# Republic
# of the Union of Myanmar

## Public Financial Management Performance Report
## Executive Summary

May 2013

CURRENCY EQUIVALENTS
March 16, 2013
1 US Dollar = 872.49 Myanmar Kyat
1 Kyat (MMK) = 0.0012 US Dollar (USD)
FISCAL YEAR
April 1 – March 31

## Abbreviations and Acronyms

| | | |
|---|---|---|
| ADB | - | Asian Development Bank |
| AG | - | Auditor General |
| ASEAN | - | Association of Southeast Asian Nations |
| AusAID | - | Australian Agency for International Development |
| BD | - | Budget Department |
| BOT | - | Build-Operate-Transfer |
| CBM | - | Central Bank of Myanmar |
| CCTO | - | Company Circle Tax Office |
| CD | - | Customs Department |
| COFOG | - | Classification of the Functions of Government |
| DFID | - | Department for International Development |
| EITI | - | Extractive Industries Transparency Initiative |
| FC | - | Financial Commission |
| FERD | - | Foreign Economic Relations Department |
| FR | - | Financial Regulations |
| GDP | - | Gross Domestic Product |
| GFS | - | Government Finance Statistics |
| GFSM | - | Government Finance Statistics Manual |
| GIR | - | General Index Registration |
| GRF | - | General Reserve Fund |
| HS | - | Harmonized Systems |
| ICT | - | Information and Communications Technology |
| IMF | - | International Monetary Fund |
| INGO | - | International Non-Governmental Organization |
| INTOSAI | - | International Organization of Supreme Audit Institutions |
| IPSAS | - | International Public Sector Accounting Standards |
| IRD | - | Internal Revenue Department |
| MEB | - | Myanmar Economic Bank |
| MFR | - | Ministry of Finance and Revenue |
| MIC | - | Myanmar Investment Commission |
| MOD | - | Ministry of Defense |
| MOGE | - | Myanmar Oil and Gas Enterprise |
| MOH | - | Ministry of Health |
| MOHA-GAD | - | Ministry of Home Affairs General Administration Department |
| MOU | - | Memorandum of Understanding |
| MNPED | - | Ministry of National Planning and Economic Development |
| MP | - | Member of Parliament |
| NGO | - | Non-Governmental Organization |
| OA | - | Other Account |
| OAG | - | Office of the Auditor General |
| ODA | - | Official Development Assistance |
| PA | - | Provisional Actual |
| PAC | - | Public Accounts Committee |
| PC | - | Planning Commission |
| PEFA | - | Public Expenditure and Financial Accountability |
| PFM | - | Public Financial Management |
| PI | - | Performance Indicator |
| PPP | - | Public-Private Partnerships |
| PR | - | Performance Report |
| R&D | - | Research and Development |
| RAT | - | Revenue Appellate Tribunal |
| RE | - | Revised Estimate |
| SAO | - | State Administrative Organizations |
| SDR | - | Special Drawing Rights |
| SEE | - | State Economic Enterprises |
| SFA | - | State Funds Account |
| SNG | - | Sub-National Government |
| SORC | - | Special Orders for Rapid Clearance |
| SPDC | - | State Peace and Development Council |
| TIN | - | Tax Identification Number |
| TWG | - | Technical Working Group |
| UNDP | - | United Nations Development Program |
| UNICEF | - | United Nations Childrens Fund |

## Foreword and Acknowledgements

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1 Rob Taliercio (Lead Economist and Task Team Leader), Shabih Ali Mohib (Senior Economist, Co-Task Team Leader), Khwima Nthara (Senior Country Economist), Doug Addison (Senior Economist), Miki Matsuura (Public Sector Specialist), Peter Brooke (Consultant), Robert Boothe (Public Sector Specialist), and Tuan Minh Le (Senior Public Sector Specialist).

## Summary Assessment

1. The Public Financial Management Performance Report (PFM-PR) is the first comprehensive review of Myanmar's PFM system. There is no recent history of development partner engagement on PFM reform and little had been understood about the status of the Government's PFM reform agenda. The objective of this report is to provide the first comprehensive assessment of Myanmar's PFM system. The report aims principally to establish an objective baseline measure of current PFM conditions, highlighting areas of absolute and relative strength and weakness. The assessment, and the associated dialogue, provides support to the Government in setting its reform priorities.

2. At the same time it should be noted that the Government is in the process of undertaking a major political and economic reform program, with major implications for public financial management and broader public sector management. The new reformist Government, sworn in on March 30th, 2011, immediately embarked on a range of political and economic reforms aimed at attaining national reconciliation, good governance, and economic development. Key economic reforms include adoption of a more liberal exchange rate policy, relaxation of trade restrictions, rationalization of tax rates, and fiscal decentralization.

