Addressing the COVID-19 Crisis: Lessons from Support for Public Financial Management

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NOTE

In this report, “$” refers to United States dollars.

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IED retains full responsibility for this report.
I. INTRODUCTION

1. The coronavirus (COVID-19) disease pandemic that hit the world in early 2020 has led to a sharp increase in fiscal pressures and demonstrated the importance of public financial management (PFM) as a part of managing the fiscal response. Lockdowns and other measures taken by governments to contain the disease have disrupted economic activity. Economic recovery is expected to be slow until the health crisis comes to an end and most international agencies have lowered their growth estimates. The Asian Development Bank (ADB) revised its growth rate forecast for developing Asia in 2020 to –0.4%.1 The International Monetary Fund (IMF) revised its global growth rate estimate for 2020 from –3.0% to –4.9%.2 Government budgets have come under severe strain due to rising expenditures on public health infrastructure and services and lower tax and other revenue collections as a result of shrinking economies resulting from lockdowns. Countries are taking measures to combat the pandemic’s supply- and demand-side impacts, local and global fallout, and lengthy uncertainty. Fiscal pressures have grown as governments struggle to meet immediate needs: public health and safety requirements, supply-side support for businesses suffering revenue losses, and demand-side income support to individuals who have lost work. Additional medium-term support will be needed to deal with business bankruptcies and to stimulate economic recovery. Both direct and indirect tax revenues have reduced due to subdued economic activity, falls in commodity prices, and tax moratoriums.3 In such circumstances, sound management of public financial resources is critical. This is true for countries that have the fiscal space to expand spending from immediately available resources, as well as for those that need to expand their debt financing due to fiscal constraints.4 How public budgets are allocated and managed is as important as the overall funding dedicated to the COVID-19 pandemic response.5

2. Fiscal strains during the crisis have often revealed underlying structural vulnerabilities, including those in the PFM architecture, that need to be addressed not only for the immediate crisis response but also for sustained, long-term recovery.6 Preparedness is key to how countries weather crises.7 Thus, PFM reforms in the context of the COVID-19 crisis must encompass both short-term measures and longer-term structural reforms. Crisis support will be much more successful when it is nested in a framework that incorporates post-crisis recovery and includes a focus on fiscal and public expenditure reforms.8 During shocks such as the COVID-19 pandemic, countries with strong public financial management systems in place have been more effective in targeting resources, re-orienting expenditures and ensuring greater accountability in the use of resources. This is why continued multilateral development bank (MDB) support for strengthening country systems remains important.

3. PFM reform support through MDBs, whether for short-term crisis response or longer-term institutional support, has largely been through policy-based lending (PBL) which takes the form of budget support that uses countries’ own PFM systems. MDBs have emphasized the need to strengthen PFM systems in recipient countries for fiduciary purposes and lending effectiveness.

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Diagnostic assessments and monitoring of public finance management systems have been common, often through joint donor initiatives such as public expenditure and financial accountability assessments and public expenditure reviews. ADB mandates the use of governance and fiduciary risk assessments for its PBL operations. Similarly, the World Bank policy prescribes risk identification and mitigation in its development policy financing. These are in addition to the imperative of incorporating PFM reforms into current COVID-19 operations and post-pandemic response operations. PFM reform programs are often multi-year and multi-component programs aimed at medium- and long-term structural reforms, but a start can be made with immediate reform initiatives during COVID-19 crisis. The Inter-American Development Bank, for example, has produced a prototype project to address fiscal issues during the crisis, structured as a series of two operations from short-term support to longer-term recovery and resilience (footnote 6).

4. **Developing economies can take guidance from past lessons as they start their post-pandemic economic recovery.** Since most of the crisis spending in these economies is financed through government borrowing, debt sustainability considerations will rise in importance as the focus starts shifting to post-crisis recovery. The economies will likely face tight fiscal conditions due to their large fiscal deficits and high levels of public debt, requiring measures to strengthen domestic resource mobilization and improve spending efficiency. They will need to strengthen their tax systems, improve tax compliance and reform their PFM systems to allow for better budget planning, execution, and control. Measures taken by governments should be guided by lessons from past PFM interventions, especially in developing countries, many of them undertaken with financial support from MDBs.

5. **This paper provides a synthesis of lessons from evaluations of PFM support by ADB, other MDBs, and the IMF, as well as lessons from research and analysis by other international organizations such as the World Health Organization (WHO).** It draws upon experience from past crises, and from previous budget support operations targeted at medium-term PFM reforms, emphasizing the lessons they offer. Despite the unique features of the present crisis, experiences from the past can still be helpful, whether in catering to immediate spending needs or in longer-term budget management. Post-crisis PFM interventions can benefit from the global and historical experience with PFM reforms; hence this paper summarizes lessons from these experiences. The lessons draw upon large-scale evaluations, validated program completion reports, and technical assistance (TA) completion reports of ADB’s PFM-related operations that have been approved over the past decade as well as the findings and lessons of evaluations of other MDB operations and research publications from centers of excellence.

