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# Committee of Experts on Public Administration



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## **Public financial management in times of emergency and implications for the credibility of budgets**

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## ***Question:***

*“What’s the similarity between true love and a pile of budget documents from low-income countries?”*

*Nicola Smithers, Public Financial Management Cluster Leader, the World Bank, 2014*

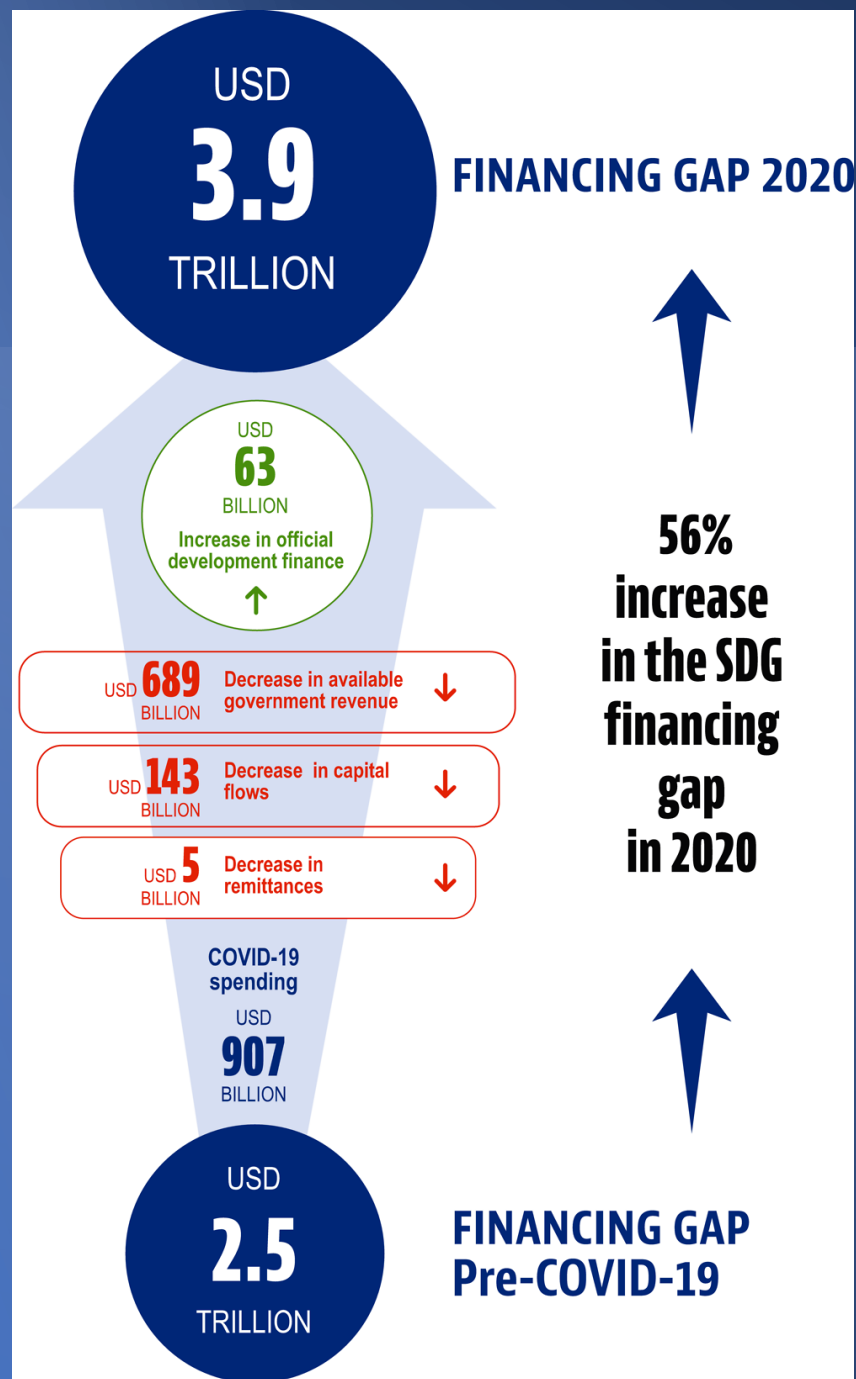
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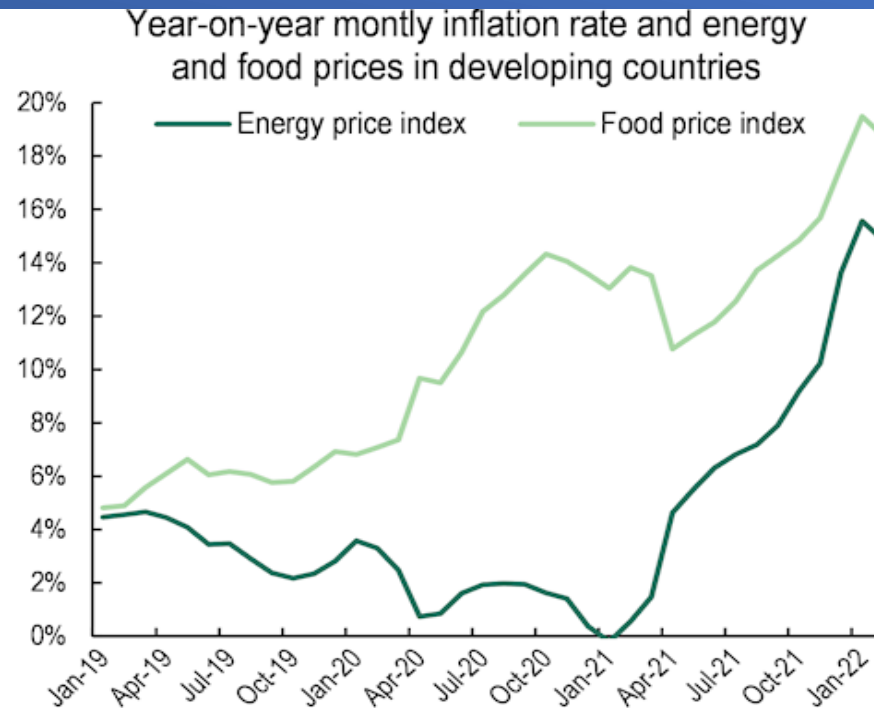
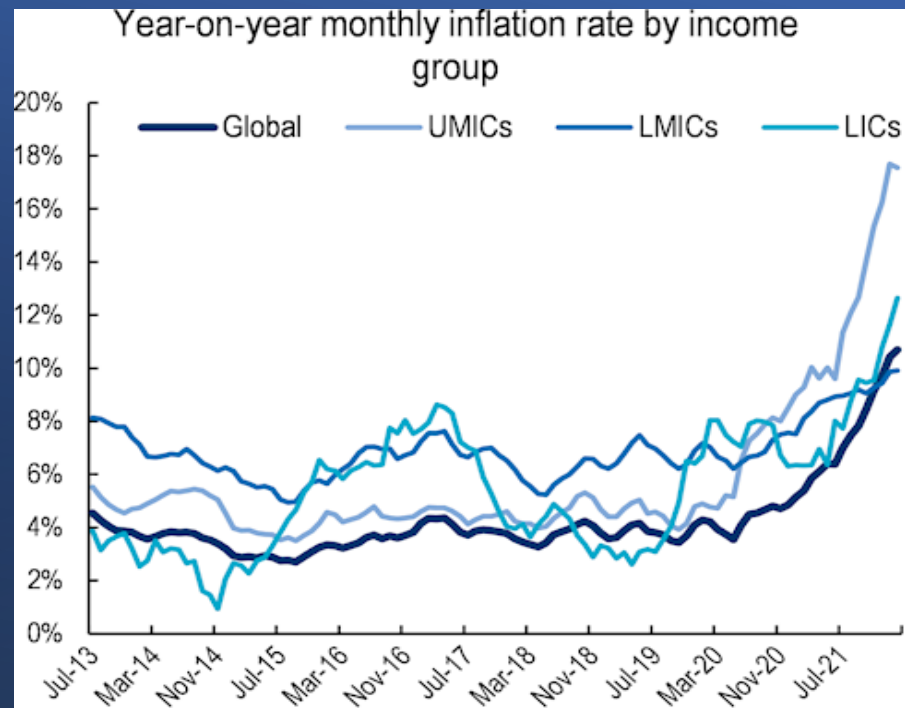