3. With regard to management of public finances, there have been two major catalysts for reforms since 2011. First, the operationalization of the Parliament and establishment of the Public Accounts Committee and the Planning and Finance Committee have resulted in enhanced external scrutiny and oversight over the budget by the Parliament, while the public airing of budget debates on the national television and the publication of the budget law in national newspapers has enhanced budget transparency. Second, the constitutional requirement for separation of regional and state budgets from the Union has required rapid deconcentration of budgeting and planning functions to support bottom up planning and budgeting processes in states and regions. In order to coordinate state/region budgets with the Union budget, the Government has also established the Financial Commission and the National Planning Commission. The new planning and budgeting practices have also resulted in a deconcentration of PFM policy functions from the President's Office to the Ministry of Finance and Revenue (MFR) and the Ministry of National Planning and Economic Development (MNPED), respectively.

4. An additional set of important PFM reforms are also in train. In particular, proposals are being developed to make the Central Bank of Myanmar (CBM) independent and to separate out the functions that it currently performs on public finance management. State Economic Enterprises (SEEs) are being given greater financial autonomy and are now allowed to keep part of their profits, but they are also required to fund most of their own working capital requirements. Some SEEs are being privatized or otherwise being fully exposed to market forces.

### Integrated Assessment of Public Financial Management Performance[2]

5. Under the Public Expenditure and Accountability (PEFA) Program, which is a joint effort of the World Bank, the International Monetary Fund, the European Commission, the United Kingdom's Department for International Development, the French Ministry of Foreign Affairs, the Royal Norwegian Ministry of Foreign Affairs, and the Swiss State Secretariat for Economic Affairs, the public financial management Performance Measurement Framework has been developed to assess whether a country has the tools to deliver three main budgetary outcomes: aggregate fiscal discipline, strategic resource allocation, and efficient use of resources for service delivery.

6. A good PFM system is essential for the implementation of policies and the achievement of developmental objectives. An open and orderly PFM system is one of the enabling elements for those three levels of budgetary outcomes:

   - Effective controls of the budget totals and management of fiscal risks contribute to maintain aggregate fiscal discipline.

   - Planning and executing the budget in line with government priorities contributes to implementation of government's objectives.

   - Managing the use of budgeted resources contributes to efficient service delivery and value for money.

2 This introductory section is drawn from www.pefa.org.

7. The PEFA Framework was created as a high level analytical instrument which consists of a set of 31 indicators and a supporting PFM Performance Report, providing an overview of the performance of a country's PFM system. Drawing on the established international standards and codes, and other commonly recognized good practices in PFM, it forms part of the strengthened approach to supporting PFM reform, which emphasizes country-led reform, donor harmonization and alignment around the country strategy, and a focus on monitoring results.

8. The PEFA Framework identifies the critical dimensions of performance of an open and orderly PFM system, using 31 core indicators, as follows:

   - Credibility of the budget: The budget is realistic and is implemented as intended.

   - Comprehensiveness and transparency: The budget and the fiscal risk oversight are comprehensive and fiscal and budget information is accessible to the public.

   - Policy-based budgeting: The budget is prepared with due regard to government policy.

   - Predictability and control in budget execution: The budget is implemented in an orderly and predictable manner and there are arrangements for the exercise of control and stewardship in the use of public funds.

   - Accounting, recording, and reporting: Adequate records and information are produced, maintained, and disseminated to meet decision-making control, management, and reporting purposes.

   - External scrutiny and audit: Arrangements for scrutiny of public finances and follow up by the executive are operating.

9. Each indicator seeks to measure performance of a key PFM element against a four point ordinal scale from A (highest) to D (lowest). The highest score is warranted for an individual indicator if the core PFM element meets the relevant objective in a complete, orderly, accurate, timely, and coordinated way. The set of high-level indicators is therefore focusing on the basic qualities of a PFM system, based on existing good international practices, rather than setting a standard based on the latest innovation in the PFM field.

10. Table 1 summarizes the links between the six PEFA dimensions and the three levels of budgetary outcomes in Myanmar and provides a high level overview of the consequences of the country's PFM system.

Table 1: Links between the key dimensions of a PFM system and the three levels of budgetary outcomes in Myanmar

| | Aggregate fiscal discipline | Strategic allocation of resources | Efficient service delivery |
|---|---|---|---|
| **Budget credibility** | In order for the budget to be a tool for policy implementation, it is necessary that it is realistic and implemented as passed. | | |
| The budget is realistic and is implemented as intended | The lack of budget credibility in Myanmar has not had a major impact on fiscal discipline, in part because revenues tend to be underestimated. | A lack of credibility in the budget in Myanmar leads to a misalignment of policy priorities and spending, as the budget is significantly remade during the year. Differences in actual spending as compared to budgeted spending have been substantial, leading to differences between stated policy and actual spending. | The significant differences in budgeted as compared to actual spending in Myanmar raise the chances of inefficiencies in service delivery due to unplanned over- or under-spending. |
| **Comprehensiveness and transparency** | Comprehensiveness of budget is necessary to ensure that all activities and operations of governments are taking place within the government fiscal policy framework and are subject to adequate budget management and reporting arrangements. Transparency is important for enabling external oversight of government policies and programs and their implementation. | | |
| The budget and fiscal risk oversight are comprehensive and fiscal and budget information is accessible to the public | Budget control in Myanmar could be pressured by the many changes that have been made in the operations of SEEs and sub-national governments.<br><br>The lack of a report on fiscal risk leaves the Government open to potentially significant problems in the future.<br><br>The underdeveloped budget classification system, the lack of comprehensiveness in budget documentation, and limited availability of information to the public limits scrutiny by the public and financial markets. | Myanmar's budget classification is not fully consistent with modern classification systems, which limits the ability of policy makers to make informed judgments about tradeoffs in spending.<br><br>The significant level of unreported government operations means that the budget law presents a quite limited picture in terms of central government revenue, expenditure, and financing, which limits transparent discussion of competing priorities, likely leading to less efficient allocation of funds. | The underdeveloped budget classification system, the lack of comprehensiveness in budget documentation, and limited availability of information to the public limits scrutiny by citizens, who would not have the ability to meaningfully analyze spending in light of their preferences. |