6. **The paper covers lessons on PFM interventions in the crisis and post-crisis contexts, as well as general lessons in program design and implementation of such interventions.** A distinction is made between lessons relevant to the support provided during a crisis (section II) and in the post-crisis recovery period (section III). Short-term budgetary measures in the context of the COVID-19 response are those aimed at meeting immediate expenditure needs, either by making use of existing budget flexibilities and emergency provisions, or by special temporary decrees. These are followed by the enactment of revised and re-prioritized budgets, reflecting increased public sector health spending, business support, and income support. Longer-term PFM reforms cover a broader spectrum and include debt management, domestic resource mobilization, and budget formulation, execution, and reporting. The final section covers general lessons on PFM interventions including those relating to the design and implementation of policy-based financing and TA, which are the main instruments for delivering support for fiscal policy and PFM reforms.

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II. LESSONS FOR PUBLIC FINANCIAL MANAGEMENT SUPPORT DURING A CRISIS

7. Providing immediate funds to frontline services is critical to address a crisis using budgetary frameworks that are already in place for crisis spending. In addition, resources can be marshalled from supplementary reserves, contingency appropriations, or budget reallocations and reprioritizations. In Indonesia for example, the local governments have disaster budgets to fund pre- and post-disaster activities, although the available budget does not fully meet disaster management needs requiring budget reallocations when disasters occur. A similar situation is found in the Philippines, which is prone to several hazards such as typhoons, storm surges and earthquakes and where the calamity fund is not sufficient to deal with the COVID-19 crisis, a national emergency is being declared by the President for easier access to financial resources and reallocation of appropriations of some budget items to respond to the crisis. In the People's Republic of China (PRC), the 2018 budget law allowed for budget reallocations and the activation of contingency funds and reserves.

8. Enacting temporary decrees or orders by executive authorities or government agencies is a very useful way of ensuring continued funding in countries where existing budget flexibilities are limited. In countries without budget provisions for crisis spending, temporary measures can be taken by ministries of finance or health. Heads of state or finance ministers in several European countries (including France, Germany, and Italy) have used decrees to free-up budgetary resources for service providers. Indonesia's finance minister has reallocated funds from non-urgent spending for COVID-19 relief.

9. Reprioritizing expenditures is crucial for countries to manage crisis support. Such reprioritization will currently be needed not only for the health sector but also for business support, as COVID-19 restrictions force temporary or permanent closures. From a public finance perspective, the extent to which a country can undertake expansionary fiscal measures for its COVID-19 response, as opposed to reprioritization, will depend on the country. In many countries, budget reallocations have enabled rapid reprogramming of expenditures to well-defined and flexible budgetary programs in the health sector. It is preferable if new funds for income support are found by identifying cuts to low priority spending rather than across-the-board cuts. In France, Germany, Japan, the Republic of Korea, the United Kingdom, and the United States, legislatures enacted spending plans to respond to the crisis. In the same way, during the 2008–2009 global financial crisis, several countries had to reprioritize expenditures for a measured stimulus and to provide support to the most affected. MDBs can help provide budget support assistance for temporary spending needs as well as with the reprioritization of expenditures.

10. Providing budget support is more effective in the short term than lines of credit through the banking system. ADB’s support to developing member countries’ response to financial crises showed that financial intermediation loans to enterprises facing liquidity problems in meeting working capital needs did not always prove useful. This was because intermediation capacity of participating institutions tends to decline during a financial crisis due to increasing levels of nonperforming loans. Also, credit discipline might be impacted by government interventions as in the case of Thailand where the government introduced a 3-year moratorium on debt repayments by rural enterprises to reduce their distress. World Bank’s support addressing the impact of past crises on business and enterprises shows that much of the financial support to small and medium enterprises, and other businesses affected by the global financial crisis in 2008 through financial intermediary loans failed to reach the worst affected

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by the crisis due to targeting difficulties and disbursements were not timely. The United States experience showed that the $3 trillion in loans and asset purchases offered by the Federal Reserve did not fully help the worst affected small businesses due to targeting issues.

11. Creating new and separate funds or entities to channel resources for managing crises can increase financial fragmentation. A study of about 40 lower middle-income countries found that using external resources, including private donations, raised concerns about transparency and accountability. A rapid review of the legislative provisions related to reporting mechanisms for these funds suggests that there is no guarantee of transparency, due to the lack of integration of funding. Health sectors are often characterized by multiple funding flows. In some countries where new special funds were created in response to the COVID-19 crisis, this has added to existing problems of lack of transparency and fragmentation of oversight, including at the subnational level. Research by the World Bank and WHO suggests that there is a need to explore new ways to integrate external funds incrementally into national PFM processes and accounts (footnote 16).