***The answer?***

*As anyone who has worked on public financial management or been in love will know, sometimes you have to suspend disbelief in order to reconcile reality with expectation.” –*

how can PFM mechanisms and instruments bridge the SDG financing gap in light of soaring interest rates and global uncertainty?

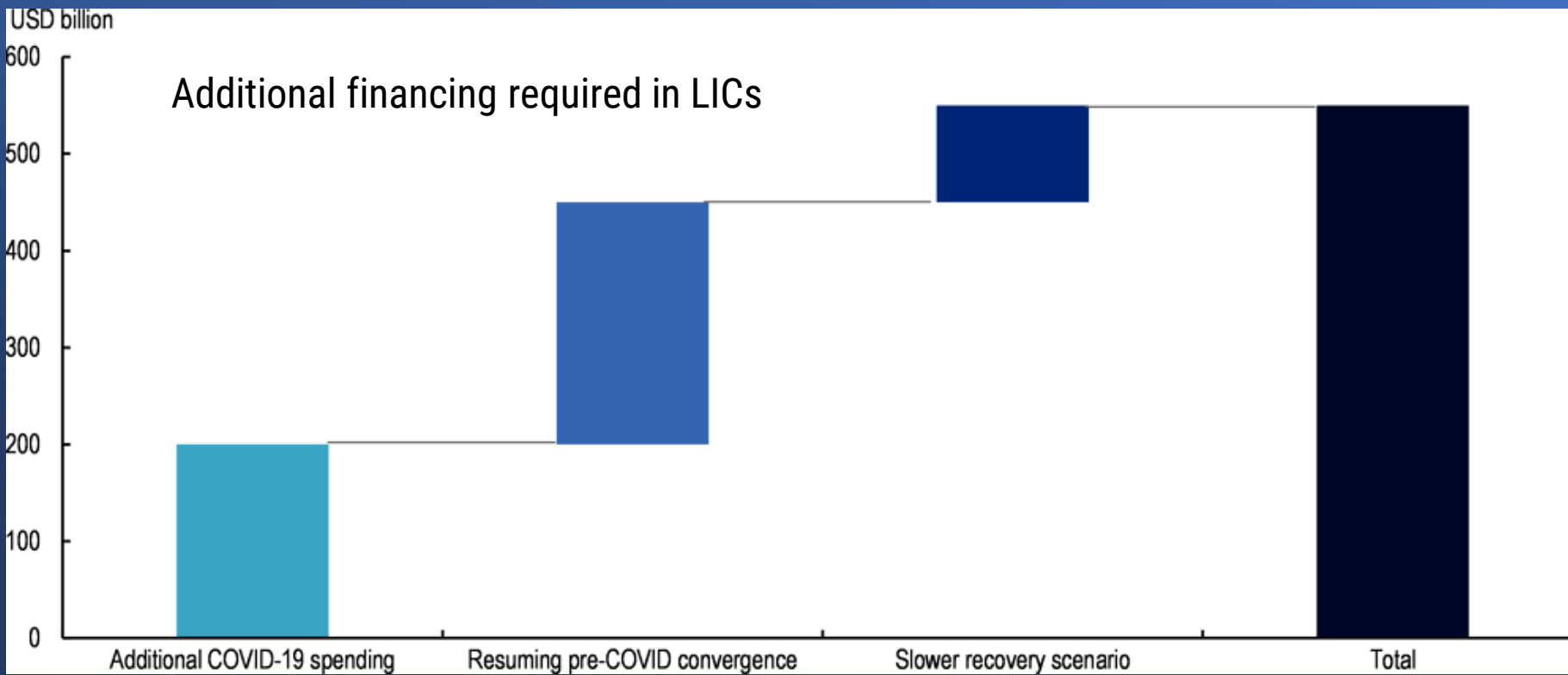




cash-strapped  
context

Source: Ha, Kose and Ohnsorge (2021[8]), "One-stop source: A global database of inflation", <https://openknowledge.worldbank.org/handle/10986/36037>.

