

PHILIPPINES-AUSTRALIA

**PUBLIC FINANCIAL MANAGEMENT
PROGRAM**

PROGRAM DESIGN DOCUMENT

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In memory of a great colleague, a deep thinker, and a dedicated public servant for the welfare of the Filipino people

“To be sure, the task remains a challenge, but not an insurmountable one. Installing a results-based approach is a test of three Ps: persistence, perseverance and partnership. Persistence, because one needs to vigorously pursue, despite the many obstacles, the objective of the program. Perseverance, because it is a test of patience, fortitude and compassion, all at the same time. And partnership, because it takes government, non-government, as well as private sector stakeholders, working together towards a common goal, to successfully implement a revolutionary program such as the PEM Reform”

Professor Emilia T. Boncodin, 2004

Acronyms

AAR	Annual Audit Report	MTEF	Medium Term Expenditure Framework
ABM	Agency Budget Matrix	MTPDP	Medium Term Philippines Development Plan
ADB	Asian Development Bank	NCAs	Notice of Cash Allocations
APDAS	Australia-Philippines Development Assistance Strategy	NEDA	National Economic and Development Authority
AusAID	Australian Agency for International Development	NGAS	New Government Accounting System
BARs	Budget Accountability Reports	NGICS	National Guidelines on Internal Control Systems
BEDs	Budget Execution Documents	OEOs	Other Executive Offices
BESF	Budget of Expenditures and Sources of Financing	OP	Office of the President
BIR	Bureau of Internal Revenue	OPIF	Organizational Performance Indicators Framework
BTr	Bureau of the Treasury	PAPs	Programs, Activities and Projects
COA	Commission on Audit	PBS	Paper on Budget Strategy
CPBD	Congressional Planning and Budget Department	PDD	Program Design Document
CSOs	Civil Society Organisations	PDF	Philippines Development Forum
DBCC	Development Budget Coordination Committee	PEFA	Public Expenditure and Financial Accountability
DBM	Department of Budget and Management	PEGR	Partnership for Economic Governance Reforms
DepEd	Department of Education	PER	Public Expenditure Review
DOF	Department of Finance	PETS	Public Expenditure Tracking Surveys
DPWH	Department of Public Works and Highways	PFM	Public Financial Management
DSWD	Department of Social Welfare and Development	PFMP	Public Financial Management Program
EERs	Effectiveness and Efficiency Reviews	PGIAM	Philippine Government Internal Audit Manual
e-NGAS	Electronic New Government Accounting System	PSC	Program Steering Committee
e-Budget	Electronic Budget System	PTC	Philippine Technical Committees
FY	Financial Year	SAOB	Statement of Allotments, Obligations and Balances
GAA	General Appropriations Act	SAROs	Special Allotment Release Orders
GAD	Gender and Development	SEPO	Senate Economic Planning Office
GDP	Gross Domestic Product	SP	Service Provider
GNI	Gross National Income	SPFs	Special Purpose Funds
GNP	Gross National Product	TA	Technical Assistance
GOA	Government of Australia	TOR	Terms of Reference
GOCCs	Government Owned and Controlled Corporations	USAID	United States Agency for International Development
GOP	Government of Philippines	WB	World Bank
GIFMIS	Government Integrated Financial Management Information System		
IA	Internal Audit		
IAUs	Internal Audit Units		
ICS	Internal Control System		
IFIs	International Financial Institutions		
IMF	International Monetary Fund		
IPSAS	International Public Sector Accounting Standards		
LGUs	Local Government Units		
M&E	Monitoring and Evaluation		
MDGs	Millennium Development Goals		
MDS	Modified Disbursement Scheme		
MFOs	Major Final Outputs		
MOA	Memorandum of Agreement		

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Executive Summary

Improving public financial management (PFM) is central to the Philippines' achieving its development goals. Progress on economic growth, poverty reduction and key social indicators has not been as fast over the past decades as government, the public and development partners had hoped or expected. Speeding up progress will require, amongst other things, a transparent and credible system to manage public resources so there is informed decision-making and effective provision of public goods and services.

Although the Philippines' PFM system is reasonably capable of maintaining an overall fiscal position, its ability to support efficient execution of the government's priority programs is limited. The PFM system could be considered a work-in-progress. The government has made solid gains in introducing a performance budgeting agenda and other reforms over the past decade. However, there is significant scope for improving the way the government uses and accounts for public resources to meet international and Philippine standards of good practice. A number of weaknesses in the PFM system remain, the most fundamental being the generally weak capacity in government agencies to execute the budget as well as the lack of accountability and transparency over the use of appropriated funds.

Why should Australia intervene?

In many countries the practice of PFM is an obstacle to the achievement of poverty reduction objectives. Australia's official development assistance to the Philippines comprises approximately 0.3 per cent of total government expenditure. If Australia is going to make a meaningful contribution to the achievement of key social and economic objectives it needs to use its funds to leverage improvements in the way the Government of Philippines (GOP) uses its own resources. Improving the efficiency and accountability of public fund use and enhancing links to service delivery are essential elements in supporting the GOP to reduce poverty and improving the effectiveness of AusAID's overall country program.

Australia has been engaged in supporting PFM in the Philippines for many years, most recently through the Partnership for Economic Governance Reforms (PEGR) that operated from 2005 to 2010. Australia has an acknowledged comparative advantage in the PFM area, with technical resources at its disposal to identify and mobilise a broad range of PFM expertise through diverse government, academic and industry contacts.

The significant potential benefits of PFM are balanced by substantial risks. The international experience of PFM reform in developing countries shows that implementing change within the civil service is difficult with frequent setbacks. The Philippines system has proved resilient to change and the slow pace of progress can be difficult for development partners with a short term outlook. Progress is not impossible though as many of the reforms to PFM are technocratic in nature and selective support by donors can nurture the progressive elements of government to improve their systems. However, expectation of program achievement should be of modest incremental progress towards realistic long term objectives.

The program's development is taking place in the Philippines election period and transition to a new Administration. As a natural part of the democratic cycle there is some uncertainty in the GOP's policy agenda. Where PFM strengthening is taken up effectively at a whole-of-government level it is anticipated that the program would be called on to provide a higher level of support. On the other hand, if the new government shows little or no sign of committing to comprehensive reform then a reduced level of support to target agencies is expected.

In a positive step the Department of Budget and Management (DBM), Commission on Audit (COA) and the Bureau of the Treasury (BTr) have formed a PFM 'core group' and signed a Memorandum of Agreement to coordinate their efforts on PFM reforms, converging at first to make headway into developing a sound Government Integrated Financial Management Information System (GIFMIS). Sustaining this agreement and institutionalising interdepartmental coordination would constitute an essential building block of effective reform management. The 'core group' is currently finalising a new Philippines PFM Reform Roadmap that will map out strategies for implementing much needed changes to the PFM system.

It is proposed that AusAID go 'back to basics' with this new Public Financial Management Program (PFMP), both in terms of 'the what' - or the outcomes the program aims to achieve; and 'the how' - or the way assistance is provided. Compared with the PEGR, the new program will have a sharper focus on PFM as a means to improving public service delivery and will uncouple the cumbersome implementation arrangements that characterised the former program.

What the program will do

The PFMP is a long term partnership between the Governments of Australia and the Philippines that reflects the long term nature of improving PFM systems. The term of the PFMP is 10 years and will be implemented in five-year phases, with points of review for each phase. In this way, both governments can evaluate the impact of the program and redirect it as needed, while providing the consistent, long-term resources that are required. A mid-term review will take place at the beginning of the fifth year of the program to decide whether the program will continue for a second five-year phase.

The proposed financing from the Australian aid program for the PFMP is up to A\$30 million for an initial five years from 2011 to 2016. There is potential for scalability in resourcing as demand for assistance increases or decreases over time. Actual program expenditure will depend on the extent to which effective use of the funding can be demonstrated. Initially, program financing will cover the first three years (up to A\$18 million), with an extension to years four and five subject to Parliamentary appropriation and the outcomes on an independent evaluation of the effectiveness of the program in the third year.

The PFMP will address the priorities of the Philippines PFM Reforms Roadmap to develop an efficient and effective PFM system in the Philippines, with a focus on budget execution and accountability and transparency to improve the delivery of public

services. This is consistent with the common purpose of the development strategies of both the Philippines (MTPDP) and Australia (APDAS) to improve the effectiveness and efficiency of government spending.

The overall program goal is:

Improvement in the efficiency, accountability and transparency of public fund use in the Philippines to enable better service delivery

This goal represents a long-term commitment by Australia to assist the GOP to achieve incremental improvements in the efficiency, accountability and transparency of the PFM system and its information flows. The PFMP will support oversight agencies and key service delivery departments. It is proposed that in working with service delivery departments the PFMP will prioritise those departments that AusAID already has sector programs with, such as Education and Social Welfare and Development.

