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The role of fiscal transparency in raising the efficiency of public ex- penditure

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The role of fiscal transparency in raising the efficiency of public expenditure

Executive summary

The current system of Public Financial Management (PFM) is only partially prepared to deal with the economic challenges Belarus faces, as different assessments in the recent past suggest. A cornerstone of a PFM reform is increased fiscal transparency, which can be defined as the “clarity, reliability, frequency, timeliness, and relevance of public fiscal reporting and the openness to the public of the government’s fiscal policy-making process” (IMF).

A number of empirical studies suggest that fiscal transparency can contribute to improving the efficiency of public expenditure, lead to lower sovereign borrowing costs, and help to reduce fiscal risks. Tools and measures for fiscal transparency recommend a set of sources (types of reports) to be produced and published, and certain standards regulating the quality of the data and other information provided in these reports to be applied. A significant number of fiscal transparency assessments and indicators is proof of the growing global importance of the topic.

In Belarus, the fiscal data availability is generally good, with only some shortcomings. Also, the statistics comply with international norms to a large extent. However, fiscal information provided is of insufficient completeness as, e.g., quasi-fiscal activities of state-owned enterprises (SOEs) are not fully captured. Thus, there are undoubted benefits in terms of increased financial transparency for Belarus.

How could policymakers improve fiscal transparency in the short-term? Our recommendations comprise further improvements of the legislative framework. This relates to improving the credibility of budget planning and allocation through mandatory approval of forecasting and planning documents. To improve performance orientation, current concepts and draft orders developed by the Ministry of Finance and the Ministry of Economy, respectively, should be adopted with high priority. A further issue is the exchange of data between government agencies, in particular regarding the activities of SOEs. Here, data collection, transmission and control can be made more efficient and comprehensive. Another recommendation concerns the quality and accessibility of budget-related data, which should be improved and extended, and offered in a user-friendly format. In particular, the activities of the Development Bank should be covered in more detail in the budget execution report. The role of the State Control Committee (SCC) in improving the efficiency of public expenditure should be further strengthened. While it performs its functions as a control body well, it could implement more performance audits, which would contribute to raising the efficiency of public spending. Also, the SCC should make more of its findings available for public access, as this would help to improve the two-way communication between this institution and the public. A final recommendation concerns the potential for PFM reform in Belarus. A significant amount of analytical work in this regard has been done in the recent past on which policymakers can build, and various donors are ready to support reform activities. The natural conclusion for the Government and the Presidential Administration as the main leader and coordinator of this process is to use this current window of opportunity for a far-reaching PFM reform that addresses existing weaknesses and inefficiencies in the allocation, implementation, reporting and evaluation of public expenditure in Belarus.

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1 Introduction

Belarus faces the challenge to maintain fiscal stability under increasingly difficult circumstances. Economic growth is expected to enter a period of stagnation, the ability to maintain a balanced budget is subject to substantial risks resulting from contingent liabilities, and the country's most important source of external financing, Russia, is facing economic difficulties which might in turn affect its capability and/or willingness to provide additional funding.

The current system of Public Finance Management (PFM) is only partially prepared for these challenges. Recently conducted assessments, like the World Bank Public Expenditure Review (PER, 2011 and 2013) and the Public Expenditure and Financial Accountability Assessment (PEFA, 2014) evaluate the technical aspects of the PFM system - including the Treasury system, and control functions - as generally rather strong, whereas policy-orientation and the strategic functions of the PFM system - including mechanisms to relate budget allocations to medium-term, and sector-specific strategies and planning - still require substantial improvement. Another weakness of the PFM system is the large share of public finances which is managed outside the core PFM process, which hampers oversight and transparency.

To respond to these challenges the Government of Belarus has embarked on a process of PFM reform to improve efficiency and transparency of the PFM system. PFM reform shall address three aspects: One aspect is the modernisation of the existing system of budgetary planning. As a result, the budget process will provide for greater use of a programme-based budgeting, the transition to medium-term budgeting, and performance evaluation of public spending. The second dimension includes efforts to create a better information system of financial reporting of budget-sponsored organisations, which will be integrated into the overall information system of the Ministry of Finance. The third objective of the PFM reform relates to introduction of a finance management information system (FMIS) which will form the technical and technological backbone of public finance management.¹ The World Bank is supporting PFM reform in Belarus through technical assistance and potential lending operations.

These objectives of modernising the PFM system, together with finding responses to external challenges like meeting financing needs will require a changed approach to processing and publishing fiscal information, or: increased fiscal transparency. This policy paper explores the role which fiscal transparency can play to enhance the efficiency of public expenditure, and to meet financing needs. The argument is based on international trends of reform and development of PFM systems which suggest that fiscal transparency can contribute to improve the efficiency of public expenditure, and help to reduce fiscal risks.

Fiscal transparency is a relevant concept for various stakeholders:

- For lenders, investors, financing institutions and rating agencies: As the quality and accessibility of information about the fiscal situation improves the conditions of financing;
- For government officials: As credible data made available in a format which meets the needs of decision-makers is a precondition for an effective allocation of public expenditure;
- For the public: As a sufficient level of information and accountability is a key element of the 'social contract' between the government, business and the general population.

This policy paper is structured as follows: In the next chapter, it provides a succinct overview of current research of the benefits of fiscal transparency and discusses the scope of the concept of fiscal transparency. The third chapter summarises the current status of fiscal transparency in Belarus. This is followed by a chapter which discusses existing shortcomings of PFM and fiscal transparency in Belarus against the potential benefits which increased fiscal transparency can offer. A chapter with policy recommendations how to address the shortcomings and to improve fiscal transparency concludes the paper.

