Status of Public Financial Management in Mozambique

Fiduciary Risk Assessment

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Abbreviations and Acronyms

CFAA	Country Financial Accountability Assessment
CGE	Conta Geral do Estado
COFOG	UN Classification of the Function of Government
CPAR	Country Procurement Assessment Review
DAC	Development Committee
DAF	Departamento Administrativo e Financeiro
DFID	Department for International Development
DNCP	Direcção Nacionaln de Contabilidade Publico
DNPE	Direcção Nacional de Patrimonia do Estado
DPPF	Direcção Provincial do Plano e Finanças
EMRS	Expenditure Management Reform Strategy
GAAP	Generally Accepted Accounting Principles
GDP	Gross Domestic Product
GFS	Government Finance Statistics
GOM	Government of Mozambique
HIPC	Heavily Indebted Poor Country
IAS	International Accounting Standard
IDA	International Development Agency
IFAC/PSC	International Federation of Accountants/Public Sector Committee
IGF	Inspecção Geral de Finanças
IMF	International Monetary Fund
INTOSAI	International Organisation of Supreme Audit Institutions
IMC	Instituto de Mozambique de Comercio
IPSAS	International Public Sector Accounting Standard
INM	Imprensa Nacional de Moçambique
MICAS	Ministério de Coordinação de Acção Social
MINED	Ministério de Educação
MISAU	Ministério de Saúde
MOPH	Ministério de Obras Publicas e Habitação
MPF	Ministério do Plano e Finanças
MTFF	Medium Term Fiscal Framework
ODI	Overseas Development Institute
OECD	Organisation for Economic Cooperation and Development
OGE	Orçamento Geral do Estado
PARPA	Programa de Acção para a Reducção da Probreza Absoluta
PEM	Public Expenditure Management
PER	Public Expenditure Review
PES	Plano Economico e Social
PFP	Policy Framework Paper
PTIP	Plano Trenal de Investimento Público
QBER	Quarterly Budget Execution Report
ROSC	Report on the Observance of Standards and Codes
SAI	Supreme Audit Institution
SISTAFE	Sistema de Administração Financeira do Estado
SNA	System of National Accounts
SSA	

TA	Tribunal Administrativo
UTRAFE	Unidade Técnica de Reestructuração Financeira do Estado
UTRESP	Unidade Técnica da Reforma do Sector Público
VFM	Value for Money (Audit)

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Executive Summary

The reform process in relation to public financial management gradually gained momentum after the peace agreement in 1992. The launching of the Expenditure Management Reform Strategy (EMRS) in 1997 as well as the approval of the Budget Framework Law the same year is a milestone in this respect.

A number of important actions have taken place, resulting in certain improvement in transparency and accountability: i) Preparation of a MTFF intended to strengthen medium-term sectoral expenditure planning within resource limits with a view to strengthen the budgetary process; ii) Introduction of functional classifiers, albeit not very detailed, increasing transparency on sectoral allocations and permitting better analysis of budget execution; iii) Closing of the state accounts in 1998 for the first time since Independence in 1975 increasing both transparency and accountability; iv) Strengthening of the internal audit, Inspecção Geral de Finanças (IGF), in 1999, and v) Establishment of an independent supreme audit institution, the Tribunal Administrative (TA) in 1998, providing the basis for improving control of public spending.

Despite this important progress the reform agenda is still quite impressive. The EMRS was never fully implemented. The strategy emphasised a comprehensive and universal budget system but extra-budgetary expenditures and revenues remain a major problem in budget planning and execution. It is estimated that about 80 per cent of all investments are financed off-budget by donors and overall around two thirds of total public spending is financed outside the public management system. But also considerable internal revenues and expenditures are off-budget. A study in 1999 showed that between 30 per cent up to more than 100 per cent of the state budget for recurrent expenditures are collected and spend off-budget. The consequence is that there is no complete overview of public spending. Procurement of goods and services is of particular concern. The legislation is not adequate, and rules and regulations are not fully complied with, thus having a negative impact on the use of public funds. The control mechanisms, IGF and TA, are still far below their desired capacity. The internal audit inspectorate, IGF, undertakes roughly one third of the number of financial audits required and practically no operational audits or value-for-money audits are carried out. TA now undertakes independent audit of the state accounts but the audited state accounts are submitted to the Parliament 20 months after the end of the financial year, thus rendering analysis and follow-up somewhat irrelevant. TA does not fulfil its mandate to undertake financial audit of about ten per cent of the public accounting units as well as a number of performance audits annually. One reason for the low performance of the institutions is the weak personnel situation.

Mozambique’s track record with respect to fully implementing agreed reforms is therefore somewhat mixed.

With a view to addressing the reform agenda a new integrated public financial management system, SISTAFE, was approved in late 2001, and planning is ongoing with a view to initiating the implementation as from 2003. If fully and correctly implemented SISTAFE will be a very modern financial management system providing the basis for full transparency and accountability in the use of public funds. Most of the critical points and weaknesses in the present system at technical level would be addressed by SISTAFE. It will, however, need strong political will and determination to implement such wide-ranging reform in view of the obstacles that have been apparent in the past. Staffing and training needs are yet to be fully defined and the issue of adequate salaries for

professional staff still needs to find a solution. Although improvement in human resources is not the answer to all present deficiencies it is a necessary condition for success of SISTAFE.

The present fiduciary risk assessment is based on recent studies such as the Report on the Observance of Standards and Codes – Fiscal Transparency Module (ROSC) from 2001, the Country Financial Accountability Assessment (CFAA) as well as the Public Expenditure Review (PER) both also from 2001 together with other studies and reports. The assessment has followed DFID's guidelines on managing fiduciary risk related to direct budget support as well as draft guidelines prepared by OECD/DAC on standards and performance indicators on public expenditure management and fiduciary risk. Nine Good Practice Principles have been assessed. The performance of Mozambique in relation to these nine principles is assessed to be acceptable, mainly because of the new major reform process about to take off. In five of the nine principles the situation in Mozambique is considered as being below a certain benchmark for assessment, i.e. the system is in need of substantial upgrading in order to provide a minimum level of transparency and accountability in public financial management. The remaining four principles are assessed to be approximately at the benchmark level for the specific principle. Planned reforms would change the situation quite dramatically.

This finding is in line with the results of a review by IMF and World Bank of public financial management in HIPC eligible countries. The assessment places Mozambique in the group of countries requiring substantial upgrading of their public expenditure management in order to be able to track poverty-reducing spending satisfactorily. In total fifteen out of twenty-four countries included in the HIPC-review were in this group. The remainder only required some upgrading and none had satisfactory public financial management systems.

The various assessments all point to the same conclusion, that major reform is necessary if the present high fiduciary risk is to be reduced to acceptable levels within a reasonable timeframe.

1. Background

The economy of Mozambique is small with total GDP standing at USD 3,6 million in 2001[1] or USD 210 per capita (Average of SSA is around USD 500 per capita). Total ODA in the form of grants amounted to USD 469 corresponding to USD 27 per head. Imports are fairly large, estimates for 2001 are USD 918 million (excluding large projects) equivalent to USD 54 per capita, whereas estimates for exports for 2001 stood at USD 263 million or USD 15 per capita. The public sector spends around one third of GDP of which government revenues only cover about 40 per cent. Resources are thus extremely scarce in the economy as a whole as well as in the public sector, which calls for prudent financial management of public funds, including efficient procurement of goods and services, as to maximize service delivery within limited budget resources.