The program will pursue four strategic objectives that respond to the highest priority problem statements and address both the supply and demand sides of the program goal. On the supply side, there is a need for government to better allocate and utilise public funds for services delivery and to deliver more timely and reliable reporting of those funds. On the demand side, there is a need to confirm, through both internal and external accountability mechanisms, that budgeted funds are being executed as intended.

The program's four strategic objectives are:

- 1) Increase the efficiency and effectiveness of the allocation, utilisation and reporting of budgeted funds by oversight agencies**
- 2) Improve PFM capability in select departments to enable more efficient utilisation and accountability of public funds for service delivery**
- 3) Generate more timely, reliable and accessible public expenditure management information**
- 4) Strengthen external oversight of public expenditure management linked to physical performance information**

These strategic objectives are the focus for PFMP activities. Other areas of PFM such as tax reform and revenue generation, Government Owned and Controlled Corporations (GOCCs), debt management and procurement are being advanced with the support of other donors and there is less strategic or technical advantage to Australia expanding its engagement into these areas of the Roadmap. However, developments in these areas are linked to the objectives of the program and will need to be observed. Each strategic objective and the proposed focus areas for action are outlined in Section 3.2.

The first phase of activities to be funded by the program will be developed in the program implementation. The type of assistance offered could include: diagnostics

around key aspects of the PFM system; long and short term technical assistance from both local and international advisers to help in the implementation of programs; production of regular ‘hot topic’ papers that inform the internal policy debate within government; and support to the ‘demand side of governance’ through academe and civil society that can work constructively with the bureaucracy and legislature to encourage well informed debate on PFM issues.

How the program will operate

The program will operate in a way that promotes change towards the achievement of an improved PFM system in the Philippines. The program’s engagement strategy for doing this is to: (i) commit support for the long run; (ii) cultivate robust relationships with the PFM stakeholder community; (iii) coordinate resources with key partners so that reforms are resourced adequately and sequenced appropriately; (iv) focus on the enabling environment for service delivery; (v) provide for consistency and flexibility in implementation; and (vi) aim for systemic change in the selection of activities.

The program will, as much as possible, use existing government structures, but recognises that many aspects of GOP policy and interdepartmental coordination around PFM are yet to be finalised. The home of program decision-making and strategic oversight of planning and implementation will be the **Program Steering Committee**. It is proposed the committee comprise the same membership as the GOP PFM ‘core group’ that is composed of senior officials from DBM, COA and BTr, plus representation by the National Economic and Development Authority (NEDA) as the agency responsible for development planning, and AusAID. This way, program assistance will be aligned to the GOP’s own PFM reform priorities. The committee will meet three times a year, or as needed, to consider progress and approve new or changed program inputs.

Within the GOP there are a number of existing technical bodies that are responsible for different aspects of the existing and emerging PFM reforms. A key role of the PFMP will be to foster and encourage the formalisation and active participation of these groups. In terms of PFMP, it is proposed that these groups form a cohort of **Philippine Technical Committees** to provide technical advice and guidance to the program through regular engagement.

It is important that leadership and management of the program have a clear AusAID character and authority to maintain its place in the PFM stakeholder community over the long-term. The **Team Leader** for this program will be an AusAID officer from the Manila Country Office. The program will require consistent, high-level liaison between Australia, the GOP, development partners and civil society to shape a program in support of the GOP’s PFM reform agenda. It is vital that Australia presents a consistent policy position and that this message is delivered by an individual with clear authority. The Team Leader will be supported by a Program Coordinator, also an AusAID officer.

It is acknowledged that no individual Team Leader or Program Coordinator has the capacity to address all the technical issues that are likely to be generated during the

implementation of the PFM reform agenda. The proposed solution is to set aside funding for a **Technical Advisory Team** composed of a small number of experts in specific technical areas who can work closely with key stakeholders, and identify and mobilise a broad range of sector expertise through diverse contacts, possibly in consortia with other institutions. The Technical Advisory Team will be contracted at program implementation and may include full-time, part-time or periodic inputs.

An **Annual Action Plan** of activities will be annually programmed through a formal process for targeting key priorities of the GOP and associated activities. The Team Leader, in collaboration with the various committees and development partners, will develop the Annual Action Plan. Endorsement of the plan will be the responsibility of the Program Steering Committee.

Managing administration of the program will be outsourced to a contracted **Service Provider** that will establish a Program Office in Manila, headed by a Program Manager. It is proposed that the Program Office be located centrally, in offices that are readily accessible to the GOP, AusAID, development partners and civil society. The Team Leader will need to maintain an office in this location also, to provide for structured consultation and liaison, as needed.

The emerging PFM reform agenda, if supported by the incoming Administration, can provide the platform for coordination between **development partners** and government to ensure sufficient resources are available to progress the agenda. The financing needs of the complete package of reforms, as outlined in the PFM Reform Roadmap, will far exceed AusAID's financial capacity to assist. Accordingly, co-financed activities and collaborative analytical work should be actively pursued with development partners under the reform program. The sub-working group on PFM of the Philippines Development Forum (PDF), which AusAID co-chairs with DBM, is an existing forum through which all interested partners can achieve greater collaboration and engagement around PFM reforms.

The rationale for including **civil society** access to the PFMP is to encourage a balance between both government and independent viewpoints on PFM issues and priorities, and to recognise the positive role that civil society can play to independently affirm real gains made in PFM. Similarly, when PFM strengthening efforts need more support, it is understood that civil society has a valid role in pointing this out and making constructive proposals for government to consider and act on, as appropriate.

Monitoring and evaluation of the program will provide management information to ensure the program is heading in the right direction. It will generate performance data to measure progress and performance of the program against agreed indicators linked to the GOP's own PFM reform targets. Monitoring and evaluation will be anchored on the program's logic and results-orientation. It will also be a mechanism for informed decision-making to increase the potential for success. Regular program reporting will be supplemented and verified by external independent evaluations of the effectiveness of the program.

1. Introduction

Design consultations for the Public Financial Management Program (PFMP) began in 2009 when the Governments of Australia and the Philippines recognised it would be mutually beneficial to continue working together to improve the public financial management (PFM)¹ system in the Philippines. This new program builds on the Partnership for Economic Governance Reforms (PEGR), which responded to some of the Government of Philippines' (GOP) high-order public expenditure management goals from 2005 to 2010.

A design mission took place during October and November 2009 to consult widely with government and development partners. An Aide Memoire of the mission's key findings was presented to the GOP on 10 November (Annex 4 refers). The design is informed by the Philippines PFM Reform Roadmap² and a multitude of reports on PFM in the Philippines including the 2007 Public Expenditure and Financial Accountability (PEFA) assessment, conducted by the World Bank in collaboration with the GOP and AusAID, and generally regarded as the most current and comprehensive report on the overall PFM system.³ The PEFA performance indicator summary is provided at Annex 3.

The PFMP is a long term partnership between the Governments of Australia and the Philippines, reflecting international experience that improving PFM systems is a long term endeavour. It is proposed that AusAID go 'back to basics' with this new program, both in terms of 'the what' - or the outcomes the program aims to achieve; and 'the how' - or the way assistance is provided. Compared with the PEGR, the new program will have a sharper focus on PFM as a means to improving public service delivery and will uncouple the cumbersome implementation arrangements that characterised the former program.

The Design Team is indebted to the senior government officials and national and international experts who contributed valuable technical advice and guidance in the preparation of this design document.

¹ Consistent with its popular use amongst government and development partners, this document uses the label of public financial management to refer to practices and processes around the use of Government funds, however, strictly speaking public expenditure management may be a more accurate term to describe the sector.

² The Philippines PFM Reform Roadmap is a collaborative effort by COA, DBM and DOF (BTr) to map out strategies for the implementation of needed PFM reforms in government and will be presented to the new Administration.

³ The PEFA assessment report of the Philippines is not yet publicly available but was accepted by the GOP in late 2009.

2. Analysis and Strategic Context

Improving PFM is central to the Philippines' achieving its development goals. As a lower middle income country, the Philippines does have considerable resources it could bring towards meeting its development objectives. However, progress on economic growth, poverty reduction and key social indicators has not been as fast over the past decades as government, the public and development partners had hoped or expected. Speeding up progress will require, amongst other things, effective service delivery by government in areas like education, health and infrastructure development. A transparent and credible system to manage public resources is crucial for informed decision-making and effective provision of public goods and services.

2.1. Country Context

The Philippines is a lower middle income country with a population of around 90 million people. It has a GNI per capita of US\$1,890⁴, compared to US\$2,010 in Indonesia and US\$2,840 in Thailand. The Philippines was not always at the lower end of middle income Asian countries. The Philippines has achieved positive growth over the past 30 years and real per capita income is now 40 per cent higher than in 1975. However, compared with China (1000 per cent), Thailand (300 per cent), Malaysia (200 per cent) and Indonesia (200 per cent), the Philippines has had steady rather than dynamic growth. This trend appears to have continued to the current day, with the Philippines economy growing by 0.9 per cent in 2009, down from 3.8 per cent in 2008 and a decade high of 7.1 per cent in 2007. Maintaining positive growth during a global recession is significant, but the Philippines 2009 growth is still well below the expected regional average of 6 per cent of GDP and the projected outlook for 2010 and 2011 suggests a continuation of this growth path.