¹ Presentation of Deputy Minister of Finance Ermolovich at the PEMPAL meeting in Minsk, October 2014. http://eng.belta.by/all_news/economics/Belarus-plans-to-upgrade-its-public-finance-management-system-by-2019_i_76523.html.

2 Fiscal transparency: A short overview

Traditionally, the quality of PFM systems is assessed by criteria which focus on overall economic and fiscal stability, allocative efficiency and operational efficiency.² The focus on a *technically* sound and smooth functioning of the PFM system according to these traditional criteria is, however, about to change. More recent trends discussed in the international PFM literature and on the agenda of international organisations, led by the IMF and the World Bank, argue that the traditional criteria for 'good PFM' should be rethought to focus more on the *functionality* of the PFM system. "One such functionality relates to the way PFM systems influence decision-making and solvency in the public sector.[...] Without a basic level of functionality, governments do not actually control the flow of funds, meaningful analysis of spending is impossible and discussions over policy choices cannot happen."³ In this respect, the criteria fiscal transparency, accountability and public participation in PFM are becoming more widely recognised as important parameters for PFM. Standards and benchmarks which are developed and promoted by the IMF, the World Bank, the OECD, and other international organisations are currently undergoing a process of review and update to better assess fiscal transparency, and new initiatives and coalitions to promote fiscal transparency are being launched.

2.1 Definition

The IMF defines fiscal transparency as the "clarity, reliability, frequency, timeliness, and relevance of public fiscal reporting and the openness to the public of the government's fiscal policy-making process". Within this,

- 'clarity' refers to the ease with which these reports can be understood by users,
- 'reliability' refers to the extent to which these reports reflect the government's true financial position,
- 'frequency' (or periodicity) refers to the regularity with which reports are published,
- 'timeliness' refers to the time lag involved in the dissemination of these reports,
- 'relevance' refers to the extent to which these reports provide users with the information they need to make effective decisions, and
- 'openness' refers to the ease with which the public can understand, influence, and hold governments to account for their fiscal policy decisions [IMF 2012]

The concept of fiscal transparency is also acknowledged by the United Nations which in 2012 adopted the 'High level principles on fiscal transparency'. UN member states are "encouraged to intensify efforts to enhance transparency, participation and accountability in fiscal policies".⁴ The principles relate to access to fiscal information, and to the governance of fiscal policy. The principles state, for instance, that governments should:

- "...publish clear and measurable objectives for aggregate fiscal policy, regularly report progress against them, and explain deviations from plans";
- "...communicate the objectives they are pursuing and the outputs they are producing with the resources entrusted to them, and endeavour to assess and disclose the anticipated and actual social, economic and environmental outcomes."; and
- "...clearly define [the government sector] for the purposes of reporting, transparency, and accountability. Government financial relationships with the private sector should be disclosed, conducted in an open manner, and follow clear rules and procedures."⁵

Fiscal transparency is aimed at increasing efficiency of the economic policy through elimination of uncertainties related to public finance sector performance and intensification of external audit. Data accessibility is viewed as a key prerequisite for conducting sound and predictable fis-

² IMF Fiscal Transparency portal <http://www.imf.org/external/np/fad/trans/>.

³ Andrews et al (2014).

⁴ <http://fiscaltransparency.net/2013/01/united-nations-adopts-transparency-resolution/>.

⁵ <http://fiscaltransparency.net/2012/11/high-level-principles-on-fiscal-transparency/>.

cal policy on the one hand, and its effective audit on the other. The data that covers general government expenditures and revenues, its debt obligations and assets is essential in this regard but it is not considered to be sufficient enough. There should be data available to analyse fiscal implications of public private partnerships, contingent liabilities and guarantees, quasi-fiscal activities and financial stance of state-owned enterprises (SOE). This is a challenging part, and there is no consensus about the technical implementation of the related data collection and disclosure.⁶

In addition to the collection and public provision of high-quality data, fiscal transparency implies fiscal risk analysis and fiscal forecasting. The availability of public finance sustainability analysis and long-term forecasts of key public finance indicators provide a background for an efficient planning both for the private and public sector. However, the primary beneficiaries of this information availability are the fiscal authorities, as they can shape their policies in accordance with a broad set of challenges related to the domestic economic environment. Public access to this data can create additional benefits for fiscal policy through stricter external control over its implementation.

2.2 Benefits

The growing attention paid to fiscal transparency by international organisations and academic research is explained by the benefits which fiscal transparency is expected to deliver. The adoption of the 'High Level Principles on fiscal transparency' is based on the belief that access to high quality information, meaningful public participation, and effective accountability mechanisms:

- enhance the integrity, quality and implementation of fiscal policies,
- increase the legitimacy of and trust in government,
- increase willingness to pay taxes and provide financing,
- reduce corruption,
- strengthen the effectiveness of development assistance,
- and thereby strengthen the efficiency, equity, effectiveness, stability and sustainability of fiscal policies and enhance the likelihood that fiscal policies have positive economic, social and environmental impacts.

These expectations towards fiscal transparency are supported by empirical studies which have found that fiscal transparency improves fiscal performance,⁷ lowers sovereign borrowing costs,⁸ decreases corruption,⁹ and limits creative accounting.¹⁰ The International Monetary Fund finds that budget transparency "helps to highlight potential risks to the fiscal outlook that should result in an earlier and smoother fiscal policy response to changing economic conditions, thereby reducing the incidence and severity of crises."^{11,12}

Sound empirical evidence in support of the high hopes placed on fiscal transparency is, however, only about to accumulate, which can be explained by the relatively short period of research in this field which covers no more than approximately the past 10 years. The following section summarises in more detail the research in the fields which have the biggest relevance in the context of Belarus: The impact of fiscal transparency on financing costs, and on the efficiency of public expenditure through the use of performance-informed PFM.