Over the last couple of years increasing amounts of untied funds[2], e.g. through direct budget support and sector programme assistance, are being provided by donors. The fundamentals for providing such support are not yet entirely in place and therefore large risks associated with providing such support exist. The untied support can, however, be seen as a handle donors can use for requesting that the necessary conditions be established, thus having a positive impact on the management and use of all public funds. Compared to traditional project support it gives donors much more leverage, provided donors are willing to draw the consequences should such reform efforts not materialise timely. A more efficient public sector – in terms of use of funds and service delivery – is a prerequisite for sustainable economic growth and improved living conditions, not only for utilising donor funds effectively and efficiently.

The track record of Mozambique shows that many reforms have been agreed upon in the past, reform commissions created and a quite a few new laws and decrees drafted with limited effect, if any, on the business conducted on the ground. The Country Financial Accountability Assessment (CFAA)[3] mentions that the previous CFAA from 1996 recommended 15 actions - if implemented – "would have made a significant impact on the accountability situation in the country, but that only three were fully implemented". The remaining twelve were either only partly implemented or not at all. It is therefore important that donors define precise requirements in relation to public financial management, including procurement of goods and services, as well as improvement in public services in a manner that provides value for money. The ongoing work in OECD/DAC, World Bank and the IMF shows that the donor community is increasingly aware of the importance of these areas on the effectiveness and efficiency of development assistance.

2. Recent Reviews

A number of reviews of public financial management in Mozambique have been prepared within the last year and a half.

The first of these recent reviews to be undertaken was Report on the Observance of standards and Codes (ROSC) by the Fiscal Affairs Department, IMF, published in February 2001. The report concludes, "that Mozambique is improving fiscal transparency in a number of areas and the authorities are aware that further improvements are needed". The ROSC specifically points to

[1] All figures are from IMF: Staff Report for the 2002 Article IV Consultation.
[2] Untied aid is defined as not being tied to specific project activities or to procurement in donor countries.
[3] World Bank: Country Financial Accountability Assessment, August 17, 2001.

inclusion of extra-budgetary activities, introduction of a comprehensive legal framework for fiscal management and improvement in budget documents and reports on budget execution as essential areas for improvement. Also reduction of the time lag in producing year-end audited fiscal accounts to no more than twelve months is stressed as an area for improvement. In an update to the ROSC[4] IMF notes, that several measures are now being implemented to address these issues.

During 2000/2001 the Country Financial Accountability Assessment (CFAA) and the Public Expenditure Management Review (PER) were prepared in collaboration and the reports were published in August 2001 and December 2001, respectively.

The CFAA estimates that, "the gap between where accounting standards are and where they ought to be is still enormous", and that "the real problem with financial management in Mozambique is not so much a lack of systems as it is a lack of adequately trained and qualified personnel". CFAA emphasizes quite strongly the weak human resource situation and sees this as the main problem in relation to improvement in public financial management. Consequently, the CFAA assesses that "one should be looking at a 10-year horizon" for overcoming the current weaknesses. In relation to public financial management the CFAA characterizes the current situation as one of high fiduciary risk and points to the following weak points: i) large extra-budgetary receipts and expenditures, ii) outmoded accounting systems and standards, iii) weak and ineffective internal and external audits and iv) relatively inexperienced parliamentary oversight.

With respect to public expenditure management review the PER notes that, "significant progress was achieved after the launching of the Expenditure Management Reform Strategy (EMRS) in 1997"[5], but that "the budget system continues to suffer from inadequacies that hinder efficiency, transparency and accountability". PER considers that "the reform process is underway but must be given new impetus and depth" and underlines that "improving budget formulation, coverage and transparency, reforming public accounting and cash management, and enhancing internal control and auditing should all be part of this new phase of reforms".

In parallel a review of public financial management in HIPC eligible countries was carried by the IMF and the World Bank and published in March 2001[6]. In each country the prevailing public financial management was assessed against fifteen criteria covering budget formulation, execution and reporting. A follow-up paper[7] on the same countries was prepared in March 2002. The final assessments were broadly in line with the first report. It was concluded, that of the 24 countries included in the study, nine require some upgrading to be able to track poverty-reducing spending satisfactorily, and the remaining fifteen require substantial upgrading. The assessment places Mozambique in the second group that requires substantial upgrading. The IMF/IDA assessment concludes that, "most HIPCs can significantly strengthen their public expenditure management (PEM) within the next 1-3 years".

[4] IMF: Update on the Report on the Observance of Standards and Codes (ROSC), Fiscal transparency Module, June 13, 2002.
[5] Ministério do Plano e Financas: Expenditure Management Reform Strategy, May 1997.
[6] IMF/IDA: Tracking of Poverty-Reducing Public Spending in Heavily Indebted Poor Countries (HIPCs), March 27, 2001.
[7] IMF/IDA: Actions to Strengthen the Tracking of Poverty-Reducing Public Spending in Heavily Indebted Poor Countries (HIPCs), March 22, 2002.

The 2002 Article IV-consultation by the IMF, June 2002, also touches on a number of the issues pertaining to public financial management, especially the implementation of the new financial management law, SISTAFE (Sistema da Administracão Financeira do Estado).

3. The present study

The current status on public financial management in Mozambique is presented below in line with DFID's guidelines[8] on managing fiduciary risk related to direct budget support. The DFID guidelines are to a large extent in line with the draft OECD/DAC[9] standards and performance indicators on public expenditure management and fiduciary risk, which has also served as background guidelines. The draft OECD/DAC guidelines build on the IMF Code of Good Practices on Fiscal Transparency[10], and IFAC/PSC International Public Sector Accounting Standards for standard setting. In total, nine Good Practice Principles have been assessed. The status is based on the results from above-mentioned reviews. The preliminary outcome was subsequently discussed with the relevant Mozambican authorities, and where relevant, status was amended to reflect clarifications and recent changes.

The draft OECD/DAC guidelines propose that indication is made of how far the public financial management process is in a country compared to some minimum benchmarks. This principle has been applied in the present assessment. This provides an easy assessment of the country's performance in relation to the defined benchmarks, thereby indicating the areas in the public financial management where the most urgent actions are needed. This will also allow for more coherent monitoring by donors providing direct budget support. For each principle of good practice, the rating A to C has been applied:

- Rating A represents a situation where there is basic compliance with the defined international best practice, although coverage may not be 100 per cent.
- Rating B indicates that the country is above a certain benchmark for assessment but there are some significant weaknesses in compliance or that the procedures need to be changed
- Rating C indicates substantial failure to comply with the rules or that the system will require substantial upgrading to meet the standard, i.e. the country's performance is below the benchmarks for assessment

4. Result of Fiduciary Risk Assessment

Principle I - A clear set of rules governs the budget process

Benchmark: Modern financial management system based on international GAAP implemented. All legislation comprising of public financial management law, budget classification and accounting policies published.

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[8] DFID: Managing Fiduciary Risk When Providing Direct Budget Support, London, March 2002.
[9] OECD/DAC Task Force on Donor Practices: Sub-group on Financial Management and Accountability, Task D Standards, Developing performance measures for public financial management, Draft, Un-dated.
[10] IMF: Code of Good Practices on Fiscal Transparency, March 23, 2001

Rating: C moving towards B

Budget law specifying fiscal management responsibilities is in operation

Fiscal management responsibilities are based on a clear separation of the executive, legislative and judicial powers of government. The powers of MPF are clearly defined both in the existing and in the new law (see below). Intergovernmental fiscal relations - state and municipalities - are simple and clear; the definition of the expenditure responsibilities of the municipalities is, however, still unclear and there is some overlap with central government (ROSC).

The present accounting system is basically manual with hand-written books and some computerized records and based on single-entry book-keeping and cash accounting principles, of which the main features date back from the 1901-accounting law[11]. As a result of a Fiscal Management Review in 1996, a reform process was initiated in 1997[12] based on a new legal framework[13] emphasising "a budget system which is universal, comprehensive and transparent". The main feature of this law was that all revenues, including project financing, counter-value and part of assigned revenues (receitas consignadas) should be included in the state budget. It was also foreseen to introduce a computerized accounting system. Special attention was to be given to manpower and training in order to implement the new system.