12. Promoting efficiency and preventing fraud require ex ante or ex post controls on frontline spending, together with appropriate tracking systems. Many countries have already adopted integrated financial management information system (IFMIS). If an IFMIS is in place with genuine government ownership, budget expenditure lines should be updated to allow consolidated reporting of COVID-19 expenditures. Program envelopes can facilitate expenditure tracking and secure accountability in resource use if all expenditures for the pandemic are reported under the same program code. Where multiple actors are involved, one ministry typically takes the lead, usually the finance ministry, as in the PRC, France, and Germany (footnote 12). However, experience with integrated COVID-19 accounts in countries without a robust financial management information system (FMIS) has been mixed; countries with an existing IFMIS seem to have done better. Adjustments to the financial management information systems in Italy, Malawi, and Timor-Leste seem to have been an effective approach to securing simple, integrated expenditure reporting for COVID-19 (footnote 16). The Republic of Korea’s effective COVID-19 response made use of its Public Finance Information Service, which runs the dBrain system (a platform used by the government for PFM to ensure operational continuity across government and to release and reprioritize funds without any disruption or delay). It is also important to ensure that countries operate under a treasury single account to consolidate and optimize the use of government cash resources, which may otherwise be sitting idle in multiple government bank accounts.

13. When country systems are weak, technical assistance can improve the monitoring of crisis response programs. The focus of the TA should be on expenditure tracking mechanisms, internal controls, and external audits. Initially, external experts can be used to monitor program-supported expenditures, with government staff taking over at a later stage when country systems start to improve. Institutional strengthening and the independence of the oversight and regulatory bodies, including external audits, are crucial for the effective and independent monitoring and enforcement of laws and regulations. ADB uses country systems for its PBL operations, so it is important that, from a fiduciary perspective, it is sufficiently comfortable with the strength of these systems. TA has an important bearing

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19 This was one of the most common comments IED made in more than 52 COVID-related reports and recommendations of the President it reviewed in 2020.
on the success of a PBL program as found in ADB’s independent evaluation on ADB’s PBL support. The evaluation found that TA can provide an important incentive for line ministries to undertake reforms and in some cases failure to provide TA undermined the achievement of desired outputs.

14. **Infusing liquidity into the system is an effective fiscal expansionary approach during a crisis and capital-intensive investment projects with long startup periods are better left to the recovery phase.** An effective countercyclical fiscal policy ensures public spending is of good quality, timely, and consistent with macroeconomic stability. Supporting labor-intensive investments, improving the maintenance of existing infrastructure, and scaling up social protection expenditure are more appropriate for crisis response. Short-term countercyclical public expenditures need to be of a high quality to be compatible with medium-term fiscal sustainability. The preservation of existing infrastructure assets through operation and maintenance and the completion of ongoing projects can have higher short-term crisis response returns than new investments with long gestation periods. The Inter-American Development Bank (IADB) has pointed to cases where increased public sector outlays for hydrocarbon companies were a part of COVID-19 fiscal responses in Latin American countries. These included injections of new resources and fiscal relief.

15. **Having a clear exit strategy from countercyclical expansion is crucial to avoid solvency problems.** Crisis response fiscal programs need to account for fiscal and debt sustainability risks (footnote 22). For countries that need fiscal consolidation, the impact on essential social programs and on investment programs needs to be carefully considered. By and large, fiscal stimulus programs need to be timely, targeted, and temporary. This is easier when countries have ongoing social protection programs such as cash transfers and systems for good poverty mapping and identification of vulnerable populations.

16. **Countries may have an opportunity to introduce a longer-term fiscal and public financial management approach including reforms during a crisis, aimed at domestic resource mobilization.** For many countries with low tax rates relative to their level of economic development and a long history of failed tax reforms, the dire fiscal situation that resulted from the global economic crisis provided incentives for governments to make politically sensitive tax reforms to boost their revenues in the medium to long term (e.g., in Costa Rica and the Dominican Republic). The evaluation of the World Bank crisis response operations undertaken by Independent Evaluation Group (IEG) showed that crisis response development policy operations (DPOs) typically supported a broad array of PFM reforms in order to help countries to attain stronger fiscal outcomes in future. However, such reforms required focused action over a long time frame to attain the expected results, and stand-alone crisis response DPOs were not designed to follow up on this reform agenda. Another IEG evaluation of the fiscal response to the global food crisis of 2007–2008 also confirmed that, after first protecting key public expenditures, the focus included building resilience for long-term structural reforms to strengthen fiscal sustainability.

