

**International Monetary Fund
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Implementing The Fiscal Transparency Code¹

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I. Introduction

The IMF and the international community in general have attached increasing importance over the past three years to improving governance and implementing international standards of good practice in key economic management areas.² These activities are seen as essential steps towards improving the effectiveness of economic management and reducing the risk of future financial crises. Standards of good practice in particular are seen as providing a framework that can provide a better focus for policy discussions and thereby help strengthen macroeconomic management and the functioning of financial market. This paper outlines the work that the IMF has undertaken in one area of standards and codes, namely, the development of implementation of the *Code of Good Practices on Fiscal Transparency* (the fiscal transparency code).

Work carried out by the IMF, including reports and observance of standards and codes (ROSCs) prepared in consultation with country authorities, is available and maintained up-to-date on the IMF external website through its Standards & Codes web page (<http://www.imf.org/external/standards/index.htm>). The intention of the fiscal transparency element of this site is to provide essential tools to enable country authorities to carry out an assessment of fiscal transparency against the code. The fiscal transparency code, the *Manual on Fiscal Transparency*, a questionnaire of fiscal transparency, and e-mail facilities are available through the fiscal transparency page. All documents are available as PDF files in six major languages other than English. The IMF will provide technical assistance to countries to help them complete a self-assessment, and fund staff work closely with the authorities in preparation of ROSCs.

The remainder of this paper discusses the structure of the code in more detail, the relationship between the transparency code and international accounting and statistical standards, experience with implementation of the code, and some next steps.

II. The Structure of the Code and Objectives Of Fiscal Transparency Assessments

Fiscal transparency is defined as being open to the public about the structure and functions of government, fiscal policy intentions, public sector accounts, and fiscal projections (Kopits and Craig, 1998). Recognizing the diversity of economic, and institutional characteristics across countries, the fiscal transparency code was developed to meet the need for a broad universal set of good practices to which all countries could aspire.

The code structure

The fiscal transparency code defines the main dimension of fiscal transparency under four general principles (see Box 1). Under each of these general principles, a set of specific principles is identified, and under each of these specific principles a set of operational good practices is defined (the latter are not included in the summary provided in Box 1). An assessment against the code thus consists in examining the practices defined in the code. The practices have been set at level of transparency generally viewed as being acceptable.³ Some advanced countries achieve level of transparency well above that suggested by the code, but many countries do not attain the code standards, and most could benefit from some improvement in their practices to reach the suggested levels. In recognition of the large gap faced by developing countries in particular, the current version of the Manual identifies a subset of fiscal transparency practices (“basic requirements”) that are seen as being a priority for those countries.

The need for comprehensive, timely, and reliable budget estimates and public accounts is, of course, strongly emphasized in the code—and, as discussed further below, the need to raise basic quality of accounting data is being given increased emphasis. However, it is clearly recognized that, by themselves, good public accounts are not enough. One of the most important features of the fiscal transparency code is that it broadens the concept of fiscal management beyond that of managing the public finances as defined by conventional budget and public accounts documents. The dimension of fiscal transparency—and, implicitly, fiscal management—are extended to include any activity of a fiscal nature. Transparent fiscal management practice, according to the code, must disclose all forms of off-budget fiscal activity, and fiscal policy statements are required to look beyond the single year. This feature, is outlined in section III of the paper, is the basis for an important distinction between the transparency code and international accounting and statistical standards.

ROSCs

Making assessments of fiscal transparency widely available to the markets and the public is one of the basic strategies for promoting implementation of the fiscal transparency code. The basic rationale for improving fiscal transparency and for making the current status of the system publicly available is, first, that comprehensive and reliable information on fiscal activity is a necessary basis for sound fiscal policy, and, second, that market awareness of fiscal policies in particular countries, in light of the status of fiscal transparency in these countries, will help to reinforce good practices and sound fiscal policies. In this way, market forces will help to encourage transparency and guide fiscal policies.