- Increasing financial instability and inflation
- Widening economic disparities between developed and developing countries
- More than half of LICs (55%) are at high risk of debt distress or already in debt distress as of end of April 2022 (IMF, 2022)
- Following years of decline, global extreme poverty rose in 2020, setting back at least three years of progress from 8.3 in 2019 to 9.2 in 2020 .
- The UN Secretary-General Report 2021 notes that, unless urgent action is taken, ending poverty will be out of reach by 2030 due to the triple threat of "COVID-19, conflict and climate" (UN, 2021)
- The cost of financing for SDGs is increasing due to inflation



Source: IMF (2021[15]), *Macroeconomic Developments and Prospects in Low-Income Countries* – 2021, <https://www.imf.org/en/Publications/Policy-Papers/Issues/2021/03/30/Macroeconomic-Developments-and-Prospects-In-Low-Income-Countries-2021-50312>.

- The pandemic led to an increase of low-income countries' financing needs over the short and long term
- Difficult trade-offs to balance a growing number of SDG financing priorities.
- Need for clear prioritisation of short-term rescue spending and longer-term investments
- **Government revenues remain the largest source of financing for sustainable development and accounted for more than 80% of the overall decline in FSD.**

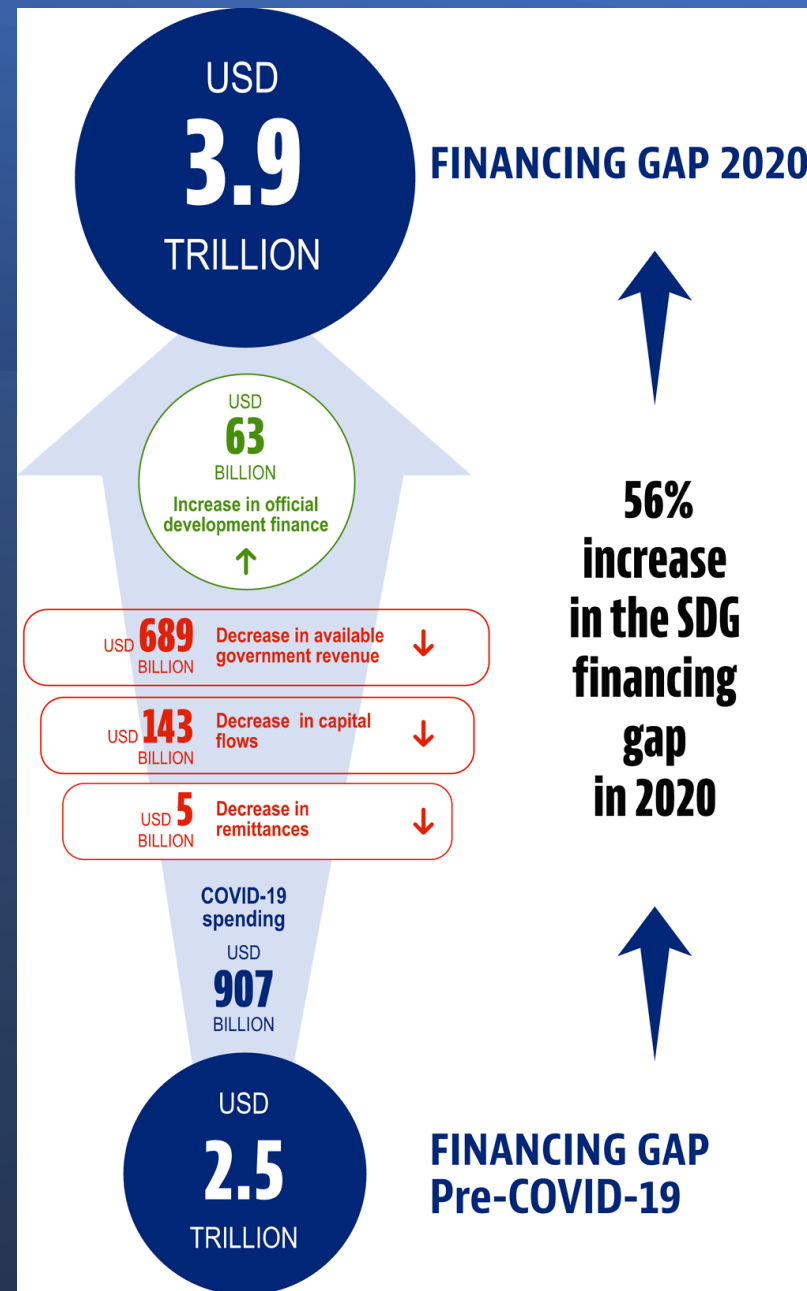
**SDG 16.6.1:** Primary government expenditures as a proportion of original approved budget, by sector (or by budget codes or similar)