| | Aggregate fiscal discipline | Strategic allocation of resources | Efficient service delivery |
|---|---|---|---|
| **Policy-based budgeting** | A policy-based budgeting process enables the government to plan the use of resources in line with its fiscal policy and national strategy. | | |
| The budget is prepared with due regard to government policy | Limited focus on medium term implications of fiscal decisions may lead to unsustainable policies in Myanmar. | Sector strategies in Myanmar may have been prepared for some sectors, but none of them have substantially complete costing of investments and recurrent expenditure, which limits the ability of planning efforts to influence future budgets. | Budgeting for investment projects and recurrent expenditure (salaries, operations and maintenance) are separate processes in Myanmar, which leads to inefficiencies in service delivery. |
| **Predictability and control in budget execution** | Predictable and controlled budget execution is necessary to enable effective management of policy and program implementation. | | |
| The budget is executed in an orderly and predictable manner and there are arrangements for the exercise of control and stewardship in the use of public funds. | Control in Myanmar focuses on transactions, which is useful but not the only important factor.<br><br>There is a high level of negotiations in areas such as revenue collection. | The effect is to provide a framework of control, but to leave the system open to abuse and corruption by those who would seek to make use of that vulnerability. | Regulation in Myanmar focuses on detailed transaction control and avoiding budget overrun rather than accountability for the efficient delivery of service. |
| **Accounting, recording and reporting** | Timely, relevant and reliable financial information is required to support all fiscal and budget management and decision-making processes. | | |
| Adequate records and information are produced, maintained and disseminated to meet decision-making control, management and reporting purposes | Highly limited information (on contingent liabilities and future costs of investment projects) reduces the scope for management of long-term fiscal sustainability in Myanmar. | Accounting and reporting tend to be viewed as a largely technical process that exerts control in avoiding overspending and providing the basis for audit. It does little to establish deeper accountability for how resources are used or play a role in active in-year financial management. | Limited information on the cost of programs in Myanmar weakens the planning and management of service delivery, and also reduces the availability of evidence needed for effective audit, providing potential opportunities for leakages, corrupt procurement, or inappropriate use of funds. |

| | Aggregate fiscal discipline | Strategic allocation of resources | Efficient service delivery |
|---|---|---|---|
| **Effective external scrutiny and audit** | Effective scrutiny by the legislature and through external audit is an enabling factor in the government being held to account for its fiscal and expenditures policies and their implementation. | | |
| Arrangements for scrutiny of public finances and follow up by executive are operating. | Myanmar's new parliament is starting to monitor aggregate fiscal discipline through the annual budget process. | The new parliament is starting to monitor and reorient spending allocations through the annual budget process. | Myanmar's parliament does not generally have sufficient information to advise on service delivery efficiency and effectiveness, but the Auditor General is contributing to identifying waste, fraud, and abuse. |

## Credibility of the budget

11. Budget expenditure credibility in recent years has been low, with the exception of revenue where credibility is higher. Differences in recent years between total actual spending and the approved budgets have been large and growing, increasing from 8.7 percent of approved spending in 2008-09 to 20.2 percent in 2010-11. Much but not all of this can be traced to adjustments made in the annual revised budget. In recent years, revenues have generally been somewhat higher than expected. Compositional expenditure deviations (that is, differences in budget as compared to actual spending in ministries) have been substantial, and often exceed the deviations in total spending. The issue of payments in arrears could not be assessed due to lack of legal definition of arrears and lack of a central arrears monitoring system.

## Comprehensiveness and transparency

12. The budget and oversight of fiscal risk are not comprehensive. Nor is fiscal and budgetary information generally available to the public. There are currently a number of limitations in the classification of budget information, as well as missing types of information in budget documents themselves and a large amount of unreported government operations, which together mean that budgetary and fiscal information is highly limited. Myanmar's budget classification system is not fully consistent with modern classification structures. The formal presentation of the budget as contained in the Union Budget Law consists of a limited amount of information, though great progress was made in FY2012/13 in making the Union Budget Law public.

