# SOUTHERN NATIONS AND NATIONALITIES PEOPLES' REGIONAL GOVERNMENT

# REPEAT PUBLIC EXPENDITURE AND FINANCIAL ACCOUNTABILITY ASSESSMENT (PEFA)

**June 2015**

**CURRENCY AND EXCHANGE RATES**

Currency unit = Ethiopian Birr (ETB)

US$ 1 = ETB 19.46 (as of April 24, 2014)

**Ethiopian Fiscal Year (EFY):** July 8–July 7

EFY 2005 = Gregorian FY 2013 (July 1, 2012–June 30, 2013)

In this document the term *FY* refers to the Gregorian fiscal year and is not the same as the term *EFY*.

**Support for this report was provided by:**

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# Acronyms and Abbreviations

| | |
|---|---|
| AFROSAI | African Organization of Supreme Audit Institutions |
| AGA | Autonomous Government Agency |
| ARG | Amhara Regional Government |
| BI | Budget Institutions (ministries, agencies, institutions, and other budgetary units) |
| BoA | Bureau of Agriculture |
| BoE | Bureau of Education |
| BoH | Bureau of Health |
| BoFED | Bureau of Finance and Economic Development |
| BRRC | Bureau of Rural Roads and Construction |
| CBE | Commercial Bank of Ethiopia |
| COFOG | Classification of Functions of Government |
| CSA | Central Statistics Agency |
| CTA | Consolidated Treasury Account |
| DSA | Debt Sustainability Analysis |
| EBO | Extra-budgetary Operation |
| EFY | Ethiopian Fiscal Year |
| EMCP | Expenditure Management and Control Program |
| ERCA | Ethiopian Revenue and Customs Authority |
| ETB | Ethiopian Birr |
| FAP | Financial Administration Proclamation |
| FY | Financial Year or Fiscal Year |
| GDP | Gross domestic product |
| GF | Global Fund |
| GFS | Government Finance Statistics, IMF |
| GPP | Grace Period Payables |
| GTP | Growth and Transformation Plan FYs 2010/11-2014/15 |
| ID | Inspection Department |
| IBEX | Integrated Budget and Expenditures |
| IFMIS | Integrated Financial Management Information System |
| IMF | International Monetary Fund |
| INTOSAI | International Organization of Supreme Audit Institutions |
| IPSAS | International Public Sector Accounting Standards |
| IT | Information Technology |
| JAICA | Japan International Cooperation Agency |
| MDG | Millennium Development Goals |
| MEFF | MacroEconomic and Fiscal Framework |
| MoE | Ministry of Education |
| MoFED | Ministry of Finance and Economic Development |
| MoH | Ministry of Health |
| MTEF | Medium-Term Expenditure Framework |
| NA | Not Applicable (in PEFA assessment) |
| NBE | National Bank of Ethiopia (Central Bank) |
| NGO | Non Governmental Organization |
| NR | Not Rated for lack of information |
| NS | Not Scored for lack of information |
| ORAG | Office of the Regional Auditor General |
| OFAG | Office of the Federal Auditor |
| PAC | Public Accounts Committee |
| PBS | Protection of Basic Services |
| PE | Public Enterprises |
| PEFA | Public Expenditure and Financial Accountability |
| PFM | Public Financial Management |

| | |
|---|---|
| PI | Performance Indicator (PEFA) |
| PPA | Public Procurement and Property Administration Agency |
| PSCAP | Public Sector Capacity Building Program |
| PSNP | Public Safety Net Program |
| RA | Revenue Authority |
| RFQ | Request for quotation |
| SCF | Save the Children's Fund |
| SNNPR | Southern Nations and Nationalities Peoples' Region |
| SNNPRS | Southern Nations and Nationalities Peoples' Regional State |
| SNNPRG | Southern Nations and Nationalities Peoples' Regional Government |
| SIGTAS | Standard Integrated Government Tax Administration System |
| TAC | Tax Appeal Commission |
| TISB | Trade and Industry Sector Bureau |
| TIN | Taxpayer identification number |
| TOR | Terms of Reference |
| TSA | Treasury Single Account |
| TVET | Technical and Vocational Education Training |
| UNDP | United Nations Development Program |
| UNESCO | United Nations Educational, Scientific, and Cultural Organization |
| UNFPA | United Nations Population Fund |
| UNICEF | United Nations Children's Fund |
| USAID | US Agency for International Development |
| ULGDP | Urban Local Government Development Program |
| VAT | Value-Added Tax |
| WaSH | Water, Sanitation, and Hygiene |
| WoFED | Woreda Offices of Finance and Development |
| WB | World Bank |
| YTD | Year-to-Date |
| ZoFED | Zonal Offices of Finance and Development |

# Summary Assessment

The first PEFA assessment of the Southern Nations and Nationalities Peoples' Regional Government (SNNPRG) occurred in FY 2010, and was one of six regional government assessments executed that year, overseen by the Ministry of Finance and Economic Development (MoFED) and financed by the EU. MoFED has also overseen this repeat assessment, financed by the World Bank.

PEFA assessments aim to provide an independent appraisal on the quality and performance of the public financial management systems (PFM) of the assessed governments. Repeat PEFA assessments address changes to PFM system performance, if any.

A summary of scores and explanation of performance changes in the PFM systems is provided in tables SA.1 and SA.2, at the end of this chapter. The performance indicators (PIs) and their various dimensions are explained fully, beginning in Chapter 3.

## *Summary*

Performance of the PFM system in the SNNPRG has improved in some ways and weakened in others since the FY 2010 PEFA assessment, in terms of PEFA scores:

- Scores increased for eight performance indicators (PIs): 1, 11, 13, 14, 16, 21, 27, and 28.
- Scores remained unchanged for 16 PIs: 4, 5, 7, 8, 9, 10, 15, 17, 18, 20, 23, 24, 25, D-1, D-2 and HLG- 1. Thirteen of these (PIs 4, 5, 8, 9,11,13,16, 17, 18, 20, 22, 28 and HLG-1) earned ratings of B and above in the 2010 assessment. Processes are underway to strengthen PI-7 (over-scored in 2010, reflected by an upward pointing arrow for the indicator.
- Scores fell for five PIs: 3, 6, 12, 22, and 26.
- The methodology has been changed for the measurements of PIs 2 and 19, and a comparison for scores is not possible.
- In terms of distribution, the number of scores above C+ (A, B+, B) totaled 15 in the FY 2010 (2010) assessment and 14 in the FY 2014 assessment, although at least two PIs were over-scored in 2010. This suggests a modest improvement.

## Budget Credibility

The budget appears credible in aggregate terms (PI-1) if allowance is made for Millennium Development Goals (MDG) fund-related advances for capital expenditure that were not retired prior to the end of the EFY 2004 and EFY 2005 (FY 2011/12 and FY 2012/13). If this allowance had not been made, the score for PI-1 would misleadingly have been D, not B.

Good revenue performance and the predictability of the block grant from MoFED have contributed to credibility. PI-3 (domestic revenue performance) scored C, but this appears to be due to data recording issues rather than performance *per se.* Taxpayer education programs, registration drives, and strengthening of the tax audit (PIs 13, 14) have contributed to strengthening performance. In particular, the introduction of block management schemes (PI-13 (ii)) is helping to strengthen voluntary compliance and thereby reduce the extent of tax arrears (PI-15). However, connectivity problems beyond the control of SNNPRG are hindering the roll out of the Standard Integrated Government Tax Administration System (SIGTAS) to woredas and the efficiency gains that would result. The FY 2010/11 establishment of city administrations with the power to earn and retain revenues also appears to have contributed to good revenue performance. The receipt of the block grant from MoFED is highly predictable. It comprises the bulk of SNNPRG's financial resources (HLG-1).

Budget preparation processes are strong when measured under PI-11. Whereas the budget appears to lack credibility in disaggregated terms, with PI-2 scoring C, SNNPRG considers the mid-year adjusted budget as more credible as a measure of budget credibility. One reason to place more emphasis on the mid-year adjusted budget is that estimates of this year's domestic revenue outcomes and of financial resource availability for the next year's budget are uncertain at the time of budget preparation, particularly in terms of external resources. Moreover, cost estimates and implementation rates are difficult to estimate precisely in advance. By the time of the mid-year review, it becomes clear which budget-related government institutions (BIs) are underperforming and which are performing well. Following consultation with BIs, the Bureau of Finance and Economic Development (BoFED) can then reallocate budgets between BIs and allocate the expenditure contingency where needed.

Current budget preparation processes enable further strengthening by establishing a medium term perspective to budgeting (currently a low rating for PI-12). A medium-term perspective to budgeting would strengthen the linkages between spending and policy objectives and improve cost and revenue estimates related to the annual budget preparation process. The Federal Government is piloting a program budgeting framework in SNNPRG (the only Regional Government where this is being piloted). Capacity constraints have slowed the pace of adoption of this framework.

Budget execution systems continue to support budget credibility by making financial resources available for spending according to the budget when needed and preventing significant payments arrears and misuse of funds. BIs are able to commit funds over several months with a high degree of assurance that funds will be available for payments. This has been facilitated by robust cash flow forecasting (PI-16) and cash management (TSA-Z account system, PI-17); strong internal controls (PIs 18-20); good domestic revenue performance (as noted above); the in-year predictability of the block grant from the Federal Government(HLG-1); and minimal fiscal risk posed by public enterprises and woreda governments (PI-9, see below). Open tendering is now the norm for procurement, which helps to keep costs within budget.

## Internal controls and audit

(i) Payroll controls (PI-18) appear to be robust under all dimensions, with an overall score of B+.

(ii) Expenditure commitments (PI-20 (i)) are formally controlled by BIs according to the remaining uncommitted ("unencumbered") budget balance, as specified by the Financial Administration Proclamation. Commitments with a time horizon for payments up to three months are also controlled by the rolling monthly cash expenditure limits derived from the cash flow forecasting system (PI-16 (i)). Proposed commitments with a longer-term payments horizon (e.g. bulk purchases, capital projects) are formally controlled according to the remaining uncommitted budget balance. However, the timing of the associated payments is covered by BIs' cash flow forecasts, which govern the cash expenditure limit for the months for which payments are due.

(iii) The other non-payroll internal control systems are comprehensive (PI-20 ii-iii). BIs have improved their understanding of internal control systems in recent years with the issuance of guidelines and by running frequent training programs for staff. High employee turnover, including for trained staff, necessitates more frequent training to familiarize staff with pertinent rules and regulations. While rules and regulations are generally respected, the Office of the Regional Auditor General (ORAG), Inspection Department in BoFED and Internal Audit report cases of noncompliance. Managers of BIs sometimes resist implementing audit recommendations.

(iv) Improvements to the procurement system have improved cost controls and, consequently, budget credibility. A major change since the 2010 assessment was the establishment of the Public Procurement and Property Administration Agency (PPA) in early FY 2012/13 in place of the Core Process in BoFED. Most procurement is now conducted through open competition (PI-19). BIs are beginning to publicize tender results and procurement plans, as well as bidding opportunities. In addition, BIs are reporting procurement operations to PPA, which has established a procurement audit system. The Financial Administration Proclamation provided for the establishment of a Complaints Review Board (CRB) under the BoFED, but the Board does not appear to be fully independent of the procurement process.

(v) The internal audit function has made little progress since the 2010 assessment, when it was still in an early stage of development. Retention of skilled staff is an issue. This does not necessarily jeopardize the current strength of internal control systems, but their long-term viability is not assured (PI-21).

(vi) Potential fiscal risk posed by government entities not included in the budget appears to be low (PI-9). The Regional Government owns only a handful of enterprises, and they do not require government subsidies. Their finances are monitored by parent bureaus and by BoFED. BoFED also closely monitors the financial situation of zonal governments (the level of government below the Regional Government), and zonal governments monitor the financial situation of woreda governments.

## Comprehensiveness and transparency of the budget

The SNNPRG prioritizes strengthening fiscal transparency. The Fiscal Transparency and Accountability Program (FTAP), established by the Federal Government in FY 2006/07 (EFY 1999), has been the main vehicle for strengthening transparency, and the General Education Quality Improvement Program (GEQIP) is another. While transparency has improved, this is not yet fully reflected in the ratings.

Despite considerable improvement, lack of transparency detracts from budget credibility. Inadequate transparency provides scope for misallocation of resources. The ability of the public (including the Regional Council) to hold the Regional Government to account for its expenditures is lower than it could be (low ratings for PIs 6, 7, 23, 24 and 25), though performance has strengthened significantly under PI-10 (availability of fiscal information to the public). Robust credibility requires that the Regional Government publicize all planned and actual spending on goods and services for which it has a mandate to provide via proclaimed budgets, budget execution reports, and annual financial statements. The draft budget document could contain far more information (PI-6), and a greater range of other fiscal information could be made available to the public in a timely manner, for example, ORAG audit reports and service delivery reports. (PI-10, PI-23).

The transparency of development partner (DP) funding of projects and programs is also problematic. Significant DP funding is embedded in MoFED's block grant to SNNPRG, by virtue of DP support to the Protection of Basic Services (PBS) program in the form of budget support. By definition, this is transparent. However, there is limited information available to the public on DP-funded projects and programs that are implemented under the auspices of SNNPRG (PI-7), though the situation is improving. DP support to SNNPRG in this form should ideally be reflected in its proclaimed budgets, executed through the Government's standard budget execution procedures, and reported on and accounted for.

The most that seems to happen, however, is that some DP-funded projects (Channel 1b, whereby DPs provide assistance directly to BoFED) are included in proclaimed budgets and, starting in FY 2013/14 (EFY 2006), in budget execution reports. Spending has been reported on separately and less transparently than for the spending of SNNPRG's own resources. The total amount is very small relative to total government expenditure, so non-transparency in this area is of limited significance, but as a matter of principle, the spending should be reported on more transparently.

Some DP funds are channeled to sector bureaus via sector Federal Government line ministries (Channel 2a). The spending of these funds should be covered by the budgets of these ministries, but it is not clear that this is the case.

Planned and actual spending under "Channels 2b and 3" projects and programs (DPs that bypass BoFED and provide assistance direct to sector bureaus or to projects and programs) are not included in SNNPRG's annual budgets and budget execution reports. BoFED claims that such assistance represents only a small proportion of total assistance to Southern Nations and Nationalities Peoples' Regional State (SNNPRS), but this is difficult to verify. Transparency has improved with regard to NGO operations, which now must report to BoFED, but such reporting remains incomplete.

A number of DP-funded projects and programs, such as the Public Safety Net Project (PSNP), are being implemented in SNNPR under the Federal Government's budget. The funds are channeled to MoFED through Channel 1a. This raises a transparency issue, since the public services being delivered under these projects fall under the mandate of SNNPRG and ideally should be part of SNNPRG's budget.

*Accounting and reporting systems:* In the interests of budget credibility, SNNPRG's accounting and reporting systems should be as accurate, comprehensive and transparent as possible. These systems are generally robust, with the help of integrated budget and expenditures (IBEX). However, DPs only began using SNNPRG's accounting and reporting systems in FY 2013/14 (EFY 2006) and in-year budget execution reports and annual financial statements (PIs 24-25) remain incomplete. Delays in clearing bank accounts and suspense accounts and advances (PI-22) have also resulted in incomplete annual financial statements.

*External audit and legislative oversight (PIs 26-28):* These functions are an important mechanism for holding the Government to account and thus contribute to budget credibility and transparency. The external audit function (PI-26) was relatively weak at the 2010 assessment and is even weaker now. The scope of audit remains at just 50 percent of expenditure; timeliness in the preparation of audit reports has worsened; and BI implementation of audit recommendations remains incomplete. Retention of skilled staff is a challenge.

On the other hand, the legislative oversight function has strengthened, and may provide some impetus to strengthen the external audit function (PIs 27, 28). The process for reviewing the draft budget (PI-27) has also improved due stronger review procedures and allotment of adequate time for review. PI-28 scored high (B) in the 2010 assessment, and its performance has improved with regard to the extent of hearings on audit reports and BIs' follow-up on the implementation of Regional Council recommendations.

## Crosscutting issues

*Capacity constraints:* Significant rates of staff turnover are exacerbating capacity constraints and limiting SNNPRG's ability to implement PFM reforms. Skilled staff members often leave for significantly higher salaries and better working conditions in the private sector and DP agencies. The problem seems particularly acute in relation to the internal and external audit functions (PIs 21, 26).

*Connectivity issues:* Internet connectivity seems to be much worse than four years ago, bur this is a nationwide issue beyond the control of SNNPRG. Sector bureaus are still not hooked up electronically to BoFED through IBEX, so IBEX is being used on a stand-alone basis in bureaus, which hinders the generation of budget execution reports and accounts. The timely availability of fiscal information to the public has declined. The expansion of SIGTAS (Standard Integrated Tax Administration System) has also slowed, hindering strengthening of revenue administration under PIs 14 and 15.

**Assessment of the Impact of PFM Weaknesses**

*Aggregate fiscal discipline:* Aggregate fiscal discipline is good, as implied by the fiscal outcome table (Table 2.1) in Chapter 2, which shows fiscal balances close to zero. The reliable and timely receipt of the block grant from MoFED, comprising the bulk of SNNPRG's financial resources, supports aggregate fiscal discipline, but robust expenditure controls are also an important factor. Routine monitoring of the financial situation of state-owned enterprises and woreda governments helps to contain any possible fiscal risk posed by these entities (Pl-9) which could put pressure on fiscal discipline.

*Strategic allocation of resources*: The absence of a medium-term perspective to budgeting is hindering the rational strategic allocation of resources (PI-12). As a first step, forward expenditure estimates need to be prepared, showing the projected costs of implementing current levels of service in the future. Fiscally realistic costed sector strategic plans are also needed as the basis for allocating financial resources to 'new' spending above the forward estimates.

*Operational efficiency*: Internal control systems appear to be generally robust (B and B+ ratings for PIs 18 and 20), and support operational efficiency by lowering the risk of wasteful spending and diversion of funds. Competitive bidding is now the norm for procurement operations (PI-19).

## PFM Reform Program

The MoFED-led Expenditure Management and Control Program (EMCP) continues to serve as the main vehicle for implementing PFM reforms at all levels of government. A PFM reform-specific donor group, co-chaired at the time of the assessment by DFID and the World Bank, liaises closely with MoFED and organizes financial and technical assistance to support EMCP implementation. The Joint Budget and Aid Reviews (JBAR) provide a further monitoring and coordinating platform for federal and Regional Governments and donor partners to review the reform plans and achievements and to resolve issues.

Sections 2, 3 and 4 elaborate on key PFM reforms being implemented over the last few years.

## Role of Development Partners

Apart from playing an important role in supporting PFM reform, development partners (DPs) also finance numerous projects and programs to help improve the regions' provision of basic services. Most financing is channeled through the Protection of Basic Services (PBS) program, which involves budget support integrated with the block grants that MoFED provides to Regional Governments. Regional Governments then budget and spend the funds using their PFM systems. Such financing was significantly supplemented through the establishment of the MDG grant in FY 2011/12.

As noted, the DP aid provided through the Channel 2 and Channel 3 programs creates some transparency problems, as indicated by low scores for PI-7 (ii) and D2–D3. This situation has recently started to improve. For example, BoFED now requires NGOs to register and submit operational and financial reports for monitoring purposes. However, a BoFED report indicated that planned operations of NGOs in SNNPR were not actually executed.

Such non-transparency can harm the planning and budgeting efforts of regional and woreda governments due to segmentation of these efforts into two sets of budgets rather than having one unified budget. As noted under 'Cross Cutting Issues" above, it can also retard capacity development in regional and woreda governments due to skilled personnel being lured away from government by higher salaries. Strong institutional and human resource capacity are pre-requisites for the success of PFM reforms (and governance reforms in general), so erosion of such capacity may harm the PFM reform effort.

## Table SA.1 PEFA Performance Indicators for the SNNPRG (FY 2010-2014)

| | **A. PFM OUT-TURNS: Credibility of the budget** | **Score 2010** | **Score 2014** |
|---|---|---|---|
| PI-1 | Aggregate expenditure outturn compared to original approved budget | **D** | **B** |
| PI-2 | Composition of expenditure outturn compared to original approved budget | **D+** | **D+** |
| PI-3 | Aggregate revenue outturn compared to original approved budget | **C** | **D** |
| PI-4 | Stock and monitoring of expenditure payment arrears | **B+** | **B+** |
| | **B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency** | **Score 2010** | **Score 2014** |
| PI-5 | Classification of the budget | **B** | **B** |
| PI-6 | Comprehensiveness of information included in budget documentation | **C** | **D** |
| PI-7 | Extent of unreported government operations | **B** ***(dimension (ii) over-scored)*** | **D+↑** ***(no change)*** |
| PI-8 | Transparency of intergovernmental fiscal relations | **A** | **A** |
| PI-9 | Oversight of aggregate fiscal risk from other public sector entities | **A** | **A** |
| PI-10 | Public access to key fiscal information | **C** | **C** |
| | **C. BUDGET CYCLE** | **Score 2010** | **Score 2014** |
| | **C (i) Policy-Based Budgeting** | | |
| PI-11 | Orderliness and participation in the annual budget process | **B+** | **A** |
| PI-12 | Multiyear perspective in fiscal planning, expenditure policy and budgeting | **C** | **D+** |
| | **C (ii) Predictability & Control in Budget Execution** | | |
| PI-13 | Transparency of taxpayer obligations and liabilities | **B↑** | **A** |
| PI-14 | Effectiveness of measures for taxpayer registration and tax assessment | **C+↑** | **B↑** |
| PI-15 | Effectiveness in collection of tax payments | **D+↑** | **D+** |
| PI-16 | Predictability in the availability of funds for commitment of expenditures | **B+** | **A** |
| PI-17 | Recording and management of cash balances, debt and guarantees | **B** | **B+** ***(no change, revised scope)*** |
| PI-18 | Effectiveness of payroll controls | **B+** | **B+** |
| PI-19 | Competition, value for money and controls in procurement | **NA** | **C+↑** ***(revised methodology)*** |
| PI-20 | Effectiveness of internal controls for non-salary expenditures | **B** | **B** |
| PI-21 | Effectiveness of internal audit | **C** | **C+** |
| | **C (iii) Accounting, Recording and Reporting** | | |
| PI-22 | Timeliness and regularity of accounts reconciliation | **B+** | **C+** |
| PI-23 | Availability of information on resources received by service delivery units | **B** ***(should have been C)*** | **C** ***(no change)*** |
| PI-24 | Quality and timeliness of in-year budget reports | **C+↑** | **C+** |
| PI-25 | Quality and timeliness of annual financial statements | **C+↑** | **C+** |
| | **C (iv) External Scrutiny and Audit** | | |
| PI-26 | Scope, nature and follow-up of external audit | **C+** | **D+** |
| PI-27 | Legislative scrutiny of the annual budget law | **D+** | **C+** |
| PI-28 | Legislative scrutiny of external audit reports | **B** | **A** |
| | **D. DONOR PRACTICES** | **Score 2010** | **Score 2014** |
| D-1 | Predictability of direct budget support | **NA** | **NA** |
| D-2 | Financial information provided by donors for budgeting and reporting on project and program aid | **D+** | **D+** |
| D-3 | Proportion of aid that is managed by use of national procedures | **D** | **At least C** ***(no change, under-scored in 2010 assessment)*** |
| HLG-1 | Predictability of transfers from higher-level government | **A** | **A** |

**Table SA.2 PI Ratings and Reasons for Performance Change**

| | **Budget Credibility** | **Score 2010 PEFA** | **Score 2014 PEFA** | **Performance change** |
|---|---|---|---|---|
| PI-1 (M1) | Aggregate expenditure outturn compared to original budget | **D** | **B** | **Performance improved.** Actual expenditure deviated from budgeted expenditure by -8.9%, -9.86% and -1.5% in FYs 2010/11, 2011/12 and 2012/13 respectively. The recorded actual expenditures in FY 2011/12 and FY 2012/13 have been adjusted for the large size of the unretired advances to contractors and suppliers for implementation of MDG Fund-financed projects. The extent of improvement may be overstated since the quality of the FY 2006/07- FY 2008/09 expenditure data seems suspect. |
| PI-2 (M1) | Composition of expenditure outturn compared to original budget | D+ *(i) D* *(ii) A* *(new method)* | **D+** **D** (i) D (ii) A | **No change.** Variance in expenditure composition exceeded 15% in at least 2 of the last 3 years. The adjusted budget later in the year appears to be regarded as the real budget. |
| PI-3 (M1) | Aggregate revenue outturn compared to original approved budget | **C** *(revised method)* *A, old method)* | **D** | **Performance reduced**. Actual revenue exceeded budgeted amounts by 281%, 2841% and 25% in FYs 2010/11, 2011/12 and 2012/13 respectively. The performance reflects data recording errors as well as estimation errors. |
| PI-4 (M1) | Stock and monitoring of expenditure payment arrears | **B+** (i) A (ii) B | **B+** **(**i) A (ii) B | **Performance unchanged.** Grace Period Payables were virtually zero at the end of the first month of the new FY. Most recurrent expenditure month-end payables are paid off the following month, including at the end of the FY. IBEX does not contain an age profile of these (dimension (ii)). |
| | **B. Comprehensive-ness and Transparency** | **Score 2010 PEFA** | **Score 2014 PEFA** | **Performance changes** |
| PI-5 (M1) | Classification of the budget | **B** | **B** | **Performance unchanged.** Budget formulation and execution is based on functional, sub-functional, administrative, and economic classification. The sub-functional classification is similar to COFOG's functional classification. |
| PI-6 (M1) | Comprehensiveness of information included in budget documentation | **C** | **D** | **Performance deteriorated.** Three of the 8 applicable information items (1, 6, and 8) were included in the draft Budget Proclamation for FY 2010/11 (EFY 2003) but not in the proclamation for FY 2013/14 (EFY 2006). |
| PI-7 (M1) | Extent of unreported government operations | **B** (i) B (ii) B | **D+↑** (i) A (ii)D↑ | **Performance unchanged. Information on DP operations continues to be deficient.** **(i)** ***No change.*** The scope in the 2010 assessment included DP funding channeled to BoFED through the Federal Government, which may or may not constitute an EBO. Analytically, however, it is more convenient to assess such funding under dimension (ii). **(ii)** ***No change.*** The rating in the 2010 assessment appears too high**.** BoFED has little information on donor projects being funded through Channel 3. |