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III. LESSONS FOR PUBLIC FINANCIAL MANAGEMENT SUPPORT AFTER A CRISIS

A. Debt Management

17. Increasing public spending, especially in fiscally constrained countries, could have implications for long-term debt sustainability. This may be particularly true in the present crisis compared with past global crises. Since 2013, the median government debt in low-income countries has risen by 20% of gross domestic product (GDP) and this debt is increasingly from non-concessional and private sources (footnote 7). If contingent liabilities are considered, the real debt burden may be even higher.27 Shadow banking systems, often operating through state-owned enterprises (SOEs), can mobilize revenues and increase general government debt. Formerly heavily indebted poor countries are increasingly experiencing debt distress as they have returned to commercial and short-term borrowing, often in foreign currency. Solutions to debt problems have taken the form of the adoption of fiscal rules, expressed as numerical limits on budgetary aggregates such as government debt, that act as permanent constraints on fiscal policy to promote fiscal responsibility.28 Where fiscal rules have been relaxed due to the COVID-19 crisis, steps will be needed to restore fiscal discipline.29 In Uganda, for example, a fiscal deficit rule has been postponed due to the COVID-19 crisis, although the risks to Uganda’s fiscal stability and credibility are increasing because of the costs of political corruption, declining social norms, and the creation of more political positions within the government. Elsewhere, reducing the debt of SOEs is an important aspect of debt management strategies. For example, a mechanism to reduce the debts of the Solomon Islands Water Authority to the Solomon Islands Electricity Authority and the submission of statements of corporate objectives by all SOEs has enhanced their efficiency and governance.30

18. Operationalizing a cabinet-approved debt risk management and mitigation policy and strategy can help strengthen reporting on debt. In the case of Tonga, the policy included processes and responsibilities for the analysis and approval of proposed new guarantees and debt, processes for prioritizing and scheduling debt repayments, and a schedule of timely and standardized reporting on the government’s debt portfolio.31 Data on debt were regularly reported and publicly released on the government website.

19. Safeguarding fiscal position against future repayment concerns entails improved public sector debt management.32 This is possible by enforcing fiscal restraint to strengthen budget process and adopting debt management guidelines and debt management strategy. Fiscal rules, by enforcing targets on key indicators such as public debt and fiscal deficit, can hold governments accountable to maintain spending in line with revenue mobilization capacity and keep the public debt at sustainable levels. These rules can be enforced either by legislating ceilings for these indicators or by setting up an independent fiscal institution to monitor the government’s compliance with fiscal rules.33 Countries vulnerable to shocks from changes in commodity prices and natural disasters must work towards building fiscal buffers to enhance resilience to shocks and achieve debt sustainability. Greater transparency of investment funds can help strengthen sustainability of the fiscal buffer. The Tuvalu government endorsed changes to the financial instructions under the Public Finance Act for greater transparency of the Consolidated Investment Fund contributions and savings plan.34

20. Managing the risks to medium-term fiscal sustainability involves timely adoption of policy measures to address them. The risks faced by different countries can be varied, such as, high food and energy subsidies (Indonesia, India, Malaysia, and the Philippines), rising pension and healthcare spending due to aging population (the Asian newly industrialized economies, the PRC and Thailand), need for greater infrastructure spending (India, Indonesia, and the Philippines), and large contingent liabilities, which could translate into large increases in government debt in the future (the PRC). Correspondingly, the policy measures addressing these risks are replacing subsidies with targeted income transfers, enforcing premium payments to reduce costs of pension and healthcare programs, encouraging private sector funding, including public-private partnerships, for infrastructure investment, and transparently managing contingent liabilities.

B. Revenue Management

21. Devising a comprehensive strategy that links tax policy reforms to revenue administration reforms can lead to large and sustained revenue gains. What and whom to tax will go hand in hand with how the taxes will be collected. Combining several tax instruments (e.g., increasing the value-added tax rate and reducing the personal income tax rate or reducing value-added tax rates while broadening the tax base by lowering exemptions) is becoming common. Increases in indirect taxation rates and broadening the tax base for both direct and indirect taxation are the most frequently observed tax policy instruments. Rate increases in excise duties and goods and services taxes were the most common instruments, followed by the elimination of exemptions and tax holidays. Property taxes have played a limited role in both low-income countries and emerging markets as countries have sought to mobilize revenues, probably because of legal loopholes (for instance, the absence of a cadaster to define property rights) and weak tax administration capacity, especially at the local level.

22. Strengthening compliance with tax laws requires a long-term commitment that balances enforcement and the encouragement of voluntary compliance. To improve compliance, countries need to shift longer-term behavior toward compliance and not just to correct incidences of noncompliance. Decisions on investigation, prosecution, and comprehensive audits should be based on the seriousness of the behavior and the amount of revenue at risk. Treatments should be proportionate to build community confidence in the fairness of the tax system and trust in the tax administration. A systematic approach requires countries to identify major compliance risks as accurately as possible and to allocate their limited resources most effectively in pursuit of revenue and fairness objectives. Compliance risk management tends to be weak in many tax systems in Asia. Since a tax policy is only as good as the underlying tax administration that collects the revenue, improving fundamental revenue administration operations (taxpayer education, information management, auditing and debt collection), as well as ensuring stable and empowered revenue administration management is critical for revenue collection.