13. Budget comprehensiveness and transparency are affected by the significant level of unreported government operations, which means that the budget law presents a quite limited fiscal picture in terms of central government revenue, expenditure, and financing. In Myanmar's case there is a high degree of extra-budgetary expenditure that is not included in fiscal reports while, at the same time, there is limited information on development partner-funded projects included in fiscal reports. There is extensive use of "Other Accounts," which are essentially accounts held by ministries and SEEs in the Myanmar Economic Bank (MEB) for management of their own-source revenues. FY2011-12 data show total Other Account receipts of 2.54 trillion kyat, which is 44 percent of total budgeted revenue, and expenditures of 2.26 trillion, which represents 28 percent of total budgeted expenditure. On the external financing side, the picture is also mixed. Though complete income/expenditure information is included in fiscal reports for all loan financed projects, it appears that only some information on grant financed projects is also included.

14. Another important consideration from the perspective of transparency and comprehensiveness is the treatment of the intergovernmental fiscal system (the system between the Union and the states and regions), which has changed a lot since the new constitution. In operational terms the assignment of functions (such as health and education) and finances (such as taxes and expenditures) is evolving. Like with many other budgetary process indicators, the system is not yet fully formed because this is the first full fiscal year in which the new system is being

implemented. The assessment shows that the system for allocating resources to states/regions is neither rule-based nor transparent, and that states/regions do not receive timely, reliable information on their transfers. Moreover, states/regions may and do request additional monies through supplementary budget allocations. These features make for an inter-governmental fiscal system that is not transparent and that impedes sound budget planning. However, it is worth noting that final state/region budget laws are published in local newspapers.

15. One of the likely consequences of a fiscal system in as much flux as Myanmar's is a probable increase in the amount of fiscal risk. In addition to the sweeping changes that have taken place at the political and constitutional level, many material changes have also been made in the operations SEEs and sub-national governments. These major systemic changes increase the likelihood of fiscal risk for four main reasons. First, the internal control environment is still relatively weak. For example, the internal audit function is only now being established in line ministries and the capacity in SEEs varies. Second, the central oversight function is narrow and underdeveloped. Third, there is a lack of a strategic approach to public financial management, with central oversight agency engagement focusing more on low value processes and less on analysis of results and impact of spending. Lastly, public fiscal information is quite limited, reducing the chances of meaningful public engagement on these issues. Moreover, a consolidated report on total fiscal risk from the point of view of the Union Government is not produced. The lack of such an analysis leaves the Government open to potentially significant blind spots. Another source of fiscal risk emanates from possible contingent liabilities from public-private partnerships (PPPs).

## Policy-based budgeting

16. The budget process in Myanmar is largely guided by prior practice. Although officials have clearly defined roles and understand their responsibilities well, there is incomplete guidance in existing laws and regulations. For the period under review, ministry spending proposals were generally made independently of any central coordination regarding future resource availability or constraints. Macroeconomic forecasts are not routinely shared with the line ministries nor are they used to help determine aggregate expenditure ceilings for current and future years. Major policy decisions or options are not required to be fully costed in terms of estimates of forward expenditures and are not required to be described in sector strategy documents.

17. The Union budget process is decentralized, with the SAOs and line ministries setting their own budgetary ceilings and devising their own expenditure proposals. Budget proposals are organized along administrative lines, by ministry and department, rather than by programs, activities, or outputs. The Budget Department (BD) of the Ministry of Finance and Revenue (MFR) is responsible for collating and consolidating the recurrent budget. The Ministry of National Planning and Economic Development (MNPED) is responsible for the capital budget. It also reviews all investment proposals prior to entry into the budget. The process is hierarchical with five levels of scrutiny before the draft budget is submitted to the Parliament for debate and eventual adoption immediately prior to the start of the next fiscal year.

## Predictability and control in budget execution

18. Spending bodies have a reasonable degree of predictability about the resources available to them in terms of the original budget assigned to them for each year. Quarterly limits on spending are set for recurrent spending (although not for capital), but the spending bodies set these limits themselves based on the phasing of their expenditure plans. They do face the risk that if they do not spend these quarterly limits, the unused balance will be removed from their budgets for the year as a whole.

19. Payment processes are not overelaborated and payments can be made efficiently through the network of MEB branches with a minimum of delay and without centralized vetting from MFR. However, payments may bunch or get carried over to another period or year in an unpredictable way causing additional budget management pressures. Furthermore, the large scale and late timing of supplementary budget approvals made in recent years has meant that provision to address additional pressures or to tackle new initiatives has not been certain until the final few months of the year.

20. The Financial Regulations (FRs), and their related instructions, the OoSa and HtaSa, dealing with transaction control and reporting, are somewhat

out of date (last revised in 1986 in the case of FRs). The financial regulations are recognized as being substantially out of date. As such, they do not fully reflect current practice other than in a general way. In addition, there are even older regulations used that deal with specific issues and situations; some of these go back to the 1950s. Their legal status is unclear although they continue to be used as the basis for practice. The finance department in each spending body appears to play a key role in deciding which mix of rules is adopted within its organization. The arrangements are thus somewhat ad hoc, differing from ministry to ministry. Moreover, the regulations are open to interpretation by financial management officials and it is not clear the regulations are well understood throughout ministries and states/regions.