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|---|---|---|---|---|
| | | | | USAID, a major DP, uses Channel 3 for all its operations. The annual reports on NGO projects prepared by BoFED do not include their actual annual expenditures.<br><br>The actual expenditures of DP-funded projects that are included in Budget Proclamations under Channel 1b are now being reported on through IBEX, hence ↑. |
| | | | | |
| | **B. Comprehensive-ness and Transparency** | **Score 2010 PEFA** | **Score 2014 PEFA** | **Performance changes** |
| PI-8 (M2) | Transparency of Intergovernmental Fiscal Relations | **A**<br>(i) A<br>(ii) B<br>(iii) A | **A**<br>(i) A<br>(ii) B<br>(iii) A | **No change,** but the introduction of a more rigorous way of assessing expenditure needs of sub-national governments has strengthened transparency under dimension (i). |
| PI-9 (M1) | Oversight of aggregate fiscal risk from other public sector entities | **A** | **A** | **No change.** |
| PI-10 (M1) | Public access to key fiscal information | **C** | **C** | **Performance unchanged in terms of rating, but improvement under information element (v) on publicizing of contract awards**. Internet connectivity issues beyond the control of SNNPRG constrained the timely posting of information on its websites. |
| | **C. BUDGET CYCLE** | **Score 2010 PEFA** | **Score 2014 PEFA** | **Performance changes** |
| | **C (i) Policy-Based Budgeting** | | | |
| PI-11 (M2) | Orderliness and participation in the annual budget process | **B+**<br>(i) A<br>(ii) A<br>(iii) C | **A**<br>(i) A<br>(ii) A<br>(iii) B | **Performance slightly improved under (iii)** on timeliness of submission of draft budgets to Regional Council. |
| PI-12 (M2) | Multiyear perspective in fiscal planning, expenditure policy and budgeting | **C**<br>(i) C<br>(ii) NA<br>(iii) C<br>(iv) C | **D+**<br>(i) D<br>(ii) NA<br>(iii) D<br>(iv) C | **Performance fell under (i) and (iii)**. The MEFF and costed sector strategies are not being prepared, partly due to capacity constraints. |
| | **C (ii) Predictability & Control in Budget Execution** | | | |
| PI-13 (M2) | Transparency of taxpayer obligations and liabilities | **B↑**<br>(i) B↑<br>(ii) B↑<br>(iii) B↑ | **A**<br>(i) A<br>(ii) A<br>(iii) A | **Performance improved under all three dimensions** (transparency of tax legislation, taxpayers' education, appeals mechanism). The rating for (iii) in 2010 was too high. |
| PI-14 (M2) | Effectiveness of measures for taxpayer registration and tax assessment | **C+↑**<br>(i) B<br>(ii) B<br>(iii) C↑ | **B↑**<br>(i) B↑<br>(ii) B<br>(iii) B | **Performance strengthened under (iii) and is in the process of strengthening under (i) and (ii).**<br>(i) Introduction of biometric finger printing system and strengthening taxpayer education/services, particularly through the new block management system.<br>(ii) Introduction of penalty waiver scheme. |

| | | | | |
|---|---|---|---|---|
| | | | | (iii) Introduction of audit plans, greater focus on risk as criterion for auditee selection, and sharp increase in the number of auditors led to a near tripling of revenue recovery. |
| PI-15 (M1) | Effectiveness in collection of tax payments | **D+↑**<br>(i) NS<br>(ii) C↑<br>(iii) D | **D+**<br>(i) C<br>(ii) A<br>(iii) D | **Performance unchanged, the limiting factor still being the D rating for (iii) on the reconciliation process**. A tax arrears recording system has been introduced since the last assessment (SIGTAS & manual ledgers), enabling the scoring of (i). Since SIGTAS is not fully functioning at present, manual reconciliation is logistically too difficult.<br>Dimension (ii) in the FY 2010 assessment appears to have been underscored. |
| PI-16 (M1) | Predictability in the availability of funds for commitment of expenditures | **B+**<br>(i) B<br>(ii) A<br>(iii) B | **A**(i) A<br>(ii) A<br>(iii) A | **Performance improved under (i) and (iii).**<br>*(i)* Cash flow forecasts prepared by BIs & updated monthly (quarterly in FY 2010 PEFA).<br>*(ii)* BIs can commit expenditures with payment time horizons up to end-year.<br>*(iii)* Reallocations between BIs are agreed between BoFED and BIs once or twice a year through a consultative review process, the adjustments being made through the mid-year adjusted budget. |
| PI-17 (M2) | Recording and management of cash balances, debt and guarantees | **B**<br>(i) NA<br>(ii) B<br>(iii) NA | **B+**<br>(i) NA<br>(ii) B<br>(iii) A | **Performance unchanged.**<br>*(i)* SNNPRG does not borrow, though new Financial Administration Procurement allows it to.<br>*(ii)* SNNPRG's consolidated cash position excludes balances of DP-held accounts.<br>(*iii*) Should have scored A in the FY 2010 assessment in relation to SNNPRG guarantees on bank loans to agricultural coops. |
| PI-18 (M1) | Effectiveness of payroll controls | **B+**<br>(i) B<br>(ii) A<br>(iii) A<br>(iv) B | **B+**<br>(i) B<br>(ii) A<br>(iii) A<br>(iv) B | **Performance improved under dimension (iv), which seems to have been scored too high in 2010 assessment.**<br>*(i)* Reconciliation in BIs between personnel records and payroll.<br>*(ii)* Timeliness of adjustments to payroll due to changes in personnel records.<br>*iii)* Strength of controls over changes<br>*(iv)* Existence of payroll audits. |
| PI-19 (M2) | Competition, value for money and controls in procurement | **NA**<br>*(Method revised: C +score under old method)* | **C+↑**<br>(i) B<br>(ii) A<br>(iii) C↑<br>(iv) D | **The scores are not comparable with those in 2010, due to revised methodology.**<br>(i) Legal framework: 4 of 6 benchmarks met.<br>(ii) More than 80% of contracts above the threshold were bid through open competition.<br>(iii) Two out of 4 procurement information elements are routinely publicized (bidding opportunities, contract awards). The other 2 elements (procurement plans, complaints resolutions are increasingly being publicized.<br>(iv) A Complaints Review Board is in place, but is not independent of the regulatory body (PPAAA). |
| PI-20 (M1) | Effectiveness of internal controls for non-salary | **B**<br>(i) B<br>(ii) B | **B**<br>(i) B<br>(ii) B | **Performance unchanged.**<br>(i) Expenditure commitment controls;<br>(ii) Understanding of other internal controls; (iii) |

| | | | | |
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| | expenditures | (iii) B | (iii) B | Compliance with internal controls**.** |
| PI-21 (M1) | Effectiveness of internal audit | **C**<br>(i) C<br>(ii) C<br>(iii) C | **C+**<br>(i) C<br>(ii) B<br>(iii) C | **Performance improved** in terms of the frequency of reports (ii). High staff turnover and little support by management to the IA function have constrained improvement under dimensions (i) and (iii). |
| | **C (iii) Accounting, Recording and Reporting** | **Score 2010** | **Score 2014** | **Performance changes** |
| PI-22 (M2) | Timeliness and regularity of accounts reconciliation | **B+**<br>(i) B<br>(ii) A | **C+**<br>(i) C<br>(ii) B | **Performance declined under both dimensions on bank account and on suspense account/c and advance reconciliation.** |
| PI-23 | Availability of information on resources received by service delivery units | **B** | **C** | **Performance unchanged.** The FY 2010 rating should have been C. Tracking of resources received by service delivery units has improved through GEQIP and FTAP, but formal reports are not yet prepared. |
| PI-24 (M1) | Quality and timeliness of in-year budget reports | **C+↑**<br>(i) C↑<br>(ii) A<br>(iii) B ↑ | **C+**<br>(i) C<br>(ii) A<br>(iii) B | **Performance unchanged overall, but the quality of reports has improved.**<br>*(i)* Expenditure commitments & DP operations still not reported on as part of budget performance reports.<br>*(ii)* Timeliness has improved due to IBEX roll out.<br>*(iii)* Quality improved due to roll out of IBEX, but data issues remain, as indicated in ORAG reports. |
| PI-25 (M1) | Quality and timeliness of annual financial statements (AFS) | **C+↑**<br>(i) B↑<br>(ii) B<br>(iii) C↑ | **C+**<br>(i) B<br>(ii) A<br>(iii) C | **No overall change, but improvement on timeliness of submission of statements to ORAG.**<br>(i) Information on revenue arrears and expenditures financed by DPs through Channel 1b (funding to BoFED direct) is missing.<br>(ii) Timeliness of AFS slightly improved, though rating unchanged.<br>(iii) No change. AFS not yet prepared according to International Public Sector Accounting Standards (IPSAS). |
| | **C (iv) External Scrutiny and Audit** | **Score 2010 PEFA** | **Score 2014 PEFA** | **Performance changes** |
| PI-26 (M1) | Scope, nature and follow-up of external audit | **C+**<br>(i) C<br>(ii) B<br>(iii) B | **D+**<br>(i) C<br>(ii) D<br>(iii) B | **Overall performance reduced under dimension (ii)**<br>*(i) Scope*: Performance unchanged. Coverage of last audit (on EFY 2004) was 51% of expenditure.<br>*(ii) Timeliness*: Performance fell sharply. The fall is sharper than the 2010 score shows; this should have been A.<br>*(iii) Auditee follow-up: Performance unchanged* The rate of follow-up by auditees on implementation of agreed remedial actions is low, despite establishment of a follow-up unit in ORAG. The way the scoring criterion is formulated makes the situation look better than it is. |

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| | | | | Capacity constraints and insufficient support from BI managers limit the pace of improvement. |
| PI-27 (M1) | Legislative scrutiny of the annual budget law | **D+**<br>(i)A<br>(ii) C<br>(iii) D<br>(iv) B | **C+**<br>(i) C<br>(ii) B<br>(iii) C<br>(iv) B | **Improvement under dimension (ii) on procedures for review of the draft budget and dimension (iii) on the adequacy of time for review of the draft budget.** Dim. (i) on scope of the legislature's scrutiny should have been C in the 2010 assessment, indicating no change since then. |
| PI-28 (M1) | Legislative scrutiny of external audit reports | **B**<br>(i) B<br>(ii) B<br>(iii) B | **A**<br>(i) A<br>(ii) A<br>(iii) A | **Performance improved under dimensions (ii) and (iii)** on extent of hearings on audit reports and extent of follow-up on implementation of Regional Council recommendations. Dim. (i) appears underscored in the 2010 assessment**.** |
| | **D. DONOR PRACTICES** | **Score 2008 PEFA** | **Score 2013 PEFA** | **Performance changes** |
| D-1 (M1) | Predictability of Direct Budget Support | NA | **NA** | SNNPRG does not receive budget support. |
| D-2 (M1) | Financial information provided by donors for budgeting and reporting on project and program aid | **D+**<br>(i) C<br>(ii) D | D+<br>(i) D<br>(ii) C | **No change.**<br>(i) Channel 2 DPs (DPs to BoFED) are no longer providing estimates of aid for next year's budget.<br>(ii) Channel 1b project units prepare quarterly reports, but not, until FY 2013/14, using IBEX codes; these are being converted from DP codes using a protocol. The score is not comparable against the FY 2010 score, which was based on Channel 2 projects as well as Channel 1b projects. |
| D-3 (M1) | Proportion of aid that is managed by use of national procedures | **D** | **At least C** | **No change.** The rating in FY 2010 was underscored, as it did not take into consideration the amount of DP budget support contained in the block grant from MoFED to BoFED. |
| HLG-1 | Predictability of block grant from MoFED | A<br>(i) A<br>(ii) NA<br>(iii) A | A<br>(i) A<br>(ii) NA<br>(iii) A | **Performance unchanged** |

# 1. Introduction

## *1.1 Background and Objectives*

The first PEFA assessment of the Southern Nations and Nationalities Peoples' Regional Government(SNNPRG) occurred in FY 2010, and was one of six Regional Government assessments executed that year (the others were Oromia, Amhara, Benizshangul-Gumuz and Harari regions and Addis Ababa City). A Federal Government assessment was carried out at the same time. The Ministry of Finance and Economic Development (MoFED) oversaw the assessments, which were financed by the EU.

MoFED has also overseen this assessment, which is financed by the World Bank. The assessment is a repeat in some jurisdictions (national government; Addis Ababa City; Oromia Regional Government; Amhara Regional Government; and SNNPRG), and new in others (Tigray and Somali Region). The SNNPRG assessment is the last of the seven assessments conducted in total.

PEFA assessments aim to provide an independent appraisal of the quality and performance of the public financial management systems (PFM) of the assessed governments. Repeated PEFA assessments address changes to PFM system performance, if any. The assessments inform both ongoing PFM reforms supported through the EMCP, and new PFM initiatives, such as the request from MoFED to the World Bank to begin preparation for a separate PFM project. Assessments may also advise proposed projects related to tax administration, audit, and transparency to be funded by DFID.

## *1.2 Scope*

The 2014 PEFA assessment covers the SNNPRG, which consists of a number of bureaus, institutions, and authorities. As was the case with the 2010 assessment, it does not cover the PFM systems of zonal administrations, which represent a separate and lower level of government; nor does it cover woreda and city administration governments, which constitute a third level of government. Together these three levels of government constitute the Southern Nations and Nationalities Peoples' Regional State (SNNPRS).

SNNPRG expenditures comprise about 27 percent of SNNPRS expenditures, as indicated in the FY 2012/13 (EFY 2005) Budget Proclamation. These include expenditures under the MDG Fund, which was established in FY 2011/12 (EFY 2004) and totaled ETB 4 billion in the FY 2012/13 (EFY 2005) budget, or 19 percent of the total SNNPRS budget.

PIs 8-9 of the PEFA Framework (Chapter 3) assess the fiscal relations between SNNPRG and the zonal administrations and the extent to which SNNPRG monitors zonal administrations' financial situations. These assessments do not cover the PFM systems of the three SNNPRG-owned public enterprises, but do address the extent that SNNPRG monitors their financial situation (PI-9). The SNNPRG has not prepared a consolidated table of SNNPRS expenditures that included those of public enterprises.

In some instances, the reference point for this assessment is the SNNPRS, since information is only available at this level. The instances are: (i) Table 2.1 and 2.2 in Chapter 2 on Fiscal Outcomes; (ii) PI-4 and Table 3.4 on expenditure arrears; (iii) PI-25 on annual financial statements; and PI-26 on external audit. The scope of legislation refers to the SNNPRS level (e.g. Financial Administration Proclamation), but tends to be implemented separately at SNNPRG, zonal administration and woreda levels. Institutions are named at regional state level, even if they are responsible for the Regional Government level (e.g. SNNPRS Revenue Authority). In general, the reference point is SNNPRG, unless otherwise specified. A World Bank-funded PFM assessment of a sample of 36 woreda governments in five regions and Addis Ababa City was conducted in FY 2011.

## 1.3 The Assessment Process

Fieldwork was conducted from May 12 to May 16, 2014, during the last of four, one-week assessments that began on April 21, 2014. Meetings were held first with the BoFED Head and Deputy Head, and then with staff of the relevant functional departments in BoFED, including: Budget and Planning; Financial Administration Core Process; Procurement and Property Administration Procurement Agency (a Core Process until FY 2012/13); Inspection Department (which monitors the internal audit function in SNNPRG); Internal Audit Department of BoFED; Aid Coordination Unit; the Revenue Authority (RA); Tax Appeals Committee; the Education, Health and Rural Roads and Construction bureaus; and the Office of the Auditor General. A meeting was scheduled on May 16 with the chair of the Economics Committee in the National Assembly, but he was out of town and unable to return in time for the meeting. It was not possible to meet the Chamber of Commerce or any other civil society organizations. A first draft report was submitted to the World Bank on August 25, 2014.

In October, the Asssessment Team conducted a second phase of the assessment. They visited Hawassa on October 23 to conduct a workshop on the first draft PEFA findings, obtain feedback from SNNPRG officials, meet with the Chairman of the Economics Committee of the National Assembly to obtain information necessary to rate PIs 27-28, and hold follow-up meetings with other SNNPRG officials. A second PEFA Assessment draft was submitted to the Bank on November 24, 2014. The Bank submitted the draft to the PEFA Secretariat on December 12, 2014. The assessment team received the comments of the Secretariat on February 2, 2015.

The current draft reflects the comments of the Secretariat as well as adjustments that were made while integrating the seven PEFA assessments and submitted to World Bank on January 23, 2015.

Appendix A contains a list of officials met. Appendix B contains a list of documents obtained.

The assessment team comprised three World Bank-funded independent consultants: Peter Fairman, (Team Leader), Getnet Haile, and Zeru Gebre Selassie. The World Bank sector leader and lead financial management specialist supervised the consultants. The Bank is the sole DP involved in this assessment.

## 1.4 Quality Assurance

A robust quality assurance has been put in place through the PEFA Secretariat PEFA CHECK system and through the World Bank peer review process.

## 1.5 Structure of the Report

Chapter 2 provides background information on SNNPRS, an assessment of budgetary outcomes, and a description of the legal and institutional framework for PFM in SNNPRS. It describes other key features of the PFM system in SNNPRS, focusing on changes since the 2010 assessment. Chapter 3 presents the evaluation of SNNPRG's PFM systems. Chapter 4 describes recent and on-going reforms and the main areas of intervention by SNNPRG.

# 2. Country Background Information

## *2.1. Economic Context, Development and Reforms*

Southern Nations and Nationalities Peoples' Region (SNNPR) is located in the south of Ethiopia, sharing borders with Oromia Region, Gambella Region, Kenya and Sudan. It is the country's fourth largest region, with a land area of 105,887 square kilometers or 10 percent of the country's total. The population is 17.9 million (Central Statistics Agency, FY 2012/13), comprising 21 percent of Ethiopia's total population. At 169 persons per square kilometer, it is the most densely populated region in the country (excluding Addis Ababa City and Dire Dawa City), and density has increased from 142 persons per square kilometer since the 2010 assessment.

Fifty-six ethnic groups live in the region, which has a diverse topography encompassing high mountains, valleys, rolling plains, lowlands, including part of the Rift Valley, seven big rivers and a number of lakes. Agriculture is an important component of the region's economy, and it has significant mineral resource potential. Tourism has become increasingly important. Hawassa, located on the shore of Lake Hawassa, is the capital.

SNNPR is divided into 14 zonal administrations (increased from 13 at the time of the 2010 assessment), and the Hawassa City administration. Hawassa City and the administrations are institutionally separate from the Regional Government and have their own governing councils. Thus, only the regional bureaus fall under the Regional Government. Below the zonal tier, there are 150 woreda governments, and four special woreda governments. Eight sub-cities fall under Hawassa City jurisdiction; below these are 21 city administrations, also known as municipalities. At the time of the 2010 PEFA assessment there were 134 woreda and special woreda governments; the city administrations were created later.

The structure of government is similar at all levels. The Bureau of Finance and Economic Development (BoFED), located in Hawassa, is the regional equivalent of the federal MoFED. Similarly, sector ministries at the federal level have their equivalents at Regional Government level in the form of 40 public sector bodies (bureaus, authorities, institutes and agencies) located in Hawassa. Zonal administrations and special woreda governments form the level of government immediately below the Regional Government level. The Zonal Office of Finance and Economic Development (ZoFED) forms the equivalent of BoFED, while sector offices form the equivalent of sector public bodies at Regional Government level. At the next level of government down, Woreda Offices of Finance and Development (WoFED) are the equivalent of ZoFEDs and sector offices are the equivalent of sector offices at the zonal administration level.

SNNPR's external audit and legislative oversight function also broadly resembles that of the Federal Government. The Office of the Regional Auditor General (ORAG), which oversees zonal administrations, woreda governments and SNNPRG, conducts the external audit function. An elected Regional Council conducts legislative oversight.

As with other regions, SNNPRG takes its lead from the Federal Government in relation to economic development strategies and government reform programs.

An effective and efficient PFM system and capable civil service are prerequisites to successful implementation of development strategies. The Expenditure Management and Control Program (EMCP) and Public Sector Capacity Building Program (PSCAP), led by MoFED and Ministry of Capacity Building, served as the main vehicles for implementing PFM reforms and strengthening capacity until FY 2011/12, when PSCAP was phased out and EMCP continued as the main vehicle.

## 2.2 Budgetary Outcomes

**Table 2.1: Fiscal Performance, SNNPRS, FYs 2010/11-2012/13 (EFY 2003-2005)**

| ETB, millions | FY2010/11 | FY2011/12 | FY2012/13 |
|---|---|---|---|
| | Actual | Actual | Actual |
| | | | |
| ***Total Financial Resources*** | ***6,542*** | ***10,390*** | ***13,566*** |
| Region's revenues | 1,356 | 1,977 | 2,889 |
| Federal Government subsidy | 5,166 | 8,413 | 10,677 |
| External assistance & loans | 20 | NR | NR |
| | | | |
| ***Total Expenditures*** | ***6,295*** | ***9,951*** | ***12,761*** |
| *Recurrent* | *4,919* | *6,531* | *8,241* |
| *Capital* | *1,376* | *3,420* | *4,520* |
| | | | |
| *By function* | *6,295* | *9,951* | *1,2761* |
| Admin. & General Services* | 2,031 | 2,668 | 3,345 |
| Economic Services | 1,584 | 3,388 | 4,433 |
| Social Services | 2,686 | 3,895 | 4,983 |
| | | | |
| ***Balance*** | ***247*** | ***439*** | ***805*** |
| Domestic debt amortization | -3.6 | -1.1 | -1.5 |
| Accumulation/Use of cash | -243.4 | -437.9 | -803.5 |

*Source:* IBEX-generated end-year trial balances.
*****Includes municipality expenditures (Code 500) of ETB 225 million, ETB 245 million and ETB 290 million in FYs 2010/11, 2011/12, 2012/13 (EFY 2003-2005), respectively.
NR = Not reported. The proclaimed budget includes externally financed projects and programs but actual expenditures are not reported in IBEX. Budgeted external assistance and loans were ETB 126 million, ETB 114 million, and ETB 123 million in FYs 2010/11-2012/13, respectively.

A doubling of Federal Government transfers and domestic revenues enabled the doubling of total expenditures and tripling of capital expenditures over the last three years. MoFED's establishment of the MDG Fund in 2011/12, with substantial support from DPs, was a principal catalyst for these rises.

In functional terms, the share of economic services in total expenditure rose to 34.7 percent in FY 2012/13 (EFY 2005) from 25.2 percent in FY 2010/11 (EFY 2003); the share of social services fell to 39.1 percent from 42.7 percent; and the share of general and administrative services fell to 26.2 percent from 32.2 percent. The rise in the share of economic services reflects the establishment of the MDG Fund.

Table 2.2 shows the economic classification of SNNPRS expenditures. The MDG Fund caused the share of capital expenditure to increase sharply to 35.5 percent in FY 2012/13, from 21.9 percent in FY 2010/11.

**Table 2.2: Economic Classification of Expenditure, SNNPRS**

| *EFYs 2003-05* | Actual | | Actual | | Actual | |
|---|---|---|---|---|---|---|
| **ETB millions** | **2010/11** | **%** | **2011/12** | **%** | **2012/13** | **%** |
| Personnel services | 3,413 | 54.2 | 4,334 | 43.6 | 5,241 | 41.1 |
| Goods & services | 1,266 | 20.1 | 1,768 | 17.8 | 2,416 | 18.9 |
| Subsidies & grants* | 240 | 3.8 | 429 | 4.3 | 584 | 4.6 |
| Interest | 0 | 0 | | 0 | 0 | 0 |

| *EFYs 2003-05* | Actual | | Actual | | Actual | |
|---|---|---|---|---|---|---|
| Capital | 1,376 | 21.9 | 3,420 | 34.3 | 4,520 | 35.4 |
| **Total** | **6,295** | **100** | **9,951** | **100** | **12,761** | **100** |

*Source:* End-year trial balance sheets generated through IBEX, provided by BoFED.
*****Includes very small amounts of interest and bank charges in FY 2010/11 (EFY 2003).
Account codes are 6100-6199, 6200-6299, 6400-6499 (including interest payments), and 6300-6399, respectively.
Domestic debt repayments of ETB 3.6 million, ETB 1.1 million, and ETB 1.5 million in FYs 2010/11, 2011/12 and 2012/13 respectively are excluded, as these are financing items under GFS.

## *2.3 Legal and Institutional Framework*

### Legal framework

The main changes that have taken place since the FY 2010 PEFA assessment include: (i) a new Financial Administration Proclamation no. 128, FY 2009/10 (EFY 2002) and accompanying Financial Administration Regulations; and (ii) the Procurement and Property Administration Proclamation, no. 146, FY 2013/14 (EFY 2006). The Financial Administration Proclamation (FAP) separated procurement and property administration from financial administration, leading to the new procurement and property administration procurement proclamation and the establishment of the Public Procurement and Property Administration Agency (PPA). Ten directives were subsequently issued for the effective implementation of these proclamations:

- Property administration directive no. 14/ EFY 2005)
- Cash management directive no. 8/EFY 2005
- Disbursement directive no. 9/EFY 2005
- Government accounts directive no. 6/EFY 2004
- Handover of Property among government bodies directive no. 11/EFY 2005
- Public procurement directive no. 13/EFY 2005
- Budget Administration directive no. 2/EFY 2002
- Guarantee directive no.10/EFY 2005
- Internal Audit directive no.3/EFY 2004
- Financial Accountability directive no.5/EFY 2004.

The directives also took into account the Business Process Reengineering (BPR) exercises conducted during FY 2007/08-2008/09.

*Tax System:* Tax laws closely follow federal legislation. The Regional Government shares some taxes with the Federal Government. While no tax revenue raising powers are assigned to woreda and city administration governments, they collect some revenues on behalf of the Regional Government. They also have sources of nontax revenue. The taxation system is covered in more detail under PI-13 in Chapter 3.

The main institutional development since the FY 2010 PEFA assessment was the establishment of the Tax Appeals Commission (TAC) in January 2011. The Income Tax Proclamation (No. 56, EFY 1995) established the legal basis for the TAC, whose workings are described under PI-13 in Chapter 3.

*External Audit:* The legal framework for this is covered under PI-26 in Chapter 3.

### Institutional framework

Since the 2010 assessment, the BoFED has been reorganized, partly to reflect the new proclamations referred to above. The Financial Administration, Procurement, and Property Disposal Core Process has been divided into two Core Processes to improve monitoring efficiency: Financial Administration and Procurement and Property Administration. Other changes are (1) the creation of a Channel 1 Unit, to oversee the various Channel 1a programs and projects being administered by different offices in BoFED; and (2) the creation of an Aid Coordination Unit to oversee the various Channel 1b programs and projects being administered by different offices in BoFED. Units were created to improve the efficiency of aid monitoring.

The Federal Government and development partners (DPs) fund Channel 1a programs, with funds flowing to BoFED from MoFED. The programs are part of the Federal Government's budget. They include the Public Safety Net Program (PSNP); Water, Sanitation and Hygiene Program (WaSH); General Education Quality Improvement Program (GEQIP); the capacity building component of the Protection of Basic Services (PBS) program (the main component is the block grant to Regional Governments from MoFED, partially funded by DPs); and the Urban Local Government Development Program (ULGDP). The Public Sector Capacity Building Program (PSCAP) used to be a Channe1 1 program, but was phased out in FY 2009/10.

The Channel 1b programs and projects are funded by DPs directly via BoFED, and are budgeted for by the Regional Government. The main DPs are World Bank and the UN Executing Agencies (UNICEF, UNDP, UNFPA).

Some sector bureaus receive funding directly from DPs. The funding is not captured in the Regional Government Budget Proclamations and thus constitutes extra-budgetary operations (EBOs). Issues concerning the reporting of EBOs are discussed under PI-7 in Chapter 3.

The BoFED oversees PFM in SNNPRG, including the budget preparation process and the draft budgets being prepared by bureaus, authorities and institutions (hereinafter referred as budget institutions (BIs)) and approved by the Regional Council (RC). BIs execute their approved budgets using the mechanisms and controls established by BoFED, principally through the electronic Integrated Budget and Expenditure Management system (IBEX) that BoFED established several years ago. This was in the process of being rolled out to bureaus at the time of the 2010 assessment. The BIs monitor budget performance during the year through IBEX, and account for their expenditures using the double entry bookkeeping system contained in IBEX, under which trial balances are generated every month. BoFED prepares annual financial statements for submission to ORAG for audit. ORAG audits these statements and prepares audit reports for review by the Economics Committee in the Regional Assembly.

Since the FY 2010 assessment, the roll out of IBEX to BIs has been completed. IBEX has also been implemented in the zonal administrations and in 78 of the 137 woredas and city administrations. At the time of the FY 2010 assessment, there was a plan to establish electronic linkages between the IBEX systems in BIs and in BoFED, but this has not happened due to connectivity problems related to power shortages. BIs systems remain stand-alone, and transmit information on budget performance to BoFED through hard copy (CDs, flash drives).

The version of IBEX currently being used, IBEX 1.3, is the same as at the time of the 2010 PEFA assessment. An upgraded version, called IBEX 1.2, is being piloted. The Federal Government is also in the process of introducing an Integrated Financial Management Information System (IFMIS), which is completely different from IBEX.

A new development that is more relevant at woreda levels is BoFED's establishment of PFM teams to visit zones and woredas to advise on implementing PFM reforms, particularly in relation to establishing effective internal audit committees. The change is partly nominal, as the teams were in place previously under the Financial Transparency and Accountability Program (FTAP).

# 3. Assessment of the PFM Systems, Processes and Institutions

## *3.1 Introduction*

The following subsections provide the detailed assessment of the PFM indicators contained in the Public Finance Management-Performance Measurement Framework (PFM PMF). The scoring methodology only takes into account the existing situation and does not cover ongoing and planned activities that may result in higher scores under future assessments, but these are summarized at the end of the discussion on each PI.

Each indicator contains one or more dimensions in order to assess the key elements of the PFM process. Two methods of scoring are used. Method 1 (M1) is used for all single-dimensional indicators and for multidimensional indicators where weak performance on one dimension of the indicator is likely to undermine the performance on other dimensions of the same indicator (in other words, by the weakest link in the connected dimensions of the indicator). A plus sign (+) is given where any of the other dimensions are scoring higher.

Method 2 (M2) is based on averaging the scores of individual dimensions of an indicator. It is prescribed for multidimensional indicators, where a low score on one dimension of the indicator does not necessarily undermine the impact of a high score on another dimension of the same indicator. A conversion table for two-, three-, and four- dimensional indicators is used to calculate the overall score. The PEFA handbook (PFM Performance Measurement Framework, www.pefa.org) provides detailed information on the scoring methodology. As of January 2011, a revised methodology is being used for PIs 2, 3 and 19.

An upward pointing arrow (↑) may be provided if a PFM-strengthening activity is underway, which, when completed, would result in a higher rating.

The PEFA assessment reviews PFM performance in real time: the relevant time period depends on the type of indicator. For some indicators, for example, PI 4, 7, 9, 24-26, 28, the relevant time period is the last completed fiscal year (2012). For others, such as PIs 1-3, the time period is the last three completed fiscal years (2010-2012). Similarly, for indicators PIs 13 and14, which concern revenue administration, and the first three dimensions of PI-18, which concern payroll control, the relevant time period is the situation at the time of the assessment. More information is available in the PEFA Secretariat’s publication “Field Guide” (March FY 2012) on evidence and sources of information to support the scoring of indicators.

Since this is a repeat assessment, it is important to ensure the validity of comparisons of ratings. Comparisons may not be valid if the scope of the new assessment for an indicator differs from that of the old assessment. Comparisons may also lack validity if the ratings in the 2010 assessment appear to be incorrect.

Comparisons are problematic under two out of the three PIs, where the rating methodology was revised effective January 2011: namely PIs 2 (variance in the composition of expenditure) and 19 (public procurement). Rescoring PI-2 in the 2010 assessment requires time-consuming data inputting on the budgets and actual budget performance for EFY2005/06-2007/08 budgets into an Excel spreadsheet. Re-scoring dimensions (i), (iii), and (iv) of PI-19 is feasible, but is difficult for dimension (ii), on the justification for the use of noncompetitive procurement methods, as per the previous methodology. Under the revised methodology, precise quantitative data are required, whereas precise data were not required under the previous methodology. The methodology for PI-3, on revenue performance, was also revised to penalize for under- or over-forecasting. However, rescoring the 2010 assessment rating for PI-3 is straightforward.

## 3.2 Budget Credibility

### PI-1 Aggregate expenditure outturn compared to original approved budget

MoFED's establishment of the MDG Fund in FY 2011/12 for capital expenditure and the use of advances against the proclaimed budget for capital expenditure, complicate assessment of PI-1. Due to delays in disbursements of the funds to BoFED, and the performance-based *modus operandi* of the MDG Fund (i.e. payment by results), the capital projects contained in the proclaimed budget were initially financed by an advance from the fund. The mechanics of the fund permit advance payments to contractors up to 30 percent of the contract. These are not counted as expenditures until payment certificates have been received, processed, and accounted for.

MoFED tends to disburse MDG Funds to BoFED late in the financial year; MoFED also uses lengthy processes to authorize capital projects and to process payments certificates. Advances consequently tend not to be retired until the following year. As shown in Table 3.1, below, this gives the impression of underperformance during FY 2012/13 in particular, as advances to contractors and suppliers (account codes 4251 and 4254) during FY 2012/13 were much larger than the advances that were carried over from the year before and subsequently retired.

Table 3.1 adjusts for this by adding end-year advances to actual recorded expenditures. Total primary expenditure was less than budgeted expenditure by 8.9 percent, 9.8 percent, and 1.5 percent in EFY 2003, EFY 2004, and EFY 2005 respectively. Had this adjustment not been made, underperformance would have been 18.6 percent and 17.6 percent respectively in these years.