⁶ Petrie (2013).

⁷ Alt / Lassen (2006a), and Alt / Lassen (2006b).

⁸ Glennerster / Shin (2008), and Hameed (2011).

⁹ Reinikka / Svensson (2004).

¹⁰ Alt et al (2012).

¹¹ IMF (2007).

¹² Literature review based on Wehner / de Renzio (2013); and Petrie (2012).

Impact of fiscal transparency on financing costs

There is ample evidence that higher levels of fiscal transparency have a positive and significant impact on sovereign ratings - and thereby on financing costs. In developing economies, this can be explained by the direct effects of reduced uncertainty as a result of more and better-quality information being available.¹³ A study by the IMF finds that fiscal transparency, in particular risk disclosure, is associated with better sovereign bond ratings and improved access to international capital markets. Improvements in the amount of information on macro-fiscal risks, contingent liabilities, and quasi-fiscal activities published lead to measurable improvements in credit ratings.¹⁴ Research based on a sample of 23 emerging economies showed a statistically significant decline in borrowing costs as a result of higher degrees of fiscal transparency.¹⁵ This study has used the publication of IMF reports, incl. Article IV staff reports, Reports on Observance and Codes ROSC, and macroeconomic statistics according to the Special Data Dissemination Standard (SDDS) as an indicator to assess the level of fiscal transparency.¹⁶

Impact of fiscal transparency on performance-orientation and efficiency of public expenditure

Amongst the recommendations put forward by the PER for improved efficiency of public expenditure - notably in the public health and education sectors - is the introduction of performance-orientation in the budget process and of performance-management in public service delivery.¹⁷ The transition towards performance-orientation in budgeting and management of public expenditures is, indeed, a trend that has been widely adopted by many countries throughout the world, including (former) transition economies (incl. Russian Federation, Poland, Turkey, Korea, and others).¹⁸ Research and evaluation shows that performance-orientation in public spending contributes to improved allocative and productive efficiency. This correlation is even more evident when individual sectors, instead of the whole of government spending, are being looked at. Sectors to benefit most from stronger performance orientation include public health and education. To become meaningful, performance-oriented budgeting and management of public finances needs to be supported by *performance information*. Performance information includes a variety of data and evaluations / assessments which link the budget (i.e., financial data) with non-financial results. Some authors have coined the term *performance-informed budgeting* (PIB) to highlight the close dependency of performance-budgeting and -management with the data and other information needed to feed this process.¹⁹

Whilst there exists a correlation between PIB and the efficiency of public expenditure, PIB alone will not yet lead to improved efficiency of public expenditure. PIB comprises not only a changed set of methods, indicators and allocation formulas applied in the budget planning and allocation phase, but also requires strengthened routines for control, audit, and accountability. In this sense, PIB needs to be implemented as an integral part of a more comprehensive reform of the system of public administration to be successful. It is in this sense of a changed approach to governance that performance-orientation and fiscal transparency are interlinked.

2.3 Tools and measures

The set of tools and measures for fiscal transparency comprises (i) sources (types of reports) which are recommended to be produced and published, and (ii) standards regulating the quali-

¹³ Arbatli / Escolano (2012).

¹⁴ IMF (2008).

¹⁵ The study used data from the years 1999 - 2002; the countries included e.g. Poland, Russia, Turkey, Venezuela, Brazil.

¹⁶ Glennerster / Shin (2003).

¹⁷ PER (2013).

¹⁸ OECD Government at a Glance (2013), http://www.oecd-ilibrary.org/governance/government-at-a-glance-2013/performance-budgeting-practices-at-the-central-level-of-government-2011_gov_glance-2013-table68-en.

¹⁹ Aritzi et al (2010); Robinson / Brumby (2005); Qi (2012); Chevauchez (2014).

ty of the data and other information provided in these reports. Sources of information which are recommended to be produced for fiscal transparency comprise:

Pre-Budget Statement, Executive's Budget Proposal, Citizens Budget, Enacted Budget, In-Year Reports, Mid-Year Review, Year-End Report, and Audit Report

Producing these types of reports is recommended by the Open Budget Initiative,²⁰ as well as by the IMF and the OECD.

Standards for providing data include the International Public Sector Accounting Standards (IP-SAS), International Standards of Supreme Audit Institutions (ISSAI), Government Finance Statistics Manual (GFSM), IMF Special Data Dissemination Standard (SDDS).

The recently updated IMF Fiscal Transparency Code of 2014 is less explicit in setting normative standards or 'checklists' for fiscal transparency and rather develops *principles* for fiscal transparency. For the purpose of making these principles operational, the Code defines a matrix of practices. Individual indicators are suggested to assess the current status of fiscal reporting in a country as 'basic', 'good', or 'advanced' practice. The description of practices refers to types of documents and the quality-standards of the data contained therein. An excerpt of the Code's structure is presented in Table 1; the full Code can easily be accessed on the internet.

An important aspect to the question about the 'right tools' for fiscal transparency has been added to the literature already in the early days of fiscal transparency initiatives. Heald (2003) argues that the specifics of the needs of the audiences are an important part of the context of fiscal transparency. Government financial reporting is not necessarily easy-to-understand information, and interpretation of the data will be subject to the specific interests of those who access it. This argument has been taken further and adapted to today's realities with their much greater degree of information available through technology-based tools. Justice et al (2014) conclude that "the quality of fiscal transparency is at least as important as its quantity: Quality [...] can broadly be understood as a function of the accuracy, sufficiency and usability for decision-making purposes by public officials, citizens, creditors, and other stakeholders of information disclosure and presentation." They also conclude that "different stakeholders need different information: Different users of information have different decisional interests and different abilities to make use of information."