21. But the emphasis is on the controlled processing of transactions and the avoidance of overspending of budget provision rather than broader accountability for the effective use of resources. The lack of linkage between plans and budgets means that expected results are not clearly defined. Classification and reporting systems are focused on identifying the spending unit and the nature of the input rather than the objectives of the expenditure or what it is intended to achieve.

22. The system of delegation of powers to spending agencies is occurring without the necessary assurances in place. The lack of centrally defined standards in areas such as payroll management and procurement do not ensure that the processes implemented at the level of the spending bodies observe at least minimum procedures and controls. In many cases, these minimum requirements are either not defined or the current status of old regulations is not clear. For example, procurement was recently released from central control by the Ministry of Commerce and delegated to spending bodies giving them at the same time a clear instruction to increase the use of open competitive tender. But each spending body was left to develop its own detailed procedures and systems.

23. There is little feedback to MFR, other than through the reports of the Office of the Auditor General (OAG), about the observance of minimum requirements (even where they are defined), variations in the effectiveness of the control regime implemented by individual spending bodies, or statistical information such as the value of procurement processed through different procurement techniques. The lack of internal audit in many spending bodies does not give assurance to senior management in ministries that financial systems and processes (not just individual transactions) are being conducted effectively and being adequately enforced. The OAG also indicates that significant problems arise with regards to procurement at all levels with regards to both purchasing and the letting of concessions. This lack of assurance exposes the control system to risk and unevenness of application. The challenge remains of achieving an appropriate level of assurance without undermining the beneficial aspects of delegation.

24. With regards to tax policy and administration, there have been some improvements in communicating with taxpayers and in offering recourse to appeal. The predictability of the flow of tax revenues continues to be affected by weak collection systems, the existence of tax incentives and discretionary powers with regard to their being applied by different administrative bodies and levels, weaknesses in the compliance management system, and high values of on-going arrears and considerable administrative negotiation surrounding the handling of those arrears. Partly as a result, tax collection has remained very low, at around 3-4 percent of GDP, in recent years. There is also a lack of assurance with regard to the operation of tax collection systems. Although there have been some improvements in the legal basis of taxation, a comprehensive, modern system of laws and regulations is still yet to emerge. Taxpayer registration is weak and fragmented. There is no central guidance on planning the auditing and investigation of taxpayers, which often occur at the local level and are not directly controlled by the central tax authorities.

## Accounting, recording and reporting

25. Accounting is maintained on a simple (cash based double entry) system. Most payments are discharged through MEB by the use of check or transfer. The use of physical cash is limited although most departments use cash for special purposes such as extended travel. Tax revenue is usually paid into MEB by the taxpayer directly, based on an assessment raised by the tax authorities although some fee and charge revenue is collected in cash and paid in by the body concerned.

26. Accounting records are originated by the spending/revenue raising body concerned. Aggregation and

reconciliation for reporting and control purposes are conditioned by the largely manual, paper based processes that are still used in both the originating bodies and in MEB. The processes of reconciliation are well documented, appear adequate, and are applied with sufficient rigor to give some confidence in the accuracy of aggregate records.

27. Reporting is done monthly. However, the process of aggregation and reconciliation takes some 3 months to complete, which delays the production of final reports for each monthly reporting cycle. In order to provide more timely data, the BD produces an interim report which it usually manages to issue within 6 to 8 weeks after the end of the month in question. But, even so, the compressed format and delayed timing of the reports combined with the limited degree of analysis that is included in summary reports weakens their capacity to support active in-year management of the emerging position. The manual aggregation processes also impose difficulties in producing information in different formats for specific or ad hoc purposes.

28. End-of-year financial statements are produced on a similar basis to those produced in-year, but with supplementary clearance arrangements. In the last few years they have been finalized within 6 months of the end of the year. But the statements largely serve the purpose of providing some discipline ensuring consolidation and reconciliation. They provide limited information as a basis for active financial management and both their form and distribution are difficult to interpret and contribute little to fiscal transparency. International accounting standards, even for cash based systems, are not fully met and there are no clear notes attached to the statements explaining the basis on which they have been produced or giving supplementary information about important issues such as guarantees and contingent liabilities. Neither in-year nor end-of-year statements are given wide circulation.

## External scrutiny and audit

29. Since 2011, the Parliament has established two specialized committees for the purpose of providing oversight of the Government's public finances, and, despite its relatively recent origins, is having a major influence on PFM, both broadly and on specific issues. The Public Accounts Committee (PAC) has a bipartisan membership and vets the budget bill and the audit report. The Planning and Finance Committee is responsible for reviewing the national development plan and legislative matters relating to the financial sector. Since 2012-13 these committees have reviewed and rationalized the executive's budget proposal significantly and have been instrumental in having the approved budget law published in the local press. These committees have engaged some technical advisors on a part time basis but do not have specialized staff or institutional support that can independently review and analyze the budget proposals and the national development plan in order to advise the PAC accordingly. Instead, the committees rely on government ministries for policy analysis.