This indicator considers

- (i) the variation between approved budget and final expenditure for the year for each major function (comparable to a sector)
- (ii) variation in expenditure from the original budget by economic classification and
- (iii) the average amount charged to the contingency reserve over the last 3 years.

From 2010 until 2021, **almost half of all countries** with available data on SDG 16.6.1/Performance Indicator PI-I of the PEFA Framework have **deviations** between planned and executed budgets above 5%.

The 2020-21 period has further steered countries away from budget credibility imperatives towards **a permanent state of exceptionalism.**



# Public financial management in times of emergency and implications for the credibility of budgets

## Annex: Budget credibility and the principles of effective governance

The table highlights the most important links, supported by concrete examples from different countries.

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Competence</b>	<ul style="list-style-type: none"><li>• An efficient public financial management system is central to the achievement of fiscal discipline and value for money. State capacities, particularly in relation to budget planning and auditing, are vital for mitigating related politically embedded biases. <b>Budget credibility is contingent on human capacities.</b></li><li>• Governments, particularly those of fragile States, do not always have the human resources or administrative structures in place to manage the budget cycle or ensure its credibility. <b>Those processes require various skills, such as management, financial accounting, medium-term and performance-based budgeting and auditing. Capacities are also required to manage credibility-enhancing software, such as integrated financial management information systems.</b></li><li>• The establishment of budget credibility-enhancing instruments requires <b>teams with diverse competencies.</b></li></ul>	<ul style="list-style-type: none"><li>• In Liberia, the roll-out of an integrated financial management information system has allowed the management of government transactions and budget formulation to be automated. The interface has integrated key components, such as appropriations, administrative expenditure and treasury management, while providing control through an embedded “do not exceed” instrument. <b>Nevertheless, a lack of competencies and resistance to change must be tackled to foster its use.</b></li></ul>