In summary can be stated that, whilst there is a set of tools which is generally recommended to be applied for ensuring fiscal transparency, there is no uniform global standard, and fiscal transparency tools will always need to be adjusted to the needs of users in any specific country context.

²⁰ The Open Budget Initiative (OBI) is a global research and advocacy programme to promote public access to budget information and the adoption of accountable budget systems; cf. OBI methodology <http://internationalbudget.org/what-we-do/open-budget-survey/research-resources/methodology/>.

Table 1: Selected Principles and Practices according to the IMF Fiscal Transparency Code

#	Dimension	Principle	Practices		
			Basic	Good	Advanced
1	FISCAL REPORTING	Fiscal reports should provide a comprehensive, relevant, timely, and reliable overview of the government’s financial position and performance.			
1.1	Coverage	Fiscal reports should provide a comprehensive overview of the fiscal activities of the public sector and its subsectors, according to international standards.			
1.1.1	Coverage of Institutions	Fiscal reports cover all entities engaged in public activity according to international standards.	Fiscal reports consolidate all central government entities according to international standards.	Fiscal reports consolidate all general government entities and report on each subsector according to international standards.	Fiscal reports consolidate all public sector entities and report on each subsector according to international standards.
...					
1.4.	Integrity	Fiscal statistics and financial statements should be reliable, subject to external scrutiny, and facilitate accountability.			
1.4.2	External Audit	Annual financial statements are subject to a published audit by an independent supreme audit institution which validates their reliability.	An independent supreme audit institution publishes an audit report on the reliability of the government’s annual financial statements.	An independent supreme audit institution publishes an audit report stating whether the government’s annual financial statements present a true and fair view of its financial position and without a disclaimer or adverse audit opinion.	An independent supreme audit institution publishes an audit report consistent with international standards which states whether the government’s annual financial statements present a true and fair view of its financial position and without major qualifications.
...					
2	FISCAL FORECASTING AND BUDGETING	Budgets and their underlying fiscal forecasts should provide a clear statement of the government’s budgetary objectives and policy intentions, and comprehensive, timely, and credible projections of the evolution of the public finances.			
...					
2.3	Policy Orientation	Fiscal forecasts and budgets should be presented in a way that facilitates policy analysis and accountability.			
2.3.2	Performance Orientation	Budget documentation provides information regarding the objectives and results achieved under each major government policy area.	Budget documentation includes information on the inputs acquired under each major government policy area.	Budget documentation reports targets for, and performance against, the outputs to be delivered under each major government policy area.	Budget documentation reports targets for, and performance against, the outcomes to be achieved under each major government policy area.

Source: IMF (2014a).

2.4 Assessments and indicators

As a result of the growing attention which is paid globally to fiscal transparency, a growing number of fiscal transparency indicators are becoming available. A short overview of the most prominent assessments and indicators is given below:

IMF Fiscal Transparency Evaluation (FTE)²¹

FTE are produced by the IMF at the request of the country to be reviewed. FTE evaluate a country's PFM system against the criteria of the Fiscal Transparency Code. So far, 8 countries have been reviewed and 6 reports published (Russian Federation, Portugal, Ireland, Bolivia, Mozambique, Costa Rica). The objective of the FTE is to provide countries with assessments of their PFM systems' capacity to deliver an accurate picture of the status of the public finances as a basis for economic policy decisions. FTE do not only provide assessments, but also formulate recommendations for further reform.

Open Budget Survey - Open Budget Index OBI²²

The Open Budget Survey measures the state of budget transparency, participation, and oversight in countries around the world. It consists of 125 questions and is conducted by independent researchers in the countries assessed. The majority of the questions assessed relate directly to the public availability and comprehensiveness of the eight key budget documents that governments are recommended publish at various points of the budget cycle. In order to allow for comparisons across countries and over time, the survey compiles the Open Budget Index (OBI), a simple average of the quantified responses for the 95 Survey questions that are related to budget transparency. The OBI assigns each country a score that can range from 0 to 100. The Index is published bi-annually; the latest available OBI of 2012 covered 100 countries. Belarus is so far not covered by the OBI.

Public Expenditure and Financial Accountability Programme (PEFA)²³

The Public Expenditure and Financial Accountability (PEFA) Programme produces the most widely officially acknowledged assessments of countries' PFM systems. In its current version, the PEFA system of indicators does not contain dimensions to specifically assess fiscal transparency. PEFA comprises indicators to assess the *effectiveness* of, e.g., internal control systems, taxpayer registration and tax collection, and also an indicator to assess public access to key fiscal information. The PEFA assessment framework is currently undergoing a revision of its indicators. This revision will also take into account aspects of transparency and public participation tools and is expected to be released in 2015. PEFA assessments for Belarus have been done in 2009 and 2014.

3 Fiscal transparency in Belarus

3.1 Data availability

Availability of fiscal information

Key information about the budget cycle is expected to be sufficiently covered by eight reports: Pre-budget statement, executive's budget proposal, enacted budget, citizen's budget, in-year reports, mid-year review, end-year report, and audit report. These reports reveal the process of formulation, approval, execution and evaluation of the budget. Most of these reports are produced in Belarus, which makes analysis of the public finance sector performance manageable for any audience. However, there are some shortcomings that limit the accessibility of the budget data for general public.

- Reports that cover stages of the budget formulation are not published. Related information can be obtained only from official statements to the mass media and articles in the journal published by the Ministry of Finance.

²¹ <https://www.imf.org/external/np/fad/trans/index.htm>.

²² Done by the Open Budget Initiative, <http://internationalbudget.org/what-we-do/open-budget-survey/>.