The underperformance may be partly due to labor supply constraints and inaccurate budgeting in the context of planned expenditure increases of 188 percent and 131 percent in FY 2010/11 and FY 2011/1205, respectively.

Performance improved to B from D in the FY 2010 assessment. This may represent a data quality issue in terms of the 2010 assessment, as actual expenditures fell short of budgeted amounts by large margins, even though actual revenues significantly exceeded expenditures.

**Table 3.1: SNNPRG Aggregate Expenditure Performance**

| ETB millions, FY (EFYs 2003-05) | 2010/11 Budget | 2010/11 Outturn | 2011/12 Budget | 2011/12 Outturn | 2012/13 Budget | 2012/13 Outturn |
|---|---|---|---|---|---|---|
| Total primary expenditure[a] | 1,684 | 1,535 | 4,856 | 4,376 | 6,357 | 6,263 |
| Deviation (%) | | -8.9 | | -9.8 | | -1.5 |
| *Note*: End-year stock of MDG Fund-related advances to contractors & suppliers | | | | 424 | | 1,447 |
| a. Defined as total recurrent expenditure plus domestically financed investment expenditure. Actual expenditures at the end of FY 2011/12 and FY 2012/13 understate the real situation, as MDG-related advances to contractors were not retired by the end of the year. To more accurately show actual expenditures, the end–FY 2011/12 stocks of MDG-related advances have been added to recorded actual expenditure for FY 2011/12. Similarly, the end-FY 2012/13 year stock of MDG-related advances have been added to recorded actual expenditures, after deducting the end-FY 2011/12 stock of advances, which were regularized as expenditures in FY 2012/13. | | | | | | |

*Source:* Budget execution tables and end-year trial balance sheets generated through IBEX by BoFED.

**Table 3.2. PI-1 Results**

| PI | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-1 | D | B | Actual expenditure deviated from budgeted expenditure by -8.9%, -9.86% and -1.5% in FY 2010/11, FY 2011/12, and FY 2012/13 respectively. The recorded actual expenditures in FY 2011/12 and FY 2012/13 have been adjusted for the large size of the advances to contractors and suppliers for implementation of MDG Fund-financed projects. | **Performance improved,** but extent of improvement may be overstated as the quality of the 2006/07-2008/09 expenditure data seems suspect. |

## PI-2 Composition of expenditure outturn compared to original approved budget

Where the composition of expenditure varies considerably from the original budget, the budget is not a useful statement of policy intent. Measurement against this indicator requires an empirical assessment of expenditure out-turns against the original budget at a sub-aggregate level. Annex A shows the original budgets and actual out-turns for each of the 20 largest BIs. The remaining heads are aggregated into a notional 21st head.

The method of assessing this indicator changed in January 2011. The previous methodology assessed PI-2 as the sum of differences between the actual and budgeted expenditures of each BI as a percentage of the approved budget minus the percentage aggregate deviation, as measured under PI-1. This was methodologically incorrect, as the rating would have been A regardless of whether the differences were all positive or negative, and regardless of the size of the differences between actual and budgeted expenditures. Under the revised methodology, the aggregate deviation is applied first to the approved budget of each BI, and then the sum of the differences between actual expenditures of each BI and the adjusted budget of each BI is calculated and expressed as a percentage of the adjusted budget.[1]

*(i) Extent of variance in expenditure composition during the past three years*

Table 3.3 shows the variance in the composition of expenditure. The variance is very high, indicating that the originally approved budget lacks credibility. Annex A does not incorporate the sector distribution of expenditures out of the advance of MDG grant funds, which is referred to under PI-1. The rating might have been higher if the team had been provided with complete information of the distribution, but only partial information was given. The variance was also very high in the 2010 assessment, however, prior to the establishment of the MDG Fund, scoring D under the previous methodology (and would probably also score D under the revised methodology).

The high variance points to issues in preparing the annual budget in the first place (e.g. overestimating the rate of project implementation, not taking into account labor supply constraints), and uncertainty over the amount of resources DPs are planning to provide. Most of the resources they provide are through Channel 1a programs (to BoFED through MoFED). The budgeting of these resources is at the federal level, but expenditures at regional level are linked to them in many ways (e.g. recurrent expenditures generated by capital expenditures funded by Channel 1 funds). Timely budgeting for these expenditures is therefore difficult if bureaus do not know until very late in the day the magnitude of Channel 1a resources they can expect next year. BoFED staff indicated that this was a perennial problem.

[1] The term "adjusted budget" is a PEFA term, and is not equivalent to the term 'adjusted budget' that appears in SNNPRG's budget execution reports. These reports show changes to the original budget due to supplementary resources and transfers in and out from/to other BIs for each BI.

As was the case in the previous assessment, authorities appear to regard the original budget as temporary for the reasons mentioned above, and anticipate the need for adjustments to the budget after it has been approved. The monthly Joint Budget and Aid Reviews (JBAR) prepared by BoFED and circulated to stakeholders do not even show the originally approved budget; performance is being evaluated against the adjusted budget.

The BIs that spent more than implied by their 'adjusted' budgets over all three years included: Health, Supreme Court, Police, Regional Council, Agricultural Research Institute and Prisons respectively. The only BI that spent less than implied by its adjusted budget in all three years was the Roads Authority, mainly reflecting absorptive capacity constraints.

**Table 3.3: SNNPRG: Expenditure Composition Variance**

| FY | Expenditure composition variance |
|---|---|
| 2010/11 | 18.4% |
| 2011/12 | 28.5% |
| 2012/13 | 15.8% |

*Source:* Appendix A.

*(ii) The average amount of expenditure actually charged to the contingency vote over the last three years*

Variance in the composition of the budget may arise from allocations to BIs from a separately budgeted contingency/reserve item. For transparency, the allocations should be to BIs that already have approved budgets and not to the contingency -item itself.

The contingency item in SNNPRG's budget was ETB 50 million, ETB 100 million, and ETB 100 million in FYs 2010/11/, 2011/12, and 2012/13, representing 3 percent, 2.1 percent and 1.6 percent of total budgeted expenditure, respectively. The amount in percentage terms has fallen since the 2010 assessment, which showed the contingency item as 3 percent, 3.9 percent, and 3.8 percent of total budgeted expenditure. The previous methodology did not contain this dimension. The sharp fall in the size of the contingency item had no influence on the rating for PI-1 (i). Not all the contingency item is necessarily allocated to BIs; some of it may be allocated to woreda governments. In any case, the amounts are small and contribute little to expenditure composition variance.

**Table 3.4 PI-2 Results**

| PI-2 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-2 | D+ (*revised method*) | D+ | | **No change**. |
| (i) | D | D | *Variance in expenditure composition exceeded 15% in at least 2 of the last 3 years* | **No change**. Variance was 18.4%, 28.5% and 15.8% in EFYs 2003-05 respectively. |
| (ii) | A | A | None of actual contingency expenditure is allocated to the contingency code. | **No change.** The contingency averaged 2.2% of the budget in EFYs 2003-05, none of which was allocated to the contingency code. The contingency averaged a much higher 14.3% of the budget in EFY 1999-01. |

## PI-3 Aggregate revenue outturn compared to original approved budget

Revenue out-turns close to budgeted amounts contribute to budget credibility. Domestic revenues comprised about 20 percent of SNNPRG's domestic financial resources in FYs 2010/11-2012/13 (Table 2.1, Chapter 2), the federal block grant being by far the largest source of domestic funds. The SNNPRG Revenue Authority (RA) and other revenue collecting departments, in collaboration with the Planning Department in BoFED, estimate the annual revenue of the SNNPRG. The estimation is based on the previous year's tax collection, BoFED's projections of real GDP growth, and the Federal Government's projections for inflation.

The revenue offices of regional zones and woredas are primarily responsible for collecting the region's revenue, mainly in the form of taxes. Since the taxes that they collect are considered part of Regional Government revenues, they are deductible from the actual annual transfers to zones and woredas.

The method of scoring PI-3 was changed in FY 2011. Over-collections are now penalized, though not as much as under-collections.

**Table 3.5 Domestic Revenue Performance for FYs 2010/11-2012/13 (EFY 2003-05)**

| | | **2010/11** | | | **2011/12** | | | **2012/13** | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | ***ETB, millions*** | **Budget** | **Actual** | **Diff.** | **Budget** | **Actual** | **Diff.** | **Budget** | **Actual** | **Diff.** |
| **Codes** | **Tax Revenue** | **218** | **932** | **328%** | **41** | **1,418** | **3382%** | **1,610** | **2,216** | **38%** |
| 1100-1199 | Direct tax on incomes | 180 | 753 | 318% | 36 | 1,069 | 2872% | 1,194 | 1,457 | 22% |
| 1200-1299 | Indirect taxes: VAT, Excise & Turnover | 37 | 179 | 378% | 5 | 349 | 7325% | 416 | 759 | 83% |
| **1400-1599** | **Nontax Revenue** | **65** | **245** | **279%** | **13** | **334** | **2399%** | **385** | **407** | **6%** |
| **1701-1719** | **Municipality Revenue** | **76** | **186** | **146%** | **13** | **235** | **1639%** | **336** | **287** | **-15%** |
| | **Total Revenue** | **358** | **1,363** | **281%** | **67** | **1,987** | **2841%** | **2,331** | **2,910** | **25%** |

*Source:* BoFED Accounts Department: Revenue performance statements and trial balance sheets (IBEX data)

Table 3.5 indicates both data recording and estimation problems. Revenues were underestimated by large margins in all three years, and the estimates for FY 2011/12 have clearly been entered into IBEX incorrectly (as indicated by the Deputy Bureau and Budget and Finance head), and perhaps also incorrectly for FY 2010/11. The 2010 PEFA assessment also indicated significant underestimation, although by much smaller margins. Forecasting errors mainly reflect inherent uncertainty in an economy where weather-dependent agricultural activities play a large role.

Municipal revenues are a new category, reflecting the establishment of city administrations in FY 2010/11 in Ethiopia, in addition to the existing ones of Addis Ababa and Dire Dawa. Municipal revenue items are many and diverse, and the category's newness exacerbates difficulties with estimates, as shown by the very large deviations above.

**Table 3.6 PI-3 Results**

| PI | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-3 | C *(revised method; 'A' old method.)* | **D** | Actual domestic revenue was below 92% or above 116% of budgeted domestic revenue in at least 2 of the last 3 years. | **Performance worsened**. Actual revenue exceeded budgeted amounts by 281%, 2841% and 25% in 2010/11, 2011/12 and 2012/13 respectively. The performance reflects data recording errors as well as estimation errors |

### PI-4 Stock and monitoring of expenditure payment arrears

This indicator is concerned with measuring the extent to which there is a stock of arrears, and the extent to which the systemic problem is being addressed.

*(i) Stock of payment arrears*

There is no official definition for arrears in the financial administration proclamation and regulations of the SNNPRS. Salaries and wages are paid after the 23rd day of each month and all goods and services are generally purchased on a cash-on-delivery basis.

A "grace period" of 30 days is provided for the payment of capital expenditure-related goods and services received before the end of the FY, but too late to process payments (Account Code 5001 in the Chart of Accounts). Unpaid payment requests submitted towards the end of the fiscal year are accrued as Grace Period Payables (GPP). End-year GPP constituted 1.89 percent, 3.21 percent and 3.42 percent of the regional expenditure as of the end of EFY 2003, 2004 and 2005 respectively, and virtually zero a month later, as shown in Table 3.7.

The 2010 PEFA assessment mentions that the GPP provision was not used at that time, as in practice most bills were paid by the end of the FY. As indicated in the trial balances for SNNPRS for FY 2008/09, GPP were zero at the end of 2008/9. The large amount of MDG Funding in FYs 2011/12 and 2012/13, and its funding mechanism, appear to be the main reasons for GPP not being zero at the end of most recent FYs.

In addition, end-year trial balances contain recurrent expenditure payables including sundry creditors, pension contributions payables, salary payable, other payroll deductions and withholding tax payables. Payables amounted to ETB 514.2 million at the end of EFY 2005, constituting 4.03 percent of total SNNPRS government expenditure. GPP provisions do not apply to these. Personnel-related payables amounted to ETB 120.5 million, ETB 144.9 million and ETB 122.3 million at the end of EFY 2003, EFY 2004, and EFY 2005, respectively, were paid within a month. The largest payable item was pension payables; delays in paying these are subject to an interest charge of 2 percent, thereby providing an incentive to pay on time. Salaries payable mainly relate to unpaid salaries. BoFED pays these liabilities quickly within a month from the end of the FY, but it is unclear at what date the non-salary payables are paid off; these, however, are very small.

The 2010 assessment indicates that recurrent expenditure payables were zero at the end of 2008/09.

**Table 3.7 End-year Expenditure Arrears in Relation to Total SNNPRS Expenditure**

| ETB, millions | EFY 2003 | EFY 2004 | EFY 2005 |
|---|---|---|---|
| Total SNNPRS expenditure | 6,298.5 | 9,952.3 | 12,761.7 |
| End year GPP (July 7) | 118.9 | 319.2 | 436.3 |
| % of SNNPRS expenditure | 1.89% | 3.21% | 3.42% |
| Balance as of August 6 (1 month after year-end) | - | 0.0 | 0.2 |
| End-year recurrent payables | 135.1 | 160.31 | 144.6 |
| *Of which, personnel related* | *120.5* | *144.9* | *122.3* |
| *Non-personnel related* | *14.60* | *15.42* | *22.3.0* |

*(ii) Availability of data to monitor the stock of expenditure payment arrears*

Capital expenditure-related GPP (only for MDG Fund financed expenditures) are recorded at the end of the FY in IBEX, as shown in the trial balance, and then for each month thereafter as long they remain outstanding. Recurrent expenditure payables are shown in the trial balance sheets on a month-to-month basis. Since there is no age profile for these in IBEX, their age at the end of the FY is unknown; however, as mentioned in the 2010 assessment, the information is available in manually maintained subsidiary ledgers. In any case, these tend to be paid off the following month.[2]

**Table 3.8 PI-4 Results**

| PI | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-4 | B+ | B+ | | **Performance unchanged** |
| (i) | A | A | The stock of arrears is low (i.e. below 2% of total expenditure). | **Performance unchanged**. The GPP were virtually zero at the end of the first month of the new FY. Most end-month recurrent expenditure payables are paid off the following month, including within the first month of the new FY. |
| (ii) | B | B | Data on the stock of arrears is generated annually, but may not be complete for a few identified expenditure categories or specified budget institutions. | **No change**. The age of the year-end GPP is tracked, as shown in the monthly trial balance sheets in the new fiscal year. There is no GPP provision for end-year recurrent expenditure payables. The age of these is not tracked in IBEX, though the information is contained in subsidiary manually maintained ledgers. |

[2] The accounting system is not on a fully cash basis. There are financial assets that can be used to pay end-year payables without affecting the budget for next year. Hence, the budget is not perfectly equivalent with cash outlay. Next year's payment does not affect the expenditure account; it debits the payable account. There is a beginning balance of cash and receivables represented by net assets that are not part of the next year's budget. Hence, end-year recurrent expenditure payables should not be regarded as arrears

## *3.3 Comprehensiveness and Transparency*

### PI-5 Classification of the budget

A robust classification system allows the tracking of spending on administrative unit, economic, functional and program dimensions.

The budget classification system at the regional level (and also zonal administration and woreda level) is identical to the federal level. (The Federal Government budget classification system is described in the Federal Budget Manual (FY 2007) and the Federal Chart of Accounts Manual (May 2007),[3] details of which are described in the 2010 assessment. A 'B' rating was assessed based on the administrative classification falling under a sub-functional classification, itself falling under a functional classification, of which there are three: administrative and general service, economy and social. For example, the education bureau (code 311) falls under the code 310 sub-function (education and training), which falls under the 300 function (social sector). Different levels of education (e.g. primary, secondary) are itemized under different heads under code 311. The economic classification falls under the administrative classification and is broadly consistent with GFS. The functions (3) and sub-functions (19) differ from COFOG, but the sub-functions can be matched to some extent to the ten COFOG functions.

**Table 3.9 PI-5 Results**

| PI | Score in 2010 | Score in 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-5 | B | B | Budget formulation and execution is based on functional, sub-functional, administrative, and economic classification, the sub-functional classification being similar to COFOG's functional classification. | **No change**. |

### PI-6 Comprehensiveness of information included in budget documentation

In order for the legislature to carry out its function of scrutiny and approval, the budget documentation should allow a complete overview of fiscal forecasts, budget proposals, and results of past fiscal years.

This indicator is assessed on the latest budget documentation, which is for FY 2013/14 (EFY 2006). The draft Budget Proclamation documentation, as submitted to the Regional Council (budget estimates), includes budget allocation of transfers to woredas and city administrations, sources of revenue and the expenditure budget. The macroeconomic fiscal framework (MEFF) has been indicated in the Growth and Transformation Plan (GTP), which covers the period from EFY 2003 to EFY 2007. Revised MEFF assumptions including aggregate growth were not been indicated in the budget document though a three year rolling MEFF preparation is required by Financial Administration Proclamation (FAP) 128/2002 EFY (article 19).

[3] The budget classification system is described in the Federal Government Budget Manual adopted in 2007. The Government prepared the report with technical assistance provided by Harvard University via the donor-supported Decentralization Support Activity project. The issue of compatibility with COFOG and the development of an application under IBEX that could generate a bridging table is discussed in paragraph 3.9.2 of the manual.

**Table 3.10 Information in Budget Documentation for FY 2013/2014**

| Requirement | Fulfilled | Explanation |
|---|---|---|
| 1. Macroeconomic assumptions, including aggregate growth, inflation, and exchange rate estimates, at the very least. | No | **Reduced performance**. The medium-term macroeconomic and fiscal framework (MEFF) is indicated in the GTP, and is required under the FAP to be updated each year, the assumptions to be reflected in the Budget Proclamation. BoFED was preparing the MEFF at the time of the 2010 PEFA assessment, but has stopped preparing it due to capacity constraints. |
| 2. Fiscal balance. | No | **No change**. If funds are carried over from the previous fiscal year, they are classified as revenue, contrary to GFS. The fiscal balance is therefore overstated. The correctly stated fiscal balance may be negative (fiscal deficit), which is then financed by use of cash balances. |
| 3. Deficit financing | Yes | **No change**. The Budget Proclamation shows a balanced budget, with no end-year balance brought forward from the previous year and no borrowing. This should have been scored as Yes in the 2010 assessment. |
| 4. Public debt stock | NA | **No change**. SNNPRG does not borrow |
| 5. Financial assets | Yes | **No change**. Financial assets consist of cash on hand and in the bank (COA codes 4101, 4103 and 4105), and accounts receivables (COA codes 4200-4299). They are reported on in monthly trial balance statements and financial position reports. They are not mentioned in the draft Budget Proclamation, but Regional Council members have access to them. This should have been scored as Yes in the 2010 assessment. |
| 6. Prior year's budget outturn (2011/12), in the same format as the budget for 2013/14 | No | **Reduced performance**. The budget documentation does not indicate the budget outturn of the previous year. Annual financial statements for EFY 2003-05 contain budget out-turns of the prior periods, but these are not part of the budget documentation. |
| 7. Current year's budget outturn (FY 2012/13), in the same format as the budget for FY 2013/14 | No | **No change**. The Budget Proclamation contains no information on the current year's budget outturn. It only shows the proposed budget for the next year. |
| 8. Summarized budget data for both revenue and expenditure according to the main heads of the classifications used (ref. PI-5), including data for the current and previous year. | No | **Reduced performance**. The budget document contains summarized budget information for the following year, but the equivalent data for the current and previous year are not included. |
| 9. Explanation of the budget implications of new policy initiatives. | No | **No change**. The budget documentation does not mention new policy initiatives and does not explain the link between the budget and the GTP |

**Table 3.11 PI-6 Results**

| PI | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-6 | C | D | Two of the eight relevant items (3 and 5) are shown in the FY 2013/14 (EFY 2006) Budget Proclamation | **Performance reduced.** 3 of the 8 applicable information items (1, 6, 8) were included in the draft Budget Proclamation for FY 2010/11 (EFY 2003), which was assessed under the 2010 PEFA assessment. |

### PI-7: Coverage of government operations

Fiscal information such as the budget, execution reports and financial statements should include all budgetary and extra-budgetary activities to allow a complete overview of revenues, expenditures, and public financing.

*i) Level of extra-budgetary expenditure (not including project expenditures financed by donors) that does not appear in fiscal reports*

The proclaimed budget and budget performance reports of SNNPRG contain the budgets and in-year/end-year budget performance reports of autonomous bodies. The spending of nontax revenues collected and retained by BIs (permissible in the case of hospitals, health centers, and regional government-run schools) has to be included in the proclaimed budget. At the time of the 2010 PEFA assessment, revenues collected in excess of the approved spending had to be surrendered to SNNPRG's Consolidated Treasury Account (CTA). If BIs wanted to spend some or all excess revenues, they had to request a supplementary budget. These restrictions have been eased to some extent since the 2010 assessment, as indicated in the Budget Proclamation for FY 2012/13, which provides for BoFED to authorize BIs to spend excess revenues.[4]

*(ii) Income/expenditure information on DP-funded projects that is included in fiscal reports*

Some external resources are channeled to SNNPRG through MoFED and sector ministries, and SNNPRG considers these domestic resources. Analytically, it is easier to consider these under dimension (ii).

As noted in Chapter 2, most of these resources come from Channel 1a (MoFED to BoFED) and Channel 2a (sector ministry to sector bureau) programs and projects, and expenditures are captured in the Federal Government Budget Proclamations and budget performance reports; the Federal Government also provides its own financing. The execution of Channel 1a and 2a programs is organized by the respective sector bureaus, and financial management is carried out by the Channel 1 Unit in BoFED (for Channel 1a programs) and sector ministries (for Channel 2a programs). The SNNPRG effectively acts as a subunit of the Federal Government.

[4] This is indicated in the budget proclamation for FY 2012/13 (EFY 2005). Specifically, Part II stipulates: (a) BoFED is authorized to permit Regional Government schools to retain and expend 100% of their annual receipts; (b) BoFED authorizes Government hospitals and health centers to retain and expend within their total budgetary appropriations, receipts of revenue from the current fiscal year not exceeding 100% of their previous fiscal year receipts; (c) BoFED may authorize the appropriations of receipts from the previous FY that exceeded planned revenues; and (d) Municipalities are authorized to retain and spend 100% of their receipts on social service delivery programs.

Though these types of funding are proclaimed at Federal Government level and do not affect the rating of this dimension, the fact that they are not proclaimed at Regional Government level raises a transparency issue. Since regional and woreda governments are responsible for channeling most of this funding, proclaiming them at Regional Government level would seem to be more transparent.

DP funding that falls within the scope of this dimension includes:

*1) Channel 1b, DPs direct to BoFED:* SNNPRG includes funding expenditures in its proclaimed budget, or the funds are transferred to woredas, which include the budgeted spending in their proclaimed budgets (CoA codes 2000-2999 and 3000-3999 under the External Assistance and External Loans category respectively). Actual spending may or may not be included in budget execution reports, depending on whether the Chart of Accounts IBEX spending codes are used. Non-inclusion indicates an unreported extra-budgetary operation (EBO), unless the spending is reported separately.

The main DPs operating in this category are World Bank, Government of the Netherlands and a number of UN agencies (UNICEF, UNDP, UNFPA, UNCDF, UNESCO). According to BoE and BoH, not all UNICEF assistance is included in the proclaimed budget, as they receive some of it directly (Channel 2b, noted below). The WFP-funded school-feeding component of the GEQIP also is not included in the proclaimed budget, though the funds are channeled directly to BoFED. BoFED was not sure if it was included in the Federal Government's proclaimed budget; other components of GEQIP are included in the Federal Government's budget.

Channel 1b fund-related expenditures were included in the proclaimed budgets for FYs 2010/11-2012/13, but were only partially reported on for FY 2010/11. The budgeted amounts are very small relative to total budgeted expenditure, falling from 2.1 percent in FY 2010/11 to 0.9 percent in FY 2012/13. The decrease was partly due to DPs providing considerable support for the MDG Fund, which MoFED established in FY 2011/12. Actual expenditures are not reported for FY 2011/12 and FY 2012/13 and only ETB 20 million out of a budgeted amount of ETB 120 million was reported for FY 2010/11; the annual trial balance sheets provide the information, as indicated in Table 2.1.

BoFED's Aid Coordination Office collates budget execution reports prepared by the project and program offices in conjunction with the relevant offices in the sector bureaus. The reports were not prepared through IBEX, as the project and program codes were different, reflecting programmatic activity-based costing methods. In any case, BoFED does not make budget execution reports available to the public, and therefore the actual expenditures represent unreported EBOs.

Starting in FY 2013/14, some of the UNEXCOM Channel 1b expenditures are being captured in the trial balance sheets on a broad economic classification basis, using a protocol that can link the UN codes to IBEX codes.

2) *Channel 2a:* Some *DP funds are channeled through Federal Government sector ministries, which then direct the funds to sector bureaus. However, the funds appearing are not proclaimed in either the Federal Government's budget or the SNNPRG's budget.* The main example of this highlighted in the 2010 PEFA assessment was the Global Fund (GF) for malaria, tuberculosis and HIV/AIDs, whereby funds were channeled through the Ministry of Health (MoH), which then channeled them through the SNNPRG Bureau of Health (BoH). Neither the Federal Government budget nor SNNPRG's budget proclaimed the funding nor did they report on the spending. The amounts involved were very large, as GF is one of the largest DPs in Ethiopia.

The MoH performance report for EFY 2005 indicates that GF operations were audited at MoH level and at BoH levels in Oromia, SNNPR, and Afar, including selected woredas in these regions. The report does not mention if GF operations were proclaimed in national or regional budgets, and, if proclaimed, whether they were publicly reported. The report says the audit report was distributed to MoH and the three BoHs, but this is not the same as a publicly available fiscal report.

GF operations at Federal and Regional Government levels are managed through the HIV/AIDs Prevention and Control Sector, which is part of the MoH and BoHs. It was a separate office until FY 2006. The sector is guided by a strategic plan, the last of which covered EFYs 1999-2003. The plan says very little about budgeting and mechanisms. It is not clear whether GF operations are included in proclaimed budgets at any level of government. The GF channeled ETB 46.9 million and ETB 49.5 million in EFY 2004 and EFY 2005, respectively, representing more than half of funds channeled through MoH. The GF was providing even larger amounts in EFY 2006 (ETB 104 million).

Apart from the GF, substantial amounts of other DP funds were transferred to BoH by MoH during EFYs 2004 and 2005, and to-date in EFY 2006. The amounts provided were ETB 12.9 million in EFY 2004 and ETB 26 million in EFY 2005. At the time of the PEFA field visit in May 2014, ETB 52 million had been provided that fiscal year (EFY 2006).[5] The DPs providing these funds include Glaxo Smith, a multinational pharmaceutical company, Center for Disease Control(CDC) (US Federal Government), World Bank, UNICEF, Global Alliance Vaccines Initiative (GAVI), UNFPA, WHO, Organon[6] and Imperial College (University of London). It is not clear whether MoH's proclaimed budget included these funds.

*3) Channel 2b*: *Through sector bureaus directly, bypassing sector ministries.* Planned spending is not included in either the federal budget or SNNPRG's proclaimed budget. The BoH indicated that significant amounts of aid are provided in this way:

- *EFY 2004, ETB 57.8 million:* WHO, ETB 12.6 million (in addition to WHO funding channeled through MoH); UNICEF, ETB 10.3 million (in addition to the Channel 1b UNICEF funding channeled to BoFED, noted above); ENAHPA[7], ETB 3.5 million; and Ethiopian Health Nutrition Research Institute (EHNRI), ETB 1.85 million;
- *EFY 2005, ETB 21.7 million:* WHO, ETB 12.7 million; UNICEF, ETB 0.95 million; EHNRI[8], ETB 2.9 million.

According to BoH, 100 donors are providing aid to BoH in various forms. To ease the burden of monitoring and managing the finances of these projects, the main donors agreed to pool their funding in a single account. This improved efficiency, but each DP still requires a separate operations report that costs considerable staff time – more time than if, for example, all DP assistance was provided as part of the block grant. Lack of coordination between BoH and donor representatives also reduces efficiency. For example, BoH staff members tend to meet with the planning and operational departments of DPs, but not with the finance departments, which hampers BoH's efforts to monitor the financial aspects of project implementation.

[5] These figures exclude funding from the MDG Fund, the transfers from which are itemized in the same table provided to the team by MoH.
[6] N.V. Organon, Oss, Netherlands
[7] Ethiopian North American Health Professionals
[8] Ethiopian Public Health Institute

*4) Channel 3, directly to projects*. The planned spending is not included in the proclaimed budgets of any level of government and is not being reported on by the relevant sector bureaus and woreda offices, which may have only limited involvement in the projects.

USAID-funded projects tend to fit into this category. USAID is a major DP in Ethiopia. According to the Bilateral Aid Department in MoFED, USAID has a US$ 1.5 billion five-year program in Ethiopia. While it discusses planning and operational issues with sector bureaus and woreda offices in the regions, it does not disclose its planned and actual spending in each region, even in aggregated terms.

NGO operations (formally known as charity and society organizations) tend to fall under this category. These mainly operate at woreda level. Under NGO Roles and Responsibilities established by proclamation in FY 2009/10 (updated from 2003), NGOs are required to register with BoFED, sign an agreement and submit project appraisal, quarterly and annual activity, and project audit reports to sector bureaus and to the NGO Unit in BoFED. The BoFED has been preparing annual reports of NGO operations since EFY2005/06, although the report for FY 2012/13 is the first to be made public. The reports covering FYs 2012/13 and 2013/14 acknowledge that there may be some data gaps and inaccuracies. Some NGOs are contracted by DPs, especially USAID. Ethiopian organizations comprise 72 percent of NGOs.

