PUBLIC EXPENDITURE AND FINANCIAL ACCOUNTABILITY (PEFA) ASSESSMENT

NEPAL PFM PERFORMANCE ASSESSMENT II

AS OF FY2013/14

GOVERNMENT OF NEPAL
Ministry of Finance

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Public Expenditure and Financial Accountability Secretariat

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MAY 2015

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CURRENCY AND EXCHANGE RATES

Currency unit = Nepalese Rupees (NPR)
1 USD = 97.15 NPR
(As of July 19, 2014)

FISCAL YEAR

July 15 to July 14
Nepalese FY2070 is equivalent to World Bank FY2013.

Government of Nepal

Government of Nepal
Ministry of Finance

Dr. Ram Sharan Mahat
Finance Minister

Message

It is my great pleasure to bring the Second Public Expenditure and Financial Accountability (PEFA) Assessment Report. I would like to congratulate the Assessment Team which was led by the Joint Secretary of the Budget and Program Division and the Coordinator of the PEFA Secretariat of the Ministry of Finance for successful conclusion of the assessment. I was the Finance Minister when the first PEFA assessment was carried out in 2007 and coincidentally I am holding this chair again at the time of second assessment.

I am quite impressed to note significant progress in several dimensions of the Public Financial Management (PFM) in our country system which has led a strong base for enhancing transparency and financial accountability. I am pleased to note the continued efforts in strengthening PFM system which has led to improved ranking in the second assessment. On behalf of the Government of Nepal I would like to express full commitment for PFM reforms as it directly contributes to our development efforts and to implement our Development Cooperation Policy.

Needless to mention that credible Public Financial Management system is one of the key foundations for an accountable government. Over the past several years, we have initiated first phase PFM reforms in the area of budget credibility, tax policy, single treasury system of accounts (TSA), improvements in external audit and reforms in public procurement system among others. All these have contributed to upward movements of the performance of Nepalese PFM system in the second assessment. I would like to appreciate the hard work and contribution of all government officials with strong support from development partners to implementing these reforms.

The second assessment has now paved a way to frame the Second Phase PFM reforms to close the gaps observed in the current assessment. I have my full support for reforms as directed by the current assessment. In terms of providing space for reforms in budget execution, our teams are already working on Budget Management and Financial Accountability Act which will address most deficiencies observed in the current assessment. Likewise, the Government has recently amended through ordinance the Public Procurement Act which I believe will provide more space for enhanced competition and transparency.

Unfortunately, Nepal recently faced a severe disaster by April 25th and May 12th earthquakes which caused a severe setback to economic development. I would personally acknowledge the support received from many development partners at the time of the crisis. While we are faced with severe crisis, I also see it positively

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that it has also created opportunity for us to rebuild our nation with support from all development partners. Continued PFM reform is critical in this process to ensure better transparency and accountability to manage public funds. I would like to request our friendly countries for their continued support in the government's efforts of reconstruction and rehabilitation as well as in implementing PFM reforms.

The PFM Steering Committee which is chaired by the Finance Secretary will provide leadership to PFM reforms. I appreciate the role played by this Committee to drive the reform initiatives and to monitor the implementation of reform actions. I also appreciate strong support received from the World Bank team in providing technical support. I would also like to thank Government of Australia, United Kingdom (DfID), Government of Norway, Government of Denmark, Swiss Confederation, the European Union and the USA (USAID) who have contributed to the Multi-Donor Trust Fund (MDTF) established for supporting PFM reforms.

Following the finalization of this Assessment, I would now like to ask the PFM Steering Committee to start working on the Second Phase PFM Reform Actions so that we have a credible action plan for implementation which in parallel will move with our high priority agenda of rebuilding the nation through reconstruction and rehabilitation to respond the needs arising from the earthquake disaster.

Finally, I wish all the best to all professionals who have been involved in the assessment process to continue to provide their leadership in the design of the Action Plan and then on implementation.

RSMahat

Dr. Ram Sharan Mahat
2015/05/31

Government of Nepal
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Government of Nepal
MINISTRY OF FINANCE

SINGHADURBAR
KATHMANDU, NEPAL

FOREWORD

I am pleased to write a foreword to a very important assessment related to Public Expenditure Financial Accountability (PEFA) which has recently been endorsed by the Public Financial Management (PFM) Steering Committee chaired by me. This is a second assessment carried out in about seven years since the first PEFA assessment which was completed out in 2007. Like the previous PEFA, the second assessment is also fully led by the Government of Nepal with technical support from the World Bank which was carried out with wide stakeholder consultations which include the government agencies, the private sector and the development partners. The current assessment aimed to record major reforms related to PFM across 31 (including 3 donor related) indicators as per the PEFA Guidelines and to identify gaps in these indicators for further improvements which create a basis for the government to undertake the next phase of PFM reforms.

I am pleased to note that the assessment has concluded overall progress in many PEFA indicators as compared to previous assessment. This has indeed created a credible basis for establishing a good PFM system in Nepal. One major shift that has contributed to improvements in various indictors was the use of information technology which helped to enhance transparency and accountability. I noted some visible improvements in all six critical dimensions of the PFM system. It is indeed encouraging to note improvements in the area of credibility, comprehensiveness and the budget formulation process. Similarly, there are improvements in accounting, reporting and audits. I am also pleased to see upward movements in donor practices. Areas that require further improvements are (i) budget execution and control, (ii) enhancing parliamentary scrutiny on the PFM system for better accountability, and (iii) enhanced control of the extra budgetary funds.

I would like to enforce that the Government recognize these gaps and would like to commit to address these gaps during the next phase of reform program. I fully trust that improvements in the PFM system as concluded would help align with the requirements of our Development Cooperation Policy in requesting all development partners to align with our country PFM system while channeling their assistance and also, will help us continue to strengthen our system in the areas where gaps are being observed in the current assessment.

I would like to recognize the leadership and contribution of Team Leaders and Joint Secretaries of various dimensions and would like to acknowledge Dr. Baikuntha Aryal, Mr. Ram Sharan Pudasaini and Mr. Madhu Kumar Marasini of the Ministry of Finance, Mr. Jayadev Shrestha (FCGO), Mr. Baburam Gautam (OAG), Mr. Naresh Kumar Chapagain (PPMO) and Mr. Puspa Lal Shakya (NPC). They have tirelessly contributed to this exercise from the time of inception to successful conclusion of the assessment. In addition, I also would acknowledge the leadership of Mr. Rajan Khanal, Secretary of MOGA, who was the Joint Secretary of the Ministry of Finance when he was leading one of the teams. I would like to appreciate the active participation and contribution of all team members associated with them.

Secretary
Ministry of Finance

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Government of Nepal
Ministry of Finance

I would like to acknowledge the leadership and coordination role jointly provided by the Budget and Program Division and the PEFA Secretariat of the Ministry of Finance to steer the entire process. In particular, I would like to commend the leadership provided by Dr. Baikuntha Aryal from MOF and four PEFA Coordinators - Dr. Mukti Narayan Paudel, Mr. Dilli Ram Sharma, Mr. Jagadish Regmi and Mr. Mukunda Raj 'Prakash' Ghimire who provided the Coordinator role of the PEFA Secretariat at different phases during the assessment phase. I would also like to thank Mr Suresh Pradhan and Mr Rajendra Bajracharya for their role while initiating the assessment.

Last but not the least; I fully recognize the key role played by the Member Secretary of the PEFA Secretariat Mr. Babu Ram Subedi, who was deeply and passionately engaged during all phases of the Assessment.

I would also like to acknowledge the leadership provided by the former Financial Comptroller General Mr. Shankar Prasad Adhikari, who was instrumental to provide guidance to the assessment Teams.

I fully recognize the support and dedication of the World Bank team who provided technical support. In particular, I acknowledge the leadership provided by the Task Leader of this Assessment Mr. Roshan Darshan Bajracharya (Senior Economist), Mr. Bigyan Pradhan (Senior Operations Officer), and Mr. Manoj Jain (Lead Financial Management Specialist) in working closely with government teams and in facilitating to successfully complete the assessment. I would also like to appreciate full support and cooperation received from the World Bank Country Director Mr. Johannes Zutt and the Country Manager Mr. Takuya Kamata in supporting the government in this endeavor. My special thanks also goes to various funding partners supporting the PFM Multi-Donor Trust Fund (MDTF) through which the financial support was received to carry out this assessment as well as to implement reforms related to PFM. I would, therefore, like to acknowledge Government of Australia, DfID, Government of Norway, Government of Denmark, Swiss Government, the European Union and the US AID for supporting PFM reform program through MDTF. Lastly, I also wish to record my appreciation to officials of several organizations who participated during the assessment.

On behalf of the Government of Nepal, I would like to reiterate the importance of PFM reforms which are critical for socio-economic development of the country. Due to recent tragedy hit by April 25th and May 12th severe earthquakes causing huge loss of lives and country assets. This has slightly affected in contributing to some delay in finalizing the assessment. The recent disaster although has been a great loss for the country, has also provided opportunities to look afresh in our development agenda ensuring better accountability and good governance ensuring a credible PFM system. We anticipate continued support from all development partners in our development efforts including your support to implementation of second phase PFM reforms.

Suman Prasad Sharma
Finance Secretary

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255/071.72

Date: 14th May, 2015

Preface and Acknowledgement

Public Financial Management (PFM) is a crucial part of governance. It is considered as the blood circulation of the government system which carries energy for government activities for socio-economic development of a country. Performance of public expenditure depends on a sound PFM system. Government of Nepal has taken various initiatives for PFM reform through First Phase PFM Reform Action Plan. Budgetary reforms, taxation system reform, treasury reform, reporting system reform etc. are the major ones. After the implementation of TSA, 'multiplier effect' has been created in the PFM system of Nepal.

This report is the second in series for performance assessment of PFM system of Nepal based on the Public Expenditure and Financial Accountability (PEFA) Framework. This assessment is conducted as the repeat PEFA Assessment to compare the PFM performance (with the PEFA Assessment Report 2008) made during the period of six years (2007/08 to 2013/14). It is found from the assessment that not only the PFM system but also the performance of processes and institutions are improved despite the political transition in Nepal. 'Nepal has made a substantial progress in public financial management, especially through the use of information technology', the report concludes.

Out of the 31 high level PFM indicators, 19 (61%) indicators are found to be upgraded with seven 'A' scores in comparison to only one 'A' score in 2008 Report. Credibility of Budget is improved and being internalized. Comprehensiveness of the budget and the formulation process has also improved. The country has made impressive strides in budget coverage, comparability and its timely reporting. Audit quality and coverage has improved, as well as, donor predictability of budget support.

In contrast to the light of these improvements, two indicators (7%) are found to be deteriorated. It is due to the absence of parliament during the period considered for the assessment for one indicator and very slight increase in extra budgetary funds for another indicator. It signifies that the continuity of crucial political institutions and regular monitoring of the PFM system are key factors for reform process.

Ten indicators (32%) are found to be remained the same as of the past assessment. With a set of impressive PFM rules, budget execution and full enforcement of these rules are found to be challenging. Enhancement of the internal control system is crucial part of the future reforms. Therefore, GoN is preparing the Second Phase PFM Reform Action Plan based on the gaps identified during the assessment and the lesson learned from the First Phase of PFM reform initiatives (2008-2013). A comparison with other countries shows that the Nepal's PFM system is relatively strong.

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As this assessment is fully government owned and based on the self-assessment model, it will help us guide and expedite the PFM reform process of GoN for the future. We are able to find gaps in our system by ourselves. This has created a self-pressure for immediate reforms in some of the areas of PFM in Nepal. It will help enhance an ownership of reform. Simultaneously, we have trained and created a critical mass of PFM reform through various workshops and field works during the period of assessment.

The assessment work was coordinated by this Secretariat. Nine working teams were formed based on the thematic areas of expertise to conduct the assessment. Technical support was provided by the World Bank. We would like to thank the PFM Steering Committee, headed by the Finance Secretary, for providing overall guidance for the assessment. We would like to thank Mr. Suman Prasad Sharma the Finance Secretary for guiding and motivating us for the job. We cannot forget Mr. Shanta Raj Subedi and Dr. Yuba Raj Bhusal, the former Finance Secretaries, for their role in the earlier days of assessment. Sincere thanks goes to Mr. Shankar Prasad Adhikari, the former Financial Comptroller General for providing us regular encouragement for the assessment. Due thanks goes to Dr. Baikuntha Aryal for regular involvement and support in the whole assessment process.

The report would not be completed, in the absence of dedicated supports from Mr. Roshan Darshan Bajracharya, the Senior Economist of the World Bank. We would like to thank him and his team: Mr. Sudyumna Dahal, Ms. Pragya Shrestha, Mr. Yogesh Bom Malla, and Mr. Deb Narayan Mahato in this endeavor. Mr. Manoj Jain, the Lead Financial Management Specialist, and Task Team Leader of SPFM, is equally thankful for this task. We cannot forget Mr. Bigyan Pradhan for his regular support and coordination. It would be injustice to forget Mr. Tony Bennet, Prof. Prithvi Raj Ligal and all the reviewers and commentators from DPs who provided comments and suggestions on the draft report.

We would like to thank all of the team leaders. Joint Secretaries Mr. Rajan Khanal (now the Secretary of MOGA), Mr. Baikuntha Aryal, Mr. Madhu Kumar Marashini and Ram Sharan Pudashaini from MOF; Mr. Mukti Narayan Paudel/ Dilli Ram Sharma/ Jagadish Regmi and Mr. Jayadev Shrestha from FCGO; Mr. Puspa Lal Shakya from NPC, Mr. Naresh Chapagain from PPMO and Mr. Baburam Gautam from OAG had diligently led the assessment teams.

We would like to thank every member of the 9 assessment teams and acknowledge them for their wonderful team work for preparing team reports in one of the six core dimensions and the thematic areas of PFM. This work would not be completed in the absence of their sincere efforts. Finally, we would like to thank and acknowledge all of the institutions which provided us the necessary information for the assessment.

B Subedi
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Babu Ram Subedi
Member Secretary

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Mukunda Raj 'Prakash' Ghimire
Co-ordinator

Contents

Abbreviations and Acronyms

ADB	Asian Development Bank
AMP	Aid Management Platform
BMIS	Budget Management Information System
DECS	District Expenditure Control System
DSA	Debt Sustainability Analysis
DTCO	District Treasury Controller Office
EMIS	Education Management Information System
FCGO	Financial Comptroller General Office
FMIS	Financial Management Information System
FPR	Financial Procedure Regulations
FY	Fiscal year
GDP	Gross Domestic Product
GFS	Government Finance Statistics
HMIS	Health Management Information System
IECCD	International Economic Cooperation Division (of MoF)
ICAN	Institute of Chartered Accountants of Nepal
IFAC	International Federation of Accountants
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standard (of IFAC)
ISSAI	International Standards for Supreme Audit Institutions
IRD	Inland Revenue Department
IMF	International Monetary Fund
LMIS	Logistics Management Information System
LSGA	Local Self Governance Act
MCPM	Minimum conditions and performance measures (for local bodies)
MDA	Ministries, Departments and Agencies
MoF	Ministry of Finance
MoGA	Ministry of General Administration
MoFALD	Ministry of Federal Affairs and Local Development
MTBF	Medium-term budget framework
MTEF	Medium-term expenditure framework
NPC	National Planning Commission
NPSAS	Nepalese Public Sector Accounting Standards
NRB	Nepal Rastra Bank
OAG	Office of the Auditor General

PAC	Public Accounts Committee
PAN	Permanent Account Number
PEFA	Public Expenditure and Financial Accountability
PETS	Public Expenditure Tracking Survey
PFM	Public financial management
PPMO	Public Procurement Monitoring Office
SAI	Supreme audit institution
SNG	Subnational government
SWAp	Sector-wide approach
TSA	Treasury Single Account
UNCITRAL	United Nations Commission for International Trade and Law

Summary Assessment

Nepal has made substantial progress in deepening the structures and processes of public financial management (PFM), particularly in the use of information technology. Investment efficiency gains achieved despite the political transition period (2006-2010) when reform was not a first priority. If these improvements are linked and catalyze reforms in all phases of PFM, it would increase the chances of Nepal's graduation to middle-income status and help in reducing poverty.

A. INTEGRATED ASSESSMENT OF PFM PERFORMANCE

The objective of this assessment is to update the Public Financial Management Review published in early 2008 (Report No. 43384-NP). The assessment is expected to assist the government in (a) establishing indicator-led assessment of the country's PFM system; (b) updating fiduciary environment of the PFM systems and processes of the country; and (c) assisting in identifying those parts of the PFM system that may need further reform and development.

The commitment to change and reform to PFM systems and process by the Government of Nepal has produced results. Among 28 performance indicators (PI), 16 indicators improved, 10 indicators remained unchanged, and 2 indicators deteriorated. However, compared to 2008 with improved systems, data availability has assisted to fine-tune the assessment and downgrade the rating of an indicator to reflect the current system. The absence of the parliament during the assessment period added to the downgrading of another indicator.

The key findings in the assessment include the following:

- **Credibility.** Budget credibility is internalized; budget outturns compared to original are stable; and monitoring of budget, especially arrears, has improved with the implementation of Treasury Single Account (TSA).
- **Comprehensiveness.** Budget comprehensiveness is the hallmark of the country's PFM system driven by technology aiding systemic changes. Enforcement of financial reporting rules to autonomous bodies, state-owned enterprises, and local governments can reduce overall fiscal risks.
- **Budget formulation process.** Multi-year budget planning has assisted in maintaining sound macro fiscal aggregate. Costed sector strategies can lend to formulating a realistic procurement plan and overall improve budget implementation.
- **Budget execution.** Rules and regulations guide budget execution, but weak enforcement of these rules have impeded gains made in upstream budget process. Linking payroll to personnel records and enforcement of rules that discourage non-competitive methods of procurement can improve budget execution.
- **Accounting and reporting.** Nepal has made impressive strides in budget coverage, comparability, and its timely reporting. Weak technical capacity in the analysis of financial statements has lowered efficiency in public expenditure. Reconciliation of revenue accounts is an issue.
- **Audits.** Audit coverage and quality has improved. But, the limited scope of performance audit and weak enforcement of corrective measures against flagged irregularities has lowered meaningful behavioral changes. Performance auditing coverage and involvement of civil society in auditing performances is expected to strengthen overall performance auditing.
- **Donors.** Donors predictability of budget support, financial reporting, and greater use of national procedures has improved.

The following discussion elaborates on the main PFM findings of the performance indicators within the six critical dimensions.

(a) Credibility of the budget (PI 1-4)

At the aggregate level, the budget, both expenditure and revenue (PI-1 and 3), is credible, and credibility has become internalized. One weak spot is the composition of expenditure (PI-2). Budget variance, although declining with the return of political stability, has resulted from a combination of poor budgets (where execution require re-allocation during the year)and some budget indiscipline (evidenced by the number of votes that spend more than the authorized budgets)particularly in public investment by the Ministry of Finance (MOF). The contingency fund is not large. And because of the TSA and Financial Management Information System (FMIS), payments are more prompt and better monitored compared to the last assessment (PI-4). The implementation of activity level budget coding is expected to strengthen program budgeting, help monitor budget implementation, and reduce expenditure variances.

(b) Comprehensiveness and transparency (PI 5-10)

Budget information has become more transparent (PI-5 and 6) after the implementation of Government Finance Statistics (GFS) classification and the TSA. The public's access to fiscal reports is good (PI-10). However, the fiscal reports are not comprehensive and many autonomous government agencies and donor projects operate outside the TSA/FMIS framework (PI-7).

Fiscal relations between central government and local bodies are complex (PI-8). Even though there are allocation formulae for unconditional block grants — the major source of revenue to the local bodies — they are not being followed. The timing of grant releases, although trimester-based, is not strictly adhered to. A review of the grant system is planned.

Local bodies and public enterprises regularly submit their financial statements to the center, but their consolidation is delayed. There is no comprehensive assessment of fiscal risk to the government despite major accumulated losses in some public enterprises (PI-9).

(c) Policy-based budgeting (PI 11-12)

Fiscal prudence at the aggregate fiscal level, facilitated by a rolling medium-term expenditure framework (MTEF), is a strong feature of Nepal's PFM (PI-11). But in the absence of costed sector strategies within an aggregate fiscal framework and lack of capacity for preparing sectorial business plans, there is much room for aligning budgets more closely to development plans (PI-12). Expansionary investment plans are constrained by weak of implementation capacity, especially on the capital expenditure side. Procurement plans are not prepared as part of annual work program budgets, therefore the budgets are not realistic. Coupled with late approval of the budget and cumbersome spending procedures, little of the year's development budget is spent in the first four months, and there always is a rush to spend in the last four months. This is mitigated to some extent by flexible virement rules.

(d) Predictability and control in budget execution (PI 13-21)

The legal and process framework for determining tax liabilities is clear and minimizes discretionary power of tax officers. This is reinforced by a transparent tax appeals mechanism (PI-13). Taxpayer registration and assessments have also been improved (PI-14). However, there are issues in the accounting for assessments and collections, and tax arrears have continued to mount each year; there is insufficient attention to clearing old arrears (PI-15).

The Parliament approval of the budget, at times, may extend into the end of the first trimester of the fiscal year. Pending approval, ministry, departments, and agencies (MDA) are authorized to spend up to four months of the previous year's budget (at least for ongoing priority projects);but new programs and projects are delayed and subject to political interference outside the formal budget-approval process. Information technology has been used to reach out to stakeholders – on the revenue side to taxpayers and on the expenditure side to resource users. This has increased efficiency in tax collection and budget management. The rollouts of the TSA and FMIS to all

75 districts have provided reliable and up-to-date information on budget execution (PI-16).

The Treasury surplus over the past years has eased cash and debt management (PI-17). The payroll is still largely managed manually, and it is not linked digitally to personnel records (PI-18). Since 2007, the legal and regulatory framework for procurement has been based on international standards. Most procurement is through open and competitive bidding, but there is lack of central data for justifying non-competitive methods of procurement, and the compliance with rules (PI-19).

The developmental impact of spending has been reduced by widespread irregularities and weak-enforcement of rules. Commitment control is weak despite the existence of rules and regulations (PI-20). Internal audit is beset by conflicts of interest as internal auditors also function, from time to time, as accounts officers. The audit is not focused on internal control systems and their risks but is oriented to identifying transactional irregularities, which reduces its effectiveness (PI-21).

(e) Accounting, recording and reporting (PI 22-25)
The TSA rollout has strengthened cash-based accounting practices and transparency. Expenditure cash reports are generated, and the mid-year reporting is comprehensive, except for the omission of several autonomous government agencies and donor project accounts. Reconciliation of revenue accounts is still an issue. Progress has been made in piloting the international financial reporting standard (cash-based IPSAS) at the ministry level. But there are technical capacity issues in the recording and analysis of financial statements as the result of over-stretched account personnel and limited refresher training to update personnel on systemic and accounting standards changes (PI-24 and 25).

(f) External scrutiny and audit (PI 26-28)
The Office of Auditor General (OAG) conducts financial and regularity audits on a majority of government revenues and expenditures using INTOSAI-based standards and submits audit reports through the President within four months of submission of the financial statements. Weak enforcement of corrective measures against flagged irregularities and lack of progress on recommendations of the OAG have contributed to the weakening of PFM governance. A high-level committee is following up on this. When in session, the Public Accounts Committee (PAC) has scrutinized issues other than budget execution; this has weakened directives by the legislature to the executive to improve budget execution performance (PI-26 to 28).

B. IMPACT OF PFM WEAKNESSES ON BUDGET OUTCOMES

Aggregate fiscal discipline. On aggregate, revenue and expenditure budgets are realized, but the composition of actual spending varies significantly from the budget, and in some cases ministries are allowed to overspend. Debt levels are reasonable and well monitored. However, fiscal risk appears high from parts of the public sector that are not within the TSA, particularly the public enterprises. There is no regular assessment either explicit or implicit of operating deficits, liabilities, and contingent liabilities.

Tax arrears arise where assessments are made but are in dispute or not paid for other reasons. This reduces certainty of taxes: the lack of follow-up and resolution of arrears puts the whole tax system into question.

Strategic allocation of resources. High variances at the project, program, and departmental levels indicate that the planned resource allocations are not being implemented most efficiently. Disorderly execution is compounded by weak project management: projects are admitted into the budget without technical analysis of their feasibility, and contracts are not adequately monitored. The omission of several autonomous government agencies and donor-funded projects from the overall fiscal picture means that resource allocations are segmented and are not optimal overall. Local body revenues and expenditures are also not integrated.

Efficient service delivery. Efficient service delivery is possible when delivery units have lead time for planning and there is assurance that planned procurement commitments can be made in accordance with program/project requirements. At present, there is no real link between budgeting, procurement planning, and authorization of spending, which lowers investment efficiency.

The splitting of large contracts into smaller lots reduces the opportunity for economies of scale. Value for money is also reduced by long and complex administrative procedures, and this is not factored in the cost of delay.

C. CHANGE IN PERFORMANCE

This is a report on the second Public Expenditure and Financial Accountability (PEFA) assessment of Nepal. The focus of the report is therefore on identifying changes in performance that have occurred in financial management of central government since 2008 when the previous PEFA assessment was done. Tables 1 and 2 summarize these changes.

TABLE 1: Summary of PEFA Rating

PFM Performance Indicators		2008	2014	Scoring method	Comparable ratings	Change since 2008
A: PFM OUT-TURNS I: Credibility of the Budget						
PI-1	Aggregate expenditure out-turn compared to original approved budget	B	A	M1	Yes	Variances reduced.
PI-2	Composition of expenditure out-turns compared to original approved budget.	C	C+ C A	M1	Changed methodology	No direct comparability.
PI-3	Aggregate revenue out-turns compared to original approved budget.	A	A	M1	Changed methodology	Performance unchanged
PI-4	Stock and monitoring of expenditure payment arrears.	D+ C D	B+ A B	M1	Yes	Stock of arrears below 2% and system in place to generate arrears data.
B: KEY CROSS-CUTTING ISSUES II. Comprehensiveness and Transparency						
PI-5	Classification of the budget	C	A	M1	Yes	Expanded budget classifications - comprehensive
PI-6	Comprehensiveness of information included in the budget documentation	B	A	M1	Yes	Performance improvement regard to information benchmark 3: deficit financing, describing anticipated debt composition.
PI-7	Extent of unreported government operations	C	D+ D C	M1	Yes	Higher proportion of extra budgetary operations than before
PI-8	Transparency of inter-governmental Fiscal Relations	C C C C	C+ C C B	M2	Yes	Subnational government's fiscal data reporting strengthened
PI-9	Oversight of aggregate fiscal risk from other public sector entities	D+ C D	C C C	M1	Yes	Performance improves regard to benchmark 2: subnational net fiscal position monitored and audited.
PI-10	Public access to key fiscal information	B	A	M1	Yes	Performance of benchmark 4 improved: Reports on central government consolidated are made public within six months of completed audits.
C: BUDGET CYCLE III. Policy-Based Budgeting						
PI-11	Orderliness and participation in the annual budget process	C+ B B D	A A A NA	M2	Yes	Issuance and adherence of budget discussion as per budget calendar.

PFM Performance Indicators		2008	2014	Scoring method	Comparable ratings	Change since 2008
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting	C+ B C C C	B B A C C	M2	Yes	Debt Sustainability Analysis conducted annually.
IV. PREDICATABILITY &CONTROL in BUDGET EXECUTION						
PI-13	Transparency of taxpayer obligations and liabilities	C+ C C B	A A A B	M2	Yes	Performance improved on the following: a) Tax obligation is clear and discretionary power limited; b) Taxpayer's access to information is comprehensive, clear and expanded.
PI-14	Effectiveness of measures for taxpayer registration and tax assessment.	C C C C	A B A A	M2	Yes	Overall improvement in taxpayer registration and tax assessment.
PI-15	Effectiveness in collection of tax payments	D+ D B D	D+ D B D	M1	Yes	Performance unchanged
PI-16	Predictability in the availability of funds for commitment of expenditures.	C+ C B C	C+ C B C	M1	Yes	Improvement on cash flow forecast, information to MDAs on expenditure ceilings and transparency of adjustment to budget allocations.
PI-17	Recoding and management of cash balances, debt and guarantees	C+ C B C	C+ C B C	M2	Yes	Performance unchanged
PI-18	Effectiveness of payroll controls	C+ C B C B	C+ C B C C	M2	Yes	Performance unchanged.
PI-19	Competition, value for money and controls in procurement	C C C C	B B D C A	M2	New dimensions, cannot be compared	Use of open competition, operation of independent administrative procurement compliant system.
PI-20	Effectiveness of internal controls for non-salary expenditures.	C C C C	C C C C	M1	Yes	Performance unchanged.
PI-21	Effectiveness of internal audit	D+ D C D	D+ D C D	M1	Yes	Performance unchanged.
V: Accounting, Recording and Reporting						
PI-22	Timeliness and regularity of accounts reconciliation	C+ B C	C+ (i) C (ii) B	M2	Yes	Reconciliation issues on the revenue accounts.
PI-23	Availability of information on resources received by service delivery units	C	A	M1	Yes	Improvement on resources made available to service delivery units incl. completion of PET survey.
PI-24	Quality and timeliness of in-year budget reports	C+ C A C	C+ C A B	M1	Yes	System able to show direct comparison between original budget and expenditure and there is no material difference in data accuracy. However, the system is unable to depict commitments on a monthly basis.

PFM Performance Indicators		2008	2014	Scoring method	Comparable ratings	Change since 2008
PI-25	Quality and timeliness if annual financial statements	C+ C A C	C+ C A C	M1	Yes	Performance unchanged
VI. External Scrutiny and Audit						
PI-26	Scope, nature and follow-up of external audit	D+ B D C	C+ B C C	M1	Yes	Audit coverage expanded and timely submission of audit reports
PI-27	Legislative scrutiny of annual budget law	D+ C D D B	D D NA NA NA	M1	Yes	No parliament
PI-28	Legislative scrutiny of external audit reports	D D C C	D D NA NA	M1	Yes	No parliament
D. Donor Practices						
D-1	Predictability of Direct Budget Support	D D D	D+ D A	M1	Yes	Improvement in timeliness of donor disbursements
D-2	Financial information provided by donors for budgeting and reporting on project and program aid	D D D	C+ B C	M1	Yes	Improvement in donor information on project support
D-3	Proportion of aid that is managed by use of national procedures.	D	C	M1	Yes	Greater use of national procedures

TABLE 2: Summary of Changes in Indicator Ratings since 2007 Assessment

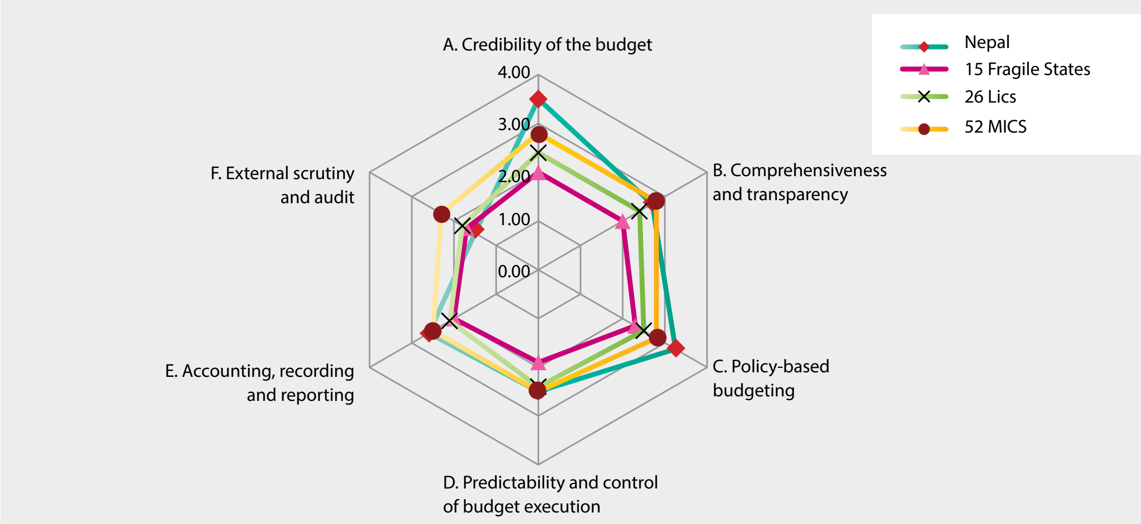
Change in Ratings	Number of Indicators	% Indicators
Upwards	19	61
Downwards	2	7
Remained the same	10	32
TOTAL	31	100

D. INTERNATIONAL COMPARISON OF THE PEFA RATINGS

A comparison with other countries shows that the Nepal PFM system is relatively strong. Figure 1 shows that Nepal's PEFA ratings are better than the average of 15 fragile states and 27 low-income countries (LICs) (except for the external scrutiny and audit where it is somewhat lower). Further, compared to the average of 51 middle-income countries (MICs), the Nepal PFM system rating is better or equal on four dimensions, and rating is lower on two (external scrutiny and audit and comprehensiveness and transparency).[1] In addition, Figure 2 shows that as the average rating for all of the Nepal PEFA indicators increased from 2008 to 2014 (numerical rating increased from 2.2 to 2.7), the performance of Nepal's PFM system improved relative to other countries over this timeframe.

