



Policy brief

RESEARCH AGENDA ON FISCAL POLICY REFORM IN ETHIOPIA

2018



The Federal Democratic Republic of Ethiopia
Ministry of Finance and Economic Cooperation

in collaboration with:



PricewaterhouseCoopers LLP



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Enhancing Skilled Delivery in Ethiopia (ESDE)


Introduction

In the context of Ethiopia's rapid economic and demographic growth, the role of the Ministry of Finance and Economic Coordination (MoFEC) is becoming increasingly important. The economy is becoming vastly more complex and the government is expanding its reach to cover more services to more people. MoFEC therefore needs to build and deepen its capacities correspondingly so that it can effectively drive fiscal policy to support the Government of Ethiopia's ambitious and far reaching development agenda (as set out in the second Growth and Transformation Plan, GTPII).

MoFEC plays a central role in ensuring macroeconomic stability and sustainability, maintaining control over a growing level and intricacy of public finances, and guiding an increasingly sophisticated economy and rapidly growing population onto the country's desired development path.

With a decreasing ability to rely on foreign assistance, the ministry also needs to mobilise more resources for public expenditure by developing the domestic debt market, unlocking private sector investment for capital projects, drawing more effectively on domestic tax revenue and engaging with the wider population in an open and transparent way. These growing realms and responsibilities require increased knowledge and capabilities, as well as a clear plan to build these. Building this capacity will require additional financial resources, but the net impact to the government's finances will be significantly positive if this process is successful.

The United Nations and other influential international organisations have made it clear that the success of the international Sustainable Development Goals rests heavily on the ability of countries like Ethiopia to raise domestic revenue and spend effectively. The impacts of MoFEC's public financial management will be felt by citizens across Ethiopia – across all income levels and people groups – for years to come, and getting this right is vital if the country is to continue developing in a meaningful and sustainable way.



Key findings

Following a diagnostic assessment, key gaps were identified and a roadmap was developed to address those gaps. The Roadmap identifies priority actions to fill knowledge and academic research gaps but also points to improvements in coordination, organisational frameworks and staff capacity. It has been divided into the following thematic areas:

- Macro-fiscal policy and macroeconomic management
- Taxation
- Budgeting
- Fiscal controls, accounting and audit
- Debt management
- Private-public partnerships, private sector growth and public procurement
- Organisation and staffing and legal services

For each thematic area, we have identified a set of actions to be taken and the recommended owner of those actions among the directorates in MoFEC. We have also noted links between actions, and activities already underway where relevant. The timetables from the individual thematic areas have been collated into one document as an attachment to this report.

There are a number of key issues that span across these thematic areas, outlined in turn below.

Staffing

As MoFEC's role is becoming increasingly important in overseeing an ever larger budget as well as an ever more complex and sophisticated economy, there are numerous new challenges. These include challenges posed by medium-term performance budgeting, working with the private sector, and managing new sources of borrowing. MoFEC's widening responsibilities need to be met with a corresponding broadening of human resources and skills. Currently, acquiring the right staff and retaining existing staff presents major problems not

only within MoFEC but also with regard to public sector staff in other institutions which MoFEC relies on to execute its role effectively. Human resources are fundamental to policy making and implementation, and mitigating these problems through a comprehensive human resources strategy is a priority.

Information

To effectively oversee fiscal policy, MoFEC needs a complete picture of the state of the public finances, including the impacts and outcomes of existing fiscal policies on different segments of the population. Reliable information, summarised in a useable way, is key to giving MoFEC full visibility of the fiscal position, to analyse policy scenarios and support policy decisions, direct and redirect resources to achieve policy goals, and to mitigate fiscal risks and maintain financial stability. A crucial part of sound public financial management is ensuring openness and transparency of revenue and spending decisions, and it will also be important for MoFEC to strengthen the way it engages meaningfully with the public.

A priority is therefore to ensure that reporting to MoFEC is fit for purpose and that all building blocks for this are in place, including adequate accounting and information systems as well as sufficient data collection.

Analytical tools

Forecasting and modelling have become indispensable tools for fiscal policy analysis for ministries of finance around the world. Making predictions about the economy and modelling different economic and policy scenarios is important for planning, setting realistic targets, managing debt and mitigating fiscal risks. Improved capabilities in modelling and simulations will also allow MoFEC to better understand the likely impact of different policy options on different segments of the population (different income groups, genders, regions, economic sectors, enterprise sizes, etc.).

Roadmap

The Roadmap presents a prioritised, sequenced set of actions for MoFEC (and in some cases other parties) to undertake over the next three years to improve the Ministry's capability in the areas we have identified as gaps. It is presented as a series of gantt charts, grouped into thematic areas that correspond – in most cases – to the responsibilities of the existing directorates.

The actions and timings are intended as a guide only, with proper programme and project planning being undertaken as part of the implementation. We expect consultation with key stakeholders to shape the scope, timing and sequencing of the actions, and for the plan to evolve over time as actions are undertaken.