According to BoFED's annual report on NGO operations covering FY 2013/14 (dated September 2014), the number of NGOs operating in SNNPRS increased to 214 in FY 2013/14 from 119 in FY 2007/08. The NGOs implemented 583 projects in FY 2013/14, more than double the 208 projects in 2008/09. The amount of planned aid increased sharply to ETB 6.75 billion in FY 2013/14 from ETB 1.3 billion in 2007/08. The rise was particularly sharp in FY 2012/13. The report indicates that not all NGOs report their budgets comprehensively, nor submit quarterly and annual activity reports and project audit reports on time (or not at all in some cases). Some do not use the stipulated formats, and some NGOs request amendments to project agreements without sufficient justification. The report does not include actual expenditures, and does not indicate contractual relationships between NGOs and sector bureaus, although it hints at them, as some of the projects are part of DP-funded WaSH (water, sanitation and hygiene) projects.[9] BoH indicated that NGOs are not reporting satisfactorily to it.

According to BoE, the UK-based Save the Children Fund (SCF) operates in the education sector with little interaction with BoE. The 2013/14 Regional Report on NGO Operations mentions two SCF projects in the sector, costing ETB 20 million over a three-year period (2011-2014. Otherwise, BoE has signed memorandums of understanding (MoUs) with 56 NGOs in the education sector at regional, zonal and woreda levels.[10]

It is difficult to know exactly how much DP assistance is not channeled through BoFED, as the sector bureaus appear not to report to BoFED on the funding they receive via Federal Government ministries (Channel 2a) or directly from DPs (Channel 2b), and do not know how much funding is being provided through Channel 3.

Full and transparent information available to BoFED and sector bureaus on DP and NGO activity in areas where SNNPRG, zonal and woreda governments are providing public services would strengthen the Government's ability to plan and budget effectively for public service provision.

[9] "Profile of Charities and Societies Organizations," BoFED, 2012/13.

[10] Projects costing above Br 7.5 million are at Regional Government level, those between Br 2-7.5 million occur at zonal government level, and those below Br 2 million are at woreda government level. *Sources:* Trial balance sheets (on Channel 1b projects); meetings with BoFED, BoH and BoE BoFED report on NGO operations in 2012/13, MoH website.

***Ongoing and planned activities***

- Effective the beginning of FY 2012/13 (EFY 2006), expenditure under some DP-funded Channel 1b projects and programs (mainly those of UN Executing Agencies) are reported on through IBEX via bridging codes, though these are not reported on in detail.
- Effective the beginning of FY 2013/14 (EFY 2006), NGOs need BoFED permission to open bank accounts related to their planned activities.
- The Bilateral Aid Department in MoFED is discussing with USAID the possibility of the use of the Channel 2 funding modality, instead of Channel 3.
- According to BoE, the UK Department for International Development (DFID) has agreed with MoE to finance an Adult Education project in SNNPR. It is not clear if the project will be covered in MoE's proclaimed budget or in BoE's budget.

**Table 3.12 PI-7 Results**

| PI | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-7 (M1) | **B** | **D+↑** | | **No change in overall performance.** Dim. (ii) appears to have been scored too high in the 2010 assessment |
| (i) | B | A | The level of unreported extra-budgetary expenditure is insignificant, below 1% of expenditure. | **Performance unchanged.** The scope in the 2010 assessment included DP funding channeled to BoFED through the Federal Government, which may or may not constitute an EBO. Analytically, however, it is more convenient to assess such funding under dimension (ii). |
| (ii) | B | D ↑ | Information on DP-funded projects and programs included in fiscal reports is seriously deficient | **No change**. The B rating provided in the 2010 rating appears too high and should have been a D. The BoFED has little information on donor projects being funded through Channels 2a, 2b and 3. USAID, a major DP, uses Channel 3 for all its operations. The annual reports on NGO projects prepared by BoFED do not include their actual annual expenditures and may not fully capture planned expenditures.<br><br>The actual expenditures of DP-funded projects that are included in Budget Proclamations under Channel 1b are now being reported on through IBEX, hence ↑. |

*Sources*: (1) Meetings with Channel 1 unit in BoFED, Aid Coordination unit in BoFED, NGO unit in BoFED, planning and budgeting departments in BoH and BoE; (2) Table provided by BoH on DP funds provided to BoH through MoH by project and DP in 2011/12, 2012/13 and up to April in 2013/14; (3) Table provided by BoH on funding provided directly by DPs in FYs 2011/12, 2012/13 and up to April 2013/14, by project and DP; (4) Report on 'Charities and Societies Organizations in SSNPRS' in FY 2013/14, published September 2014; and (5) a report prepared (September 2014) by the NGO unit in BoFED on the extent that NGOs are complying with the "NGO Roles and Responsibilities" stipulated under the 2009 Proclamation on NGOs.

### PI-8 Transparency of intergovernmental fiscal relations

*(i) Transparency and objectivity in the horizontal allocation of fiscal transfers to lower level governments*

The FY 2012/13 (EFY 2005) Budget Proclamation shows budgeted expenditures of governments below the level of SNNPRG (zones, special woredas, woredas and city administrations) comprising 54.4 percent of total SNNPRS budgeted expenditures (ETB 7.6 billion out of ETB 14 billion). The main form of financing of this expenditure continues to be the unconditional block grant from BoFED; the EFY 2005 Budget Proclamation indicates a block grant of ETB 4.93 billion, representing 64.6 percent of budgeted expenditure.[11]

At the time of the 2010 PEFA assessment, SNNPRG was using the same transfer formula as that of the Federal Governmentfor determining its block grant allocations to the 15 zonal and five special woreda administrations. The horizontal allocation of the block grant from the Federal Government to Regional Governments until FY 2008/09 was based on three criteria: (1) population (65 percent weight); (2) development status (25 percent); and (3) revenue generating capacity (10 percent). The Federal Government intends to phase this out in favor of a new formula that gives more explicit emphasis to the expenditure needs of each sector (rather than the vaguely defined development status) in order to more explicitly and accurately realize the fiscal equalization purpose of the fiscal transfer formula. However, as indicated in the 2014 Federal Government PEFA assessment, the Federal Government has not introduced the new formula.

However, in FY 2012/13 the SNNPRS introduced the new formula, which takes into consideration more explicitly defined expenditure needs based on the estimated fiscal gap of each woreda. Recurrent expenditure needs assessment is based on the areas of responsibility assigned to zones and special woreda administrations, as determined by law (primary and secondary education (including Technical and Vocational Education Training /TVET)), public health, agriculture and natural resources, and drinking water in line with policy objectives and defined service standards.) Capital expenditure needs are estimated based on infrastructure deficits per woreda per strategic sector.

The total amount of transfer to each zonal administration/special woreda is consequently determined to be the sum of recurrent and capital expenditure needs and the nontax revenue generating capacity of woredas.

While not directly relevant to the assessment of this dimension, the situation has changed in two ways since the 2010 PEFA assessment: (i) revenues generated by a woreda in excess of the budgeted amount can be spent by woredas, provided they are proclaimed through a supplementary budget; and (ii) budgeted direct DP assistance to woredas does not result in an offsetting reduction in the budgeted block grant; previously it was offset in the interests of equity of the per capita allocation of financial resources between lower level governments.

The budgeted block grants to each of the zonal and special woreda administrations, and through them to each rural woreda/city administration, are fully shown in the Budget Proclamations of the SNNPRS.

*(ii) Timely provision of reliable information to subnational governments on the allocations to be made to them by central government for the following year.*

The MoFED provides an initial ceiling on the likely allocation of the block grant to the SNNPRG in February each year. BoFED uses this estimate to notify zonal and special woreda

[11] Other financing indicated in the EFY budget proclamation for lower level governments comprised ETB 2.1 billion in own revenues, ETB 170 million of health institution revenue, ETB 85 million from external loans and assistance (Channel 1 funding, as indicated under PI-7), and ETB 350 million in municipal revenue. The MDG grant from MoFED, established in 2011/12, is allocated to sector bureaus for capital spending in the five basic sectors. The spending mainly takes place in woredas, but the allocation criteria are according to sectors, not to woredas. The allocation of the MDG grant is therefore outside the scope of PI-8.

administrations as to how much block grant funding they are likely to receive, according to the allocation formula (dimension (i)), which enables them to start preparing their budgets.

Following approval of the Federal Government's budget at the end of June (end of fiscal year on July 7), regional governments make the necessary adjustments to their budgets if there has been any change to the initial ceiling, and inform the zones and special woredas of any changes made to their block grant allocations. Zonal and special woreda governments then adjust and finalize their draft budgets, usually within only a few days from the end of the FY. Quite often, the initial and final ceilings turn out to be more or less the same, and since the SNNPRS already has a good idea of the percentage of the overall block grant that it will receive from the Federal Government, it has a high degree of confidence in how much will be allocated in monetary terms. According to the BoFED Budget, Plan, Monitoring and Evaluation Core Process Owner, this is also true with respect to the resources to be received by zones and woredas.

*(iii) Extent to which consolidated fiscal data (at least on income and expenditure) is collected and reported for general government according to sector categories.*

Using IBEX, reports are prepared by the Accounts Department of BoFED following the standard chart of accounts used throughout all levels of government, according to administrative, sector and economic classification. The report for FY 2012/13 (EFY 2005) was finalized in early 2014 (within six months of the end of the FY) and was available to the team upon arrival in Ethiopia in April 2014. The process would be quicker were it not for connectivity problems.

**Table 3.13 PI-8 Results**

| PI-8 (M2) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | A | A | | **No change.** |
| (i) | A | A | The horizontal allocation of almost all transfers (at least 90% by value) from the Regional Government is determined by transparent and rules-based systems | **No change in terms of the rating,** but the introduction of a more rigorous way of assessing expenditure needs of sub national governments has strengthened transparency. |
| (ii) | B | B | Zonal and special woreda administrations are provided reliable information on the allocations to be transferred to them ahead of completing their budget proposals, so that significant changes to the proposals are still possible. | **No change.** Final ceilings are usually close to the initial ceilings and adjustments, if required, can be made within a few days. |
| (iii) | A | A | Fiscal information consistent with central government fiscal reporting is collected for 90% of zonal and special woreda administration expenditure and consolidated into annual reports within 10 months of the end of the FY. | **No change**. |

*Sources:* BoFED; Consolidated SNNPRS expenditure reports, EFY 2003-2005.

**PI-9 Oversight of aggregate fiscal risk from other public sector entities**

*(i) Extent of Regional Government monitoring of financial position of public enterprises*

SNNPRG provides start-up capital to public enterprises when they are established, but does not subsidize them. The Water Works Authority was the only SNNPRG-owned public enterprise at the time of the 2010 assessment. Since then, SNNPRG added two public enterprises: the Regional Housing and Development Enterprise and the Design and Construction Enterprise. Each enterprise has a governing Board whose members are drawn from the parent sector bureau. The SNNPRG does not provide guarantees for loans received by these enterprises; any loans they receive have to be collateralized against their own assets.

Monitoring and oversight of these enterprises is based on the proclamation enacted for their establishment. The enterprises prepare quarterly reports and annual financial statements, which are audited, and submit these to their respective Board members and to the Regional Cabinet. BoFED has access to these reports upon request. Given so few enterprises to monitor, the concept of consolidated formal fiscal risk reports does not apply. Board members, Regional Cabinet and BoFED can identify any potential fiscal risk through scrutiny of the quarterly reports and annual financial statements.

*(ii) Extent of monitoring of the fiscal position of subnational governments*

Zonal administrations are not allowed to borrow. Enforced financial regulations prohibit over committing of expenditure (in terms of the approved or adjusted budget), thus payments arrears through over-commitment are not possible. Zonal administrations' main source of revenue is the block grant. Since the block grant is very predictable, it is unlikely that zonal administrations would face significant resource shortfalls. When woredas and zones incur shortfalls in the collection of nontax revenues (which they own, as opposed to the tax revenues that they collect on behalf of SNNPRG) relative to budgeted amounts, BoFED may transfer cash to them in the form of loans to be refunded from next year's collections. As of July 7, 2013, the trial balance showed a receivable of ETB 287.4 million (account codes 4206-4207). Any shortfalls in refunding can be offset by reductions in the monthly block grant. The zonal and woreda administrations, therefore, have a strong incentive to collect the nontax revenues for which they have budgeted.

The SNNPRG guarantees loans made by banks to farmers' cooperatives and unions, and zonal administrations are responsible for ensuring that these loans are repaid (PI-17). As in the other regions, defaults result in SNNPRG reducing the block grant by the amount of the default, thereby also providing a strong incentive for zonal and woreda administrations to follow up on defaulters.

The SNNPRG BoFED monitors the financial situation of the zonal administrations and special woredas through the reports they submit every month. The Single Pool system at woreda level facilitates such monitoring, the WoFEDs being effectively in charge of the PFM systems of the woreda sector bureau.

**Table 3.14 PI-9 Results**

| PI-9 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | A | A | | **No change.** |
| (i) | A | A | The concept of consolidated fiscal risk reports does not apply to SNNPRG, as there are only 3 public enterprises, none of which receive subsidies, and all of which report quarterly and submit audited annual accounts to their governing boards. BoFED has access to | **No change**. |

| | | | | |
|---|---|---|---|---|
| | | | these. | |
| (ii) | A | A | Zonal and woreda administrations cannot generate fiscal liabilities for SNNPRG. Their fiscal position is continuously monitored. | **No change**. |

*Source:* Information provided by BoFED.

### PI-10 Public access to key fiscal information

Transparency depends on whether information on the fiscal plans, position, and performance of the Government is easily accessible to the general public, or at least to interested groups.

Transparency has improved to an extent, partly through the PFM Support Teams established by BoFED since the 2010 PEFA assessment through the Fiscal Transparency and Accountability Program (FTAP), and the technical assistance (TA) aspects of the follow-up PBS program. Nationwide Internet connectivity issues outside the control of SNNPRG have constrained public access to SNNPRG websites, which, if they had been functioning properly, would have facilitated timelier updating and thus a higher rating. More details are provided in Table 3.15, below.

**Table 3.15: Elements of Information for Public Access**

| Elements of information for public access | Availability and means |
|---|---|
| 1. Annual budget documentation when submitted to legislature. | **Not met. No change**. The budget documentation is not available to the public until the Regional Council approves the budget (at which point it is published through the Budget Proclamation). The Budget Speech is publicized on radio and TV, but not in document form, and details on the proposed budget are not provided. Interested members of the public are allowed to watch the debate on the draft budget. |
| 2. In-year budget execution reports within one month of their completion. | **Not met. No change**. BoFED prepares monthly budget execution reports, both at regional bureau and woreda level, but does not publish them, either in hard copy or through its website (www.snnprsbofed.gov.et). The Regional Council receives quarterly and semi-annual budget performance reports, but these are not available to the public. As with other SNNPRG websites, BoFED's website was not functional at the time of the assessment. |
| 3. Year-end financial statements within 6 months of completed audit. | **Not met. No change.** Audited year-end financial statements are not published, either by BoFED or by ORAG; the Regional Council has access to them. |
| 4. Availability of external audit reports to the public. | **Not met. No change**. There was some temporary improvement, with the audit reports for FYs 2007/08 and 2008/09 (EFY 2000 and 2001) published on ORAG's website (www.snnpraudit.gov.et). The website, however, has not been updated since 2010 and therefore the reports for EFY 2002 and EFY 2003 (2009/10 and 2010/11) have not been posted. |
| 5. Contract awards with value above approximately US$ 100,000 are published at least quarterly. | **Met**: Improvement. Contract awards are now publicized on notice boards (PI-19) and on www.snnprsbofed.gov.et, when it is functioning (depending on connectivity, beyond the control of PPA). |
| 6. Availability to public of information on resources for primary service units. | **Met. No change**. Availability of information on resources provided for primary service delivery units (SDU) has improved through the FTAP program and the operations of GEQIP (with regard to primary schools). Information on planned and actual spending and resource availability is posted on public notice boards (as elaborated |

| | |
|---|---|
| | on under PI-23). The project is in the process of being rolled out to all woredas. Mass media and community organizations are increasingly disseminating information. |
| 7. Information collated by ORG on fees, charges and taxes collected by woreda governments | **Not met.** The information is contained in IBEX-generated in-year revenue performance reports, but these are not available to the public (element 2). |

**Table 3.16 PI-10 Results**

| PI-10 | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | C | C | The 5th and 6th items are met. | **Unchanged in terms of the rating, but performance has improved under element 5.** The 7th element was added in FY 2013 under the PEFA SNG Guidelines (FY 2013), but for comparability, performance change is assessed based on the original six elements. Nationwide Internet connectivity issues beyond the control of BoFED and ORAG hinder publicizing of reports. |

*Sources:* BoFED, ORAG reports, Budget Proclamations.

## *3.4 Policy-Based Budgeting*

### PI-11 Orderliness and participation in the annual budget process

*(i) Existence of and adherence to a fixed budget calendar*

The budget calendar has changed little since the 2010 PEFA assessment, though it has shifted forward by about two weeks, which reduces time for budget preparation. The calendar allows six weeks for sector bureaus to submit their budget requests to BoFED, following its issue of the Budget Call (BC) in mid-February (i.e. submit by end of March); at the time of the 2010 assessment, the BC was issued in late January. Most bureaus (90 percent, according to BoFED) meet this deadline, but some do not submit until mid-May. Following evaluation by BoFED of these requests and subsequent hearings with BIs during April, BoFED presents its recommendations to the Regional Cabinet on allocations to bureaus and on block grant allocations to zonal administrations and woredas. These recommendations consider proposals submitted by BIs for any new spending (i.e. additions to existing services and establishment of new services).

By mid-April, MoFED has issued its notification on block grant allocations to Regional Governments. The allocations, by virtue of their dominant role in financing regional state expenditure, effectively set the regional states' overall spending. The notification is regarded as temporary, pending parliamentary approval of the Federal Government budget at the end of June. Following Regional Cabinet approval of BoFED's recommendations, budget ceilings are sent out in mid-May to bureaus, which then have three weeks to prepare detailed estimates to fit within these ceilings and submit to BoFED. Much of the estimation work has already been carried out during the preparation of budget requests. BoFED prepares the draft Budget Proclamation based on these estimates.

Some adjustments to the ceilings may be necessary if the block grant to SNNPRS, approved by the Federal Parliament at the end of June, differs from the one indicated earlier by MoFED. Any differences tend to be minor, allowing the finalized draft Budget Proclamation to be submitted to Cabinet and then the Regional Council for approval by the end of the financial year on July 7, or shortly thereafter.

The BoE and BoH indicated that the time allowed to prepare budget requests was sufficient, though BoE indicated that the process should start a little earlier.

*(ii) Guidance on the preparation of budget submission*

The "Guidelines for Public Bodies Preparing Budget Requests" contained in the Federal Government's Budget Manual (FY 2007) have not changed since the 2010 PEFA assessment. A two-stage process is involved. First, BoFED issues a circular that requires bureaus to complete standardized budget preparation forms to submit budget requests. The forms provide for the detailed estimation of recurrent and capital expenditures for the coming year based on the expected outturn for the current year; in other words, based on the existing levels of services. They also provide for prioritized and well-justified proposals for new capital projects.

Following the submission of Budget Requests to BoFED and subsequent discussion of these, the Regional Cabinet may decide on reallocations between BIs (partly based on the proposals in the budget requests for new capital projects), taking into account the allocation to bureaus of any extra fiscal resources ("fiscal space") that may have become available, particularly through the identification of matching savings by BIs. The BoFED then sets firm ceilings for preparation of the detailed budget estimates, the ceilings having been approved by the Cabinet, and instructs BIs to prepare detailed estimates on the basis of the ceilings. In effect, there are two budget circulars corresponding to the two stages, the first of which is formally known as the BC.

The sector bureaus interviewed had no problem with the clarity of the budget preparation guidelines.

*(iii) Timely budget approval by the legislature*

In two of the last three years, the budget has been approved around the start of the Ethiopian financial year (July 7). The budget for FY 2013/14 (EFY 2006) was not approved until July 28, 2013, due to the mourning period for the late Prime Minister.

**Table 3.17: PI-11 Results**

| PI-11 (M2) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B+ | A | | **Performance improved under dimension (iii)** |
| (i) | A | A | A clear annual budget calendar exists, is generally adhered to and allows budget institutions sufficient time (and at least six weeks from receipt of the budget circular) to complete the detailed estimates. | **No change** in terms of rating. The calendar is not 100% followed, but BIs still have enough time to prepare budget requests. |
| (ii) | A | A | A comprehensive and clear budget circular is issued to regional bureaus that reflects ceilings approved by Cabinet prior to the circular's distribution to MDAs. | **No change**. |
| (iii) | C | B | The legislature approves the budget close to the start of the fiscal year, but a delay of up to two months has happened in 1 of the last 3 years. | **Performance improved**. |

*Sources:* Federal Government Preparation MI (FY2007); Budget Proclamations; meetings with Planning & Budget Department, BoFED and with BoH and BoE.

### PI-12 Multiyear perspective in fiscal planning, expenditure policy and budget

*(i) Preparation of multiyear fiscal forecasts and functional allocations*

The Federal Budget Manual (FY 2007) indicates (under section 6, Budget Calendar) that Regional Governments, as with the Federal Government, should prepare a medium-term macroeconomic and fiscal framework (MEFF). The 2010 PEFA assessment indicates that BoFED was doing this with forecasts of fiscal aggregates being prepared for the following three years on a rolling basis (as also confirmed under Element 1 of PI-6 on content of budget documentation submitted to the Regional Council). BoFED is no longer preparing this, however, due to capacity constraints caused by high staff turnover. It is beginning to prepare forecasts of regional GDP as a first step towards preparing an MEFF.

A medium-term expenditure framework (MTEF), showing projections of functional allocations, is also not yet in place for the following reasons:

- The MEFF, which would provide the aggregate spending ceiling for the MTEF, is not yet in place.
- Sector bureaus are not yet preparing rigorous forward expenditure estimates (FEE), a prerequisite for an MTEF; FEEs (also known as baseline estimates) are projections of

expenditures under existing service delivery levels, and include the recurrent costs implied by committed capital expenditures.

- A program budgeting framework is still being rolled out at the federal level within the Federal Government's MTEF. Piloting has started in some regions, including the SNNPR. BoFED has prepared draft pilot program budgets for FY 2014/15 (EFY 2007) for the education and agriculture sectors, partly using the framework used by the UN Executing Agencies (e.g., UNICEF) – in particular, for its projects in Ethiopia. The drafts have been submitted to Cabinet. Roll out for FY 2015/16 (EFY 2008) is a possibility.
- High staff turnover causes capacity constraints.

*(ii) Scope and frequency of debt sustainability analysis*

This dimension is not applicable, as SNNPRG does not borrow and has no debt obligations. As indicated under PI-9 and PI-17, it guarantees short-term commercial bank loans to farmers' cooperatives but protects itself against the risk of default.

*(iii) Existence of costed sector strategies*

Sector strategies are prepared at Federal Government level based on the Growth and Transformation Plan (GTP 2010/11-2014/15), and then adapted to regional level. The 2010 PEFA assessment indicated that the BoE and BoH had prepared costed sector strategic plans. The assessment team was unable to review these, but a review of the Federal Government equivalents indicated that they were fiscally unrealistic.

The BoE and BoH now have new strategic plans based on the GTP: the Education Sector Strategic Plan and the Health Sector Development Plan, both covering FY 2010/11-2014/15 (EFY 2003-2007). During its first visit (May 2014) the team was unable to obtain copies of the plans, partly because of Internet connectivity problems, but the Planning and Budgeting Department in BoFED indicated that neither was costed. The team was able briefly to review the Health Sector Development Plan IV, covering EFYs 2003-2007. The Plan places more emphasis on quality and less on access; it is well prioritized but not costed.

*(iv) Linkages between investment budgets and forward expenditure estimates*

Capital projects are selected based on sector strategies, which are based on the GTP.

Formal forward expenditure estimates are not yet prepared, as noted in dimension (i). BoH noted that even if they were being prepared, the separation of recurrent and capital budgeting functions between lower levels of government and the Regional Government respectively would complicate the inclusion of future recurrent costs implied by committed capital projects. For example, zonal administrations bear the recurrent costs of operating a health center, while Regional Governments bear construction costs.

The Guidelines for Preparing the Capital Budget (contained in the 2007 Federal Budget Manual) stipulate that a public body should assess the recurrent budget implications of new capital projects before it includes them in its Budget Request. It seems that public bodies find these guidelines difficult to follow, though they do it to some extent. As noted in the 2010 PEFA, the linkage in the education sector is implicit, as the number of classrooms and schools to be constructed ultimately depends on projections of student enrollments and the recurrent expenditures that these generate. The DP-supported General Education Quality Improvement Program (GEQIP) includes a capitation grant element that partly provides for maintenance expenses.

MDG's FY 2011/12 grant for funding capital projects in zonal and woreda administrations is, with the help of DPs' grant funding, putting more pressure on zonal/woreda administrations to budget accurately for the future recurrent costs implied by capital investments.

**Table 3.18: PI-12 Results**

| PI-12 (M2) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-12 | C | D+ | | **Reduced performance under dimensions (i) and (iii)**. |
| (i) | C | D | No forward estimates of fiscal aggregates are undertaken. | **Reduced performance**. BoFED has stopped preparing MEFFs, partly due to capacity constraints. |
| (ii) | NA | NA | Not applicable | **Unchanged performance.** |
| (iii) | C | D | Sector strategies have been prepared for some sectors, but none of them have substantially complete costing of investments and recurrent expenditure. | **Reduced performance**. Currently, there are no costed sector strategic plans, partly due to capacity constraints. Previously there were some costed, but fiscally unrealistic plans. |
| (iv) | C | C | Planned investments are based on the GTP and sector strategies, where these exist. Formal forward expenditure estimates are not yet prepared, but annual budget submissions indicate to an extent the future recurrent costs implied by proposed capital investments. | **No change**. |

*Sources*: (1) GTP; (2) meetings with Planning and Budgeting Department in BoFED and with representatives of BoH, BoE and Rural Roads Authority; (3) "SSNPRS Education Sector: Summary Report on GTP Targets (2003-07) and Achievements in the Education Sector," submitted to BoFED, October 2012; and (4) Health Sector Development Plan IV (EFYs 2003-07).

## *3.5 Predictability and Control in Budget Execution*

### 3.5.1. Revenue administration

### PI-13: Transparency of taxpayer obligations and liabilities

### Background

Proclamation no. 104/FY 2011 (implemented after the 2010 PEFA Assessment) reestablished the Southern Nations Nationalities and Peoples Regional State Revenue Authority (RA) to manage the SNNPRG tax system more effectively. In its first incarnation, the RA had limited power and responsibility, but it now has a wider scope of responsibilities, including investigating tax offenses and organizing its own prosecution and investigation units. The General Manager is a member of the Regional Executive Council and accountable to the President. The RA's Human Resource Management (HRM) system falls outside the civil service system.

The RA has three core functions: (1) collection, assessment and data measurement; (2) revenue study, taxpayer education and training; and (3) enforcement, audit and investigation. It employs 3528 staff located in the 172 zone, woreda and city administration branches. RA headquarters is not involved in operational activities, and instead mainly plays a coordinating role. Actual revenue collection is undertaken by the 172 tax centers.

The Constitution of the Federal Democratic Republic of Ethiopia (FDRE) clearly defines the power and distribution of taxation responsibilities of the Federal and Regional Governments (articles 96-98) with regard to SNNPRS, as tabulated in Table 3.19.

**Table 3.19: SNNPRG Revenue Assignments**

| | |
|---|---|
| SNNPRS revenues (Article 97) | • Taxes on incomes of regional and private sector employees<br>• Fees for usufructory land rights (Land Use Tax (urban and rural))<br>• Taxes on the incomes of private and unincorporated farmers<br>• Taxes on the profits of resident merchants<br>• Sales tax/turnover tax<br>• Water transport fees within the region<br>• Rental incomes on Regional Government houses and properties<br>• Taxes on Regional Government enterprises (including excise tax)<br>• Regional license fees<br>• Royalties on the use of forest resources |
| Revenues shared between the federal govt. and SNNPRS (Article 98) | • Taxes on jointly-owned enterprises<br>• Taxes on corporation profits and shareholder dividends<br>• Taxes on large-scale mining, petroleum and gas operations |

VAT, which was introduced after the establishment of the Constitution, is shared between the Federal Government and the regions as follows:

- VAT assessed on incorporated bodies with a head office in Addis Ababa is assigned to the Federal Government;
- VAT assessed on incorporated bodies with their head office in SNNPR is shared between the Federal Government and the SNNPRS on a 70:30 basis;
- VAT assessed on sole traders is assigned to the region in which the trader is based;
- Recently, excise tax on chatt was assigned to the SNNPRS.

There are no revenue sharing arrangements between the SNNPRG and the zonal and woreda governments. In principle, tax revenues collected by woreda offices belong to the SNNPRG. For the sake of efficiency, the local governments retain revenues from agricultural income tax and rural land use fees up to the approved budget ceiling, and the block grant from SNNPRG is commensurately reduced. Nontax revenues, such as royalties, casino license fees, and stamp duties, belong to the woreda or city administration governments and are collected by them

*(i) Clarity and comprehensiveness of tax liabilities*

The 2010 PEFA assessment lists the tax laws that are under implementation by the SNNPRS and consistent with the revenue assignments described above. Some of these have since been amended, including:

- Income Tax Proclamation No. 56/FY 2003 (EFY 1995) as amended by Proclamation No.136/FY 2010 (EFY 2003). The amendment standardized the criteria for levying penalties, thereby reducing the scope for the exercise of discretionary power by officials;
- Stamp Duty & Sales Proclamation 135/FY 2010 (EFY 2003) as amended by Proclamation No. 203/FY 2011 (EFY 2003);

- Turnover Tax Proclamation No. 57/FY 2003 (EFY 1995), as amended by Proclamation No. 134/FY 2010 (EFY 2003);
- Chatt Sales Tax Proclamation No. 23/FY 1999 (EFY 1991) as amended by Federal Proclamation No. 125/FY 2013 (EFY 2005);
- Regulation No. 91/FY 2011(EFY 2003) along with directives for the use of cash register machines (introduced in FY 2011) in the interests of efficiency, reliable data collection, fairness and effectiveness.

The 2010 assessment noted that the legislation was reasonably comprehensive and clear, with limited and clearly stated discretionary powers, though in practice the amount of discretion exercised by RA might exceed limits.[12] The 2010 amendment to the Income Tax Proclamation reduced the scope for the exercise of such discretion.