[1] The assessment data were quantified using the following conversion for each Performance Indicator (PI): A = 4, B+ = 3.5, B = 3, C+ = 2.5 C = 2, D+ = 1.5 and D = 1. This is based on first calculating the dimension-level average for each country, and thereafter the average for each dimension for each country group.

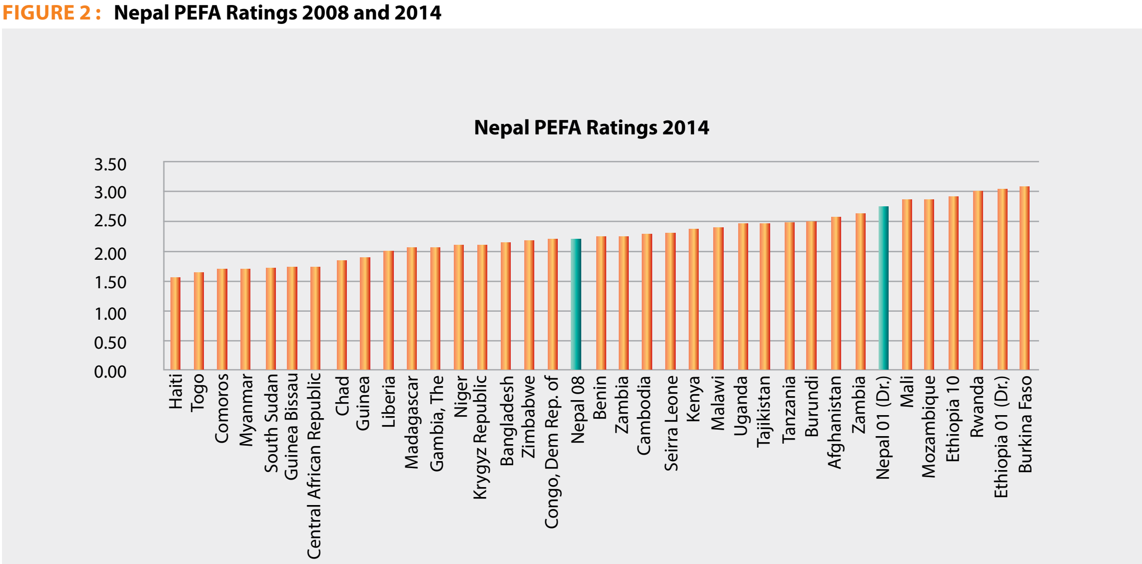
FIGURE1 : International Comparison of PEFA Ratings



Country	Credibility of budget	Comprehen-siveness and transparency	Policy-based budgeting	Predictability and control of budget execution	Accounting, recording and reporting	External scrutiny and audit
Nepal	3.5	2.7	3.25	2.5	2.6	1.5
15 fragile states	2.0	2.0	2.3	1.9	2.0	1.7
26 LICs	2.4	2.4	2.5	2.4	2.1	1.8
52 MICs	2.8	2.8	2.8	2.5	2.5	2.3

Source: Ratings for international comparisons reported in Afghanistan PEFA, August 2013, p. 10.

FIGURE 2 : Nepal PEFA Ratings 2008 and 2014



1.

Introduction

1.1 OBJECTIVE

The objective of this assessment is to update the Public Expenditure and Financial Management (PEFA) assessment published in early 2008 (Report No. 43384-NP). The assessment is expected to assist the Government of Nepal to (a) establish indicator-led assessment of the country's PFM system,(b) update the fiduciary environment of the PFM systems and processes of the country, and (c) assist in identifying those parts of the PFM system that may need further reform and development.

The specific objectives of this assessment are to:

- Update the overview of PFM performance in accordance with the PEFA Performance Management Framework;
- Establish and explain the level of performance against PEFA 2008 ratings;
- Prepare PFM progress report that would feed into government and donor dialogue on PFM reform in the short, medium and long term, including (i) identifying possible short-term interventions to assist in improving the processes and (ii) identifying priority PFM reform areas that can be developed to improve the management and control of resource use (tax and aid) within a medium- to long-term period.

1.2 COMPOSITION OF TEAM AND ROLES OF STAKEHOLDERS

This assessment was undertaken in full ownership and participation of the Government of Nepal. The institutional and organizational approach taken by the Government of Nepal ensured coordination among various government institutions. The assessment was led by the Ministry of Finance (MoF) and coordinated by PEFA Secretariat (Nepal) and guided by the process developed by the PEFA Secretariat based in Washington, D.C. This PEFA assessment was guided by the successful partnership arrangement for the first assessment in 2008 when the World Bank had worked in close partnership with the government-led team. The government team vetted the assessment of individual indicators.

The Government's high-level PFM Steering Committee, chaired by the Finance Secretary, provided policy guidance for the assessment. The Steering Committee guided and approved the assessment content and specific indicator ratings. A working committee of Joint Secretaries from selected ministries provided additional guidance and specific comments on the assessment report and proposed rating. The working committee was chaired by the PEFA Secretariat (Nepal) Coordinator and co-chaired by the Chief of the Budget and Program Division (MoF). The member secretary of the PEFA Secretariat (Nepal) was also member secretary to the working committee. The PEFA Secretariat (Nepal) coordinated the work of assessment leaders in six core dimensions compromising nine teams. The lead focal persons of the six core dimensions were also on the working committee. The lead focal person was responsible for delivering the assessment reports under the core pillars. Nepal's development partners (ADB, EU, DfID, and IMF) actively participated at various stages of the assessment and peer reviewed the project concept note and advised the Bank team at thematic PFM donor meetings. Each assessment team had five to eight members based on comprehensiveness of the indicators.

1.3 PEFA ASSESSMENT PROCESS

The Government's responsibility was assigned to PEFA Secretariat (Nepal) by establishing the Steering Committee. The assessment was launched at an inaugural session attended by government task teams and World Bank representative. At the inaugural session, the government team and the Bank discussed issues pertaining to the PEFA Framework and the working methodology to be adopted. This helped to enhance the understanding of the processes and to mutually agree up-front on the potential outcomes of the assessments. Subsequently, series of training workshops on the PEFA assessment were organized for the assessment teams.

The working committee compiled the PEFA high-level performance indicator set (Annex 2 of the concept note) together with any applicable supporting documentation and analyses. An inventory of existing materials was prepared, with the starting data and documents available from previous and ongoing assessments.

The task team supported and followed up with fieldwork, where required, to collect missing information, with special focus on shortcomings in institutional arrangements, systems, and processes in the PFM cycle. The assessment included collection of additional documentation, including meeting minutes, and interviews with government counterpart teams and main stakeholders. Thereafter, the team prepared a Draft Performance Report in May 2014, a rapid assessment in accordance with the PEFA PFM Performance Measurement Framework guidelines. The team highlighted reform areas under each indicator. The report was updated and refined following advice from a World Bank team. A specialist in the use of PEFA methodology assisted in the later drafts and visited Nepal in August 17-20, 2014. A fourth draft was prepared from additional inputs and evidence provided by the working committee and was distributed to all stakeholders on August 11, 2014. Meetings were held with the PEFA Secretariat at the Financial Comptroller General Office (FCGO) and with the MoF Budget Division. This final draft of the report addresses all the comments received up to November 31, 2014.

1.4 SCOPE OF THE ASSESSMENT

The report covers the central government, as defined in IMF-GFS, which includes autonomous government agencies at central level (see indicator PI-7), but not public enterprises and local governments except insofar as they may be a source of fiscal risk to the Government of Nepal (PI-9). This is the same coverage as required by the PEFA framework for central government (Blue Book) and includes all 31 indicators covering all phases of public financial management as prescribed in the PEFA Framework.

1.5 REFORM SUGGESTIONS

Respective teams were encouraged to list suggested reform activities against all indicators. These are listed in Annex 2. These suggested reforms are the starting point toward finalization of PFM reform activities, post finalization of this assessment.

1.6 QUALITY ASSURANCE

The involvement of multiple stakeholders helped to assure quality of the assessment as did the review of the concept note by major development partners including the PEFA Secretariat in Washington. The findings of the assessment were shared with the donors in September 2014 and their comments assisted the finalization of the draft report. The World Bank also provided continuous quality control support.

2.

Country background information

2.1 ECONOMIC GROWTH

The economy grew by 5.2 percent in FY14 compared to 3.5 percent in FY13 and 4.6 percent in FY12. This was possible despite the lackluster industrial growth (2.7 percent in FY14 compared to 2.5 percent in FY13 and 3 percent in FY12) as private actors held back investment owing to political uncertainty and poor investment climate, including frequent labor problems. The government estimated GDP growth at 5.2 percent in FY14.The GDP growth was due mostly to (a) good agriculture sector performance (4.7 percent in FY14 compared to 1.1 percent growth in FY13) owing to a good monsoon and timely supply of inputs during the plantation season and (b) strong services sector performance (6.1 percent in FY14 compared to 5.2 percent in FY13 with some linkages to growth in remittance transfers.

Inflation. Inflation stood at 9.1 percent against the government target of 8 percent. The continued increase in food prices (11.6 percent in FY14 compared to 9.7 percent in FY13) kept inflation high despite a slower rise in non-food prices (6.8 percent in FY14 compared to 10.1 percent in FY13). Food prices remained inexplicably high despite a bumper harvest both in Nepal and India.

Fiscal outturn. Timely adoption of the budget saw a growth in government expenditure, but the quality of the expenditure remained questionable with 46 percent of the expenses bunched in the last trimester and 21 percent of the expenditure spent in the last month of the fiscal year. In FY13, owing to significant delays adopting a full-fledged budget, Nepal experienced a (real) fiscal contraction with solid revenue growth far outstripping the Government's ability to invest.

Revenue collection remained strong. Tax and non-tax revenues reached 18.38 percent of GDP as compared to 17.60 percent in FY13 and 16 percent in FY12. On the expenditure side, government expenses grew after falling down to 21.19 percent of GDP in FY13 relative to 22.21 percent of GDP in FY12. Government expenditure reached 23.33 percent of GDP (including financing) with only 3.31 percent going to capital formation.

2.2 CHALLENGES/PRIORITY AREAS

Developing a growth promotion vision/agenda. Nepal aspires to graduate to "developing country" status by 2022.The authorities have not articulated the development to underpin this outcome nor have they identified policies and reforms that are needed to attain the goal.

Resolving Nepal's 'fiscal paradox'. Nepal is the only country in South Asia to record a budget surplus (helped by buoyant revenue growth). Its level of indebtedness is modest and it is flush with liquidity (thanks to large remittance inflows); yet it struggles to maintain investment even at existing low levels.

Boosting investment. Faster and sustained economic growth will not be possible without higher levels of investment, but Nepal's model of growth appears premised on remittance-financed consumption.

2.3 PFM INSTITUTIONS

Major responsibility for the management of the public finance in Nepal rests by law with the Parliament, Ministry of Finance, the National Planning Commission (NPC), the Public Procurement Monitoring Office (PPMO), and the Financial Comptroller General Office. Annex A provides more details on structures of these and other public finance institutions.

2. Country background information

Nepal is a federal republic with a multi-party polity. The President is the head of state and the Prime Minister is the head of Government. Both are elected by the Parliament. The most recent election, held in November 2013, elected 240 representatives through the first-past-the-post system and 335 representatives through proportional representation. The elected Constituent Assembly is also the legislative body.

Structure of Nepal's public sector. Nepal's public sector functions at three levels: central, district and local. For administrative purposes the 75 districts are grouped in 14 zones and 5 development regions. Nepal has 3,754 village development committees and 99 municipalities. Each of the 75 districts has a district development committee. The Local Self Governance Act (LSGA) declares as "local bodies" all district development committees, village development committees, and municipalities with their own legal personality, rules and regulations, and elected political leadership. However, as there has been no local election since the local councils were dissolved in 2002, these entities have been run by civil servants assigned by the central government. For this PEFA assessment, these local bodies are considered as sub-national governments rather than de-concentrated central government units. Fiscal relations between the local bodies and central government are described under PI-8in part 3, Assessment of PFM Systems, Processes, and Institutions].

Ministries with nationwide operations have their own district offices, and these are counted as de-concentrated units. Their revenues and expenditures are included in the central budget and accounts while that of local bodies are separate from the central budget and accounts.

According to a 2013 OAG report there are 3,744 public offices (including the Supreme Court, executive, legislature, constitutional bodies, Nepal army, armed police force, Nepal police, courts, and MDAs), 92 corporate bodies, and 808 boards and other institutions. Table 8 shows the approximate structure and expenditure of the Government of Nepal.

National Planning Commission. The Prime Minister chairs the National Planning Commission and a Vice-chair appointed by the government leads its day-to-day affairs. The NPC functions include the following:

- Formulate development policies and prepare periodic development plans within the framework of a long-term development perspective;
- Explore internal and external resources and indigenous and foreign technology and make recommendations to the Government;
- Explore innovative approaches for sustainable development;
- Formulate annual programs and assist the Government in implementation;
- Provide guidelines, advice, and suggestions to sectorial MDAs and local bodies and assist them in plan and project formulation;

TABLE 3 : Structure of General Government July 2013

	Number of units	NR millions			% of total
		Expenditure	Transfers from central government	Net expenditure	
Central government ministries, incl. de-concentrated offices	45	302,054	23,300*	270,054	68.0
Autonomous government agencies (estimate)	1,460	95.000		95,000	23.9
District development committees	75				
Municipalities	58	32,000		32,000	8.1
Village development committees	3,915				
TOTAL	**5,553**			**397,054**	**100.0**

Sources: Budget Speech and Annexes 13 July 2014, and World Bank estimates. Note: The number of VDC and Municipalities is of pre changes. The latest count is in the text section.

* Parts of the grants to social service (code 26400, NR 79,190m) are to Autonomous government agencies. This should be deducted as well as the 23,300m to local bodies, but could not be identified. The total therefore includes some double counting.

- Advise Government on institutional development of M&E systems to monitor program and project implementation according to plan targets and outlay, and carry out impact evaluations;
- Provide guidelines for data collection and carry out action research necessary for the evaluation of new policies and for the refinement of the planning process;
- Provide guidelines on policy targets and priorities regarding annual budget formulation to the Ministry of Finance and all line ministries before issuing the budget formulation circular;
- Formulate a policy framework for approval of district-level projects by ministerial secretaries;
- Approve central-level projects;
- Set annual targets for development programs by December of each year; and
- Advise government offices on accepting any kind of aid (kind or cash) and aid agreements.

Financial Comptroller General Office. Major responsibilities of the FCGO is treasury management. The FCGO oversees all government expenditures against the budget, centrally records revenue collection and other receipts, and prepares consolidated financial statements. Its functions cover conducting internal audit of revenue and expenditures. Another important responsibility is to ensure timely repayment of internal and external debts, investing in loans and equity of public enterprises, and maintaining records of these financial transactions. It also manages pension distribution to retired government employees.

The FCGO has 4 divisions and 14 sections. Its field offices are spread across all 75 districts of the country. In each district there is a District Treasury Controller Office (DTCO) that is involved in releasing budgets to government offices, budgetary controls, and reporting. One office under FCGO manages pensions of retired civil servants. The Government Dues Recovery Office is responsible for recoveries.

Public Procurement Monitoring Office. The main PPMO functions are to prepare a public procurement policy and recommend implementation measures to the Government. The office also coordinates procurement, including debarment proceedings, and supports capacity building through professional development plans and training for public officials and bidders. It also plans and coordinates technical assistance on public procurement and functions as the secretariat of the Procurement Review Committee. The PPMO reports to the Government annually. It also monitors public procurement through site visits and documents. Other functions include:

- Developing indicators for continuous monitoring of the public procurement proceedings;
- Advising on public procurement;
- Establishing and maintaining websites dedicated to public procurement management;
- Developing and issuing standard bidding documents for civil works, goods, and consultancy; and
- Issuing manuals, directives, instructions, and technical notes for public procurement.

MINISTRY OF FINANCE

International Economic Cooperation Division (IECCD), Ministry of Finance is responsible for mobilization and optimal use of resources through foreign aid for accomplishing the development goals of reducing poverty reduction and realizing sustainable, high-economic growth.

Economic Policy Analysis Division is charged with analyzing economic trends and issues like government expenditure, revenue mobilization, budgetary deficit, internal and external debt, price and inflation, and monetary and foreign exchange policy. Its responsibilities also include conducting studies for taking actions for attaining sustainable economic growth and stability in line with the changing global context. It also conducts market analysis, monitors prices, adopts measures for maintaining price stability, and works to prevent money laundering.

Budget and Program Division helps in implementing government fiscal policies by preparing public expenditure plans needed for attaining sustainable and pro-poor growth facilitated by stable, prudent, and sustainable macroeconomic environment.

Monitoring and Evaluation Division is responsible for enhancing good performance practice against standards through quality control, and productivity gained from efficient use of resources for enhancing the revenue base.

Financial Sector Management Division improves, coordinates, monitors, develops, and expands the banking and the financial sector.

Revenue Management Division is mainly responsible for formulating revenue policy and guidelines, carrying out revenue forecasting, and implementing policies.

PEFA Secretariat (Nepal) was established in 2009 to coordinate PFM reform activities. The Finance Secretary is the chair of the Steering Committee, which provides overall policy and reform guidance. A Working Committee with representatives from all PFM-related institutions executes the reforms. The Secretariat has also been assigned the role of coordinating this PEFA assessment.

Public enterprises and autonomous government agencies. Nepal has 37 public enterprises that report annually to Ministry of Finance. The OAG lists another 808 parastatals (autonomous government agencies, boards, and committees) in Nepal but does not distinguish between commercial and non-commercial or between public enterprises and autonomous government agencies. These bodies report to their parent ministries and are subject to audit by the OAG. The World Bank made an analysis of all parastatals in 2013, classifying them according to IMF-GFS. There appear to be at least 1,372 non-commercial entities that are part of central government according to GFS criteria [see text under PI-7 (i) in part 3, Assessment of PFM Systems, Processes, and Institutions].

3.

Assessment of the PFM systems, processes, and institutions

3.1 BUDGET CREDIBILITY (PI-1-4)

Effectiveness of public financial management is measured by how the Government implements its policies and plans with regard to its budget. The credibility of the budget is determined by how close the intention (planned, expenditure, and revenue) is with actual use of resources and expenditures. Four indicators measure the budget credibility based on planned versus actual status of implementation.

PI-1: AGGREGATE EXPENDITURE OUTTURNS COMPARED TO ORIGINAL APPROVED BUDGET

The government's ability to implement the budget is important for delivering the intended public services as expressed in policy, and for ensuring the planned outputs. This indicator measures the government's ability to spend budgeted expenditures by comparing actual expenditure outturn with primary budgeted expenditure.[2]

Scoring method: M1

Assessing dimension PI-1: The difference between actual primary expenditure and the originally budgeted primary expenditure.

Rating PI-1: A. In no more than one year in the last three years has the actual expenditure deviated by an amount equivalent to more than 5 percent of budgeted expenditure

Justification of rating

In the three fiscal years under review, the actual expenditure went above the threshold of 5 percent only once in FY13. The deviation was 5.9 percent while the deviations for FY12 and FY11 were at 1.9 percent and 4.05 percent, respectively (Table 3.1, and more details in Annex B). A tighter and implementable budget size (guided by realistic budget formulation guidelines)and the mid-year budget review, which steered budget execution for remaining period of the fiscal year using data generated by the Treasury Single Account (TSA), strengthened budget formulation and use processes. These new processes supported by data are marked improvements compared to the first PEFA assessment.

TABLE 3.1 : Budget Outturn

	NRs billions		
	FY2011	FY2012	FY2013
Original budgeted total primary expenditure	213.93	229.27	291.54
Actual expenditure	205.26	233.67	274.19
Difference between actual and original budgeted primary expenditure	8.66	-4.40	17.35
Difference as percent of original budgeted primary expenditure	4.05%	1.92%	5.95%

Source; Financial Comptroller General Office.

PI-1 Summary

Indicator	Evidence used	Rating	Framework requirement	Information sources	Rating in 2008	Explanation of change, since 2008
PI-1	Percentage of actual expenditure to budgeted expenditure for last three fiscal years.	A	In no more than one year, over last three years, did actual expenditure deviate by an amount more than 5% of budgeted expenditure	Annual reports of FCGO	B	Budget preparation process has been strengthened through budget guidelines and budget preparation manuals; data generated from TSA guideline budget preparation and mid-year budget review; virement from surplus heads to high burn-rate heads are based on data generated by TSA while contingency funds are tied for intended activities

2 Primary expenditure is defined as total expenditure net of debt services and donor-funded expenditure.

PI-2: THE COMPOSITION OF EXPENDITURE OUTTURN COMPARED TO ORIGINAL APPROVED BUDGET.

Execution of the policy intent is firmer when there is minimum change at the budget execution level as compared to original budget. Minimum changes during the execution stage from original budget, at the administrative level, confirm policy intent execution with minimum variance in expenditure compositions. This is measured through two dimensions: (i) the extent to which reallocations between budget heads during the execution have contributed to variance in expenditure composition, and (ii) size of contingency budget and level of actual expenditure charged to the budget head. The second dimension recognizes that it is prudent to include an amount to allow for unforeseen events as a contingency reserve. Yet, such a reserve should not be so large as to undermine the overall budget credibility.

Scoring method PI-2: M1
Rating PI-2: C+

***Assessed dimension (i):* Extent of the variance in expenditure composition during the three years, excluding contingency items.**
***Rating dimension (i):*C.** Variance in expenditure composition exceeded 15 percent in no more than one of the last three years

Justification of Rating:
The variances in the composition of expenditure at the MDAs for the review period (FY11-FY13) compared to the expenditure[3] were 11.8 percent in FY11; 16.7 percent in FY12, and 5.3 percent in FY13 (more details in Annex B).

In FY13, of five large spending MDAs (46 percent of the total budget), the composite variance was 4.4 percent and overall variance only 8.3 percent. Variance signals the remaking of the budget during the implementation phase, but the variance has been brought under control recently with closer monitoring of implementation by budget managers, assisted by on-line data (Table 3.2).

Under the current practice, appropriation under policy financing and miscellaneous is held by the Ministry of Finance (MoF), which is then subsequently transferred to appropriate ministry in the course of activity implementation. This is the case for public investment (loans and shares) in large energy, irrigation, and drinking water projects. This has led to large variances under the code MoF – Public Enterprises (see Annex B).

Table 3.2 : Five Largest Ministries

Data for year = 2013	Five Largest Ministries Rs. Billion					
Administrative or functional head	**Budget**	**Actual**	**Adjusted budget**	**Deviation**	**Absolute deviation**	**Percent**
Ministry of Education	45.9	46.0	44.7	1.2	1.2	2.7
Ministry of Local Development	24.6	25.3	24.0	1.3	1.3	5.4
Ministry of Home Affairs	23.5	23.7	22.9	0.8	0.8	3.6
Ministry of Defence	21.4	21.1	20.9	0.2	0.2	1.0
Ministry of Physical Planning and Construction	22.3	19.4	21.7	(2.3)	2.3	10.7
Allocated expenditure	137.8	135.5	134.3	1.2	5.9	
Contingency	12.3	2.0				
Total expenditure	150.1	137.5				
Overall (PI-1) variance						8.3
Composition (PI-2) variance						4.4
Contingency share of budget						1.4

[3] Adjusted for the aggregate deviation.

***Assessed dimension (ii):* The average amount of expenditure actually charged to the contingency vote over the last three years.**
Rating for dimension (ii): A. Actual expenditure charged to the contingency vote was on average less than 3 percent of the original budget

Justification of rating:
The total contingency budget (current and capital) as a share of budget is low. While the current contingency fund is for non-budgeted expenditure (natural emergencies, executive decisions, and others), capital contingency budget is appropriated for projects that were unable to complete negotiations within the budget preparation cut-off date. Both these accounts are under Mo jurisdiction and have clear guidelines on the use of these funds. The budgeted allocation to the contingency fund during the last three years averaged 0.25 percent of the total budget, but little expenditure was charged against the contingency budget. The use of the budget was mainly confined to virement to ministries, where actual expenditure was charged in accordance with good practice.

Table 3.3: Share of contingency fund use in total budget

S. N.	Fiscal Year	Percentage	Average
1.	2011	O	
2.	2012	0.04	0.25%
3.	2013	0.7	

The relatively high use of the contingency budget in 2012/13 was on account of second Constituent Assembly election and in anticipation of plausible government restructuring.

The improvement in appropriation and use of the contingency budget is the result of following measures: (a) budget can only be allocated under the contingency head by clearly stating the purpose; (b) past budget implementation information anchors budget planning and formulation alongside the aim to optimize the use of resources on the ground; and (c) mid-year budget review process for redirecting resources and/or freezing resources allocated for unjustifiable activities.

PI-2 Summary						
Indicator	**Evidence**	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change, since 2008**
PI-2		C+				
PI-2(i)	Variance in FY11 was 11.8%, in FY12was16.7%, and in FY13 was 5.3%.	C	In three assessed FYs, only FY12 was the composition of variance above 15%	Annual report of FCGO	C	Methodology change
PI-2(ii)	Actual expenditure to the contingency budget was 0.25% on an average for three years.	A	Actual expenditure charged to contingency budget was on average less than 3% of original budget	Annual report of FCGO	NA	Methodology change

PI-3: DIFFERENCE BETWEEN ESTIMATED REVENUE IN APPROVED BUDGET AND ACTUAL REVENUE OUTTURN

Revenue accuracy lends to budget credibility to the extent that resources users are assured of funds from the treasury as negotiated. This assessment compares deviation of revenue from forecast to collection.

Scoring method: M1
Assessed PI-3: **Actual domestic revenue collection compared to domestic revenue in the original, approved budget.**
Rating PI-3: A. Actual domestic revenue was between 97 percent and 106 percent of budgeted domestic revenue in at least two of the last three years

Justification for Rating

The Budget and Resource Committee—Vice-Chair of National Planning Commission, Governor of the Nepal Rastra Bank (NRB), and MoF Secretary—prepares and provides the ceiling of the estimated resource (revenue and aid) availability and its use (budget expenditure) for any given fiscal year, thereby initiating the process of annual budget formulation process six months before the new fiscal year begins.

Table 3.4 : Revenue collection versus budget target

Fiscal Year	NPR billion		%
	Budget estimates	Collection	
2011	216.644	198.376	92
2012	241.77	244.374	101
2013	289.605	296.021	102

Only in one year of the three fiscal years, was revenue collection below 97 percent of the target (Table 3.4). In FY11, revenue collection was 92 percent of target. Annual remittance inflow of 25 percent of GDP has fueled consumption. This has not only contributed to the economy's growth through the consumption route but has also resulted in robust revenue collections. Revenue collection, as a percentage of the budget target was 101 percent in FY12 and 102 percent in FY13 as a result of administrative reforms in taxation.

Table 3.5 : Selected major taxes

FY2011	NPR billion		
	FY2011	FY2012	FY2013
Tax revenue	**172.8**	**211.7**	**259.2**
Income Tax	42.1	52.9	66.1
Taxes on Property	6.6	3.6	5.3
Consumption tax	88.4	110.6	129.3
Trade Tax	35.7	44.7	58.5
Non-Tax revenue	**25.6**	**32.7**	**36.8**
Charges	10.2	0.3	0.3
Sales of services	1.6	6.9	11.2
Dividends	8.6	9.4	10.8
Others	5.2	16.1	14.5

PI-3 Summary					Score in 2007	Explanation of changes, since 2007
Indicator	**Evidence**	**Score**	**Framework requirement**	**Information Sources**		
PI-3	The actual domestic revenue collection compared to revenue estimates in FYs 2011, 2012 and 2013 are respectively 92%, 101% and 102% of revenue target.	A	Actual domestic revenue collection was between 97% and 106% of budgeted domestic revenue in at least two of the last three years.	Annual Economic Statement published by the Office of Comptroller General	A	Tax administrative reforms' impact on tax collection backed by conspicuous consumption fueled by remittance inflow.

PI-4: STOCK AND MONITORING OF EXPENDITURE PAYMENT ARREARS

The indicators assess the size and the system that tracks expenditure arrears. High level of arrears denotes inadequate commitment controls, cash rationing, inadequate budgeting for contracts, lack of information, etc. that not only lowers the credibility of the budget but can also lead to lower accountability of money use. There are 2 dimensions to this indicator

Scoring method: M1
RatingPI-4: B+

> ***Assessed dimension (i): Stock of expenditure payment arrears (as a percentage of actual total expenditure) and any recent change in the stock.***
> ***Rating:* A.** The stock of arrears is low (i.e., is below 2 percent of total expenditure)

Justification of the Rating

'Arrears' in Nepal means liabilities for goods/services received or work done for which invoices have been received but have not yet been paid. They are counted as arrears even though the invoice may not be immediately payable. According to FCGO, there are arrears on goods and services and work done, including salary arrears, but no arrears in debt service. The rule is that bills should be paid within 30 days of receipt. Financial Procedure Rules 2064 has specific guidelines in recording arrears and Rule 40 (7) states:

No liability shall be created in a manner to incur expenditure beyond the budget limit for the current year. However, in exceptional circumstances, when expenditure incurred is above appropriated budget, the amount due and payable shall be entered in the statement of due amount, setting out the reason for making payment of the amount as per the bill and voucher for the coming year, and get it certified by the Office In-charge and the District Treasury Comptroller Office (DTCO) within the 15th day of the month of Shrawan (last day of end of fiscal year, usually 15th of July).

This statement of arrears is to be forwarded with the financial statement to the pertinent supervisory office, concerned ministry, DTCO, and OAG. There is no age analysis of arrears.