²³ <http://www.pefa.org>.

- Citizen's budget is not introduced in Belarus, so information in stylized and simplified form is not available for the general public.
- In-year reports are published monthly and quarterly. Monthly reports are available in the Belstat monthly bulletin²⁴ and at the website of the Ministry of Finance.²⁵ The quarterly reports are published by the Ministry of Finance within GFS reporting²⁶ and domestic budget accounting.²⁷ These reports present information about budget execution according to different classifications and different levels of budget consolidation. However, all of them are aggregated, while detailed reports are produced, but not publicly available.
- The most detailed information about public finances is presented in the law on the enacted budget. It presents detailed data on revenues and expenditures in economic and functional classifications, as well allocation of expenditures by state-agencies and programmes. However, the law covers only the central government budget, while data on general government sector is not published.

Table 2: Availability of fiscal information: Publication of standard reports in Belarus

	produced (✓) publicly available (✓✓)	Comments on availability
Pre-Budget Statement	(✓)	According to the Art 85 of the Budget Code the project of the main directions of the fiscal and tax policy for the upcoming year should be presented to the government before May, 1. It is not made public.
Executive's Budget Proposal	(✓)	Budget proposal is discussed and presented to the government, parliament and must be approved by the President. The initial proposal is not made public.
Enacted Budget	(✓✓)	The enacted budget is set in a law and is published at the web-site of the Ministry of Finance and in the legislation.
Citizens Budget		Is not prepared in Belarus.
In-Year Reports	(✓✓)	There are numerous types of reports that present current trends in public revenues and expenditures on a monthly and quarterly basis. Detailed reports are not publicly available.
Mid-Year Review		Is not prepared in Belarus.
Year-End Report	(✓✓)	Is set in a law on adoption of execution of the annual budget. It is published in legal databases and at the website of the Ministry of Finance.
Audit Report	(✓)	Is prepared by the State Control Committee and is a prerequisite for adoption of the Year-End Report. Is not made public.

Source: Own compilation.

Quality of statistics: compliance with international standards

Belarus' statistical reporting complies with international standards to a large extent. This covers public finance statistics as well. Belarus reports fiscal data within Special Data Dissemination Standard (SDDS) and Government Financial Statistics (GFS) of IMF. The SDDS reports of the IMF do not highlight any significant drawbacks of the data and its timeliness.²⁸ The IMF Article IV staff reports also stress consistency of the statistical data and soundness of the methodologies applied. However they stress some areas within public finance statistics that need improvement: "classification of some expenses (e.g. subsidies to corporations, social benefits to households, capital transfers to corporations); inconsistency between GFS and

²⁴ This section is not published online.

²⁵ http://minfin.gov.by/budget_execution/analytical_information/.

²⁶ <http://minfin.gov.by/gfs/f80ad5490c7ea984.html>.

²⁷ http://minfin.gov.by/budgetary_policy/analytical_reports/.

²⁸ IMF (2013)

monetary data; valuation of assets and liabilities (at nominal or market value); and compilation for public corporations".²⁹

The World Bank Reports on the Observance of Standards and Codes do not find structural shortcomings in the statistical standards. Still it recommends reforms, especially in financial reporting, accounting and auditing standards³⁰. Belarus is not applying the International Public Sector Accounting Standards (IPSAS).

A more detailed analysis of the public finance data was conducted by the World Bank in the scope of the PEFA report. It paints a fairly mixed picture. On the one hand, budget classification and accounting is reported to be well-structured, consistent, and comprehensive. On the other hand, there are deficiencies in the extra-budgetary activities reporting, as well as in public access and external control.³¹

Apart from these, not many other assessments made by international organisations are available. Belarus is not covered by the Open Budget Index, and so far has not joined the Open Government Partnership.³²

Completeness of information

Public finance statistics do not completely present financial flows within the public sector. They cover only the general government sector, while sector of the state-owned enterprises is not accounted for. However, assets and liabilities of SOEs, which represent a significant share of Belarus' economy,³³ may significantly influence the stance of the general government accounts, as state enterprises and banks tend to rely on regular public support. A thorough analysis of the fiscal policy risks stemming from the SOEs financial stance is hindered by the absence of clear boundaries between the public and the private sector.³⁴

A significant share of the public sector in the economy also implies the presence of quasi-fiscal activities, which are not fully reported:

- There is the wide-spread practice of directed lending by the banking sector under the government programmes. A part of the directed loans are managed by the Development bank, established by the state to finance state programmes. Its liabilities are not fully covered within the public finance accounting process.
- The practice of price regulation leads to cross-subsidization (in the utilities sector, agri-food sector, etc.) that is not accounted for in the budget reports.
- SOEs still fulfil some social policy functions.

The PEFA report stresses also the fact that budget reports miss information on extra-budgetary flows related to the own funds of the budget institutions, which makes analysis of the public finance based on budget reports biased. Another issue that will need more attention in the future are public-private partnerships and the related increase of contingent liabilities of the public sector. Nowadays contingent liabilities are reported within public debt statistics and are regulated by the annually set ceiling.

²⁹ IMF (2014b).

³⁰ World Bank (2009).

³¹ PEFA (2014).

³² Open Government Partnership (OGP); The Open Government Partnership is a multilateral initiative that aims to secure concrete commitments from governments to promote transparency, empower citizens, fight corruption, and harness new technologies to strengthen governance. It was launched in 2011 and, since then, has grown from 8 countries to 65 participating countries. In all of these countries, government and civil society are working together to develop and implement ambitious open government reforms. For several topics, the OGP has established dedicated working groups. These currently include: a Fiscal Openness Working Group, a Legislative Openness Working Group, an Access to Information Working Group, an Open Data Working Group, and an Openness in Natural Resources Working Group. <http://www.opengovpartnership.org/sites/default/files/attachments/FOWG%20Draft%20Workplan.pdf>.