The Philippines economy is unique amongst large developing Asian economies for having a large service sector that comprises approximately three quarters of the economy. The Philippines manufacturing sector is smaller than other major Asian economies and public and private investment is very low. As a percentage of GDP, gross fixed capital formation in the Philippines is 14 per cent of GDP; in Indonesia it is 25 per cent and China 45 per cent. A key driver of the economy is remittances from overseas, which are around 10-12 per cent of GDP. Remittances balance the trade deficit, support the domestic economy, keep a strong flow of foreign currency coming into the country and have kept the economy in positive growth during the global recession.

Progress on the Millennium Development Goals (MDGs) is mixed in the Philippines. Although strong progress has been made in many areas, the Philippines will likely miss key targets in poverty reduction, education and maternal health. The progress on poverty has been particularly concerning. The proportion of the population living below \$1.25 a day in 2006 was 23 per cent or around 20 million people. Some progress has been made with poverty incidence dropping from as high as 35 per cent in 1991. But in

⁴ Source: World Bank estimate.

the last decade poverty reduction has halted and rates are now higher than they were in 1997, even in a period where by historical standards economic growth was relatively strong. Regional comparisons highlight that the Philippines progress has been slow in comparative and absolute terms. Indonesia, Thailand, China and Vietnam all have had greater success in reducing poverty.

Various factors have contributed to the lack of progress on poverty reduction in the Philippines despite the country's economic growth. One is the inequality of income distribution in the Philippines economy which increased in the 1990's and remains relatively high.⁵ Another is the growing population that over the past decade has averaged 2.2 per cent annually. Under these conditions economic growth has not been strong enough to impact positively on people living in the poorer rural areas that mainly rely on the agricultural sector for employment and typically have less access to basic services, lower levels of education and larger families.

The low level of government expenditure on economic infrastructure, social service delivery and poverty reduction programs can also attribute to the slow progress on poverty reduction.⁶ The lower expenditure is partially a consequence of the overall tight fiscal position of the government (see below). Part of the solution to rendering growth pro-poor, and most relevant to this design, is to increase public spending on education, transport and other services, while at the same time improving the efficiency and accountability of public fund use so that funds flow more efficiently to where they are allocated and governance is improved.

2.2. Fiscal Management

Improving fiscal sustainability has been a key priority for the Philippines over the past five years, an objective that has been partially achieved. In 2004, the GOP declared the fiscal position as unsustainable and strong action was needed to head off a fiscal crisis. Subsequently, the headline deficit was successfully brought back under control through a combination of increasing the size and scope of consumption tax⁷, privatizations, shrinking expenditure and strong economic growth.

As shown in Graph 1 on the next page, the budget deficit was reduced from 5.3 per cent of GDP in 2002 to less than 1 per cent between 2006 and 2008 and the government has been able to reduce the size of the debt stock (from 78 to 57 per cent of GDP). The improved fiscal position meant that in 2009, at the onset of the global recession, the

⁵ The Gini coefficient for the Philippines is 44, compared to Malaysia (38), Indonesia (39), Vietnam (39) and Thailand (42) (source: World Bank). The Gini coefficient is used as a measure of income distribution inequality, with 0 implying complete equality while higher scores indicate more unequal distribution and 100 corresponding to complete inequality.

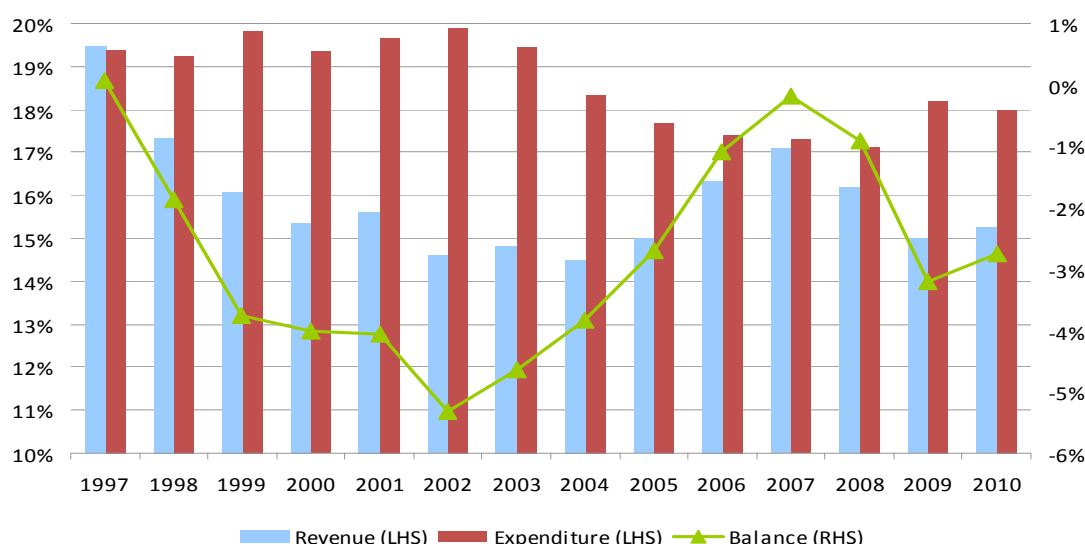
⁶ Government spending on education in the Philippines averaged 2.5 per cent of GDP during 2002-07 compared with 4.1 per cent for the East Asia region. In public health the Philippines spent 1.3 per cent of GDP in 2006 compared with 2.0 per cent for the East Asia region. Source: World Bank.

⁷ The Expanded Value Added Tax legislation (EVAT) was passed in 2005, which increased the general VAT from 10 per cent to 12 per cent and added petroleum to the products taxed.

government was able to fund a modest stimulatory expansion without significant negative consequences.⁸

The medium term fiscal situation will be tightly constrained. The deficit for 2009 was 3.9 per cent of GDP, up from 0.9 per cent in 2008. Part of the increase in spending has been stimulus spending. The increased deficit has also been driven by a decline in revenue which is partially unplanned. The GOP has outlined a medium term fiscal plan to get the finances back on track. However, restoring the budget to a more sustainable footing will be challenging as the revenue base and collection efficiency has declined in recent years and part of the expenditure increase has come through permanent public pay rises. At the time of writing the 2009 tax revenue take is projected to be 12.8 per cent of GDP⁹ compared with around 14 per cent in each of the three prior years and 17 per cent back in 1996. A tight fiscal and revenue situation places more pressure on government expenditure to be allocated well and executed through effective PFM systems.

Graph 1. National Government Revenue, Expenditure and Budget Balance: 1997 to 2010 (as a % of GDP)



2.3. Sector Analysis

Although the Philippines' PFM system is reasonably capable of maintaining an overall fiscal position, its ability to support efficient execution of the government's priority programs is limited. The Philippines' PFM system could be considered a work-in-progress, with progress unevenly distributed over different components. Past diagnostic studies such as the 2007 PEFA assessment and various reports produced by the GOP, other development partners and technical assistance through the PEGR show that some components of the PFM system are working adequately while others are not.¹⁰ Some

⁸ The debt premium on Philippines Government is currently below the level it was in September 2008.

⁹ Source: World Bank estimate

¹⁰ The most relevant donor reports are: Improving Budget Execution and Cash Management, IMF, 2008; Philippines Country Procurement Assessment Report, joint ADB and WB, 2008; Managing the Politics of

policies and practices were originally effective at achieving one objective but have outlived their usefulness. Other policies and practices work well in isolation, but overlap and conflict with other parts of the PFM system. Some of the aspects of the PFM system of the national government that are operating well include:

- relatively comprehensive budget documentation;
- a framework for strategic prioritisation of the budget through the introduction of a Paper on Budget Strategy¹¹ and a performance budgeting framework;
- tight controls of cash releases which has allowed the government in times of crises to effectively control expenditure and thus the budget aggregates;
- high quality procurement law that approximates international best practice;
- reasonably transparent and predictable allocation of transfers to Local Government Units (LGUs);
- systems improvement in various departments that has led to strengthening some aspects of financial management; and
- comprehensive coverage of external audits by the supreme audit institution, the Commission on Audit (COA).

These same diagnostics reveal that there is significant scope for improving the way the government uses and accounts for public resources to meet international and Philippines standards of good practice. A number of weaknesses in the Philippines' PFM system remain, the most fundamental being the generally weak capacity in government agencies to execute the budget and implement programs that deliver services to people, as well as the lack of accountability and transparency over the use of appropriated funds.

Budget formulation – the GOP has introduced a Medium Term Expenditure Framework (MTEF) and an agency-by-agency performance orientation in the budget known as the Organizational Performance Indicators Framework (OPIF). These innovations have enhanced policy considerations in the annual budget decision-making and are moving the GOP towards a results-based budget. The challenge that GOP now faces is how to fully institutionalise these reforms in the absence of a modern financial management information system that can generate timely and reliable information. While budget documentation is relatively comprehensive it could be made more user friendly and include a clearer narrative that links budget decisions to government policy.