There is legal and process clarity and guidance to discourage expenditure payment arrears/ liabilities for the next fiscal year. Such expenditure can only be paid if the money authorized for the current fiscal year is sufficient. Capital expenditure arrears are to be incorporated into the annual program of the next fiscal year and must be approved by the concerned ministry and the National Planning Commission.

The stock of expenditure payment arrears was below 0.5 percent of expenditure in the last two years (FY12, 0.31 percent of total expenditure; and FY13, 0.15 percent of the total expenditure).

Table 3.6: Arrears in FY 12 and 13

Fiscal Year	Budget head	Amount (Million NPR)	Arrears (Million NPR)	(%)
2011/12	Recurrent	243,460	665.7	0.27
	Capital	51,390	257.5	0.50
	Total	294,850	923.2	0.31
2012/13	Recurrent	247,456	170.2	0.07
	Capital	54,598	287.1	0.52
	Total	302,054	457.3	0.15

Source: FCGO – FMIS Arrears reporting module.
Note: Consolidated Financial Statements for FY12/13 Executive Summary, para.11, Table 13 is headed "Outstanding Advances and Arrears" but should be headed "Outstanding Advances and Irregularities", nothing to do with expenditure arrears.

Assessed dimension (ii): Availability of data for monitoring the stock of expenditure payment arrears.
Rating: B. Data on stock of arrears is generated annually but may not be complete for a few identified expenditure categories or specified budget institutions

Justification of the Rating

Enforcement of Form 18 (arrears form) initiates the recording of payment outstanding at transaction level. Thereafter, the District Expenditure Control System (DECS) records expenditure payment arrears. With the implementation of TSA, outstanding consolidated payment arrears is generated automatically, which is then verified for material inconsistency. Both internal and external audits certify the scale and level of outstanding arrears. The OAG report in 2012/13 does not mention expenditure arrears as an issue. Table 3.7 shows a DECS-generated arrears record for FY13 detailing the name of district, ministry, by charts of accounts and total. These reports are then automatically compiled into consolidated arrear report and then submitted to OAG. There is no evidence of age profiling of the arrears.

Table 3.7: DECS-generated arrears record for FY13

Government of Nepal	
Ministry of Finance	
Financial Comptroller General Office	
Expenditure Payment Due	
Fiscal Year 2012/13	
District/Ministry/Office/Budget Sub-head/ Expenditure Line-item	***Expenditure Payment Due***
01 Taplejung	
314 Ministry of Home Affairs	
01-314--01 District Administration Office	
3140163 District Administration Offices	
21111 Salary	177,087.00
Total	**177,087.00**
3491023 Reconstruction and Restoration Program	
26412 Conditional Recurrent Grant for Government agencies, committees, and boards	148,800.00
Total	**148,800.00**
District wide total	**325,887.00**

PI-4 Summary

Evidence Used	**Rating**	**Framework requirement**	**Source of information**	**Rating in 2008**	**Explanation of change since 2008**
(i) Stock of expenditure payment arrears (as a percentage of actual total expenditure) and any recent change in the stock.					
Financial statement of FCGO of FY11/12 and12/13. The expenditure payment arrears to actual expenditure were respectively0.31% (FY11/12) and 0.15% (FY12/13). Records maintained by DTCOs in TSA/ DECS based on statements submitted by spending units and verification of observations by internal audit and external audit by OAG.	A	The stock of arrears is low (i.e., below 2% of total expenditure)	Annual report of FCGO FY2011/12 and FY2012/13. Annual Report of OAG and statements produced by the SUs.	C	Stock of expenditure payment arrears has reduced significantly due to strong control measures used by MoF and enhancement of recording system through FMIS/ TSA/DECS.
(ii)Availability of data for monitoring the stock of expenditure payment arrears.					
Annual report of the FCGO DECS/TSA system (enforced since 2009) has forced the offices to record such arrears in FMIS and prepare district-wise annual report.	B	Data on the stock of arrears is generated annually but does not include an age profile.	FMIS, DECS/TSA system, annual report of FCGO, office-wide reports and annual audit reports of OAG.	D	The record system of expenditure payment arrears has been significantly improved due to the improvement of FMIS and implementation of the DECS/ TSA system. Monitoring of expenditure payment arrears is possible in the online system. Government has strongly enforced the means of control while releasing the authorization letter.

3.2 COMPREHENSIVENESS AND TRANSPARENCY (PI-5-10)

Comprehensiveness and transparency of budget is assessed through six indicators (PI-5-10). These indicators assess the classification of budget information in relation to comparable international indicators, its comprehensiveness, and the access of stakeholders to this information. The assessment also includes the extent to which unreported information on operations and fiscal relations between layers of government is transparent and available in the public domain.

PI- 5 CLASSIFICATION OF THE BUDGET

This indicator assesses comparability of budget cycle information, its formulation, execution, reporting, and recording in relation to international standards. Standards from IMF Government Finance Statistics (1986 or 2001 version) and UN Classification of Functions of Government (COFOG) are used for comparison.

Scoring method: M1
Assessed dimension: The classification system used for formulation, execution, and reporting of the central government's budget.
Rating PI-5:A. The budget formulation and execution is based on administrative, economic, and sub-functional classification, using GFS/COFOG standards or a standard that can produce consistent documentation according to those standards. (Program classification may substitute for sub-functional classification, if it is applied with a level of detail at least corresponding to sub-function.)

Justification of Rating

The budget cycle—formulation, execution, recording, and reporting—is based on administrative, economic, and functional classification using GFS/COFOG standards. Both classifications and the charts of accounts are aligned. The chart of accounts covers both revenue and expenditure accounts. Reports can be generated for all stages of the budget cycle to 50 sub-functions. The remaining 19 GFS sub-functions are not presently applicable and hence not in use, but can be operationalized as needed. The budget architecture can provide this information upon operationalization.

Gender responsive, pro-poor, climate change, and the strategic pillars of the periodic Plan are also used to classify the budget. The chart of accounts can generate all information, for all stages of budget cycle, from the FMIS system. This information is publicly available in both, print and electronic, platforms.

Like budget, revenue codes are GFS compliant and are recorded and monitored using the administrative, economic, and functional classifications. While the revenue codes cover 100 percent on the economic side, the social security tax and a few other taxes are covered on the administrative side of revenue codes. As noted above, all fiscal information is publically available. However, revenue classification does not include the social contribution; it is included separately as the social security tax under the remuneration tax head.

PI-5 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
Budget formulation and execution is presented in summary form in accordance with economic and functional classifications using GFS 2001 standards. The detailed budget formulation and execution is presented on the administrative classification, broken down by program and sub-program as per the country's need.	A	Budget formulation and execution is based on administrative, economic, and functional classification using at least the 10 main COFOG functions, and GFS 2001 standards for50 of 69 sub-functions. The remaining 19 sub-codes are not applicable in the country but can be made operational when the need arises.	Budget Formulation Manual, January 2011 (MoF). Chart of Accounts, May 2009 (FCGO). Budget Operation Guideline, 2011 (MOF). Consolidated Financial Statement F/Y 2011/12 (FCGO).	C	Compared with 2008, performance has improved with more effective use of functional and economic classification according to GFS 2001 standards. Budget documentation is now comprehensive.

PI-6: COMPREHENSIVENESS OF INFORMATION INCLUDED IN BUDGET DOCUMENTATION.

Nine information elements measure the comprehensiveness of the budget submitted by the central government to the legislature for scrutiny and approval. These nine information elements are as follows:

(1) Macro-economic assumptions, including at least estimates of aggregate growth, inflation, and exchange rate;
(2) Fiscal deficit, defined according to GFS or other internationally recognized standard;
(3) Deficit financing, describing anticipated composition;
(4) Debt stock, including details at least for the beginning of the current year;
(5) Financial assets, including details at least for the beginning of the current year;
(6) Prior year's budget outturn, presented in the same format as the budget proposal;
(7) Current year's budget (either the revised budget or the estimated outturn), presented in the same format as the budget proposal;
(8) Summarized budget data for both revenue and expenditure according to the main heads of the classifications used (refer toPI-5), including data for the current and previous year; and
(9) Explanation of budget implications of new policy initiatives, with estimates of budgetary impact of all major revenue policy changes and/or some major changes to expenditure programs.

Scoring method: M1

Assessed dimension: Share of the 9 elements listed information in the budget documentation most recently issued by the central government (in order to count in the assessment, the full specification of the information benchmark must be met).

Rating PI-6:A. Recent budget documentation fulfills 7 of the 9 information benchmarks.

PI-6 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Recent budget documentation fulfills 8 of 9 benchmarks.	A	Recent budget documentation fulfills 8 of 9 information benchmarks	Budget speech 2013/14; FCGO accumulated Financial Report; Economic Survey; MTEF document.	B	Previous assessment rating 5-6 of 9 marks. Budget documentation has now been more comprehensive.
Is there sufficient information to fulfil the requested rating?	Information element:	Information sources			
Yes	Macro-economic assumptions, including estimates of aggregate growth, inflation & exchange rate.	Budget speech of FY 2013/14(Para 401). Estimates of economic growth of 5.5% and 8% inflation have been set. Estimation of debt servicing is based on foreign exchange rate of any particular date of the current fiscal year.			
Yes	Fiscal deficit, defined according to GFS or other internationally recognized standard	Budget/fiscal deficit is calculated as per GFS 2001 standards and provided in the annex-1 of Budget Speech. In para 400 of the Budget Speech states and clarifies the level of fiscal deficit.			
Yes	Deficit financing, describing anticipated composition.	Deficit financing aggregate level decomposition is available in annexes: 1, 4, and 8 of Budget Speech. Loan wise decomposition information is available on the source book – 'White Book'.			
NO	Debt stock, including details at least for the beginning of the current year.	FCGO and Central Bank report debt stock. Economic survey reports end of the year debt stock (ten years) at aggregate level. But, there is no complete external debt database as there is no recording of on-lent loans and guarantees and no entity records domestic debt beyond the registry in place at the Central Bank.			

PI-6 Summary				Rating in 2008	Explanation of change since 2008
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
No	Financial Assets, including details at least for the beginning of the current year.	There is no Information on financial assets (aggregate).			
Yes	Prior year's budget outturn, presented in the same format as the budget proposal.	Last two year's line item wise budget is presented in the budget speech book and appropriation book (red book) annexes.			
Yes	Current year's budget (either revised budget or the estimated outturn), presented in the same format as the budget proposal.	Approved budget or estimated outturn is included in Budget Speech 2013/14 annexes: 1,4, 8.			
Yes	Summarized budget data according to main heads, including data for current & previous year.	Summarized budget data for, revenue and expenditure, according to the main heads of the classification (ref. PI-5), including data for the current and previous year, is presented in Budget Speech annex: 4, 8 and appropriation book (red book annex).			
Yes	Explanation of budget implications of new policy initiatives, with estimates of the budgetary impact.	Explanations of budget implications of new policy initiatives, with estimates of the budgetary impact of all major revenue policy changes and/ or major changes to the expenditure programs are explained in detail in the Budget Speech. These numbers are then reflected in the annexes.			

PI-7: EXTENT OF UNREPORTED GOVERNMENT OPERATIONS.

This indicator assesses the completeness of central government's operation (revenue and expenditure) by including fiscal statements on extra-budgetary operations and donor cash-funded activities. Two dimensions, one focusing on the level of extra-budgetary operations (which are not reported) and non-reported donor-funded activities but implemented by the Government (commodity grant, supplies and contracts to which the Government is not a party, donor technical assistance, and MDA-implemented trust funds) should be included to complete the picture of central government revenue, expenditure, and financing.

Scoring method: M1

RatingPI-7: D+

Assessed dimension (i): The level of extra-budgetary expenditure (other than donor-funded projects), which is unreported (i.e., not included in fiscal reports).
Rating: D. The level of unreported extra-budgetary expenditure (other than donor-funded projects) constitutes more than 10 percent of total expenditure.

Justification for Rating:

Annually, the subnational governments (SNGs) and many public enterprises and autonomous government agencies submit financial reports to their respective parent ministries and the Ministry of Finance. However, a consolidated fiscal report of all autonomous government agencies and subnational governments is not prepared thus lowering the accountability of resource use. There is no good handle on extra-budgetary operations stemming from subnational governments and autonomous government agencies. The consolidated financial statement does not cover revenues and expenditures of major autonomous government agencies and various funds (e.g., peacebuilding activities under Ministry of Peace and Reconstruction, other than shown in the budget book, Citizen Investment Trust, Employee Provident Fund, and Social Security Fund). The OAG estimates that there are at least 1,372 autonomous government agencies, with many reported to be outside the central government budget and therefore outside the central accounting and reporting system. These bodies were roughly estimated to have had expenditure of NPR 95 billion in FY 2012.

There are also significant unreported tax expenditures and quasi-fiscal expenditures. Though these categories are not counted as expenditure under current accounting/reporting standards, they are "hidden expenditures" and evidently an important part of the whole fiscal architecture. Tax expenditures (granted to diplomatic institutions, donor-funded projects, and other tax-exempted entities as per section 18 of Finance Ordinance 2013) add up to NRs 31.4 billion, approximately 11 percent of total revenue collection.[4] Quasi-fiscal activities, particularly by public enterprises selling at below cost, have not been accounted. Even without these two categories, unreported expenditure is considerably more than 10 percent of total expenditure, which in 2012/13 was NRs 302.1 billion.

Justification of Rating

All loan-financed project financial activity is reported, recorded, and audited. There are some exceptions when it comes to grant-financed activities, some of which are implemented outside the government's purview. The Development Cooperation Report 2013 cites the status of aid reporting as follows: (a) on budget 64 percent and (b) on treasury (i.e., channeled through the Treasury and therefore included in FMIS and financial reports) as 46 percent.[5] Only 29 percent (0.64 x 0.46) of all aid was fully reported. The Development Cooperation Report does not analyze this between grant and loan, but shows that 18.5 percent of all aid was on loan terms (US$177.90 million), while 81.5 percent was on grant or technical assistance terms (US$781.93 million). Table 3.8 indicates that only 13 percent of grant aid and technical assistance (US$100.45 million) was fully reported.

Assessed dimension (ii): Income/expenditure information on donor-funded projects, which is included in fiscal reports.

***Rating:* C.** Complete income/expenditure information for all loan-financed projects is included in fiscal reports

Table 3.8 : External assistance in FY12/13

	US$ millions		
	Reported	**Not reported**	**Total**
Grant and TA	100.45	681.48	781.93
Loan	177.90	0.00	177.90
Total	278.35	681.48	959.83

PI-7 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
PI-7	D+			C	
Dimension (i): There are 1,062 parastatals (including autonomous government agencies, trust funds, and state corporations) in which government has a majority stake. Estimated unreported expenditure is considerably more than 10% of total expenditure; comprehensive details on expenditure and on-tax revenues are not included in fiscal reports, not even as consolidations with other central government expenditure.	D	The level of unreported extra-budgetary expenditure (other than donor-funded projects) is estimated to be over 10%.	OAG Report 2013 Budget Speech 2013	C	Expanded coverage of government operations and strengthening of processes, systems, and institutions compared to last assessment.
Dimension (ii): Development Cooperation Report 2013 cites the status of aid reporting as 29% on budget and on Treasury, of which all loan aid is reported and the balance (US$681.48 million) is grant and TA aid.	C	Complete income/expenditure information is included in fiscal reports for all loan financed projects and at least 50% (by value) of grant-financed projects.	Development Cooperation Report 2012/13 Budget Speech 2013	c	The 2008 assessment said complete income/expenditure information for all loan-financed projects is included in fiscal reports. The 2013 Development Cooperation Report shows that the figure is more than 50%.

4 OAG Report 2014.

5 These numbers could be well-below numbers reported to OECD in 2013.

PI-8: TRANSPARENCY OF INTER-GOVERNMENTAL FISCAL RELATIONS.

The Local Self-Governance Act (LSGA) has assigned both expenditure and revenue assignments to the subnational governments.[6] The central government makes large budgetary resource transfers to the subnational governments for providing basic services to the public through the budget. These transfers are above what is collected under devolved-revenue assignments. Through three dimensions, this indicator assesses the extent to which there is transparency in inter-governmental fiscal relationship. All three dimensions are rated according to performance in the last completed financial year (i.e., FY13/14). The central government makes transfers directly to the district development committees (first subnational tier of government), municipalities, and village development committees (second subnational tier of government).

Scoring method: M2
Rating PI -8: C+

Assessed dimension (i): Transparent and rules-based systems in the horizontal allocation among subnational governments of unconditional and conditional transfers from central government (both budgeted and actual allocations).

***Rating:* C.** The horizontal allocation of only a small part of transfers from central government (10-50 percent) is determined by transparent, rules-based systems.

Justification for Rating:

The LSGA (1999) empowers local (three-tiered) governments to implement development activities based on local priorities. Since 2002, government has devolved agriculture and livestock extension services, primary education, and primary health to local governments by creating management committees to run the services. A budget is provided for carrying out these functions, which government agencies also continue to provide. The funding comprises conditional and unconditional block grants, revenue generated from devolved-revenue assignments, and lateral grants made to the subnational governments by international nongovernmental organizations (INGOs) and national nongovernmental organizations (NGOs), including many central-level donors. These lateral funding resources do not come under purview of the central government and hence are outside the budget.

A transparent, rule-based system guides the central unconditional block grants to subnational governments. The Ministry of Finance makes the vertical allocation by deciding how much will be divided among the subnational government as unconditional (block) and conditional (earmarked) grant, capital and recurrent. Conditional grants are mostly tied to education, roads, and other infrastructure spending.

Dimension (i) is concerned only with the horizontal allocation to each local body.

Five criteria guide the central government's vertical allocation to the subnational governments, the population weightage being about 50 percent in the transfer formula (Table 3.9). In FY12/13, the total transfer by the central government to the local bodies was NPR 23.3 billion(or 7.7 percent of total central government expenditure), out of which unconditional grant was NPR 10.3 billion (3.4 percent). In addition to central government transfers, subnational governments receive performance grants after meeting minimum performance conditions. This minimum condition and performance measurement (MCPM) system was piloted in 2004 and now applies to all local bodies.

There is no recent evidence of the use of the horizontal allocation formula reportedly prepared by the National Planning Commission. The allocation formulae are now being updated with technical assistance factoring in the poverty status and social outcome of regions and districts.

Dimension (i) covers also the horizontal allocation of revenues that are collected by central government and shared with subnational governments, principally mining and mountaineering royalties, in accordance with LSGA 1999 (section 220) and the Local

[6] Expenditure assignment: all basic services and revenue assignment: land tax, rent tax, entertainment tax, and housing tax.

Self-Governance Regulation 1999, rule 211. The allocation is prescribed by law and is transparent although there is ambiguity on some revenue items.[7] The local share of the central collections in 2012/13 was about NPR1.1 billion. A third form of transfer from the centre to local bodies is social payments to senior citizens; disabled, endangered ethnic groups; single women security scheme; and others. The social payments are transferred to local bodies under a separate budget line. They are all earmarked and are counted here together with conditional grants.

A rough calculation shows that total central transfers to local bodies in FY12/13 were about NPR 32 billion, of which unconditional grants (NPR 10.3 billion) and shared revenues (NPR 1.1 billion) were reasonably transparent and predictable. It added up to NPR 11.4 billion, or 36 percent of all central transfers.

Assessed dimension (ii): Timeliness of reliable information to subnational governments on their allocations from the central government for the coming year.
Rating: C. Reliable information to subnational governments is issued before the start of the sub national's fiscal year, but too late for significant budget changes to be made.

Justification of Rating

LSGA 1999 prescribes the timetable to be followed for the preparation of subnational government budget planning and formulation process. Budget guideline directives and ceilings for respective subnational governments are communicated in print and also posted on the website (www.mofald.gov.np). Subnational government budget preparation is very much a top-down-driven process. In the absence of elected local governments, the timeline has not always been followed. Although budget ceilings are known, final shape of the budget program is decided by a coordination body of local political parties and civil society in the districts and in Kathmandu. Line ministries, on behalf of the subnational government, contribute substantially in shaping up the budget, which is published later than the prescribed date. In FY15, for example, the National Planning Commission sent budget ceilings to the district development committees on December 2, 2013, and a week later the Ministry of Federal Affairs and Local Development asked local bodies to submit the budget proposal by mid-March 2014. It was too late for making significant changes.

Assessed Dimension (iii):Extent to which consolidated fiscal data (at least on revenue and expenditure) is collected and reported for general government according to sectorial categories.
Rating: B. Fiscal information (exante and expost) that is consistent with central government fiscal reporting is collected for at least 75 percent (by value) of subnational government expenditure and consolidated into annual reports within 18 months of the end of the fiscal year

Table 3.9. : Criteria for allocation to subnational governments

Level/Entity	Population	Poverty (human dev. index)	Area	Cost index[/a]	Weighted revenue[/b]
District development committee	40%	25%	10%	25%	--
Municipalities	50%	25%	10%	--	15%
Village development committee	60%	--	10%	30%	--

[/a] This is based on the cost of a standard basket of goods since the cost varies from one local body to another.
[/b] While other criteria are based on need, the revenue criterion is based on collection of own source revenue, to encourage mobilization of local revenue.

[7] Unclear, overlapping, and ambiguous revenue assignments create confusion on responsibilities, jurisdiction, and tax rates. For example, tax on rental income from house and land is under the tax authority of both, central government and LBs. The central level levies 15% tax on such rental, whereas the Local Self-Governance Regulation permits municipalities to charge 2%. The regulations do not specify whether the 2% municipal share is in fact included in the central government tax rate of 15% or if municipalities can raise their 2% on top of central governments share. Municipalities have not been able to collect any substantial revenue from this source due to this confusion (LBFC report, p. 23).

Justification of Rating

Fiscal information (exante and expost) of district development committee is consistent with central government fiscal reporting, more on the expenditure side than revenue. On-budget resource transferred to subnational government is recorded and accounted. The Office of Auditor General limits auditing of subnational government accounts to only district development committee. Accounts of second-tier governments (municipalities and village development committees) are outside the purview of OAG. On-budget expenditure information collected is consistent for at least 75 percent (by value) of subnational government expenditure.[8] Consolidated expenditure annual reports are prepared within 8 months of the end of the fiscal year. All central-level transfers, conditional and unconditional, and expenditures are reported under GFS codes. With urbanization and increase in rural household income rise, the subnational government's dependence on central government transfers is declining but is still large in absolute terms. Although there is no firm handle on the percentage of subnational government expenditure funded through their own resources, one report suggests that in FY13 subnational governments funded 10 percent of their expenditure through its own resources compared to 2 percent a decade earlier. There are lapses in reporting revenue collected by the subnational governments, and the reporting is not done under the GFS format.

PI-8 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
PI-8	C+			C	
Since 1998/99, grants have increased annually incrementally on a criteria and formula base, but it does not exceed 50 percent of total budget fund transfer to local bodies.	C	(i) Horizontal allocation of only a small part of transfers from central government (10-50%) is determined by transparent and rules-based systems.	MOFALD Report Budget Appropriation Book, 2012/13	C	Although horizontal allocations to SNGs are reasonably transparent, the entire de-concentration grant was not reflected in the 2007 assessment as there was no mechanism to verify source of information (aggregated). The process of verification has improved with move to on-line budget preparation from past manual-based budget preparation.
Grant information (ceiling for next FY, i.e. July to December 2013) was issued to SNG levels, but it was too late for significant budget changes to be made.	C	(ii) Planning information to SNG is issued before the start of the SNG fiscal year, but too late for significant budget changes to be made.	Issue of budget ceilings to local bodies from planning section, MOFALD.	C	Partly due to change in FY, but delays also noted in previous 2 years.
SNG reports are collected and Local Fiscal Commission prepares consolidated financial statement within 8 months after completion of the fiscal year.	B	(iii) Fiscal information (at least expost) that is consistent with central government fiscal reporting is collected for at least 75% (by value) of SNG expenditure and consolidated into annual reports within 10 months of the end of the fiscal year.	LBFC Publication	C	Fiscal information with central government fiscal reporting is collected for at least 75% (by value) of SNG expenditure and consolidated into annual reports within 8 months of the FY end. But it is supposed that at least 75% (by value) of SNG expenditure is the same as previous because the increment in local revenue is not more than 2%.

8 http://www.fcgo.gov.np/report-publications/district-wise-expenditure

PI-9: OVERSIGHT OF AGGREGATE FISCAL RISK FROM OTHER PUBLIC SECTOR ENTITIES.

Macro fiscal aggregate management prudence is the responsibility of central government, and Nepal has done well on this rating by staying within the agreed level of net domestic borrowing. However, all fiscal risks arising from activities of subnational governments, autonomous government agencies, and public enterprises, including state-owned banks, may not be fully captured in the year-end financial statement of the central government, thus raising questions on the reported aggregate fiscal risks. This indicator assesses the capacity of the central government to monitor and manage the fiscal risks arising from its units, affiliated agencies, boards, and other levels of government.

Scoring method: M1
Rating PI-9: C

Assessed dimension (i): Extent of central government monitoring of autonomous government agencies and public enterprises.
Rating: C. Most autonomous government agencies and public enterprises submit fiscal reports to the central governments, at least annually, but a consolidated overview is missing or significantly incomplete.

Justification of Rating

The Financial Procedures Act 1999 and its Regulation, as well as other laws enforce and stipulate that all autonomous government agencies and public enterprises must have their accounts audited, and reported to the parent ministry or the Ministry of Finance. The Ministry of Finance publishes the status of all major public enterprises annually (Yellow Book). Altogether 37 major public enterprises submit their financial statements, and these entities cover above 90 percent of government obligations. In FY13, the OAG had audited the financial account of 92 corporate bodies, 805 boards and committees, and 75district development committees. Not all audits become part of the annual OAG report. The scale of risks arising from these entities is not reported in the consolidated report but is said to be large. For example, a loan of NPR27 billion to the Nepal Electricity Authority was written off two years ago, and yet this Authority still reports a loss of NPR 14 billion. Some government-owned entities, such as Nepal Oil Corporation, Janakpur Cigarette Factory, and Nepal Drug Limited have large accumulated losses; therefore, the consolidated report on fiscal risk is weak.

Assessed dimension (ii): Extent of central government monitoring of subnational government's fiscal position.
Rating: C. The net fiscal position is monitored at least annually for the most important level of subnational government, but a consolidated overview is missing or significantly incomplete.

Justification of the Rating

The LSGA 1999 authorizes subnational governments to meet their fiscal gap through debt and can accept foreign loan with prior central government consent. As financial institutions request the central government guarantee of loan extended to subnational governments, the volume of such loans are low because the loan guarantee is not provided without cabinet approval.

The OAG audits subnational government's internal audit reports, but such audits are weak in coverage and reporting of all fiscal transactions are significantly incomplete. ICAN-registered auditors audit the financial accounts of subnational governments. The monitoring division of the Ministry of Federal Affairs and Local Development monitor all the local bodies and the Local Governance Finance Commission monitors and appraises the functioning of all local bodies on the MCPM-indicator basis and prepares a consolidated report. But an overall fiscal risk report does not exist. The TSA is yet to capture information of revenue and expenditure of local governments, other than central government transfers to local bodies. Since government accounting is on a cash basis and the existing process to capture arrears is loosely implemented, the scale and level of reported outstanding arrears is an underestimate.

PI-9 Summary				Rating in 2008	Explanation of change since 2008
Evidence used	Rating	Framework requirement	Information sources		
	C			D+	
Major public enterprise and autonomous government agencies submit financial accounts to the Accountant General's Department and MoF on an annual basis. A consolidated overall fiscal risk report has not been issued	C	All major autonomous government agencies and public enterprises submit fiscal reports, including audited accounts to the central governments at least annually, but consolidated overview is missing or significantly incomplete.	OAG Report, 2012 Accountant General's Department; website	C	The creation of a new unit in 2009 at the MoF has resulted in the centralization and consolidation of information on public enterprises and autonomous government agencies and also in the publication of an overall report.
Fiscal information on SNG is monitored annually on the basis of MCPM. Financial status analysis of SNG is also prepared annually. But it is not used to produce an overall fiscal risk report.	C	The net fiscal position is monitored at least annually for the most important level of SNG, but a consolidated overview is missing or is significantly incomplete.	Local Government Fiscal Commission Report, 2013. MCPM assessment report of local bodies 2012.	D	SNG fiscal and accounting information is monitored but not used to produce a fiscal risk analysis or report. In the period examined in 2007, SNGs were not monitored annually.

PI-10: PUBLIC ACCESS TO KEY FISCAL INFORMATION

Easy access to fiscal information to the public determines the level of transparency. This is measured through six elements of fiscal information.

> ***Scoring method: M1***
> ***Assessed dimension:*** Number of six listed elements of public access to information that are fulfilled:(i) annual budget,(ii) in-year budget reports,(iii) year-end financial statements,(iv) external audit reports,(v) contract awards greater thanUS$100,000,and (vi) funding resources to primary service units in at least 2 sectors such as elementary schools and primary health clinics.
> **Rating: A**

Justification of the Rating

The government makes all of the 6 listed types of information available to the public.

(i) ***Annual budget documentation:*** *A complete set of documents can be obtained by public through means when it is submitted to the legislature.*

The Budget Speech is uploaded on MOF website immediately upon its presentation in Parliament. All budget-related documents are uploaded on MOF website and also published.[9] Similarly, the National Planning Commission publishes and makes available on its website the MTEF, and central-level programs and projects (part 1) and district-level programs and projects (part 2) within a month of budget presentation. Furthermore, Right to Information Act, 2007, guarantees public access to information held by government upon request to the appropriate body.

(ii) ***In-year budget execution reports:*** *Reports are routinely made available to the public through appropriate means within a month of completion.*

All expenditure reporting can be received on a real-time basis through the TSA system at the FCGO. The Ministry of Finance meets the press each month and delivers statements on monitoring of budget implementation, revenue and foreign assistance mobilization, and status of public expenditure and public enterprise management. The Central Bank

9 Economic survey, status paper of public enterprises, resource book and annual appropriation document (Red Book) resource book as well as the three-year capital budget by project and programs.

prepares a weekly treasury position and provides it to the concerned authorities on demand. However, this report is not available to the public. The Central Bank makes its fiscal reports public in its monthly economic monitoring report. In addition, the mid-term and year-end evaluation of budget implementation status is also published.

(iii) ***Year-end financial statements:*** *The year-end financial statements are made available to the public through appropriate means normally within six months of completed audits.*

The FCGO prepares the annual financial statements within six months and publishes the Consolidated Financial Report. The FGCO submits audit information to the OAG upon completion.

(iv) ***External audit reports:*** *All reports on central government consolidated operations are made available to public through appropriate means within 6 months of completed audit.*

External audit is completed within eight months after the FY end, and it takes an additional three months for submitting it to the legislature. After completing the audit, the report is made available to the public either as a published document or by posting it on the website.

(v) ***Contract awards:*** *Award of all contracts with value above US$100,000 equivalent is published at least quarterly through appropriate means.*

The Public Procurement Act (PPA) 2006 is the legal basis for contract management. Information concerning approval of tender has to be published (Section 47 of PPA). All approved and awarded tenders are reported on the official portal of PPMO regularly. Government offices publicize the approved tender documents on their websites. The district-level offices paste such documents on notice-boards of offices with high public movement such as district administrative offices, district treasury offices, and chamber of commerce and industry.