Governance principle	Relation to budget credibility	Examples
<p><b>Sound policymaking</b></p>	<ul style="list-style-type: none"> <li>• <b>The linking of budget planning to concrete outcomes brings together policymaking and budget credibility.</b></li> <li>• <b>Budget credibility is often the “gateway reform” in middle- and low-income countries</b>, as it allows revenue gaps and capacity to be estimated and expenditures to be linked to strategic allocations of resources.</li> <li>• Sound policymaking is a lever of budget credibility, particularly since the overall macroeconomic position of a government contributes directly to its overall credibility and trustworthiness. Macroeconomic goals are achieved when funds are disbursed in line with original commitments.</li> <li>• <b>Sound policymaking and budget credibility are thus mutually reinforcing.</b></li> <li>• <b>Information technology systems, such as integrated financial management information systems, can provide support for decision-making by providing visibility on revenues and spending trends, thereby rendering results-based budgeting possible.</b></li> <li>• Political will is crucial to achieve budget credibility.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Peru</b> deployed the second iteration of its integrated financial management information system, an electronic system enhancing the obtention of financial statements, in 2015. It has allowed the Government to operationalize <b>the principle of sound policymaking by integrating a results-based budget approach to expenditures. It is the only country in Latin America to run a single system for all levels of government (approximately 1,450 spending units).</b></li> <li>• Budget credibility checks have also acted as levers for sound policymaking in Argentina, allowing policymakers to better account for inflation. <b>The country’s E-SIDIF online integrated financial information system allows outcomes identified in the budget to be linked to strategic goals, greatly enhancing the country’s ability to estimate needs in the light of embedded risks. From 2016 to 2018, the deviation rate between aggregate expenditure out-turn and the approved amount dropped from 136 per cent to 115 per cent, while allowing government officials to account for inflation in spending by increasing the approved amount.</b></li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Collaboration</b>	<ul style="list-style-type: none"> <li>Multi-stakeholder collaboration sometimes constitute a bottleneck, budget credibility can reinforce communication between institutions and stakeholders, thereby enhancing policy coherence.</li> <li><b>Increased collaboration between institutions allows budget-planning authorities to access larger quantities of institutional data, thus contributing to greater budget credibility.</b> Collaboration is key, not only at the intergovernmental level, but also within line ministries and, in particular, within ministries of finance.</li> <li><b>Collaboration and budget credibility become mutually reinforcing in the long term.</b></li> </ul>	<ul style="list-style-type: none"> <li>Inter-institutional collaboration and better planning allowed <b>the Dominican Republic to increase its score from the lowest to the highest in the budget credibility assessment of the Public Expenditure and Financial Accountability programme in 2018.</b> Greater collaboration enabled the integration of a large number of institutional data sets and the production of three budget execution reports.</li> <li><b>The United Republic of Tanzania and Kenya have both included ministry- and sector-related reviews of public expenditure in the budget process.</b> Nine sector-specific working groups review the components of the expenditure proposals of ministries and benchmark them against priorities. In addition, open sector hearings are organized in Kenya, at which stakeholders have a chance to comment on sector policies and allocations.</li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Integrity</b>	<ul style="list-style-type: none"> <li>• <b>Integrity means that public funds are spent according to plan and in the interest of citizens.</b> Moreover, the achievement of <b>fiscal outcomes improves State legitimacy</b> by reducing both real and perceived corruption.</li> <li>• <b>At the same time, budget credibility excludes the possibility of practices such as unrealistic or hidden budgeting.</b></li> <li>• Integrity allows deviations to be accounted for and safeguards against the establishment of spending “black boxes”, such as special purpose funds, to be established.</li> <li>• While aggregate budget credibility, as determined by the Public Expenditure and Financial Accountability programme, tends to become less important in fragile States, <b>evidence suggests that a positive and statistically significant relationship persists in such States with regard to compositional budget credibility and on the basis of the World Bank’s definition of fragility.</b></li> </ul>	<ul style="list-style-type: none"> <li>• The Philippines embarked on an ambitious budget reform to improve the integrity of its budgetary process, which had been exposed to abuses, particularly given the existence of special purpose funds, special accounts in the general fund and off-budget accounts, as well as weak oversight. During the period 2010–2016, the Government curtailed the use of these mechanisms, unified reporting requirements and ended budget re-enactments.</li> <li>• Prior to the war, the Government of Ukraine, following the “integrity revolution”, had implemented a new public procurement law to reduce abuses that were undermining public bidding processes. <b>The objective was to improve budget credibility by directing funds where they were most needed.</b> The e-procurement system “Prozoro” became a best practice example in the field.</li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Transparency</b>	<ul style="list-style-type: none"> <li>• Transparent budgetary systems correlate with greater credibility and fiscal discipline.</li> <li>• <b>Fiscal transparency and reporting are critical for budget credibility</b>, one reason being that punctual reporting allows real-time management of public resources.</li> <li>• Software that permits improvements in budget credibility also provides fiscal transparency through open, clear, valid and reliable data that can be published and made accessible to a large number of stakeholders.