Topic/action	Year 1				Year 2				Year 3			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
T1. Review of coordination between MoFEC and ERCA	Tender	Action		(Action)								
T2. Reviewing tax incentives regime		Action										
T2.1 Coordinate tax expenditure studies currently underway												
T2.2 Possible follow-up work on tax expenditures, including public consultation		(Action)										
T2.3 Tax expenditure budgeting												Action
T3. Understanding the tax system and its impacts												
T3.1 Initial study into the coherence of the overall tax system						Tender	Action					
T3.2 Build/augment tax models and modelling capability									Tender	Action		
T3.3 Build analysis skills through analysis of tax incidence and equity outcomes and apply across all key taxes						Tender	Action					
T3.4 Review studies on taxpayer compliance costs and potentially follow up with additional analysis									Action	(Action)		
T3.5 Build and apply models to estimate tax potential of all major taxes											Tender	Action
T4. Presumptive income tax												
T4.1 Review presumptive income tax settings						Tender	Action					
T4.2 Implement and communicate new settings												
T5. Property taxation												
T5.1 Research potential enhancement of property taxation												
T6. Study on stamp duties and fees												
T7. Training on double taxation agreement (DTA)												
T7.1 Research potential enhancement of property taxation												
T8. Taxpayer education												
T8.1 Investigate best practices around secondary school level taxpayer education												
T8.2 Initiate process to introduce taxpayer education into the curriculum												
T8.3 Introduce courses on international taxation in higher education curricula												

Topic/action	Year 1				Year 2				Year 3			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
B1. Effectiveness and efficiency of national public spending												
	Tender	Action										
		Tender	Action	Review								
				Tender	(Action)							
B1.2 Evaluate programme budgeting												
B1.3 Build the required staff capacity												
B1.4 Refine reporting requirements and spending approvals process												
B2. Review pricing policies (explicit and implicit subsidies)												
B3. Effectiveness and efficiency of decentralised govt. spending												
B3.1 Review reporting requirements of local governments to MoFEC												
B3.2 Assess budget allocation process with respect to GTP II objectives												
B4. Public infrastructure												
B4.1 Review capability req. to understand public infrastructure needs/costs												
B4.2 Enhance capability/establish new public infrastructure unit												
B4.3 Prepare initial national infrastructure plan												
B5. Public consultation and transparency												
B5.1 Assess gaps in public access and feedback in budget preparation												
B5.2 Strengthen the public engagement and consultation system around budget												
B6. Inter-governmental transfer system												
B6.1 Review of transfers from the federal government to regional governments												
B6.2 Review of transfer system from the regional governments to local governments												

Topic/action	Year 1				Year 2				Year 3			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
F1 IPSAS implementation	Tender	Action										
			Tender									
					Action							
F1.1 Training programme to fill immediate IPSAS knowledge gaps												
F1.2 Develop a training and certification programme												
F1.3 Rollout training programme across public service professionals												
F2 IFMIS implementation												
F2.1 Review of conceptual design of IFMIS					Tender	Action						
F2.2 Training and technical assistance for staff on IFMIS implementation									Tender			
F2.3 Tender												
F3 Audit												
F3.1 Monitoring of follow-up mechanisms regarding audit findings												Action
D1. Development of the domestic debt market												
D1.1 Research best practice for development of domestic debt market	Tender					Action						
D1.2 Develop implementation plan for the domestic debt market												(Action)
D2. Preparation for negotiations with commercial creditors												
D2.1 Hire and/or train staff to support commercial negotiations												
D2.2 Development of a negotiation strategy												
D3. Build debt sustainability analysis capability												
P1 Study on PPP risk mitigation												
P1.1 Review the risks associated with PPP's and mitigation measures	Tender					Action						
P1.2 Revise accounting standards to ensure appropriate recording of PPP liabilities												
P2 Review of how public sector procurement law is applied in practice												
P2.1 Initial research and development of discussion document												
P2.2 Engage programme with private sector												
P2.3 Prepare policy paper for consideration by MoFEC/Ministers												
P3 Understanding the impact of existing fiscal policy on the private sector												
P3.1 Initial research and development of discussion document												
P3.2 Engage programme with private sector												
P3.3 Prepare policy paper for consideration by MoFEC/Ministers												

Topic/action	Year 1				Year 2				Year 3			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Legal												
L1. Legal services												
L1. Enhancement of legal drafting skills		Tender	Action									
O1. MoFEC staff retention												
O1.1 Assess the size and nature of the retention issue for MoFEC	Action											
O1.2 Assess skills and training needs across MoFEC as per this research agenda			Action									
O1.3 Develop a People Strategy to build staff capacity and attract and retain new staff			Tender	Action		Review (Action)						
O2. Capacity of MoFEC-facing staff in public bodies												
O2.1 Assess public body capacity gaps				Action								
O2.2 Review responsibilities and incentives for PB performance				Tender	Action							
O2.3 Develop strategy to sustainably close the capacity gap in public									Action			
									Tender	Action	Review	(Action)

	Additional Actions
Taxation	<p>T9. VAT optimisation study</p> <p>T10. Study on customs and excise tax regime</p> <p>T11. Tax evasion and avoidance</p> <p>T11.1 Research project to understand potential compliance issues of cross-border transactions</p> <p>T11.2 Taxation of high net worth individuals (HNWIs)</p> <p>T11.3 Study on the potential losses from transfer pricing in Ethiopia</p>
Budget	<p>B7. Fiscal policy impacts on climate resilient green economy growth</p> <p>B8. Coordinate household and other surveys to ensure consistent collection of age and gender disaggregated data</p>
Financial controls, acc. & audit	<p>F4 Treasury functions</p> <p>F4.1 Assessment of best practice of treasury functions</p> <p>F4.2 Experience sharing missions to best practice countries in the region</p>

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