Reform: Overhauling the Legal Infrastructure of Public Procurement in the Philippines, WB, 2006; and Public Expenditure, Procurement and Financial Management Review, joint ADB and WB, 2003.

¹¹ The Paper on Budget Strategy is the equivalent of a budget policy statement which is currently submitted only for consideration by the Development Budget Coordination Committee (DBCC) and Cabinet and remains an internal government document.

Political engagement in budget formulation is significant and occurs through a review and approval process that involves both chambers of Congress, the Executive and the President.¹² However, the debate between these arms of government often results in failure to reach a consensus General Appropriations Act (GAA) in time for the start of the fiscal year requiring the previous year's budget to be "re-enacted" until the new appropriations law is enacted.¹³ Re-enacted budgets undermine overall budget credibility as well as the ability of the bureaucracy to execute the budget as intended. It also entails huge management costs for agencies on top of an already complex appropriation structure.¹⁴ A Budget Circular issued by the Department of Budget and Management (DBM) sets out a formula for supplying budget resources when there are Congressional delays in passing the current year's Budget. However, this formula does not appear to be well understood or applied across departments.¹⁵

Much of Congress' attention on the budget is said to be focused on identifying specific projects for individual members' local constituencies or "pork barrel" rather than discussing national strategic priorities. The Philippines Constitution also accords the President a high degree of discretion to re-allocate portions of the budget during execution. Indications are that this discretionary authority is used extensively and re-allocations, especially in the use of Special Purpose Funds (SPFs), are not always transparently reported on.

Budget execution – from the point of view of effective service delivery and poverty reduction, the greatest concern about the way the current PFM system operates is the inefficient execution of the approved budget. Poor budget execution results from (i) spending agencies' weak capacities in policy coordination and project management; (ii) the cumbersome budget execution procedures and internal reporting requirements; and (iii) introduction of ad hoc changes in policies or rules regarding specific sectoral programs.

Other causes of weak budget execution are specific to individual spending agencies and include common weaknesses in expenditure planning including forecasting of cash disbursement requirements and program/project management. At times the agency's ability to execute the budget (and programs/projects) efficiently is hampered by frequent changes in the agency's own policies regarding those programs or inability to

¹² Once Congress receives the President's budget proposal in around July each year, the House Appropriations Committee reviews and approves it and sends it on to the Senate Finance Committee for its review and approval. Any discrepancies in the budget are then resolved through a bicameral conference before the final general appropriations bill is sent back to the Executive for the President to endorse it or veto it in whole or in parts.

¹³ In the last decade the Philippines operated under a re-enacted budget in 2001, 2002, 2004, 2006, 2007, 2008, 2009 and 2010.

¹⁴ The appropriation structure in the Philippines consists of three different types of appropriations: GAA, automatic appropriations and continuing appropriations; and during a fiscal year the government frequently transfers funds from one appropriation category to another.

¹⁵ Each department reported variable practices by DBM in funding the Re-enacted Budget Period from 1 January until the passage of the current year's GAA. There was also mixed reports about the withholding of allotments during the year after the budget was enacted, with some line departments reporting it was not an issue while others claiming that it was.

coordinate well among different units involved in service delivery and financial management.

The long process and tight management of cash releases has been consistently cited as a key constraint to service delivery.¹⁶ There is considerable debate between central agencies and line departments on this issue to pinpoint why slow execution takes place. However, it appears in need of objective and structured analysis to determine the scope and scale of the problem and the impact on public services delivery; and to identify effective remedies for the GOP to consider.¹⁷ The misunderstanding or inconsistency of process and practices around cash releases is potentially placing these departments in a position where they are no longer confident of cash supply, and disbursement on public services delivery is adversely affected.

Monitoring and reporting – many of the PFM procedures in the Philippines remain manual and paper-based, which limits the capacity of finance managers to produce timely and accurate data that can easily and expeditiously be shared with others. Paper-based reporting impedes or at best slows down the central unit's effort to consolidate data for monitoring and general reporting purposes. In the worst cases, the units formally in charge of receiving and consolidating financial information (e.g. Centres for Health Development which manage the Department of Health's regional operations) are ignored by the front-line units obligated to submit regular financial reports (e.g. hospitals).

The various actors in the systems lack reliable data, or have to go to great effort to find the data necessary to fulfil their mandate. Currently, the GOP is able to track total expenditure releases from the Treasury on a monthly basis, but this is not a sufficient basis for management. Equally crucial, especially for the purpose of ascertaining value for money of the budget, is data on budget execution by composition of spending. There is currently limited access to meaningful financial information for both in-year and ex-post reporting on budget execution. The high levels of executive discretion in budget management increases flexibility in in-year resource allocation to address unanticipated costs, but may reduce transparency and accountability if abused.

The difficulties departments have with budget reporting are partially due to a lack of coherence between the format DBM formulates the budget in and the one COA reports on. The budget execution data reported by DBM do not include actual cash payments made; 'actuals' figures are reported on the basis of obligations. On the other hand, COA's financial reports do report on expenditures on the basis of cash payments, but do not follow the GAA structure and therefore cannot be used for the purpose of comparing the budget and the actuals. Agencies are, in effect, required to report on the same things twice in different formats. This mismatch results in additional administrative costs for the government to be able to meaningfully report on how the budget is executed.

¹⁶ Improving Budget Execution and Cash Management, IMF, 2008

¹⁷ The World Bank's report on Budget Execution in the Department of Education is a useful start, but only covers a tiny fraction of the overall budget.

Accountability and transparency – lack of accountability and transparency arises from several structural and procedural weaknesses in the PFM system. These include: (i) a weak system of external reporting, exacerbated by fragmented data and unconnected manual and electronic information management systems; (ii) certain procedures for budget approval and execution which obfuscate the government's stated policy priorities and create a level of uncertainty and delay in budget allotments, and spending authorities distorting cash flow forecasts and execution plans; and (iii) the structure of the budget which places a significant portion of the approved appropriations outside the spending agencies and normal accountability mechanisms.

In a democratic country, ensuring efficiency and effectiveness in managing public resources requires oversight from actors both inside and outside the executive. The public, as well as the public institutions with oversight responsibilities such as the legislature, should have access to comprehensive and timely information on the various aspects of public financial management by the government. Better information and transparency allows key decision-making bodies to make informed decisions about the use of public funds and encourages a stronger focus on service delivery by the bureaucracy by keeping it accountable.

The precarious internal reporting and data availability deprives decision-makers of reliable information to manage public finance adequately. This has a number of practical consequences such as the following:

- political decision-makers, whether they be the President, Cabinet or the Congress, cannot match resource allocation decisions they have made with actual implementation;
- senior bureaucrats of the oversight agencies are not provided with the financial information to allow them to effectively manage the use of allocated resources and the economy throughout the budgetary year;
- line agencies lack the ability to enforce full control over the resources they are entrusted to manage; and
- the absence of public information encourages a perception of corruption and mismanagement – this perception has been growing in the last decade.

The lack of timely and reliable information frustrates the efforts of spending departments, central agencies and oversight bodies in the Senate and House of Representatives to monitor public expenditure performance; and so has undermined the credibility of public reporting on government finances. Civil Society Organisations (CSOs) also cannot find data to offer an informed, yet independent, perspective on the effectiveness of public services delivered through successive Budgets.

As a consequence of weak information flows on government finances, public and insider opinion veers towards the negative connotations of deliberate misinformation and potential corruption. This may contribute to the Philippines disappointing scores on

some governance perception ratings.¹⁸ Overcoming the lack of faith in the data will require concrete reforms to allow reliable and timely data to be available to key actors both inside and outside the system.

Information systems – at a practical level significant benefits could be obtained from improved reporting through computerisation of manual government financial processes and reporting. Some government departments are required to manage well over a million paper documents a year to keep internal financial records. The administrative burden from huge amounts of manually recorded transactions is difficult to manage for even highly competent finance staff.

COA has a mandate to strengthen PFM systems in the Philippines, and has developed several tools that would allow greater automation. Both the Electronic New Government Accounting System (e-NGAS) and Electronic Budget System (e-Budget) developed by COA were implemented in various national government agencies, LGUs and Government Owned and Controlled Corporations (GOCCs) before COA decided in May 2008 to suspend further rollout of the application systems in other government agencies. The reason for the suspension was to: (i) assess and enhance COA's strategies in implementing the application systems; (ii) formulate guidelines on the keeping of the general accounts of government; (iii) harmonise Philippine Government Accounting Standards with the International Public Sector Accounting Standards (IPSAS); (iv) revise the NGAS Manual and Chart of Accounts; and (v) enhance e-NGAS, e-Budget and other related computerised financial management information systems to conform to the revised NGAS.