A report on the new system[14] concluded that the legal framework of 1997 would create the basis for establishing a modern accounting system. It was estimated that in some areas it would take up to ten years to implement the reform due to very outmoded system in force and lack of qualified personnel. For a number of reasons only part of that reform was implemented. Important progress has taken place though, such as preparation of the MTFF, closing of the state accounts, and introduction of functional budget classification categories (Decree 25/97). A computerized system was, however, never selected by MPF and cash-flow management continues to be a problem. Also the critical issue of staff was not addressed sufficiently deep-rooted, although training of some 5,000 staff did take place. There appears to have been little impact of the salary reform of the late 1990s, as most institutions still struggle to attract qualified staff.

The PER and the CFAA –both prepared in 2001 - consider the objective of recording and reporting on the implementation of the state budget as being too limited, and its coverage as incomplete both at central and provincial level. The present system is considered archaic and outmoded, not responding to the requirements of a financial management system today.

In early 2002 a law for a modern public financial management system[15] was approved. The Public Finance Law (SISTAFE) was approved by Parliament in December 2001 and went into force as from 1 January 2002. The law is a framework law and it outlines the basic principles and general standards of an integrated financial management system. SISTAFE encompasses five sub-systems of budget, accounting, cash flow management, state assets and internal control and the overall

[11] Regulamento de Fazenda de 3 de Outubro de 1901.
[12] Ministério do Plano e Finanças: Expenditure Management Reform Strategy, May 1997.
[13] Law no. 15/97, Lei de Enquadramento do Orçamento do Estado e da Conta Geral de Estado.
[14] Ministério do Plano e Finanças: O Sistema de Contabilidade Pública, Novembro de 1998, prepared by Marta Inés Sastre.
[15] Boletim da República, 13 de Fevereiro de 2002, Serie 1 – Número 7, 2 Suplemento: Sistema da Administracão Financeira do Estado- SISTAFE, Law no. 09/2002.

responsibility is clearly defined. Decree No. 17/2002 of 27 June 2002 gives detailed information on principles, standards, processes, and instructions for the implementing of the various sections of SISTAFE and enters into force as from financial year 2003. Despite a few unclear points, as below, it will be up-to-date and provide the basis for transparency and accountability in the use of public funds, if fully and correctly implemented. According to MPF's plans it will take about three years to implement in all areas, but it is planned to implement the major part of the new system already in 2003. In the transitional period both the new and the existing legislation will be in force.

Over the years a number of issues have been discussed between the Government and donors. Most of the critical points and weaknesses in the present system are being addressed by SISTAFE, of which the salient points are (Articles refer to the law on SISTAFE):

- Accounting basis: Expenditures will be accounted for by utilising a modified accrual accounting principle whereas revenues will be cash based (Art. 41). Commitments will thus be registered (which is not possible today) and arrears calculated;
- The present supplementary period of three month to close the accounts will cease to exist in the new system as the modified accrual accounting system on expenditures requires accounts to be closed at the end of the financial year (Art. 30);
- Government expenditures for General Government clearly defined as GFS (IMF standard);
- GAAP-accounting standards (Art. 46) taking into consideration standards from INTOSAI, IFAC and IIA will be applied;
- A new government chart of accounts has been prepared and is expected to be approved by August 2002;
- Treasury equilibrium is a basic principle (Art. 13g);
- Consolidated account/Single account in Treasury (Art. 55) replacing all accounts (around 1000) held by the entities, projects and programmes;
- The principle of applying current prices (as opposed to fixed price level) has adopted already as from financial year 2002, thus allowing direct comparison between budget planning and execution (Art. 21).
- The preparation of the state budget take into consideration multi-annual investment budgets (Art. 21,2). In the Decree is it further specified that budget preparation shall be based on the priorities defined in the Government Programme and the Economic and Social Plan (PES) as well as budget limits defined in the MTFF.

A few points are still outstanding:

- Art. 33 on revenues is not clear. It would allow the government to build up large sums of due, non-collected taxes as asset; thereby allowing the government to incur new debts without violating targets on fiscal stability;
- Achieving treasury equilibrium in practical terms is yet to be defined; this will demand a high level of information and control with revenue flows and donor funding; (Art. 13g and Art. 24, 4d);
- Budget amendments through contingency fund mechanism during the year will still be possible (Art. 13,3 and Art. 34).

Development during the last year: The existing legislation is long outdated (Fazenda 1901), and only marginal improvements had been made in recent years, of which the most important was the

Lei do Enquadramento, Law no.15/1997, which was only partially implemented. The new legislation, SISTAFE, was prepared and approved in December 2001 (postponed from March 2001) and the associated decree approved June 2002. A brief report containing the preliminary plans, timetable and budget for implementation of SISTAFE[16] was presented to the donors in July 2002. The overall implementation period is planned for July 2002 – August 2005. Training of staff is foreseen during the first half of 2003 and preparation of procedure manuals during the same period. Staffing needs are yet to be fully defined. Nevertheless it is the intention to start implementing SISTAFE as from early 2003. If this is to be realised, training must be undertaken already in 2002 and procedures manuals must also be ready not later than end 2002.

Accounting policies and account code classifications are published and applied

The 1997 Framework Law contains the basic accounting principles but "there is no declaration or explanation of the accounting principles used in the budget documents" (ROSC). The state budget is public, but the accounting principles are neither mentioned in the budget, the QBER, nor the state accounts. (PER and CFAA have no mention of this sub-point).

In connection with the 1997-law, a decree (25/97) was approved, which defined new budget classifiers according to organizational, economic, functional and territorial criteria. Despite the improvement, especially with respect to inclusion of the functional criterion, the budget classification did not present sufficient detail to permit monitoring of certain classes of expenditure, which have significant economic impact (the 1997-classification did only define 14 broad functional areas, such as health, education, etc.). As from the 2002-budget a new more detailed classification system has been introduced.

A new chart of account based on COFOG will be introduced in SISTAFE. The basic accounting principles are described on which the accounting will be done in the future. A separate decree has been prepared and approval by the Council of Ministers is expected by August 2002. It will have effect as from financial year 2004.

Principle II - The budget is comprehensive

Benchmark: General Government is defined as in SNA 1993, or GFS 1986, and all major government activities are included in the budget.

Rating: C moving towards B

All general government activities are included in the budget

The previous legislation did not specify a definition for General Government (SNA, 1993 or GFS, 1986). It has been decided to follow GFS 1986 for General Government in budgeting for government activities in SISTAFE. The HIPC assessment showed that more than 90 per cent of the countries surveyed did not provide budget data consistent with GFS.

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[16] Ministério do Plano e Finanças, UTRAFE: Plano de Acção e Orçamento, 26 de Julho de 2002.

One of more important criticisms of the current state of public financial management in Mozambique is the importance of extra-budgetary expenditures and revenues. On the revenue side the off-budgets include retained revenues (receitas proprias), assigned revenues (receitas consignadas) as well as donor-financed investments. The latter often contains a certain percentage of funds for recurrent costs, which are registered as capital costs. On the expenditure side the most frequent off-budget activity is payments of recurrent and investment costs using the retained revenue or assigned revenue. The retained revenue and assigned revenue typically consists of fees, fines, interest on bank accounts, sales of goods (e.g. medicines, water provision, maps), sales of state patrimony, social and infrastructure provision (health care, education fees, sewerage services), regulatory service provision (construction licences, fines) and other payments for services by the sectors.