</li> </ul>	<ul style="list-style-type: none"> <li>• Jordan sought to improve its budget credibility and overall pfm through an enhancement of fiscal transparency. Since then, fiscal reports have become more comprehensive, forward-looking and connected to five-year medium-term budget frameworks, while a programme classification system has been introduced. This has contributed to more effective fiscal forecasts.</li> <li>• Liberia and the United Republic of Tanzania were able to increase budget credibility by dividing their budgets into line-itemized core and contingent sections, and then disbursing contingencies when revenues that exceeded core budget requirements became available.</li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Independent oversight</b>	<ul style="list-style-type: none"> <li>• Budget credibility greatly enhances the credibility and accuracy of public accounts, particularly in relation to the budget cycle, both committed and enacted, as it allows the evaluation and validation of revenues and expenditures and the inspection and justification of deviations.</li> <li>• Recurrent audits of State budgets foster improvements <b>in public financial management and budget credibility more broadly and can emphasize the role of supreme audit institutions for society.</b></li> <li>• The participation of civil society organizations and non-governmental organizations adds an additional layer of credibility to such assessments.</li> <li>• Independent oversight strategies improve budget credibility through the involvement of external stakeholders and the population at large.</li> </ul>	<ul style="list-style-type: none"> <li>• In Serbia, Transparency Serbia, a non-profit organization and member of the International Budget Partnership, examined ad hoc <b>transfers of contingency funds from the national budget</b>; those funds were suspected of being used for political patronage. The issue gathered media attention and public engagement sufficient for the Fiscal Council to commit to examining the issue. <b>Independent oversight therefore generated momentum towards greater budget credibility.</b></li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Leaving no one behind</b>	<ul style="list-style-type: none"> <li>National development objectives and service delivery are correlated with the achievement of parity between commitments and actual revenues collected and spent. This is particularly relevant when addressing the socioeconomic needs of the poor and other vulnerable and marginalized groups.</li> <li>A lack of budget credibility has a human cost, as <b>deviations in expenditure imply reduced or inconsistent spending on policy areas that need it the most</b>. In relation to the Sustainable Development Goals, underspending can have tragic consequences for livelihoods.</li> <li>The principle of leaving no one behind is particularly relevant in fragile and conflict-affected countries, where <b>improvements in budget credibility can contribute to more coherent public financial management practices, which in turn reduce the risk of conflict relapse, consequently shielding the most vulnerable</b>.</li> </ul>	<ul style="list-style-type: none"> <li>Uganda protects certain segments of the budget from in-year cuts, ensuring that those segments are subject to greater oversight and monitoring than the rest of the budget. This has shifted budget allocations towards social services, improved the predictability and monitoring of spending in these areas and strengthened donor-government relations.</li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Non-discrimination</b>	<ul style="list-style-type: none"> <li>• <b>The application of the principle of non-discrimination in budget preparation prevents the exclusion of specific groups</b> and ensures the equal treatment of all groups regardless of race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth, disability or other aspect. Moreover, non-discrimination strategies can lead to the identification of previously invisible needs of marginalized groups.</li> <li>• <b>Using the principle of non-discrimination to examine spending versus commitment also allows the re-examination of the core assumptions on which spending is based.</b> This could facilitate the integration of gender equity objectives. <b>Focusing on impact rather than on spending trends can also lead to greater data disaggregation.</b></li> <li>• <b>Non-discrimination can reinforce budget credibility and vice versa, provided that the following measures are applied: public debate,</b> cooperation with legislative bodies and the judiciary, the involvement of those directly affected or discriminated against and the harnessing of new technologies. In that regard, the role</li> </ul>	<ul style="list-style-type: none"> <li>• In Colombia, the public advocacy organization Dejusticia has engaged the Constitutional Court in order to prioritize health coverage for vulnerable groups, including the poor and refugees, and to cover their needs through the emergency fund established in response to the COVID-19 pandemic. This reinforces the crucial role that civil society and non-governmental organizations play in preventing discrimination and fostering inclusion.</li> <li>• In Senegal, the Federation of Associations of Persons with Disabilities has successfully fought for the social inclusion of persons with disabilities, including access to basic services and COVID-19-related relief.</li> <li>• In India, where the Dalit community continues to face marginalization, the National Campaign on Dalit Human Rights has developed an application to monitor the roll-out of emergency expenditures, in order to measure their impact at the community level. This has paved the way for the outlining of key recommendations to the authorities on adequate budgetary measures to best address the</li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Participation</b>	<ul style="list-style-type: none"> <li>• Legislative consultation and public participation are required, in particular when introducing major budget amendments, in order to avoid weakening budget credibility.</li> <li>• Governance reforms, including the enhancement of budgetary credibility, are dependent on an implicit exchange that entails the provision of benefits to stakeholders in exchange for support.</li> <li>• Consequently, public involvement is a key lever for budget credibility. Public involvement can also improve the meaningfulness of data collected and reported.</li> </ul>	<ul style="list-style-type: none"> <li>• The Ministry of Finance of Malaysia has established a reporting unit through which feedback is gathered from the public on fiscal measures that comprise, in emergency cases, deviations from foreseen spending plans.</li> </ul>