The country fiscal ROSCs are the main instrument currently used by the IMF⁴ to promote the fiscal transparency code, aside from continuing technical assistance in a range of good practices and broad dissemination of the code and manual through seminars and the internet. These carried out by the countries on a voluntary basis and are being progressively integrated with a regular Article IV surveillance discussion between the IMF and its member countries. Specific transparency issues may, as in the past, be raised as part of the normal surveillance dialogue. When a country agrees to do a ROSC, however it involves a sequence of steps including a detailed self-assessment (in some cases with technical assistance from the IMF), a discussion of practices and issues with Fund staff, and preparation of a ROSC document consisting of two components: (I) a description of practices

in relations to the code; and (II) a Fund staff commentary, which suggested priorities for improvement. The ROSC is, reviewed by Fund staff and by country authorities and is circulated to the IMF Board, generally as part of Article IV discussion. The fiscal ROSCs along with other ROSCs are, placed in the binder, which provides background to IMF Article IV discussion and will eventually be available to the Boards of both the IMF and the World Bank. ROSCs are to be updated annually (by way of indicating areas of progress to identified priorities) and will periodically be reviewed more extensively. ROSCs, with the agreement of the authorities are published on the IMF website:

<http://www.imf.org/external/np/rosc/rosc.asp>.

III. The Fiscal Transparency Code and Accounting And Statistical Standards

The fiscal transparency code does not attempt to define all possible standards applicable to fiscal activity. However, the code has been developed in cognizance of the main relevant standards, and revision of the code undertaken from time to time will aim to ensure that all developments in such areas are taken into account. Development of international standards for public sector accounting, under the aegis of the International Federation of Accountants—Public Sector Committee (IFAC-PSC) and the revision of the IMF's government finance statistics (GFS) manual for fiscal statistics reporting are two areas that are of obvious importance to fiscal transparency. Box 2 summarize the main recent developments in these areas.

These developments both aim, in long term, at establishing accrual recording and reporting as the basis of public sector accounting and fiscal statistics. Both, however, also recognize that cash basis accounting, with various modifications, is used by the majority of governments and that, despite the know shortcomings of cash accounting, it will take a considerable time for many countries to adopt accrual basis accounting and fiscal reporting in full. Thus the IFAC-PSC accounting standards are being set for the polar cases of pure cash and pure accrual basis accounting, but most countries will be at some intermediate stages on this spectrum, where the financial statements and disclosures required by cash accounting are too weak, and those of a full accrual basis system far to demanding. The revision of the GFS system is based on full accrual reporting, but it recognizes that many governments will record only on a cash basis for some time in the future, and that either cash reports will be used or some form of adjustment to estimate accrual data will be required until recording is upgraded.

The fiscal transparency code is fully supportive of these efforts. The code does not advocate accrual accounting, but the manual recognized adoption of accrual accounting as being among the best practices for a advanced economies. In some respects, the standards advocated by the code can be seen as practical intermediate measures toward the general adoption of accrual standards and comprehensive reporting of fiscal data. The fiscal transparency code, for instance, advocates reporting on government financial assets and disclosure on contingent liabilities irrespective of the accounting standards and policies adopted.

Accounting standards and policies, of course, become relevant in determining the evaluation of assets and inclusion of assets and inclusion of assets reports in a integrated financial statement. But it is important to encourage all governments to take the first step toward an inventory of assets—even if, in the first instance, these are recorded at historical costs or records are incomplete. In this way, it is envisage that the fiscal transparency code will act as a force to encourage countries toward goal of adopting appropriate accounting standards and that the international community will cooperate in encouraging progress on both fronts.

The fiscal transparency code, however, encompasses broader aims than either the adoption of international accounting standards or reporting GFS data on an accrual basis. Accounting

standards are aimed at establishing standards for reporting on the financial position of an entity rather than the impact of fiscal activity on the economy. The revised GFS, while it will use accrual accounting principles as the basis for reporting on the activity of the general government sector will do so on an institutional basis; that is, it will report on the fiscal activity by general government, but on the fiscal activity by other elements of the public sector (often called quasi-fiscal activity).