The Expenditure Management Reform Strategy (EMRS) from 1997 stated the need to "ensure a unique and comprehensive budget" by including "internally and external funded expenditures and sources of funds". As mentioned above this principle was also reflected in the 1997-Budget Framework Law, thus requiring universal coverage by the state budget. In the PFP for 1999-2002 the Government committed itself to "progressively remove institutional and legal impediments to inclusion of off-budget revenue and expenditure flows in the budget".

A study from 1999[17] revealed that rather large amounts - both donor financed and own resources - were being executed outside the budget in the ministries covered by the study (MICAS, MOPH and MISAU were included in the study, whereas MADR and MINED declined to participate). The study also found that most retained revenues had no legal basis for their collection or expenditure. In 2000 MPF issued an instruction to ministries and independent accounting units to comply with the existing legislation, but the PER from 2001 found that ministries still did not follow the rules with the excuse that the treasury system was not functioning properly, and it would be difficult – if not impossible – to reclaim funds once transferred to the central treasury. The PER reported that "there are a multiplicity of payment, deposit, transfer, requisitioning and reporting practices". How far the process of legalising the collection of retained revenues is not clear.

The PER stated that "substantial flows of own source revenues are currently unaccounted for in Mozambique's budget system" and concluded that "the budget offers only a partial view of public revenue and expenditures, violating the principles of universality and integrality, and undermining the effectiveness of the budget as a tool of public policy". PER recommended, that "as a general principle the emphasis should be on information in the budget rather than the funds themselves".

Also ROSC (2001) and the CFAA considered the budget to be incomplete with significant receipts and payments - relative to the size of the budget - still excluded. Some special funds, the Agrarian Fund and Roads Maintenance Fund and INSS fall outside the budgetary procedures (ROSC) and only a summary of their financial activities is presented in an annex to the CGE. No information on guarantees, endorsements, or contingent liabilities of the public sector is provided in the budget document (ROSC). The opinion of TA to the state accounts (CGE) emphasized that the law had to

[17] Ministério do Plano e Finanças: Identificação dos "Off-Budgets" e Mecanismos para a sua Integração no Orçamento do Estado, Marco de 2000, prepared by Austral Consultoria e Projectos.

be adhered to, and it concluded, that "no expenditure can be undertaken, unless it is clearly included in the budget".

Information on tax exemptions has so far not been provided in the budget and thus the magnitude relative to the entire state budget has not been known. As from 2003 the Government will follow the ROSC recommendation of including reporting on the cost of tax exemptions, a so-called tax expenditure budget. A new law, Codigo de Incentivos Fiscais, was approved in June 2002 and will take effect as from the financial year 2003. The opinion of TA to the CGE (both 1998 and 1999) has, however, already quite clearly recommended that the CGE should include information on lost tax revenues.

The basic principle in SISTAFE is universality and unity, i.e. all revenues and expenditures should be included in the state budget. The new accounting system will enable inclusion of all expenditures, irrespective of source of financing. There will be created special accounts to deal with foreign financing executed outside the government system. Consequently, all donor financing would be reported in the budget in the future, once SISTAFE has been fully implemented in 2006. As mentioned above, revenues collected directly by the sectors should already have been on-budget as the previous legislation was clear about this point, but there appeared to have been lack of appropriate follow-up. Also Tribunal Administrativo (TA) in its opinion to the state budget forwarded to the Parliament recommends quite clearly that retained and assigned revenues and off-budget expenditures financed by these revenues should be included in state accounts (CGE) in order to comply with the 1997 Budget Framework Law (see below). According to MPF efforts are now being made to include these in the 2003 budget; but it is not clear how major changes could be achieved in view of the obstacles that have been apparent in the past. The capacity of MPF to ensure and control that the major part would be included is clearly limited.

Extra-budgetary expenditure is not material

Extra-budgetary expenditure is indeed material. According to the study by Austral off-budget revenues are quite important compared to the official state budget allocations to sectors. The 1999-study by Austral revealed that in the Ministry of Public Works (MOPH) they constituted more than 100 per cent of the state budget for recurrent expenditures (1998), whereas amounts corresponding to around one third of the recurrent state budget in the Ministry of Health (MISAU) were collected outside the state budget. IMF notes, that up to 45 per cent of funding in some sectors is off-budget.

Extra-budgetary expenditures financed by donors are equally important. In relation to the investment budget off-budget financing by donors represented in 1998 between more than 70 per cent in MISAU to nearly 200 per cent in MOPH compared to the on-budget spending (Austral Study).

The various missions dealing with public financial management over the last couple of years have estimated that donors are financing about two thirds of the entire public spending (recurrent and investment). The QBER[18] reveals that about 50-60 per cent is financed by donors, so considerable efforts will be needed to bring on-budget both retained revenues, assigned revenues and all donor funding as well as off-budget expenditures presently financed directly by the retained or assigned revenues in the sectors outside central MPF control.

[18] Ministry of Planning and Finance: Relatório de Execucão do Orcamento do Estado/Quarterly Budget Execution Report (QBER).

Principle III - The budget supports pro-poor strategies

Benchmark: Clear linkage between medium-term outlook and annual budgets and clear identification of expenditures for poverty reduction activities in budget documents and budget execution reports.

Rating: B

Budget allocations are broadly consistent with any medium term expenditure plans for the sector or for the overall budget

Mozambique has a number of medium-term planning instruments: The Government Programme 2000-2004 sets out the overall objectives for government's policy. The poverty reduction strategy PARPA (Plano de Acção para a Reducção da Pobreza Absoluta) represents the specific government policies for poverty reduction and should be a sub-set of the former. MTFF was introduced in 1998 and is in principle updated on an annual basis. The three-year Public Investment Plan (PTIP) is a primary tool for investment planning and management (CFAA).

The annual budget documents consist of the state budget (OGE), and the associated Social and Economic Plan (PES). PES reviews the state of the economy for the past year and the Government's policy priorities for the following year (CFAA). PES thus sets out the government's policy priorities for the following year in accordance with the overall guidelines in PARPA. Five budget documents are therefore in principle prepared each year.

In the PFP 1999-2002 the Government stated, that "a medium-term expenditure framework will be prepared and linked to the annual budget, so as to match sectoral expenditure priorities with resource availability". MTFF was intended to rectify the absence of a link between medium-term sectoral expenditures and overall resources, given the projected macroeconomic framework, as well as to improve the link between multi-annual sectoral expenditure objectives and the annual budget (PER). PER considers, however, that the MTFF to date has been disjointed from the budget process. MPF still considers the MTFF as an internal technical working document and despite recommendations by ROSC and other reports, it appears to be no intention to publish the document for the time being. The PER cited government officials for saying, that the MTFF "does not have much influence" over the budget process because it is not seen as "credible". The PER concluded that "the value-added of preparing MTFF not readily apparent within the Government" and that MTFF "needs to be incorporated formally into the budget process and have high level political support.

The latest plan is the MTFF 2001-2005, prepared in 2000, while new tables giving forecasts up to 2010 were prepared in 2001. The MTFF provides the basis for the formulation of tentative sectoral budgets (CFAA), but such causality is not entirely clear. Donor allocations to sectors determine to a large extent sectoral spending, which subsequently is reflected in the MTFF and the PARPA. There is, however, no mechanism to ensure coherence between donor contributions and state budget allocations. Neither is there necessarily any substitutability between the two types of funding.

According to a report by ODI[19] "the process of recurrent budget preparation is increasingly sectoral rather than territorial" and "budget allocations are now determined centrally by MPF in consultation with the respective line ministry rather than provincial governments". The budget allocations are determined on a modified incremental basis, although education and health apply formulae to determine some components of the budget (ODI report). Despite the preparation of medium-term forecasts and plans, emphasis still appears to be on the annual budget and the PES. The various planning documents and budgets "are documents, rather than the outputs from processes" (Consulting Africa report)[20]. The latter probably explains the fragile link between the medium-term outlook and the annual budgets.