<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Subsidiarity</b>	<ul style="list-style-type: none"> <li>• The principle of subsidiarity allows the operationalization of budget credibility through <b>strategies that achieve a balance between subnational autonomy and stable relations with the central or federal Government.</b></li> <li>• <b>Financial management systems that can integrate all levels of government can promote budget credibility by ensuring that transfers to the subnational government level are visible, efficient and correspond to the needs of constituencies.</b></li> <li>• Similarly, <b>effective fiscal consolidation at the subnational government level requires a high degree of accuracy in forecasting tax revenues and in estimating public expenditures.</b> Therefore, subsidiarity and budget credibility are mutually reinforcing.</li> </ul>	<ul style="list-style-type: none"> <li>• The roll-out of budget credibility-enhancing systems, such as integrated financial management information systems, can lead to the buy-in of many users and improves subsidiarity. Such systems can have more than 4,000 users. In some cases, as in Brazil, they can have more than 100,000 users, thereby providing more effective geographical and institutional coverage to estimate the needs of regions and municipalities.</li> <li>• <b>South Africa publishes a media statement on budget credibility at the local level, including analyses of over- or underspending trends, conditional grants and recommendations, on a periodic basis.</b> This practice fosters transparency, collaboration and positive relations between central and local government.</li> </ul>