Resolution of these issues so that government has an accepted platform for financial processing and reporting would potentially allow more accurate and timely reporting. It would also deliver considerable efficiency gains. Further information on the GOP PFM information systems is at Annex 1.

In a positive step, DBM, COA and the Bureau of the Treasury (BTr) have formed a PFM 'core group' and signed a Memorandum of Agreement (MOA) to coordinate their efforts on PFM reforms, converging at first to make headway into developing a sound Government Integrated Financial Management Information System (GIFMIS). Sustaining this agreement and institutionalising interdepartmental coordination would constitute an essential building block of effective reform management. One of the gains to be made under a whole-of-government approach is that stronger and more accountable PFM systems restrict access for opportunistic behaviour. Conversely, gains in this area are diminished where PFM systems are strengthened in only a few departments.

¹⁸ Data shows that the Philippines' performance on a range of governance indicators is below the median for all countries and in some cases has deteriorated over the last decade. Source: D Kaufmann, A Kraay & M Mastruzzi, 2009, Governance Matters VIII: Governance Indicators for 1996-2008.

2.4. Lessons Learned

AusAID's predecessor to this program, the PEGR, responded to several of the GOP's high-order public expenditure management goals in the areas of budget planning, programming and then monitoring via internal controls. This new program learns from a range of lessons from the PEGR, as well as internationally, on how to best support progress on PFM reforms in the Philippines. Important lessons are outlined below.

- **A whole-of-government PFM strengthening program would be invaluable**

The GOP has identified strengthening PFM as a priority through various avenues, including the Medium Term Philippines Development Plan (MTPDP), annual Budget messages and various policy documents released by the government oversight authorities such as DBM and COA. However, these documents are either very broad policy statements or very specific operational level guidance; none articulate a comprehensive PFM reform strategy. At a practical level the PFM initiatives of the GOP have thus far taken place primarily within the responsibility of each individual oversight agency and line departments (e.g. DBM's performance budgeting or COA's e-NGAS).

The existence of independent initiatives led by different oversight agencies is an understandable reaction to organisational responsibilities. Key potential improvement within the system comes from better coordination amongst the oversight agencies. To overcome these silos requires strong high-level leadership and continuous inter-agency coordination. In practice, this means that the government should establish an institutionalised means of coordination amongst oversight agencies leading different components of PFM strengthening efforts, as well as some of the line agencies demonstrating willingness to spearhead improvements.

A whole-of-government overarching agenda or strategy on PFM strengthening would be invaluable in galvanizing support for PFM improvements especially at the political level. Development of the Philippines PFM Reform Roadmap by the 'core group' is a positive step in this regard. AusAID should facilitate this effort by supporting those agencies that have a mandate and commitment to improving the PFM system. The PEGR board was not always able to provide a joined-up government view, in part because the economic governance focus of the PEGR was too broad. Ideally, the PFM 'core group' would be the appropriate oversight and advisory body for the new program.

- **High-level strategic and performance budgeting reforms need to be built on a solid and reliable system of usage and reporting of budgetary resources**

The GOP has made sound gains in introducing more strategic and performance orientated budgeting with assistance through the PEGR. However, a key lesson from international and Philippines experience is that a properly functioning public sector accounting and reporting mechanism is needed to underpin higher level reforms in budget planning and programming. Budgets are only functional if they are fully funded

and executed as close as possible to what was planned. Implementing departments and oversight agencies can improve overall management in the execution of budgets if they can access and report on the physical and financial utilisation of funds on a timely basis. Improved access to and utilisation of public financial resources by service delivery agencies overcomes a key constraint to achieving development outcomes, that of inaccessible and unreliable budgets. Similarly, high quality physical and financial reporting by implementing departments informs budget allocations. One area that AusAID's future assistance should give greater emphasis to is reforms establishing the fundamentals of well controlled, predictable and accountable cash release to line agencies.

- **Lack of clarity and information on procedures and systems means there is a degree of miscommunication and mistrust inside and outside government that needs to be overcome – the lack of trust in financial management is partially a disservice as there are many pockets of competent people and systems**

Many of the procedures for financial use and reporting are basically sound. However, in practice procedures are often inconsistent between agencies and not fully documented. This means that while experienced senior officers understand how the system operates, this knowledge is not equally shared across the bureaucracy and application of process is reportedly not always consistent. Similarly, financial use and reporting systems are often sound in isolation but do not always connect with each other. Combined with a mainly manual and paper-based system, this can result in decision-makers not always having reliable information to manage public finances adequately. Unfortunately, it is also the case that in the absence of information, people inside and outside the government can assume the worst, which erodes public trust in government.

- **PFM reform in the Philippines is a long and slow process, even relative to other lower middle income countries – ‘reform fatigue’ is evident in many parts of government, and a better approach may be to stress improvement and implementation of existing systems**

The history of PFM reforms in the Philippines clearly shows that substantial change requires a long period of incubation and progress is slow. For example, in 2007 some of the major achievements of the PEGR were the introduction of a semi-functioning set of forward estimates as part of the introduction of a MTEF and the production of the OPIF Book. This was seen as a first step along the path of more strategic and performance budgeting. However, this was a first step that had been attempted in several guises since the early 1990's and even now the full implementation could be considered in its early stages. Similarly, the development of a new government accounting system, e-NGAS, begun in 2001 but is still several years away from full functional usage in all government departments.

The Philippines is hardly unique in this aspect; the pace of PFM reform is often frustrating in many developed and developing countries, although the status quo does

appear particularly well entrenched in the Philippines. In this environment fatigue can set in as reforms have been discussed for many years, but often the benefits from implementation have yet to be fully realised. In this context, the PEGR's focus on achieving 'transformative reform' was probably ambitious.

- **A shared understanding of key problems and a shared commitment to solutions is required to sustain an effective political economy for PFM improvement**

Despite strong leadership for key reforms such as the OPIF, reform implementation was gradual and uneven across the bureaucracy. While a gradual approach to reform may be necessary, even desired, lessons from the PEGR show that part of the reason for this can be explained by the inability of the change process to bridge fragmented elements of the national government, build trust, and manage differences of opinion. In a fragmented environment there is a tendency for governments, often supported by development partners, to jump too quickly to technical solutions without building a shared understanding of the key problems which may or may not be technical in nature.

Early versions of the Philippines PFM Reform Roadmap¹⁹ signal that general agreement has been reached on a detailed set of PFM technical requirements, which GOP will now need to cost, prioritise and sequence before these can be implemented. The devil will be in the detail, but it will be important to ensure progress of related initiatives across all key agencies involved in the implementation of reforms. Further, on-going collective support from the GOP and development partners will be needed to sustain an effective political economy and communication strategy around the Roadmap and its implementation. Without this "cheer squad", reforms could stall and fatigue set in.

- **Flexibility and selectivity of activities are required for a long-term program of support to be effective**

A key challenge in moving a reform forward in the Philippines is how to manage the implementation process within a complex PFM system without overburdening the bureaucracy's absorptive capacity or alienating key actors within the system. Lessons from the PEGR all point to flexibility and selectivity as essential components of donor assistance to PFM reforms. A long-term program of support to a changing reform context needs flexibility in implementation, both in the types of assistance that can be provided and the range of partners to engage with. A common risk for development assistance is agenda-capture, more common when an activity is housed within a single counterpart agency. Flexibility allows a program to adapt as the government's reform agenda and its reform 'champions' alter over time. Selectivity in the reforms that can be supported at any one time can improve the prospects of available program resources having an impact, particularly where there is a clearly understood decision-making framework for the selection of activities.

¹⁹ Philippine Public Financial Management (PhilPFM), Reform Roadmap Workshop – Consolidated Matrix of Identified Gaps, Strategies and Desired Results, GOP, as of March 8, 2010.

- **AusAID needs to have a deep understanding of complex government functions such as PFM to engage effectively in a constructive and informed debate**

Donors, including AusAID, have to understand the sectors they engage in and the reforms they support to add value to the government's agenda. The Philippines has the longest tradition of democracy in South East Asia, a vibrant open press and an outwards looking population. Internal capacity of many government bodies is high and the internal debates may be more robust than development partners realise. In all countries there is a legitimate creative tension between local practice and what is considered ideal international practice. The key is to identify the areas where current practice differs from what is a fundamental area of effective governance. Some issues are legitimately contestable within government such as the best way to measure performance of government expenditure or the extent to which internal audit function can be outsourced.

Under the PEGR AusAID outsourced much of the policy engagement and programming responsibility to a managing contractor. While this minimised the administrative burden on AusAID it created a number of issues including: confusion over the relative status of AusAID and the PEGR which at times complicated relationships with the GOP and development partners; loss of oversight by AusAID over a program engaging in sensitive areas; limiting in-house corporate knowledge of the reform agenda; and the creation of incentives through governance and management arrangements that in some cases led to supply driven development. In the future AusAID should look at ways to strengthen its in-house expertise to engage in complex and sensitive areas in PFM.