The fiscal transparency code is centrally concerned with the same institutional coverage as the revised GFS. But, because fiscal policy can be carried out by a variety of off-budget mechanisms, the fiscal transparency code requires supplementary reporting on the extent of activity encouraged through tax exemptions, quasi-fiscal activity of financial and nonfinancial state owned enterprises or central banks, and issuance of guarantees⁵. Some, but not all of this kind of activity can be covered by disclosure requirements under international accounting standards. In some areas, there are considerable technical difficulties in establishing an agreed basis for quantitative measures.

The position of the fiscal transparency manual on these matters is that it is almost always possible to make a broad descriptive statement of such activities and, often, at least partial quantification is possible. Where these activities are relevant to judging the fiscal position of government or the risk associated with the fiscal projections, then such matters should be disclosed to the public and independent analysts. While less rigorous than accounting or statistical standards, the requirements of the fiscal transparency code provide an important outer security barrier to help assure accountability for use of public funds. Over time, moreover, rigorous standards can possibly be developed in many areas of off-budget activity and these can be formally included as part of accounting and statistical standards.

VI. Implementation—Experience to Date

Since the inception of the work on assessment of standards and codes by the IMF, the World Bank, and other international agencies in early 1999, a large number of assessments on the core standards of interest to the international community have been carried out. Assessments relative to the fiscal transparency code have been completed for around 25 countries by end-September 2001, and further 36 are in the pipeline, with most of the expected to be substantially completed by end-April 2002. Some of the findings are as follows:

*** There are widespread problems of basic data quality in developing and transition economies.** Although as yet the ROSC sample size is small, the ROSCs combined with other traditional TA give a clear indication of a lack of rigorous standards in presenting budget and accounting data among developing and transition economies. In response, the revision of the fiscal transparency Manual now nearing completion is giving particular emphasis to establish clearer definition of data quality issues (in conjunction with similar efforts on the data dissemination standard).

*** Few countries report adequately on contingent liabilities, tax expenditures, or quasi-fiscal activities.** The finding is not surprising and, even though the sample size is small, the lack of systematic reporting on this aspects is known to be widespread, the ROSCs provide a vehicle for systematically recording practice and suggesting reasonable improvements. Recommendations are being made by staff in a high proportion of the ROSCs that improvements are needed in reporting various kinds of off-budget fiscal activity. There may be scope for a set of specific technical programs aimed at encouraging improved standards of reporting in these elements across a wide range of countries.

ROSCs provide a potentially useful mechanism for identifying good practices and disseminating these more widely. Particularly in later group of ROSCs, some emphasis has been given to exploring certain aspects of practices and highlighting these. Understandably most examples of good practice come from advanced countries, but cases where improved practice has been adopted in response to a perceived weakness (see Box 3) have also been highlighted.

The ROSC have evolved from an initial set of “experimental” summary reports to a relatively extensive (although necessarily still summary) assessment of the fiscal management system against each element of the code. In principle, this form of assessment should provide a relatively objective benchmark from which countries can set priorities and a baseline to record long term improvements in fiscal transparency.

Efforts have been made to encourage countries from all regions and economic groupings to participate in the fiscal ROSC process. In terms of standard groupings used by the IMF World Economic Outlook (but modified by replacing the “transition economy” group of WEO with an “emerging\transition economy” grouping), the distribution of ROSCs now underway or completed is as follows:

	<i>Total underway</i>	<i>Of which, published on IMF sites</i>
• Advanced Economies:	8	6
• Emerging market\transition economies	21	13
• Developing economies	16	6

For the advanced economies, the general expectation is the most good practices of the transparency code will observe or exceed; the focus for this group is in highlighting aspects of best practice that have potential application elsewhere and examining the possibilities of further improvement in areas such as application of accrual accounting and budgeting to government or improving tax expenditures reporting practice. For the other groupings, the main benefits of the ROSCs are the identification of weakness in current coverage or quality of fiscal data. Participation in the ROSC process allows the government to make a public commitment to improve fiscal transparency practices (see Box 3).

V. Next Steps

The broad principles embodied in the fiscal transparency code appear to have been accepted as a practical basis for assessing and improving fiscal transparency in countries across all regions of the World. It is evident that substantial resources, both from international organizations and from individual countries, are required to carry out assessments—and even more to implement needed reforms. But the benefits in term of improved efficiency and equity of fiscal decisions are likely to exceed these cost by a wide margin—and the costs of **not** making the effort to apply basic standards of transparency and accountability are potentially enormous.