According to CFAA the budget cycle and process broadly mirror international practice, but basically all reports utilised for this assessment (especially ROSC, CFAA and PER) conclude that there is urgent need for reducing the number of planning documents. PER states that PTIP "in particular seems superfluous" and that it "does not provide an accurate estimate of capital expenditures because it also includes recurrent outlays and reflects many of the shortcomings associated with dual budgeting". PER therefore recommends that PTIP should be abandoned while PES should be reinforced and used as a document for the monitoring of PARPA". ROSC, CFAA and PER all recommend that the MTFF and the annual budgets become an integrated process. According to the decree on SISTAFE budget preparation in the future, inter alia, will be based on the financial envelopes established in the MTFF (see Principle I above).

As from 2001 the QBER includes a table on priority spending, thus allowing tracking of poverty-related spending, as requested by the HIPC-agreement. In 2001 around 50 per cent of the recurrent budget and about two thirds of the investment budget was categorized as priority spending. This is clearly an improvement in reporting on budget execution, although the QBER could be improved further (see below). It is, however, not possible to link directly the MTFF and the annual budget execution report due to difference in design of tables, and thus the fulfilment of MTFF cannot be asserted.

Principle IV - The budget is a reliable guide to actual expenditure

Benchmark: Level and composition of budget outturn close to budget.

Rating: B

Budget outturn shows a high level of consistency with the budget

The two main documents for monitoring of budget outturn is the QBER and the state accounts (CGE). It is, however, not possible to establish a complete picture of the budget outcome due to the incompleteness of the accounts as a result of large off-budgets (see above). Both the QBER and the CGE provides information on expenditures executed directly by the state system only, and therefore

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[19] Overseas Development Institute, Decentralised Planning and Financing Programme: Financial Flows and Financial Management Systems for provincial and District Administrations, 7 February 2002, prepared by Adrian Fozzard.

[20] Consulting Africa: Perspectives on Improving Planning and Budgeting in Mozambique, Draft Report, May 2002; prepared for the second Joint Donor Review of G10.

excludes most donor-financed activities as well as activities financed directly by retained and assigned revenues. Estimates are that more than fifty per cent - may be as much as up to two thirds - are financed off-budget, which makes close scrutiny of budget execution somewhat illusory. As pointed out by both the PER and the CFAA the incompleteness of the QBER and the CGE "is a result of budget coverage being partial".

The QBERs published in 2000 and 2001 do not allow analysis of budgetary changes during the year, as there was "no initial information on budget and subsequent amendments for comparison" (ROSC). The budgets up to 2002 were prepared in fixed prices and were adjusted for inflation during the financial year, thereby making it difficult to compare directly actual expenditures with original budget figures. The budget figures presented in the reports were adjusted budget allocations. The CFAA recommends the budget should be prepared and executed in current prices to facilitate comparisons. Also the PER point to this by saying that "QBER should show, for each item in the budget classification, the initial appropriation and the revised appropriation (if any), hence providing a consolidated view of the adjustments introduced to the budget during the execution phase". As from the financial year 2002, the state budget is being implemented in current prices, which should facilitate comparison in the future. This is also one of the basic principles in SISTAFE, as the new accounting system will provide the possibility of including all expenditures in the accounts. The CGE covers the accounts of all government agencies except for the autonomous institutions and public enterprises (ROSC). The information on final budget outturn is provided without indication of the budget appropriation, so no direct comparison is possible.

The sub-set of the budget reported in the QBER is broadly in line with the budget. The 2001 annual report on budget execution showed that 94 per cent of the recurrent budget and 90 per cent of the investment budget (local component) was implemented as planned following the economic classification. Also the distribution on the economic categories shows a reasonable degree of consistency with the revised budget figures. But are pointed out by ROSC the budget figures approved by the Parliament are not presented. In addition, the budget execution figures contain, the so-called treasury operations (Operações de Tesouraria), which are advance payments used for reimbursement of actual expenditures. Without the advance payments, i.e. the budget execution figures thus covering the month January to November only, the corresponding figures were 84 per cent and 24 per cent, respectively. The functional classification of expenditures (Mapa 4) gives no information on budget figures as approved by Parliament, making it impossible to check if allocations to sectors did receive the planned funds and followed the plans according to the various budget documents.

Cash management problems are a recurrent problem hampering budget execution and there are long delays in disbursing the advance payments for recurrent costs (non-salary items) and investment costs to the sectors, which impact negatively on the performance of the sectors. It is therefore somewhat surprising that there is such a high degree of consistency concerning recurrent costs. This area merits further investigation to fully understand the mechanisms. Full implementation of SISTAFE should solve the cash management problem to a large degree (payments are going to be made via the consolidated account in Treasury, not by the accounting units, so treasury operations will disappear eventually), provided there is reasonable predictability and transparency in revenue collection and in disbursement of donor funds.

There are no budgetary objectives that can be measured and assessed against results, as the present functional classification is too broad and contains no specific budgetary programmes to support financial policies and performance budgeting. The only indicator of government's financial situation relates to the overall balance (ROSC). The PER recommends that the QBER should include information on funds and institutions that benefit from financial autonomy and should provide information on the complementary period. According to the PER the Authorities have agreed to address the latter issue. The PER also recommends that other financial reports than the CGE should be prepared and published, of which the most important are: report on external and internal debt, report on retrocession, statement of cash-flow, statement of tax expenditures and statement of physical assets.

Principle V - Expenditure within a year is controlled

Benchmark: Budget execution report published monthly, not later than one month after the end of the month to allow for corrections; Internal audits undertaken of about 30 per cent of all public accounting units per year; Level of arrears used as indicator for performance of public financial management.

Rating: C moving towards B

In year-expenditure reports are prepared

Timeliness and periodicity of fiscal reports are being improved (ROSC) with the publication of QBER, which began with the 1st. quarter of 2000. This has increased fiscal transparency, as for the first time information is available to the public on the Government's fiscal accounts (ROSC). QBER is normally available 45 days after the end of the quarter. Since 2001, the report also contains a summary of donor funding, and an interim system for tracking of HIPC-funding has been established. The reporting on expenditures is still a mixture of actual spending and advance payments and the report could benefit from further refinement, especially in reporting on sector spending (see above).

The HIPC assessment showed that nearly 90 per cent of the 24 countries studied had poor in-year reporting of budget execution.

Internal Control undertaken with sufficient coverage

In the EMRS the role of a superior internal audit unit within MPF was emphasized with a view to guaranteeing that "established rules and regulations in the areas of revenue collection and use of public funds are followed and that the principles of effective, efficient and economic use of resources are respected". It was recommended to update the mandate of IGF, review existing legislation and train staff. This commitment was reiterated in the PFP 1999-2002, where it was stated that "to achieve greater accountability, the Government will implement action plans to strengthen the auditing functions of the government departments". In 1999 a new decree, 40/99, was approved, defining mandate, organisational structure and key operational policies of the IGF.

The assessment of the PER is that the "IGF is still being organized and is far from achieving its required level of coverage or professional capacity" as required by law. All ministries, departments and local government units are supposed to have an internal audit unit but very few actually have them, and few of them are covered by IGF's audit on a regular basis (CFAA). IGF undertakes internal audits of approximately ten per cent of the public accounting units per year, which is far below the benchmark of 30 per cent of the public accounting units audited per year. IGF applies auditing standards of INTOSAI and has a detailed manual of auditing procedures for the public service. Basically financial audits are undertaken by the IGF, whereas performance or operational audits are only undertaken to a very limited extend. From time to time IGF is also charged with special investigations, which sometimes makes it difficult to maintain its plans.