2.5. Consistency with Other Programs

2.5.1. Other AusAID Programs

PFM is highly relevant to other AusAID programs in the Philippines that aim to improve government service delivery. Programs in sectors such as education and health struggle to make real progress without addressing PFM issues.²⁰ It is proposed that in working with service delivery departments the PFMP will prioritise those departments that AusAID already has sector programs with, such as the departments of Education, Social Welfare and Development, and Public Works and Highways. It is not expected that the PFMP will lead engagement with these departments, but instead play a complementary and supporting role to sector programs by providing technical inputs on PFM issues to build capacity and facilitate reform alignment across agencies.

²⁰ An example has been the European Commission's experience in the health sector. The European Commission is a significant donor and leading a sector-wide approach. Although they did not originally intend to become heavily involved in financial policy they have found it increasingly necessary as budget execution issues are emerging as one of the key constraints to health program effectiveness. The European Commission now has several advisors working with both the Health Department and DBM on PFM issues.

Improving national government PFM practices has been identified as an important factor in education, social welfare and national infrastructure. Priority areas could include assisting these large spending agencies with budget execution and reporting at a number of levels, including improving cash management procedures at the national office, strengthening internal controls over execution at sub-national level and better physical performance reporting through OPIF. Supporting internal control processes and internal audit in some agencies is required as part of AusAID's contribution to multi-donor initiatives such as the support for the GOP's conditional cash transfer program.

If a comprehensive PFM reform agenda does not materialise in the short term a fallback position might include directing program resources to supporting PFM solutions in select major spending agencies. Prioritisation beyond AusAID's sectoral programs will be through joint agreement between the GOP and AusAID.

There are opportunities to expand the role for civil society in PFM strengthening through more collaborative engagement with the GOP. Supporting civil society-government links is consistent with a separate civil society initiative being developed by AusAID that would aim to strengthen the capacity of CSOs to engage more effectively with government in the key sectors of Australia's Development Assistance Strategy.

2.5.2. Development Partners

The emerging PFM reform agenda, if supported by the new Administration, would provide the platform for coordination between development partners and government to ensure sufficient resources are available to progress the agenda. The financing needs of the complete package of reforms, as outlined in the PFM Reform Roadmap, will far exceed AusAID's financial capacity to assist. Accordingly, co-financed activities and collaborative analytical work should be actively pursued with development partners under the reform program. The sub-working group on PFM of the Philippines Development Forum (PDF), which AusAID co-chairs with DBM, is an existing forum through which all interested partners can achieve greater collaboration and engagement around PFM reforms.

In line with aid effectiveness principles (Paris/Accra), good links have already been built with development partners active in the Philippines on PFM issues through mutual support for the roll-out of core government programs such as OPIF and internal audit and controls, as well as analytical products. If the PFMP proceeds as planned, AusAID in the near term would be making the largest financial contribution to assisting the GOP with expenditure management amongst the development community. However, there are a number of small to middle size initiatives from several development partners, the most significant being:

- The World Bank has carried out a series of AAA tasks and is supporting budget planning and formulation, procurement, internal audit, and with AusAID funding conducted a PEFA assessment in 2007. The World Bank also plans to increase its engagement with CSOs to strengthen independent budget and policy analysis.

- The Asian Development Bank (ADB) is active in a number of areas, including the roll-out of the OPIF and internal control processes to selected departments, procurement reform, debt management, reform of GOCCs, and is also supporting local governance.
- The European Commission, through its health sector program, is working on PFM strengthening in the Department of Health and sub-national transfers. A separate program for sub-national PFM strengthening is in the pipeline.
- The IMF, World Bank and the United States²¹ are active on the revenue side.

The GOP's commitment to developing a GIFMIS as a central pillar of the emerging PFM reform agenda provides an opportunity for closer collaboration amongst development partners. The ADB has agreed to provide initial technical assistance in 2010 to support an inter-agency steering committee (known as the GIFMIS Committee) to prepare an implementation plan for a GIFMIS project. If the development banks were to provide financing for the project, AusAID would be well placed through the PFMP to provide complementary grant assistance.

It is feasible that the Roadmap becomes an implementation plan that can be assigned to development partners and eventually lead to a pooled fund approach to implementing this reform. In this event, the PFMP needs to be flexible enough to accommodate this development. In the meantime, and to avoid duplication of effort, AusAID and development partners should strive for greater policy coherence so there is a clear and consistent policy position over the long term. Development partners might also consider joint monitoring of their respective programs and be prepared to undertake joint monitoring of the government's PFM reform program if requested. In terms of the PFMP, other donors will be invited to participate in monitoring of program activities as well as overall program effectiveness via the biennial evaluations.

2.6. Rationale for AusAID Involvement

In many countries the practice of PFM is an obstacle to the achievement of poverty reduction objectives. Strengthening the GOP's PFM system is vital to AusAID's broader country program objectives of achieving economic development, poverty reduction and the MDGs. Australia's official development assistance to the Philippines comprises approximately 0.3 per cent of total government expenditure. If AusAID is going to make a meaningful contribution to the achievement of key social and economic objectives it needs to use its funds to leverage improvements in the way the GOP uses its own resources.

Improving the efficiency and accountability of public fund use and enhancing links to service delivery are essential elements in supporting the GOP to reduce poverty and improving the effectiveness of AusAID's overall country program. Development

²¹ The Millennium Challenge Corporation was reportedly considering a tax collection strengthening project with the Bureau of Internal Revenue of about US\$50 million, but has delayed making a decision regarding the grant until after the Philippines national elections in May 2010.

partners active in sectoral programs are usually strong advocates of increasing the size of allocations to the sector. However, with a fiscally restrained medium term outlook, development partners must engage in the debate on not just the ‘how much’ but the ‘how’. Key to achieving better use of GOP own resources and responding to the ‘how’ includes improving processes and parts of the PFM system. The potential significant benefits of successful PFM reform justify intervention even if progress is slow.

Australia has been engaged in supporting PFM in the Philippines for many years, most recently through the PEGR. It is legitimate that AusAID takes a lead role in supporting the emerging PFM reform agenda as it has a number of comparative advantages in the sector. These include:

- willingness to commit resources for the long term typically required for PFM strengthening programs;
- knowledge, credibility and existing relationships from previous engagements and the capacity to further build in-house expertise;
- ability to blend international experience from pursuing PFM reform in a number of countries, including Australia, with local knowledge and expertise; and
- flexibility to operate in a coordinated and complementary way with the development banks and other donors, including shifting to more harmonised arrangements in the medium term.

3. Program Description

3.1. Problem Statement

Significant improvements in the allocation and management of public resources in the Philippines need to be built on a platform of reliable and timely public expenditure information; with capable government systems, organisations and people in place to use this information to make informed decisions and enable the effective provision of public goods and services. This information needs to be transparent and credible to both government and external observers; and properly linked to physical performance data if the GOP policy goals are to be met.

The cornerstone of future analyses and reforms will be the information provided by the public expenditure management systems of the GOP. At present these are fragmented, largely manual and require processing millions of manual transactions per annum. In a fiscal environment where the GOP seeks more detailed public expenditure information more often, so that it can better target resources and improve expenditure management, these fragmented and manual systems are inadequate.

Accordingly, the highest priority problem statements for the GOP to be addressed through the PFMP are:

- Government needs to streamline its PFM systems to generate more timely and reliable public expenditure management information;
- Government needs to better coordinate oversight of PFM at the national level to improve the allocation, utilisation and reporting of budgeted funds;
- Government needs to improve PFM capability in agencies to execute the budget and implement programs; and
- Government public expenditure management and performance information needs to have its credibility affirmed by effective oversight, including external to government.

Providing solutions to these problems will provide the GOP with the public expenditure data sets required for more efficient allocation and use of public resources by government, as well as promote public confidence in the use of taxpayer resources.

3.2. Goal and Objectives

The PFMP will address the priorities of the Philippines PFM Reform Roadmap to develop an efficient and effective PFM system in the Philippines, with a focus on budget execution and accountability and transparency to improve the delivery of public services. This is consistent with the common purpose of the development strategies of the Philippines (MTPDP) and Australia (APDAS) to improve the effectiveness and efficiency of government spending.

The overall program goal is:

Improvement in the efficiency, accountability and transparency of public fund use in the Philippines to enable better service delivery

This goal represents a long-term commitment by Australia to assist the GOP to achieve incremental improvements in the efficiency, accountability and transparency of the PFM system and its information flows. The PFMP will support oversight agencies and key service delivery departments. Improvements to PFM will be explicitly recognised as important components of sector strategies such as education.

The program will pursue four strategic objectives that respond to the highest priority problem statements and address both the supply and demand sides of the program goal. On the supply side, there is a need for government to better allocate and utilise public funds for services delivery and to deliver more timely and reliable reporting of those funds. On the demand side, there is a need to confirm, through both internal and external accountability mechanisms, that budgeted funds are being executed as intended.