*(ii) Taxpayer access to information on tax liabilities and administrative procedures*

The 2010 PEFA assessment indicated that the location of RA branch offices in woredas and towns facilitated access by the public and businesses to explanatory brochures. In addition, the RA was running radio programs twice a week, conducting question-and-answer sessions in tertiary education institutions, and promoting tax clubs in schools, churches and mosques, and youth and women's associations. It provided face-to-face training to Category A and B taxpayers. RA was also developing a website that would also improve taxpayer access to information.

The RA established its website (www.snnpr.rev.gov.et) in 2011, giving taxpayers easy access to tax rules, regulations, directives and other information. The website is functional despite some connectivity problems. In addition, the RA currently uses the services of three radio stations (Radio Fana, Radio Shashemene and Radio Sodo) to disseminate information to taxpayers; conducts tax-related conferences; and awards prizes to people who pay their taxes on time. In 2013, the RA signed a citizen's charter with the regional Chamber of Commerce to help improve taxpayers' compliance. Woreda and city administration levels are also expected to sign the charter. The RA also prepared explanatory manuals for the three categories of taxpayers (A, B, and C). The dissemination of information and education services has enabled the RA to receive extensive feedback from taxpayers on the clarity of tax laws and the services provided to customers.

The introduction of the block management system in 2011 as a means of strengthening compliance (PI-14) also provided a useful means of strengthening taxpayer understanding of the tax system.

*(iii) Existence and functioning of a tax appeals mechanism*

The 2010 assessment indicated that a tax appeals system had been put in place for the four major taxes, provided for under the Income Tax Proclamation No. 56/2003 (EFY). The appeals system consisted of three tiers: (1) Appeals Review Committee (ARC) within RA; (2) independent Tax

[12] These are: (a) Minister of Finance and Economic Development may waive tax liabilities up to ETB 100,000 at his discretion in cases of grave unavoidable hardship; approval of the Council of Ministers is required for waivers of tax liabilities greater than ETB 100,000; (b) the Head of BOFED may waive tax liabilities under similar circumstances up to ETB 75,000 at his discretion; approval of the Council of Regional State is required for higher amounts. A similar discretionary power is provided to the Head of BOFED in the case of the turnover tax (section 39) and to the Regional Government in the case of the land use fee and agricultural income tax (e.g. because of drought). Presumptive taxation (for businesses with less than ETB 100,000 turnover a year) implies discretionary powers by definition (as, in the absence of books of account, the Revenue Authority has to make an estimate of turnover and reach agreement with the business people on this).

Appeals Commission (TAC); and (3) the Court of Appeal (the judicial system of the region – High Court, Supreme Court and, Panel Court). The ARC and TAC were established at regional, zonal, woreda and city levels. The tax appeals mechanism is the same for each type of tax and is described in detail in the Income Tax Proclamation and an associated directive, and is summarized in the other tax proclamations.

A taxpayer has 10 days to appeal to the ARC against an assessment. The appeal is lodged in the respective woreda or city administration office, via the Revenue Study, Taxpayer Education and Training Work Process of the office. The ARC consists of three members, all from the Work Process, who are appointed by the head of the Process in the next higher level of government. The ARC hears both sides and is expected to respond to the appellant within a day, but the actual response time averages three days. If the appellant is not satisfied with the ARC's decision, he/she can apply to the second appellate tier (the TAC).

A taxpayer has up to 30 days to appeal to the TAC but must pay 50 percent of the disputed assessment pending resolution. The TAC should respond within five to 10 days, although exceptional cases might take a month or longer.

The team visited the regional TAC office in Hawassa and met Ato Anesa Melko Hebro, chairperson of TAC and the advisor to the SNNPRG President, who appointed him. The TAC operates at different levels of government, each independent of each other. The chairperson at each level is appointed by the head of the Government one level up. The TAC was established in January 2011 and works like a court. It is completely independent from the Regional Government. The TAC has six members, comprising two from the region's Chamber of Commerce (nongovernmental), one from the Trade Bureau, one from BoFED, one from the Justice Bureau and one from the RA, in a non-voting capacity. The TAC convenes only to hear appeal cases, and will not convene if members from the Chamber of Commerce (CoC) and Justice Bureau are absent. A decision is usually reached within a day over simpler cases, but a maximum of 30 days is available if required in rare and complicated cases.

Most cases submitted to TAC concern VAT-related issues, for example businesses trying to avoid VAT registration by hiding their income to stay below the threshold. The TAC may request technical assistance from the RA, but in most cases the expertise of the TAC members (who are mostly accountants and lawyers) is sufficient to resolve cases. The decision of the TAC is wholly implementable. Table 3.20 shows the appeal cases handled by the two appellate bodies.

**Table 3.20: Tax Appeals Commission and Review Committee Performance**

| Cases received and verdicts passed | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **Body** | **FY 2010/11** | | **FY 2011/12** | | **FY 2012/13** | | **Total** | | **%** |
| | **Cases** | **Verdicts** | **Cases** | **Verdicts** | **Cases** | **Verdicts** | **Cases** | **Verdicts** | **Perfor mance** |
| **ARC** | **3,679** | **2,973** | **3,559** | **3,456** | **30,978** | **30,908** | **38,216** | **37,337** | **98%** |
| **TAC** | **7** | **7** | **2** | **2** | **2** | **2** | **11** | **11** | **100%** |
| **Total** | **3,686** | **2,980** | **3,561** | **3,458** | **30,980** | **30,910** | **38,227** | **37,348** | **98%** |

*Source:* SNNPRS Review Committee & Tax Appeal Commission

The number of cases increased by 840 percent over the three-year period, indicating increasing use of the appeals system. Ninety-eight percent of the 38,227 cases received over the period were addressed. The very large increase in FY 2012/13 is related to presumptive taxes being levied on Category C taxpayers, who number 130,000 out of 154,000 taxpayers. Presumptive tax is levied on presumptive levels of turnover estimated by RA, so queries are likely to be higher under this tax scheme than for other taxes.

The proportion of complaints being settled at the ARC stage jumped sharply to 79 percent in FY 2012/13, from 16 percent in FY 2011/12, perhaps indicating better understanding by taxpayers of the tax system.

The proportion of cases decided in favor of taxpayers (conviction rate) by the TAC was 36 percent, while 64 percent of cases were settled in favor of the RA. The ARC conviction rate was roughly 30 percent in favor of taxpayers and 70 percent in favor of the RA. Decisions are implemented straightaway, including the refund of the portion of the 50 percent deposit owed back to the appellant. These statistics indicate that the appellate system is reasonably free and fair.

A party dissatisfied with the decision may appeal to the High Court (tier 3) within 30 days of the decision on the grounds that the decision is erroneous in terms of the law. The appellant, however, must deposit 100 percent of the assessed tax liability. An appeal to a higher appellate court may still be made within a further 30 days. Very few cases have followed this route.

**Table 3.21 PI-13 Results**

| PI-13 (M2) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B↑ | A | | **Performance improved under all dimensions** |
| (i) | B↑ | A | Legislation and procedures for all major taxes are comprehensive and clear, with strictly limited discretionary powers of the revenue authority. | **Performance improved** with standardization of criteria for waiving penalties, which reduced opportunities for the exercise of discretionary power. |
| (ii) | B↑ | A | Taxpayers have easy access to comprehensive, user-friendly and up-to-date information on tax liabilities and procedures, and the RA supplements this with taxpayer education campaigns. | **Performance improved**. The establishment of the RA website gives taxpayers better access to tax rules, regulations and directives. |
| (iii) | B↑ | A | A tax appeals system of transparent administrative procedures with appropriate checks and balances, and implemented through independent institutional functions, is completely set up and effectively operating with satisfactory fairness, and its decisions are promptly acted upon. | **Performance improved**. The 2010 PEFA rating was too high, as the TAC was not in fact established until after the assessment. |

*Sources:* Revenue proclamations; meetings with the RA and TAC.

## PI-14 Effectiveness of measures for taxpayer registration and tax assessment

*(i) Controls in the taxpayer registration system*

The 2010 PEFA assessment noted the requirement under article 44 of the Income Tax Proclamation (ITP) for all people with a potential or actual tax obligation to obtain a taxpayer identification number (TIN). The issue confronting the RA was to ensure that everyone (individuals and businesses) who should have a TIN did have a TIN. Checkpoints included:

- The requirement to have a TIN to obtain/renew a business license (article 46, ITP). The RA could then check whether a business was registered for other taxes (VAT, excise taxes, turnover tax). An electronic connection with the Trade and Industry Sector Bureau (TISB) alerting the RA to an application for a business license would have strengthened this checkpoint, but such a connection has not yet been established. The RA has access to the business directory maintained by the TISB; this showed an increase in the number of businesses to 159,000 from 132,000 during the first nine months of EFY 2006 (due to the booming economy), reinforcing the need for RA to keep on top of the situation.
- The requirement that prospective bank borrowers have tax clearance certificates, which in turn requires TINs. Banks do not, however, yet require TINs from bank account applicants.
- The requirement for businesses bidding for government contracts to have tax clearance certificates.
- Other checkpoints include the Ethiopia Revenue and Customs Agency (ERCA) and business registries in other regions.

A major development since the 2010 PEFA assessment is the establishment of an automated SIGTAS-linked TIN registration system using biometric finger printing-based technology. This began in September 2009 at the federal level through the initiative of ERCA and has since been in the process of being been established at regional level. As of the time of the study 356,803 fingerprints, including those of students and business enterprises, have been collected in SNNPR. Of these, 170,466 are formal taxpayers (including government employees) of whom 154,000 are business people. There are now 22 tax centers with online finger print services converting fingerprints to TINs. Once a taxpayer is registered, a card containing the TIN and bearing a photo of the taxpayer is produced and issued as soon as possible. The process is not yet complete, as SIGTAS has still mainly been established in urban areas.

The strengthening of taxpayer services and education programs (PI-13 ii) is contributing greatly to voluntary compliance with taxpayer registration and declaration obligations. The newly signed citizen's charter will enable more taxpayers to register. The introduction of the block management system in FY 2011/12 appears to have been particularly effective. For instance, in FY 2012/13, 132,000 taxpayers were registered. During the first nine months of FY 2013/14, a further 27,000 were registered, an increase of 12 percent.

*(ii) Effectiveness of penalties for noncompliance with registration and declaration obligations*

Penalties for noncompliance are based on Federal Government tax laws and have not changed since the 2010 PEFA. They are set out in the tax proclamations and appear to be high enough to have potential and significant impact. Section VII of the Income Tax Law provides for seizure of property in the event of default; Section VIII provides for administrative penalties; and Section IX provides for criminal penalties. The Turnover, VAT and Excise Tax Proclamations have penalties of similar scale and also charge interest on late payments. The penalty for late payment under the Agriculture Income Tax proclamation is two percent of the amount of tax due for each month the payment is in default and criminal penalties are according to the penal code. The Stamp Duty and Chatt Excise Tax also stipulate penalties.

A new penalty added since the 2010 PEFA assessment pertains to cash register machines. According to article 17 of the Cash Register Machine Regulation No.91/FY 2011, when a taxpayer, in violation of the regulation, fails to use sales machines, in addition to being held criminally responsible for his acts as provided by the relevant tax law, his business license shall also be revoked.

The main issue with the penalty system appears to be that taxpayers are still not complying with their obligations, suggesting that the system is ineffective. The penalty waiver introduced (following the Federal Government's example) through the amendment to the Income Tax Proclamation of 2010 (PI-13 i) permits penalties to be waived if taxpayers pay past due taxes and associated interests. The incentive for complying with the directive is the avoidance of heavier penalties at a later date (due to accrued interest).[13] Government's revenue ends up higher using such a penalty waiver scheme.

*(iii) Planning and monitoring of tax audit and fraud investigation programs*

About 15 percent of the 154,000 taxpayers in SNNPRS are in the A and B categories (9,000 in Category A, with turnover of at least ETB 500,000 a year, 15,000 in Category B, with turnover of ETB 100,000-500,000), while 130,000 taxpayers fall into Category C, most of whom are small taxpayers, who do not maintain books of accounts and pay presumptive tax; the predominance of Category C taxpayers has changed little since the 2010 PEFA assessment. Therefore, this dimension applies only to taxpayers in the A and B categories. Capacity constraints preclude audit of all these taxpayers every year. Auditee selection should focus on taxpayers who pose relatively significant risk.

The 2010 PEFA assessment noted that following the adoption and implementation of a BPR process, the tax audit system was in the process of being strengthened through the creation of a Tax Audit Department, the adoption of a risk-based audit approach, and the carrying out of audits based on annual audit plans. Strengthening has continued since then. The tax audit procedures for taxpayers in the 36 tax centers that use SIGTAS have been aligned with SIGTAS, enabling the use of rigorous risk-based criteria for auditee selection according to tax area. The bulk of Category A and B taxpayers use these tax centers. Risk-based audit criteria are still in the process of being introduced in the 172 SRA branches that are not yet using SIGTAS.

Under the direction of the Tax Audit Department at RA HQ, audit plans are prepared at regional, zonal and city administration levels and then compiled centrally. Since FY 2010/11 (EFY 2003), desk audits, comprehensive audits, service audits (during closing of businesses, which can be a long process), and investigative audits have been conducted. The number of auditors working at all government levels doubled from 65 to 127 over the last three years. Greater emphasis was placed on audit yield, and risk factors were the main criteria for auditee selection. As shown in Table 3.22, audit coverage was reduced to facilitate greater focus on risk. As a result, revenues nearly tripled due to the doubling of the number of auditors and a more than halving of the number of files per auditor. Auditor productivity, as measured by revenue generated per auditor, increased to ETB 0.98 million per auditor in FY 2012/13 from Br 0.69 million per auditor in FY

[13] A downpayment arrangement for tax liabilities is designed based on the directive, usually with a time limit of one to six months). Payments are made on a monthly basis and the sooner the payment is made the higher the rate of the penalties waiver (from 20 percent up to 100 percent). If tax liabilities are paid within one month the probability of a penalty waiver is 100 percent; if within two months, up to 80 percent waiver, depending on the reasons forwarded by the taxpayer for not complying. SIGTAS is programmed to administer these waivers.

2010/11.

**Table 3.22: RA Audit Plan and Performance for FYs 2010/11-2012/13**

| Budget year (FY) | No. of files to be audited | No. of files audited | Audit coverage % | Revenue generated (ETB, millions) | No. of auditors | Files per audit-or | Revenue generated per auditor (ETB millions) |
|---|---|---|---|---|---|---|---|
| 2010/11 (EFY 2003) | 538 | 496 | 92.2% | 44.66 | 65 | 8 | 0.69 |
| 2011/12 (EFY 2004) | 668 | 549 | 82.2% | 60.07 | 82 | 7 | 0.73 |
| 2012/13 (EFY 2005) | 755 | 422 | 55.9% | 124.29 | 127 | 3 | 0.98 |

*Source:* SNNPRS-RA Plan monitoring & feedback Sup Work Process

**Table 3.23 PI-14 Results**

| PI-14 (M2) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | C+↑ | B↑ | | **Performance strengthened under (iii) and is in the process of strengthening under (i) and (ii)**. |
| (i) | B | B↑ | Taxpayers are registered in a complete database with some linkages to trade licensing and company registration systems. | **Performance strengthening.** (i) The introduction of a biometric finger printing system. (ii) Further strengthening of taxpayer services and education programs, particularly through the new block management system. |
| (ii) | B | B | Penalties for noncompliance exist for most relevant tax areas. | **Performance strengthening**. The introduction of the penalty waiver scheme is an improvement, but not yet enough to increase the score. |
| (iii) | C↑ | B | Tax audits and fraud investigations are managed and reported on according to a documented audit plan, with clear risk assessment criteria for audits in at least one major tax area that applies self assessment. | **Performance strengthened**. A Tax Audit Department was established at the time of the 2010 assessment. Since then, annual audit plans have been introduced with greater focus on risk and the number of auditors increased sharply. Revenue generated nearly tripled as a result. |

## PI-15 Effectiveness in the collection of tax payment

*(i) Collection ratio for gross tax arrears*

It was not possible to rate this dimension in the 2010 PEFA assessment. The RA did not have a rigorous mechanism for tracking tax debts. SIGTAS was operational in only a few revenue offices and only covered VAT.

SIGTAS now has a debt tracking facility, covers more taxes and is operational in 36 out of the 172 RA branches, which is a small percentage in terms of numbers, but a significant percentage in terms of revenues collected. In practice, electric power and connectivity problems constrain SIGTAS operations. It is not yet operational in many woreda and city administration offices, where manual ledger cards are maintained instead for tracking arrears. Table 3.24 summarizes arrears of the region in FYs 2010/11, 2011/12, and 2012/13, based on SIGTAS and ledger cards.

**Table 3.24: RA Arrears Data, FYs 2010/11-2012/13 (EFYs 2003 -2005) (ETB, millions)**

| | 2010/11 | 2011/12 | 2012/13 |
|---|---|---|---|
| 1.Revenue collections | 932.02 | 1418.1 | 2216.8 |
| 2.End-year arrears | 111.8 | 91.5 | 101.1 |
| *3. End-year arrears as % of revenue collections (2/1)* | *12* | *6.5* | *4.5* |
| 4. End-year arrears collected following year | | 61 | 70.8 |
| *5. % end-year arrears collected (4/2 of previous year)* | | *54.6* | *77.3* |
| *6. Average arrears collection ratio, 2011/12-2012/13* | | *66%* | |

*Source*: SNNPRS-RA Tax Audit, Investigation, and Fraud Core Process

Table 3.24 indicates that the stock of end-year tax arrears varied between 4.5 percent of revenue collections and 12 percent during FY 2010/11 and 2012/13. Of the end-FY 2010/11 arrears (taxes overdue) of ETB 111.8 million carried over to FY 2011/12, ETB 61 million was collected that year (54.6 percent collection ratio), and new arrears of ETB 40 million accumulated. This resulted in end-FY 2011/12 arrears of ETB 91.5 million, equal to 6.5 percent of revenue collections. Of this amount, ETB 70.75 million was collected in FY 2012/13 (77.3 percent collection ratio) and new arrears of ETB 80 million were accumulated. This resulted in end-FY 2012/13 arrears of ETB 101 million, equal to 4.5 percent of total revenue collections. The collection ratios in FY 2011/12 and 2012/13 averaged 66 percent.

*(ii) Effectiveness of transfer of tax collections to the Treasury by the Revenue Authority*

A significant proportion of Regional Government tax revenue, particularly profit tax, turnover tax, Agricultural Income Tax, and Rural Land User fees, is collected by RA branches in woredas and city administrations and deposited daily into bank accounts held by WoFEDs and Town Administration Finance and Economic Development offices (ToFEDs). The RA cashier attaches copies of daily deposit receipts to taxpayer files. Bank advices and third copies of the receipts are then registered and enumerated in a form known as Me-Hi-65 and delivered to the WoFED or ToFED, which give the final treasury receipt to the RA cashier.

Although not directly relevant to this dimension, which focuses only on revenues due to the RA, a unique aspect in the SNNPRS is that service charges, fees, and other revenues collected by sector bureaus are deposited into their accounts in the CBE, from which transfers are made nearly every day to BoFED's bank account in CBE. In other regions, except Amhara, sector bureaus collect and transfer these revenues directly to BoFED.

*(iii) Frequency of complete accounts reconciliation between tax assessments, collections, arrears records, and receipts by the Treasury*

RA branches reconcile collected revenues monthly, and credit the amounts to BoFED's bank within 15 days from the end of the month. As indicated under PI-22 (ii), on clearance of suspense accounts reconciliation problems may arise due to recording errors in terms of revenue classification when revenues are deposited in the bank.

In principle, the arrears-tracking module in SIGTAS and the system of manual taxpayer ledgers introduced since the 2010 assessment should enable complete reconciliation between taxes collected and assessed, as arrears can be tracked, as noted under dimension (i). SIGTAS is functional, however, in only 36 RA branch offices and its operations are constrained by power and connectivity problems. Manual ledgers number in the thousands (one ledger per taxpayer), and are maintained in RA branch offices throughout the region, which makes routine and frequent reconciliation logistically impossible.

**Table 3.25 PI-15 Results**

| PI-15 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | D+↑ | D+ | | **Performance improved under (i)** |
| (i) | NS | C | The average debt collection ratio in the two most recent fiscal years was 66%, and the total amount of tax arrears at the end of each year was significant (above 2%) as a % of total revenue collections. | Dimension assessed on basis of SIGTAS recording system or through manual ledger card where SIGTAS is not operating. |
| ii | C↑ | A | Transfers to BoFED are made daily. | **No change**. The dimension appears to have been underscored in the 2010 assessment. |
| iii | D | D | Complete reconciliation of tax assessments, collections, arrears and transfers to BoFED does not take place annually. | **No change**. In principle, the tax debt recording system introduced since the 2010 assessment permits reconciliation. In practice, with SIGTAS only partly operational, routine reconciliation on the basis of the manual debt tracking ledgers is logistically too difficult. |

**PI-16 Predictability in the availability of funds for commitment of expenditures**

Effective execution of the budget in accordance with the work plans requires that the BIs receive reliable information on availability of funds within which they can commit expenditure for recurrent and capital inputs.

*(i) Extent to which cash flows are forecast and monitored*

The situation is the same as at the 2010 assessment, except that the revised Financial Administration Proclamation (2009) that came into effect in 2011, underpinned by a supporting Directive (2012), placed greater emphasis on the need for good cash flow forecasting.

The draft Budget Proclamation is approved by the RC in July, but is not fully implemented until September/October, as the proclamation is not disaggregated into account codes. Prior to that, the recurrent budget is released monthly on the basis of 1/12th of the approved budget.

Sector bureaus prepare a monthly cash flow projection for the new budget year at the beginning of the year. Projections include disaggregated revenue and expenditure projections, the latter taking procurement plans into account, and advance payments to contractors. The bureaus send the projections to Planning and Budgeting Department in BoFED for review. BoFED generally accepts forecasts with few modifications. At the same time, BoFED makes monthly revenue projections and combines these with its projections of the block grant from MoFED. The block grant comprises the bulk of SNNPRG's financial resources and the monthly receipts of this are highly predictable. The beginning-of-year cash flow forecasting provides the basis for BoFED to prepare a monthly cash plan for each BI.

Starting annually in September/October, cash flow forecasts are revised each quarter for each month within the quarter for recurrent expenditure (quarterly for capital expenditure), on the basis of actual cash flows to date, as shown in monthly reports prepared by BIs and submitted to BoFED. The forecasts have to be submitted to BoFED no later than 10 days before the beginning of the next quarter. BoFED holds meetings with BIs to discuss their out-turns and forecasts, and may compare BI performance against its cash plan to determine the scope for reallocations of underutilized budgets towards BIs that are over-performing and need more money. The Bureau of Health (BoH) provided the team with its monthly cash plan for FYs 2012/13 and 2013/14 (EFYs 2005-06) in aggregated form.

About 60 percent of expenditure consists of transfers to lower level governments and wages and salaries, the monthly forecasting of both of which is very straightforward.

Forecasting of receipts of donor project and program assistance is problematic, as noted in the 2010 PEFA report and under PI-2 in this assessment (a reason for the low rating for PI-2). This dimension is rated, however, only in relation to "domestic resources" cash flow forecasting.

*(ii) Reliability and horizon of periodic in-year information to regional bureaus on ceilings for expenditure commitment*

According to the head of BoFED's Financial Administration Department, BIs can commit expenditure with unlimited time horizons up to the end of the FY for eventual payments based on their cash plans, which are based on cash flow forecasts. If the timing of the payments turns out to be different from the timing anticipated in the cash flow forecast, the BI in question can request a re-phasing from BoFED and/or allocation from the contingency item. This happens rarely: a recent example was a payment certificate a contractor submitted in the third quarter, and not in the fourth quarter as per the cash plan. The BoE confirmed the infrequency of such events, and that BoFED has never refused such a request for adjustment. The predictability of the block grant from MoFED, and the large proportion of SNNPRG's financial resources that it comprises, make it likely that sufficient resources will be available for budget execution.

*(iii) Frequency and transparency of adjustments to budget allocations, which are decided above the level of management of regional bureaus*

As indicated in the annual Budget Proclamations for FY 2012/13 and 2013/14 (EFYs 2005-06) BoFED can make adjustments to budget allocations:

- *Transfers between bureaus that leave total spending unchanged.* Prior Cabinet approval is required. According to the head of the Financial Administration Department in BoFED, such transfers are rare; and

- *A change in allocations that results in an increase in total spending.* Prior Regional Council approval is required via a supplementary budget. In recent years, woreda and city administrations that collect nontax revenues larger than planned can spend the excess, subject to BoFED approval. Woreda and city administration councils approve the excess through a supplementary appropriation after the fact (which poses the risk of wasteful spending).

BIs may transfer appropriations between their cost centers (i.e. virements), without prior BoFED approval, unless the transfer is between projects.

In the case of the first bullet point above, some BIs may request reallocations if they need extra funding for some reason. BIs with unutilized budget (e.g. due to capital project implementation slower than planned, which is often the case due to capacity constraints) may notify BoFED through their updated quarterly cash flow forecasts. BoFED can then reallocate to other BIs. Reallocations from capital budgets to recurrent budgets are not allowed. BoFED must consult with BIs about the possibility of reallocating away from their approved budgets (except in the case of BIs underperforming on their wages and salaries budget). The reserve/contingency item in the Budget Proclamations (about 2 percent of the proclaimed budget) may be used to supplement BI budgets during the year.

The Head of the FAD in BoFED indicated that there are few annual reallocations between BIs. They are usually made based on quarterly reviews (both financial and physical) of budget performance and, in particular, the Midterm Review. Based on these reviews the expenditure contingency item may be allocated (averaging about two percent of total budgeted expenditure, as noted under PI-2).

The frequency of reallocations is low, however, occurring once or twice a year (mainly at mid-year). This results in the adjusted budget, as shown in in-year budget execution reports generated by IBEX. Supplementary appropriations proclamations are also infrequent, usually just once a year.

The in-year adjustment system has been in place for several years and familiarity and understanding of it have increased over time.

**Table 3.26: PI-16 Results**

| PI-16 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B+ | A | | **Performance improved under (i) and (iii)**. |
| (i) | B | A | A cash flow forecast is prepared for the fiscal year and updated monthly for recurrent expenditure (quarterly for capital expenditure) based on actual cash inflows and outflows. | **Performance improved**. The 2010 report states that capacity constraints precluded monthly updates. |
| (ii) | A | A | BIs are able to plan and commit expenditure for at least 6 months in advance in accordance with the budgeted appropriations. | **No change**. |
| (iii) | B | A | Significant in-year adjustments to budget allocations take place only once or twice a | **Performance improved**. The |

| | | | | |
|---|---|---|---|---|
| | | | year following quarterly, and, in particular, a midterm review that results in the adjusted budget. BoFED makes the adjustments based on a consultative process and does not impose them on BIs. Thus, the adjustments are carried out in a transparent and predictable way. | difference between A and B is mainly increasing familiarity with the system over time. |

**PI-17 Recording and management of cash balances, debt and guarantees**

*(i) Quality of debt data recording and reporting*

The SNNPRG may borrow from domestic sources with authorization of the Regional Council as per Financial Administration Proclamation 128/2009 (FY), article 41. This was not the case at the time of the previous PEFA assessment, which took place prior to the enactment of this proclamation. SNNPRG did not borrow in EFY 2003, 2004, and 2005[14].

*(ii) Extent of consolidation of the Government's cash balances*

BIs require BoFED's approval to open bank accounts. There are more than 650 bank accounts at regional bureau and zonal administration levels, excluding at woreda/city administration level offices.[15] There are four categories of bank accounts: the Z account, B account, MDG account and donor accounts (Channel 1a and 1b accounts). Z accounts are referred to as "zero balance accounts", which are virtual bank accounts that BoFED opened in CBE for 48 sector bureaus. BoFED sets a monthly cash withdrawal ceiling for each BI based on their monthly cash requirements, as derived from their cash flow forecasts (PI-16). BIs effect payments from the Z account to the extent of the ceiling. CBE clears the balance from Z accounts against BoFED's Central Treasury Account (CTA) at CBE on a daily basis. This arrangement represents the Treasury Single Account (TSA), which has been operational since FY 2007/08. Z accounts are not operational at zonal and woreda levels.

BoFED updates the record for CTA accounts on a weekly basis. There is no daily cash position report produced (unlike some regional BoFEDs). Instead, BoFED orally requests the balance from the CBE on a demand basis. CTA represents more than 75 percent of the Regional Government level cash balances.

B accounts are deposit accounts (revenue accounts) into which revenues collected by the BIs and woredas are deposited. Revenue collected by the RA is transferred to the CTA held by BoFED. The balance of all B accounts is transferred to CTA at the end of the fiscal year (July 7).

The MDG Fund account, established in FY 2011/12 (EFY 2004), is not part of the TSA. Instead, cash is transferred to the respective BIs into separate bank accounts opened at CBE for this purpose. The balance of MDG accounts is consolidated into BoFED's financial reporting system on a quarterly basis.

DP-funded projects maintain separate bank accounts at the level of BoFED, BIs and woredas, none of which are part of TSA. BoFED itself holds six Channel 1 bank accounts. Sector bureaus may hold multiple DP-funded bank accounts. For example, the BoE and BoH hold more than ten. Some DPs would like to have a separate bank account, but others do not mind if the money is kept in a pool bank account. BoH, for example, has more than 100 different DP funds, many of

[14] BoFED explained that the payables referred as "Treasury bill," and "direct advances" are accounting errors and do not indicate any borrowings.
[15] According to BoFED's stock count as of July 7, 2013.

which are kept in a pool account (but, as noted under PI-7 ii, efficiency gains from this arrangement are limited). The balance in each account is known at the level of BIs and reconciled periodically (PI-22), but is not consolidated into the overall SNNPRS cash balance position.