³³ See Ehrke et al (2014) for details.

³⁴ Official statistics treat as state owned enterprises only those with 100% state ownership.

External Audit

External control over the execution of the general government budget is produced by the State Control Committee (SCC). The PEFA report stresses that “the coverage of SCC audits is reasonably comprehensive but the scope of work is limited”.³⁵ The SCC produces careful and full-fledged audit of the use of budget funds and state property in accordance with the legislation and its compliance with the enacted budget. However, the main focus of this control is on the financial (‘compliance’) audit. Audit of efficiency of public spending (‘value-for-money audit’) is performed by the SCC to a much lesser extent.

Results of the audit are not publicly available. However, some information is presented via mass media after its adaptation to the related format.

3.2 Forecasts and risks management

The transparent decision making in the public finance sector implies medium and long-term forecasting of the fiscal indicators. It allows economic agents to adjust their behaviour according to the forthcoming changes in the social, public investment, and tax policies. This element of fiscal transparency is missing in Belarus, as the budget cycle is limited to one-year coverage.³⁶ Medium-term planning is not introduced due to high uncertainties related to the overall macroeconomic situation and the low predictive power of economic forecasts.³⁷ Economic policy aimed at macroeconomic stabilization, clearly assigned goals of monetary policy, and an approved roadmap of the measures aimed at sustaining long-term growth are preconditions that will minimize uncertainties and allow for effective economic and fiscal forecasting.

Elements of risks management are introduced in the budget procedures in order to react to the challenges resulting of high uncertainties within the domestic economic environment and external factors. The PFM system of Belarus allows for a reserve fund of the Government, a Presidential reserve fund, and local government reserve funds that provide buffers for financing unexpected expenditures. According to the legislative framework, the volumes of the Government and President reserve funds must not exceed 2% of the revenues of the central government budget.³⁸ The reserve fund of the Government and local government reserve funds are aimed at covering costs related to mitigating consequences of natural disasters and financial assistance of legal entities. The sources of the Presidential fund are used according to the decisions of the President. For instance, it was used to avoid a sequestration of the general government budget in 2009. The anticipated negative gap between actual and initially planned revenues was assigned to this fund. Simultaneously, public expenditures that were expected to be cut were also reallocated to this fund, implying that they would be financed in case public revenues do not actually fall.³⁹ Planned expenditures of the President and Government funds are included in the central government budget as separate lines, whilst execution report does not distinguish these expenditures as they are distributed across other lines of the budget (social policy, general government expenditures).

4 Potential benefits for Belarus

This chapter summarises the prevailing shortcomings in fiscal transparency - in the broader sense as applied in this paper - in Belarus and outlines potential benefits which the country could gain by addressing these shortcomings.

The **weak connection of public finance management with policy objectives** is highlighted in reports produced by rating agencies, as well as in reports focusing on public expenditure

³⁵ PEFA (2014).

³⁶ Budget programmes which are typically covering a multi-year period provide data for total cost, and a forecast of costs for the two years following the current budget year.

³⁷ Official economic forecasts largely serve as a set of target indicators rather than scenario predictions of economic prospects.

³⁸ Budget Code of Belarus, Art. 43.

³⁹ <http://news.tut.by/economics/140279.html>.

management and accountability.⁴⁰ Weak policy guidelines result in limited predictability of future developments in the field of public finances, as well as in insufficient policy-orientation and guidance in the annual budget process. Improvements in this area can be assumed to have a positive effect on investors and rating agencies' perception of Belarus' mid-term fiscal perspectives. More clearly developed policy guidelines, along with more clearly developed roles and competencies of government agencies in the budget process (namely, stronger roles of the Prime Minister and the Ministry of Finance), as well as a mid-term perspective for the budget process can be expected to result in a more transparent and effective allocation of public funds.

Better developed policy guidelines need to be **based on credible, comprehensive, and timely data**. This comprises high-quality macroeconomic forecasting, as well as reliable information about the amounts of contingent liabilities and other fiscal risks which are currently not duly reflected in the fiscal balance. For fiscal risks to be better controlled and mitigated, they need to be properly understood and assessed. When fiscal risks can be adequately assessed, room for manoeuvre in the management of public funds may widen, and credit ratings may benefit. More information about fiscal risks might, however, also result in tightened room for fiscal decisions, and credit ratings might be adjusted downwards. More transparency about the actual fiscal situation and related risks is, however, positive even in such a negative-at-first-sight scenario as this allows for mitigation measures, potentially including international support.

Whilst the process of obtaining, processing and exchanging budget execution data is of good quality for line-item (input-based) budgets, this is not necessarily the case for budget programmes, including subsidies to SOEs included in budget programmes. **Shortcomings in data collection during implementation and evaluation of budget programmes** appear to be mainly due to more complex performance criteria which include non-financial parameters. Our findings suggest that insufficient reliability and timeliness of data processing and -exchange is to be explained by insufficiently streamlined 'ownership' of budget programmes, including SOE-subsidies. With budget programmes accounting for ca 16% of total budget expenditure (FY 2015 state budget), proper management, control, evaluation and audit of effectiveness is, however, of crucial importance for overall efficiency and effectiveness of public spending. Reform initiatives to streamline the management of budget programmes - in particular where SOE subsidies are involved - have been proposed by the government. This can be expected to improve the situation if adopted and implemented.⁴¹

In addition to government-internal issues of managing budget programmes, there are also aspects which would justify **increased transparency vis-a-vis the public**. Government programmes in general are mostly designed to address issues which have a direct impact on the population; in addition, where SOEs are involved, their operation guarantees employment for a large share of the population. Information about measures to support these programmes, as well as about the results which these state-financed programmes deliver is, therefore, of direct relevance for the public. The government will gain trust and public support when communicating more openly with the public. Changes, up to cuts where necessary, in state-financed programmes can be more credibly explained when the economic rationale behind such changes or cuts can be credibly explained.