The program's four strategic objectives are:

- 1) Increase the efficiency and effectiveness of the allocation, utilisation and reporting of budgeted funds by oversight agencies**
- 2) Improve PFM capability in select departments to enable more efficient utilisation and accountability of public funds for service delivery**
- 3) Generate more timely, reliable and accessible public expenditure management information**
- 4) Strengthen external oversight of public expenditure management linked to physical performance information**

A wide range of assistance is required to build momentum around existing and emerging GOP reforms to achieve these strategic objectives. This includes supporting the formal government mechanisms that can deliver PFM systems changes and the quality assurance process that monitors the impact of any systems changes undertaken. It also requires support for the performance monitoring mechanisms by both government and external observers and the intersection between them.

The first phase of activities to be funded by the program will be developed in the program implementation. The type of assistance offered could include: diagnostics around key aspects of the PFM system; long and short term technical assistance from both local and international advisers to help in the implementation of programs; and production of regular 'hot topic' papers that inform the internal policy debate within government. Each strategic objective and the proposed focus areas for action are explained below.

3.2.1. Strategic Objective 1 – Increase the efficiency and effectiveness of the allocation, utilisation and reporting of budgeted funds by oversight agencies

Focus areas: reform strategy and program development; focused diagnostics on PFM issues; improvements in budget execution (and formulation) systems and procedures; interdepartmental information flows and reporting

Key partners: BTr, COA, DBM, ADB, WB

The PFMP will assist oversight agencies to implement a comprehensive reform agenda as outlined in the Philippines PFM Reform Roadmap, including further strategy development if required. The success of the Tagaytay Conference in May 2009, and its successor in February 2010, in setting out a broad, initial consensus on the priorities that remain after 20 years of PFM reforms in the Philippines was a positive development.²² Whole-of-government collaboration on PFM issues related to the allocation, utilisation and reporting of budgeted funds is emerging and there is general agreement amongst oversight agencies that having access to additional resources to boost this effort is needed.

An early focus of the program could be to support the finalisation of the Roadmap and maintaining the political economy around its implementation, through, for example, communication and change management strategies to garner a wide level of support. The program could fund key initiatives mainly in and around budget execution, but also on systems and procedures of budget formulation and how the budget is presented. Making the budget documentation more user friendly to government and the public and including a clearer narrative linking the budget to government policy priorities is just one improvement that could have a significant benefit. The MOA between DBM, COA and BTr to develop a GIFMIS is a promising start to fostering greater coordination on PFM reforms. Each agency has identified early opportunities for improving interdepartmental information flows and reporting. Ideal sequencing would be to first assist the GOP to finalise and formalise the reform agenda, then test departmental support for these reforms, and finally implement selected reforms as needed.

The program could also support appropriate forums for bringing together key stakeholders such as the PFM ‘core group’, technical committees and select line agencies so that better coordinated implementation is likely. Focused diagnostics of PFM issues will be required to determine working priorities for oversight and line agencies in some of the areas identified initially by the Roadmap including but not limited to cash management and release procedures, in-year budget processes, and accounting and reporting processes and capabilities.

²² Conference-Workshop on Public Expenditure and Financial Management Reform. DBM and World Bank, June 2009.

3.2.2. Strategic Objective 2 – Improve PFM capability in select departments to enable more efficient utilisation and accountability of public funds for service delivery

Focus areas: internal control systems; internal audit; agency institutional reforms in budget formulation and execution; capacity building in PFM, agency reporting through OPIF

Key partners: DBM, DepED, DPWH, DSWD, OP, ADB, WB, EU

The program will assist service delivery departments to build their capability to implement priority programs/projects more efficiently and better account for how budgeted funds are used. The program will prioritise those departments that AusAID already has sector programs with such as the Department of Education (DepEd), Department of Social Welfare and Development (DSWD) and Department of Public Works and Highways (DPWH). In some instances program support might encompass a broad set of institutional reforms in one agency that includes budget formulation and execution, improving cash management procedures, strengthening internal controls, and better physical performance reporting through OPIF. At other times assistance might target specific reforms across multiple departments.

It is proposed that an early focus of the program is to strengthen and institutionalise internal control systems and internal audit (ICS/IA) in select departments. Good progress has been made in this area including the finalisation of the National Guidelines on Internal Control Systems (NGICS). There is a further need to improve the basic operations of internal controls so that internal audit and management offices and their staff are capacitated and adequately skilled to support the assessment, implementation, monitoring and evaluation of controls. In many cases this requires the formation and/or strengthening of IA Units and Management Divisions, and the formulation and execution of IA Plans.

A concerted effort by GOP agencies on these tasks can make headway into internal audit becoming an effective tool for gauging and improving agency performance. Part of the approach is to build up the capacity of the inter-departmental Reference Panel on ICS/IA, which is jointly led by DBM and the Office of the President (OP), so that it serves as a formalised structure capable of overseeing and facilitating ICS/IA strengthening across government. At the same time it is proposed that efforts are also focused on the larger spending agencies and then rolled out across government at an appropriate pace so there is sustainability of reforms. In the longer term, linking internal audits to OPIF reporting would reinforce previous and current efforts to strengthen ICS within government.

3.2.3. Strategic Objective 3 – Generate more timely, reliable and accessible public expenditure management information

Focus areas: OPIF usage and reporting; budget and consolidated public expenditure reporting; agency financial reporting; information systems analysis; change management processes, capacity building

Key partners: BTr, COA, DBM, DPWH, ADB, WB

The generation of more timely, reliable and accessible public expenditure management information is at the core of the GOP's PFM reform agenda and its commitment to developing a GIFMIS. The planning phase for the GIFMIS project has commenced and may take 12 months or more. It is clear from international experience within the region and further afield that developing a modern financial management information system will take several years to complete and cost many millions of dollars. While it will be up to the GOP to finance the project, potentially with external financing, the PFMP will be well placed to provide complementary grant assistance. Analysis of information systems such as e-NGAS and e-Budget could also be considered, as well as support for change management and capacity building of the bureaucracy.

Despite the absence of a GIFMIS there are areas where public expenditure management information can be improved and made more accessible. One is streamlining and consolidating agency financial reporting to populate OPIF reports that can inform Congress and civil society. Another is beefing up financial reporting to the public, especially budget execution reports, some of which are already produced for internal purposes.²³ The program could provide the technical inputs to implement these improvements. Rolling out e-NGAS within the DPWH is an initiative that has received AusAID support and this could be continued under the PFMP.

Continuing reforms in performance budgeting will also support accountability and transparency in the use of government funds. While gains have been achieved in the development and sustained use of OPIF across government, challenges remain in rolling out OPIF government-wide and using OPIF as a tool for agency performance management and resource allocation decisions. Key challenges include: (i) better articulation of Major Final Outputs (MFOs) or goods and services delivered by government departments; (ii) cleaning up the list of programs, activities and projects so they directly align with the MFOs; (iii) identification of more robust performance information; and (iv) production of verifiable public expenditure and performance information through OPIF reporting.

Improving the utilisation of OPIF hinges on improvements in the integration of budget preparation, budget execution and accountability systems to generate more timely and reliable information. The program could assist DBM to finalise and operationalise OPIF guidelines to provide clear standards for linking MFOs and performance indicators and

²³ Agencies already submit Statements of Allotments and Obligations Balances (SAOBs) more or less regularly to DBM which could be consolidated and published.

identifying more robust performance information. This could include supporting the DBM Budget Inspectorate to evaluate OPIF financial data in major spending agencies. The program could also support pilot agency/s to better institutionalise OPIF internally by cascading concepts down to corporate and business planning, thereby supporting the implementation of OPIF. Generating a common understanding of the benefits of OPIF will be important and the OPIF Working Group, if it were to become a whole-of-government forum, could play a key role in the institutionalisation process.

3.2.4. Strategic Objective 4 – Strengthen external oversight of public expenditure management linked to physical performance information

Focus areas: capacity building of CSOs and Congress; civil society-government linkages; ‘hot topic’ papers on PFM issues; independent evaluations of physical and/or financial performance

Key partners: BTr, COA, DBM, CPBD, SEPO, Academia, CSOs, WB

The rationale for including civil society access to the PFMP is to encourage a balance between both government and independent viewpoints on PFM issues and priorities, and to recognise the positive role that CSOs and academia can play to independently affirm real gains made in PFM. Similarly, when PFM strengthening efforts need more support, it is understood that civil society has a valid role in pointing this out and making constructive proposals for government to consider and act on, as appropriate.

There are opportunities to expand the role for civil society in PFM strengthening through more collaborative engagement with the bureaucracy, including the technical offices²⁴ of Congress, and ultimately with Members of Congress. For a well informed debate on PFM issues there needs to be capacity building of CSOs in budget monitoring and evaluation. The program would build capacity of CSOs to perform analyses and syntheses of published and ‘grey’ materials and provide written articles on topics of general interest, or as requested, to inform the GOP and civil society on PFM activities. This will help to build the demand side for better accountability and transparency. If requested by the GOP, the program could also work with oversight agencies and the technical offices of Congress to build the capacity of Congress in its budget oversight function and as a way to gain institutional buy-in of the PFM reform agenda.