It must be recognized, however, that implementation of standards across a wide range of countries involves a very significant change in approach by international organizations, by bilateral agencies, and by countries themselves. In advanced countries, many of these changes will be driven by countries themselves—many of whom are standard setters. The advantage of international standards for these countries is through establishing clear base for inter-country comparison and dialogue. The European Union provides a good example of a mechanism for establishing common standards for fiscal transparency for aspirant members that are consistent with good practices of the fiscal transparency code.

The issues are much more difficult for the broad range of developing and transition economies in the rest of the world. Here, the challenges are, first, to establish an

environment whereby good practices of fiscal transparency are recognized by the legislature and the public and rewarded by the market, and second, to align programs of technical assistance to reinforce these incentives. A number of mechanisms need to be developed or strengthened:

The quality of fiscal data should be explicitly indicated in government fiscal reports

(by way of noting that fiscal accounts data are reconciled with bank data, whether are based on final audited accounts or are provisional etc.). And, conversely, fiscal analysts should be aware of the status of fiscal data quality when they draw fiscal policy conclusions.

ROSC assessments of fiscal transparency should be used by fiscal analysts—and, on other hand, fiscal analysts or specialists should indicate any inaccuracies or gaps in the fiscal ROSCs. In this respect, some further development of the information basis of ROSCs is undoubtedly needed (particularly the early experimental reports)—and there needs to be a critical mass of publicly available ROSCs to interest financial analysts.

Improving fiscal transparency should be recognized as an important basis for setting priorities for fiscal management technical assistance by countries and be all multilateral and bilateral agencies. The IMF has taken the lead in establishing the basis for a standard for fiscal transparency, and, as noted, the intention is that ROSCs should serve as a benchmark to help set priorities for technical assistance and measure progress over time. It is essential for this to be effective, however, that the standard be more widely recognized and used.

BOX 1: MAIN PRINCIPLES OF THE FISCAL TRANSPARENCY CODE

1. Clarity of rules and responsibilities

1. The government sector should be clearly distinguished from the rest of the public sector from the rest of the economy, and policy and management roles within government should be well defined.
2. There should be a clear legal and administrative framework for fiscal management.

2. Public availability of information

1. The public should be provided with full information on the past, current, and projected fiscal activity of government.
2. A commitment should be made to the timely publication of fiscal information.

3. Open budget preparation, execution, and reporting

1. Budget documentation should specify fiscal policy objectives, the macroeconomic framework, the policy basis for the budget, and identifiable major fiscal risk.
2. Budget data should be classified and presented in a way that facilitates policy analysis and promotes accountability.
3. Procedures for the execution and monitoring of approved expenditures and for collecting revenue should be clearly specified.
4. There should be regular fiscal reporting to the legislature and the public.

4. Independent assurances of integrity

1. Fiscal data should meet accepted data quality standards.

2. Fiscal information should be subject to independent scrutiny.

BOX 2: international Standards for Financial and Fiscal Reporting

Efforts are being made to improve accounting and financial reporting standards by a member of governments. The work of IFAC and the proposed revision of the *GFS Manual*, together with the Code, and further steps toward development of standards that will help improve international comparability of data and contribute to improve fiscal transparency. It is important to distinguish the different objectives of these initiatives \, and to coordinate work in all three areas as closely as possible.

IFAC-PSC Study (<http://www.ifac.org>)

The Public Sector Committee (PSC) of IFAC in May 2000 released its study on financial reporting *Governmental Financial Reporting* at <http://www.ifac.org/Guidance/Pub-Download.tmp?PubID=960182179426> to help national governments prepare financial statements that provide on the financial performance and position of the government. The study discusses principles that are the basis for international public sector accounting and reporting standards now being developed by the PSC as part of its continuing standards project. The PSC has released the first eight International Public Sector Accounting Standards (IPSAS) and a further six exposure drafts that are intended to lead the standards. For the most part, the IPSAS are based on modification of International Accounting Standards designed for the private and modified for applicability for public sector. ED 9, however, proposes to establish requirements for financial reporting under cash accounting. These principles will be of value for most governments that operate a near cash basis system.