(vi) ***Resources available to primary service units:*** *Information is publicized through appropriate means at least annually, or available upon request, for primary service units with national coverage in at least two sectors such as elementary schools or primary health clinics.*

No discrimination is made of program- or project-level activities. All programs are in the line-item budgetary system. The Ministry of Finance makes the Budget Speech and the annual budget appropriation book (Red Book) available to the public, and the National Planning Commission provides program and project information in two parts. The ministries can provide additional information as needed.

Table 3.10 : 2013 Budget Preparation Schedule and timeliness and compliance.

Legend	Required completion date	Actual date NPC program finalization date	Actual date Budget discussion at MoF
Budget circular date	Dec 10	Feb 2,	Feb 2, 2013
Budget discussion date	March 11	March 28	June 14,2013
Budget finalization date	May 12	April 10	July 13, 2013
Budget discussion time frame.	March 2	March 28	July 13, 2013
Cabinet approval of budget.	May 18	July 15	
Budget submission date to the Parliament*	May 16	July 15	July 15,2013
Parliament approval of the budget (ordinance) *	July 11		July 15

* In the absence of Parliament, budget announced through an Ordinance by the President

PI-10 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
PI-10	A	Government makes available all of the 6 listed types of information.	MoF website *www.mof.gov.np.*	B	
All budget documents are published on MoF website after it is submitted to Parliament; the approved budget is published after approval	Met	(i) Annual budget documentation is made public when submitted to legislature.	MoF website *www.mof.gov.np.*		
The annual budget execution report is available to the public after it is presented to Parliament on the MoF website within one month of completion.	Met	(ii) In-year budget execution reports are published within one month of their completion.	MoF website *www.mof.gov.np.*		
The audited final accounts are made available to the public in a timely manner.	Met	(iii) Year-end financial statements are published within 6 months of completed audit.	MoF website *www.mof.gov.np.* FCGO consolidated Financial report.		Budget documents are timely made available to the public. The change reflects progress made in public access to FCGO and OAG reports.
All reports are available to the public after they are presented in Parliament on the OAG website within six month of audit completion.	Met	(iv) Timely availability of external audit reports to the public.	Auditor's general website.		
Information on tender awards is published systematically.	Met	(v) Contract awards with value above USD$100,000 are published before and after contract is awarded.	Concerned office website, notice board and daily newspapers.		
Information on resources received by primary service providers is available upon request.	Met	(vi) Availability to public of information on resources to all primary service units.	MoF website *www.mof.gov.np* Concerned agencies provide information upon request or are published on notice board.		

3.3 POLICY-BASED BUDGETING (PI-11-12)

PI-11: ORDERLINESS AND PARTICIPATION IN THE ANNUAL BUDGET PROCESS.

The Ministry of Finance and National Planning Commission jointly prepare the national budget. There is active participation from ministries, departments, and agencies in budget preparation where settlements on outstanding issues are done. Parliament actively participates in policy debates. Active participation of the legislature in budget formulation through the Budget Committee is an area that could be further strengthened.

Scoring Method: M2

Rating: PI-11: A

Assessed dimension (i): Existence of and adherence to a fixed budget calendar

Rating: A. A clear annual budget calendar exists, is generally adhered to, and allows MDAs enough time (at least six weeks from receipt of budget circular) to meaningfully complete their detailed estimates on time.

Justification of Rating

There is a clear and detailed annual budget preparation calendar. The Budget Formulation Guideline contains all necessary information and guidance for MDAs on budget preparation, including calculators for respective data requested under budget request forms. The budget preparation starts with the issuance of a joint circular (NPC/MoF) with budget ceilings and guidance to the MDAs of the next FY budget priorities, four months before the start of the new fiscal year. This circular assigns dates of budget submission, negotiations, roles, responsibilities, and activities during the preparation process and responsibilities of the concerned institutions. But in practice, there are lapses in the adherence to the budget circular timelines. Although several reasons can be assigned to missed deadlines, repeated budget negotiations force the MDAs to miss suggested budget preparation dates largely as a result of insufficient planning at the MDA level and incremental nature of budget ceilings that forces both the resource providers and users to negotiate several times. Otherwise, sufficient time (four months) is provided to MDAs to prepare, negotiate, and finalize the budget in a meaningful manner. The FY 2013 budget preparation milestones are shown in Table 3.10.

While sufficient time is provided for budget negotiations, approval of annual work program and spending authorizations are completed later in the fiscal year. The OAG report (2013) states that spending authorization amounting to 2.3 percent of FY13 budget was given at the end of the fiscal year.

Assessed dimension (ii): Guidance on the preparation of budget submissions.
Rating: A. A comprehensive and clear budget circular is issued to MDAs, which reflects ceilings approved by Cabinet prior to the circular's distribution to MDAs.

Justification for Rating

The Resource Committee guides the preparation of a medium-term macroeconomic framework. Members of this committee are the NPC vice-chairperson, member-secretary, and finance secretary; Central Bank Governor, and the Financial Comptroller General. This committee decides the size of the budget based on the agreed macro fiscal framework for the new fiscal year. The sectorial- and ministry-level ceilings are prepared by the National Planning Commission in close consultation with the Ministry of Finance using the agreed ceiling as basis. A clear and comprehensive budget guideline with ceilings is then issued to the MDAs. This circular is the beginning of the budget preparation cycle, keeping the size within the limit set by the Resource Committee. The final size of the budget is larger than the ceiling reflecting the changed resource availability, and the Cabinet endorses this higher number before the budget is submitted Parliament.

Assessed dimension (iii): Timely budget approval by the legislature
Rating: NA. The legislature approves the budget before the start of the fiscal year, but a delay of up to two months has taken place for approval in one of the last three years.

Justification for Rating

The Finance Minister submits the proposed budget to the Parliament for approval, a week before the start of the fiscal year (i.e., mid-July). It usually takes 2 months for Parliament to pass the budget and obtain the President's seal required by all laws. In the last three years, there were two instances when the budget was approved though an executive ordinance because there was no Parliament. Therefore, the rating is not applicable in this dimension.

PI-11 Summary				Rating in 2008	Explanation of change since 2008
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
There exists a clear annual budget calendar. For this purpose, MoF publishes Budget Formulation Guidelines by consulting with all stakeholders that are involved in the budget formulation process, including NPC. Generally, the Guidelines need to be updated every two years. The latest version was published in 2012. The budget calendar has clearly mentioned the dates, roles, responsibilities, and activities during the budget preparation process and responsibilities of the concerned institutions. It allows MDAs reasonable time (about 2 months from the receipt of the budget circular) to send their budget and program proposals to the NPC and MoF for budgetary discussions.	A	(i) Existence of an adherence to a fixed budget calendar.	NPC records	B	Update in budget preparation guidelines that has facilitated the line ministry to prepare budget for discussion with MoF/NPC two months in advance, well before budget announcement date.
A Resource Committee has been set up in NPC for the preparation of medium-term macroeconomic framework. This Committee meeting is chaired by the vice-chairperson of the NPC and is participated by all the members of the NPC, its Member- Secretary, Finance Secretary, Central Bank Governor and the Financial Comptroller General. Moreover, a clear and comprehensive budget guidelines (macro and sectorial) and budget ceiling is circulated to all the MDAs keeping the total budget size within the limit set by the Resource Committee.	A	(ii) Clarity/ comprehensiveness of political involvement in the guidance on preparation of budget submissions (budget circular or equivalent).	Records of NPC	B	A comprehensive and clear budget circular is issued to MDAs, which reflects ceilings approved by Cabinet.
In the last three years there were two instances when the budget was approved through an executive ordinance because there was no Parliament.	NA	(iii) Timely budget approval by the legislature or similarly mandated body (within the last three years).		D	Absence of Parliament.

PI-12: MULTI-YEAR PERSPECTIVES IN FISCAL PLANNING, EXPENDITURE POLICY, AND BUDGETING

This indicator refers to practice of multi-year fiscal policy, its planning and budget practice by the central government. There are four indicator dimensions: (i) preparation of multi-year fiscal forecast and functional allocations, (ii) scope and frequency of debt sustainability analysis (DSA), (iii) existence of sector strategies with multi-year costing of recurrent and investment expenditure, and (iv) linkages between investment budget and forward expenditure estimates

Scoring Method: M2
Rating of PI-12: B

Assessed dimension (i):Multi-year fiscal forecasts and functional allocations.
Rating: B. Forecasts of fiscal aggregates (on the basis of main categories of economic and functional/sector classification) are prepared for at least two years on a rolling annual basis. Links between multi-year estimates and subsequent setting of annual budget ceiling are clear, and differences explained

Justification of Rating

Nepal has had a MTEF since FY2002/03. This framework covers a three-year period anchored by a macroeconomic fiscal framework on a rolling annual basis, with economic and functional classifications. The first year of the MTEF is the fiscal year budget; the forecasted budget ceilings for the next two years are enunciated on the MTEF document. Although forward ceilings are set, the actual budget size may differ with availability of resources, change in policy focus, and regime changes. Annual policy changes anchored by budget allocations are announced through the budget speech.

Assessed dimension (ii): Scope and frequency of debt sustainability analysis (DSA).
Rating. Debt sustainability analysis for external and domestic debt is undertaken annually.

Justification of Rating

IMF has conducted the DSA for Nepal for three consecutive years as part of its Article IV report. The 2013 DSA concluded that Nepal's risk of debt distress is low; it was a change from the previous assessments that had concluded that Nepal faced moderate risk of debt distress. Although the authorities expressed some concern in the change of mix of loans and grants of IDA assistance with the change in DSA rating, they broadly agreed with the 2013 DSA findings.

Assessed dimension (iii): Existence of costed sector strategies.
Rating: C. Statements of sector strategies exist for several major sectors but are only substantially costed for sectors representing up to 25 percent of primary expenditure, or costed strategies cover more sectors but are inconsistent with aggregate fiscal forecasts.

Justification of Rating

Dimension (iii) refers to the last completed budget (FY2013/14).

The Government prepared business plans for seven sectors, but it could not be continued. Sector wide approaches (SWAps) had been adopted in three sectors (i.e., education, health, and rural roads). These sectors and subsectors have costed strategies. But these costed strategies are inconsistent with aggregate fiscal forecasts of MTEF. The allocation for these three sectors covers about 20 percent of the total budget (net of donor funds). Some initiative was taken to prepare SWAp in trade as well.

Assessed dimension (iv): Linkages between investment budget and forward expenditure estimates.
Rating: C. Many investment decisions have weak links to sector strategies and their recurrent cost implications are included in forward budget estimates only in a few (but major) cases.

Justification of Rating

Although sector strategies are spelled out in the plan document, links between strategies and their investment and recurrent cost implications are weak. Few sectors like education, health, and rural roads have costed sector strategies. In absence of sector strategies, the business plans guide the investment, but it is limited to a broad level of recurrent aggregate cost structure.

PI-12 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Nepal has been preparing the MTEF since the FY02/03. This MTEF is prepared for a three-year period. It has a macroeconomic framework for a three-year period based on the main categories of economic and functional/sector classifications prepared on a rolling annual basis. The first year of the MTEF is the budget, and the forward forecast sets the ceiling for the coming years. Links between multi-year estimates and subsequent setting of annual budget ceilings are clear and differences are explained in the MTEF document. Therefore, there exists a clear link between MTEF and the annual budget. The previous periodic plans (i.e., the 11thand the 12thplans) were fiscally anchored by the MTEFs. Disaggregate sectorial and sub-sectorial ceilings were also enunciated in the MTEF. However, there is the provision for crossing the ceiling allocated for the ministries if they could mobilize additional external resources. So there is some flexibility allowed to the ministries	B	Preparation of multi-year fiscal forecast and functional allocations.	NPC and MoF reports	B	No change. Forecast for two years are provided, and budget speech enunciates the budget focus.
The FCGO debt-servicing unit maintains records of external debt. External debt information is received from development partners and is recorded by the FCGO debt-servicing unit. The Central Bank used to publish the total outstanding debt, both domestic and foreign, in its quarterly bulletin. It is not usual practice for the government to do debt sustainability analysis. However, agencies like IMF and World Bank used to regularly publish the DSA reports that could be used by the government for its analysis.	A	Scope and frequency of DSA.		C	
A few years ago, the Government prepared the business plans for seven sectors. But it was not continued. Sector strategies were prepared in the periodic plan documents. SWAPs are in place in education, health and rural road sectors. Some initiative was also taken to prepare a SWAp in the trade sector. The budget allocation for these three sectors covers about 27% of the total.	C	Existence of sector strategies with multi-year costing of recurrent and investment expenditure.	NPC, MoF, MFALD, MoE, and MoHP reports.	C	
Although sector strategies are spelled out in the plan document, the links to them and their investment and recurrent cost implications is weak. Sector strategies with cost estimates exist only in education, health, and rural roads. Therefore the link between sector strategies, the investment, and forward expenditure estimates is weak in most of the sectors.	C	Linkages between investment budget and forward expenditure estimates.	NPC, MoF, MFALD, MoE, and MoHP reports	C	

3.4 PREDICTABILITY AND CONTROL IN BUDGET EXECUTION (PI-13-20)

Resource predictability lowers fund shortage apprehension of the front-line agencies to plan and deliver services during the fiscal year and beyond. Resource predictability and availability supports the budget execution rate, strengthens forward planning to leverage expenditure outputs on time, and subsequently lowers transaction costs associated with non-availability of funds during budget execution cycle. Above all, it reduces the requirement of re-budgeting, thereby strengthening policy execution through implementation. Availability of domestic resources fortifies resource predictability and fund availability for implementers to leverage the intended spending outputs.

PI-13: TRANSPARENCY OF TAXPAYER OBLIGATIONS AND LIABILITIES

This indicator has three dimensions, namely: (i) Clarity and Comprehensiveness of Tax Liabilities; (ii) Taxpayer's Access to Information on Tax Liabilities and Administrative Procedures; and (iii) Existence and Functioning of a Tax Appeal Mechanism

Scoring Method: M2
Rating PI-13: A

> ***Assessed dimension (i): Clarity and Comprehensiveness of Tax Liabilities***
>
> ***Rating: A.*** Legislation and procedures on tax are comprehensive and clear. The discretionary power of government officials is absolutely controlled by law.

Justification of Rating

Article 89 of the Interim Constitution of Nepal 2007bars taxation without legislation. Tax rates are fixed by law and can be changed only when the related provisions are amended by parliament. The Government's Working Procedure Rules 2007 and Work Division Rules 2012 make the Ministry of Finance responsible for revenue administration. The Inland Revenue Department (IRD) is the principal agency responsible for income tax, value added tax (VAT), and excise tax collection, while the Department of Customs administers custom tax. Department of Revenue Investigation works to control leakages and recommends punitive actions. The MoF Revenue Management Division coordinates the work of these three departments.

Tax is collected based on provisions of the following laws, rules, and regulations: Value Added Tax Act 2052 (1995) and Value Added Tax Rules 1996 for VAT management, Income Tax Act 2001 and Income Tax Rules 2002 for income tax management, and Customs Act 2007 and Customs Rules 2007 for customs management. Similarly, the Excise Act 2001 and Excise Rules 2002 are enforced for managing excise duties. All these laws and regulations have their own procedures. In addition to the aforementioned laws and regulations, the Income Tax Directives 2009, Value Added Tax Directives 2012, Excise Duty Directives 2011, Customs Tax Directives 2008, and Rent Tax Directives 2011 clarify and ensure transparency tax laws and collection.

The administrative discretionary powers come under the Income Tax Act 2001, section 11; VAT Act 1995, section1; and section 9 of the Excise Duty Act 2001 and Custom Tax Act 2007. These provisions articulate situations and conditions wherein discretionary power is delegated to tax officers and is confined to the situation when material difference arises in tax assessment. Revenue Exemption Rules and Regulations 2002 guide the Ministry of Finance on tax exemptions, which can be executed only after securing Cabinet approval and only under special circumstances.

Tax collection is primarily based on self-declaration. The taxpayer can pay the tax by self-declaring the liability, and the onus lies on tax departments to provide reasonable evidences for requiring payments above the self-declared amount—reinforcing mutual accountability. Likewise on trade tax, there is the clear, legal provision that allows the taxpayer to declare the transaction value of goods at the customs point; if officials have reasonable doubts, they can buy the declared consignment at the declared rates. These provisions have been embedded in the tax laws not only to strengthen mutual accountability of tax declaration and collection, but to also reduce the discretionary power of tax administrators.

In addition to these measures, an independent Revenue Consultative Committee—a stakeholders committee with membership drawn from nominations from the Federation of Nepalese Chamber of Commerce and Industry, Nepal Chamber of Commerce, a professor of economics from a university, and representatives of other stakeholders—provide policy suggestions to the Government for strengthening and improving revenue administration. The Revenue Consultative Committee holds meetings with the budget team during the formulation and occasionally on a needs basis. This committee suggests measures (legal, administrative, and policy) to strengthen revenue administration to the Finance Minister. These processes and institutional arrangements have reduced real and perceived discretionary power of tax administration because the committees allow stakeholder oversight.

Assessed dimension (ii): Taxpayer's access to information on tax liabilities and administrative procedures

Rating: A. Taxpayers have easy access to comprehensive, user friendly and up-to-date information tax liabilities and administrative procedures for all major taxes, and the revenue administration supplements this with active taxpayer education campaigns.

Justification of Rating

The taxpayer has easy and trouble-free access to tax laws and other information on revenue administration. The information is clear, transparent and updated regularly. Different acts and rules of revenue administration and directives[10] and procedures, including tax calculator, remuneration tax calculator are available on websites of different agencies. Information on legal tax obligations and administrative procedures are also available on the website.[11]

The booklet with information on tax and methods of calculation for compliance with the tax laws, brochures, and circulars are also available on the websites of the different revenue agencies. Every revenue administration office displays a Citizen's Charter with information for taxpayers on the tax administration procedures. The Citizen's Charter provides information on rates, timeframe for tax procedures, charges, timeframes for tax installments, fines for delays, and more. The information on tax installment schemes is published and broadcast in both print and broadcast media. The Government has established 13Tax Service Offices in Kathmandu Valley and 13 Taxpayer Service Centers in districts and regions to facilitate and improve tax information and collection. This has improved access and interface of taxpayers with tax administration.

The Inland Revenue Offices and Taxpayer Service Offices carry out taxpayer education programs on laws, procedures, and administrative processes all over Nepal. In FY13, 1.1 million people were provided tax education, up from 0.626 million people in FY12 and 0.541 million people in FY11. In addition, the informative programs about taxes are also broadcast on Nepal Television. The notices on obligations of taxpayers are also published and broadcast regularly. Such notices are prepared on specific subjects/issues. Sector-related interaction programs on tax are also organized. Taxpayer education programs are not confined to particular places, rather they are run throughout the country. Facilitators are deployed at the Customs Department and major Custom Offices to inform the taxpayers. The outreach to taxpayers through seminars and workshops doubled to 1,173 events in FY13 from 513 events in FY11. Such programs benefit taxpayers who get guidance on taxation and where and how to access this information, while the tax administration obtains direct feedback and suggestions for

10 Value Added Tax Act 1995 and Value Added Tax Rules 1996; Income Tax Act 2001 and Income Tax Rules 2002; Customs Act 2007 and Customs Rules 2007; Excise Act 2001 and Excise Rules 2002; Income Tax Directives 2009, Value Added Tax Directives 2012, Excise Tax Directives 2011, Customs Tax Directives 2008, and Rent Tax Directives 2011.

11 www.ird.gov.np, www.customs.gov.np, www.mof.gov.np.

improvements. These reviews, seminars, and workshops have contributed to the uniformity of implementation of tax laws, strengthened homogeneity in decision-making processes, and enhanced transparency of the tax administration. These measures have also been rewarded by taxpayer willingness to fulfill legal obligations. Almost all of materials on tax laws and taxpayer education are available in Nepali language; some materials are also available in English.

Assessed dimension (iii): Existence and functioning of a tax appeal mechanism.
Rating: B. A tax appeals system of transparent administrative procedures is completely set up and functional, but it is either too early to assess its effectiveness or some issues relating to access, efficiency, fairness or effective follow up on its decisions need to be addressed.

Justification for Rating

The Income Tax Act 2001, Value Added Tax Act 1995, Custom Act 2007, and Excise Act 2001 allow taxpayers to appeal for administrative reviews, when the revenue administration disagrees with the self-assessed tax liability. In addition, the taxpayers can also appeal decisions of the tax officer on Income Tax, VAT, and Excise to the IRD Director General.

An independent Revenue Tribunal chaired by a judge from the Court of Appeals has been established under Revenue Tribunal Act 2031. Tax appeal cases have doubled to 1,570 in FY13 from 760 in FY11. The decision rate (judgment dispensed) is about 23 percent of cases that are registered each year. The taxpayer has the recourse to appeal at the Supreme Court if not satisfied with the verdict of the Tribunal. In such a case, the Supreme Court may direct the Tribunal to re-evaluate the judgment. However, most tax appeal decisions are not made promptly, and this causes the taxpayer's payments to remain tied up for long periods of time.

PI- 13 Summary							
Summary	**Evidence**	**Rating**	**Method**	**Framework requirement**	**Information source**	**Rating in 2008**	**Reasons for change since 2008**
PI-13 (i)	Value Added Tax Act 2052 (1995)and Value Added Tax Rules 2053 (1996); Income Tax Act 2058 (2001) and Income Tax Rules 2059 (2002); and Customs Act 2064 (2007) and Customs Rules 2064 (2007); Excise Act 2058 (2001) and Excise Rules 2059 (2002); Income Tax Directives 2066 (2009), Value Added Tax Directives 2069 (2012), Excise Tax Directives 2068 (2011), Customs Tax Directives 2065 (2008) and Rent Tax Directives 2068 (2011); as well as Annual Reports of Inland Revenue Department and Custom Department all clearly exhibit the comprehensiveness and clarity of legislations and procedures. The discretionary power of government officers too is totally controlled by the law.	A	M2	Laws and procedures for all major taxes are comprehensive and clear, with strictly limited discretionary power for the government entities involved	Tax laws and rules, annual reports of IRD and Customs Department, and Directives of Income Tax, VAT, Excise and Custom Tax.	C	The laws and rules have been improved to make things clear; the discretionary power of tax administration has been controlled.
PI-13 (ii)	Tax laws and rules, directives, procedures, tax calculators, brochures, circulars, FAQs are available on departmental websites. Citizen's Charters are displayed at all revenue offices. Taxpayer education programs – workshops, seminars, interactions, etc. are being organized regularly. Facilitators and Taxpayer Service Offices have been established. The information flow is broad and comprehensive.	A	M2	Taxpayers have easy access to comprehensive, user friendly and up-to-date information on tax liabilities and administrative procedures for all major taxes, and the government supplements this with active taxpayer education campaigns.	Tax and revenue laws, annual reports of departments, information and directives available in the websites of the departments	C	Acts and Rules are made available on the websites. Taxpayer Service offices have been established. Facilitators as well as help counters also help to ensure information flow.
PI-13 (iii)	Revenue Tribunal, Administrative Review Committee and Tax Evaluation Review Committee have been established.	B	M2	A tax appeals system of transparent administrative procedures completely set up and functional, but it is either too early to assess its effectiveness of some issues relating to access, efficiency, and fairness or effective follow up on its decisions need to be addressed.	The records of decisions of Review Committees established under Income Tax Act, Value Added Tax Act, Excise Act and Custom Act. The review records of Inland Revenue Department and Revenue Tribunal.	B	

PI-14: EFFECTIVENESS OF MEASURES FOR TAXPAYER REGISTRATION AND TAX ASSESSMENT

Scoring Method: M2

Rating PI14: A

> ***Assessed dimension (i): Control in the Taxpayer Registration System***
> ***Rating: B.*** Taxpayers are registered in a complete database system with some linkages to other relevant government registration system and financial sector regulations.

Justification of Rating

A nine-digit Permanent Account Number (PAN) has been in operation since 1999. In 2014, 1.2 million people had this unique taxpayer identification (Table 3.11). Tax laws clearly state that every taxpayer should mention their PAN withal turnovers to related government agencies, its enforcement is weak. A system of automatic provisional PAN is provided to all new businesses once they register for business at the Office of the Company Registrar. The Inland Revenue Department is connected to the Company Registrar's Office through a dedicated Internet line; when a new business is registered, this data is automatically transmitted to IRD, which promptly provides a provisional PAN to the applicant. The client receives business registration certificate along with the PAN. With enforcement of PAN on the coverage side, tax revenue collection has improved substantially. Encouraged by this initiative, plans are underway to link PAN to the services provided by Land Tax Office on land and house registrations, Department of Transport Management on vehicle registration, and Kathmandu Municipality on house plan registration for construction. With enforcement of PAN at these service areas, non-tax revenue collection is expected to increase with comprehensive linkages to government registration system facilitating monitoring and enforcement of financial sector regulations.

Table 3.11: PAN registration records up to FY2014

Account name	Number of registrants
VAT	133,299
Income Tax	686,173
Personal PAN	433,093
TOTAL	1,252,656

Source: IRD

> ***Assessed dimension (ii): Effectiveness of penalties for non-compliance with registration and declaration obligations***
> ***Rating: A.*** Penalties for all areas of non-compliance are sufficiently high to act as deterrents and are consistently administered.

Justification of Rating

Penalties for non-compliance included in the tax laws and penalties are on a higher side. For example, Income Tax Act 2001 states, "a taxpayer who doesn't comply to the tax laws are penalized with a fine up to 100 percent fine."Similarly, the Value Added Tax Act 2052 (1995) states, "taxpayer, who is found guilty of non-compliance of VAT tax law during market monitoring and tax assessment, will be penalized with a fine up to NRs.10,000 every time. And if the taxpayer is found guilty of tax evasion, he/she will be penalized up to 100 percent fine." Likewise, the Excise Act 2058 states, "taxpayer's goods can be detained and held in custody for non-compliance". For non-compliance to Customs Act 2007, the taxpayer can be penalized up to 200 percent as fine and even be imprisoned.

A Separate Revenue Investigation Department has been established under the Revenue Leakage (Investigation and Control) Act 1995 and a Post-Clearance Audit Office has been set up under the Custom Act 2007. These offices investigate tax evasion. The IRD prepares an annual plan for tax assessment and investigation for implementation. The IRD investigated 373 tax evasion cases in FY12 and determined NPR 1.75 billion as payables (tax and fines). In FY13 it investigated 737 cases and determined NRs 2.09 billion as payable.

> ***Assessed dimension (iii): Planning and Monitoring of Tax Audit and Fraud Investigation Programs.***
> ***Rating: A.*** Tax audits and fraud investigations are managed and reported on accordingly to a comprehensive and documented audit plan, with clear risk assessment criteria for all major taxes that apply self-assessment.

Justification of Rating

Annual work plan is prepared for to undertake the number of tax audits and investigations of self-assessed tax statements. Annual targets for tax audit and fraud investigation are set for all offices. Taxpayers are selected on the basis of potential risk of non-compliance. Different indicators guide the identification of such risks.

The numbers of tax audits have increased four-fold and, based on these audits, tax collection has increased by three folds in the span of three years (Table 3.12).

Table 3.12 : Tax audits and revenue collection

SN	Year	Number of cases	NRs			
			Income	VAT	Excise	Total
1	2011	1,513	1.93	0.38	0.05	2.37
2	2012	3,255	3.31	1.25	0.11	4.68
3	2013	4,115	6.15	1.13	0.06	7.33

Source: IRD

PI-14 Summary

Summary	Evidence	Rating	Method	Framework requirement	Information Source	Rating in 2008	Reasons for change since 2008
PI-14 (i)	The record of taxpayers with PAN remains intact in IRD central database system. Every taxpayer is registered with a nine- digit PAN. The work to establish linkages with other government agencies is just beginning.	B	M2	Taxpayers are registered in a central database system for individual taxes, which may not be fully and consistently linked. Linkage to other registration/ licensing functions may be weak but are then supplemented by occasional surveys of potential taxpayers.	Directive published by IrD, directives and notices on website.	C	Expansion and scope coverage of PAN.
PI-14(ii)	Legal action is taken against taxpayers not included in the tax system according to the provisions of penalties in the Value Added Tax Act 2052 (1995), Income Tax Act 2058 (2001), Excise Act 2058 (2001) and Custom Act 2064 (2007), and on the basis of the report of tax audit, fraud investigation and market monitoring.	A	M2	Penalties for noncompliance generally exist, but substantial changes to their structure and levels of administration are needed for real impact on compliance.	The provisions of tax laws and statements and data provided by IRD in FY13.	C	Many taxpayers who did not participate in tax system were penalized according to Value Added Tax Act. This action has increased the criteria of tax and tax participation.
PI-14 (iii)	The work plan of selecting taxpayers on the basis of potential risk of noncompliance and tax audit existed in accordance with the provisions of the laws, annual reports of departments, and the information provided by IRD.	A	M2	Tax audits and frauds investigations are managed and reported on according to a comprehensive and documented audit plan, with clear risk assessment criteria for all major taxes that apply self-assessment.	IRD annual reports of 2068 (2011), 2069 (2012) and 2070 (2013). The numbers of tax audit and fraud investigations according to the documents provided by Custom Department. The number of post-clearance audits and revenue earned by them.	B	The indicators for risk identification are set. The tax audit and investigation are carried out on the basis of annual work plan.

PI-15: EFFECTIVENESS IN THE COLLECTION OF TAX PAYMENTS

The scale of tax arrears represents laxity in the enforcement of tax rules and weakness in its systems and process effectiveness. Large tax arrears denote elements of dysfunctional tax structure and are an opportunity cost missed in funding planned investment. In Nepal, the scale of reported tax arrears is large and its management is weak partly due to the judicial arrangements to dispense tax appeal cases.

Scoring Method: M1
Rating PI-15: D+

Assessed dimension (i): Collection ratio for gross tax arrears, being the percentage age of tax arrears at the beginning of a fiscal year, which was collected during the fiscal year (average of the last two fiscal years).
Rating: D. The debt (arrear) collection ratio in the most recent year was below 60 percent and the total amount of tax arrears is more than 2 percent of total annual collection.

Justification of Rating

Systems for identifying arrears, recording and auditing are in place but enforcement of arrears collection is weak. The record of tax collection and arrears is placed in the Central Database System (software database) segregated by major tax streams and is updated annually. The OAG carries out the annual audit of these arrears and submits the report to the legislature. Although tax offices are given annual targets to collect arrears and such targets are included in their performance indicators, the aggregate outstanding is on the rise (Table 3.13). One reason for the rise of arrears, among many, is the practice of carrying forward cumulative arrears, many of which are more than two decades old. The OAG reported outstanding cumulative government revenue arrears of NPR102.88 billion in its 2012/13 report – this was 34.8 percent of the total collection.

Table 3.13: Tax arrears

	Tax arrears in NRS in billions	
OAG Report	**Cumulative**	**Annual**
2013	102.88	9.71
2012	93.17	29.86
2011	63.31	10.41
2010	52.90	19.97
2009	32.93	

Source: OAG 2013 report.

An Arrears Settlement Evaluation and Monitoring Committee was formed twice to settle old arrears but failed to reach a meaningful conclusion in settlements. In the absence of opening balance of arrears, it is difficult to estimate what was realized during the fiscal year other than through derived means, as noted above. There is no data on actual collection of opening arrears for each of the last two years, but it is evident from the rising trend of arrears that the collection ratio is very low.

Assessed dimension (ii): Effectiveness of transfer of tax collections to the Treasury by the Revenue Administration.
Rating: B. Revenue collections are transferred to the Treasury at least weekly.