The main problem in IGF is the lack of sufficient resources. Of 112 staff 60 are professional staff but none with an internationally recognized qualification and its budget is insufficient to undertake its role as defined (CFAA). "Poor coverage of internal control limits its effectiveness as a deterrent" (ODI-report). Audit reports are primarily geared to the identification of systemic failures in budget management, such as scale of alternations, excess expenditures and un-reconciled advances, but fails to identify deficiencies in procurement (ODI-report). The Chief Inspector does not prepare an Annual Report on Internal Audit as recommended by INTOSAI, and consequently the real performance of IGF is difficult to assess.

IGF has developed a strategic plan for its development but, according to the CFAA, needs political and financial support for the implementation hereof and a committee to monitor its implementation. It is planned to strengthen internal control within the framework of SISTAFE. Two main activities are foreseen: preparation of procedure manuals and restructuring of the management of the internal control function. Both activities are important with a view to increasing the internal control and audit capacity not only in the IGF but also in the line ministries, where the primary control should take place. IGF is in the process of recruiting 30 new staff, which will increase its capacity considerably. It remains to be seen that increasing the professional staff with approximately 50 per cent will allow IGF to fully fulfil its role, as the output in quantitative terms has to triple to reach the benchmark. There is also an issue of improving the quality of audit reports of the IGF.

Nearly 90 per cent of the countries in the HIPC-assessment do not have an effective internal control, thus contributing to the low level of reliability of public financial management.

Systems operating to control virement, commitments and arrears

A cash-based accounting system does not allow for control of commitments and arrears as some stages in the expenditure process, e.g. commitment and verification, are neither defined nor recorded (ROSC). This lack of records makes it impossible to identify any payment arrears during budget execution. No separate list of arrears is prepared. Prior to authorising payment of invoices the outstanding balance of the budget line in question is checked manually by the finance department in the accounting unit and the information noted on the payment slip with indication of the new balance.

Virement (transfer from one budget line to another) is quite widespread but it is difficult to establish an overview of the extent due to the limitations in the reporting system (see above). The TA-opinion observed that many budget changes and virements are not included in the CGE and have not been approved by the competent authorities (see below). The TA also criticised the lack of budgetary discipline in budget execution, for instance by exceeding the budgetary limits established by law. The report on the TA-opinion recommends MPF to become more stringent and to ensure that the legislation is complied with.

ROSC notes that there is no information on guarantees, endorsements, or contingent liabilities of the public sector provided in the budget documents. Information is limited to annual debt service and there are no established limits on new indebtedness. ROSC assesses that financial reporting is done primarily through CGE.

There has not been any noticeable improvement in this area due to very nature of the accounting system. SISTAFE will automatically provide information on commitments and arrears as the new accounting system will apply modified accrual accounting for expenditures. Thus gradually over the period 2003-2006 will more and more information become available on the real status of public finances.

Principle VI - Government carries out procurement in line with principles of value for money and transparency

Benchmark: Procurement undertaken in a transparent manner according to comprehensive procurement legislation based on internationally recognised model laws such as UNCITRAL. Organisational structures in place to monitor that rules and regulations are adhered to and that any misconduct is referred to relevant authority for sanction.

Rating: C moving towards B

Appropriate use of competitive tendering rules

The public procurement system appears to have a number of serious weaknesses with negative effect on the use of public funds. Existing procurement and tendering rules are relatively clear but the legislation is scattered over a number decrees and an outmoded law based on Portuguese legislation (1969-Law with amendments for use in Mozambique 1971). Procurement regulation has serious flaws such as lack of procedure manuals and standard tender documents. Consequently, tenderers have very little information on the process (such as tender opening, negotiation, and arbitration), as well as the criteria used for evaluation. Tender documents often omit critical instructions, and the technical specifications are often inadequate. Existing legislation is often not adhered to and there are frequent exemptions from tendering. This is facilitated by lack of proper recording of decisions and lack of identification of the persons responsible for procurement, making it difficult to hold the relevant persons responsible for misconduct.

There is no central directorate or tender board in Mozambique for overseeing the procurement process and establish procurement policies. DNPE in MPF is presently overall responsible for public procurement of goods whereas MOPH has the authority in relation to public works but neither appear to have the authority nor the expertise required for undertaking such a role. Evaluation committees do not always have qualified staff and independent observers are usually absent. Procurement commission responsible for tendering should be set up in all provinces, but most provinces have not established such structure. Reception committee required by law to monitor awards and contract implementation, including monitoring that the requested quality is being delivered, are rarely used.

An official registry of suppliers and contractors is used in tendering but it is not updated on a regular basis, thereby limiting open competition. A ten pro cent margin of preference for domestic goods of comparable quality is applied thus discriminating against foreign suppliers. There is limited national expertise in procurement, especially at provincial level, which is being exacerbated by lack of clear rules and standard documents and procedures, thus creating favourable conditions for corruptive practices.

The ROSC update notes with reference to the original ROSC that there is “a need to improve compliance with procurement and bidding rules for government purchases of goods and services”.

DNPE has informed that a new comprehensive decree is being drafted, based on UNCITRAL, Portuguese law and the present legislation. It will encompass all types of procurement, including public works. It suggests eliminating the ten per cent preferential treatment of national firms and in general it will be more open to the international market. It is, however, not foreseen to introduce standard tender documents. A Permanent Procurement Commission will be established at central level to oversee the process. At provincial level permanent commissions will be created for overseeing procurement at provincial level. According to the new decree, certain equipment such as IT and vehicles will be purchased via central procurement but otherwise emphasis will be on decentralisation of procurement. Many of the critical points in the existing legislation appear to be addressed in the new decree. The new decree is to be approved by the Council of Ministers end December 2002, so it can enter into force as part of SISTAFE as from 2003.

Decision-making is recorded and auditable

In principle all decision-making in the existing system is recorded and audited, but as rules are not always adhered to, for instance procurement commissions are not established, existing records of decision-making are either not existing or of limited value.

The new decree is expected to strengthen transparency by identification of the persons responsible for procurement. A system of fines and disciplinary processes has been foreseen in the new decree. A comprehensive training programme is being planned to upgrade staff qualification and improve administrative routines.

Effective action taken to identify and eliminate corruption

The Transparency International perception index (2000) rank Mozambique as no. 81 out of 90 countries, and the ETICA-survey from August 2001 supports the conclusion that corruption is prevalent in Mozambique both petty corruption and large scale corruption on higher level. The impact of this measure is not yet clear. The private sector complain about preferred tenderers being awarded contracts, liaisons between private companies and high ranking persons, lack of transparency in the evaluation process (created by poor documents, non-objective evaluation criteria, etc.), lack of access to information and poor performance in the execution of contracts. It appears that the private sector has little confidence that public procurement is carried out in a fair and open manner. The mal-functioning of the judicial system makes arbitration a non-valid option in relation to unfair treatment.

As mentioned above the internal control of IGF has too limited coverage and it fails to identify deficiencies in procurement. The Government has requested the Tribunal Administrativo to approve all contracts (ex-ante control) with a view to reducing corruptive practices and has agreed to meet with the private sector to discuss reforms in the area of procurement.

Principle VII - Reporting of expenditure is timely and accurate

Benchmark: Reconciliation of bank accounts and fiscal records done at least monthly; Public accounts closed within two months of the end of the financial year and audited accounts presented to the legislature within one year.

Rating: B

Reconciliation of fiscal and bank records is carried out on a routine basis

Central government financial reporting is governed Decree No. 7/98. The financial departments in the budgetary entities (DAFs) must obtain extracts of bank statements for which they are responsible and reconcile all entries herein with the items in the books (5^{th} day of the month) and forward this to DNAP or DPPF, whichever is appropriate. (10^{th} of the month).