23. Determining the pace of tax reforms depends on the political independence and capacity of institutions dealing with this subject and on public trust in these institutions. The successful implementation of new taxes and a computerized risk-based audit system in the Maldives hinged on the political independence and reform-minded leadership of Maldives Inland Revenue Authority (MIRA). Public awareness campaigns helped build public trust for the MIRA, while strengthening human resources

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37 In terms of sequencing, it is preferable to broaden the revenue base first before raising tax rates.
and the institutional capacity of the MIRA led to successful results in taxpayer registration, compliance, enforcement, and tax collection.

24. **Supporting tax policy and revenue reforms is best done through policy-based loans, especially programmatic loans.** This is also true for other areas of PFM. Over 2005–2015, most World Bank support for tax policy and administration reform was provided through programmatic policy-based loans. Investment projects represented only 11% of the total (footnote 24). Most World Bank funds for tax reforms were committed in middle-income countries with a pre-existing tax to GDP ratio between 10% and 20%.

25. **Financing through policy-based lending combined with technical assistance tends to be more successful in supporting tax administration reforms than tax policy changes.** Possibly this is because tax policy changes are usually backtracked due to political opposition. IEG’s review of evaluation evidence showed that tax objectives were achieved in 72% of the World Bank DPOs. Many operations in Latin America and the Caribbean countries supported a mix of tax policy and tax administration measures that usually—with the notable exception of Colombia—included measures providing for the elimination or reduction of tax exemptions which had largely failed to achieve their goals.

26. **Improving government revenue in a sustainable way usually requires tax policy and administration reforms but these alone are not sufficient.** Other competent institutions, such as the judicial system, need to become involved. Pervasive issues, such as corruption, must be addressed across the public sector. IEG’s project performance assessments of a series of PFM operations in Guatemala in 2012 and 2014 concluded that tax administration and tax policy reforms in the face of major governance issues and long-standing opposition from influential interest groups were unlikely to be successful. Under these conditions, targeting governance issues over a longer period is necessary.

C. Risk Management

27. **Internal audit mechanisms can be an effective alternative to ex ante controls on public expenditures.** However, a balance is required between the need for accountability and flexibility in spending decisions. Risk-based controls for large purchases have been adopted in some cases, in others performance frameworks can be established to measure and track spending. Pre-audits can be used in the case of higher risk payments. A risk-based prioritization framework can be used to prevent corruption, for example in areas where the risk of harm to health outcomes is the greatest. Multi-stakeholder, multi-sectoral oversight bodies, increased public participation in monitoring, and stronger oversight mechanisms allow citizens to exercise accountability and help expose and reduce corruption. Whistleblower protection is critical to encourage citizens to participate without fear of retaliation. Measures to increase the transparency and openness of data and decision making, as well as channels for citizens to safely report instances of potential corrupt acts, are also of paramount importance. Examples include the use of GovTech solutions to report falsified medical products, shortages in supplies, and other irregularities related to procurement.

28. **Implementing governance and accountability mechanisms such as public or social audits, public hearings, information disclosure, independent committees, and monitoring or oversight bodies have important roles in improving PFM.** In the Georgia Social Services Delivery Program, for example, reform measures such as the establishment of internal audit units in ministries to strengthen public finance management, and the implementation of a comprehensive monitoring framework of legal

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public law entities for enhanced transparency in the management of public resources improved the potential for increased effectiveness of public expenditure in social sectors. The Nauru Fiscal Sustainability Reform Program showed that there was greater recognition of the importance of independent financial and operational audits in providing up-to-date financial reports and that performance audit reports could help ensure the accountability and transparency of government operations, increasing confidence in the information provided by the government. However, as an Armenia program revealed, risk-based audit planning, audit committees, and certification of internal auditors can take years before they produce tangible results in improving accountability and combating fraud, and before they are accepted as important accountability mechanisms. Strengthening the external audit function of the government is a faster alternative than improving the regulatory regime. External auditors report publicly and provide more transparency to government and public sector decision making and performance.