Justification of Rating

As per the provision of Article 4 of the Financial Procedures Act 2055, taxpayers deposit the payable tax amount directly at accounts at Central Bank and/or its dedicated accounts maintained at the commercial banks. The law allows a minimum of two days to complete this transaction. With the implementation of the TSA, revenue collection is reconciled and collection reported through the NRB's weekly Central Treasury reports denoting that collected revenue was deposited into the Treasury account within a week.

Most revenue collected is deposited directly to the bank for revenue accounts and is transferred to the Treasury on a daily basis, with few exceptions. Revenues collected through banks are recorded daily by DTCOs on receiving statements. These data are reconciled daily with the banks, and monthly with the tax or revenue collection offices. There are some lapses in the transfer of revenue collected to the Treasury the same day resulting from revenue collected by diplomatic missions, after office closes, distance between the revenue offices and the nearest bank, and negligence of a few tax offices. The latter is a weakness in enforcement.

Assessed dimension (iii): Frequency of complete accounts reconciliation among tax assessments, collections, arrears records and receipts by the Treasury.
Rating: D. Complete reconciliation of tax assessments, collections, arrears and transfers to Treasury does not take place annually OR is done with more than 3 months' delay.

Justification of Rating

Tax collected is deposited into the revenue accounts maintained at the Central Bank and/or the designated commercial banks. In the absence of an effective system that records (a) assessed tax dues, (b) collections received, and (c) outstanding balance of tax accounts, the reconciliation of the three processes is minimal. This has made aggregate reconciliation of tax accounts difficult. This has perpetuated the practice of reporting aggregate numbers in terms of assessment dues, revenue collected, and arrears, with little effort and incentive to clear arrears at the transaction level.

PI-15 Summary

Summary	Evidence	Rating	Method	Framework requirement	Information source	Rating in 2008	Reasons for change since 2008
PI-15 (i)	FY2013 OAG report.	D	M1	The debt collection ratio in most recent year was below 60% and total amount of tax arrears is significant (i.e., more than 2% of total collection.)	Annual reports 2068 (2011) and 2069 (2012) of the OAG.	D	
PI-15(ii)	Financial Procedures Act sets a 2-day time limit for revenue to be deposited to the Treasury account. While this provision is adhered to, a few administrative units deposit the revenue collection only within a week.	B	M1	All tax revenue is paid directly into accounts controlled by the Treasury and all transfers to the Treasury are made daily, with a few exceptions.	Financial Procedures Act 2055 (1998) and Financial Administration Rules 2056 (1999).	B	TSA system is employed. Almost all revenue offices have the facility for taxpayer to deposit tax through a bank.
PI-15 (iii)	Financial Procedures Act 1998 and Financial Administration Rules 1999 require that the account reconciliation of revenue should be done. But the account reconciliation between data recorded in Central Database System and the revenue collected in Treasury is not completed within 3 months from the end of the fiscal year.	D	M1	Complete reconciliation of tax assessments, collections, arrears and transfers to Treasury does not take place annually or is done with more than 3 months delay.	Financial reports and annual reports published by respective departments.	D	

PI-16: PREDICTABILITY IN THE AVAILABILITY OF FUNDS FOR COMMITMENT OF EXPENDITURES.

Effective execution of the budget, in accordance with the work plans, requires that the spending MDAs receive reliable information on fund availability that they can spend for recurrent and capital inputs. This indicator assesses the extent to which the Ministry of Finance provides reliable information on fund availability to MDAs that manage administrative (or program) budget heads (or votes) in the central government budget and therefore are the primary recipients of such information. The MDAs referred to in this indicator are the same as those concerned in indicator PI-11.

Scoring Method: M1
Rating PI-16: C+

> ***Assessed dimension (i): Extent to which cash flows are forecast and monitored.***
> ***Rating: C.*** Cash flow forecast is prepared for the fiscal year but is not (or partially and infrequently) updated

Justification of the Rating

The Operational TSA System Guidelines 2011 states monthly allocation of appropriation (i.e., OAG Form 20) should be prepared after receiving the letter of authorization, the annual program is approved, and annual procurement plan completed and agreed upon. Upon completion of this process, a copy of this information is sent to the District Treasury Offices at the beginning of the new financial year. However, in practice, at the beginning of the year, a consolidated cash flow forecast is prepared for the fiscal year and is part of the budget document submitted to the Parliament. Because most programs are finalized after submission of the budget to the parliament, the submitted cash flow projection is at best an estimate.

In the absence of a mechanism to provide a consolidated cash flow statement, much less a forecast, reconciliation of cash position still remains an issue. In-year reconciliation of government operation is weak and the IMF is planning technical assistance to forecast cash flows at the request of the Government.

> ***Assessed dimension (ii): Reliability and horizon of periodic in-year information to MDAs on ceilings for expenditure commitment***
> ***Rating: B.*** MDAs are provided reliable information on commitment ceilings at least quarterly in advance.

Justification of the Rating

MDAs are provided reliable information on commitment ceilings at least quarterly in advance. MDAs are assured of the availability of budget and fully authorized in advance to spend based on the approved programs. They are well informed within 15 days of the start of the new fiscal year. The MTEF prioritization criteria have enabled MDAs to plan and commit expenditure for (at the least) four months in advance. Priority one projects (80 plus of total budget) are assured one-third of funds from the approved budget on the very first day of the fiscal year and expenditure funds are replenished on the day statement of expenditure is submitted to the DTCOs. Likewise, priority two and three budget lines are assured one-sixth or an amount equal to two months of the approved budget value. This practice is anchored by the Financial Procedures Regulations 2007.

Section 32 of the Financial Procedures Regulations 2007 states that after the enactment of the Appropriation Act, the Finance Secretary will send the budget statements and authorization letter to the secretaries of ministries, and the secretaries of ministries will send to department and offices similar authorization letters, approved programs, sources of expenditure, and detailed line items within 15 days of receipt of MoF authorization. Upon enactment of the Appropriation Act by Parliament, a statement of programs and projects with the ceiling of the budgeted amounts (the Red Book) is issued simultaneously. The Red Book providesMDAs with reliable indication of actual resources available for commitment more than four months in advance.

> ***Assessed dimension (iii): Frequency and transparency of adjustments to budget allocations, which are decided above the level of management of MDAs.***
> ***Rating: C.*** Significant in-year adjustments are frequent, but undertaken with some transparency.

Justification of the Rating

There are transparent legal provisions for adjustment and virement from one budget heading to another and one source of financing to another. Article 95 of the Interim Constitution has provision for supplementary budget estimates. The Minister for Finance presents to the Legislature-Parliament a supplementary estimate, either the sum authorized for spending for a particular service by the Appropriation Act for the current financial year is insufficient, or a need has arisen for expenditures on some new service not provided for by the Appropriation Act for that year, or that the expenditures made during that financial year exceed the amount authorized by the Appropriation Act. Likewise, Article 99 of the Constitution also governs matters relating to the transfer of monies appropriated by the Act from one head to another and other financial procedures are governed by law according to Article 99 of the Constitution.

Section 8 (Transfer of budget) of the Financial Procedures Act 1999 states that if the amount under any heading specified in the Appropriation Act is not sufficient and such a shortfall is surplus under any one or more than one heading specified in that Act, the Ministry of Finance may transfer the budget from one heading to another subject to the ceiling specified in the Appropriation Act (not exceeding more than 10 percent). The provisions relating to the transfer of budget under subheadings is prescribed in the Financial Procedure Rules 2007. Section 40(3) of the Financial Procedure Rules 2007 allows government secretaries or department heads to transfer amounts not exceeding more than 25 percent of the budget subheading to which the amount is to be transferred from other subheadings. Likewise, the DTCOs can transfer funds within the recurrent and capital expenditures of the budget when directed by the FCGO.

However, in practice, there are substantial levels of virement, and the scale of this activity increases during the last trimester of the fiscal year, especially on the capital account side. In FY13 a staggering NRs 52.521 billion was transferred from 236 budget subheadings to 514 sub-heading. This alone was 13 percent of the FY13 expenditure. On the capital side, virement was 32 percent of capital expenditure (according to the 2013 OAG report). The OAG report also noted that 497 new programs were added through the contingency budget headings. The same report also states that excess expenditure was made in 28 budget heads—NRs 9.88 billion or 3.3 percent of FY13 expenditure. Budgetary discipline is weakened when 70 percent of capital expenditure is done during the last trimester, and, more specifically, during the last month of the fiscal year. The scale of virement and bunching of expenditure during the last trimester alludes to the fact that although budget transfer is anchored and done within the rules and regulations that govern such transfers, the in-year budget transfer is significant.

PI-16 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
PI-16	C+			C+	
Line ministries prepare pro-forma cash flows at start of each fiscal year and also prepare monthly pro-forma cash flows, however these are updated only when there is a significant deviation from anticipated expenditure	C	(i) A cash flow forecast is prepared for fiscal year and is updated monthly on basis of actual cash inflows and outflows.	District Treasury Offices, finance officers of major spending agencies	C	Change in this rating was caused by the implementation of TSA system all over the country
There are provisions of authorization guidance letters from MoF and FCGO to MDAs along with the ceiling of budgeted amount (Red Book) after promulgation of Appropriation Act; increasing trend on revenue collection and more predictability and transparency in foreign aid mobilization have increased the reliability and horizon of information on ceiling for committing expenditure.	B	(ii) MDAs are provided reliable information on commitment ceilings at least quarterly in Advance.	MoF, District Treasury Offices, finance officers of major spending agencies	B	No change
Signification-year virement.	C	(iii) Significant in-year adjustments to budget allocations take place only once or twice in a year and are done in a transparent and predictable way.	MoF, District Treasury Offices, finance officers of major spending agencies	C	No change

PI-17: RECORDING AND MANAGEMENT OF CASH BALANCES, DEBT AND GUARANTEES.

Fiscal space knowledge or lack thereof is an important element of overall aggregate fiscal management. This information is best addressed when a country operationalizes an effective debt management system and has processes in place to plan, issue, and monitor debt dynamics and issuance of debt instruments prudently. One important element of monitoring of a country's debt dynamics is the system and processes in place for debt management. Monitoring of debt determines how well the country manages borrowing. Nepal's debt-to-GDP ratio is lowest in the region as a result of prudent fiscal policy implementation supported by functional debt management processes.

Scoring method: M2
Rating PI-17: C+

> ***Assessed dimension (i): Quality of debt data recording and reporting.***
> ***Rating: C.*** Domestic and foreign debt records are complete, updated, and reconciled annually. Data quality is considered fair, but some gaps and reconciliation problems are recognized. Reports on debt stock and service are produced annually (occasionally) or with limited content.

Justification of the Rating

The MoF Economic Affairs and Policy Analysis Division is responsible for debt management. This is done in coordination with the NPC, NRB, and FCGO and other divisions. The NRB Open Market Operation Committee, with representation from the MoF, NRB, and FCGO, manages the issuance of internal debt instruments, both timing and type. Debt records and transaction records (payment and issuances) are updated regularly and reconciled at least once in a year.

The FCGO keeps the records of debt data that is complete and is made public in the Economic Survey annually. Stock and operations are covered in monthly NRB economic data, while debt service is covered at the FCGO's FMIS. The FCGO is responsible for recording of external debt operation, repayment of domestic and external debts, and preparing a consolidated financial statement on public debt operations. The NRB is entrusted with responsibility of managing domestic borrowings. The NRB Public Debt Management Department is responsible for issuing and accounting of domestic debt in compliance to the Public Debt Act 2002 for raising funds in accordance with the Appropriation Act provisions. The NRB maintains accounts of detail transactions on domestic debt and its liabilities.

The use of the Commonwealth Secretariat Debt Recording and Management System was discontinued in 2004. Thereafter, all debt data have been entered and updated manually in Excel worksheets, a process weakness that needs immediate correction to ensure data security. Since 2013, the FCGO has been using MS-Access to record debt data. As data recording is done manually, data security and reconciliation is an in-year issue. Donor technical assistance is now being provided to rectify the security of debt data recording. The identified software has management information capabilities.

> ***Assessed dimension (ii): Extent of consolidation of the government's cash balances.***
> ***Rating: B.*** Most cash balance are calculated and consolidated at least weekly, some extra-budgetary funds remain outside the arrangement.

Justification of Rating

The TSA is in operation. Cash balances are calculated daily with some lapses.[12] Major cash balances are calculated weekly and are reflected in the weekly Treasury Report that gives budgetary cash expenditure, revenues, foreign grant, loan, cash accounts of local authorities, and financing balance. However, off budget expenditure (estimated 18 percent for government and 36 percent for donor) is not part of Treasury reporting.

The TSA rollout has also enabled the Government to centralize the payment function at DTCOs and strengthened cash management by closing down 13,717 bank accounts. The system can now support the compilation of consolidated cash flow statements for individual ministries as well as for the central government. However, expenditure incurred by local bodies' from their own sources of revenue (about 2 percent of the total central revenue) and extra-budgetary expenses are still outside the TSA recording system.

Extra-budgetary funds are expected to be significant as there is over 10 percent of total expenditure whose exact figure is not known to the Government.

[12] Nearly14,000 bank accounts of 4,000 spending units have been closed, leaving 443 Treasury-managed bank accounts that are operated by 79 DTCOs.

Assessed dimension (iii): System for contracting loans and issuance of guarantees.
Rating: C. Central government's contracting loans and issuance of guarantees are always approved by a single responsible entity but are not decided on the basis of clear guideline, criteria, or overall ceilings.

Justification of Rating

The Interim Constitution states that "No loan shall be raised and guarantee given by the Government of Nepal except in accordance with law." The National Debt and Guarantee Act is the basis of borrowing and is amended at the beginning of the fiscal year. During annual budget preparation, the Resource Committee (comprising the NPC chairman, NRB Governor, and the Finance Secretary) recommends the annual debt ceiling (external and internal). A debt bill (along with the appropriate bill, estimate of revenue) has been presented to the Parliament for approval. However, there is no organic budget/debt law on debt ceiling. Currently, the Government is preparing a Fiscal Responsibility and Budget Management Act that is expected to recommend overall debt ceiling.

The Economic Affairs and Policy Analysis Division coordinates the overall debt strategies and operations in coordination with the NPC, NRB, FCGO, and other divisions. Therefore, the Ministry of Finance approves all contracting of loans and issuance of guarantees. The Foreign Aid Policy 2002 restricts any form of external guarantee: "{government will}…not guarantee foreign loans for government-owned or other institutions." Additionally, the NRB Act 2002 has also made provisions for extending overdraft to Government not exceeding 5 percent of preceding fiscal year's revenue. This has to be repaid within 180 days.

Although the rules and regulations governing contracting of loans and issuance of guarantee are clear, enforcement remains an issue. According to Clause 4(1) of the Credit and Guarantee Act 2025 the Government of Nepal can provide guarantee only in case of government development projects and to purchase new aircraft for the Nepal Airlines Corporation. As per the decision of the Government, it had provided guarantee to the Nepal Oil Corporation of NRs5 billion (NPR 1 billion from the *Karmachari Sanchaya Kosh* or Employees Provident Fund, and NPR4 billion from the *Nagarik Lagani Kosh* or the Citizens Investment Trust). Accounting documents show that Government has made NPR 18.8 billion available to the Nepal Oil Corporation as of January 2013. The money came from the aforementioned two institutions. Si milarly, the Government has not realized principal and interest, which amounts to NRs 2.4 billion provided to 25 different organizations, including the *Gorakhkali Rubber Udyog*. According to the existing law, the Government is not allowed to provide guarantee to these organizations.

PI-17 Summary

Evidence used	Rating	Framework requirement	Information source	Rating in 2008	Explanation of change since 2008
Domestic and foreign debt records maintained by dedicated unit at FCGO are complete, updated, and reconciled annually. Data quality is fair. Some gaps and reconciliation problems are observed. Reports on debt stock and servicing are published annually.	C	Domestic and foreign debt records are complete, updated, and reconciled at least annually. Data quality is considered fair, but some gaps and reconciliation problems are recognized. Reports on debt stock and service are produced only annually with limited content.	MOF, FCGO, Central Bank.	C	No change in performance.
Cash balances are calculated and consolidated at least weekly. Extra-budgetary funds remain outside the arrangement.	B	Most cash balance are calculated and consolidated at least weekly, some extra-budgetary funds remain outside the arrangement.	Treasury, Finance officer of major spending agencies.	B	TSA implemented. No change in performance.
Government contracting loans and issuance of guarantees are always approved by single responsible entity but are not decided on the basis of clear guideline, criteria, or overall ceilings	C	Central government contracting loans and issuance of guarantees are always approved by single responsible entity but are not decided on the basis of clear guideline, criteria, or overall ceilings.	MoF (Debt Management Department) and Central Bank.	C	No change in performance.

PI-18: EFFECTIVENESS OF PAYROLL CONTROLS (SCORING METHOD M1)

Often weak management of the wage bill, usually one of the biggest items of government expenditure, leads to the financial hemorrhaging of the Treasury. Effective control of the payroll system strengthens sound financial management. Payroll management is underpinned by personnel database system that is dynamic in nature and has the capability to capture evolving personnel information. Four dimensions capture the status of payroll management.

Scoring method: M1
Rating PI – 18: C+

Assessed dimension (i): Degree of integration and reconciliation between personnel records and payroll data.
Rating: C. A personnel database may not be fully maintained, but reconciliation of the payroll with personnel records takes place at least every six months.

Justification of the Rating

The payroll expenditure is managed by FCGO. Responsibility for personnel records of civil service management (recording, updating, and changes) rests with designated departments: (a) Department of Civil Personnel Records,(b) Department of Teachers Personnel Records,(c) Department of Police Personnel Records, and (d) Office of Army Personnel Records the Department of Civil Personnel Records. These four departments report to the concerned ministries. This is near 100 percent record of central government employees but not for all government-owned organizations.

All personnel records are stored electronically. Different employee recruitment streams require management of individual databases, but there is no inter-linkage. Payroll data, personnel records, and personnel database of the recruitment streams are yet to be electronically linked to a central repository or control system. Re-conciliation (manual) of these data bases are undertaken three times a year: (a) at the time of passing the salary report, (b) at the time of budget preparation, and (c) at the time of internal and external audit. But stiller-conciliation issues exist. Budget appropriation is based on posts rather than on verification of employees at work, and this has created discrepancies in cash management. To mitigate this issue, at the Ministry of Education, personnel records and payroll data of teachers are reconciled once every four months (while releasing budget to the school management committees). This has helped to effectively control a large component of the payroll cost. However, there are lapses in payroll reconciliation of teachers funded through the *Rahath quota* and Per Child Fund-funding sources. Both modes of salary payment, bank transfer (in urban areas), and cash (in remote areas) are used.

According to a 2014 OAG report, the recording of teacher payments through conditional and unconditional grants remains an issue.

Assessed dimension (ii): Timeliness of changes to personnel records and the payroll.
Rating: B. Up to three months delay occurs in updating changes to the personnel records and payroll but affects only a minority of changes. Retroactive adjustments made occasionally.

Justification of Rating

The DTCO audits payroll data of central government employees each month, and OAG audits these records annually. Although personnel and payroll data are not directly inked, payroll is supported by full documentation of all personnel and checked against the previous month's payroll data. All promotion, transfer, and rewards are bought to the notice of record keeping agencies and account sections of concerned offices. Once the information is updated, payroll change is recorded, account sections are notified of the changes, and transaction is rechecked at the time of payment of the next month's salary. The duration for completing any status change is less than one month in urban areas and less than three months for personnel working in the rural areas. As reported by the OAG, retroactive adjustment is rare, maximum of 3 percent of salary payment.

Assessed dimension (iii): Internal controls of changes to personnel records and the payroll.
Rating: C. Controls exist but are not adequate to ensure full integrity of data

Justification of Rating

The Good Governance Act defines the role of secretary, minister, and other authorities regarding transfer, compensation, and other personnel management activities. The Ministry of General Administration undertakes management audits annually on changes of personnel records, and this process is followed for staff transfer decision-making. Although this audit activity acts as a system of checks and balances in personnel management, full integrity of payroll data is far from complete because it does not have an audit trail, and also because enforcement of rules and regulations are at best weak.

Assessed dimension (iv): Existence of payroll audits to identify control weakness and/ or ghost workers.

Rating: C. Partial payroll audits or staff surveys have been undertaken within the last three years.

Justification of Rating

In general, payroll of every employee is verified and certified by the Personnel Records Department of the civil service; concerned records keeping departments of the army, police, and teachers; and DTCOs. Internal audit is also done. Spending units make monthly checks, and OAG does the final audit. However, there is no physical verification, and such verification activity is limited to book data reconciliation.

An annual, full complete payroll audit is not done, but audit of the payroll has taken place in the last three years. The DTCO carries out internal payroll audits once a month, and OAG audits the records. These two audits control the "double dipping" to a large extent. But lapses in reconciliation of the process, especially for contract (temporary) worker records and the weak verification process, has resulted in a few "ghost workers", the scale of which is minimum compared to total civil service strength of nearly half million.

PI-18 Summary				**Rating in 2008**	**Explanation of changes since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Overall Rating PI-18	C+			C+	
Each employee gets a personal ID with the first appointment and changes in personal profile are updated regularly. Payroll of each month is verified with the salary report, transfer order, and other changes. However, reconciliation problems do exist for lack of integration of the personnel database and payroll every month.	C	(i) A personnel database may not be fully maintained, but reconciliation of the payroll with personnel records takes place at least every six months.	Auditor General, Treasury Controller, MoGA, Department of Education, Hydropower Project Development Committee, Department of Civil Personnel Records, Department of Police Personnel Records, Department of Teacher Personnel Records, District Education Office, Banke and Kailali, Audit Report 2069, PSC Annual Report 2069, Education Information Report 2014.	C	
Personnel records are updated after receiving authorized letter of changes in personnel profile from the government offices. Letters in transit may create reconciliation problem.	B	(ii) Up to three months delay occurs in updating changes to the personnel records and payroll but affects only a minority of changes. Retroactive adjustments made occasionally	Auditor General, Treasury Controller, MoGA, Department of Education, Hydropower Project Development Committee, Department of Civil Personnel Records, Department of Police Personnel Records, Department of Teacher Personnel Records, District Education Office, Banke and Kailali, Audit Report 2069, Annual Report 2069 PSC, Education Information Report 2014.	B	No change

PI-18 Summary				Rating in 2008	Explanation of changes since 2008
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Personnel records are maintained, according to civil service law, jointly by record keeping agencies, ministries, and the office concerned. However, there is a different system and basis for keeping personnel records. Authority and basis for changes to personnel records and the payroll are clear and are checked in the management audit	C	(iii) Controls exist but are not adequate to ensure full integrity of data.	Auditor General, Treasury Controller, MoGA, Department of Education, Hydropower Project Development Committee, Department of Civil Personnel Records, Department of Police Personnel Records, Department of Teacher Personnel Records, District Education Office, Banke and Kailali, Audit Report 2069, Annual Report 2069 PSC, Education Information Report 2014.	C	No change
Personnel records are verified.	C	(iv) A payroll audit covering all central government entities is partially conducted, but there is no physical verification.	Auditor General, Treasury Controller, MoGA, Department of Education, Hydropower Project Development Committee, Department of Civil Personnel Records, Department of Police Personnel Records, Department of Teacher Personnel Records, District Education Office, Banke and Kailali, Audit Report 2069, PSC Annual Report 2069, Education Information Report 2014.	B	Change.

PI-19: TRANSPARENCY, COMPETITION AND COMPLAINTS MECHANISMS IN PROCUREMENT

This indicator was revised in 2011 and now contains four dimensions. While the procurement system operates within its own framework, it benefits from the overall control environment that exists in the PFM system, including public access to information, internal controls operated by implementing agencies, and external audit. The procurement system also contributes to many aspects of the PFM system, providing information that enables realistic budget formulation, providing access to information to stakeholders that contribute to public awareness and transparency, and supporting efficiency and accountability in delivery of government programs. (The following indicators impact on or are influenced by procurement: PI-4, PI-10, PI-12, P-20, PI-21, PI-24, PI-26 and PI-28).

Scoring method: M 2
Rating PI-19: B

> ***Assessed dimension (i): Transparency, comprehensiveness, and competition in the legal and regulatory framework.***
> ***Rating: B.*** The legal framework meets five of the six listed requirements.

Justification of the Rating

The Public Procurement Act (2007) and Public Procurement Rules (2007) regulate public procurement. The Act (clause 64) establishes the Public Procurement Monitoring Office and defines its functions and powers. The PPMO functions directly under the Office of the Prime Minister and Council of Ministers. Different laws and rules require the PPMO to ensure that all public procurement takes into account the principles of (a) an open, transparent, objective, and competitive procurement, and (b) "obtain the maximum returns of public expenditures in an economical and rational manner by promoting competition, fairness, honesty, accountability and reliability in public procurement processes," Public Procurement Act"

The legislation and regulation are easily available online (both in Nepali and English), and printed copies can be purchased at a minimum cost in various bookstores across Nepal. Additionally, any public document must be available to the public by the Right to Information Act. The PPMO has a well-functioning website.

The regulatory framework applies to all procurement carried out by a public entity (defined in Section 2b of PPA). PPA (clause 3) clearly states that any procurement contrary to the PPA provisions will become null and void. After the enforcement of the PPA/PPR all procurement-related regulations and bylaws have been amended to comply with PPA/PPR provisions.

The situations where procurement methods (other than open domestic competition) may be used are specified in the law and its regulations. For example, sections 15 and 41 of PPA provide guidance on the international bidding and direct procurement in detail, respectively.

The PPA also provides for public access to procurement information in relation to bidding opportunities, contract awards and government procurement plans, and data on the resolution of procurement complaints. Bidding opportunities and contract awards are publicly accessible while government procurement plans are not. This benchmark has not been met.

An independent Procurement Review Committee, as provided by PPA (sections 47, 48), has also been established.

Assessed dimension (ii): Use of competitive procurement methods.
Rating: D. For less than 60 percent of the value of the contracts awarded or reliable, data is not available.

Justification of Rating
Open competition is clearly identified by the PPA as the default method. Clause 9 states that "Public entity making any procurement shall, to the extent possible, make by inviting open bids, and provide equal opportunity to qualified bidders to participate in such procurement process without any discrimination." Section 8 discourages piecemeal procurement by stating: "in making procurement pursuant to this Act and the rules framed under this Act, procurement shall not be so made in piecemeal as to limit competition." However, several OAG reports have stated that this practice of slicing procurement into smaller packages in order to avoid the open bidding thresholds is still widely prevalent.

When direct procurement method is selected, public entity has to provide justification and clarification as stated in the Section 41 of PPA. Furthermore, departure from a competitive process or direct procurement has to be approved by the Cabinet (Section 41).

The OAG report on FY2013 states that only 8.46 percent of procurement is done through less competitive methods and the rest on a competitive basis.

At its initiative, FCGO independently completed a sample study of selected districts on the mode of procurement and concluded that 88.77 percent of procurement at the sampled districts was through the open competitive method and only 11 percent under direct procurement. However, this dimension is rated D since there was insufficient data to determine the value of contracts awarded other than by open competition, and the percentage of such contracts were legally justified.

Table 3.14: Procurement competition

Method	Sample ministries	No. of contracts	Amounts (billion)	%
Open competition	21	5,139	22.92	91.56
Piecemeal	13	729 pieces	0.81	3.23
Direct procurement (limited competition)	19		1.31	5.23
Total			25.01	100

Source: OAG report on FY2013, paras.63-65. Note that OAG shows that 5,139 is the total number of contracts. 'Piecemeal' is where contracts are split to bring them under the threshold to avoid competitive tendering.

Assessed dimension (iii): Public access to complete, reliable and timely procurement information.
Rating: C. At least two of the key procurement information elements are complete and reliable for government units representing 50 percent of procurement operations (by value) and made available to the public through appropriate means.

Justification of Rating

Key procurement information, except procurement plans, is disseminated through a variety of means in a timely manner, for example:

- Tender or pre-qualification is published in a daily newspaper of national circulation; in the case of an international tender, it is published in international media.
- Notice on request for sealed quotation is published in a newspaper with local or national circulation.
- Solicitation of bids is published on the website of the concerned entity in the case of a central-level public entity or the PPMO; and in case of a district-level public entity, such notice may be placed on the website of that entity or the PPMO.

Publication of opportunities provides sufficient time—consistent with the method, nature, and complexity of procurement—for potential bidders to obtain documents and respond to the advertisement. Currently, there are 32 different portals under various government entities to publish information on procurement of national and international goods, works, and services. It is reported that these multitude of sources of information cover 75 percent of total procurement. Such may not be the case in announcing contract awards. The PPMO is now trying to combine all these portals into a one-stop portal. Data on procurement complaints is published in the annual report of PPMO.

Assessed dimension (iv): Existence of an independent administrative procurement complaints system.
Rating: A. The procurement complaints system meets all seven criteria.

Justification of Rating

The Public Procurement Act has a formal complaints or appeals mechanism (Clauses 48 through 51) and meets criteria (ii) and three of the other five criteria under review.

The Public Procurement Review Committee is a requirement of the law that also defines its functions. The committee comprises a chair and two members. The chair is drawn from the pool of former judges of the Appellate Court and one member from the pool of retired first-class officers of the Engineering Service of the Government of Nepal. Although PPA does not specify members shall be drawn from the private sector and civil society, it does state that one member should be a public procurement expert. The Committee members should not be holding a post in any public entity or be involved in any kind of procurement activity. The Committee does not charge any fee; but 0.5 percent of the total procurement value must be deposited for the review process. The fee is refundable in the complaint is justified but is forfeited if the complaint is dismissed. The law spells out clear procedures for reviewing complaints with a timeframe for appeals by the bidders, and decision-making by the Review Committee. The Committee has the authority to suspend the procurement process and issues decision within the required (30 day maximum) time period. Its decisions are binding on all parties.

As per the record made available by the Public Procurement Review Committee, there were 22 complaints registered and reviewed in FY13. Thirteen decisions were made in favor of the procuring entities. Decisions made by Review Committee are published in the annual PPMO reports.