*(iii) Systems for contracting loans and issue of guarantees*

SNNPRG is allowed to borrow under the 2009 Financial Administration Proclamation but has not done so. It issues guarantees to CBE for loans to agricultural unions and cooperatives in the region for annual purchases of fertilizer for distribution to farmers. Guarantees have to be approved by BoFED and the Regional Council. If the unions or cooperatives fail to collect from the farmers, BoFED withholds its subsidy to the zones and woredas in which the farmers are located. The zones and woredas must then follow up with farmers on the loans they owe. The ceiling for the guarantee is determined by a proclamation issued by SNNPRG for every crop season. Data pertaining to the extent of guarantee were not available. The annual scheme is simple and clear.

For the 2010 assessment for ARG, the assessment team was not made aware of the loan guarantee scheme, hence the NR rating.

**Table 3.27: PI-17 Results**

| PI-17 (M2) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B | B+ | | Only dimension (ii) was scored in the 2010 assessment. Dim. (iii) should have scored A. |
| (i) | NA | NA | SNNPRS does not borrow | **NA** |
| (ii) | B | B | Most cash balances are calculated and consolidated at least weekly through the CTA/Z account system. CTA represents more than 75% of the regional cash balance. | **Performance unchanged**. |
| (iii) | NR | A | There is a system of provision of loan guarantee. | The NR rating in the 2010 assessment occurred because the assessment team was not made aware of the loan guarantee scheme. The guarantee system is simple and clear. |

### PI-18 Effectiveness of payroll controls

Payroll and personnel management are decentralized to public body level in Ethiopia, so the assessment team met officials from three BIs in addition to BoFED: BoE, BoH and Rural Road Authority (RRA).

Payroll is processed using in-house developed payroll software. The payroll software is used only for processing salaries of permanent staff. Excel is used to prepare payroll for project staff. Since EFY 2003, salaries have been paid into bank accounts.

*(i) Degree of integration and reconciliation between personnel records and payroll data*

The Finance, Procurement and Property Administration Departments (FPPAD) pays wages and salaries on the 24$^{th}$ of each month on the basis of an approved payroll sheet generated from payroll processing software. The Human Resource Department (HRD) maintains a personnel database in manual form, and informs FPPAD in writing whenever there is a change to personnel records. Each BI department maintains attendance and department heads transfer the attendance sheet (after signing) to HRD every month covering the period from 23rd of the previous month to 22nd of the current month. In addition, HRD issues to FPPAD a monthly list of employees to be paid for the month, consistent with any changes to personnel records it has made.

There is no online integration between the payroll system and the HR personnel database, as the latter is not automated. However, the accountants who prepare the payroll check the current month's payroll against the previous month's payroll and the communications from HRD on changes it has made to personnel records. Similarly, internal auditors check the current month's payroll sheets against the previous month's payroll and check whether changes are supported by evidence. Department managers sign payroll sheets to verify that they are correct before payment is transferred into employees' bank accounts.

*(ii) Timeliness in the introduction of changes to the personnel records and payroll*

HRD's records are updated on the same day the change (employment, termination, penalty, transfer, etc.) has taken place. All changes are copied to relevant departments and FPPAD. Payroll changes are made by FPPAD within a few days from the receipt of letters from HRD indicating changes, if any, in personnel records. Changes received after the 23rd of the month will be reflected on the subsequent month's payroll. Most changes are made before 23rd of the month, so retroactive adjustments to payroll records are rare. If a staff member resigns after receiving a full month's payroll on the 23rd of the month, the excess payment will be taken out of his/her termination-related benefits.

*(iii) Internal controls over changes to personnel records and the payroll*

The supporting documents for the changes in the personnel and payroll records are well documented and accessible for audit and review. The payroll software is password protected and only the accountant in charge of updating the software has access. The payroll sheet is signed by the accountant for preparation, verified by the Senior Finance Officer and approved by the head of the FPPAD.

The audit trail thus consists of letters of authorization of changes in personnel records signed by the head of HRD, the supporting documentation for these changes, records of changes made in the software used for payroll preparation in FPPADs, and the letter of authorization of the payroll run by the head of FPPAD.

*(iv) Existence of payroll audits to check for oversight errors and/or ghost workers*

As noted under dimension (i), internal auditors at each BI check payrolls against attendance sheets, as well as supporting documents for addition and deletion of staff from payroll and review the correctness of computations. They also check whether attendance sheets are maintained properly and account for absenteeism.[16] These checks do not constitute a comprehensive payroll audit, which would include a check that the personnel records are correct. A comprehensive audit that covers both payroll and personnel records has not yet been conducted.

ORAG also audits payroll as part of the annual financial audit. In a separate HR audit, internal auditors and ORAG audit personnel records for completeness and compliances and sometimes

[16] The Internal Audit units at BoE, BRRC and BoFED are copied for letters in connection with changes to personnel data.

review these records against payroll.[17] The Inspection Department and ORAG reported no irregularities related to internal control over payroll.

**Table 3.28: PI-18 Results**

| PI-18 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B+ | B+ | | **Performance improved under dimension (iv); it may have received too high a rating in the 2010 assessment.** |
| (i) | B | B | Personnel data and payroll data are not directly linked but the payroll is supported by full documentation for all changes to personnel records each month and checked against the previous month's payroll data. | **No change**. Payroll processing automated but automation is not yet extended to HR. BIs' HRDs submit hard copy documentation of changes to personnel records to FPPADs every month, which then make the appropriate changes in their payroll software. Reconciliation is conducted each month by the internal audit units of BIs. |
| (ii) | A | A | Required changes in the personnel records and payroll are updated monthly, generally in time for the following month's payments. Retroactive adjustments are rare. | **No change**. HRDs have to submit changes to personnel records to FPPAD before 23rd of the month in order for the changes to be reflected in the payroll for that month. Changes submitted after the 23rd will be reflected in the next month's payroll. Most changes are submitted before the 23rd so retroactive adjustments are rare. |
| (iii) | A | A | Authority to change records and payroll is restricted and results in an audit trail. | **No change**. The control system on payroll is strong and the system provides an audit trail so that changes to personnel and payroll records can later be reviewed. |
| (iv) | B | B | A payroll audit covering all Regional Government entities has been conducted at least once in the last 3 years (whether in stages or as a single exercise). | **Performance improved**. A comprehensive payroll audit has not yet been conducted. Payroll and personnel records audits are conducted separately but regularly by internal audit departments and by external audit as part of financial audit. These constitute partial audits only and do not look at the interface between the two systems, though there is a separate HR audit.<br><br>The score in the 2010 assessment seems too high, as the internal audit unit was still getting off the ground. A C rating seems more appropriate. |

*Source*: BoFED, Inspection unit, Internal Audit units at BoE, BRRC, BoH, ORAG.

[17] BoFED's Internal Audit reported one case in FY 2012/13 (EFY 2005) whereby FPPAD mistakenly omitted a letter from HR to suspend a salary payment to a staff. This was found out by internal audit and the money was recovered.

## PI-19: Transparency, competition, and complaints mechanisms in procurement

### *Background*

At the time of the 2010 PEFA assessment, SNNPRS procurement legislation was governed by Proclamation no. 96 (March 2006), which was based on the Federal Procurement Proclamation (2005). On July 28, 2012 (EFY 2005), the SNNPRS Public Procurement and Property Administration Proclamation no. 146 (FY 2012) replaced Proclamation no. 96, and relevant regulations and directives (guidelines) were issued at the same time. The main differences included the unifying of procurement and property administration functions under one law, and the establishment in FY 2012 of the Public Procurement and Property Administration Agency (PPA) as an autonomous state body with regulatory, monitoring, advisory, and capacity building functions in relation to the procurement activities of budget institutions. Previously, procurement was regulated and monitored through a Core Process of BoFED.

Specific functions of the PPA according to the proclamation include: (a) to review and decide on requests from procurement entities to deviate from the prescribed methods of procurement; (b) to conduct procurement audits; (c) to prepare quarterly and annual reports for BoFED on the functioning of the procurement system, and, upon request, provide data on the nature and volume of public procurement. To support the PPA, a guideline and manual for the procurement of goods and services was issued in FY 2012/13 (EFY 2005).

Specific responsibilities of procuring entities include: (1) preparing annual procurement plans connected with budget preparation; (2) maintaining records and documents on procurement operations, including the grounds for using procurement procedures (restricted tendering; direct procurement; request for proposals in relation to consultancy services; request for quotations; and two-stage bidding); (3) advertising open tenders; and (4) using alternative procurement methods if the conditions specified in the proclamation for use of such methods are satisfied.

As discussed under dimension (iv) the Proclamation established a board to review complaints at the same time that PPA was established.

The PPA has 21 staff members holding relevant degrees and procurement expertise. According to the Director, pay levels are high (Grade 8, Director level) relative to the average civil servant), and encourage retention. However, some BIs interviewed noted a shortage of procurement expertise and the need for training.

*(i) Transparency, comprehensiveness and competition in the legal and regulatory framework*

The requirements for the scoring of this dimension and whether they were met in 2012/13 are listed in Table 3.29. The previous methodology did not include this dimension.

**Table 3.29: Transparency in Procurement**

| Requirement | SNNPRG practice |
|---|---|
| (1) The legal framework is organized hierarchically and precedence clearly established. | **Yes,** as indicated in the SNNPRS Public Procurement and Property Administration Proclamation 146/FY 2012 (EFY 2005), gazetted on July 28, 2012. |
| (2) It is freely and easily accessible to the public through appropriate means. | **Yes,** as provided for by article 7 of Chapter 1 of Proclamation 146/FY 2012 |
| (3) It is applied to all procurement undertaken using government funds. | **Yes,** as provided for in Chapter 1, article 4 of Proclamation 146/FY 2012. It also applies to public enterprises competing for government contracts. |
| (4) Open competitive procurement is the default method of procurement and clearly defines the situations in which other methods can be used and | **Yes,** as provided for in Proclamation 146/FY 2012, section 33 of Chapter 3, and elaborated on in the section on “Background” above**.** |

| | |
|---|---|
| how this is to be justified. | |
| (5) It provides for public access to all of the following procurement information: government procurement plans, bidding opportunities, contract awards, and data on resolution of procurement complaints. | **No**. The proclamation only provides for public access to bidding opportunities, though in practice other information is provided (dimension (iii)). |
| (6) It provides for an independent administrative procurement review process for handling procurement complaints by participants prior to contract signature. | **No.** The proclamation provides for a Complaints Board (section 72 of Chapter 14), but does not explicitly state that the Board is independent of the procurement process. The proclamation states that the PPA shall be the Secretariat for the Board, which would seem to compromise the independence of the Board. |

*(ii) Use of competitive procurement methods*

This dimension was contained in the previous methodology, but the scoring criterion was specified in general terms, and the revised methodology requires quantitative data. The ratings under the old and revised methodologies are therefore not comparable.

The 2010 PEFA assessment indicated that open tendering was in the process of becoming the main procurement method. This was partly due to the implementation of the recommendations resulting from the BPR exercise, which covered many aspects of PFM. In connection with procurement, the number of bureaucratic steps was reduced, making it easier for BIs to use open tendering methods. In interviews, BIs indicated that they were increasingly using open competition. However, BoFED was not collecting data to verify that this was the case.

According to the Director of the PPA, procuring entities are required under the proclamation (Chapter 2, Article 15, para. 5) to apply in advance to PPA to use direct procurement methods if the conditions for using these are met, as listed in the proclamation (Chapter 6, Articles 51-52). Use of direct procurement methods without meeting the conditions and without prior approval of PPA may attract penalties. PPA may notify the Regional Council in such cases.

The PPA routinely collects operations-related information from procurement entities. Statistics provided to the team showed that open bidding was used for 82.3 percent, 87.8 percent and 91.3 percent of the value of all procurements above the threshold (above which open competition is required) in FYs 2010/11, 2011/12 and 2012/13, respectively. Some procurements conducted using direct procurement are for fuel purchases, which is justified by the fact that the Government controls fuel prices. The BoE, BoH and Bureau of Rural Roads Construction (BRRC) confirmed that they usually use open competition methods. The BRRC may use direct procurement methods in urgent cases, for example to replace broken equipment.

The PPA established a procurement audit process in FY 2011/12 in relation to FY 2010/11 (EFY 2003). Audits are conducted according to a ten-point checklist (increased from eight points at the beginning of FY 2013/14), which is based on the PEFA Framework. Coverage is 100 percent a year for “poverty eradicating” bureaus; it is 80 percent for all other bureaus, health centers and high schools. At the time of the PEFA assessment (April-May, 2014), 27 of 43 bureaus had been audited about one and a half months before the end of the fiscal year. Less than 60 percent compliance with the checklist was reported to the President. The PPA prepares a report on each auditee and distributes it to BoFED as well as the auditee.

This dimension is scored using the criterion stated in the draft revised framework (circulated for comment on August 7, 2014). This is easier to use than the current criterion, which requires information on unjustified use of noncompetitive procurement methods. Unless a procurement audit system has been fully established covering all budget institutions, this information is difficult to collect (hence the D rating in the first draft). The current criterion may produce anomalous results resulting in a D rating due to insufficient evidence, even though use of open competitive procurement methods is in fact the norm.

*(iii) Public access to complete, reliable and timely procurement information*

This dimension was not included under the previous methodology.

Four information elements are required in order to score A: procurement plans, bidding opportunities, contract awards, and data on the resolution of procurement complaints. The proclamation requires publication only of bidding opportunities (dimension (i)), but additional procurement-related information is usually publicized as well.

The FTAP has been instrumental in pushing for increased transparency in procurement practices. Bidding opportunities and contract awards are routinely made available to the public through newspapers (for bidding opportunities), notice boards and radio stations, as confirmed by BoFED, BoE (starting EFY 2006), BoH and BRRC. The BRRC indicated that it started to post bid evaluations and letters to winners and losers on its notice board in (EFY 2005). It was not posting annual procurement plans, but sending these to BoFED. BoFED and Hawassa City administration are posting procurement performance reports. The TVET bureau indicated that it was posting procurement plans and resolutions on procurement complaints on its notice boards, as well as the results of a procurement compliance audit.

*(iv) Existence of an independent administrative procurement complaints system*

The previous methodology included a dimension for assessing the complaints system in much less restrictive terms, since the complaints system did not have to be independent except in order to obtain an A rating. The ratings under the old and revised methodologies are therefore not comparable.

The PPA serves as the Secretariat to the Complaints Review Board (CRB) and provides it with office facilities in BoFED and technical assistance. The CRB is accountable to BoFED. The proclamation explicitly provided for the CRB, in contrast with the procurement proclamations of the other regional governments assessed, which left the explicit provision to the procurement directive to be issued later. The Board members comprise the regional Chamber of Commerce, which represents the private business sector, relevant public bodies, public enterprises, and three representatives from BoFED. The Secretariat consists of a secretary and a lawyer.

The first stage of the complaints process is the submission of a complaint to the head of the procuring entity independent of the entity’s bid evaluation committee. If the complaint remains unresolved the complainant then appeals to the CRB.

The number of complaints submitted to the CRB is growing: they rose from 29 in FY 2011/12 (EFY 2005) to 70 during the first half of FY 2013/14 (EFY 2006). According to PPA, suppliers’ increasing awareness of procurement process rules is causing the rise. The CRB does not have full information on the number of complaints that are resolved at procuring entity level. The Bureau Head is supposed to report the numbers of resolved complaints to the CRB but does not necessarily do so.

Complaints submitted to the BRRC are mainly settled there. According to BRRC, complaints are often invalid or incomplete.

In interviews, the BoE indicated it had received no complaints in EFY 2006. The Bureau Head resolved two complaints in EFY 2005. One complaint went to the CRB in EFY 2005 and was resolved in favor of BoE (BoE was tendering for a braille printer; the only apparent supplier argued that the printer should be purchased through direct procurement, but the Board decided in favor of BoE). A public enterprise manufactures education materials, but BoE makes it compete for the supply of these materials. It was not possible to have a similar meeting with the procurement staff in BoH.

The proclamation does not explicitly state that the CRB is independent of the PPA. Moreover, while the CRB includes private sector representation, the PPA is its secretariat, and both institutions are accountable to BoFED. Thus, the CRB does not appear to be genuinely independent of the procurement process.

**Table 3.30: PI-19 Results**

| PI-19 (M2) | Score 2010 | Score 2014 | Justification for score | Performance change |
|---|---|---|---|---|
| | NA | C+ ↑ | | No comparison possible due to change in method of assessment |
| (i) | NA | B | Four of the listed requirements are met. Requirement (v) on transparency is not met, though it is being met to some extent in practice. | |
| (ii) | NA | A | The total value of contracts awarded through competitive methods in the most recent fiscal year (2012/13 at the time of the PEFA field visit) was over 80% of the total value of contracts. | |
| (iii) | NA | C↑ | Bidding opportunities and contract awards are routinely publicized. Some bureaus have started to publicize procurement plans and information on resolution of complaints. | |
| (iv) | NA | D | The Complaints Review Board (CRB) was established under the Procurement Proclamation (July 2012). It does not appear to be independent of the procurement process, for the reasons given in the narrative. To score higher than D requires that "the CRB is not involved in any capacity in procurement transactions or in the process leading to contract award decisions."<br><br>Otherwise, the CRB satisfies 4 of the other 5 requirements listed in the Framework (using the draft revised Framework). The requirement that is only partly met is that the CRB "issues decisions within the timeframe specified in the rules/regulations." | |

*Sources*: Procurement and Property Administration Proclamation (#146/2012); "About public procurement in SNNPRS," PPA; meeting with Head of PPA; table of procurement operations compiled by PPA for all SNNPRS by procurement type and method and by account code; meetings with BoE, BRRC.

### PI-20 Effectiveness of internal controls for nonsalary expenditure

This evaluation refers to the internal controls for nonsalary expenditures at the time of assessment (May 2014).

The financial control systems are embedded in the financial regulations (derived from the Financial Administration Proclamation) and associated internal directives. Other control systems, such as those related to personnel management, are embedded in the civil service regulations. The following directives and guidelines have been adapted from the federal directives and guidelines and distributed to all BIs.

- Proclamation and Regulations
    - Financial Administration Proclamation no. 128 (EFY 2002)
    - Financial Administration Regulation no. 93 (EFY 2002)
    - Procurement and Property Administration Proclamation no. 146 (EFY 2002)

- Directives, Manuals and Guidelines
    - Guideline/Manual for the procurement of goods and services no. 13 (EFY 2005)
    - Property administration directive no. 14 (EFY 2005)
    - Cash management directive no. 8 (EFY 2005)
    - Disbursement directive no. 9 (EFY 2005)
    - Government accounts directive no. 6 (EFY 2004)
    - Handover of Property among government bodies directive no. 11 (EFY 2005)
    - Public procurement directive no. 13 (EFY 2005
    - Budget Administration directive no. 2 (EFY 2002)
    - Guarantee directive no.10 (EFY 2005)
    - Internal Audit directive no. 3 (EFY 2004)
    - Financial Accountability directive no. 5 (EFY 2004)

In addition, the Internal Audit Manual of the SNNPRS, in place at the time of the 2010 PEFA assessment, contains the basic principles of internal control systems. Internal auditors and ORAG are responsible for ensuring compliance with internal control systems.

*(i) Effectiveness of expenditure commitment controls*

For the control of commitments, some BIs, such as BoH, use non-automated hand written ledger cards, and others, including BoE, use the IBEX budget control module. According to the Financial Administration Proclamation 128/EFY 2002 (Articles 29 (2) and 32 (1)), approval of BIs' proposed expenditure commitments depends on whether the proposed expenditures are included in the approved budget, and, if so, if there is sufficient remaining uncommitted balance in the approved budget.

The IBEX commitment control module is more of a commitment-reporting module than a control module. It indicates the remaining unencumbered budget balance after BIs enter new purchase orders and sign contracts, as required. It does not block commitments entered that would result in payments leading to monthly cash expenditure limits being breached that month and within the quarter.

As indicated by the head of the Accounts Department in BoFED, financial administration departments in BIs would use manual control processes to block commitments resulting in the breach of monthly cash expenditure limits. Thus, cash availability is taken into consideration as well as unencumbered budget availability.

BIs can also use manual control processes to commit expenditures for payments in later quarters based on their cash plans, which derive from the cash flow forecasts, as approved by BoFED. Monthly cash expenditure limits eventually set by BoFED for later quarters take into account the projected payables arising from the earlier commitments. Most purchases are on a cash-on-delivery basis, with the exception of long-term construction projects and the provision of consultancy services

Some BIs may not strictly adhere to the commitment and budgetary control system. ORAG's report for FY 2011/12 (EFY 2004) indicated that 63 BIs spent about ETB 2.7 million beyond their approved budget (0.06% of the total budget), but this is a very small amount.[18]

*(ii) Scope, relevance and understanding of other internal control regulations and procedures*

As indicated above, a number of guidelines and directives were issued in FY 2011/12 and FY 2012/13 aiming to strengthen the internal control systems. These manuals are available to staff at all levels.

The internal control systems include segregation of duties for preparing, checking, certifying and approval in the movement of resources, including through cash and check disbursement; and receipt, issuance and disposal of stock items and properties. The segregation of roles applies to all processes, including payroll preparation (PI-18), procurement (PI-19), staff advances, use of real assets, and personnel administration. The processes are both financial (e.g. bank reconciliation) and physical (e.g. stock counts) and so involve most of the personnel within an organization, not just those in the financial management area. The internal audit function (PI-21) reviews the compliance of the manuals and guidelines.

High employee turnover, including for trained staff, necessitates more frequent training to familiarize staff with rules and regulations. Various training courses were conducted in the areas of accounting, procurement, property administration and internal audit as part of the EMCP (supported by the PBS program).

*(iii) Degree of compliance with internal controls*

Generally, rules and regulations are respected. ORAG, ID and internal audit reports note incidents of BIs not complying with regulations. BIs' lack of awareness of rules and regulations due to capacity constraints, including high staff turnover, contribute to these irregularities.

According to ORAG's report on FY 2011/12, out of the 300 audited entities: 29 BIs neglected certain parts of procurement procedures; 109 BIs effected inappropriate per diem payments; 102 BIs effected payments without sufficient supporting documents; 63 BIs overspent their approved budgets; 22 BIs failed to collect revenues; 36 BIs did not settle suspense advances on time; and many BIs did not maintain inventory and fixed assets registers and did not conduct annual physical counts.

The Inspection Department(ID) reported a lack of cooperation from the management of BIs in terms of willingness to respond to audit findings and to take appropriate remedial actions.

**Table 3.31: PI-20 Results**

| PI-20 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | **B** | **B** | | **No change.** |
| (i) | B | B | The Financial Administration Proclamation (FY 2011) - which prohibits entering into commitments without availability of unencumbered balance -, the cash flow forecasts, the | **No change.** |

[18] The scoring criterion appears to be wrongly specified as it indicates that commitment controls should limit commitments to actual cash availability in order to score A or B. However, actual cash availability is not known for commitments that generate payables beyond the end of the month, in which case approval of commitments should be based on projected cash availability.

| PI-20 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | | | cash plans prepared by BIs (as monitored routinely) on the basis of those forecasts, and manual control processes in BIs all help to guard against cash unavailability at the time of payment. Although the vast majority of BIs control commitments, ORAG reports indicate irregularities by some. | |
| (ii) | B | B | Financial and nonfinancial control systems are comprehensive, well documented and generally understood. The revised manuals, regulations and proclamations in effect since 2011 are accessible to staff. Ongoing training courses are enhancing the understanding and awareness of staff and managers | **No change**. |
| (iii) | B | B | Compliance with rules and regulations is general good. As indicated in ORAG, Inspection Department reports, and internal audit reports, there are instances of noncompliance in certain areas by some BIs. | **No change**. |

*Sources*: Financial Administration Proclamation no. 128 (EFY 2002), various regulations and directives, BoFED, BoH, BoE.

### PI-21: Effectiveness of internal audit

#### *Background*

Regular and adequate feedback to management is required on the performance of the internal control systems, through an internal audit function (or equivalent systems monitoring function).

The Financial Administration Proclamation no. 128 (FY 2011) authorizes BoFED to oversee the internal audit functions of BIs, develop internal control standards and assist in building the capacities of the internal audit units. The ID at BoFED is discharging this responsibility, as was the case at the time of the 2010 PEFA assessment. The ID has issued the following manuals (based on the ones prepared by MoFED):

- Internal Audit Standard, Code of Conduct/Ethics and Internal Audit manual) adapted from the Internal Audit manual of MoFED issued in 2004 (prior to the previous assessment);
- Training module (four volumes) issued in October 2012 (i.e. since the 2010 PEFA assessment). The modules cover all aspects of internal auditing including risk analysis, planning, audit procedures, documentation, and reporting writing;
- Guideline for Inspection and Code of Ethics, issued January 2008 (prior to the previous assessment).

The ID has seven internal auditors;[19] six hold BA degrees in accounting and one has a master's degree.

*(i) Coverage and quality of the internal audit function*

The internal audit function was in the process of being established at the time of the 2010 PEFA assessment. It is now fully established in all BIs, though capacity gaps that existed at the time of the 2010 assessment remain to some extent. BIs are responsible for the audits of institutions that report to them (for example, the Internal Audit (IA) Unit at BoE audits 118 schools).[20] IA departments formally report to both the heads of the bureaus in which they are established and to ID (i.e. dual subordination). Training manuals have been developed (based on the Federal Government IA Manual), focusing on meeting professional standards (as per the International Standards for the Professional Practice in Internal Audit, issued by the Institute of Internal Auditors).

As per the Internal Audit Manual (in place prior to the 2010 assessment), IAs focus on systemic issues. IA departments conduct financial and compliance audit, internal control reviews, HR and, to some extent, property audits. They do not yet practice performance audits. In February 2014, 10 internal auditors attended training on performance audit organized by MoFED. The ID reviews the reports and annual audit plans of IA units and occasionally visit woredas. However, ID has limited capacity in terms of manpower to supervise and support the majority of the woredas in developing their IA functions.

The internal audit function in principle covers all funds, including Treasury and DP-funded projects within the BIs. Internal audit units have been auditing Channel 1 and 2 DP-funded programs since EFY 2005 (FY 2012/13), at the request of MoFED. BoFED's Internal Audit Department (IAD) covered 50 percent of DP-funded projects during EFY 2005. However, the time required to audit DP-funded programs detracts from time available to audit the BIs.

Although IA manuals and the organization of the IA function appear to meet standards, in practice, and in contrast to the other regions assessed, the internal audit function has not developed significantly since the 2010 PEFA assessment. Staff levels have shrunk since EFY 2005, when numbers had climbed to 2312 from a mere handful in EFY 2002. ID estimates that 40 percent of internal audit positions are vacant. ID claims that turnover is high due to lack of support from the management; problems with some managers trying to influence the content of audit reports; lack of independence (as reported by ID to MoFED); unsatisfactory pay levels (ID's proposal for increasing the allowances of internal auditors was rejected by the regional Civil Service Commission); and insufficient office facilitation, particularly at the woreda level.[21] The BRRC and BoE mentioned that internal auditor turnover was an issue. For example, BRRC recently trained two internal auditors who subsequently left.

According to ORAG, only 20 percent of the internal audit reports meet the standard and ORAG therefore does not rely on the majority of internal audit reports. According to ID, some IA units do not base the annual audit plans on priorities and risk assessment.

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[19] This is a relatively low number of staff compared with Somali region, which employs 20 internal auditors in the ID.

[20] At zonal and woreda levels, outside the scope of this assessment, the IA function is in a system within the ZoFEDs and WoFEDs.

[21] As also emphasized in the woreda government PFM study contracted by the World Bank in 2011, the study including woredas in SNNPR, as well as in other regions.

*(ii) Frequency and distribution of reports*

Internal Audit units in Regional Government level BIs submit audit reports monthly to the heads of their BIs.[22] At the time of the 2010 PEFA assessment, the IA function was still being established and reporting was irregular.

The IAD in BoFED (as its own BI)[23] prepared 26 audit reports during FY 2012/13 (EFY 2005), including 12 financial audits, two property audits, two HR audits, two project audits, four internal control reviews and two budget execution audits. BRRC[24] prepared 12 monthly internal audit reports and four quarterly MDG audit reports. ID also conducts special audits based on the request of the Court and the Anticorruption Commission. The ID conducted 15 special audits in EFY 2005. ID does not report to ORAG since there is no legal obligation to do so. ORAG auditors often request internal audit reports during their audit of BIs, and these are provided.

***(**iii) Extent of management response to internal audit findings*

Sector Bureau Heads are required to respond within 15 days to the findings of internal audit reports (30 days for zonal and woreda level offices) though some, including BoFED, which is supposed to set an example, take longer.[25] According to ID's estimation, 25 percent of the managers are responding and only 10 percent of them are taking action. Bureaus tend to respond more fully and promptly than zones and woredas. The IADs of BoE and BoFED maintain follow-up registers of their audit findings and recommendations. According to them, 90 percent of the managers respond to their findings. Similarly, the IA unit at BRRC indicated that response to audit findings is generally satisfactory.

ID recently submitted a summary of major audit findings to the Regional Council. It also submitted audit findings that indicate commission of fraudulent activities to the Anti-Corruption Commission. To enhance the understanding of managers of BIs, training was organized by ID for a number of woredas. Relatively regional bureaus are responding better than woredas and zones. ID currently has limited workforce capacity to follow up audit findings.

***Ongoing and planned activities***

The BoE is planning to place internal auditors at all schools at woreda level since the Single Pool system cannot cover all of them.

**Table 3.32: PI-21 Results**

| PI-21 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | C | C+ | | **Performance improved under dimension (ii).** High staff turnover and minimal management |

[22] Internal audit departments in WoFEDs send audit reports monthly to the internal audit departments in their parent ZoFEDs. The reports include the consolidated audit findings of IA units in schools and health centers. The ZOFED IADs report to ID quarterly by summarizing the major audit findings of the WoFED IADs and including the monthly internal audit reports prepared by the IA units in colleges and hospitals, and their own audit findings.

[23] The Internal Audit unit at BoFED, which has only four staff members, is the most organized Internal Audit unit from all the internal audit units visited during this PEFA assessment.

[24] The BRRC has six internal auditors at head office level and has 1 auditor in each of its 10 district offices. District Auditors report quarterly to the Head of IAD at BRRC.