Focusing on increasing public access to more budget reports in general, as recommended by the overall principles of fiscal transparency is, on the other hand, not considered of top priority for Belarus. Public access to key fiscal information is at a satisfactory level (PEFA PI-10, score B; improved since 2009). Moreover, tradition and culture in Belarus on the one hand, and resources and capacities at government organisations on the other hand, appear to be not yet ready for making active use instruments of public *participation* in managing public funds. Instruments as citizen's budgets (which is being made available in, e.g., the Russian Federation), participatory budgeting (where good experience has been made in, e.g., the Philippines), or public participation in monitoring public procurement or in the audit of public finances require resources, skills and capacities of government organisations and their staff, as

⁴⁰ Moody's (2014a); Moody's (2014b); PER (2011); PER (2013); PEFA (2014).

⁴¹ This paper does not attempt to assess to *quality* of the proposed improvements to the management of budget programmes. It will be important to obtain, collect, process, and evaluate the 'right' (amount of, and type of) data. cf, especially Chevauchez (2014) in this respect.

well as of civil society organisations. These resources, skills, and capacities will need to be given more time to develop before such instruments can be meaningfully applied. Instead, the Belarusian society would benefit from increased access to relevant data, which shall be made available in user-friendly format.

5 Policy Recommendations

To address the above outlined challenges, a number of policy decisions are recommended. These are outlined in the following chapter. The measures identified and proposed here are in a format which allows for implementation in a **short-term perspective**. In doing so, this paper aims to contribute to **kick-starting** the process of preparing and implementing a comprehensive PFM modernisation programme for which financial and technical support has been envisaged by the World Bank.⁴² Recommendations are based on findings from discussions with the Ministry of Finance, Ministry of Economy, State Control Committee, and the study of recent assessment reports, in particular, the PER and PEFA.

I.) Continue improving the legislative framework

Ia) - to improve credibility of budget planning and allocation

The Budget Code defines the documents which are required to be produced in the period leading up to the draft annual budget bill. Articles 83, 85, and 86 describe in detail the "Forecast of the key parameters of the economic development of the Republic of Belarus"; "Forecast of the most essential monetary indicators of the Republic of Belarus" (Art 83); "Main directions of fiscal and tax policy of the Republic of Belarus" (Art 85); and "Mid-term financial programme" (Art 86). For neither of these documents, the Budget Code requires their approval or adoption. **The legislative framework can be improved by making the individual stages of the budget process - in particular the forecasting and formulating of objectives stage - more credible through mandatory approval of forecasting and planning documents.** (cf. also PI-11 (ii)⁴³ of the PEFA report - score: C)

Ib)- to improve performance orientation

The Ministry of Finance is developing a concept for introducing programme-based budgeting and mid-term planning which, amongst other, proposes amendments of the current practice towards a comprehensive coverage of revenue and financing sources for the implementation of budget programmes. For the purpose of making the budget process credible and reducing fiscal risks this is to be considered with priority and shall be made a mandatory requirement as soon as possible - if needed, independently (i.e., earlier) than the completion and adoption of the Ministry of Finance concept in its entirety.

The Ministry of Finance concept also includes details how to better define performance criteria for budget programmes. This will require further work and shall be treated with priority.

With the objective of improving the efficiency of public expenditure, the Ministry of Economy has prepared a draft legal act regulating the design and implementation of development programmes. These development programmes are a tool for the implementation of the socio-economic development strategy 2016-2020, and the draft legal act develops mechanisms for the allocation of subsidies to SOE as part of the development programmes. It is recommended to **clarify the relation between the development programmes as per this draft legal act and current legislation like, e.g., the budget programmes** (according Art. 87 of the Budget Code), as well as with draft legislation to be adopted in the future.⁴⁴ Compliance with

⁴² World Bank PID (2014)

⁴³ „Orderliness and participation in the annual budget process - Dimension (ii) Clarity / comprehensiveness of and political involvement in the guidance on the preparation of budget submissions"

⁴⁴ Other legislative acts concerned include the Resolution of the Council of Ministers of 31.03.2009 № 404 "On Approval of the Regulation on the formation, financing and monitoring the implementation of national, regional and sectoral programs and repealing certain decrees of the Council of Ministers of the Republic of Belarus" (reg. № 5/29550 of 04.09.2009).

other legislation provided, it is recommended to consider **adopting the draft legal act with high priority** so that these regulations can be fully applied for the implementation of the socio-economic development strategy 2016-2020. The draft legal act allocates responsibility for the **development of rules for evaluation of efficiency of budget programmes** to the Council of Ministers and the Development Bank. This work will need to be given due attention, and sufficient resources for this need to be made available.

II.) Improve exchange of data between government agencies

The activities of SOEs are under the auspices of the related line-ministries. This leads to a great number of organisations involved in data-collection, -transmission and control. Our findings suggest that the process of data collection and -processing under the current system is not sufficiently efficient, and does not allow for a comprehensive coverage of all fiscal risks, incl. contingent liabilities. For the purpose of making data collection more predictable and reliable it is recommended to clarify and streamline procedures for data collection and exchange between government organisations. The proposed legal act concerning design and implementation of development programmes can be expected to improve this situation by concentrating responsibilities in a smaller number of government organisations. The adoption of this provision and effective implementation is recommended. Alignment with the planned Finance Management Information System (FMIS, which shall be implemented as part of the World Bank PFM project) shall be considered and, if appropriate, implemented.

