



Asian Regional Seminar on Public Financial Management

PFM Reforms: The lessons learnt -promises and tears

Session 4: Diagnostic tools
PEFA as Tool for PFM Reform

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World wide it is difficult to find a country that is not undertaking some PFM reform program—and also difficult to find a country satisfied with the results.

Typical complaints about reform programs:

- **Unrealistic in scope:** *cases of overloading*
- **Unrealistic in timing:** *systematic underestimation of the time required*
- **Not geared to country needs:** *danger of donors pushing their own solutions, “one size fits all” approach*
- **Politicians do not really support reform:** rather support the financing that comes with it

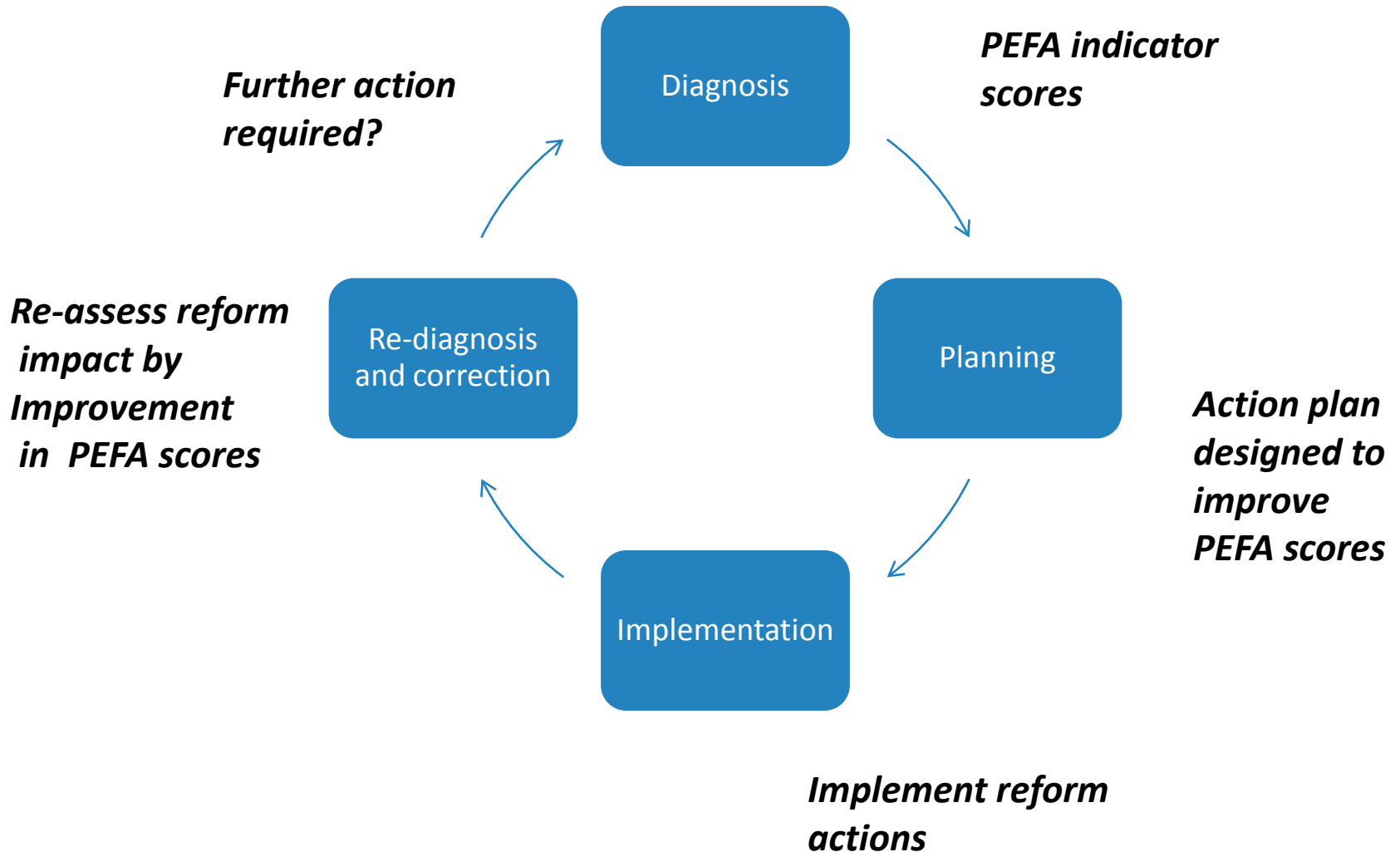
Many of these complaints have been directed at PEFA's influence on reform programming

PEFA—Public Expenditure and Financial Accountability—is *a major diagnostic tool*, widely adopted and promoted by donors & IFOs

- **Widely accepted**, technically supported and continually being improved
BUT concentrates on PFM functionality, weaker on non-technical aspects?
- **Comprehensive** in its approach to PFM
BUT still are important missing elements?
- **Reiterative** in its application, used to gauge progress in PFM reforms
BUT some PFM reforms often take a long time to have an impact?
- **A basis for increased donor financing**
BUT could lead to donor-led reforms with weak domestic support?