[25] The finance, procurement, and property administration department (FPPAD) in BoFED took 60 days to respond to the findings and recommendations of the IAD at BoFED for the internal audit report issued on 8th of February 2014. The report should have been responded to in 15 days, so the response was 45 days late, and much later than the response time of other BoFED departments.

| PI-21 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | | | | support of the IA function have constrained improvement under dimensions (i) and (iii). |
| (i) | C | C | The IA function is established at all levels of government. Although the IA manuals meet the standards, high staff turnover and minimal management support of the IA function has compromised its quality. | **Performance unchanged**. |
| (ii) | C | B | Generally, audit reports are submitted monthly at the regional level to the auditee, ID and, on request, to ORAG. | **Performance improved**. IA units were in the early days of being established at the time of the 2010 assessment and reporting was irregular. |
| (iii) | C | C | Management response to audit findings and recommendations is estimated to be around 25%, with action taken estimated at just 10%. | **Performance unchanged**. The IA function was still in the process of being established at the time of the 2010 assessment, so improved performance would be expected. |

### 3.5.2 Accounting, recording and reporting

### PI-22 Timeliness and regularity of accounts reconciliation

*(i) Regularity of bank account reconciliations*

BoFED and BIs maintain several different bank accounts, including the Central Treasury Account (CTA) held by BoFED in CBE, the related Z accounts (as part of the TSA) held by BIs in CBE, revenue deposit accounts, MDG accounts and DP accounts. The purpose of these accounts is explained under PI-17.

The end-month balance on the CTA is required (as per the directive under the FAP) to be reconciled every month within a month with the general ledger held in IBEX in BoFED. The CTA account is usually, though not always, reconciled within 15 days from the end of the month. One of the purposes of reconciliation is to identify and clear unknown or unreconciled differences in a timely manner. If this is not done, the reconciliation exercise lacks meaning. The PEFA team saw that the bank reconciliation statement for the CTA for the month ending April 6, 2014 statement showed unreconciled differences carried forward for the last four months. The unreconciled differences represent bank error (ETB 4,407) and a lump sum ledger balance error of ETB 1.8 million. Other bank accounts are usually reconciled within seven days from the end of the month.

Some of the BIs reconcile bank accounts monthly but may delay two months.[26] The ORAG audit report for FY 2011/12 (EFY 2004) indicated that some BIs are not reconciling bank accounts on time; it does not state how many.

The situation appears to have deteriorated since the 2010 PEFA assessment, which indicated timely bank reconciliation and no significant unreconciled differences between bank account balances and BoFED's records.

*(ii) Regularity of reconciliation and clearance of suspense accounts and advances*

Based on the financial administration directive, suspense accounts and advances should be settled in seven days. No new advance should be provided to staff unless the previous advance is settled. Suspense payments that are part of the petty cash system should be reconciled periodically and be subject to the scrutiny of monthly internal audits. According to the directive, suspense accounts not cleared within seven days should be transferred to staff advance and deducted from salary.

According to BoFED, reconciled items from unknown deposits into bank accounts may take more than 30 days before they are cleared; some BIs do not reconcile and clear suspense accounts and advances on time. This is also indicated in the ORAG report for EFY 2004, which shows that 36 BIs (out of the 220 audited entities) did not settle and reconcile advances and suspense accounts on time. Some of the reconciliation statements of BoE and BoH showed unreconciled items carried forward for multiple months. In the case of BoH, for example, different credits on the bank statement with a total amount of ETB 9.2 million, and debit entries of ETB 474,073, were not cleared until after seven months. The reason is said to be the failure of CBE to provide bank advices, which are the prime supporting documents for processing transactions.

The end-year balance on suspense account (Account Code 4201) was between ETB 7.8 million and ETB 9.8 million for EFYs 2003- 2005. The FY 2010 PEFA assessment indicates that this balance was zero at the end of FY 2008/09. The purpose of the account is to record unknown debits until they are cleared against documents. The balance of suspense account at ETBRC[27] (ETB 50,913) has been outstanding for more than five years.

As of July 7, 2013 (end-EFY 2005) the receivables balances included staff advances of ETB 28.4 million, as shown in the trial balance sheet (Account Code 4203). The 2010 PEFA assessment indicates that this balance was zero at the end of FY 2008/09.

Ageing reports were not available to determine how soon advances and receivable accounts have been cleared or reconciled. Long outstanding receivables have been a concern in some of the BIs (as noted in ORAG and ID reports) (PI-20). Most of the BIs visited indicated that most advance and suspense clearance activities are conducted in the first two months from the end of the fiscal year.

Advances to contractors and suppliers from the MDG Fund are not included in the scope of this dimension. They are retired as payments certificates are submitted and cleared, which may carry over to the next fiscal year.

[26] In the case of BoE, the last reconciliation for its Z account (GOV 426/6055) was Yekatit (month ending March 9, 2014), when the last reconciliation in relation to the time of the PEFA team's visit from May 12-16 should have been for the month ending April 9. In the case of BoE, the last reconciled balance on its MDG account was that of January (TIR) 2014. At the time of the PEFA assessment in May, the end-February and end-March account balances should have already been reconciled.

[27] The balance sheet ledger items for BRRC do not show up-to-date balances since the opening balance as of July 8, 2013 was not posted.

**Table 3.33: PI-22 Results**

| PI-22 M2 | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B+ | C+ | | **Overall decline** |
| (i) | B | C | CTA/Z accounts are usually reconciled monthly within 4 weeks from the end of the month. Some of the BIs may not reconcile their other bank account balances within 4 weeks of the month, including for the MDG account. | **Performance declined**, as indicated by unreconciled differences being carried forward. |
| (ii) | A | B | Suspense accounts and advances are generally reconciled and cleared within two months from the end of the fiscal year. ORAG's report for EFY 2004 indicated that some BIs do not clear or settle their advance accounts on time. | **Performance declined**. |

*Sources*: ORAG report for EFY 2004, trial balance sheets for EFY 2003-05, meetings with BoFED Accounts Department, and BoE, BoH, BRRC.

### PI-23 Availability of information on resources received by service delivery units

The 2010 PEFA assessment indicated that the systems for monitoring the resources provided to primary education and health service delivery units were more or less in place, and were being strengthened through the Federal Government-World Bank-UNICEF–funded General Education Quality Improvement Program (GEQIP), a similar type of program for primary health posts funded by UNICEF, and the PBS-funded FTAP. The data generated by these systems were not yet being implemented into the preparation of annual service delivery reports available to politicians (the Cabinet, in particular) and the public (the latter is covered by PI-10), although there were no technical obstacles to preparing such reports.

The monitoring systems have continued to develop since the 2010 assessment in terms of the quality and comprehensiveness of the data, but annual resource monitoring reports are still not being prepared, The main development is that primary schools which receive assistance through GEQIP are able to open bank accounts, and, therefore, purchase inputs directly in cash rather than receiving them in kind from woreda education offices. The BoH records cash expenditures more quickly and reliably. The BoH prepares an annual service delivery report, which it showed to the team. The report presents actual versus planned outputs and outcomes in physical terms (e.g. numbers of live births), but does not contain any information on the resources used (planned and actual) in the delivery of outputs.

**Table 3.34: PI-23 Results**

| PI-23 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | B | C | | |
| | B | C | Primary schools and health posts are not cost centers, but data on resource flows to these SDUs are generated through the resource allocation systems of woreda education and health offices, supported by federal and DP-funded projects (FTAP, GEQIP and a UNICEF-funded primary health care project). Data are channeled to zonal administration | **Performance unchanged.** Monitoring systems have strengthened, partly due to GEQIP, but service delivery reports are still not being prepared.<br>The B rating in the 2010 assessment was too high as |

| | | | | |
|---|---|---|---|---|
| | | | offices, but formal reports on resource flows to primary education and health care SDUs are not yet prepared. | reports were not being prepared. |

**PI-24 Quality and timeliness of in-year budget reports**

This indicator assesses the scope of reports, their timeliness, and the quality of information on actual budget implementation.

***Background***

IBEX was not fully rolled out, even at the level of sector bureaus, at the time of the 2010 PEFA Assessment. IBEX has now been fully implemented at sector bureau, zonal and woreda levels, except for a few woredas in South Omo zone. Bureaus still operate IBEX on a stand-alone basis only, since on-line connectivity remains a problem, partly because of power shortages.

*(i) Scope of reports in terms of coverage and compatibility with budget estimates*

Sector bureaus submit monthly IBEX-generated reports to BoFED in hard and soft copy; zonal administrations also submit reports to BoFED that incorporate reports sent to them by woredas. The reports compare budget and out-turns for revenues and expenditures by source of funds and include detailed trial balance statements, which include payables and receivables as well as revenues and expenditures. BoFED consolidates these into monthly detailed budget execution reports (drilling down to the sub-agency detail) and monthly trial balance statements. The reports, in the form of tables, show the original budget, the adjusted budget and actual revenue and expenditure to date. The reports can be configured to show revenues and expenditures for regional bureaus, zones and woredas separately and combined, and to show expenditures by source of financing (domestic funding; block and MDG grants; own revenue; and external loan and assistance). MoFED receives these reports as a matter of course.

One limitation is that reports show actual expenditures but not expenditure commitments, even though the information on commitments is contained in the budget-reporting module of IBEX as well as in manual ledgers. The absence of a fundamental piece of information – the remaining uncommitted ("unencumbered," in the language of the Financial Administration Proclamation) balance – limits the utility of the reports for managing the budget. BoFED also submits a quarterly budget transfer summary table to Cabinet, which shows the funds transferred from BoFED to zonal and woreda offices, and prepares the quarterly Joint Budget and Aid Review (JBAR) for MoFED. The JBAR is a table showing expenditure in disaggregated form, similar in format to the tables mentioned above, but using the adjusted budget as the basis for assessing performance, and not the original budget, thereby impeding its usefulness.

As is evident from the trial balance sheets (the account codes for external assistance and loans show no data), and the expenditure tables, the IBEX generated reports for FYs 2011/12 and 2012/13 did not include expenditures funded through Channel 1b (funding from DPs directly to BoFED, as noted under PI-7), as these were recorded through different accounting software packages (mainly the IT-based financial management program, Peachtree). The Channel 1b reports are mainly statements of expenditure. The trial balance statement for FY 2010/11 (EFY 2003) did, however, include external assistance and loans. Connectivity problems may have precluded the information from being included in the trial balance sheets for FYs 2011/12 and 2012/13. Since the beginning of FY2013/14, some Channel 1b assistance is being reported on in IBEX using an interface between Peachtree and IBEX codes. As noted under PI-7 (ii), DP expenditures funded through Channel 2b and Channel 3 programs are not recorded at all.

*(ii) Timeliness of the issue of reports*

According to the directive under FAP, sector bureaus are required to submit monthly reports to BoFED within seven days from the end of the month. Reports are submitted in soft and hard copy. In practice, some BIs (e.g. BoE) submit monthly reports within five days and other BIs (e.g. BoH) within 15 days (the frequency and time specifications for woredas to report to zones, and zones to report to BoFED, are monthly, within five and 12 days, respectively, from the end of the month). Using IBEX, BoFED is able to consolidate this information into disaggregated monthly revenue and expenditure reports, in the form of tables, within 30 days from the end of the month.

BoFED also prepares quarterly consolidated in-year financial reports for submission to the Cabinet, Regional Council (on demand basis) and MoFED (JBAR). For example, the third quarter report for the quarter ended on April 8, 2014, was sent to MoFED on April 25, 2014, within 17 days from the end of the quarter.

*(iii) Quality of information*

The rollout of IBEX over the past few years has improved the quality of in-year financial reporting. The continued lack of electronic interface requires BoFED to check the data received from bureaus and zones (and for ZoFEDs to check the data they receive from woredas). BoFED estimates that post-reporting corrections and adjustments average about 10 percent of overall transactions. The improvement in internal audit (PI-21) function and the increase in audit coverage by ORAG (PI-26) helped to improve the quality of in-year financial reports.

ORAG[28] still expresses concerns about the quality of financial reports in some of the audit entities particularly at woreda levels, although qualifications are declining. Out of the 220 entities audited in relation to FY 2010/11 (EFY 2003), 158 of them had qualified audit opinions; 57 of them (including five sector bureaus, including BOE) had adverse opinions (many data issues) and five had disclaimer opinions (data too inaccurate in order to form an opinion). Out of the 300 audited entities audited in relation to FY 2011/12 (EFY 2004), 50 of them had adverse opinions, the majority being for woredas (and thus outside the scope of this indicator). The adverse opinions are mainly based on the omission of transactions from reports, which affects the completeness of consolidated financial reports at BoFED level. The absence of reports on Channel 1b expenditures also detracts from the completeness of reports.

**Table 3.35: PI-24 Results**

| PI-24 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | **C+↑** | C+ | | **Performance unchanged overall, but the quality of reports has improved**. |
| (i) | C↑ | C | Detailed comparison is possible for revenues and domestically financed expenditure for each BI and by economic classification.<br>The operations of Channel 1b donor funded projects are reported separately. Expenditure commitments are still not reported. | **No change**. |
| (ii) | A | A | Reports are prepared on a timely basis. | **No change**, but timeliness has improved due to greater IBEX |

[28] ORAG consolidated audit report for the EFY 2003 (issued in 2012), and audit follow-up report issued in January 2014.

| PI-24 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | | | | coverage at the BI level. |
| (iii) | B↑ | B | The quality of reports has improved due to the roll out of IBEX and strengthened by internal auditors and ORAG. However, there are still concerns with the quality of reports, mainly at woreda level but also at regional bureau level. | **Performance unchanged** in terms of the rating, but has improved due to the roll out of IBEX. |

### PI-25 Quality and timeliness of annual financial statements

Consolidated year-end financial statements can be good indicators of the PFM system's transparency. PI-25 assesses the quality of annual financial reporting by referring to financial statements' comprehensiveness, timeliness and the standards used.

***Background***

The Financial Administration Proclamation (no. 128/2009 FY) lists the required content of the annual financial report, which includes consolidated fund, debt and contingent liabilities, budget outturn, budget subsidy transfer, special funds, and the opinion of the Auditor General.

*(i) Completeness of the financial statements*

BoFED prepares annual financial reports containing information on the flow of funds (both revenues and expenditures), a comparative statement of financial position, trial balances, and the budget execution reports of bureaus, zones, and woredas. The reports also contain the comparative notes to the accounts and accounting policies as required by the Financial Management Manual. Information on revenue arrears (receivables) is missing.

The consolidated financial report does not include the accounts for DP-funded projects and programs, which are included in the proclaimed budgets of SNNPRS. BoFED directs Channel 1b program and project funds from DPs to bureaus and produces the pertinent reports; however, BoFED does not include the reports in its annual financial statement since it does not use IBEX to compile them. DP-funded projects through Channel 2b (DPs direct to bureaus) and Channel 3 (DPs direct to projects) are not reported on as they are not included in the proclaimed budget in the first place (as discussed under PI-7).

*(ii) Timeliness of financial statements*

According to the Financial Administration Regulation no. 9 (FY 2011) (article 58 (2)), BoFED should submit consolidated annual financial statements to ORAG within three months from the end of the fiscal year. In practice, BoFED submitted the consolidated annual financial statements to ORAG after nine months and 24 days, five months and 21 days, and five months and 15 days for EFYs 2003, 2004 and 2005 respectively. The financial statements cover woreda governments as well as the Regional Government, so preparation takes longer than it would if the statements covered only the Regional Government.

**Table 3.36: Timeliness of Financial Statement Submission to ORAG**

| FINANCIAL STATEMENTS | FY 2010/11 (EFY2003) | FY 2011/12 (EFY 2004) | FY 2012/13 (EFY 2005) |
|---|---|---|---|
| Statements received by ORAG | May 3, 2012 | December 31, 2012 | December 24, 2013 |
| Timeliness of submission (from the end of the EFY) | 9 months and 24 days | 5 months and 21 days | 5 months and 15 days |

*Source*: BoFED

*(iii) Accounting standards used*

BoFED has not changed its use of accounting standards. The annual financial statements are still prepared on an historical cost basis, using a modified cash basis of accounting. Revenue is recognized on receipt, except for aid in kind (which should be valued before being brought to account);[29] employee income tax and fines (recognized on processing of payroll); interest on salary advances (also recognized on processing of payroll); and deduction of withholding tax from payments to suppliers (on payment of invoices). External assistance is also recognized on receipt. The Financial Administration Proclamation requires the recognition of contingent liabilities, but BoFED does not estimate these.

Expenditures, including those on fixed assets and property, are recognized on a cash basis during the year, but capital expenditures are accrued at the end of the year for the annual statements. The accounts are kept open for a grace period of one month after the end of the financial year so that outstanding liabilities are paid and cash payments catch up with recorded expenditure. Salary and pension payments are recognized monthly on processing of the payroll. Loans received (Account Code 4050-4059) are recorded as liabilities. Interest on public debt is recognized on payment. Investments in public enterprises are recorded as expenditure (Account Code 6412 and 6413) in the year of payment.

The financial statements are not in line with International Public Sector Accounting Standards (IPSAS). The financial statements for EFY 2003, 2004 and 2005 (FYs 2010/11-2012/13) did not contain detailed analysis of statements of financial position and statements of financial performance. Extensive notes and supplementary disclosures were not provided. Analysis of accounts payable and receivable were not included in the reports. Donor-funded projects are not included in the consolidated report (the expenditures under the Channel 3 projects should at least be disclosed as they are public funds).

Most of the reports for Channel 1b funds are simplified reports such as statements of expenditures designed in accordance with the reporting requirements of the various donors and not in accordance with standard financial reporting formats.

**Table 3.37: PI-25 Results**

| PI-25 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | C+↑ | C+ | | **No overall change, but improvement on timeliness of submission of statements to ORAG.** |
| (i) | B↑ | B | Annual consolidated financial reports are prepared and contain most expenditures, revenues, assets and liabilities. | **No change.** Information on revenue arrears and expenditures funded by DPs through Channel 1b (included in the proclaimed budget) is still missing. |
| (ii) | B | A | The statement for 20012/13 (EFY 2005) was submitted to ORAG 5 ½ months | **Performance improved**. The annual |

[29] This does not happen. Aid-in-kind received by BIs in the form of assets and consultancy services are not recorded.

| PI-25 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | | | after the end of the FY. | financial statement for 2008/09 (EFY 2001) was submitted to ORAG 10 months after the end of the FY. |
| (iii) | C↑ | C | Financial statements are prepared on a modified cash basis of accounting consistently over time, but financial statements are not fully in line with IPSAS. | **No change**. |

## *3.6 External Scrutiny and Audit*

### PI-26: Scope, nature and follow-up of external audit

The use of public funds can be transparent only with a high quality external audit.

***Background***

The Office of the Regional State Auditor General (ORAG) was established in FY 2004 (EFY 1994) under Proclamation no. 83/FY 2004 (EFY 1994), in accordance with Article 51 (3a) of the revised Constitution of the SNNPR. There was no change in proclamation since the previous PEFA assessment. The proclamation states:

- The Auditor-General and Deputy Auditor-General shall be appointed by the Regional Council (RC) upon nomination by the head of government and will be accountable to the Regional Council (RC). The term of Office of the Auditor General shall be seven years. Upon expiry of the term of office, the RC may reappoint the Auditor General for another term;
- ORAG shall carry out the examination of performance audit, resources control audit and special audits;
- ORAG shall audit the accounts of private contractors relating to government contractual work that involve sums exceeding ETB 500,000;
- ORAG shall report audit findings to heads of the pertinent offices or organization, including Bureau of Justice and the Secretariat of the Head of Government. Where audits reveal grave irregularities or the commission of a crime, and if findings are related to corruption, ORAG shall inform the Ethics and Anti-corruption Commission of the region;
- ORAG shall provide the required training and certificate of competence to internal auditors;
- ORAG shall issue, renew, suspend, and cancel certificates of competence.

There are 223 auditor positions under ORAG's new structure. At the time of the 2010 PEFA assessment, there were 154 auditors and ORAG was planning to fill the vacant positions very soon. About 80 percent of auditors have a BA degree in accounting and six of them have master's degrees in related fields.

*(i) Scope/nature of audit performed (incl. adherence to auditing standards)*

**Extent of audit coverage**

According to the Proclamation, SNNPRS ORAG is responsible for the audit of the accounts of all SNNPRS organizations, including public enterprises and private companies holding contracts from SNNPRS in excess of ETB 100,000.[30] There are 1,028 audit entities in the region, including sector bureaus, zonal offices and woredas, but excluding schools and health centers. The single pool system, (whereby the WoFED and ZoFED manage the finances of the woreda and zonal sector offices respectively) permits aggregation, so that an external audit can cover several public bodies as one aggregate body.

ORAG categorizes BIs into three categories based on the level of risk: high, medium, and low. An entity's complexity also determines the level of the risk. Audit entities with big budgets are classified as high risk. Bureau of Agriculture (BoA), BoH, BoE and Bureau of Water Resource (BWR) are categorized as high-risk audit entities. In principle, ORAG targets auditing 75 percent of the entities categorized as high risk, and 60 percent of the entities categorized as moderate risk.

ORAG's financial audit includes DP-funded project accounts managed by BIs, where some of the funds are also audited by Office of the Federal Auditor (OFAG). Though ORAG has the mandate to audit public enterprises, in practice it has never approved the nomination of private auditors to audit public enterprise. There were no instances where ORAG audited private companies in connection with government procurement.

During the audit for EFY 2004, ORAG covered 356 audit entities, representing about 34 percent of the total audit entities in the region. Excluding revenue audit and special audit, audit coverage in terms of expenditure reached 51 percent, the same as in FY 2008/09 (the last year covered by the 2010 assessment).

**Nature of the audit**

ORAG conducts financial audits separately at the level of BI, and a financial audit based on annual consolidated financial report of the region. ORAG also conducts special audits and performance audits, but not environmental or IT audits. Special audits are based on the requests from the Anti-Corruption Commission, courts, other government bodies, and individual informants. During FY 2013/14, ORAG conducted 300 financial audits, three performance audits, 51 continuous audits and seven special audits.

**Adherence to auditing standards**

[30] Proclamation 83/2004.

ORAG follows the audit standards of the Office of the Federal Auditor General (OFAG), which is a member of the International Organization of Supreme Audit Institutions (INTOSAI). ORAG employs separate audit manuals for regulatory audit (now using the FY 2012 version), Performance Audit (since EFY 2004) and Environmental Audit. ORAG also uses INTOSAI's 2012 release of the regulatory audit manual and the performance audit manual.[31]

*Publication of Audit Reports (INTOSAI Standard)*:

Audit reports for EFY 2000 and 2001 are posted on the website of ORAG (www.snnpraudit.gov.et) and were available at the time of the assessment. Audit reports for EFY 2002 and 2003 are not posted yet because of the problem with the webserver, as indicated by ORAG.

**Independence of ORAG from the Executive (INTOSAI Standard)**

As noted above, ORAG is accountable to the RC and in principle is independent of SNNPRG. ORAG submits its draft budget to RC for approval (Article 16 of the Proclamation). ORAG recently revised its own organizational structure and salary scale, which became operational after the approval of Civil Service Commission of the SNNPR.

*Cooperation and Public Relations*

The Proclamation provides ORAG the right of access to all information required for it to fulfill its responsibilities (article 20), thus meeting another INTOSAI standard.

*Audit Methodology*

ORAG is increasingly focusing its annual audit on internal control systems using a risk-based approach (as stipulated in article 8 of the proclamation) as per INTOSAI and African Organization of Supreme Audit Institutions (AFROSAI) standards, rather than on individual transactions. Human resource management and property systems, for example, are tested on a sample basis.

ORAG looks at internal audit department reports (PI-21) as part of its work. These departments also follow up on ORAG's findings. According to ORAG, the quality of internal audit reports still needs improvement. ORAG estimates that only about 20 percent of the work of IADs meets quality standards.

**Table 3.38: Scope of Audits of SSNPRG (EFY 2004)**

| Elements covered | % of expenditure audited | Audits carried out | Audit standards applied |
|---|---|---|---|
| - Revenue<br>- Expenditure<br>- Assets<br>- Liabilities (debt) | 51% of audit entities were audited in 2004 Coverage does not include revenue audit and special audits | - Financial audits focusing on systemic problems (of systems) disbursement, cash management, property, procurement, recording, reporting, etc.)<br>- Special audits and Performance audits | - INTOSAI |

*Source*: SNNPRS ORAG

31 The manual was issued by ORAG in FY 2009/2010 (EFY 2002). Some other ORAGs (e.g. Somali ORAG) use the exposure draft on performance audit issued in 2012).

*(ii) Timeliness of submission of audit reports to the legislature*

According to the ORAG Proclamation, ORAG should submit an audited consolidated annual financial report to BoFED within one year from the receipt of the report from BoFED. The duration provided by law is longer than the three to eight months allotted to other the ORAGs of other regions. BoFED is required to submit the annual financial statement to ORAG no later than three months after the end of the FY, giving ORAG 15 months from the end of the FY to submit the audited financial report to BoFED, which then submits to the Regional Council. BIs are required to submit their account within two months from the end of the fiscal year (article 58 (d)).

ORAG completed the audit of 259 and 300 public bodies during FY 2010/11 (EFY 2003) and FY 2011/12 (EFY 2004) respectively. It takes two to three months to audit individual BIs. Auditing consolidated financial statement requires much longer than before the 2014 assessment: the last completed audited financial statement is for FY 2010/11, and was completed 20 months from the date of receipt of the report from BoFED. In contrast, it took three to four months to audit the annual statements during the period covered by the previous assessment (three months for FY 2007/08 (EFY 2000)).

**Table 3.39: Timeliness of Financial Audit**

| FINANCIAL STATEMENTS | 2010/11 (EFY 2003) | 2011/12 (EFY 2004) | 2012/13 (EFY 2005) |
|---|---|---|---|
| Received by ORAG | July 12, 2012 | December 31, 2012 | December 24, 2013 |
| Audits of financial statements completed by ORAG and submitted to the Regional Council<br><br>Duration of audit | March 21, 2014<br><br>1 year and 10 months | Not yet<br><br>1 year and 6 months elapsed | Not yet |

*(iii) Evidence of follow up on audit recommendations*

ORAG established a Follow Up Department in FY 2011/12 (EFY 2004) dedicated to inspecting audit findings. Audit entities are required to submit a report on the action they have taken for qualified audit opinions. For adverse and disclaimer audit opinions, the auditors from the Follow Up Department auditors will personally visit auditees to check whether they are implementing ORAG's recommendations.

The RC's Economics Committee is also following-up on audit findings through visits to auditees. ORAG assign auditors join these visits if the issues are serious.

ORAG maintains follow up records using Excel spreadsheets.[32] In addition, ORAG issues a semi-annual report on the actions that auditees take after field visits from ORAG's Follow Up teams. According to the report issued on January 2014 (for the audits conducted in FY 2012/13), 20 of the 50 audit entities with adverse and disclaimer audit opinions were visited. These included the

[32] The record contains information on whether the response of the auditee is satisfactory and the date on which the response was received.

regional sector bureaus (BoA)[33] and the Regional Cooperative Promotion Office. Out of the 240 action items, the auditors reported that auditees had acted on only 40 of them (about 17 percent).

**Table 3.40: PI-26 Results**

| PI-26 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | **C+** | D+ | | **Reduction under (i) & (ii)** |
| (i) | C | C | Coverage of 51% | **No change**. |
| (ii) | B | D | See table above | **Performance declined**. The decline is sharper than the 2010 rating shows, the rating being based on an average of the time taken to submit the accounts and the time taken to submit the audit reports on individual BIs. The 2010 rating should have been A, if based only on the accounts. |
| (iii) | B | B | As required by law, auditees respond to audit findings by indicating what actions they will take to address the findings, but in practice the follow-up rate in terms of implementing these actions is very low (17%), despite establishment of a Follow Up Department in ORAG in 2011/12. | **No change** in terms of the scoring criterion, but the B score overstates performance. |

### PI-27 Legislative scrutiny of the annual budget law

*(i) Scope of the legislature's scrutiny*

The Budget Finance and Audit (BFA) Committee reviews all sources of budget financing (federal subsidy, external loans and assistance and regional internal revenues), expenditure allocation at regional BIs and woreda level, and the budget allocation formula (for distributing the block grant to zones, special woredas, woredas and city administrations). The source of information is not just the draft Budget Proclamation, but also supporting documentation. It used to review the macroeconomic and fiscal framework (MEFF), but this is not currently being prepared for capacity reasons.

The documentation is comprehensive, but is provided right at the end of the budget preparation calendar, so there is very little scope for any revisions that the Committee might suggest for incorporation into the draft budget.

*(ii) Extent to which the legislature's procedures are well established and respected*

The draft budget is submitted by the Regional Cabinet to the Speaker of the Regional Council, who forwards the draft budget to the BFA Committee. At the time of the 2010 PEFA assessment,

33 BoA did not respond to any of the 15 findings and recommendations of ORAG.

this was called the Economics Committee, which discussed sector issues as well as budget and PFM issues. It is now called the BFA Standing Committee, and other standing committees look at sector issues. The review of the draft budget may involve the participation of these committees where sector issues are involved.

An improvement since the 2010 assessment is the permanent employment of three out of the five BFA Committee members. Previously, the Economics Committee members were working on a part-time basis, resulting in procedures not being fully respected due to difficulties in convening all its members as and when required.

*(iii) Adequacy of time for the legislature to provide a response to budget proposals*

The procedures were revised in FY 2010/11 (EFY 2003) to reduce the time for RC review to 20 days from 30 days, giving the executive a longer period to review the draft Budget Proclamation prior to its submission to the RC. The budget committee completes its review, including discussions with BoFED over its queries on the draft budget, within one week. The BAC requires less time than it did four years ago, as it is easier to convene its members. The BAC then prepares a note on the draft budget and may propose minor changes. Following a speech from BoFED, it then presents the budget to the RC. The RC usually approves the draft Budget Proclamation within one day.

