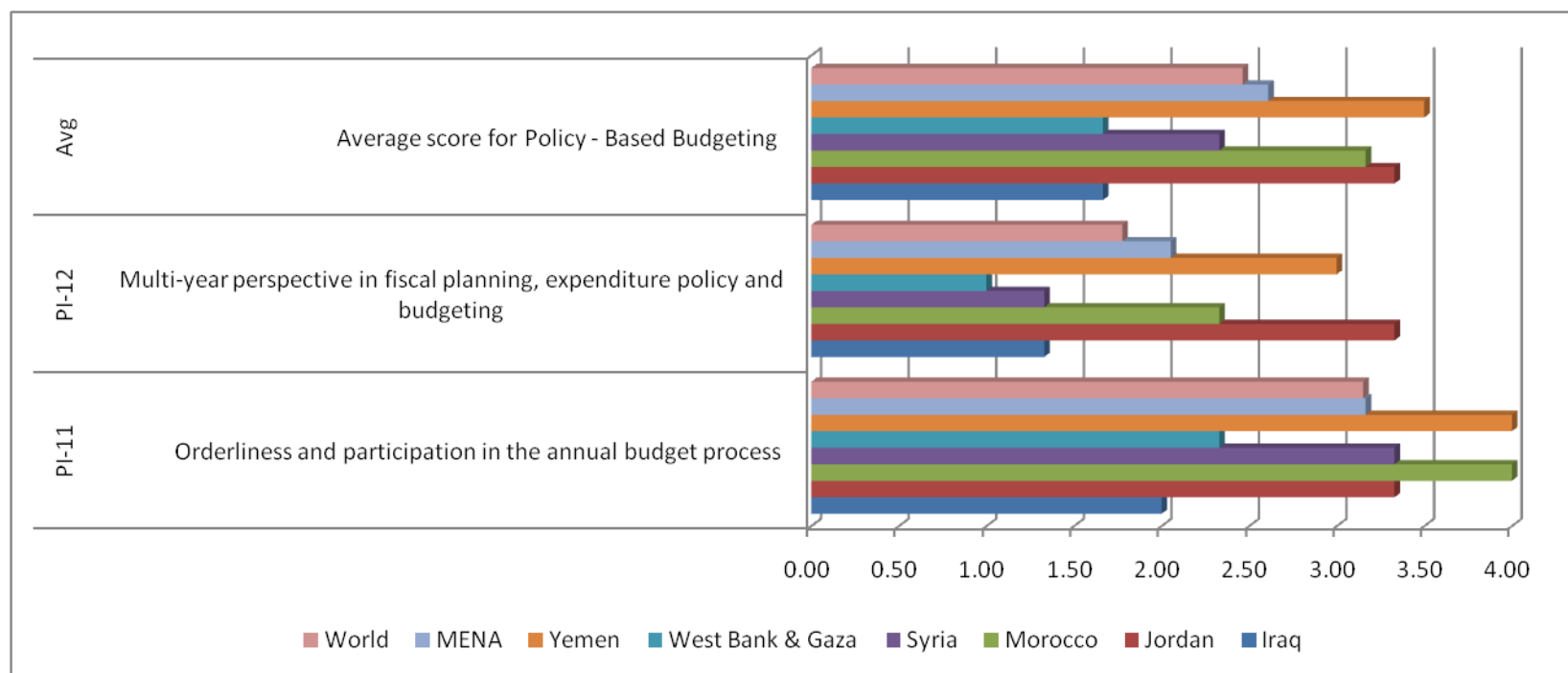
**Credibility of the Budget**



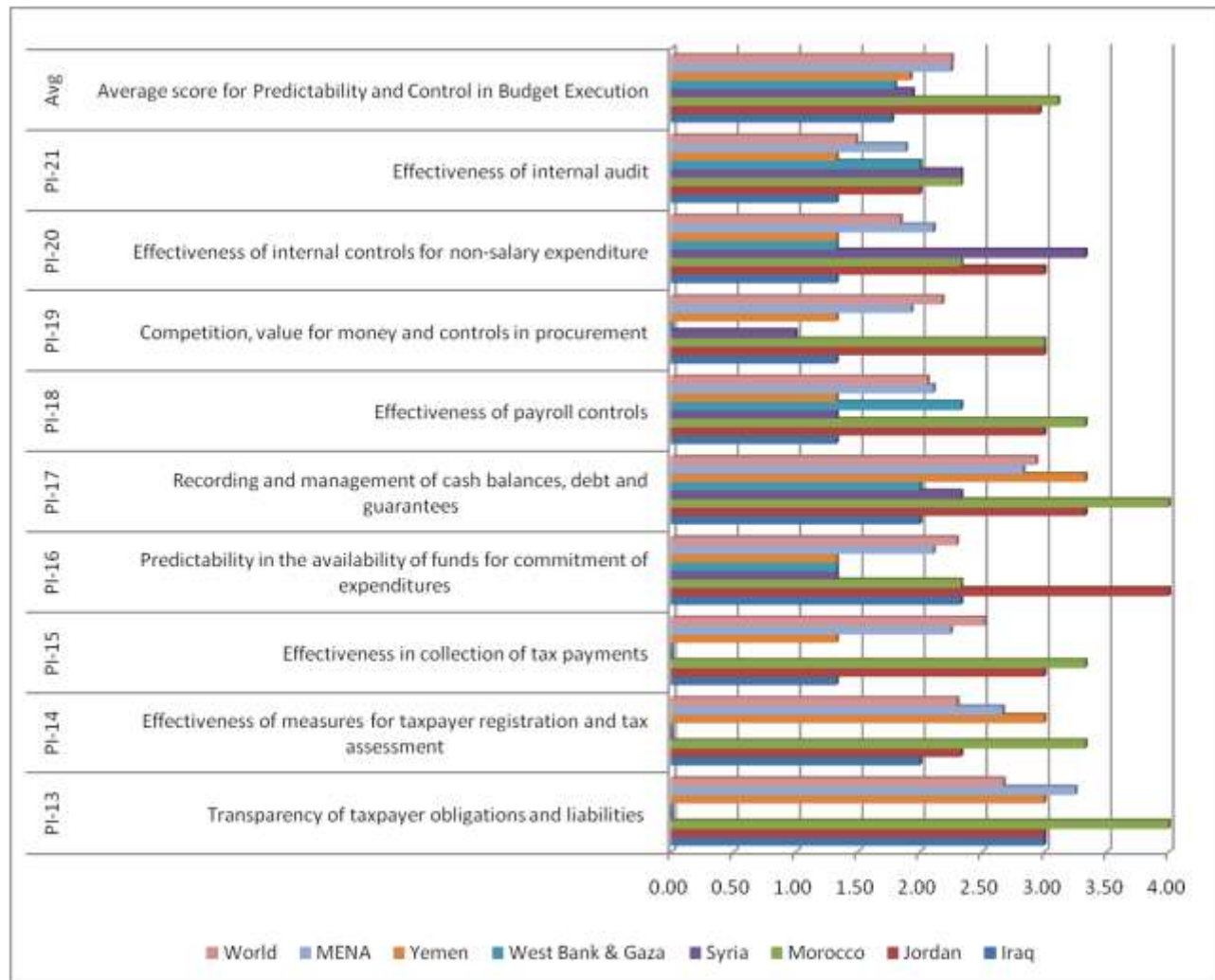
## Comprehensiveness and Transparency



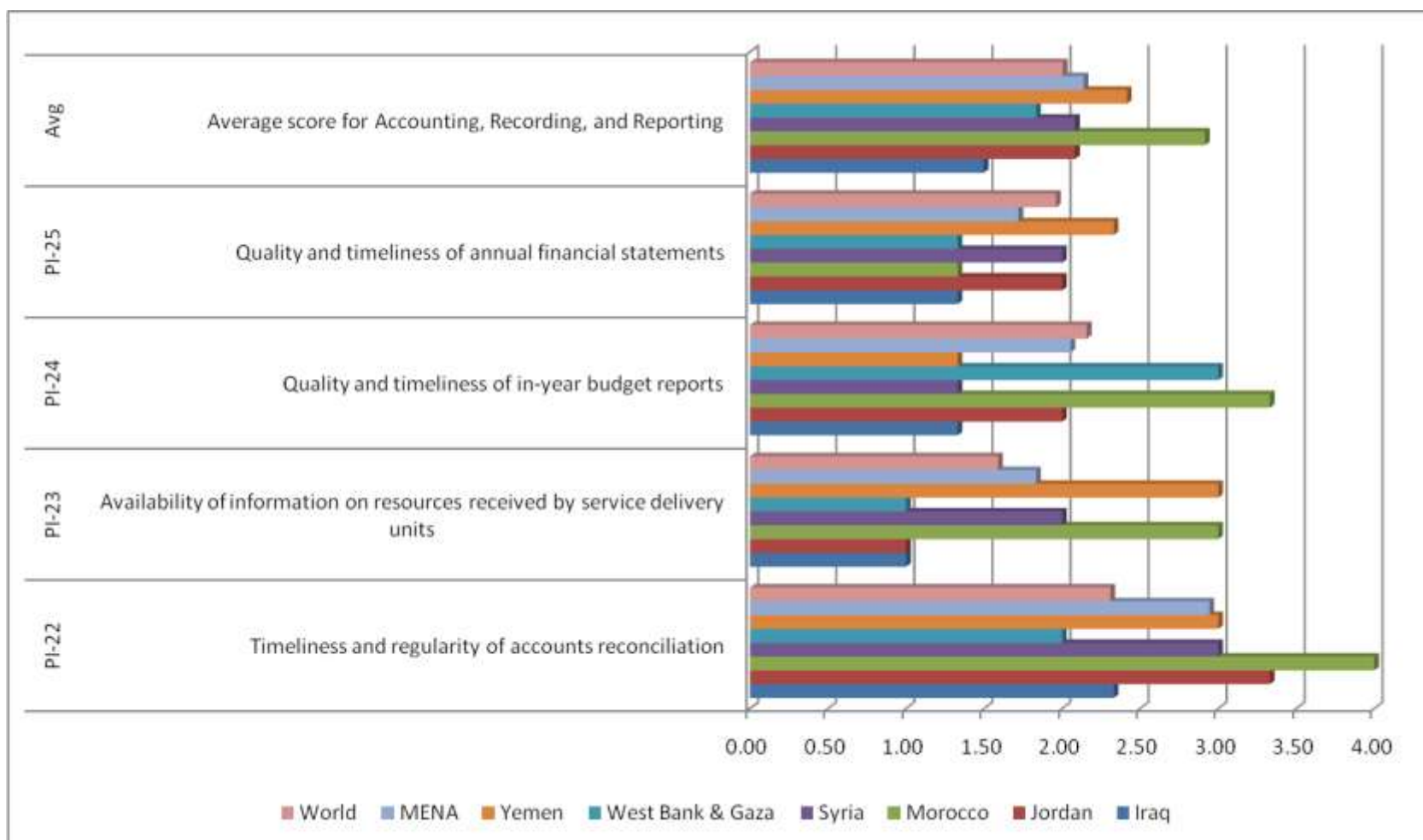
## Policy-Based Budgeting



## Predictability and Control in Budget Execution



## Accounting, Recording & Reporting



## External Scrutiny & Audit