*Increasingly used as a **planning tool** for these reforms*

Diagram. 1 The PEFA based reform planning process



Why has this PEFA approach to reform been disappointing?

It is argued in this presentation there are weaknesses at all stages that often have not be recognized:

1. Weaknesses in diagnosis
2. Weaknesses in planning
3. Weaknesses in implementation
4. Failures in re-diagnosis and correction of prior mistakes/delays arising from weaknesses 1-3:

- Key functions neglected in the analysis--especially support functions
- Institutional, and political economy constraints to reform not addressed
- Management of the reform process neglected

Weaknesses in Diagnosis

Despite continual attempts it is not easy to move from PEFA indicators to a reform plan:

- PEFA are high level indicators, reform actions usually are more detailed
- PEFA indicators “indicate” a problem, need to find the reason for the problem before defining the solution (i.e. more analysis required—requires data that may not be available)
- PEFA is like a snapshot of the PFM system at a point of time: must distinguish difference in levels from movements between them (the true meaning of reform, ***and sidesteps the problem of implementation***)

Other doubts on PEFA's comprehensiveness in diagnosing PFM problems...

- **Can't see the forest for the trees**
 - misses the big picture because this is built up from individual indicators (bottom-up) with limited top-down analysis
- **Not all indicators are born equal**
 - some indicators (e.g. Pls2-4) are derivative, should they have equal analytical weight?; controversy over donor indicators and proposed deletion?
- **Often mistakes form for substance**
 - describes the PFM system from laws and regulations, what should be, not what is—in many countries informal systems dominate
- **Some PFM dimensions are missing, or not adequately covered ...**

Gaps in PEFA's coverage?

- Gaps recognized and proposed modifications: asset management; account reconciliation between treasury and MDAs; treatment of below-the-line accounts & special payment procedures, public investment management)
- higher order PFM functions pertaining to performance budgeting—most PIs cover basic financial compliance; while new more comprehensive indicators to deal with fiscal framework proposed, little on performance management issues
- support functions not adequately covered (--some coverage in descriptive sections—basic requirements for:
 - legal system
 - IT capacity
 - HR capacity
 - TA and financial support—partly captured by D indicators?

Weaknesses in planning

Many of the problems in employing PEFA as a planning tool arise from its strengths as a diagnostic tool:

- It is comprehensive, so indicators cover the whole PFM system
- It treats all indicators equally, ignoring their impact on the whole system

As a consequence *there is no guide for prioritization in planning reform actions.*

Often a developing country can have a large number of NA, D and C grades across all PFM functions—

How to choose between them?

Unfortunately often no choice is made

Result = overloaded and unmanageable reform action plans

Prioritization in the planning of PFM reforms:

Two popular approaches:

- “ **basics first approach**” –Schick

But how to define “basics” ?

Tomassi has recently empirically identify “basic” PFM levels for the PEFA indicators

- **the platform approach**– Brooke

Focuses on packages of reform activities of supporting measures, that once completed form the basis or “platform” to move on to a further package of complementary reforms

Often PEFA scores used to identify platforms, more explicitly with:

- **Quist** : gives empirical direction to the interdependency of reform activities of the platform approach
- **Andrews**: uses the PEFA assessments to divide countries into PFM levels, and asks what it takes to improve PEFA to move from one level to the next level, defining a development path or reform sequence

BUT these broad strategies are not detailed enough for an action plan

How to Prioritize within an action plan?

Different options used:

- **Tactical**

- choose reform activity that will easily show success, **but** “low lying fruit” may not be the most productive?

- **Weakest link first, for maximum impact on PFM system**

- identify bottlenecks and remove them first, **but** how to identify?

- **Timing required**

- choose reform activity to match the country’s feasible time horizon for successful implementation, **but** reforms nearly always underestimate the time required

- **Political demand**

- An approach that turns away from technical considerations, and may ensure local commitment, **but** has dangers....

A controversy in prioritization concerns political commitment--should the authorities' demands always dominate PFM priorities?

This, it is argued, will ensure maximum political commitment, BUT:

- what if the politician's choice is over-ambitious?
- what if choice is motivated more by politics or rent seeking rather than impact on PFM reform?
- What if this biases reforms: those that are highly visible or fast to implement (because politician's time horizon may be short)?
- what if a reform is associated with one figure that might change?

Weaknesses in the Implementation of PEFA-based action plans

Often implementation runs into difficulties caused by the above problems in diagnosis and planning:

- lack focus/priorities**
- missing key constraints**
- underestimating the degree of HR/TA/IT/time required**

But also failure to come to terms with the wider environment of PFM reform:

- institutional constraints**
- political economy constraints**

As a consequence in action plans there is not enough focus on change management skills to navigate/overcome these constraints--what can be termed the "soft side" of PFM reform

What is meant by the wider environment?