Dimension	PI-19 Summary			Rating in 2008	Explanation of change since 2008
	Rating	Framework requirement			
Overall P-19	B			D	
(i)Transparency, comprehensiveness and competition in the legal and regulatory framework	B	The legal and regulatory framework for procurement should:		Not comparable	Not comparable. The new methodology uses 4 dimensions, instead of 3, and is more comprehensive. The major reform since 2006 has been the passage in parliament of PPA2006 embodying a comprehensive set of international good procurement practices. This became effective from FY08. The PPA/PPR as a modern procurement law with provisions in line with UNCITRAL model law is in place and in practice. Master Procurement Plan and Annual Procurement Plan as provisioned in law are not available in public at large.
		be organized hierarchically, and presence is clearly established	✓		
		be freely and easily accessible to the public through appropriate means	✓		
		apply to all procurement undertaken using government funds	✓		
		make open competitive procurement the default method of procurement and define clearly the situations in which other methods can be used and how this is to be justified	✓		
		provide for public access to all of the following procurement information: government procurement plans, bidding opportunities, contract awards, and data on resolution of procurement complaints	×		
		provide for an independent administrative procurement review process for handling procurement complaints by participants prior to contract signature	✓		
(ii) Use of competitive procurement methods	D	Open competitive method as a default. Electronic bidding.		Not comparable	(ii) OAG report shows that most of procurement is done by using open competition and electronic bidding in large procurement entities, DoR, DoI, DoLLIDAR etc., but no information on legitimacy of non-competitive contracts.
(iii) Public access to complete, reliable, and timely procurement information.	C	Bidding opportunities, contract awards, and data on resolution of procurement complaints are made available to the people and it comprises of more than 75% of the procurement operations.			
(iv) Existence of an independent administrative procurement complaints system	A	Complaints are reviewed by a body that:		Not comparable	Not comparable. The new methodology uses 4 dimensions, instead of 3, and is more comprehensive. The major reform since 2006 has been the passage in Parliament of the PPA 2006 embodying a Comprehensive set of international good Procurement practices: this became effective from FY 2008. An independent Procurement Review Committee is in place and reviewing the complaints.
		• is comprised of experienced professionals, familiar with the legal framework for procurement and includes members drawn from the private sector and civil society as well as government;	✓		
		• is not involved in any capacity in procurement transactions or in the process leading to contract award decisions;	✓		
		• does not charge fees that prohibit access by concerned parties;	✓		
		• follows processes for submission and resolution of complaints that are clearly defined and publicly available	✓		
		• exercises the authority to suspend the procurement process;	✓		
		• issues decisions within the timeframe specified in the rules/regulations	✓		
		• issues decisions that are binding on all parties (without precluding subsequent access to an external higher authority).	✓		

PI-20: EFFECTIVENESS OF INTERNAL CONTROLS FOR NON-SALARY EXPENDITURE.

A country needs an effective internal control system in operation for managing risks to ensure value-for-money spent. Rules and regulation also need to be enforced and changed only for genuine reasons to leverage public investment to development outputs. That such a system is in place must be evident from reports – internal and external audits or other surveys – carried out by budget managers. One such indicator of an effective control system is how well non-salary expenditure is managed, starting with control of expenditure commitments and including managing of expenditure arrears that result when payment obligations mismatch the projected cash availability.

Three dimensions are rated under the evaluation of this indicator: (i) effectiveness of expenditure commitment controls; (ii) comprehensiveness, relevance, and understanding of other internal control rules/ procedures; and (iii) degree of compliance with rules for processing and recording transactions.

Scoring Method: M2

Rating PI-20: C

Assessed dimension (i): Effectiveness of expenditure commitment controls.

Rating: C. Expenditure commitment control procedures exist and are partially effective, but they may not comprehensively cover all expenditure or they may occasionally be violated.

Justification of Rating

There are clear, legal provisions [Constitution, Article 9; Financial Procedure Act, Section 5, Financial Procedure Regulations (FPR) 2007] and systems and processes (Resource Committee, MTEF, Budget, Budget Authorization, and the release process) to guide and to enforce budget commitment controls. The DTCOs release funds only after ensuring that all due diligent documents are tallied and are in conformity to the rules of budget release procedures. Implementation of the TSA and its status report, and weekly Treasury reports assist budget implementers in ensuring that release orders match with cash availability. The DTCOs are expected to keep records of cash estimate on the basis of Ma.Le.Pa.Form-20.Section 35(2) of FPR 2007 states that, "any expenditure should be incurred only if there is an approved budget and balance to cover the expenditure amount". The OAG 2014 report states that 28 budget heads had expenditure above the allocation; this is 3 percent of fiscal year expenditure. While this alludes to presence of laxity in expenditure commitment control, the above situation is the result of virement undertaken, within economic codes and at project level, within a ministry matching the changing implementation environment on the ground. There is no record of any line ministries' expenditure that is above budget ceiling – the hard budget constraint set for all individual line ministries.

Assessed dimension (ii): Comprehensiveness, relevance and understanding of other internal control rules/procedures

Rating: C. Other internal control rules and procedures consist of a basic set of rules for processing and recording transactions, which are understood by those directly involved in their application. Some rules and procedures may be excessive, while controls may be deficient in areas of minor importance.

Justification of Rating

Rules and procedures under FPR 2007; procurement rules, operational guidelines, and norms prepared by the Ministry of Finance; and respective control rules and procedures in health, education, physical infrastructure, and local development sectors developed by MDAs govern internal controls and procedures of budget execution. But the enforcement is weak. Various OAG reports suggest developing and implementing internal control systems that contribute to improve fiscal discipline and to reduce fiduciary risks.[13] The 2014 OAG report states, "There is a general trend of not complying with the provisions

[13] OAG report, 2010(pages 11 and 450); OAG report, 2011(pages 13, 14 and 452); and OAG report, 2012(pages 13 and 425).

stated in rule (95) 1 of the FPR 2064 (2007) as most of the concerned ministries/departments have not prepared and implemented internal control systems, concerned ministries/departments have not undertaken inspection and monitoring, salary reports have not been passed and the procurement plan was not prepared. The internal audit conducted by the DTCO has not been effective."

Assessed dimension (iii): Degree of compliance with rules for processing and recording transactions.
Rating: C. Rules are complied with in a significant majority of transactions, but use of simplified, emergency procedures in unjustified situations is an important concern.

Justification of Rating

There is compliance in most transactions and a breach of rules is an offence. A committee led by the Chief Secretary monitors progress made on the recommended actions to be taken in the OAG report. OAG recommendations on issues of weak controls, despite being addressed, have not produced the desired results. The scale of irregularities is on the rise, in absolute terms, but is on a decline as a percentage of the audited amount. The 2014 OAG report cites areas where controls have been circumvented in relation to (a) compliance of law, (b) revenue leakages and control, (c) procurement, and (d) contract management

PI-20 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Overall PI-20	C				
Commitments for all expenditure categories are registered in the accounting system: this incorporates comprehensive controls that limit expenditure commitments according to cash availability (conformity with budget allocations and availability).	C	Expenditure commitment control procedures exist and are partially effective, but they may not comprehensively cover all expenditure or they are occasionally violated.	Financial Procedure Act 2055, Financial Administration Regulation 2064, Public Procurement Act and Public Procurement Regulation, LSGA2055, Local Self Governance Regulation 2056, Local Bodies Financial Administration Regulation 2064; OAGN Annual Reports 2067, 2068, and 2069; MOF records; FCGO records related to commitment controls and internal audit.	C	No change.
Internal controls are implemented through rules/regulations and FMIS, including all execution stages. There are many formal procedures/ manual to disseminate and communicate internal control rules, and the DTCOs (IAA) are considering checking its effectiveness.	C	Other internal control rules and procedures consist of basic set of rules for processing and recording transactions, which are understood by those directly involved in their application. Some rules and procedures may be excessive while controls may be deficient in areas of minor importance.	As above.	C	There is some progress in formulating controlling rules but not sufficient enough to affect the rating.
The existing control mechanisms are understood and followed in most transactions. However, occasionally simplified procedures are used without further justification.	C	Rules are complied with in a significant majority of transactions, but use of simplified, emergency procedures in unjustified situations is an important concern.	As above.	C	No change

PI-21: EFFECTIVENESS OF INTERNAL AUDIT

Under the PI-21, the assessment focus is provision of regular and adequate feedback to management through an internal audit function, which will ultimately evaluate the performance of the internal control systems and support promotion of good governance. To fulfill this objective, the internal audit function should meet international standards such as the International Standards for the Professional Practice in Internal Audit. The following arrangements and processes are expected for assuring effectiveness of internal audit:

- Appropriate structure (particularly with regard to professional independence);
- Sufficient breadth of mandate (access to information and power to report);
- Use of professional audit methods (including risk assessment techniques).

Scoring Method: M1
Overall Rating PI-21: D+

Assessed dimension (i): Coverage and quality of the internal audit function.
Rating: D. There is little or no internal audit focused on systems monitoring.

Justification of Rating

The coverage of internal audit is 100 percent, but there is still a question on the quality of reports. Even though a clear set of professional internal audit standard does not exist, the internal audit manual covers many critical aspects of those standards. There is a very little focus on systemic issues.

The FCGO through the DTCO is responsible for internal audits. The internal audit sections of the district development committees and municipalities are responsible for auditing all local development funds in local bodies. The coverage of internal audit is 100 percent. There is a separate account sub-group in the civil service of internal auditors who work at DTCO. Under current legal provision, DTCO should perform internal audit of revenue, expenditure, deposits, and other funds of all government offices. The internal audit also covers all financial transactions and their processes, target achievement, and use of financial resources. The DTCO prepares a report on the financial transaction status. The current auditing practice, scope, and coverage is insufficient to cover all systemic issues. It is enough for checking numeric and arithmetic errors, verifying the accuracy of transactions, and preparing the treasury report. The OAG report states that other systemic issues (especially in achieving result, checking effectiveness of internal control system, and efficient use of financial resources) are not addressed properly.

Assessed dimension (ii): Frequency and distribution of reports.
Rating: C. Reports are issued regularly for most government entities, but may not be submitted to the Ministry of Finance and the supreme audit institution.

Justification of Rating

There is clear requirement that DTCO should audit every 4 months and distribute its reports. As per the requirement, reports are to be issued regularly for all government entities. But in practice, reports are issued annually but not tri-semester. The reports are submitted to the supreme audit institution but not to Ministry of Finance.

There is no separate internal audit standard, but the regulation and guidelines list the subject areas to be covered in detail with checklists and reporting formats for checking standards of different financial activities. In FY13/14,FCGO began publishing the internal audit report.

Assessed dimension (iii): Extent of management response to internal audit findings.
Rating: D. Internal audit recommendations are usually ignored (with few exceptions).

Justification of Rating

DTCO reports to respective expenditure units, and respective unit mangers are requested to implement recommendations in the report. But follow-up is rare. The OAG report states that there is weak follow-up for tracking implementation of the recommendations. There is no information on actions taken by managers.

PI-21 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
Overall PI-21	D+			D+	
Coverage of auditing is 100%, which cover all financial transaction and its process, achievement of targets; utilization of financial resources in efficient, economic, and effective way; checking the internal control system within organization; and presenting actual report of financial transaction. As per provision, current auditing practice is not enough to cover the all systematic issues. It is mainly successful in checking numeric and arithmetic errors, verifying the accuracy of transaction, and preparing treasury position. OAG reports have stated that other systematic issues (especially in achieving result, checking effectiveness of internal control system, and efficient use of financial resources) are not addressed properly. There is no separate internal audit standard but the regulation and guidelines have mentioned subject areas to be covered in detail with checklists, reporting format, and checking standards of different financial activities for internal audit purpose.	D	Coverage and quality of the internal audit function.	Financial Procedure Act2055, Financial Administration Regulation 2064, Local Self Governance Act 2055, Local Self Governance Regulation 2056, Local Bodies Financial Administration Regulation 2064; OAGN Annual Reports 2067, 2068, and 2069; MOF records; FCGO records related to commitment controls and internal audit.	D	No change.
Internal audit reports are issued to audited entity and their concerned ministry and department. It is also sent to OAG and FCGO. The reports are not sent to MoF. The compiled internal audit report is published by FCGO. It has started to share suggestions with concerned line ministries and central agencies. The report should have been produced each trimester, which is not the case. It is done annually in most cases.	C	Frequency and distribution of reports.	As above	C	No Change.
DTCO reports to respective expenditure units and the manager is required to address the suggestions. The manager needs to take action on suggestions of the internal audit, and supervising agencies are required to monitor and take actions as needed. The OAG report states tracking of implementation is weak. There is no information on actions taken by managers.	D	Extent of management response to internal audit findings.	As above	D	Although, It is almost impossible to ignore the recommendation provided by the managers, there is little evidence of follow up.

3.5 ACCOUNTING, RECORDING AND REPORTING (PI-22-25)

This framework ensures that adequate records and information are produced, maintained, and disseminated to meet decision-making control, management and reporting purposes. Four indicators (PI-22-25) are assessed in this part of the framework.

PI-22: TIMELINESS AND REGULARITY OF ACCOUNTS RECONCILIATION

This indicator assesses the timeliness and reconciliation of government accounts to ensure the functioning of internal control and its foundation for good quality information (data reliability) availability to management. This assessment is also about minimizing any material differences held in various government accounts and the use of suspense accounts.

Reconciliation of accounts is being enforced after the introduction of the TSA and material evidence difference is under control to a large extent. Material differences do exist as a result of difference in coverage such as the omission of grants and direct payments by donors from the FMIS/TSA.

Scoring Method: M2
Overall Rating PI 22: C+

Assessed Dimensions (i): Regularity of bank reconciliations.
Rating: C. Bank reconciliation for all Treasury-managed bank accounts takes place quarterly, usually within eight weeks of end of quarter.

Justification of Rating

A total of 1,988 treasury-managed accounts are in use (of which, 81 percent are denoted as miscellaneous accounts).With the implementation of TSA system in FY2013, a single bank account (expenditure, revenue, deposit and other) for all spending units is operated by DTCOs. The accounts are maintained at government-approved banks and its branches (130 units). The DTCOs perform "day close" function and send daily reports to NRB for account settlement. On the expenditure side, besides check-issued amount not being cashed, there was no other material difference. Issues of wrong labeling of source of fund have been addressed as per due diligence guidelines. On the revenue accounts, "material differences" are settled subsequently in the following month. The origin of material differences in the revenue account can be largely categorized under the following: (a) wrong label of tax stream, (b) wrong label of tax office location, (c) human error in data feeding, and (d) laxity in enforcement on follow-up taking longer in reconciliation of material differences. To mitigate these identified issues, the Government has initiated the rollout of the Revenue Management Information System at large tax collection offices to daily reconcile these differences that are picked up by the system to not wait for end of the month to initiate reconciliation activities.

Assessed dimension (ii): Regularity of reconciliation and clearance of suspense accounts and advances.
Rating: B. Reconciliation and clearance of suspense accounts and advances take place at least annually within two months of end of period. Some accounts have balances brought forward.

Justification of Rating

Reconciliation and clearance of suspense accounts are in practice. There are clear provisions for settlements of advances in the accounting as per FPR 2007. There is no particular provision for suspense accounts (items that are temporarily held pending final disposition) in government accounting. The FPR 2007 has a provision for offices to settle advances within 21 days from the date of receipt of the statement along with bills and vouchers. There has been a noticeable improvement in management of advances following the introduction of TSA with the enforcement of rules by DTCOs, which manage records of advances of OAG Form-22. Based on this record the operating units are required to submit details of outstanding advances in the prescribed format (OAG form-14) every month to concerned DTCO and line ministries/departments. While submitting accounts of the last month of every fiscal year, the responsible person submits a statement of the advance outstanding for that FY and the previous FY, description of the advances whose time-limit for settlement has expired, and those accounts for which time limit has not expired. The submission also includes detailed records and reasons to the concerned ministries/departments.

There are processes to limit overdue advances: Bank cash book (OAG form-5);monthly statement of expenditure (OAGform13);statements of advances outstanding (OAG form-14);annual financial statement (OAG form-17);central statement of outstanding advance(OAG-204);annual financial statement, including foreign resource (OAG form-208);central financial statement of Government resource (OAG-209);central financial statement, including foreign resource (OAG form-210);brief financial and performance report(OAG-211); and expenditure statement, including foreign resource (OAG form-213). The enforcement of these forms has yielded positive outcomes, and reconciliation of accounts is undertaken within two months of FY-end. Advances outstanding at year-end are carried forward by the last voucher and brought forward by the first voucher during the next fiscal year in the bank cash book.

Of the total outstanding advances at the end of FY2013, only 7.5 percent have crossed the time limit for settlement (FMIS, FCGO).[14] The Auditor General's Annual Report 2014 showed38 percent as outstanding advances from the total irregularities at the time. The time expired irregularities were 7.5 percent, and those with time for settlement were 19.5 percent.

PI-22 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
Overall PI-22	C+			C+	Reconciliation issues.
There are issues in reconciliation of revenue accounts while reconciliation of expenditure accounts are done as per schedule. Data generated by FCGO system, monthly, quarterly and year-end reports are verified.	C	(i) Bank reconciliation for all Treasury-managed bank accounts takes place quarterly, usually within eight weeks of end of quarter.	FCGO (statistics analysis, IT, and treasury sections of FCGO), past PEFA assessor, DTCOs, operating units, FPR2007	B	Lax management oversight on enforcement of reconciliation of accounts on the revenue side, partial fulfillment.
Suspense accounts are not maintained in government accounting. FPR 2007 has clear provision for taking and clearing the outstanding advances. Clearance of advances takes place regularly on the basis of prescribed period.	B	(ii) Reconciliation and clearance of suspense accounts and advances take place at least annually within two months of end of period. Some accounts have uncleared balances brought forward.	FCGO (statistics analysis, IT, and treasury section of FCGO), past PEFA assessor, DTCOs, operating units, FPR2007.	C	FPR 2007 has clear provision for taking and clearing the outstanding advances. Likewise various advance-related OAG Forms (No. 5, 13,14,17,208, 209, 210, 211, and 213) have been amended so that outstanding advances are clearly distinguished between time-limit and other not exceeded.

[14] 2013 Consolidated Financial Statement reports – 3.37% as outstanding advance of actual expenditure.

PI-23 AVAILABILITY OF INFORMATION ON RESOURCES RECEIVED BY SERVICE DELIVERY UNITS

Front-line service delivery units are often reported to face difficulties in securing approved appropriation of funds. Timely availability of appropriated funds denotes effectiveness of the PFM systems in place. Besides accounting information, timely capture of relevant information facilitates correction measures to leverage output from the use of public resources. Such informed decision-making can facilitate the provision of basic services through front-line service providers.

Scoring method: M1

Dimension (i): Collection and processing of information to demonstrate the resources that were actually received (in cash and kind) by the most common front-line service delivery units (focus on primary schools and primary health clinics) in relation to the overall resources made available to the sector(s), irrespective of which level of government is responsible for the operation and funding of those units.

Rating PI-23: A. Routine data collection or accounting systems provide reliable information on all types of resources received in cash and in kind by both primary schools and primary health clinics across the country. The information is compiled into reports at least annually.

Justification of Rating

Expenditure data is regularly collected from the service delivery units. The primary schools and primary health clinics receive resources from District Education Office and District Health Office and are recorded at district offices. These offices collect data, in kind and cash, monthly in health sector and trimesterly in the education sector.

In the health sector, Logistics Management Information System (LMIS) collects information of all supplies on a monthly basis. This software-backed information collection was introduced in 2009, and its reports are electronically available and inform the status of medicine supplies to the District Public Health Service, region, and centers. These reports are available in the public domain within 7 days of the next month.[15] In addition, a separate inventory status report is also available on the website. Since the last two decades, the Health Management Information System (HMIS) has been in operation to capture qualitative health information on 38 indicators. These reports are then compiled every month to produce a monthly central report and are used for decision-making by health workers, program managers, and directors.

Similarly, the Education Management Information System (EMIS) compiles education-related expenses and supplies on a trimester basis. In addition, through social audits, Parent-Teacher Associations monitor the functioning of community-managed schools every trimester (one third of total schools). These reports are then submitted to Department of Education for necessary corrective steps, if so recommended. These reports are mandatory for the release of funds to the school. In addition to social audits, it is also mandatory to submit financial audits of the previous year expenditure to release current fiscal year, third-trimester funds of the current fiscal year. To corroborate the data supplied and what is in practice, in 2013 an education Public Expenditure Tracking Survey (PETS) was completed to inform the education decision-makers of the status of education sector.

PI-23 Summary				Rating in 2008	Explanation of change since 2008
Evidence Used	**Rating**	**Framework requirement**	**Information sources**		
PETS undertaken by NPC in 2012 and again under School Sector Reform Program in 2013. All expenditure (cash and in-kind) data routinely recorded.	A	(i) Collection and processing of information to demonstrate the resources that were actually received (in cash and kind) by the most common front-line service delivery units (focus on primary schools and primary health clinics) in relation to the overall resources made available to the sector(s), irrespective of which level of government is responsible for the operation and funding of those units.	Department of Health, District Health Office, District Education Office , Primary School	C	Improved coverage and MIS systems in place (HMIS, LMIS, IMS has developed) incl. special surveys undertaken.

15 www.dohslmd.gov.np

PI-24 QUALITY AND TIMELINESS OF IN-YEAR BUDGET REPORTS

In-year budget execution information facilitates informed corrections during implementation. However, for this to happen systems and processes must be in place to generate budget execution (commitment to expenditure) information in real time that is both dependable and of substance. Three dimensions of this indicator assess the status of in-year budget reports.

Scoring method: M1
Overall Rating PI-14: C+

Assessed dimension (i): Scope of reports in terms of coverage and compatibility with budget estimates.

Rating: C. Comparison to budget is possible only for main administrative headings. Expenditure is captured either at commitment or at payment stage (not both).

Justification of Rating

The system (classification side) allows direct comparison to the budget. However, the system is unable to depict commitments on a monthly basis.

Government prepares and submits budget request electronically through the Line Ministry Budget Information System (LMBIS). The FCGO produces daily budget execution reports through the TSA/FMIS. Synchronization of the BMIS and FMIS databases has enabled systems to generate budget execution data by functions, administrative, and economic heads. The TSA helps to generate real-time cash expenditure by all three categories. This information has enabled budget managers to make informed decisions on budget execution, and therefrom make necessary in-year implementation changes. The following data is available on the FCGO website: (a) daily budgetary status, (b) monthly ministry expenditure status and burn rate, (c) monthly ministry and economic head cumulative expenditure and current monthly expenditure by economic classification, (d) monthly district-wise budget execution (cumulative and current month expenditure), and (e) yearly consolidated financial statement.[16] In addition to these reports, Central Bank produces weekly Treasury position, and MoF Revenue Division produces monthly revenue collection that has information on target achievement, monthly collection, and collection rates of all major taxes. These reports assist budget managers to make mid-year budget corrections. Such statements are announced through the mid-year budget review, which includes, in addition to expenditure reports, the physical monitoring assessment of priority projects/programs.

The current system is short in coverage of commitment. The system is weak in reporting outstanding commitments and/or the uncommitted balance reported/shown on monthly reports. To address this, a pilot program is underway; if proven effective, this program will be mainstreamed in the next fiscal year.

Assessed dimension (ii): Timeliness of the issue of reports.
Rating: A. Reports are prepared quarterly or more frequently and issued within 4 weeks of end of period.

Justification of the Rating

As noted above, there are systems and processes in place to generate daily aggregate expenditure report, monthly ministry-wise functional and economic head expenditure reports, and weekly treasury reports. The monthly reports are made available on the website no later than 7 days into the new month. Dedicated lines reporting the expenditure status (daily and monthly reporting of expenditure against commitment by charts of accounts under administrative and functional classifications against budget codes) are made available to designated persons (MoF budget division, NPC Vice Chairman, OAG, and secretaries of selected line ministries) thus facilitating informed decisions. The Ministry of Finance implements mid-year budget corrections through its midterm review report, data of which is generated from FMIS and substantiated by field reports on implementation status of national priority projects.

Assessed dimension (iii): Quality of information
Rating: B. There are some concerns about accuracy, but data issues are generally highlighted in the reports and do not compromise overall consistency/ usefulness.

16 http://www.fcgo.gov.np/report-publications/

Justification of Rating

There are no serious material concerns on data integrity and accuracy. Sometimes there are minor data errors. Barring few issues in the GFS classification that reports lower levels of capital expenditure, the quality of information is accurate. Reconciliation issues, identified under PI-24, are the result of coverage and process issues but in no way hamper decision-making. Since FMIS records actual transaction-level data and no fund is released/authorized without submission of previous expenditure report, there is no materially significant issue about data reported by the ministries.

PI-24 Summary

Evidence Used	Rating	Framework requirement	Information sources	Rating in 2008	Explanation of change since 2008
The current system is short in coverage of commitment. The system is weak in reporting outstanding commitments and/or uncommitted balance reported/shown on monthly reports. To address this, a pilot program is underway; and if proven effective, this program will be mainstreamed in the next fiscal year.	C	Classification of data allows direct comparison to the original budget. Information includes all items of budget estimates. Expenditure is covered at both commitment and payment stages.	FCGO, DTCO, line ministries, MoF	C	Synchronization of BMIS and FMIS databases has enabled systems to generate budget execution data by functions, administrative and economic heads. With the implementation of TSA, real-time cash expenditure can be generated by all three categories. This information has enabled budget managers to make and take informed decision on budget execution. It also allows them to make necessary in-year budget implementation changes. But, the system is short in coverage of commitment.
Reports are produced every month within 7 days of the close of the month. After TSA rollout, daily reporting system with timely information is available in the FMIS.	A	Reports are prepared quarterly or more frequently, and issued within 4 weeks of end of period.		A	No Change in performance
Government reports are now generated from FMIS. Reconciliation of check issued and cashed can be done on a daily basis.	B	There are some concerns about accuracy, but data issues are generally highlighted in the reports and do not compromise overall consistency/ usefulness.		C	Significant improvements in bank reconciliations have been achieved through TSA system. At the district level it is done on daily basis, and at the Central Bank it is done monthly. That is why it is providing more accurate data. FMIS generates central report with help of the TSA system in real time.

PI-25 QUALITY AND TIMELINESS OF ANNUAL FINANCIAL STATEMENTS

The quality of annual financial statements depends on the process of preparation, ERP software in DECS, and accounting principles/standards used by the Government. Consolidated annual financial statements are prepared by using DECS in each DTCO; such reports from all 75 districts are consolidated by the FCGO. The same annual financial statements are also prepared manually and compiled at each ministry and consolidated again at the FCGO level. Both manual and system-generated annual financial statements are reconciled by FCGO for any errors, omissions, and other clerical errors before sending them to OAG.

Scoring Method: M1
Overall Rating PI-25: C+

> ***Assessed dimension (i): Completeness of the Financial Statements***
> ***Rating: C.*** A consolidated government statements is prepared annually. Information on revenue, expenditure, and bank account balance may not always be complete; but the omissions are not significant.

Justification of Rating

The Government is using cash basis of accounting for the purpose of preparing annual financial statements covering expenditure and revenue under single financial statements. Financial statements of government-owned entities, especially public enterprises, are prepared separately annually. The FCGO loan section generates a total liabilities report, and this data feeds into the annual Economic Survey. The recording of asset information is not yet mainstreamed, but asset record-keeping is practiced in selected departments of a few ministries. While data is recorded and accounts are generated, the Government has yet to compile whole-of-the-government accounts or consolidated financial statements in accordance with Nepal Public Sector Accounting Standards (NPSAS), based on International Public Sector Accounting Standard (IPAS) 1.6, which requires consolidation of the transactions of controlled entities, in part, financial cash reporting. This has not yet happened.

> ***Assessed dimension (ii): Timeliness of Submission of the Financial Statements***
> ***Rating: A.*** The statements are submitted for external audit within 6 months of the end of the fiscal year.

Justification of Rating

The Financial Procedure Act 2055 and FPR 2064 require the annual financial statements to be prepared within 6 months from FY-end. The FCGO is responsible for compiling and submitting the consolidated annual financial statements to the OAG. For FY12/13, FCGO submitted the annual financial statements to OAG within 6 months from the FY-end (mid-January 2014).

> ***Assessed dimension (iii): Accounting standards used***
> ***Rating: C.*** Statements are presented in consistent format over time with some disclosure of accounting standards.

Justification of Rating

The NPSAS, based on IPSAS, was developed by the Accounting Standards Board, Nepal, in FY2009/10 and was approved by the Cabinet on September 15, 2009 (2066/5/30). However, the standard is not used for preparing the annual financial statements. The Government piloted the NPSAS in two ministries in FY14. All ministries, DTCO, and entities prepare consolidated financial statements when using OAG form no. 13 (Statements of Expenditure), no. 14 (Statements of Advances), no. 15 (Statements of Bank Accounts), no. 9 (Statements of Revenue), and no. 17(Annual Financial Statements).

PI-25 Summary					
Evidence Used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
The Government uses cash basis of accounting for preparing annual financial statements covering expenditure and revenue of the budget under single financial statements. The recording of asset information is not yet mainstreamed.	C	A consolidated government statement is prepared annually. Information on revenue, expenditure, and bank account balances may not always be complete; but the omissions are not significant.	Statistical Analysis Section of FCGO	C	No change in performance but Government has introduced software called Public Asset Information System, but it is yet to be mainstreamed.
Consolidated financial statement and the public accounts were submitted within the statutory 6 months after FY-end.	A	The statement is submitted for external audit within 6 months of FY-end.	Statistical Analysis Section of FCGO	A	No change.
NPSAS was developed in 2009. It is in the process of implementation – piloted in two ministries.	C	Statements are presented in consistent format over time with some disclosure of accounting standards.	Accounts Strengthening and Human Resource Section, FCGO	C	No change in rating. During this period NPSAS was developed and approved by Government in 2009.

3.6 EXTERNAL SCRUTINY AND AUDIT (PI-26-28)

This set of 3 indicators (PI-26-28) looks at the quality and timeliness of external scrutiny of the government's budget estimates as well as the public accounts.

PI-26: SCOPE, NATURE AND FOLLOW UP OF EXTERNAL AUDIT

A high-quality audit report strengthens judicious use of public resources and supports transparency in the use of public funds. This report must be comprehensive in coverage, adhere to international audit standards, and focus on transaction levels as well as systemic PFM issues. The audit report should provide comfort that financial statements as a function of internal control and procurement systems, including public institutions' performances, are in line with accepted good practice approaches. In Nepal, external audit reports have substantially improved in quality and coverage, especially the FY13 OAG report. This report is a milestone in PFM reform; but there is room for improvement in the follow-up of audit recommendations.

Scoring Method: M1
Overall Rating PI-26: C+

Assessed dimension (i): Scope/nature of audit performed (including adherence to auditing standards).
Rating: B. Central government entities, representing at least 75 percent of total expenditures, are audited annually, at least covering revenue and expenditure. Wide-ranging financial audits are performed and generally adhere to auditing standards, focusing on significant and systemic issues.

Justification of the Rating
The OAG was constitutionally established in 1959. The Constitution mandates auditing of accounts, all budgetary and extra-budgetary funds, of all government offices and government-owned autonomous agencies. The full scope of government auditing includes the following with regularity: attestation of financial statements of the audited entities, evaluation of entity's compliance or noncompliance with applicable statutes and regulations, audit of internal control and audit functions, and audit of the probity and propriety of administrative decisions taken within the audit entity. In addition, OAG undertakes

Table 3.15: Number of different types of audit carried out by the OAG (NPR Million)

Table PI-26- Number of different types of audit carried out by the OAG (NPR Million)							
S.No	**Entity**	**2012/13**		**2011/12**		**1010/11**	
		Number of Identity	**Audit Amount (Rs.)**	**Number of entity**	**it Amount**	**Number of Entity**	**Audit Amount**
1	Financial Audit	4770		4589		4441	
	Government Office	3708	742,594	3796	527,561	3655	467,375
	Corporate Body	88	971,790	69	7,787	72	759,660
	Board and other organisation	901	82,116	649	37,348	639	32,355
	Distinct Development Committee	73	68,159	75	31,850	75	30,757
2	Performance Audit	27		23		16	
	IT Audit	4		2		0	
	Environment Audit	1		0		0	
	Total	**4802**	**1,844,660**	**4614**	**604,546**	**4457**	**1,290,147**

Source: Annual report of the OAG

selected performance audits and has expanded its activities to IT and environment audits.

The audits cover 95 percent of total expenditures of Government offices and more than 90 percent of the autonomous bodies, development committees, district development committees, and other organizations (Table 3.15).