29. **Identifying subnational PFM reform interventions is critical but it requires a deeper understanding of political issues and adaptability.** For example, under the Strengthening Public Management Program in Nepal, rather than designing internal audit manuals for village development committees, other approaches could have been considered, such as supporting the Financial Comptroller General’s Office to establish separate audit teams in its district-level treasury offices, or a supreme national audit body that could establish offices nationwide to support the eventual external audits of village development committees. Clear delineation of the key institutional arrangements of the federal system would have strengthened PFM systems at subnational levels. In terms of designing interventions in Nepal, connecting subnational PFM to the main PFM reform agenda would have helped subnational efforts to retain their relevance as federal-level restructuring proceeds. Strengthening anticorruption systems in a holistic manner, rather than limiting activities to training and advocacy, would have been a more beneficial approach. Creating awareness within the government of Nepal of the importance of mechanisms such as the National Vigilance Centre in fighting corruption and promoting transparency and accountability is crucial, along with capacity building and dialogue on reform priorities to strengthen oversight and audit institutions. Public service delivery, including emergency response support and disaster risk management, is the primary responsibility of subnational and local governments so sound PFM systems at the local level are essential to improve public services and reduce fiduciary risks.

D. **Budget Formulation, Execution and Reporting**

30. **Undertaking budgetary reforms is bound to be challenging and achievements can be elusive.** As a result, providers of budget support for PFM need to temper expectations. An IEG evaluation of a long-term series of poverty reduction support credits showed that the progress that had been made in addressing technical limitations in budget formulation, execution, reporting, and procurement had been uneven across countries and over time. There were some positives, such as the use of administrative and economic classifiers and a reduction in the aggregate variance of total budget expenditure. However, few operations were able to reduce extrabudgetary funding, channel all donor funds into government budgets, or achieve progress in integrating medium-term expenditure forecasting with the budget cycle. In terms of execution, greater progress was achieved in reducing expenditure arrears than in improving the effectiveness of the environment for internal controls. More than half of the programs were able to achieve progress on budget reporting.

31. **Carrying out well-sequenced budget reforms will lead to better outcomes, especially in countries with weak capacity.** A gradual and phased approach is needed in introducing the components of a medium-term expenditure framework (MTEF). The MTEF process needs to be integrated

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45 IED. 2013. *Validation Report: Social Services Delivery Program in Georgia*. Manila: ADB.
with the budget process from the outset, with the MTEF outer year projections published as part of the budget circular. In the Lao People’s Democratic Republic, TA strengthened the continuous capacity development within the Ministry of Finance to improve the budget process, through the development of an illustrative MTEF for the government based on spreadsheets with several key assumptions, which were developed in coordination with National Statistics Centre, and the National Economic Research Institute. The TA worked with Fiscal Policy Department staff in the ministry to convey essential principles, and fiscal strategy techniques and methodologies. An MTEF helps the budgeting system comply with the expenditure constraints imposed by fiscal responsibility laws, which commonly limit fiscal aggregates such as debt and deficits. A medium-term expenditure perspective is a useful aid in adhering to the fiscal targets since it provides a framework for taking budgetary decisions over 3 to 5 years.

32. **Implementing an FMIS yields good outcomes when the support is comprehensive.** Support is needed all down the line, beginning with the process review, system design, procurement, system implementation, and maintenance arrangements, followed by systematic coverage in the utilization stage to cover the geographical and functional scope of the budget. This was a finding of a comprehensive review of all the World Bank FMIS operations, based on evaluations and self-evaluations, together with a literature review. A sound FMIS is essential for the efficient tracking and management of expenditures. MDBs have made important contributions in this area and can do more in future. The Word Bank has recognized the importance of information and communication technology (ICT) for automating budget management and has approved around six such operations each year over the past two decades, especially in the poorest countries. Objectives have included improvements in service delivery, public sector effectiveness, expenditure management, and better transparency and accountability. Public expenditure tracking systems are good mechanisms for ensuring checks and balances and for increasing accountability and they are often used to track budget allocations to flagship programs.

33. **Implementing large-scale ICT-related activities such as revenue administration management information systems and integrated treasury management information systems, needs adequate time and long-term commitment to ensure the quality of final products.** The implementation of such systems in Sri Lanka, which involved loosely defined activities for system customization, configuration, redevelopment, and testing, could have benefited from more time for the systems to respond to political and policy changes. In automating treasury management systems or revenue management systems, there are important legacy problems to address as well as important capacity development concerns that need to be properly understood. In the Sri Lanka Fiscal Management Efficiency Project and in many other instances, the preparatory work is often incomplete, and the procurement process ends up in mis-procurement, leading to long delays and cost overruns. Such projects need realistic timelines and adequate risk mitigation measures.

34. **Implementing complex and time-consuming PFM reforms, such as strengthening the management information system, is better if done in a modular manner.** The basic architecture can be put in place initially and once there is greater familiarity with the functionality of the system, the coverage can be expanded. A modular approach will reduce the project’s complexity and keep demands on staff time and efforts manageable. It will allow a phased approach as in-depth reforms can be completed in one agency first before being replicated in others. This was another lesson from the Sri Lanka Fiscal Management Efficiency Project.