Three levels:

- At highest level, ***conditioning factors***: political environment; economic environment, socio-cultural and general governance environment; technological and capacity environment
- At middle level, factors that arise from ***the institutional design of the PEM system*** itself: critical relationships between legislative and executive branches; within the executive branch, the role of the MOF and its relationship to the MDAs/president's office/SNGs
- At the lowest level factors that arise from ***the internal structure of PFM organizations***, the managerial culture, the limitations of leadership and skills and other capacity constraints.

Implementation: the need to engineer change

Part of the action plan needs to address:

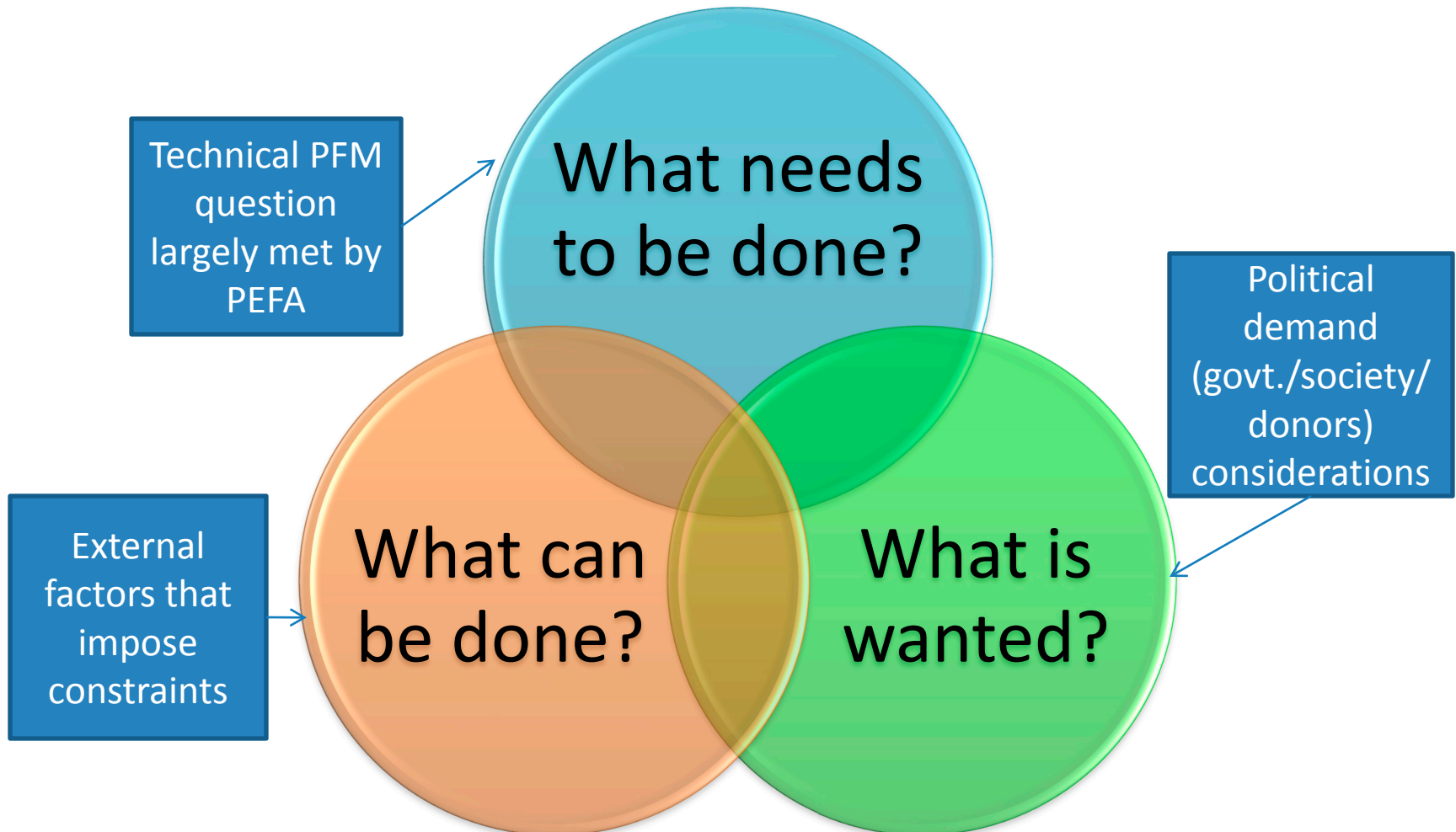
- the implementation strategy and
- the mechanics of implementation:

i.e. focused on managing the reform process as a whole rather than concentrating on individual reform actions (often the PEFA focus)

An important component of implementation strategy is the management of change...

But is often neglected

Success in Implementation involves aligning achievable reform options



Message? : Better Recognition of the Limitations of PEFA's role in reform.

- Cannot substitute for a detailed analysis of causes for weak indicators
- Cannot supply important information required for this analysis
- Cannot identify detailed reform actions required for improving indicator performance
- Cannot prioritize between these reform actions, i.e. determine sequence of reform
- Cannot determine the best implementation strategy or tactics

Recommended that PEFA not be overloaded: to inform, not determine reform actions