30. The Office of the Auditor General (OAG), also despite its relatively recent origins, is having a significantly positive impact on the management of public finances in Myanmar. The OAG is a semi-independent body reporting to the Parliament through the President's Office. The OAG has purview over all the public sector, except for the Ministry of Defense. The OAG is also the entity responsible for setting accounting and auditing policy for the public sector. The OAG has adopted international audit standards and conducts mostly financial audits with some procurement and performance audits. The OAG has yet to submit an audit report to the Parliament – under the Parliamentary form of government which started functioning from 2011 onward. A formal response is provided by ministries to the audit findings within 1 month of receiving the audit opinion, but there seems to be little evidence of systematic follow-up.

## Assessment of the Impact of PFM Weaknesses

31. The analysis of the six PEFA dimensions suggests a system that would benefit from strengthening in all areas. The extant limitations of the system suggest that it is highly constrained in delivering across the board on the three levels of budgetary outcomes: aggregate fiscal discipline, strategic allocation of resources, and efficient service delivery. The weak control environment, combined with limited budget comprehensiveness and transparency, suggest a system that is at risk to corruption as well.

### Table 2: Summary PEFA Framework Assessment

| | Overall Score | Dimensions | | | |
|---|---|---|---|---|---|
| | | i. | ii. | iii. | iv. |
| **A. PFM OUT TURNS: Credibility of the Budget** | | | | | |
| PI-1. Aggregate expenditure out-turn compared to original approved budget | C | C | | | |
| PI-2. Composition of expenditure out-turn compared to original approved budget | D+ | D | A | | |
| PI-3. Aggregate revenue out-turn compared to original approved budget | B | B | | | |
| PI-4. Stock and monitoring of expenditure payment arrears | N/R | N/R | D | | |
| **B. KEY CROSS CUTTING ISSUES: Comprehensiveness and Transparency** | | | | | |
| PI-5. Classification of the budget | D | D | | | |
| PI-6. Comprehensiveness of information included in budget documentation | D | D | | | |
| PI-7. Extent of unreported government operations | D+ | D | C | | |
| PI-8. Transparency of inter-governmental fiscal relations | D | D | D | N/A | |
| PI-9. Oversight of aggregate fiscal risk from other public sector entities | C | C | N/A | | |
| PI-10. Public access to key fiscal information | D | D | | | |
| **C. BUDGET CYCLE** | | | | | |
| **(i) Policy-based Budgeting** | | | | | |
| PI-11. Orderliness and participation in the annual budget process | C+ | C | D | A | |
| PI-12. Multi-year perspective in fiscal planning, expenditure policy and budgeting | D+ | D | B | D | D |
| **(ii) Predictability and Control in Budget Execution** | | | | | |
| PI-13. Transparency of taxpayer obligations and liabilities | C+ | C | B | C | |
| PI-14. Effectiveness of measures for taxpayer registration and tax assessment | D+ | D | C | D | |
| PI-15. Effectiveness in collection of tax payments | D+ | D | A | C | |
| PI-16. Predictability in the availability of funds for commitment of expenditures | D+ | D | A | A | |
| PI-17. Recording and management of cash balances, debt and guarantees | C+ | C | C | B | |
| PI-18. Effectiveness of payroll controls | D+ | D | B | C | D |
| PI-19. Competition, value for money and controls in procurement | D | D | D | D | D |

| | Overall Score | Dimensions | | | |
|---|---|---|---|---|---|
| | | i. | ii. | iii. | iv. |
| PI-20. Effectiveness of internal controls for non-salary expenditure | D+ | D | D | B | |
| PI-21. Effectiveness of internal audit | D+ | D | D | C | |
| **(iii) Accounting Recording and Reporting** | | | | | |
| PI-22. Timeliness and regularity of accounts reconciliation | C+ | D | A | | |
| PI-23. Availability of information on resources received by service delivery units | D | D | | | |
| PI-24. Quality and timeliness of in-year budget reports | C | C | C | C | |
| PI-25 Quality and timeliness of annual financial statements | D+ | C | A | D | |
| **(iv) External Scrutiny and Audit** | | | | | |
| PI-26. Scope, nature and follow-up of external audit | C+ | C | N/A | B | |
| PI-27. Legislative scrutiny of the annual budget law | N/A | N/A | N/A | N/A | N/A |
| PI-28. Legislative scrutiny of external audit reports | N/A | N/A | N/A | N/A | |
| **D. DONOR PRACTICES** | | | | | |
| D1. Predictability of direct budget support | N/A | | | | |
| D2. Donor financial information provided for budgeting and reporting on project/ program aid | D | D | D | | |
| D3. Proportion of aid that is managed by use of national procedures | D | D | | | |