GFS revision

The GFS is not accounting or financial reporting standards, but a standard for analytical reporting of fiscal statistics; GFS looks at economic impact rather than accounting entity performance. It is desirable that government accounts classification and financial reporting standards be developed in a way that is compatible with the generation of such statistical reports, so that a single information system can meet both accounting and fiscal reporting needs. It is also important that GFS fiscal reports be completely reconciled with government budget reports and the final accounts to provide assurance of data reliability and comprehensive coverage of the fiscal accounts. The GFS is being revised and a full draft is available at: <http://www.imf.org/external/ubs/ft/gfs/manual/index.htm>. The public recognized the growing importance of accrual concepts for government accounting and aims to harmonize GFS completely with other international financial statistics system (notably the SNA) that use accrual concepts. The proposed would nor require that countries adopt accrual accounting: a staged transition is envisaged, and countries could adjust data from their cash accounts, or, in many cases use cash data where differences between cash and accrual are not substantial.

BOX 3: FISCAL TRANSPARENCY IN PAKISTAN

The fiscal ROSC for Pakistan provides an illustration of the way in which the process can operate in developing or emerging market economies. Pakistan has, for several years been carrying out a long-term program to improve its accounting system through computerization and introduction of a new accounting model (NAM), which will replace the present accounts classification and take some preliminary steps

toward accrual basis accounting for government. Progress in implementing this system, however, has been delayed for several years, in part because the accounting function was not fully under the executive branch of government. In the absence of effective reform, fundamental accounting functions such as adequate coverage and timely reconciliation with bank accounts were not being rigorously implemented. These systematic weaknesses led to the emergence of significant data discrepancies in a number of areas.

The Pakistan government undertook a review of its fiscal reporting practices and also participated in a fiscal ROSC during 2000⁷. As a consequence of this work, fiscal monitoring committees were established at federal and provincial level to ensure that basic reconciliation processes were undertaken. In parallel, the accounting function, formerly under the Auditor General, has now been transferred to the executive branch of government under the Controller General of Accounts within the Ministry of Finance. The ROSC also identified a range of other areas where fiscal data need to be progressively improved to inform fiscal policy making, including reporting on contingent liabilities and tax expenditures, developing a medium-term budget framework, and compiling comprehensive data on government financial assets. These reforms should, in turn, support the long-term aim of establishing a computerized government financial management information system and modern accounting principles.

The ROSC process (and allied technical assistance from variety of agencies) in Pakistan has helped to highlight the critical role that improvement in fiscal data quality—and importantly an explicit institutional commitment to maintenance of data quality—can play in establishing firmer fiscal management and control. A firm commitment by the government to improve fiscal transparency also helps to define the objectives and set priorities for fiscal reform, which, in turn, facilitates the formulation and implementation of technical assistance in this areas.

¹ Prepared for the 10th International Anti-Corruption Conference, Prague October 7-11, 2001. An earlier draft this paper was presented at the International Consortium on Governmental Financial Management, Miami, Florida, April, 2001

² The IMF and the World Bank are jointly involved in promoting standards by assisting countries complete assessments against key standards in the form of *Reports on the Observance of Standards and Codes* (ROSCs), some of which results from the joint Bank-Fund *Financial Sector Assessments Program* (FSAP). Implementation of standards has also been advocated by the Financial Stability Forum (FSF), the G-20, the Manila Framework Group, Asia and Pacific Economic Cooperation (APEC), and Western Hemisphere Finance Ministers.

³ Practices identified in the code are derived from observed good practice and will be updated periodically. The current version was approved by the Executive Board in March 2001.

⁴ In addition the fiscal transparency code has been used by some NGOs as an input to their assessments of budgetary practice in particular countries (e.g., IDASA assessment of budgetary practice in the Republic of South Africa).

⁵ And, in addition, the code includes requirements for medium-term and long-term projections and for clear specifications of policy assumptions and objectives.

⁶ As at August 31, 2001

⁷ See <http://www.imf.org/external/rosc/pak/fiscal.htm>