There have been no significant changes during the last couple of years, but there seems to be less of an urgent need in this particular area. SISTAFE will allow reconciliation of fiscal and bank records to be carried out more frequently as the new accounting system will be fully computerised.

Audited annual accounts are submitted to parliament within the statutory period

Within twelve month following the end of the financial year DNAP must forward to Tribunal Administrativo (TA) the accounts for external audit. The first financial year to be audited since independence was 1998.TA is required to submit its report and opinion on the financial statement to the Parliament by 30 August the following year, i.e. 20 month after end of the financial year in question (see above). The long time delay is caused by three factors: i) the complementary period of three months; ii) MPF has until 31 December to closed the books and prepare the financial statements; and iii) Tribunal Administrativo has eight month to audit the accounts and prepare its report. Both the PER and the CFAA considers this time lag too long, thereby rendering the document useless as a tool for management of the economy and its finances. The PER also considers this as “one of the factors that seriously limits accountability”.

With the implementation of SISTAFE it is planned to reduce the period for forwarding audited accounts to the Parliament from twenty to eleven month (Law 09/02, Art. 50).

Principle VIII - There is effective independent scrutiny of government expenditure

Benchmark: The state accounts audited by the supreme audit institution, Tribunal Administrativo (TA), and the audited accounts forwarded to the parliament no more than twelve months after the end of the financial year; Financial audits undertaken of approximately ten per cent of all public accounting units annually as well as about five performance audits of these carried out annually.

Rating: C moving towards B

Government accounts are independently audited

TA is a court of law with the responsibility for the independent audit of the government accounts and financial statements; its legal purview provided for in the Constitution (Art. 173). Laws from 1997 (14/97, 15/97, 16/97) establish the legal regime for ex-ante and ex-post supervision of public spending as well as the basic principles of control and supervision for the general state budget, including evaluation of the performance of public administration in financial management. "TA has the power, not only to investigate and report financial misconduct, but also to apply sanctions and impose punishment" (PER) (unlike Anglo-Saxon type supreme audit institutions which can only report their findings to parliament). Its jurisdiction extends throughout Mozambique and covers the state and its services, autonomous state services organisations, municipalities, public enterprises with state majority shareholding, grants and donations from international organisations, and a number of other actors. TA has thus wide powers and prerogatives. The assessment of the PER is that "the responsibilities and powers accorded to the Tribunal Administrativo are adequate and well specified in the legislation".

The law (16/97) stipulates that the state accounts should be assessed according to the criteria of economy, efficiency and effectiveness in public spending, but there is no auditing of the performance of institutions or budgetary programmes (VFM-audits) (ROSC). The law also stipulates that the audit of the state accounts should include state assets, but so far there has not been any audit of capital accounts. This is due to non-compliance in the state accounts to provide information on state assets. TA is also charged with audit of subsidies, fiscal benefits and credits, but the CGE does not give any information on such transactions. The audits encompass scrutiny of revenues, recurrent expenditures and investments. Scrutiny of macroeconomic policies, including forecasts and assumptions, is very limited and is not provided to the public (ROSC).

The TA-report and its opinion (parecer) must be published in the public gazette, Bolletim de Republica. It certifies the accuracy, regularity, legality and economic and financial correctness of the accounts and of the financial management. The first state accounts to be audited after independence were those for the financial year 1998. The Committee on Plan and Budget in the Parliament analyses and gives its opinion to the Assembly by October. So far the 1998 and 1999 accounts have been audited and the report and opinion of TA discussed by the Parliament.

The TA notes that in general there "continues to be lack of compliance with the existing legislation pertaining to the preparation and execution of the state budget, which was already pointed out in previous TA opinion" (i.e. the CGE for 1998). The following general observations and recommendations on the state accounts for 1999 were given by the opinion of the TA:

- There are inconsistencies in the tables presented in the CGE due to "scattered" bookkeeping, which is often done manually;
- There is no information on state assets in CGE, despite previous recommendation from the Parliament to the Government to "utilise all resources to include a register on state assets in the CGE";
- Foreign financed investments are practically not registered, although this should be done according to the 1997-Framework Law (Law No. 15/97);
- Information from a certain number of bank accounts can only estimated due to lack of a system to register all movements of funds;

- For the same reason (lack of a registration system) a considerable part of new foreign debts incurred are estimates only and the information in the CGE is “not very reliable”;
- Information on off-budget revenues and associated expenditures, which in certain institutions constitutes considerable amounts, is still not included, despite recommendation by TA for the 1998-CGE to do so.

In relation to the specific observations in the 1999 TA-opinion the more important were:

Conc. the budget process:

- Divergence between budget figures on investments published by the national printers (INM) and the information on the same provided by the MPF to the TA;
- Many budget changes and virements made during the financial year are not included in the CGE and have not been approved by the competent authorities to allow for monitoring and control of these;
- Adjustments of budget figures for recurrent costs, in principle to allow for inflation only, have often included other adjustments and redistributions, without prior approval by the competent authorities;
- Adjustments of budget figures for investment costs are often made without the equivalent adjustment in the provisional allocation, making it difficult to monitor and control the transactions made;
- All revenues are not included, especially for financing of the budget deficit;
- Non-inclusion of retained and assigned revenues and associated expenditures as well as allocations for amortization of public debt and loan concessions.

TA recommended MPF to be more stringent in its future administration of the public finances, especially the budget documents with a view to ensuring that the legislation is complied with; by the inclusion of all off-budget revenues and expenditures, also prescribed by the law, and by timely publication of all budget changes undertaken during the financial year.

Conc. budget execution of revenues:

- Certain information on verified expenditures, cancellations, revenues and balances is not presented according to the economic classification, which makes it difficult to analyse and compare with other tables;
- Lack of consistency in information provided making it difficult to compare information from various tables;
- Detailed information on taxes, both assigned and not-assigned, with indication of the institution or organisation responsible for collection is missing;
- Detailed information on transfer of profits from state enterprises is needed, not only total amounts.

TA recommended MPF to observe the legislation in force, to provide information according to approved classifications such as the economic classification as well as information on fiscal benefits, and to be more consistent in the preparation of the CGE. TA reiterated the necessity to establish a central register for grants and loans contracted by the State with a view to establishing a complete and clear picture of all revenues and their use.

<u>Conc. budget execution of expenditures</u>:

- Lack of budgetary discipline in budget execution; the limits established by the law have often been exceeded;
- Spending in certain areas without parliamentary approval;
- Continuation of financing expenditures not foreseen in the OGE, namely those financed by assigned revenues, loans to public enterprises and amortization of public debts, which TA stressed is breach of the 1997-Framework Budget Law;
- Information on externally financed investments is still estimates only;
- Non-respect of the budget classifications in certain tables;
- Lack of information on subsidies and insufficient registration in a systematic manner per beneficiary.

TA recommended MPF to adhere to current legislation as well as established rules and regulation, to strengthen control of assigned revenues and associated expenditures and inclusion of these on the budget and to provide information on subsidies and the beneficiaries hereof. TA also recommended that complete information on investments financed by foreign sources should be presented.

TA also has the responsibility for undertaking financial audits and performance audits of public accounting units, of which there is around 700 in total. About ten per cent of all public accounting units should be audited annually and about five performance audits should be undertaken applying INTOSAI norms. Since its creation in 1998 TA has not finalised any financial audits or performance audits of any of the public accounting units, and only about twenty per cent of the required verification of the public accounting units is actually performed. Technical assistance has been provided since 1999 but it has not been accompanied by reinforcement in the staffing situation, making it difficult to undertake institutional strengthening. The President of TA does not prepare an annual Auditor General's Report as recommended by INTOSAI. It is consequently difficult to assess the real difficulties and challenges as well as the performance of the institution.