III.) Improve the quality and accessibility of budget-related data

The **annual budget** is available on the Ministry of Finance website. The data is presented there in pdf-Format. This allows for full access to budget information, however, with limited user-friendliness. User-friendliness can be enhanced by publishing data in machine-readable format like Excel (Example: Budget of the Russian Federation).⁴⁵ Also, the published budget would benefit from more information being published about the 78 (2015) budget programmes which make up for ca 16% of total budget expenditure. Whilst each budget programme is indicated with full details, thus providing for additional documentation to be found in public sources, including key information and providing a direct link to the budget programme 'passport' would make it easier to work with budget data. Beyond the simple publication of machine-readable budget data, examples for more sophisticated tools to visualise and explain budget data abound in international practice.⁴⁶ Implementing these, however, is resource-intensive and not considered of immediate priority for Belarus.

Producing and publishing **budget execution reports** in a more comprehensive and user-friendly format is recommended as a measure to increase trust and confidence of both, the public and expert community within Belarus, as well as of international organisations and rating agencies. It would also serve the purpose of developing capacities of Ministry of Finance staff. To be more comprehensive, budget reports should be expanded to also include a narrative part which discusses deviations from planned revenue / expenditure targets, performance of government programmes, and details about guarantees financed from the budget.⁴⁷

The **Development Bank of the Republic of Belarus** is the government's main vehicle to finance long-term and capital-intensive investment projects as defined by government programmes. Fiscal transparency and predictability can be improved and fiscal risks minimised by **making the Development Bank the sole implementer of government-financed lending programmes** (as is planned by the authorities but not yet fully implemented), and by **including detailed information in both, the budget, and the budget execution report**. Cur-

⁴⁵ http://minfin.ru/ru/performance/budget/federal_budget/budj_osp/index.php.

⁴⁶ The budget of Germany is presented on a dedicated website www.bundeshaushalt-info.de; Tools like a citizen's budget are recommended by advocates of budget transparency and subsequent manuals and guidelines are available. Example: The Power of Making It Simple: A Government Guide to Developing Citizens Budgets <http://internationalbudget.org/publications/the-power-of-making-it-simple-a-government-guide-to-developing-citizens-budgets/>.

⁴⁷ Budget execution reports of the Russian Federation provide an example for more comprehensive budget execution reports: http://minfin.ru/ru/performance/budget/federal_budget/budgeti/11-14/.

rently, aggregated amounts are included in the budget, but no information about government-financed lending implemented specifically through the Development Bank is included in the budget execution report (2013).

IV.) Strengthen the role of the State Control Committee in improving efficiency of public expenditure

The SCC performs well in its function as a control body. There is, however, untapped potential for the SCC to also perform the function of a modern audit institution. The SCC has already obtained experience in implementing performance audits (also known as 'value-for-money audit') in joint work with the audit institutions of the Russian Federation and Kazakhstan in the scope of the Eurasian Customs Union. This experience can be applied to implement performance audits of budget institutions and SOE in Belarus. Corresponding methodologies have been developed and enacted since 2012.⁴⁸ **Implementing more performance audits will contribute to raising the efficiency of public expenditure in Belarus by providing relevant information about inefficient spendings** to the Ministry of Finance, Ministry of Economy and the spending units concerned. It will also help the SCC to align its work with the standards of international organisations of audit institutions (INTOSAI, EUROSAI) in which the SCC is a member and which have assisted in developing the performance audit standards. Finally, it is recommended that the **SCC makes more of its findings available for public access**. The SCC has established good practice of responding to concerns and proposals raised by citizens and individual business entities in cases of illicit use of public funds. This suggests that the role of the SCC is accepted by the public, and it is recommended to tap the potential for identifying ineffective use of public funds through a more substantial two-way communication between SCC and the public.

V.) Utilise the potential for PFM reform

In the recent past, Belarus has benefited from substantial analytical work undertaken by international experts who have analysed the system of public expenditure and the public financial management system in general. A number of recommendations - albeit of rather general nature - have resulted from this work which has been carried out in close and fruitful cooperation with Belarussian authorities. The World Bank has committed to support reforms in this area through a USD 1.2 m grant, and a potential loan to support PFM reform. The IMF, EU, UNDP, and other bilateral donors can also be expected to support reform in the area of PFM. This is to say that the current situation provides a *window of opportunity* for addressing weaknesses and inefficiencies in the allocation, implementation, reporting and evaluation of public expenditure. **The most important recommendation, therefore, is to use this window of opportunity and to make sure the maximum possible impact can be derived out of the resources made available.**

For this, PFM reforms need to be given **clear objectives and priorities, and need to be coordinated by, and with active involvement of the top of the Government and the Presidential Administration**, to avoid a number of issues being addressed in isolation from each other. Currently, various reform initiatives are being developed and proposed at the level of line ministries which demonstrate a high level of commitment for reform. Leadership, coordination and a clear allocation of roles and responsibilities from the top of the executive is essential for successful implementation. PFM/public expenditure reform will need to involve more than just the Ministry of Finance and subordinated bodies at Republican and subnational level. Instead, the Ministry of Economy, Belstat, line ministries, and the SCC will also need to be involved.

⁴⁸ In 2012, the SCC Chairman issued Instruction № 38 of July 18, 2012 to approve the Methodological Recommendations on Performance of Audit by the SCC Bodies. These were developed based on performance audit standards and guidelines accepted in the framework of the INTOSAI, EUROSAI, and ASOSAI. SCC is a member of INTOSAI and has access to its methodological resources." (PEFA, p 76).

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