35. **Ensuring a functioning FMIS is in place is not sufficient for achieving good PFM.** An effective FMIS requires a clear commitment from the Ministry of Finance that all transactions will be routed

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50 Outer years refer to years other than the budget year in the 3-5-year term of the MTEF.
through the system, and that all expenditures will be subject to the FMIS’s automated, ex ante, internal controls. Payment instructions (e.g., cheques or vouchers) that are issued outside the system should not be honored. Significant political capital is needed to overcome resistance from vested interests in the previous system.  

36. Linking accounts through a single treasury account (so that balances are known) should help to bring all funds within the purview of the treasury. Idle balances should be of particular concern to countries prone to external shocks; without a treasury single account, these funds cannot be drawn on to fill unanticipated financing gaps. Budget support operations may provide leverage for accelerating such reforms.

37. Building and upgrading a public financial management information system (PFMIS) when a country’s needs are evolving requires a careful assessment of costs. When there is a very low level of institutional capacity and the country’s future needs are difficult to project, the cost of upgrading and customizing an off-the-shelf PFMIS may place an excessive burden on the budget. If the local capabilities are adequate, the PFMIS may be developed in-house, which may allow for more flexibility in future upgrades and the tailoring of the system to the government’s evolving needs. Assessing local information technology capabilities and, if necessary, providing training, are prerequisites for choosing the right option.

38. Ensuring sound project implementation arrangements, oversight, and management are critical for FMIS projects in countries with low capacity. For example, the completion report for an African Development Bank FMIS project in Malawi noted that a lack of dedicated project oversight among project coordination and implementing institutions had seriously delayed project implementation. To minimize implementation delays, project coordination and implementing institutions should include some staff who are fully dedicated to project activities and have contract management skills. The Malawi project showed that, in addition to coordination and implementation skills, heads of institutions need to carry out regular and high-level reviews to address the project implementation challenges.

IV. GENERAL LESSONS ON PROGRAM DESIGN AND IMPLEMENTATION FOR ALL PUBLIC FINANCIAL MANAGEMENT INTERVENTIONS

39. Implementing PFM reforms effectively needs to proceed at a pace that is consistent with the government’s capacity. Assessing the government’s capacity to undertake reform conditions will help improve the appropriateness of policy actions and program outputs. The Republic of Marshall Islands’ Public Sector Program was less than successful because its design was overambitious and did not consider the historically slow pace of reforms in the country and the political sensitivity surrounding these reforms.

40. Addressing capacity issues through TA will strengthen the implementation of reforms. TA that is provided along with policy-based programs can help governments meet their policy action targets while simultaneously strengthening their capacity to ensure the effectiveness and sustainability of reforms. The scope of such TA should be determined by an accurate assessment of training and capacity building needs at the fact-finding stage. The implementation of a goods and services tax in

the Maldives to broaden the tax base demonstrated how well-designed and adequately resourced TA can help governments with limited technical capacity to deliver a complex set of reforms. 60

41. Identifying and measuring short-term progress in PFM reform through the design and monitoring framework provides an important indication of whether the outcomes expected by program completion are likely to be achieved. A results framework that allows for the success of the program to be judged over a longer term, with interim outcomes confirming that the long-term outcomes are likely to be met, will improve performance measurability. This will require relevant and measurable performance indicators, e.g., on fiscal costs and the quality of the service delivery, which can measure whether the program led to efficient service delivery to the public (footnote 46).

42. Implementing TA successfully in PFM program depends on a strong government commitment to reforms. In the case of Bhutan, the government’s strong commitment was reflected in clearly defined deliverables matching the policy actions of the program, the selection of teams with appropriate skills, a proper oversight and monitoring mechanism, effective coordination between the consulting team and counterpart staff, and regular reviews by ADB and the government. 61 Problems were identified and resolved in a timely manner, and resources were promptly provided whenever required. Similarly, the successful implementation of the West Bengal Development Finance Program was due to the political commitment of the government of West Bengal to the reform program and the Finance Department’s reform-minded leadership. 62 Adequate TA resources were provided, and the program had a good project management structure with clear milestones for deliverables. Progress toward the projected outcomes was regularly reviewed, and problems identified and resolved in a timely fashion. More generally, research findings have shown that aid inflows are effective only in countries with sound policy and institutional settings, 63 a message that has been echoed by MDBs such as the IADB. 64 A long-term IEG evaluation of public sector reform supported by the World Bank concluded that there was strong evidence that government weakness and corruption was key to explaining the project failures and disappointing development record of the 1970s, after which public sector management took center stage in development lending. 65 A recent IEG evaluation of a series of PFM operations in Poland showed how satisfactory outcomes in the terms of fiscal consolidation, strengthened fiscal institutions and improvements in the efficiency and sustainability of social spending were linked to high levels of country commitment, and these in turn were reinforced by Poland’s external commitments to the European Union, as an accession country. Policies not required by the European Union were more easily reversed. 66