At the time of the 2010 PEFA assessment, 10 days were set aside for discussion by the RC of the draft budget, though 30 days were allowed. The Chairman of the Economics Committee considered this insufficient time to review the draft Budget Proclamation, given the lack of explanatory narrative in the documentation. Since explanations within the draft have improved, the time for review now appears adequate. Nevertheless, keeping the maximum review time to 30 days would have been a better safeguard.

*(iv) Rules for in-year amendments to the budget without ex-ante approval by the legislature*

No change in performance.

**Table 3.41: PI-27 Results**

| PI-27 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-27 | D+ | C+ | | **Improvement** under dimensions (ii) and (iii). |
| (i) | A | C | The Budget and Audit Committee reviews the draft Budget Proclamation accompanied by supporting documentation, but only at a very late stage where the detailed draft budget has already been more or less finalized. | **No change**. The dimension was overscored in the 2010 assessment |
| (ii) | C | B | Simple procedures exist for the legislature’s review and are respected. | **Performance improved**. 3 out of the 5 Budget and Audit Committee members are permanent employees, whereas previously they were part-time, causing procedures to be not always respected. |

| PI-27 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| (iii) | D | C | A change in procedures in EFY 2003 reduced the amount of time for review of the draft budget to 20 days from 30 days. The actual time needed for effective review is less than 2 weeks, due to an improvement in rigor in preparing the draft budget and greater availability of supporting documentation. | **Performance improved**. Sufficient time is provided for effective review of the draft budget. Previously the time was insufficient. |
| (iv) | B | B | Clear rules exist for in-year budget amendments by the executive and are usually respected, but they allow extensive administrative reallocations. The requirement for *ex-ante* approval by the RC of supplementary budgets is met. | **No change**. |

### PI-28 Legislative scrutiny of external audit reports

The legislature has a key role in exercising scrutiny over the execution of the budget that is approved.

*(i) Timeliness of examination of audit reports by the legislature*

The CBA takes two months to review audited annual financial statements (AFS). There are many individual BI audit reports (220 with regard to FY 2011/12 (EFY 2004), so the CBA pays particular attention to those with adverse opinions and disclaimers of opinions. The time needed to review these is variable, so this dimension is assessed only with regard to the audited AFS.

*(ii) Extent of hearings on key findings undertaken by the legislature*

Hearings are held only in regard to BIs with adverse opinions and disclaimers of opinions. The hearings usually involve field visits. Hearings cover all of these (57 adverse, five disclaimers), an improvement since the 2010 PEFA assessment.

*(iii) Issue of recommended actions by the legislature and implementation by the executive*

The Regional Council issues recommendations based on ORAG's reports. In FY 2012/13 (EFY 2005), the establishment of a taskforce to follow up on implementation gave these recommendations teeth. The taskforce comprises representatives from 11 institutions including Justice, BoFED, Revenue, ORAG, and the Police. It conducted between one and three field visits to follow-up on audit findings and RC recommendations. The taskforce submitted reports based on these visits to the speaker by CBA.

**Table 3.42: PI-28 Results**

| Indicator | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| PI-28 | B | A | | **Performance improved under dimensions (ii) and (iii).** |
| (i) | B | A | The scrutiny of the audited annual financial statements is completed within 2 months of receipt | **No change**. The 2010 assessment took into account the time taken to review individual BI audit reports, |

| Indicator | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | | | | but in practice the time to review these is variable and only applies to those with adverse and disclaimers of opinions (numbering 62 in relation to EFY 2004.) |
| (ii) | B | A | Hearings cover all BIs that have been given adverse or disclaimers of opinion by ORAG. | **Performance improved**. In-depth hearings cover all BIs receiving adverse or disclaimers of opinion from ORAG. Previously they did not cover all of these. |
| (iii) | B | A | The legislature usually issues recommendations on action to be implemented by the executive, and evidence exists that they are generally implemented. | **Performance improved**, partly due to the establishment of the follow-up inter agency Task Force. |

## *3.7 Donor Practices*

### D-1: Predictability of direct budget support

SNNPRG does not receive direct budget support from donors. Budget support is provided to the Federal Government and helps to finance the block grant from the Federal Government to the regional governments (one of the conditions being adequate funding of the Protection for Basic Services (PBS) program).

### D-2: Financial information provided by donors for budgeting and reporting on project and program aid

*(i) Completeness and timeliness of budget estimates by donors for project support*

The bulk of DP funding of budgeted expenditures is channeled through the PBS block grant, and, more recently, through the MDG grant. The amount of DP funding provided directly for funding projects and programs through Channel 1b funding modality has been relatively very small: 10.7 percent of total budgeted expenditure of ETB 6.6 billion in EFY 2003; and less than one percent of total budgeted expenditures of ETB 10.8 billion in EFY 2004 and ETB 14 million in EFY 2005, the main reason appearing to be the establishment of the MDG grant in FY 2011/12 (EFY 2004).

The DPs that have been providing project/program support through the budget are mainly World Bank and the UN organizations. The IBEX classification codes have not been used to classify budgeted expenditures in the Budget Proclamations, only the project totals being shown

At the time of the 2010 assessment, DP funding channeled directly to sector bureaus (Channel 2b) was captured to some extent in the proclaimed budgets of those bureaus. This is no longer the case (as indicated under PI-7).

*(ii) Frequency and coverage of reporting by donors on actual donor flows for project support.*

The IBEX-generated budget execution reports do not include actual expenditures, as shown by zero entries for external assistance and loans in the trial balance sheets for EFYs 2004 and 2005.

Expenditures were reported on for EFY 2003, according to the trial balance sheet for that year. It is not clear why reporting stopped in EFY 2004.[34] The Aid Coordination Unit compiles financial quarterly reports outside IBEX on the Channel 1b projects using the IT-based financial management program, Peachtree, as at the time of the 2010 assessment.

The DPs providing support through Channel 1b have started, effective the beginning of FY 2013/14 (EFY 2006), to record planned and actual expenditures using IBEX codes.

**Table 3.43: D-2 (M1) Results**

| D-2 (M1) | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | D+ | D+ | | **No change.** |
| (i) | C | D | Not all major DPs provide budget estimates for disbursement of project aid at least 3 months in advance of the coming fiscal year. Estimates use DP codes that are not consistent with the Government's budget classification. | **Decline in performance.** At the time of the 2010 assessment, Channel 2 type funding was captured in part in the Budget Proclamations. This is no longer the case. Only Channel 1b type projects and programs are budgeted for. These use DP codes, not IBEX codes, though they are starting to do so, |
| (ii) | D | C | Reports are prepared quarterly by the Channel 1b project units in BIs, the reports being consolidated by the Aid Co-ordination unit in BoFED. The reports are prepared using accounting systems other than IBEX. Beginning EFY 2006 (2013/14) some Channel 1b DPs are using IBEX codes for budgeting for and reporting on expenditures | **Change in scope; comparison not possible.** The 2010 D rating was based on the non-reporting of budgeted Channel 2 aid, whereas this was not budgeted for in subsequent years. The rating is therefore not comparable with the 2014 score. Actual expenditures of budgeted Channel 1b projects (only 1% of SNNPRG expenditure) are reported on quarterly, but not according to IBEX codes. |

### D-3: Proportion of aid that is managed by use of national procedures (country systems)

The assessed dimension refers to the overall proportion of central government aid funds that are managed through national procedures (budget execution, banking, procurement, accounting, reporting and auditing).

DPs are generally still using their own systems to record their transactions and prepare reports. They did not use IBEX until the end of FY 2012/13 (EFY 2006), and therefore could not use SNNPRG's budget execution (including payment), accounting and reporting systems. DPs began using IBEX codes for planned and actual expenditures in FY 2013/14 (EFY 2006). An unknown amount of DPs' expenditures occur through Channels 2 and 3 and does not use Regional Government systems.

[34] The 2010 report also notes that World Bank and AfDB financed projects were using the IBEX codes for reporting, but this seems to be no longer the case.

- BoFED approval is required for Project Implementation Units (PIUs) to open bank accounts, but these are not yet part of the TSA/zero balance budget execution system, partly because DP-funded projects and programs do not use IBEX. Liquidity management inefficiencies result if surplus cash is sitting in DP project/program bank accounts and cannot be accessed for funding execution of the proclaimed budget.[35]
- Expenditure commitment and payment controls through IBEX do not apply to DP-funded projects and programs.
- Budget execution reports and accounts generated through IBEX do not cover DP-funded projects.

Government procurement systems are approaching international best practice standards, but DPs still rely on their own procurement systems, with the exception of UN Executing Agencies. Some DPs, such as the World Bank, consider that the Government procedures are too tough, despite meeting best practice, so they continue to use their own procedures (for example, for the WaSH program).

While ORAG and internal auditors have the mandate to audit DP-funded projects and programs, DPs tend to recruit their own external auditors, which can result in redundant auditing.

Human Resource Management systems also tend to recruit staff of PIUs under different conditions than those of civil servants.

According to MoFED, 20.1 percent of the block grant to BoFED from MoFED in FY 2012/13 consisted of budget support provided by DPs, based on 20.1 percent of SRG's share of MoFED's allocation of block grants to regions (Table 3.11 of Federal Government PEFA). The total block grant to BoFED in FY 2012/13 was ETB 7.2 billion (indicated in the Budget Proclamation), so the DP share was ETB 1.44 billion. Channel 1b-related funds amounted to ETB 85 million in EFY 2005 (external loans and grants indicated in the Budget Proclamation), mainly using DP systems for budget execution. Channel 2a and 2b-related aid amounted to at least ETB 90 million (all BoH) in FY 2012/13, and mainly used DP systems. Channel 3 aid would have had to exceed ETB 1,265 million in FY 2012/13 for D-3 to be scored as D (less than 50 percent of DP aid uses SNNPRG systems), which was highly unlikely.

**Table 3.44: D-3 Results**

| D-3 | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| | D | At least C | At least 50% of aid funds are managed through national procedures, due to the large amount of aid provided through PBS. | **No change.** The rating in 2010 was underscored, as it did not take into account the budget support provided through PBS. |

### HLG-1 Predictability of transfers from Federal Government

This indicator is assessed in terms of the predictability of the receipt of the block grant, whose amount and use is specified in the Budget Proclamation. Predictability is very good, both end-year and in-year, with amounts disbursed on time in 12 installments for the recurrent expenditure

[35] The 2010 report notes that Irish Aid, a major DP at the time, used the Z-account system, the only DP to do so. Irish Aid has suspended its operations since then due to the Irish banking crisis.

component. The capital expenditure component is disbursed mainly on an as-required basis, so this indicator does not apply to it.

The MDG Fund grant comprises the other main transfer from MoFED. The proposed use of the grant is included in the proclaimed budget on sector bureau basis (for water, education, health, agriculture and rural roads bureaus). Payment occurs on a reimbursement basis, and is conditional on demonstration that proposed projects have been or are being implemented. Predictability cannot be measured.

As indicated under PI-13, profits taxes, GoE and the Southern Nations and Nationality Regional Government (SNNPRG) share VAT and excise duties. The Ethiopian Revenue and Customs Agency (ERCA) directly collect its share of profit taxes through Regional Government branches. It collects SNNPRG's share of VAT and excise duties and deposits these into BoFED's account. Transfers depend on actual collections, which cannot be determined *ex-ante.*

As indicated under PI-8, SNNPRG receives a special purpose Urban Development grant from GoE. Disbursement to projects is based on performance, so predictability cannot be measured. The funds amount is relatively small, comprising 5 percent of the total transfers from BoFED to woredas.

*(i) Annual deviation of actual total HLG transfers from the original total estimated amount provided by HLG to the subnational entity for inclusion in the subnational budget*

Annual deviation of actual block grant transfers to BoFED from the original total estimated amounts is very small.

*(ii) Annual variance between actual and estimated transfers of earmarked grants*

The MDG grant is disbursed on a performance basis. This dimension is therefore not applicable.

(iii) *In-year timeliness of transfers from HLG (compliance with timetables for in-year distribution of disbursements agreed within one month of the start of the subnational fiscal year)*

Predictability is very good, with amounts disbursed on time in 12 monthly installments for recurrent expenditure, according to a schedule agreed with MoFED. The capital expenditure component is disbursed mainly on an as-required basis, so this dimension does not apply to it.

**Table 3.45: HLG-1 Results**

| PI | Score 2010 | Score 2014 | Justification | Performance change |
|---|---|---|---|---|
| HLG-1 (M-1) | A | A | | **No change**. |
| (i) | A | A | HLG transfers have fallen short of the estimate by more than 5% in no more than 1 of the last 3 years. | **No change**. |
| (ii) | NA | NA | | **NA** |
| (iii) | A | A | Actual transfers have been distributed evenly across the year in all of the last three years in accordance to a schedule agreed at the time of budget approval. | **NA** |

*Source:* Table provided by BoFED.

# 4. Government Reform Process

## *4.1 Recent and Ongoing Reforms*

All government reforms, at all levels, are planned and managed within the overall national plan, the Growth and Transformation Plan (GTP), prepared by the Federal Government. The GTP (FYs 2010/11-2014/15) was issued in November 2010. Each Regional Government has its own GTP, derived from the Federal Government's. The national GTP took over from the *Plan for Accelerated and Sustained Development to End Poverty, (PASDEP), FYs 2005/06-2009/10*. SNNPRG sector bureaus base their sector development strategies on sector ministry strategies (particularly education, heath, agriculture, water resources and roads), themselves based on GTP (and previously based on PASDEP).

The Expenditure Management and Control Program (EMCP) coordinated by the EMCP Coordinating Unit in MoFED and led by the Federal Government, has been the main program governing PFM reform since FY 2002. The Public Sector Capacity Building Program (PSCAP) also supported PFM reforms from FY 2005 to 2013.

The Promoting Basic Services Program (PBS) (formerly the Protection of Basic Services Program) is a nationwide program that aims help expand access to basic services and improve their quality. The PBS was established in EFY 2006 and is now in its third phase. PBS is mostly funded in the form of a block grant from MoFED to Regional Governments. A portion of funding goes to specific projects, such as the Fiscal Transparency and Accountability Program (FTAP). Some project examples include the design of service delivery templates for posting outside service delivery units; design of budget performance templates for posting outside WoFEDs; support for local civil society organizations that improve opportunities for citizens to provide feedback on service delivery to local administrators and service providers; and, as part of the second phase of PBS, in the form of TA and training for PFM strengthening in woredas through BoFED-provided PFM support teams.

At the time of the 2010 PEFA assessment, most PFM reforms had already been implemented or were in the process of being implemented. Reforms that occurred since the 2010 assessment or that are still underway include:

- *Adoption of a revised legal framework governing PFM, based on the Federal Government's Financial Administration Proclamation.* The revised legal framework came into force in 2012, and was accompanied by accompanying regulations and 13 directives and manuals (as outlined under PI-20), all aiming to strengthen PFM. One organizational change was the separation of the public procurement and property administration function from the financial management and the related enactment of a separate Public Procurement and Property Administration Proclamation. Institutionally, this meant the public procurement and property administration process was separated from the financial administration and property management process and converted into the separate Public Procurement and Property Administration Agency (PPA).
- *Strengthening of revenue administration (PIs 13-15):*
    - Commencement of biometric finger printing project, the purpose of which is to ensure that all potential taxpayers who do not yet have tax identification numbers (TINs) are registered for obtaining TINs.

  - Introduction of the community block management system as a mechanism to inform taxpayers about their liabilities and obligations and mobilize them so that they pay their obligations on time.
  - Introduction of electronic cash register machines so that payments of VAT by customers are automatically paid into BoFED's central treasury account.
  - Introduction of the penalty waiver directive, as a way of inducing taxpayers to pay their tax liabilities on time.
  - Consolidation of tax audit reforms with greater emphasis on risk assessment as a method of identifying auditees.
- *Strengthening procurement*. Procurement has strengthened, partly due to the creation of the PPA. Most procurement is now conducted through open competition, which represents a major change since the time of the 2010 assessment. A Complaints Review Board (CRB) is in place and physically located in BoFED, but its impartiality is questionable. Most complaints are resolved at the procuring entity level before they reach the CRB.
- *Implementation of internal audit system.* The internal audit system that was still in its early days at the time of the 2010 assessment is not fully functional due to high staff turnover of staff and lack of rigor among BIs in implementing audit recommendations.
- *Creation of PFM reform support teams.* With support from PBS through the FTAP, PFM reform support teams, mainly from BoFED, were created and are providing technical support to ZoFEDs and WoFEDs

## *4.2 Institutional Factors supporting Reform Planning and Implementation*

Government leadership and ownership of its PFM reforms is high. Most PFM reforms fall under the EMCP, coordinated by the EMCP Coordinating Unit in MoFED. The Coordinating Unit monitors progress. The program is divided into 12 projects each of which has a designated Project Manager. Performance is monitored against a rolling thee-year action plan. The current action plan lists 56 activities being conducted by responsible bodies (MoFED Directorates, the Public Procurement Authority, regional and woreda administrations, etc.). Progress reports are used to revise and update the action plan.

# Appendix A: PI-2 Tables

| | 2010/11 (EFY 2003) | | | | | | |
|---|---|---|---|---|---|---|---|
| **Code** | **Administrative Unit Head** | **(Million ETB ) Budget (1)** | **(Million ETB ) Actual (2)** | Budget adjusted for agg. dev.(3) | Dev. (4 = 2-3) | Abs. dev. | % dev. |
| 311 | Education Bureau | 156 | 153 | 146 | 7 | 7 | 4.7% |
| 341 | Health Bureau | 103 | 103 | 97 | 6 | 6 | 5.9% |
| 211 | Agriculture & Resource Dev. Bureau | 96 | 93 | 90 | 3 | 3 | 2.9% |
| 122 | Supreme Court | 23 | 24 | 21 | 2 | 2 | 10.4% |
| 218 | Irrigation Development Agency | 52 | 36 | 49 | -12 | 12 | 23.9% |
| 214 | Pastoral Area Development | 21 | 20 | 19 | 1 | 1 | 5.5% |
| 127 | Police Commission | 62 | 62 | 59 | 3 | 3 | 5.1% |
| 111 | Regional Council | 82 | 81 | 77 | 5 | 5 | 5.8% |
| 213 | Agriculture Research Institute | 24 | 47 | 22 | 24 | 24 | 101.4% |
| 221 | Water Resources Development | 80 | 53 | 75 | -22 | 22 | 27.9% |
| 273 | Roads Authority | 334 | 287 | 314 | -27 | 27 | 8.0% |
| 312 | TVET Agency | 147 | 141 | 138 | 3 | 3 | 1.7% |
| 128 | Ethics & Anti-Corruption Commission | 12 | 13 | 11 | 2 | 2 | 16.6% |
| 152 | BoFED | 60 | 31 | 56 | -25 | 25 | 42.6% |
| 129 | Prisons Administration Agency | 74 | 87 | 69 | 18 | 18 | 23.9% |
| 158 | Mass Communications Agency | 68 | 55 | 64 | -9 | 9 | 12.9% |
| 121 | Justice Bureau | 12 | 11 | 11 | 1 | 1 | 5.4% |
| 242 | Culture & Tourism Bureau | 14 | 15 | 13 | 2 | 2 | 14.9% |
| 233 | Enterprise Development Agency | 23 | 23 | 22 | 1 | 1 | 2.4% |
| 277 | Urban Development Bureau | 50 | 1 | 47 | -46 | 46 | 91.3% |
| | 21 (= sum of rest) | 143 | 199 | 135 | 64 | 64 | 44.9% |
| | Total expenditure excl. contingency | 1,634 | 1,535 | 1,535 | 0 | 283 | |
| | Contingency | 50 | 0 | | | | |
| | Total expenditure incl. contingency | 1,684 | 1,535 | | | | |
| | Overall (PI-1) variance | | | | | | 8.9% |
| | Composition (PI-2) variance | | | | | | 18.4% |
| | Contingency share of budget | | | | | | 0.0% |

| | 2011/12 (EFY 2004) | | | | | | |
|---|---|---|---|---|---|---|---|
| **Code** | **Administrative Unit Head** | **(Million ETB ) Budget (1)** | **(Million ETB) Actual (2)** | Budget adjusted for agg. dev.(3) | Dev. (4 = 2-3) | Abs. dev. | % dev. |
| 311 | Education Bureau | 398 | 411 | 331 | 80 | 80 | 24.2% |
| 341 | Health Bureau | 383 | 387 | 318 | 69 | 69 | 21.8% |
| 211 | Agriculture & Resource Dev. Bureau | 204 | 185 | 169 | 16 | 16 | 9.4% |
| 122 | Supreme Court | 29 | 28 | 24 | 4 | 4 | 16.6% |
| 218 | Irrigation Development Agency | 244 | 163 | 203 | -40 | 40 | 19.8% |
| 214 | Pastoral Area Development | 115 | 95 | 96 | -1 | 1 | 0.9% |
| 127 | Police Commission | 74 | 71 | 61 | 9 | 9 | 15.4% |
| 111 | Regional Council | 48 | 67 | 40 | 27 | 27 | 68.0% |
| 213 | Agriculture Research Institute | 174 | 174 | 145 | 30 | 30 | 20.7% |
| 221 | Water Resources Development | 237 | 346 | 197 | 149 | 149 | 75.5% |
| 273 | Roads Authority | 395 | 327 | 328 | -1 | 1 | 0.3% |
| 312 | TVET Agency | 293 | 234 | 243 | -9 | 9 | 3.7% |
| 231 | Trade & Industry & Town Development Bureau | 52 | 59 | 43 | 15 | 15 | 35.8% |
| 152 | BoFED | 168 | 189 | 140 | 49 | 49 | 35.2% |
| 129 | Prisons Administration Agency | 154 | 170 | 128 | 41 | 41 | 32.3% |
| 158 | Mass Communications Agency | 53 | 53 | 44 | 9 | 9 | 21.0% |
| 241 | Transport Bureau | 1,419 | 713 | 1,179 | -466 | 466 | 39.5% |
| 242 | Culture & Tourism Bureau | 22 | 18 | 19 | -1 | 1 | 4.1% |
| 233 | Enterprise Development Agency | 59 | 36 | 49 | -13 | 13 | 26.6% |
| 332 | Sports Commission | 85 | 38 | 70 | -32 | 32 | 46.2% |
| | 21 (= sum of rest) | 152 | 190 | 126 | 64 | 64 | 50.6% |
| | Total expenditure excl. contingency | 4,756 | 3,952 | 3,952 | 0 | 1,127 | |
| | Contingency | 100 | 0 | | | | |
| | Total expenditure incl. contingency | 4,856 | 3,952 | | | | |
| | Overall (PI-1) variance | | | | | | 18.6% |
| | Composition (PI-2) variance | | | | | | 28.5% |
| | Contingency share of budget | | | | | | 0.0% |

| | 2012/13 (EFY 2005) | | | | | | |
|---|---|---|---|---|---|---|---|
| **Code** | **Administrative Unit Head** | **(Million ETB) Budget (1)** | **(Million ETB) Actual (2)** | Budget adjusted for agg. dev.(3) | Dev. (4 = 2-3) | Abs. dev. | % dev. |
| 311 | Education Bureau | 546 | 447 | 457 | -10 | 10 | 2.2% |
| 341 | Health Bureau | 532 | 552 | 445 | 106 | 106 | 23.9% |
| 211 | Agriculture & Resource Dev. | 367 | 281 | 307 | -26 | 26 | 8.4% |
| 122 | Supreme Court | 34 | 32 | 28 | 4 | 4 | 13.1% |
| 218 | Irrigation Development Agency | 148 | 167 | 124 | 43 | 43 | 34.8% |
| 214 | Pastoral Area Development | 180 | 119 | 151 | -32 | 32 | 21.4% |
| 127 | Police Commission | 101 | 89 | 85 | 4 | 4 | 4.8% |
| 111 | Regional Council | 23 | 54 | 19 | 35 | 35 | 181.4% |
| 213 | Agriculture Research Institute | 185 | 174 | 155 | 18 | 18 | 11.9% |
| 221 | Water Resources Development | 721 | 380 | 604 | -224 | 224 | 37.1% |
| 273 | Roads Authority | 323 | 267 | 271 | -4 | 4 | 1.3% |
| 312 | TVET Agency | 370 | 305 | 310 | -6 | 6 | 1.8% |
| 231 | Trade & Industry & Town Dev. Bureau | 157 | 156 | 132 | 24 | 24 | 18.3% |
| 152 | BoFED | 98 | 178 | 82 | 96 | 96 | 116.8% |
| 129 | Prisons Administration Agency | 122 | 148 | 103 | 46 | 46 | 44.6% |
| 158 | Mass Communications Agency | 143 | 130 | 120 | 10 | 10 | 8.6% |
| 241 | Transport Bureau | 1,722 | 1,359 | 1442 | -82 | 82 | 5.7% |
| 242 | Culture & Tourism Bureau | 27 | 22 | 23 | 0 | 0 | 2.0% |
| 232 | Enterprise Development Agency | 72 | 52 | 61 | -9 | 9 | 14.2% |
| 332 | Sports Commission | 115 | 76 | 96 | -21 | 21 | 21.4% |
| | 21 (= sum of rest) | 269 | 252 | 225 | 27 | 27 | 12.0% |
| | Total expenditure excl. contingency | 6,257 | 5,240 | 5240 | 0 | 827 | |
| | Contingency | 100 | 0 | | | | |
| | Total expenditure incl. contingency | 6,357 | 5,240 | | | | |
| | Overall (PI-1) variance | | | | | | 17.6% |
| | Composition (PI-2) variance | | | | | | 15.8% |
| | Contingency share of budget | | | | | | 0.0% |
| | | | | | | | |

# Appendix B: Persons Seen

Head, BOFED
Deputy Head BOFED.
Ato Desalegne Tassew, Head, Monitoring and Evaluation Process
Ato Samuel Gondar, Head, Financial Administration and Property Management Department, BOFED
Ato Getu Esayas Atango, Head, Procurement, Disposal and Property Administration Process, Education Bureau
Ato Moses Balcha, Head, Revenue Authority,
Heads, FAPMDss, Education, Health, Water Resources, and Agriculture Bureaus.
Ato Sahle Gebre Behutiya, Auditor General, ORAG
Chairman, Budget and Finance Committee, Regional Council.

# Appendix C: Documents Seen

**List of Document Reviewed / Consulted**

**SNNPR**

Procurement and Property Administration Manual 14/2005

Procurement Guidelines 13/2005

Annual Regional Budget Execution Report – EFY 2004

Education Sector – GTP Summary – Issued in October 2010

Financial Audit Report – Bureau of Education

Budget Ceiling Letter – EFY 2006

Financial Reports for EFY 2003, 2004 and 2005 including trial balances, revenue reports, budget and expenditure report, Financial position

Response letters to audit findings and recommendations: Bureau of Education

3rd Quarter Performance Report – Road Authority – EFY 2006

Expenditure Analysis by Woreda and Category

Field Report by Regional Council, which includes the follow-up on the actions taken as per the audit findings and recommendations - February 2013

Procurement Performance Report and Procurement Plan ( Plan for EFY 2006 and Performance for EFY 2005)

Internal Audit Annual Plan – BoE

Financial Administration Regulation 93/2003

Capital Projects Budget Request – BoE EFY 2004

Inspection Annual Budget and performance report Issued in June 2013

Regional 5 years Growth and Transformation Plan – EFY 2003-2007

Health Sector Result Oriented Plan ( EFY 2003-2007)

Regional Strategic Plan (EFY 2003-2007)

Regional Statistical Abstract – EFY 2004

Regional Constitution – No 35/2001

A Proclamation Issued to Re-establish Office of the Auditor General Proclamation NO. 83/ 2004

Annual Audit Reports – EFY 2001, 2003 and 2004

Audit follow-up performance Report – EFY 2006

Special Audit Reports – EFY 2003

Multiple regional level reports

Draft Budget for EFY 2003, 2004 and 2005

Monthly Financial Reports of Bureau of Education, Bureau Health, Bureau of Road Authority

Budget manual

a. Cash Management Directive No. 8/EFY 2005
b. Disbursement Directive No. 9/EFY 2005
c. Government Accounts Directive No. 6/EFY 2004
d. Handover of Property among Government Bodies Directive No. 11/EFY 2005
e. Public Procurement Directive No. 13/EFY 2005
f. Budget Administration Directive No. 2/EFY 2002
g. Guarantee Directive No.10/EFY 2005
h. Internal Audit Directive 3/EFY 2004

2. Financial Accountability Directive 5/2004.
3. Profile of Charities and Societies Organizations, BoFED, 2012/13
4. The Internal Audit Reports of Internal Audit of BoFED
5. Income Tax Proclamation No. 56/2003 (EFY 1995) as amended by Proclamation No.136/2010. (EFY 2003). The amendment standardized the criteria for levying penalties, thereby reducing the scope for the exercise of discretionary power by officials..;
6. Stamp Duty & Sales Proclamation 135/2010 (EFY 2003) as amended by Proclamation No. 203/2011 (EFY 2003 ;
7. Turnover Tax Proclamation No. 57/2003 (EFY 1995, as amended by Proclamation No. 134/2010 (EFY 2003); and
8. Chatt" Sales Tax Proclamation No. 23/1999 (EFY 1991) as amended by Federal Proclamation No. 125/2013 (EFY 2005).
9. Regulation No. 91/2011(EFY 2003) along with directives for the use of cash register machines (introduced in 2011) in the interests of efficiency, reliable data collection, fairness and effectiveness.
10. Income Tax Proclamation No. 286/2002 (1994 E.C.)
11. Income Tax Regulation No. 78/2002 as amended by Regulation No. 164/2009;
12. Proclamations No. 47/2004 (1996E.C.) for Agricultural Income Tax and Rural Land Use Fee
13. Stamp Duty & Sales Proclamation 110/1998 as amended by Proclamation No.612/2009
14. Proclamations No. 285/2002 (1994E.C.) for value added tax (VAT) on goods and services as amended by Proclamations No. 609/ 2008 (2001E.C.)
15. Regulation No. 79/2003 (1995 E.C.); e) Excise Tax Proclamation No. 307/2002 as amended by Proclamation No. 610/2009;
16. Livestock sales tax Proclamation No. 126/2013 (2005 E.C.);
17. "Khat (Chaat)" Sales Tax Proclamation No. 125/2013(2005 E.C.)