*Note: "Not Rated" (N/R) is used when adequate evidence is not available; "Not Applicable" (N/A) is used when a new system or process has not yet been in place for at least a full fiscal year.*

32. Myanmar's PFM system is highly informal: there is a lack of foundational legal underpinnings (e.g., organic budget law) and it is not fully clear which regulations are legally in force (so ministries have adopted different approaches, e.g., using old colonial regulations from India as guidelines). Myanmar's system does focus narrowly on control but not on accountability: regulation focuses on detailed transaction control and avoiding budget overruns rather than accountability for the efficient delivery of service. There is little visibility for how controls are applied in practice between different levels of the administration and with the parliament. Reliance is placed on the Auditor General rather than internal standard setting and review. The financial regulations focus on control at the transaction level whereas a large amount of supplementation and virement takes place. There is a high degree of delegated negotiability in areas such as revenue collection. The effect is to provide a framework of control and practice, but to leave the system open to abuse by those who would seek to make use of that vulnerability.

33. The system emphasizes control rather than dynamic management of resources in order to achieve a high quality of expenditures in delivering policy objectives. Key weaknesses are: a lack of effective connection between strategic plans and budgets on the one hand and between recurrent and capital expenditure on the other; an emphasis on managing the short term rather than planning strategically for the medium to long term; and information and cash forecast management is cumbersome and inflexible and focused on cash control rather than informing decisions about new commitments, priorities, and options. The impact is to undermine the ability of the system to focus attention on the strategic allocation of resources in delivering policy objectives. Public finances are exposed to a watering down of the quality of expenditures as increasing resources become available.

34. The exposure of public financial management to external risks is not adequately managed and this will become more important:

- The role of public finances within broader management of the economy has been complicated and entwined. Monetary and public financial management have been inter-dependent and commercial activity has been dominated by SEEs. These overlaps are being unwound, but will expose public financial management to new risks.
- Key areas of risk and exposure that will become more important are the management and control of debt and cash. These have been under-managed in the past.
- There is an absence of a clear framework of understood policies and parameters within which public finances will be managed.

35. The impact is that as more demands are placed on public financial management, in an environment of a more open economy, aggregate fiscal discipline is vulnerable to being undermined.

### Prospects for Reform Planning and Implementation

36. The Public Finance Management (PFM) reforms being undertaken are part of a much broader reform program of the Government. With regards to management of public finances, there have been two major catalysts for reforms since 2011. First, the operationalization of the Parliament and establishment of the Public Accounts Committee and the Planning and Finance Committee has resulted in enhanced external scrutiny and oversight over the budget. Second, the constitutional requirement for separation of regional and state budgets from the union budget has required rapid deconcentration of budgeting and planning functions to support bottom up planning and budgeting processes at the state and region level.

37. The fast pace of reform has meant that the authorities have made signficant changes in PFM practices without either drawing up a reform strategy or updating the rules and regulations that govern public finances to be in-line with the current practices. Where regulation has been passed, it has remained at a relatively high level with signficant leeway given to agencies to determine policy implementation. This has made the current PFM system underregulated and largely practice based.

38. Recognizing the need to robustly manage the emerging PFM reform program, the Office of the

President has endorsed MFR's request to establish PFM Reform Steering and Technical Committees. The decision was taken to repurpose the existing PEFA Steering and Technical Committees into the new managerial and technical level reform committees. The purposes of the reform committees will be to design and drive the reforms as well as coordinate the program with the development partners.

39. The Government appreciates that weaknesses remain and is thinking through an appropriate PFM reform program to address these challenges sequentially. In this regard, the Ministry of Finance and Revenue, together with the Ministry of National Planning and Economic Development, are intending to develop a PFM reform strategy based on technical inputs from this report, the recent IMF Public Finance Management Assessment, and the planned Public Expenditure Review. It must be stressed that the Government would need careful prioritization at each stage. Taking into account scarce capacity, Government should vigorously resist the temptation to overload the agenda.

40. It would be conceptually useful to define a short term and a medium term reform objective. The possible short-term objective could be conceptualized as *"Strengthen MFR's ability to manage the transition while addressing key regulatory gaps and laying the foundation for the future reforms."* The transition refers to the new developments in Myanmar, which is a complicated and transitional process that involves constitutional and economic reform that places new pressures on the PFM system. The regulatory gaps refer to key missing pieces and ambiguities in the PFM process that could be addressed quickly through interim measures.