INTOSAI Fundamental Principles (INTOSAI Standards) are Nepal's audit standards that have been adapted to meet the country's need. INTOSAI significantly upgraded the auditing standards to be followed by SAIs since the last assessment in 2008. For instance, new detailed auditing guidelines, particularly for the audits of financial statements, were endorsed by the 20thINTOSAI Congress in 2010; and new fundamental auditing principles or auditing standards for financial, compliance, and performance auditing were endorsed by the 21st INTOSAI Congress in 2013. Since the Government has yet to prepare financial statements in accordance with a recognized financial reporting framework, auditing of financial statements is weak compared to the recognized international standards. The Government is piloting new procedures in SOAGP, but the coverage does not include all revenues and expenditures.

In 2012, OAG shifted to risk-based auditing from the traditional voucher-based approach. This move is expected to enhance audit effectiveness by focusing only on high-risk areas but thus allowing scarce personnel time to focus on priority areas. To enhance transparency and accountability, as provisioned by ISSAI 20, OAG publishes its mandate, responsibility, mission, vision, auditing standards, code of ethics, quality assurance procedures, directives, tools, and guides for its work and strategy on its website. Recently, the Auditor General commissioned an advisory committee, comprising an external expert and experienced persons, to enhance the quality and credibility of work of OAG. The preparation of a communication policy is underway. The OAG-developed auditing standards, guide, and directives are listed in Table 3.16.

Table 3.16: List of auditing standards, guidelines and directives developed by the OAG

	Published date (B.S.)
1. Audit Directives	2029/2047
2. Administrative Expenses Audit Guide	2052/2063 (2006)
3. Procurement Audit Guide	2052/2065 (2008)
4. Project Audit Guide	2052/2057 (2000)
5. Performance Audit Guide	2052/2063 (2006)
6. Revenue Audit Guide	2052/2063 (2006)
7. Government Auditing Standards	2053 (1996)
8. Government Audit Policy Standards	2063 (2006)
9. Government Audit Operation Guide	2063 (2006)
10. Code of Ethics for OAG Personnel	2056/2070 (2013)
11. Quality Assurance Handbook	2069 (2012)

Assessed dimensions (ii): Timeliness of submission of audit reports to legislature.
Rating: C. Audit reports are submitted to the legislature within 12 months of the end of the period covered (for audit of financial statements from their receipt by the auditors).

Justification of Rating

The Auditor General submits an annual report with observations and recommendations to the parliament through the president. Though legislation does not specify a time for annual reporting, OAG has been able to significantly reduce its reporting period from more than 12 months to within 9 months of the end of the period covered (for audit of financial statements from their receipt by the auditors). OAG submitted its last three annual reports within 9 months (Table 3.17). Similarly, OAG has significantly reduced the size of its report by including only matters specified in the Interim Constitution and other significant and systemic financial and management issues to make it user-friendly.

Table 3.17: Submission Schedule for Auditor General's Report

	2009/10	2010/11	2011/12
Date of submission to the president	April 13, 2011	April 11, 2012	April 11, 2013
Submission from FCGO to OAG	January 14, 2011	January 13, 2012	January 14, 2013

Assessed dimensions (iii): Evidence of follow-up on audit recommendations
Rating: C. A formal response is made, though delayed or not very thorough, but there is little evidence of any follow-up.

Justification of Rating

OAG submits its report to the parliament for corrective action through the president's office. The Financial Procedures Act requires OAG to conduct follow-up on the implementation of audit report observations and recommendations. As provisioned by the Financial Procedures Act 1998, the Irregularity Clearance Evaluation and Monitoring Committee formed under the chairmanship of Chief Secretary is responsible for follow-up. Other committee members are MoF Secretary, MoGA Secretary, Financial Comptroller General, and a person nominated by the Government. This committee has been working consistently to follow up on audit observations to clear audit observations / irregularities. There is a rewards system for those who comply, and corrective provisions for non-responders. The Public Accounts Committee also follows up on audit observations. Follow-up of irregularities is at about 50 percent of audit observations so there is room for improvement (Table 3.18). Enforcement of sanctions for non-clearance of irregularities can improve the current follow-up clearance status. Most efforts are concentrated on clearance of irregularities while system reform measures are weak.

With regard to performance, a separate follow-up audit is conducted to ensure that audited entities properly address the OAG observations and recommendations. The OAG is a constitutional body but facing weak follow-up of its recommendations by the PAC; a more meaningful follow-up of OAG recommendations is required for improving the overall PFM performance.

Table 3.18: Overall irregularity clearance status

	NRs million		
	Total irregularity amount	**Clearance amount**	**Percent cleared**
2012/13	32,843	14,363	43.73
2011/12	37,956	15,203	40.05
2010/11	45,194	20,938	46.33

Source: Irregularity Clearance Evaluation and Monitoring Committee Annual Report (2070)

PI-26 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Overall PI-26	C+			D+	Improvement in dimension (i); some improvements in dimension (ii) but not adequate improvement in dimension (iii) for higher-level rating.
In 2012/13 OAG performed financial audit of 4,670 entities covering all MDAs, autonomous government agencies, district development committees, and other organizations. The same year, 27 performance audits, 4 IT audits, and 1 environment audit were conducted. The audit covers more than 95% of total expenditures of government offices and more than 90% autonomous government agencies. The audit is conducted in accordance with INTOSAI Fundamental Principles. OAG has developed, published, and implemented auditing standards, guides, and directives that are in line with INTOSAI standards.	B	Central government entities representing at least 75% of total expenditures are audited annually, at least covering revenue and expenditure. A wide range of financial audits is performed and generally adheres to auditing standards, focusing on significant and systemic issues.	OAG	B	Improvement in adherence of auditing standards to some extent, but audit coverage remains same as previous assessment.
OAG submitted audit report to Parliament within 9 months after FY-end.	C	Audit reports are submitted to legislature within 12 months of end of period covered (for audit of financial statements from their receipt by the auditors).	OAG	D	OAG submitted its last three annual reports within 9 months of the end of period covered.
OAG has maintained records of preliminary audit report for the purpose of follow-up. In 2012/13 OAG approved the clearance of irregularities made by entities of NPR 20.588 billion out of NPR 89.164 billion.	C	A formal response is made, though delayed or not very thorough, but there is little evidence of any follow-up.	OAG	C	Timely and evidence-based response is made, and there is a regular mechanism for follow-up but focused on clearing irregularities rather than focusing on system reform.

PI-27: LEGISLATIVE SCRUTINY OF THE ANNUAL BUDGET LAW

The Constitution empowers legislature scrutiny over executive body on budget approval and its use. Four dimensions measure the effectiveness of the accountability of the government to the electorate.

Scoring method: D
Overall Rating PI-27: D

Assessed dimension (i): Scope of the legislature's scrutiny
Rating: D. The legislatures review is non-existent or extremely limited, or there is no functioning legislature.

Justification of Rating

There was no functioning legislature during the review period. The legislature's review covers details of expenditure and revenue but only at a stage where detailed proposals have been finalized.

The Constituent Assembly was dissolved on May 27, 2012; following a new election, newly elected lawmakers took oath of office on January 22, 2014. A 51-member PAC was constituted on April 20, 2014. The critical period for rating this indicator is FY12/13; so dimension (i) and the overall indicator "D" rating is based on actual practice, not the law, in FY12/13.

The annual budget is prepared under joint leadership of Ministry of Finance and National Planning Commission working with line ministries. The Finance Committee examines the budget allocated for various programs on the basis of priorities and submits its report, with recommendations, to Parliament. However, the scope of meaningful pre-budget discussion between the legislature and executive body is minimum. The Finance Minister presents the budget in Parliament for approval after Cabinet approval. The tabling of budget for parliamentary approval initiates the debate. In Nepalese parliamentary practice, any change in the budget amount is tantamount to vote of "no confidence"; hence, while there is a debate in Parliament, there is no change in the size of the allocation. Upon budget approval, the executive body does take into consideration genuine suggestions from the parliamentary debates and makes necessary changes to the content without breaching the ceiling.

Assessed dimension (ii): Extent to which legislature's procedures are well established and respected.
Rating: NA. No Parliament during the assessment period.

Justification of Rating

There are provisions for legislative review in the Interim Constitution, which sets overall guidance for the review. The Working Procedure Rule of Parliament has set detailed procedures for reviewing the appropriation and finance bills and other bills related to the budget. The Parliament reviewed the budget when it was in place. The legislative procedures for budget review are well established by law. There are various review committees in Parliament that examine the annual budget and submit recommendations. The recommendations submitted by the parliamentary committees are accepted after deliberation, and the budget is revised accordingly, if necessary. As there was no Parliament during the assessed period, the budget was implemented through presidential ordinance.

Assessed dimension (iii): Adequacy of time for the legislature to provide a response to budget proposals, for both detailed estimates and, where applicable, proposal on macro-fiscal aggregates earlier in the budget preparation cycle (with time allowed in practice for all stages combined).
Rating: NA. No Parliament during the assessment period.

Justification of Rating

There is no provision in the system for involving the legislature during the budget preparation cycle, and it has no role in reviewing the budget proposals. The time allowed for the legislature's review (about a month) is clearly insufficient for a meaningful debate. In FY13, the budget was announced as an presidential ordinance; after a new Parliament was elected, it passed the budget without any debate.

Assessed dimension (iv): Rules for in–year amendments to the budget without ex-ante approval by the legislature.
Rating: NA. No Parliament during the assessment period.

Justification of Rating
Clear rules exist for in-year budget amendments by the executive and are usually respected, but they allow extensive administrative reallocations.

There is a clear provision for a supplementary budget in the Interim Constitution.

The legislature reviews government policies that are the basis of annual budget preparation. With respect to rules for in-year budget amendments without exante approval by the legislature, the Finance Procedure Act has clearly defined the conditions under which the executive can amend the budget. It also specifies the limits on the extent and nature of the amendments. The Appropriation Bill sets a ceiling for adjustments: 10 percent of the budget. The Secretary and the Head of the Department have authority for virement up to 25 percent of the approved expenditure from one line item to another without affecting the approved programs. These rules are usually respected but administrative reallocation is large.

PI-27 Summary				**Rating in 2008**	**Explanation of change since 2008**
Evidence used	**Rating**	**Framework requirement**	**Information sources**		
Overall PI-27. Annual budget is prepared under joint leadership of MoF and NPC with the line ministries. Finance Committee examines the budget allocated for various programs on basis of priorities and submits its report with recommendations to Parliament. However, there is inadequate meaningful pre-budget discussion between the legislature and the executive body. Upon approval by the Cabinet, the budget is presented in Parliament for approval. The budget is approved after a discussion in Parliament	D	There was no functioning legislature.	Interim Constitution 2007, MoF, Parliamentary Secretariat Records.	C	Absence of Parliament in two of the three years of assessment period.
As there was no Parliament during the assessed period, the budget was announced through a presidential ordinance	NA	In the absence of a functioning legislature in FY13/14, this dimension does not apply.	Interim Constitution 2007, MoF, Financial Procedures Act 1998 and FPR 1999, and working Procedure Rules of Parliament. Parliamentary Secretariat.	D	Absence of Parliament in two of the three years of assessment period.
Budget for FY13/14 was implemented through an ordinance and was approved by the newly elected Parliament without debate.	NA	In the absence of a functioning legislature in FY13/14, this dimension does not apply.	MoF, Parliamentary Secretariat.	D	Absence of Parliament in two of the three years of assessment period.
With respect to rules for in-year budget amendments without exante approval by the legislature, the Finance Procedure Act has clearly defined conditions under which the executive can amend the budget; it also specifies the limits on extent and nature of the amendments.	NA	Clear rules exist for in-year budget amendments by the executive and are usually respected, but they allow extensive administrative reallocations.	MoF, Parliamentary Secretariat.	B	Absence of Parliament in two of the three years of assessment period.

PI-28 LEGISLATIVE SCRUTINY OF EXTERNAL AUDIT REPORT

The Public Accounts Committee exercises scrutiny over external audit reports. Its effectiveness is contingent on committee's skills mix and skills set. Three dimensions measure the legislative scrutiny of external audit report.

Scoring method: M1

Overall Rating PI-28: D

Dimension assessed (i): Timeliness of examination of audit reports by the legislature (for reports received within the last three years).
Rating: D. Examination of audit reports by the legislature does not take place or usually takes more than 12 months to complete.
Dimension assessed (ii): Extent of hearings on key findings undertaken by the legislature.
Dimension assessed (iii): Issuance of recommended actions by the legislature and implementation by the executive.
Rating for (ii) and (iii): NA.

Justification of Rating

In the absence of Parliament, there was no PAC during the review period. However, even during periods when Parliament was in session, discussions did not take place on the OAG reports. The last PAC discussion on the OAG report had taken place more than three years ago.

With regard to no assessment under dimensions (ii and iii), there was no parliament during the review period (FY013). But, when the Parliament was in session, the PAC spent reasonable amount of time on in-depth discussions on important issues flagged by the OAG report. Generally, the government implements the recommendations made by the legislature with few exceptions. In the absence of the Parliament, the executive formed a "follow-up" committee that reports to Chief Secretary's office on the progress made on actions recommended in the OAG report.

PI- 28 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
No audit reports scrutinized in the last three years	D	(i) Scrutiny of audit reports is usually completed by the legislature within 12 months from receipt of the reports.	Office of the Prime Minister and Council of Ministers, Parliamentary Secretariat.	D	Absence of Parliament in two of the three years of assessment period.
Not applicable	NA	(ii) Extent of hearings on key findings undertaken by the legislature.	Office of the Prime Minister and Council of Ministers, Parliamentary Secretariat.	C	Absence of Parliament in two of the three years of assessment period.
Not applicable	NA	(iii) Issuance of recommended actions by the legislature and implementation by the executive	Office of the Prime Minister and Council of Ministers, Parliamentary Secretariat.	C	Absence of Parliament in two of the three years of assessment period.

3. 7 DONOR PRACTICES

The PEFA performance measurement framework includes three indicators to assess donor practices. The first indicator (D-1) measures predictability of direct budget support, the second (D-2) measures financial information provided by donors for budgeting and reporting on project and program aid, and the third indicator (D-3) captures the proportion of aid managed under national procedures.

Methods of assessment included review of data available in published and unpublished materials, data available in the Aid Management Platforms (AMP), BMIS and FMIS, administration of questionnaires, and interviews and discussions with relevant key informants. Nine donors, including both direct budget support providers and 5 largest donors, were requested to respond to the questionnaires of which only 6 donors responded (response rate of 67 percent). The responses were used only for verification. The major source of data came from MoF and FCGO records.

D-1 PREDICTABILITY OF DIRECT BUDGET SUPPORT

Direct budget support constitutes an important source of revenue for central government in many countries. Poor predictability of inflows of budget support affects a government's fiscal management in much the same way as the impact of external shocks on domestic revenue collection. Both the shortfalls in the total amount of budget support and the delays in in-year distribution of in-flows can have serious implications on government's ability to implement its budget as planned.

Direct budget support consists of all aid provided to the government treasury in support of the government's budget at large (general budget support) or for specific sectors. When received by the government's treasury, the funds will be used in accordance with the procedures applying to all other general revenue. Direct budget support may be channeled through separate or joint donor holding accounts before being released to the treasury.

Scoring method M1
Overall Rating D-1: D+

Assessed dimension (i): Annual deviation of actual budget support from the forecast provided by donor agencies at least six weeks prior to the government submitting its budget proposals to the legislature (or equivalent approving body).
Rating: D. In at least two of the last three years, direct budget support outturn fell short of the forecast by more than 15 percent, or no comprehensive and timely forecast for the year(s) was provided by the donor agencies.

Justification of Rating

As defined for this assessment, direct budget support constitutes all program support provided to the Government Treasury in support of the budget (at large) or for specific sectors. In line with this definition, amounts provided to School Sector Reform Program, National Health Sector Program, Nepal Peace Trust Fund, Japan KR-1 and KR-2, Japan DRF, UK DRF, and ADB Rural Reconstruction and Rehabilitation Sector Development Program are taken as basis of analysis. The ADB, Denmark, European Union, Finland, GAVI Alliance, Germany,Japan, Norway, Switzerland,United Kingdom, and World Bank are major contributors of direct budget support in Nepal. Line of credit and concessional loan operations from EXIM banks, which were included in the 2008 assessment, are excluded from the calculations as these tend to have strings attached and are implemented under turn-key and discrete project modalities rather than direct budget support.

The Ministry of Finance captures information on aid flows through 3 major systems: (a) BMIS in the Budget and Program Division (MoF), (2) FMIS housed in FCGO and (3) AMP in MoF International Economic Cooperation Division (IECCD). The BMIS and FMIS could not generate reports on quarterly forecasts and quarterly actual disbursements. This restricted calculation of the deviation of actual disbursement from the corresponding forecasts on a quarterly basis. The BMIS provided information only on the annual budget estimate of direct budget support, which is virtually the forecast of actual disbursement for the year. Similarly, FMIS provided information only on annual expenditures, which is more or less similar to annual actual disbursement. As this indicator requires information on forecast and actual disbursement on a quarterly basis, it was not possible to depend fully on BMIS and FMIS. This situation demanded triangulation of different available data sources. The AMP captured data on actual monthly disbursements that could easily produce information on actual quarterly disbursements. The percentage share of actual disbursement reported to AMP on each quarter was applied for quarterly distribution of annual budget estimate captured in BMIS. Similarly, the same percentages were applied for quarterly distribution of planned disbursement generated from AMP. Most donors reported actual disbursement to AMP each month.

In practice, many donors, including the World Bank, ADB, and other bilateral donors providing direct budget support, reported their actual disbursement on a monthly basis and planned disbursement on an annual basis. The Government systems, other than AMP, do not capture this information as soon as it is provided. The World Bank provided access to its web-based Client Connection where it updates its information on regular basis. Thus, majority of direct budget support donors provided commitment to the Government before the fiscal year began allowing it to allocate the amount among sectors or programs through the budget. All donors, including direct budget support providers, reported planned disbursement (forecast) to AMP on an annual basis. During consultations, donors providing direct budget support stated that they were ready to report even quarterly if the government required them to do so. With a view toward making reporting efficient and not overloading the system with unrequired data, Ministry of Finance agreed to accept annual planned disbursement, and the reporting arrangement was made accordingly.

From the practical and qualitative information gathered from donor responses and MoF officials, the evidence revealed that deviations of direct budget were 41.1 percent in 2010-11, 23.3 percent in 2011-12, and -7.5 percent in 2012-13. Therefore, direct budget support outturn was found to fall short of the forecast by more than 15 percent in at least two of the three fiscal years. The evidence have resulted in a rating of "D"for this dimension. However, the qualitative data show some progress toward aid predictability.

The AMP is a comparatively new system and compliance was found to be low. Many of the donors either did not report or reported late. Such underreporting and delayed reporting of planned and actual disbursement raises questions about reliability. However, donors are gradually getting accustomed to AMP,and compliance has been increasing, hopefully eventually with predictability. This assessment also identified some systemic gaps that need improvement.

Assessed dimension (ii): In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates).
Rating: A. Quarterly disbursement estimates have been agreed upon with donors at or before the beginning of the fiscal year, and actual disbursements delays (weighted) have not exceeded 25 percent in two of the last three years.

Justification of Rating

As explained under dimension (i), donors did not forecast quarterly budget support disbursements. However, donors providing direct budget support provided annual commitment to the Government, which was virtually a forecast. The Government was free to draw on the budget support amount with no other conditions attached prior to disbursement. Therefore, the Government had control over the amount. This type of flexibility provided more detailed predictability than quarter-by-quarter forecasts.

This dimension's rating has been upgraded to "A" from "D"in the 2008 assessment because the previous assessment followed the rating criteria in strict sense while the more current assessment explored rating rationale from criteria as suggested in the guidelines. The four prescribed rating criteria were not practical. They are set on the assumption that the quarterly forecast is compulsory for greater predictability of direct budget support, which is not always the case. Where there is Government control over the fund, the quarterly forecast may not be required because the amount of aid committed before budget formulation provides greater predictability for resource management. Despite this, the assessment team found some cases where even direct budget support donors failed to forecast before budget formulation mainly because of their own administrative delays. This rating was in consonance with how the donors responded in the questionnaires. Almost all respondents said that they were providing more detailed estimates of their direct budget support.

D-1 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation of change since 2008**
Disbursement against forecast in 2010-11, 2011-12, and 2012-13 was found to be 58.9%, 76.7% and 107.5%, with deviation of 41.1%, 23.3%, and -7.5% , respectively.	D	In at least two of the last three years, direct budget support outturn fell short of the forecast by more than 15%.	AMP, BMIS, FMIS, Responses from donors, discussion with Budget and FCGO staffs.	D	No change
FCGO record system of direct budget support shows that the amount once agreed to by donors is deposited in the Government Treasury. This shows level of Government control over budgetary support.	A	The Government can draw on budget support on basis of reimbursement of expenditure with no other conditions prior to disbursement. The Government has control over the amounts it will receive. Therefore, quarterly disbursement estimates was not required.	FCGO record system, FMIS, AMP, Budget and Program Division of the MoF.	D	2008 assessment followed the rating criteria in strict sense while this assessment explored rating rationale out of the four prescribed criteria. Despite no quarterly forecasts, the Government has control over the fund for resource management.

D-2: FINANCIAL INFORMATION PROVIDED BY DONORS FOR BUDGETING AND REPORTING ON PROJECT AND PROGRAM AID

Predictability of disbursement of donor support for projects and programs (below referred to only as projects) affect the implementation of specific line items in the budget. Project support can be delivered in a wide range of ways, with varying degrees of Government involvement in planning and management of resources. A lower degree of Government involvement leads to problems in budgeting the resources (including presentation in the budget documents for legislative approval) and in reporting of actual disbursement and use of funds (which will be entirely the donors 'responsibility where aid is provided in-kind). While the Government through its spending units should be able to budget and report on aid transferred in cash (often as extra-budgetary funding or through separate bank accounts), it is dependent on donors for budget estimates and reporting on implementation for aid in-kind. Donor reports on cash disbursements are also important for reconciliation between donor disbursement records and government project accounts.

Scoring method M1

Overall Rating D2: C+

> ***Assessed dimension (i) : Completeness and timeliness of budget estimates by donors for project support.***
> ***Rating: B.*** At least half of donors (including five largest) provide complete budget estimates for disbursement of project aid at stages consistent with the Government's budget calendar and with a breakdown consistent with the Government's budget classification.

Justification for Rating

Out of 39 donors, only 21 reported actual disbursement to AMP, out of which 15 were found to report the planned disbursement annually. The planned disbursement was more or less consistent with the Government's budget calendar and classification. Donors provided budget with broad categories (for example, training and workshops, consultant services, works, goods and non-consulting services, and vehicles). These broad categories were broken down as per Government budget classification. The number of donors reporting planned disbursement to AMP was 15 out of 39 donors reporting actual disbursement in FMIS that included providing aid under "reimbursable" and "cash payment" modality. Aid disbursed under "direct payment" modality was only partially reported. In terms of amount, the largest 5 donors reported US$539,017,209 as planned disbursement out of total planned disbursement of US$696,119,295 reported to AMP, which was 77.43 percent of the total planned disbursement.

Though 21 donors reported to AMP in 2012-13, the actual number (39) was recorded higher in the budget. This shows the low level of compliance with AMP. However, the percentage share of the reported planned disbursement by the 5 largest donors is still more than half of all aid. These donors were not reporting planned disbursement on quarterly basis.

The donor's questionnaire responses were that almost all funds they provided were based on the estimates provided and were consistent with the Government budget calendar and budget classification. The donor statements could not be fully corroborated with evidences generated from Ministry of Finance, but still there was slight improvement in the rating compared to the previous assessment.

> ***Assessed dimension (ii): Frequency and coverage of reporting by donors on actual donor flows for project support.***
> ***Rating: C.*** Donors provide quarterly reports within two months of end of quarter on all disbursements made for at least 50 percent of the externally financed project estimates in the budget. The information does not necessarily provide a breakdown consistent with the Government budget classification.

Justification for Rating

Donors report actual disbursement to AMP on a quarterly basis (i.e., in November, March, and June). Total disbursement of US$959,951,290 is more than the planned disbursement amount of US$696,119,295. The actual disbursement appears to be higher than the planned disbursement. This is because (a) donors under-reported planned disbursement and (b) actual FY12-13 disbursement had a backlog from the previous years. Even though data shows more actual disbursement than planned, this is not reliable as there is a huge gap between commitment and disbursement of aid to Nepal. This indicator cannot be rated only on basis of AMP-generated data; neither can it be rated on the basis of average percentage. Referring to FMIS data, the 5largest donors reported actual disbursement of NRs 37943.65 million in FY12-13 while the budget estimate in the corresponding period was only NRs 60514.49 million (62.7 percent). The amount disbursed by the 5 largest donors in FY12-13 was 91.48 percent of total disbursement in the same period. The amounts received from donors are not reported exactly in accordance with Government line items. However, they provide actual disbursement in categories that can be recorded as per Government budget classification. Taking these facts and figures into consideration, this dimension was rated “C” up from “D” in the previous assessment. The reasons for the grade increase were due to impact of AMP and improved compliance with FMIS.

D-2 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in PA**	**Explanation to change since 2008**
Donors reporting planned disbursement to AMP were more than half in terms of number of donors (15 out of 21) and amount (77.43%).	B	(i) At least half of donors (including the 5largest) provide complete budget estimates for disbursement of projects aid at stages consistent with the Government’s budget calendar and with a breakdown consistent with Government's budget classification.	AMP, FMIS, responses from donors.	D	AMP, which was not in place during 2008 assessment, was made operational in 2010. This provided data on planned disbursement.
Actual disbursement reported to FMIS was 62.70% of budget estimate FY12-13.	C	(ii) Donors provide quarterly reports within one month of end of quarter on all disbursements made for at least 50% of externally financed project estimates in the budget, with a breakdown consistent with Government budget classification.	AMP, responses from donors.	D	AMP, which was not in place during 2008 assessment, was made operational in 2010. This provided data on planned disbursement.

D-3: PROPORTION OF AID THAT IS MANAGED BY USE OF NATIONAL PROCEDURES.

National systems for management of funds are those established in the general legislation (and related regulations) of the country and are implemented by mainstream line management functions of the Government. The requirement that national authorities use different (donor-specific) procedures for the management of aid funds diverts capacity away from managing the national systems. This is compounded when different donors have different requirements. Conversely, the use of national systems by donors can help to focus efforts on strengthening and complying with the national procedures also for domestically funded operations.

The use of national procedures mean that banking, authorization, procurement, accounting, audit, disbursement, and reporting arrangements for donor funds are the same as those used for Government funds. All direct and un-earmarked budget support (general or sector based) will by definition use national procedures in all respects. Other types of donor funding such as earmarked budget support, basket funds, and discrete project funding may use some or no elements of national procedures.

Scoring method M1

Overall Rating D-3: C

Assessed dimensions (i): Overall proportion of aid funds to central government that are managed through national procedures.

Rating: C. Fifty percent or more of aid funds to central government are managed through national procedures.

Justification of Rating

During FY12-13, the annual average amount contributed by 5 largest on-budget donors was 60.32 percent. This figure helped to upgrade the rating for this indicator to "C" from "D" in the 2008 assessment.

Donors providing aid out of the budget did not use national procedures. Even within the category of on-budget aid, some donors used direct payments, only partially using national procedures. The information captured in AMP could not segregate direct payments made using national procedures from those not using the national procedures. Therefore, this assessment excluded the direct payment modality from the amount proportioned as using the country system. Though the amount using the direct

Table 3.19: Largest 5 on-budget donors using country system in FY12-13

	World Bank	ADB	DFID	Japan	Norway	Total	Weighted average of each procedure
Total budget (US$)	231,404,440	101,204,607	89,989,120	65,759,647	30,537,319	518,895,134	
Exchange rate	95	95	95	95	95		
Latest budget (NPR million)	21983.42	9614.44	8548.97	6247.17	2901.05		
Procedures							
Budget	97.96%	99.87%	36.21%	63.77%	66.13%		81.4%
Banking	97.96%	92.53%	25.55%	18.99%	66.13%		72.5%
Accounting	96.56%	73.20%	25.55%	18.99%	40.7%		66.6%
Procurement	96.56%	76.07%	25.55%	18.99%	40.7%		67.1%
Reporting	97.96%	82.64%	44.22%	82.81%	66.13%		81.9%
Auditing	96.56%	76.07%	25.55%	18.99%	40.7%		67.1%
Simple average of all procedures							72.8%

Source: AMP, MoF, and World Bank calculations.

payment modality was insignificant in 2011-12, it increased in 2012-13 by about 10 percentage points. This shows that direct payment is becoming popular among development partners. The direct payment modality should be brought under national procedures through reforms in the PFM system (Table 3.19).

Global monitoring surveys on implementation of aid effectiveness principles, including Busan commitments, have shown progress toward meeting the target of disbursing 70 percent of aid using PFM and procurement systems by 2015. Reports show that Nepal is on track to meet its target, given the increase from 55 percent in 2010 to 64 percent in 2013. Of the total amount disbursed in 2012-13, nearly 64 percent was reflected in the Government budget while the remaining 36 percent was not. Of the 64 percent aid disbursed on budget, only 46 percent was actually channeled through the national treasury (using national PFM systems).

D-3 Summary					
Evidence used	**Rating**	**Framework requirement**	**Information sources**	**Rating in 2008**	**Explanation to change since 2008**
Proportion of on-budget, reimbursable, cash, and direct payment flow out of total disbursement from each of the 5 largest donors	C	50% or more of aid funds to Government are managed through national procedures	AMP and Global Monitoring Survey data compiled by MoF, Development Cooperation Report, 2011-12	D	AMP, which was not in place during 2008 assessment, was made operational in 2010. This provided data on use of country system.

4.

Recent and ongoing reforms

The ongoing PFM reforms were initiated Government of Nepal. Some of the initiatives are financed by the Multi-Donor Trust Fund for PFM, administered by the World Bank. This is a basket arrangement, established in 2010, supported at present by six donors (Australia, Denmark, European Union, Norway, the Swiss Confederation, United Kingdom and United States of America) that have so far pledged US$17.7 million.

4.1 REFORM COMPONENTS UNDER PFM MDTF

Component 1 deals with strengthening PFM system and capacities. This component has one main operation that relates to strengthening the PFM system and three sub-components:

(a) ***Supporting implementation of TSA system.*** The TSA was fully rolled out covering all 75 districts in July 2013 (a year ahead of schedule) and covers over 95 percent of all Government expenditure. The TSA allows real-time checks on the available uncommitted budget before DTCOs authorize spending, and it allows central accounting for all central- and district-level revenue and expenditure by FCGO. TSA rollout has brought about cost savings (rationalization on number of spending units); provided the platform to improve cash management (revenue reporting is being strengthened); assisted management decision (real-time data facilitating mid-course budget correction); strengthened inter-linkages of PFM activities (designing of LMBIS to TSA completed for implementation).

(b) ***Implementation of public sector accounting standards.*** Under this sub-component, the Nepalese Financial Reporting Standards is modeled on IFRS and were drafted by the Accounting Standards Board after an extensive consultative process. The Institute of Chartered Accountants of Nepal has announced these standards with a road map for implementation. Pilots for rolling out Nepalese Public Sector Accounting Standards in two ministries have been completed and financial statements in accordance with cash-based IPSAS, Part I, have been prepared. Final reports are likely to be issued by mid-July 2014, after which a senior policy-level workshop is held and gradual implementation of NPSAS is decided as the way forward.