43. Pilot testing of social protection that is embedded in the policy actions targeting vulnerable groups can help ensure follow-on actions from the government. For example, after completion of a program in Tonga, the government established a new Social Protection and Disability Division within the Ministry of Internal Affairs. 67 A TA project can play a crucial role in pilot testing social protection schemes, initiating policy discourse in social protection, and helping to build government consensus and capacity for social protection. A pilot proxy means test (PMT), developed through a TA in Mongolia, helped build a consensus among the government and the public on the importance of PMT-based targeting in ensuring social protection benefits reached those in greatest need. 68 If prior pilot work collects valuable

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evidence that convinces governments, the PBL support can take the reforms to scale. Pilot projects are useful in assessing ease of implementation, adaptability, and the potential for full-scale implementation, and in identifying new potential bottlenecks and areas requiring further reforms. In Bhutan’s Strengthening Economic Management Program, the successful pilot testing of a new property valuation methodology demonstrated the potential to increase local revenues from property taxes substantially and contributed to potential revisions of outdated tax laws.\(^6^9\)

44. **Ensuring good government and development partner coordination and collaboration contributes to successful program implementation.** The experience from supporting reform programs in the Pacific is that strong coordination among development partners can contribute to a program’s success. In Kiribati, joint donor support provided a significant incentive for reform as well as providing sizable support relative to the country’s GDP.\(^7^0\) In the Tuvalu program, the presence of a highly consultative process allowed development partners to coordinate their budget support and TA for reforms.\(^7^1\) A single, government-led, policy matrix enhanced coordination and collaboration among development partners and made line ministries actively compete to have reforms listed in the policy reform matrix. In Solomon Islands, coordinated donor support prevented duplication of effort and reduced transaction costs for both the government and development partners.\(^7^2\) A formal working group comprising the government and development partners helped channel a growing share of development partner support through government systems. Greater consultation and negotiation between the government and all major development partners can lead to a more accurate assessment of the challenges, the design of appropriate long-term structural reforms, and more accurate monitoring.\(^7^3\) Georgia’s experience has shown that rapid response and collaboration among development partners in collectively assisting the government to design a crisis response can help alleviate a financial crisis, limit economic contraction, and address constraints arising from infrastructure damage, investment climate deterioration, financial difficulties, and the worsening social conditions of internally displaced persons.\(^7^4\)

45. **Establishing reform preconditions for the release of grant funds provides appropriate incentives for the government to undertake reforms aimed at improving government revenues.** In the Strengthening Fiscal Stability Program in Kiribati, improvements made to the governance and operation of SOEs and the replacement of SOE subsidies with targeted assistance brought about significant government savings (footnote 70). Improved value-added tax implementation and fishing revenue administration increased revenue collections. Stronger measures to ensure compliance with the Debt Policy of 2013 prevented expensive commercial borrowing, the re-accumulation of overdraft balances, and inappropriate loan guarantees to SOEs and joint ventures. In the Maldives, the implementation of a goods and services tax was effective in enhancing the revenue base (footnote 60).

46. **Implementing ICT-based investments in governance can improve the effectiveness of tax programs.** The introduction of ICT-based tax administration systems and processes in Tajikistan effectively increased revenues and streamlined expenditures, especially on social programs.\(^7^5\) In Nepal, similar measures helped enhance the quality and accessibility of public services.\(^7^6\) However, in implementing ICT investments, varying levels of readiness in staff skills, data and resource requirements, and implementation timelines need to be taken into account. Having clear operating guidelines, appropriate physical facilities, training, and IT support from the central government can enhance the sustainability of such investments.

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47. Focusing on the key needs and constraints of vulnerable groups, setting realistic timelines, and properly sequencing policy actions on social protection benefit from an established system for beneficiary identification, delivery and monitoring. Without a system that specifically tracks vulnerable groups, it is harder to assess the results of budget increases to the social sector (footnote 67). An intersectoral database using PMT data can be used to target the social protection programs of all government agencies. If such a database is one of the TA components, it can help the executing agency of the program to coordinate policy reforms across the social welfare, education, health, and urban development sectors, and across government agencies, including the ministries of health, education, culture and science, and labor and social protection (footnote 68). It is preferable to build and nurture reliable and strong social protection systems during non-crisis periods so that they can be scaled up during a crisis and scaled down later. With reliable social protection systems in place, governments can reach out effectively to the vulnerable and disburse assistance quickly, with minimal wastage and leakage.

48. Achieving the higher-level objective of good governance demands sustained efforts over time since PFM reforms can take decades before they can be completed. The continued provision of financial and, more importantly, knowledge by development partners will be needed over a long period. Strong development partner harmonization and coordination have been enabling factors in successful project and program outcomes to date.

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