41. ***Managing the transition*** should focus on the most immediate needs arising from the economic policy and public sector reforms underway. There are three top priorities. First, arrangements must be made to manage the separation of the CBM from the MFR. The MFR will need to deal with the public finance functions to which the CBM previously contributed (consolidate accounting statements and systems, debt management, cash flow management). Second, given that Myanmar's system is in a state of massive flux, a premium should be put on prudent risk management. The MFR would benefit from developing an analysis of fiscal risks emanating from the transition and mechanisms to address them (including SEE risks). For example, while current accounting systems will not permit a systematic risk analysis, a number of simple steps could be taken, including making lists of major contingent liabilities (which may or may not include valuations), quasi-fiscal operations of SEEs that could impact their performance and the budget, and tax expenditures. Similarly it would be important to start articulating clearly the central-local government fiscal relations system while incorporating measures to mitigate risks of contingent liabilities that may arise from borrowing by state and regional governments. Third, given Myanmar's wealth of natural resources, and its embrace of a more market-oriented economy, it is critical that policies and systems be established to strengthen regulation and management of natural resource revenue flows. Myanmar has already made an important start on strengthening governance of the natural resource sector by taking steps toward adoption of the Extractive Industries Transparency Initiative, which bodes well – but much more will be required to ensure that Myanmar captures its revenue potential in a sustainable way and that flows are channeled through government systems in a way that allows for transparency and accountability.

42. At the same time it would be important to ***address high priority gaps in the regulatory framework*** (mainly, improvements in financial regulations and minimum rules on procurement and internal audit) while commencing development of stronger overarching public finance legislation (e.g., a budget law) to be implemented over the medium term. For example, high priority gaps exist in procurement and internal audit, given the presidential instructions issued in 2012 ordering ministries to set up internal audit units and undertake competitive procurement. Ministries urgently need a modicum of guidance on minimal acceptable standards and processes in order to comply with the President's orders.

Similarly, another short term priority is building a stronger budget policy unit/function, which would include developing macroeconomic forecasting capacity, developing a fiscal policy framework, and strengthening prioritization of capital spending. This latter priority is also related to the expected growth of revenue, including from natural resources, from higher rates of economic growth as well as revenue policy (tax and non-tax) reforms.

43. ***Laying the foundation for future reform*** refers to the need to set up a management structure and develop tools needed to design and implement the reforms. A key first step, which the President's Office has authorized in early 2013, is establishing an executive reform committee and secretariat to prepare and lead a PFM reform program. Other critical elements of the reform program would include: a vision of reform (the system reform objectives for a 10 year period, say); detailed reform action plans (by PFM sub-system: expenditure, tax, procurement, external audit, etc.); a capacity development plan, including ICT; and a performance management framework (e.g., monitoring of selected PEFA PIs). It is also worth noting that the PFM reform program will have further implications for MFR organizational design (which will become apparent after reform program is developed), which would need to be addressed.

44. In a way the proposed approach –*"Strengthen MFR's ability to manage the transition while addressing key regulatory gaps and laying the foundation for the future reforms."* – is only really playing "catch up" with the fast moving realities of Myanmar today. The PFM reform program that Myanmar develops will need to carefully prioritize and sequence reform measures, given scarce capacity and the significant need for improvement across the board. The PEFA Performance Report indicates the need for strengthening across all areas of all PFM sub-systems. Obviously, all these areas cannot be addressed simultaneously. Nor does the Performance Report provide guidance about which areas to prioritize for reform. Rather, the diagnosis as to which PFM areas to address depends on country contextual factors, such as the level of capacity, policy objectives, macroeconomic conditions, and political economy constraints.

45. One approach to PFM reform sequencing is focusing on the basic functionalities of the system, and this may well be the best way to think about the reform program in Myanmar. "Getting the basics right first" provides some overarching guidance as to what should be done (as well as not done), but much more work needs to be done to arrive at a specific set of short- and medium-term priorities. Key contextual factors are Myanmar's decision to decentralize rapidly, which has already started, and its significant natural resource wealth, both of which must be taken into account when developing the logic of reform sequencing.

46. A "basics first" logic of prioritization could suggest the following four priorities: *First*, the credibility of the budget (defined as divergence between the budget plan and actual spending) is low, thus creating negative impacts on line ministry planning and service delivery. There are a number of reasons why credibility is low, including: the use of large (and late) supplementary budgets, weak revenue forecasting, limitations in public investment planning, and the lack of information on donor funded projects. These measures to strengthen budget credibility would increase reliability for Union ministries as well as the newly empowered states and regions. *Second*, management would benefit from incrementally better information on the budget and actual spending. Priorities here include: strengthening budget classification, providing some basic ICT functionality to plan, record, and analyze expenditure; strengthening the comprehensiveness of information provided in budget documentation; and enhancing oversight of fiscal risk (as discussed above). *Third*, building up some basic regulations and controls would help reduce fiduciary risk. Key measures here would include: strengthening taxpayer registration and assessment; strengthening procurement; and improving payroll controls. *Fourth*, making external oversight more robust would provide enhanced incentives for better public financial management. Key reform measures here would include: improving the quality and timeliness of in-year budget reports; further building up the scope and quality of external audits; and providing adequate technical support to the Parliamentary committees reviewing Government plans and

budgets. These four priorities are not meant to be definitive but rather suggestive. As noted in this report, a PEFA Performance Report, by itself, is not adequate to plan a PFM reform program. Much more work will be needed, but it is hoped that these suggestions provide some useful inputs to the Government as it commences the next steps in its reform process.

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