The capacity of TA is rather low. The management has limited background in auditing thereby creating a bottleneck in the system. During the last couple of years the audit staff has decreased in number from thirteen to ten staff of which eight are professional staff. It would require about twenty additional auditors if TA should be in a position to carry out its audit mandate. It is reported that the difference is salaries between the TA and IGF for audit staff is more than a factor two, making it little attractive to work for TA, and consequently recruitment of staff is difficult. If proper audit capacity is to be created, serious action is needed in relation to contracting of staff and defining competitive salaries. The amount needed would be less than half a per cent of the direct budget support provided by donors. TA does not have an independent budget, as MPF sets and approves its budget. The CFAA recommends that TA should negotiate with government an audit fee to be approved by the parliament each year, as a separate item of the state budget. In the TA-opinion the management points to this fact by stating that TA "continues to be confronted with limited resources, human as well as material".

CFAA considers that TA is too weak to carry out the full range of its duties. The ROSC recommends that TA should focus on ex-post auditing and control in accordance with the rules and procedures of external auditing recommended by INTOSAI, and the time lag for preparing CGE-audits should be shorted to no more than 12 months.

Government agencies are held to account for mismanagement and criticisms and criticisms and recommendations made by the auditors are followed up.

This is an area where it is extremely difficult to get reliable information. Donor experience suggests that disciplinary actions are taken against staff found guilty of misappropriation of funds or serious mismanagement, although the process is lengthy. Such personnel are normally transferred to another position within the government apparatus.

The CFAA assesses that the Attorney General's Office is in need of improvement of its capacity to deal with mismanagement and corrupt practices in the state apparatus. Parliamentarians need training in financial oversight in order to provide effective democratic control of public spending (PER and CFAA). In this context is should be taken into account that major donor financed project and programmes are still outside the state accounts and consequently there is no parliamentarian oversight and control of nearly 80 per cent of the country's investments. Donors put in own audit arrangements, e.g. ProAgri. The 2000 audit in ProAgri showed many of the same weaknesses and deficiencies as the audit of the CGE and the auditors gave three qualifications: i) no control and inadequate register of assets, ii) salaries to staff treated as "adjustments", and iii) reconciliation of bank statements incorrect.

The follow-up on TA and AR criticism from the first audit of the CGE in 1998 has been limited due to the long time lag for finalisation of audited accounts, which did not allow comments and recommendations to be incorporated in the state budget for the following year. The 1999 TA-report mentions that some improvements have taken place but that most points are still outstanding due to the reason mentioned above.

Principle IX - The budget process is transparent

Benchmark: All information on fiscal activities of the Government published, giving clear information on the functional distribution of expenditures.

Rating: B moving towards A

Information on the fiscal activities of Government should be available in the public domain.

The state budget (OGE), the state accounts (CGE) and the reports from TA as well as the QBER and PTIP are all published. The MTFF is still considered an internal working document and is not published (see above). The OGE and the PES as well as the CGE are discussed in the Parliament and subsequently published in Boletim da República. Issues such as long-term distribution, sectoral priorities and the level of public expenditures appear not at the centre of the discussions in the Parliament. The Committee on Plan and Budget analyses the TA-reports and prepares its opinion, which is then reported to the full Assembly.

The Press has commented on the two reports published by TA so far. It has also published interviews with parliamentarians both from the party in power and from the opposition. The financing of the state budget by own resources and long-term sustainability seems to be absent from the public debate. From time to time critics are raised by the Press and the civil society on for instance use of funds, but it is not clear which impact it has had on the way business is conducted. Ordinary citizens have limited access to information on public financing, partly because of language problems (estimates are that only about fifteen per cent of the population understands Portuguese, which is the official language), partly because of the low level of schooling and associated low incomes, so few people have access to or can read newspapers in a meaningful manner.

As mentioned earlier there is a number of shortcomings, especially with respect to coverage of the state budget, preventing the public to gain full information on financing of state activities. As from 2003 the Government will follow the ROSC recommendation of including reporting on the cost of tax exemptions in the state budget. The Government will also try to include as much off-budget funding into the state budget (see above). Currently there is no information on state assets, but the new accounting system would provide information on the government balance sheet.

Information should be presented in a way that facilitates policy analysis and promotes accountability

The information published is presented in a way, which does not facilitate policy analysis or comparison with past information. SISTAFE will go some way of improving this, but it must be accompanied by a number of other actions. PER finds that in spite of progress, “reporting remains partial, and has not been developed into an effective tool of policy planning, formulation and monitoring” and recommends that reporting in general should be further improved. ROSC recommends the following actions to improve transparency and accountability: i) more specific objectives and priorities for fiscal policy; ii) budgetary outturns for at least the previous two years; iii) maximum limits, stock and flow of public debt; and iv) information on major contingent liabilities, tax incentives, and quasi-fiscal activities. ROSC also recommends, that the QBER “should provide more detailed information, consistent with other sources, on the financing of the public deficit”. ROSC recommends publishing the MTFF.

5. Conclusions

The various assessments all point to the same conclusion, that major reform is necessary if the present high fiduciary risk is to be reduced to acceptable levels within a reasonable timeframe. The various reports on public financial management, i.e. CFAA, PER and ROCS, consider the main weaknesses to be:

- Considerable off-budget revenues, both donor funding and government retained and assigned revenues, as well as off-budget expenditures financed from such sources;
- Nearly 80 per cent of public investments donor-financed and excluded from the state budget;
- The present accounting system and standards archaic;
- Public procurement non-efficient and non-transparent;
- Internal and external audits and control extremely weak;
- Parliamentary oversight inexperienced.

CFAA considers the gap between the present accounting standards in Mozambique and internationally accepted standards as “enormous”, implying a high level of fiduciary risk. The CFAA states that this is at a high cost to the country, both directly and indirectly. Donors often demand advisors to work as gap-fillers to ensure an acceptable level of transparency in financial transactions. There is also the risk of not ensuring flow of foreign investments both in private and public sectors, if fiduciary risk continues at the present high level (CFAA).

At present situation there is no complete overview of the use of funds for public activities, due to the weaknesses listed above. It is consequently very difficult to undertake performance measures of service delivery in the sectors. Consequently, there is a limited guarantee that the economy is on the right track towards a more sustainable growth path with less dependency on donor funding of public activities.

The approval of a new public financial management law, SISTAFE, constitutes the basis for undertaking profound reform, but strong political will to implement the outlined reforms will be needed in the coming years, if significant changes are to take place. Despite progress in a number of areas during the last decade it must be noted that required actions in a number of areas were never undertaken, which could otherwise have had a profound impact on the level of fiduciary risk in Mozambique today. As pointed out by several of the studies on public financial management part of the problem is not lack of rules and regulations but adherence to these. The vested interest in various parts of the system should not be underestimated. This includes interests of donors seeing progress in “their” areas of co-operation, which had led to the establishment of parallel financial management systems in connection with financing of projects and programmes, thereby undermining the state system as well as the democratic control of the use of public funds, irrespective of their origin. If donors move away from budget support pressure for reform might also be less and consequently donors could contribute to increased fiduciary risk in the medium-term.

The assessment of fiduciary risk does not directly include contingent liabilities, although it is related to transparency in the use of public funds. Contingent liabilities constitute a specific and non-negligible risk in Mozambique. At present there is no public overview of the magnitude of contingent liabilities and, as a consequence, the risk that funds have to be used from the state budget to cover losses cannot be estimated. There are contingent liabilities related to various areas, such as pension schemes (e.g. INSS), state interest in privatised banks and enterprises with significant state participation, and natural disasters. As the PER puts it: “fiscal adjustment that targets the budget deficit and debt burden does not necessarily prevent fiscal instability”. In cases where the state has to finance such events, as a minimum there would be an impact on the Government’s programme for poverty reduction, which is the main objective for providing direct budget support.

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