(c) ***Strengthening the PEFA Secretariat.*** Capacity-building activities of the PEFA Secretariat continue to make progress in reaching out to various stakeholders across the country, including remote districts, demand-side stakeholders, line departments, and the general public. This can contribute toward increasing PFM awareness and building a solid foundation for the ensuing PFM reforms. Research work in five high-priority areas has begun.

Component 2 deals with enhancing PFM accountability. This component has two sub-project operations that relate to strengthening OAG and strengthening the civil society organizations use of social accountability to improve PFM. This involves supporting OAG for moving to a risk-based audit approach, development of performance auditing, and collaboration with civil society organizations. Strengthening civil service organizations in the use of social accountability in local planning and monitoring of projects and service delivery is another activity.

Component 3 deals with deepening PFM-related knowledge. This component carries out analytical work for knowledge dissemination. Two analytical works have been completed: the Public Expenditure Tracking Survey in the education sector and the Operational Risk Assessment in the PFM sector.

Component 4 deals with strengthening budgeting process for results. This component has 13 sub-component operations that relate to strengthening the budgeting process, focusing in 3 areas: (a) strengthening budget credibility (8 subcomponents); (b) strengthening linkages of priorities and service targets to budget (2 subcomponents) and (c) strengthening program performance accountability (3 subcomponents). A diagnosis of reforms has been prepared along with an action plan, including the completion of various on-going activities. The team seeks to internalize ownership of the budget reform process among government stakeholders, foster mutual accountability among key institutions for delivery of agreed activities, and synchronize upstream reform plans with on-going downstream PFM reform and institutional strengthening activities.

4.2 INSTITUTIONAL FACTORS SUPPORTING REFORM PLANNING AND IMPLEMENTATION

Government leadership and ownership of PFM reforms is high, with appropriate organizational arrangements for management and coordination. Following the 2005/ PEFA assessment, the Government formed a national-level PEFA/PFM Steering Committee to serve as a focal agency to drive PFM reforms. The Steering Committee is chaired by the Finance Secretary and comprises representatives from MoF, NPC, OAG, and FCGO; and private sector representatives from the FNCCI and Transparency International Nepal from Civil Society. . It has 14 members and aims to meet twice a year. The overall objective of the PFM Reform Steering Committee is to provide strategic direction to PFM.

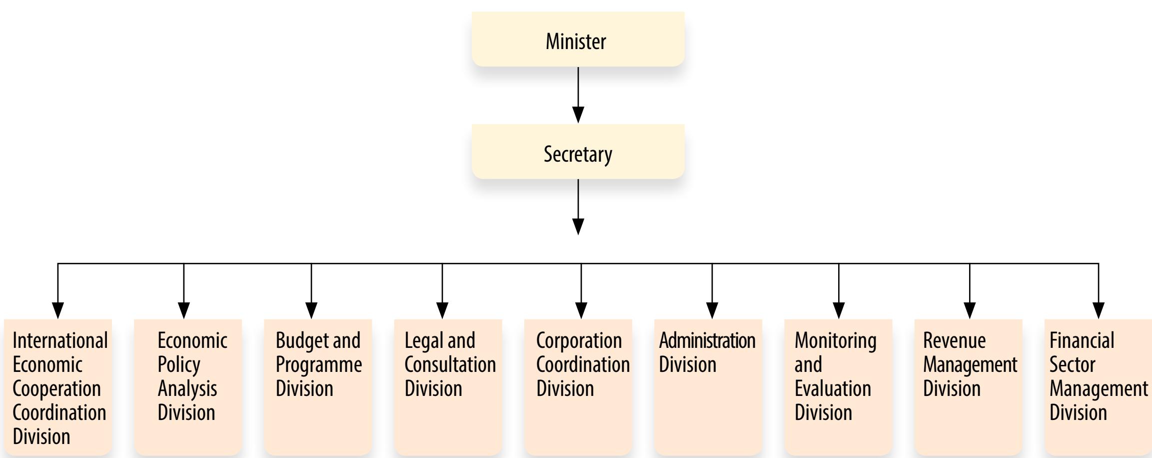
The GON established a PEFA Secretariat in 2009 under MOF to coordinate PFM reform activities. The FCGO Joint Financial Comptroller General, who also serves as Member Secretary of the PEFA Steering Committee, heads the Secretariat. In October 2014, the Secretariat had 5 full-time staff. It has suffered from frequent staff transfers, but the Government of Nepal committed in 2013 that the core team of the Secretariat would not be changed for at least two years. The PEFA Secretariat has its own budget independent of FCGO, where it is located. The Secretariat is functioning as a central platform to (a) facilitate support to the PFM Steering Committee, (b) support implementation of the PFM Strategy (c) support research and analysis in high-priority PFM areas or sectors, and (d) develop and implement a communications strategy to raise PFM awareness.

A PEFA Working Committee has also been created to support implementation of decisions of the Steering Committee and to support the Secretariat. The Working Committee is chaired by the PEFA Secretariat (Nepal) Coordinator and has representatives from key line ministries, MoF: Budget Division, Revenue Division, NPC, OAG.

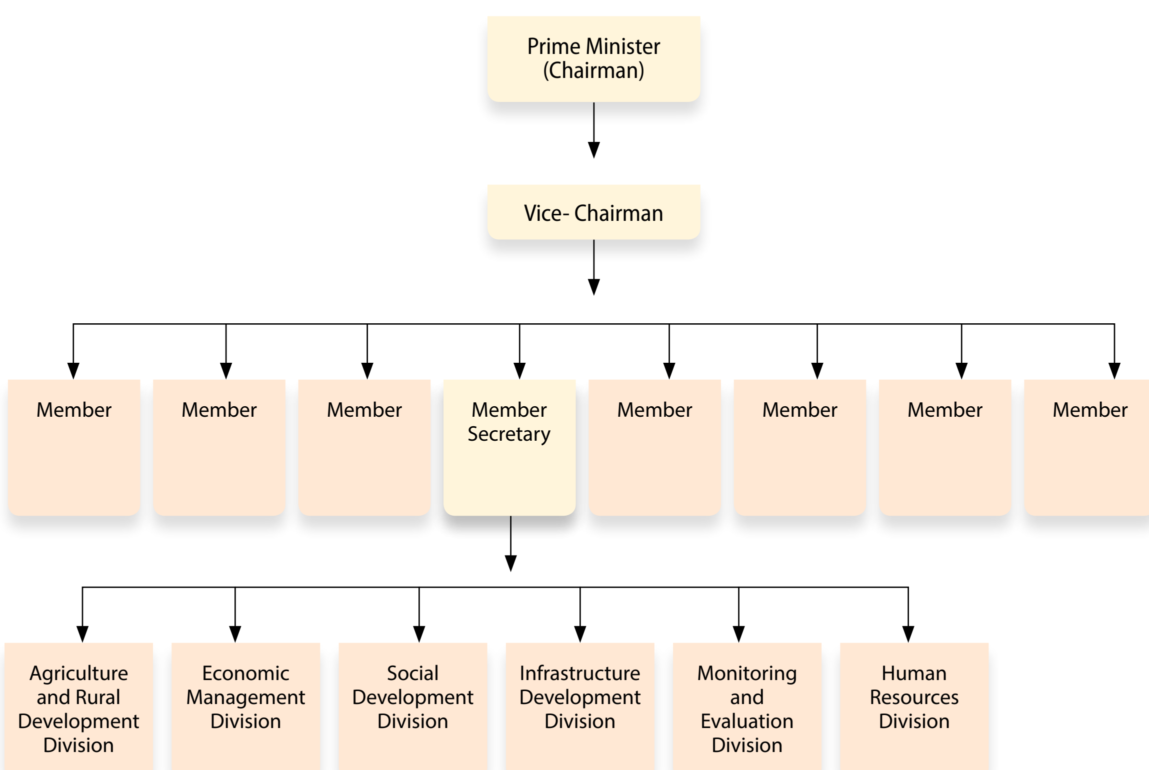
ANNEX A:

Organizational Structure of PFM Institutions

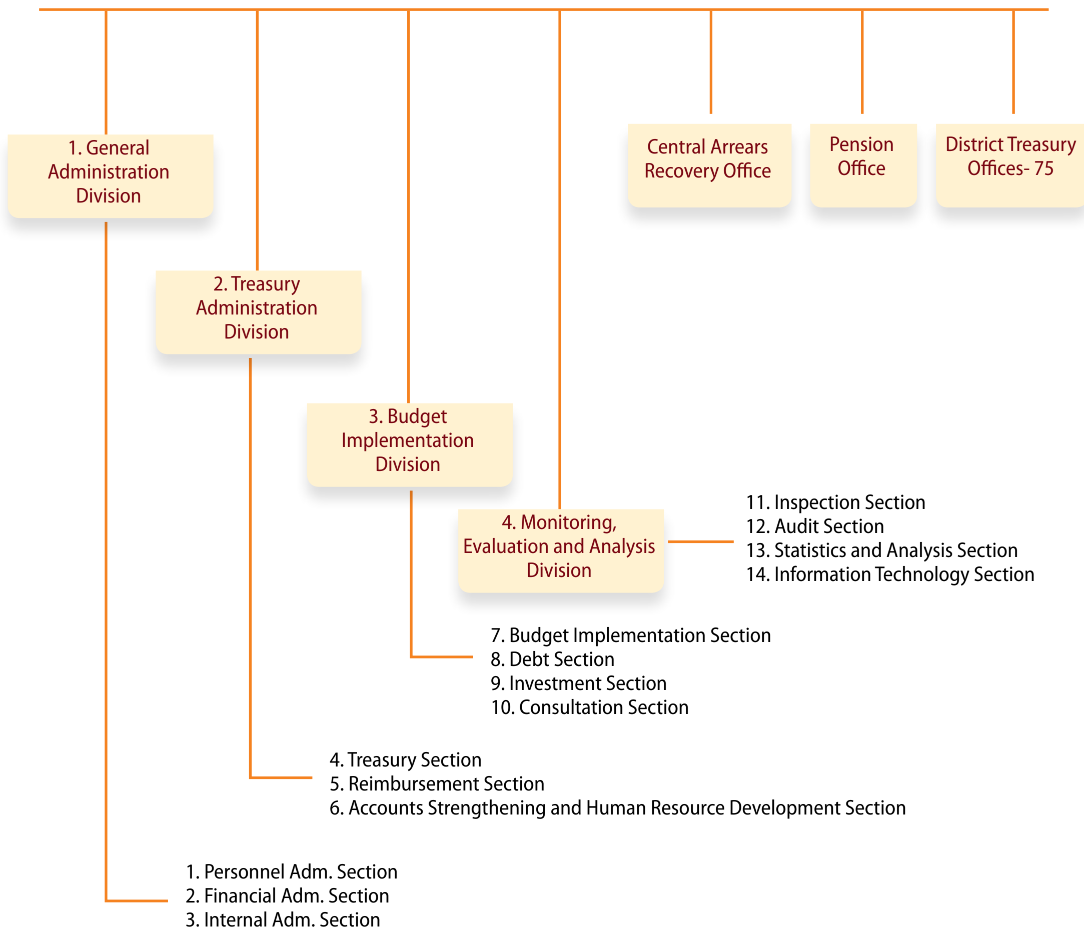
Organogram of Ministry of Finance



Organogram of National Planning Commission



Finance Comptroller General Office



PPMO Organizational Structure

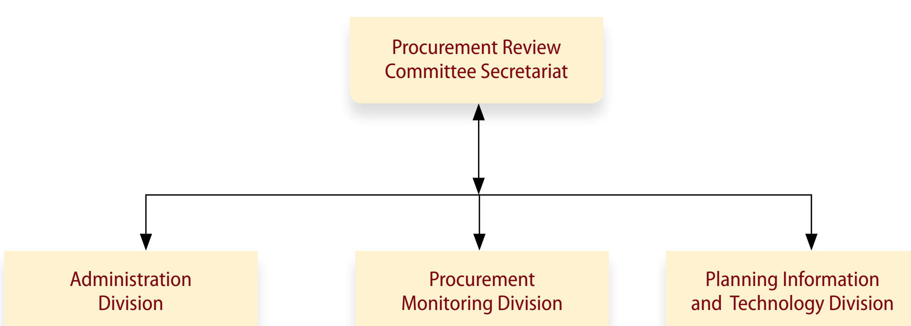


Table A1.1: The legal and institutional framework for PFM

Financial Management	The Interim Constitution (2007), Financial Procedural Act (1999), Audit Act (1991) and Good Governance (Management and Operation) Act (2008) provide the legal framework for PFM in Nepal. The Public Procurement Act (2007) provides the legal framework for purchases. Local government financial management is provisioned under Local Self Governance Act (1999).
Revenue Administration	Income Tax Act (2002), Value Added Tax Act (1996), Customs Act (2007) and Excise Duty Act (2002) provide the legal framework for tax administration. Various laws, rules, and directives support implementation of these laws.
Debt Management	Loan and Guarantee Act (1968) provides the legal framework for foreign loans whereas the Public Debt Act (2002) provides the framework under which government securities are issued and serviced. Under the Nepal Rastra Bank Act (2002), Nepal Rastra Bank is the manager of government and advises it in formulating the annual borrowing program.
Borrowing by Local Authorities	Local Self Governance Act (1999) allows local authorities to raise credit/loan with or without pledging any property under its ownership and possession or under guarantee given by the Government of Nepal, from a bank or any other organization, according to the policy approved by the local authority.
Procurement	Public Procurement Monitoring Office (PPMO) has been established as provided by the Public Procurement law. Public Procurement Act (2007) and Public Procurement Regulation (2007) form the legal framework for procurement in Nepal.
Audit	Clause 123 of the Interim Constitution of Nepal (2007) mandates the Office of the Auditor General (OAG) to audit government offices and any other institutions permitted by the law. The scope of audit the OAG can undertake is provisioned under Audit Act (1991).
Public Accounts Committee	Public Accounts Committee is provided for by Article 58 of the Interim Constitution of Nepal (2007) for discussing the OAG reports, to monitor progress on budget implementation, and to make recommendations to the Executive based on the discussions.

ANNEX B:

Calculation sheet for PFM performance indicators

Calculation Sheet for PFM Performance Indicators PI-1 and PI-2 (as revised January 2011)

Step 1: Enter the three fiscal years used for assessment in table 1.

Step 2: Enter budget and actual expenditure data for each of the three years in tables 2, 3, and 4 respectively.

Step 3: Enter contingency data for each of the three years in tables 2, 3, and 4 respectively.

Step 4: Read the results for each of the three years for each indicator in table 5.

Step 5: Refer to the scoring tables for indicators PI-1 and PI-2 respectively in the Performance Measurement Framework in order to decide the score for each indicator.

Table 1 - Fiscal years for assessment	
Year 1 =	2010/11
Year 2 =	2011/12
Year 3 =	2012/13

Table 2

Data for year = 2010/11

Administrative or Functional head	Budget	Actual	Adjusted Budget	Deviation	Absolute Deviation	Percent
Ministry of Education	36,485,879,000	37,029,365,246	35,564,294,702	1,465,070,544	1,465,070,544	4.1%
Ministry of Local Development	25,171,642,000	24,143,378,773	24,535,840,132	-392,461,359	392,461,359	1.6%
Ministry of Home Affairs	21,741,704,000	21,530,864,808	21,192,537,759	338,327,049	338,327,049	1.6%
Ministry of Defence	18,291,422,000	19,089,126,566	17,829,405,248	1,259,721,318	1,259,721,318	7.1%
Ministry of Physical Planing and Construction	16,532,442,000	15,300,284,975	16,114,854,720	-814,569,745	814,569,745	5.1%
Ministry of Agriculture and Cooperative	8,205,921,000	7,710,154,820	7,998,650,457	-288,495,637	288,495,637	3.6%
Ministry of Health and Population	7,895,862,000	7,252,358,894	7,696,423,131	-444,064,237	444,064,237	5.8%
Ministry of Irrigation	5,838,836,000	5,822,790,276	5,691,354,845	131,435,431	131,435,431	2.3%
Ministry of Peace and Reconstruction	4,217,183,000	3,279,054,466	4,110,662,622	-831,608,156	831,608,156	20.2%
Ministry of Forest and Soil Conservation	4,021,320,000	3,835,726,724	3,919,746,858	-84,020,134	84,020,134	2.1%
Ministry of Finance	3,815,965,000	3,040,920,031	3,719,578,849	-678,658,818	678,658,818	18.2%
Ministry of Finance - Investment (Public Enterprises)	3,214,150,000	11,738,272,993	3,132,964,888	8,605,308,105	8,605,308,105	274.7%
Ministry of Foreign Affairs	2,465,565,000	2,013,296,427	2,403,288,140	-389,991,713	389,991,713	16.2%
Ministry of Information and Communication	2,454,979,000	2,286,149,650	2,392,969,528	-106,819,878	106,819,878	4.5%
Ministry of Land Reform and Management	1,827,826,000	1,494,558,237	1,781,657,570	-287,099,333	287,099,333	15.7%
Ministry of Industry	1,697,909,000	1,090,571,889	1,655,022,099	-564,450,210	564,450,210	33.2%
Ministry of Energy	525,504,000	393,545,286	512,230,475	-118,685,189	118,685,189	22.6%
Ministry of Tourism and Civil Aviation	913,406,000	784,289,799	890,334,591	-106,044,792	106,044,792	11.6%
Ministry of Commerce and Supply	895,542,000	1,188,991,809	872,921,812	316,069,997	316,069,997	35.3%
Ministry of Environment	197,243,000	164,438,568	192,260,907	-27,822,339	27,822,339	14.1%

Administrative or Functional head	Budget	Actual	Adjusted Budget	Deviation	Absolute Deviation	Percent
Other Ministries (Except Interest and Contingency)	44,161,374,000	36,064,776,102	43,045,917,007		6,981,140,905	15.8%
allocated expenditure	210,571,674,000	205,252,916,340	205252916340.04	0.0	24,231,864,889.4	
contingency	3,356,231,000	10,057,814				
total expenditure	213,927,905,000	205,262,974,154				
overall (PI-1) variance						4.05%
composition (PI-2) variance						11.81%
contingency share of budget						0.00%

Table 3

Data for year = 2011/12

Administrative or Functional head	Budget	Actual	Adjusted Budget	Deviation	Absolute Deviation	Percent
Ministry of Education	40,846,177,000	42,768,023,071	42,164,982,793	603,040,278	603,040,278	0.014301922
Ministry of Local Development	14,708,962,000	14,261,267,919	15,183,872,156	-922,604,237	922,604,237	0.060762118
Ministry of Home Affairs	21,614,559,000	25,944,845,777	22,312,431,059	3,632,414,718	3,632,414,718	0.162797801
Ministry of Defence	19,100,966,000	22,629,943,747	19,717,681,357	2,912,262,390	2,912,262,390	0.147698015
Ministry of Physical Planing and Construction	19,740,936,000	19,630,974,429	20,378,314,151	-747,339,722	747,339,722	0.036673285
Ministry of Agriculture and Cooperative	9,166,077,000	9,160,048,407	9,462,023,312	-301,974,905	301,974,905	0.031914411
Ministry of Health and Population	8,367,262,000	8,332,711,625	8,637,416,869	-304,705,244	304,705,244	0.035277358
Ministry of Irrigation	5,910,565,000	5,749,702,162	6,101,400,176	-351,698,014	351,698,014	0.057642181
Ministry of Peace and Reconstruction	5,216,886,000	8,266,813,113	5,385,324,272	2,881,488,841	2,881,488,841	0.5350632
Ministry of Forest and Soil Conservation	4,091,376,000	4,438,860,942	4,223,474,785	215,386,157	215,386,157	0.050997382
Ministry of Finance	3,877,130,000	2,930,129,157	4,002,311,397	-1,072,182,241	1,072,182,241	0.26789076
Ministry of Finance - Investment (Public Enterprises)	4,594,242,000	13,746,500,990	4,742,576,885	9,003,924,105	9,003,924,105	1.898529918
Ministry of Foreign Affairs	2,243,165,000	2,161,363,971	2,315,590,358	-154,226,387	154,226,387	0.066603485
Ministry of Information and Communication	2,335,165,000	2,672,827,160	2,410,560,774	262,266,386	262,266,386	0.10879891
Ministry of Land Reform and Management	1,983,652,000	1,983,064,450	2,047,698,428	-64,633,979	64,633,979	0.032583325
Ministry of Industry	1,902,489,000	1,201,010,428	1,963,914,908	-762,904,480	762,904,480	0.40100336
Ministry of Energy	671,124,000	552,741,201	692,792,667	-140,051,467	140,051,467	0.208681952
Ministry of Tourism and Civil Aviation	916,165,000	681,139,561	945,745,338	-264,605,777	264,605,777	0.28881891
Ministry of Commerce and Supply	1,285,475,000	909,232,706	1,326,979,297	-417,746,591	417,746,591	0.324974497
Ministry of Environment	197,119,000	177,893,620	203,483,407	-25,589,786	25,589,786	0.129818975
Other Ministries (Except Interest and Contingency)	57,512,830,732	45,389,234,884	59,369,754,927	-13,980,520,044	13,980,520,044	0.243085236
allocated expenditure	226,282,322,732	233,588,329,318	233,588,329,318	0	39,021,565,748	
contingency	2,985,879,268	82,410,710				
total expenditure	229,268,202,000	233,670,740,028				
overall (PI-1) variance						1.92%
composition (PI-2) variance						16.71%
contingency share of budget						0.04%

Table 4

Data for year = 2012/13

Administrative or Functional head	Budget	Actual	Adjusted Budget	Deviation	Absolute Deviation	Percent
Ministry of Education	45,912,438,000	45,973,332,970	44,748,619,450	1,224,713,520	1,224,713,520	0.0274
Ministry of Local Development	24,628,089,000	25,294,767,671	24,003,800,069	1,290,967,602	1,290,967,602	0.0538
Ministry of Home Affairs	23,498,434,000	23,735,207,596	22,902,780,304	832,427,292	832,427,292	0.0363
Ministry of Defence	21,437,668,000	21,108,965,681	20,894,251,950	214,713,731	214,713,731	0.0103
Ministry of Physical Planing and Construction	22,285,472,000	19,389,296,716	21,720,565,259	-2,331,268,544	2,331,268,544	0.1073
Ministry of Agriculture and Cooperative	10,136,002,000	9,892,082,705	9,879,067,982	13,014,722	13,014,722	0.0013
Ministry of Health and Population	7,767,325,000	7,962,501,673	7,570,433,758	392,067,914	392,067,914	0.0518
Ministry of Irrigation	6,686,633,000	6,831,016,628	6,517,135,847	313,880,781	313,880,781	0.0482
Ministry of Peace and Reconstruction	8,964,389,000	6,047,278,989	8,737,153,796	-2,689,874,807	2,689,874,807	0.3079
Ministry of Forest and Soil Conservation	4,179,732,000	4,376,457,806	4,073,781,416	302,676,390	302,676,390	0.0743
Ministry of Finance	3,249,763,000	3,104,033,525	3,167,385,879	-63,352,354	63,352,354	0.0200
Ministry of Finance - Investment (Public Enterprises)	10,989,438,000	12,404,193,088	10,710,870,528	1,693,322,560	1,693,322,560	0.1581
Ministry of Foreign Affairs	2,184,541,000	2,218,230,694	2,129,165,824	89,064,870	89,064,870	0.0418
Ministry of Information and Communication	2,560,332,000	2,523,560,235	2,495,431,028	28,129,207	28,129,207	0.0113
Ministry of Land Reform and Management	1,835,526,000	1,930,368,737	1,788,997,885	141,370,852	141,370,852	0.0770
Ministry of Industry	1,531,867,000	1,330,990,049	1,493,036,232	-162,046,183	162,046,183	0.1058
Ministry of Energy	510,789,000	485,567,957	497,841,186	-12,273,229	12,273,229	0.0240
Ministry of Tourism and Civil Aviation	1,662,130,000	2,174,004,424	1,619,997,240	554,007,184	554,007,184	0.3333
Ministry of Commerce and Supply	1,324,695,000	810,524,408	1,291,115,763	-480,591,356	480,591,356	0.3628
Ministry of Environment	452,748,000	520,404,704	441,271,447	79,133,257	79,133,257	0.1748
Other Ministries (Except Interest and Contingency)	77,423,235,000	74,030,576,718	75,460,660,129	-1,430,083,411	1,430,083,411	0.0185
allocated expenditure	279,221,246,000	272,143,362,973	272,143,362,973.0	0.0	14,338,979,764.9	
contingency	12,317,284,000	2,047,853,259				
total expenditure	291,538,530,000	274,191,216,232				
overall (PI-1) variance						6.0%
composition (PI-2) variance						5.3%
contingency share of budget						0.7%

Table 5 - Results Matrix

	for PI-1	for PI-2 (i)	for PI-2 (ii)
year	**total exp. deviation**	**composition variance**	**contingency share**
2067/68	4.05%	11.81%	0.25%
2068/69	1.92%	16.71%	
2069/70	5.95%	5.27%	
Score for indicator PI-1:			**A**
Score for indicator PI-2 (i)		**C**	
Score for indicator PI-2 (ii)		**A**	
Overall Score for indicator PI-2			**C+**

ANNEX C:

PEFA assessment teams and working groups

1. PEFA STEERING COMMITTEE (LEADING BODY)

2. ADVISORY BODY

Secretary, Ministry of Finance: Mr. Shanta Raj Subedi/Mr. Yub Raj Bhushal/ Mr. Suman Prasad Sharma
Secretary, National Planning Commission: Mr Yub Raj Bhushal/ Mr. Som Lal Subedi/ Mr. Sharada Prasad Trital
Financial Comptroller General, FCG Office: Mr. Suman Prasad Sharma/ Mr. Shankar Prasad Adhikari

3. PEFA ASSESSMENT WORKING COMMITTEE

Dr. Mukti Narayan Paudel/ Mr. Dilli Ram Sharma/ Jagadish Regmi, Coordinator, PEFA Secretariat, Nepal	Coordinator/Chair
Dr. Baikuntha Aryal, Joint Secretary, Ministry of Finance	Co- Chair
Ram Sharan Pudasaini, Joint Secretary, Ministry of Finance	Member
Puspa Lal Shakya, Joint Secretary, National Planning Commission	Member
Rajan Khanal, Joint Secretary, Ministry of Finance (Now the Secretary of MOGA)	Member
Naresh Kumar Chapagain, Joint Secretary, PPMO	Member
Jayadev Shrestha, JFCG, FCGO	Member
Babu Ram Gautam, Deputy Auditor General, OAG	Member
Madhu Kumar Marasini, Joint Secretary, MoF	Member
Babu Ram Subedi, Member Secretary of PEFA Secretariat (Nepal)	Member Secretary

4. PEFA ASSESSMENT WORKING GROUPS

Group A (PFM Outturns: Credibility of Budget, PI -1 to PI- 4)

Dr. Baikuntha Aryal, Joint Secretary, Ministry of Finance (Budget Division): Coordinator
Nirmal Hari Adhikari,Under Secretary, MOF, Budget Division
Baburam Subedi, DFCG and Member Secretary, PEFA Secretariat(Nepal)
Yugraj Pandey, Director, IRD
Upendra Khanal, Under Secretary, Ministry of Finance
Umesh Raj Rimal, Section officer, MoF

Group B (Comprehensiveness and Transparency of Budget, PI -5 to PI- 10)

Ram Sharan Pudasaini, Joint Secretary, Ministry of Finance, Coordinator
Bhumiram Sharma,Under Secretary, Monitoring Division
Baburam Shrestha,Under Secretary, MoFALD
Balaram Rijyal, Under Secretary, Budget Division, MOF
Sukdev Banskota,DFCG, FCGO
Prakash Lamsal, CA, ICAN
Dilaram Sapkota, Under Secretary, MoF
Bhanubhakta Neupane, Public Enterprises Coordination Division, MoF

Group 'C' (Policy Based Budgeting, PI -11 to PI- 12)

Puspa Lal Shakya, Joint Secretary, National Planning Commission, Coordinator
Thana Prasad Pangeni, Under Secretary, MoF (MTBF)
Yam Lal Bhushal, Under Secretary, NPC (MTEF)

Krishna Prasad Paudel, Deputy Financial Comptroller General, FCGO
Ramesh Siwakoti,Under Secretary, Ministry of Physical Infrastructure and Transport
Rudra Bhatta, Section Officer, National Planning Commission

Group 'D' (Predictability and Control in Budget Execution , PI -13 to PI- 15)
Rajan Khanal, Joint Secretary, Revenue Division,MOF: Coordinator (now Secretary of MOGA)
Dikar Dev Bhatta, Under Secretary, MOF, Revenue Division
Jeevan Kumar Ghimire, Under secretary
Narayan Prasad Sharma,Director, Department of Customs
Hari Phuyal, Deputy Financial Comptroller General, FCGO
Govinda Prasad Subedi, Director, Inland Revenue Department

Group E (Predictability and Control in Budget Execution, PI -16 to PI- 18)
Dr. Mukti Narayan Paudel, Coordinator, PEFA Secretariat
Mr. Kaman Singh Khatri, Deputy Financial Comptroller General, FCGO(Debt and Investment Section)
Krishna Bahadur Bohara,Under Secretary, MoF
Baburam Gyawali, Deputy Financial Comptroller General, FCGO
Suresh Krishna Sharma , Under Secretary, Ministry of Urban Development
Bala Dev Joshi,Director , Department of Civil Records
Tolendra Karki, Accounts Officer, PEFA Secretariat/FCGO

Group F (Predictability and Control in Budget Execution , PI -19 to PI- 21)
Naresh Kumar Chapagain,Joint Secretary, PPMO, Coordinator
Subash Chandra Shiwakoti, Deputy Financial Comptroller General, FCGO , Internal Audit Section
Yagya P.Dhungel,Under Secretary, MOF, Budget division
Sushil Pandey, Deputy Financial Comptroller General, FCGO, Procurement /Unit IT Section
Krishna Kumar Karki, Under Secretary (Law)

Group G (Accounting, Recording and Reporting, PI -22 to PI- 25)
Jaya Dev Shrestha, JFCG, FCGO, Coordinator
Chandra Kumar Shrestha,Under Secretary, MOF
Shaligram Sharma, Paudel, Deputy Financial Comptroller General, Budget and Internal Administration
Sanjay KC, CA, Accounting Standard Board
Suryamani Gautam, Under Secretary, FCGO
Ganga Bdr Chhetri, Under Secretary, FCGO
Anupama Karki, Accounts Officer, FCGO/PEFA

Group H (External Scrutiny and Audit, PI -26 to PI- 28)
Babu Ram Gautam, Assistant Auditor General, OAG, Coordinator
Kedar P. Paneru, Under Secretary, Budget Division
Bhawanath Dahal, Director, OAG
Ishwar Kafle, Deputy Financial Comptroller General, FCGO
Indra Prasad Aacharya, Director, OAG

Group I (Donor Practices, D -1 to D- 3)
Madhu Kumar Marasini, Joint Secretary, MoF, Coordinator
Dr. Narayan Dhakal Under Secretary, MoF, IECCD
Hari Pandey, Under Secretary, MoF
Hari Sharan Pudashaini, US, Budget Division
Homakanta Bhandari, Section Officer, MoF
Janak Dulal, Accounts Officer, FCGO

Nepal Public Financial Management Multi-Donor Trust Fund

Supported by:

Australian Aid

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State Secretariat for Economic Affairs SECO

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