<i>Governance principle</i>	<i>Relation to budget credibility</i>	<i>Examples</i>
<b>Intergenerational equity</b>	<ul style="list-style-type: none"> <li>• The application of the principle of intergenerational equity imposes on the entire budget cycle several considerations related to budget credibility and the indicators used to measure it, <b>including the centrality of generational buy-in, whereby each generation derives benefits in accordance with its contribution.</b></li> <li>• Intergenerational equity is based on the assumption that <b>the benefits derived by the current generation from expenditures must not destabilize the fiscal position of future generations.</b> Subsidies to reduce the price of goods in the short term, for example, distort a country's long-term fiscal and monetary position, thereby hampering intergenerational equity.</li> <li>• •The application of intergenerational equity within the budget cycle <b>improves budget credibility by increasing fiscal discipline and by equating spending</b> trends that hamper future fiscal positions with long-term deviations.</li> <li>• <b>intergenerational equity is based on a delicate balance between debt financing and debt amortization, which in turn requires expenditure decomposition to be enacted in terms of current, tax financed expenditure and capital, debt financed expenditure.</b> This distinction can often be difficult to ascertain, particularly in relation to assets.</li> </ul>	<ul style="list-style-type: none"> <li>• Tunisia achieved substantial improvements in its fiscal position by reforming its subsidies and reducing them from 2.8 per cent of gross domestic product in 1990 to 1 per cent in 1999. <b>Such reforms increased budget credibility by reducing embedded risks to fiscal and monetary positions in the long term.</b></li> </ul>