There are already examples of constructive collaboration between the government, civil society and development partners to improve PFM practices.²⁵ The World Bank also plans to increase its engagement with CSOs to strengthen independent budget analysis. As the number of CSOs working in this area is relatively small there may be an opportunity for AusAID and the World Bank to combine their respective efforts.

²⁴ For example, the Congressional Planning and Budget Department (CPBD) of the House of Representatives or the Senate Economic Planning Office (SEPO).

²⁵ One area is public works and highways where the CSO ‘RoadWatch’ feeds back its own findings to the DPWH management and the development partners. Another example is the Budget Network, which is already established and brings together some 20 CSOs with the support of the United States Agency for International Development (USAID).

The program would also support academia and CSOs to complete independent evaluations of physical and/or financial accomplishments that feed into the departmental internal audit programs, so bringing an external oversight element and further reassuring senior managers that the ratings given to their department's performance are reliable and credible both within and outside government. Supporting CSOs to independently publish on websites, or through other media, the 'scorecard' of findings of analysis for major spending departments could form part of the approach to improving accountability and transparency. This approach allows a more open exchange of information with civil society and brings an informed, independent opinion on the question of whether PFM is improving in the GOP.

In terms of the PFMP, all engagements between civil society and government will need to be based on the principles of constructive collaboration. This requires:

- mutual respect for the stated goals of each party and the value added that each brings to the others mandate;
- regular meetings attended by all key counterparts;
- transparent exchanges of readily available information on an agreed timing;
- agreement on the format, volumes and time-frames for any supplementary information requested; and
- agreement on the format and timing of publication of any performance scorecards.

There is unlikely to be a constructive role in this approach for more activist CSOs with a direct media-campaigning philosophy, or those with a 'gotcha' agenda that may be seen to incorporate a political bias.

3.3. Engagement Strategy

The Philippines system has proved resilient to change and the slow pace of progress can be difficult for development partners with short term result and reporting horizons. Progress is not impossible though as many of the reforms to PFM are technocratic in nature and selective support by donors can nurture the progressive elements of government to improve their systems. Expectation of program achievement should be of modest incremental progress towards realistic long term objectives. The program will need to operate in a way that promotes change towards the achievement of an improved PFM system in the Philippines. The engagement strategy outlines how the program will do this.

Commit support for the long run – Australia needs to make a long-term commitment alongside GOP and other development partners if the scope and scale of the proposed reforms outlined in the Philippines PFM Reform Roadmap are to be carried to fruition. The first test of the political economy around the reforms will be the national elections

in May 2010, after which the new Administration will need to endorse and support the Roadmap. This work largely takes place before the PFMP is mobilised in early 2011; and is the primary responsibility of GOP central agencies. Donor partners can assist by presenting a united front on the subject of the Roadmap in their in-coming government briefings.

Cultivate robust relationships – a key factor in the realisation of PFM reforms under the Roadmap will be buy-in from the PFM stakeholder community. Cultivating robust relationships supported by an effective communication strategy around the Roadmap as a whole will be important. In terms of the PFMP, this requires:

- leadership and management of the program to have a clear AusAID character and authority to maintain its place in the stakeholder community over the long-term;
- a program management structure and consultation process that formally and effectively links key stakeholders from the bureaucracy, donor community, civil society and political leaders;
- fostering and deepening relationships with these stakeholders over the course of the program's implementation to ensure a regular, constructive and contestable debate on PFM issues and solutions;
- paying sufficient attention to change management processes within the institutions and agencies affected by reforms;
- a communication and information strategy to collate and disseminate appropriate information between and across key stakeholders.

Coordinate resources for reforms with key partners – Australia cannot resource all aspects of the Roadmap; it is too extensive a package of reforms for the budget resources of the PFMP. This reality identifies a strong need for PFMP to liaise and coordinate closely with GOP oversight agencies and development partners in the Roadmap's implementation so that it is resourced adequately and sequenced appropriately. Without this shared approach the GOP's outcomes may not be realised and the PFMP's objectives would be compromised. Consequently, the PFMP will need to have a particular focus and be selective in the reforms that it supports if the available resources are to have an impact over the long term.

Focus on the enabling environment for service delivery – a key feature of Australian aid to the Philippines is its focus on improving the delivery of public services, through support to policies and capacity to implement those services. Analysis and experience shows that an area where Australia can effectively support service delivery outcomes is through enhanced budget execution and improved accountability and transparency over the use of appropriated funds. It is proposed that this be the focus for PFMP activities. The program logic is that by supporting activities that allow agencies to better allocate, access and use budget funding, there will be a direct link to better services delivery

outcomes. This logic can be directly tested by other Australian aid initiatives that are active in sectors, such as education and infrastructure.

Other areas of PFM such as tax reform and revenue generation, GOCCs, debt management and procurement are being progressed with the support of other donors and there is less strategic or technical advantage to Australia expanding its engagement into these areas of the Roadmap. However, developments in these areas are linked to the objectives of the PFMP and will need to be observed.

Provide for consistency and flexibility in implementation – it is clear from international experience that a long-term program of support to a changing reform context requires consistent leadership and direction, especially when operating in multiple agencies; and flexibility in implementation. The consistency of leadership and direction will maintain the program focus over the long-term, even though activities may change or be terminated and new ones added. It will also enable quality advice and support to the government that is grounded in the local context and facilitates reform alignment across government. Flexibility of implementation will allow different forms of assistance to be delivered to the GOP by different partners as the needs of the reform agenda alter over time (see form of aid below). These features of the engagement strategy will help the program to remain relevant and effective over the long-term.

Aim for systemic change in the selection of activities – in selecting activities the primary consideration for the program is systemic change. The program will support the parts of the PFM system that are considered most essential for improving public service delivery. In other words, program resources will flow to those GOP agencies and managers that set the rules or have responsibility for their implementation; therefore to either oversight or service delivery agencies. Resources will also be directed to development partners and CSOs that are able to contribute to the overall PFM strengthening effort. To create demonstration effects it will be important for assistance to be directed to agencies and implementers that can deliver demonstrable results within a reasonable timeframe. This approach relies on diagnostics that can inform the Roadmap on trends and priorities, as well as identify capacity issues crucial to reform management and agency performance improvement.

3.4. Form of Aid

The program adopts a ‘facility’ form of aid and will provide flexible and responsive assistance to a set of high level objectives agreed with the GOP, as well as respond to opportunities and change ‘champions’ where they emerge. The determination of specific outputs will be undertaken through the joint development of a series of activities planned each year within agreed parameters for the selection of activities and for quality and standards. The key components of the program’s form of aid are:

- *Financing arrangements* – the program will provide grant financing. Implementation will be by: (i) directly contracted technical assistance; (ii) directly sub-contracted outputs for large scale tasks; and (iii) accountable cash advances to implementing partners with the capacity and accountability measures to deliver the required outputs. Technical assistance is one, and only

one, part of the capacity building equation. In the early years of the program there is an acceptance that technical assistance will form the majority of overall program costs if in demand by the GOP. Program resources will also be transferred indirectly through contractual payments to the Service Provider.

- *Delivery mechanism* – AusAID will take a direct leadership role in the program and will staff the Team Leader and Program Coordinator positions. However, to minimise the administrative burden on AusAID and the GOP in implementing the program, a private sector Service Provider will be selected through a competitive international tender to provide administrative support to the program.
- *Legal instrument for implementation* – the program will operate under the auspices of a Subsidiary Arrangement to the General Agreement on Development Cooperation between the Governments of Australia and the Philippines.

3.4.1. Capacity development approach

The PFMP adopts AusAID's definition of capacity development as: 'the process of developing competencies and capabilities in individuals, groups, organisations, sectors or countries, which will lead to sustained and self-generating performance improvement'. This definition makes clear that capacity development is a process as well as an objective – how capacity development is undertaken will influence how successful it is.

The purpose of capacity development in the PFMP is to improve government performance in using public funds through sustainable systemic change towards the policies and objectives the GOP sets for itself. Thus 'capacity' is defined in terms of performance. While it is acknowledged there are many and varying definitions of capacity, for the purposes of this program it is important that the concept of capacity remains directly linked to institutional performance and results.

The program will embed itself within the GOP context and work across government institutions through a systematic response to performance objectives and implementation. An orientation towards performance and results can create tensions between directing capacity development resources towards immediate performance improvement tasks (the 'doing') and the long-term, more difficult enterprise of mentoring, coaching and advising (the 'building'). In practice, there will be a need for a range of resources across the spectrum of activity between these two extremes.

The program will support agencies to use diagnostic tools to analyse capacity issues crucial to improving agency and system-wide performance, and help formulate the most effective form of assistance. Before decisions are made about the type of support it is important to be clear about what the issues are. The capacity diagnostic will form a key part of the program's capacity development strategy. The strategy will be prepared at program implementation to document the capacity diagnostic methodology and specific

approaches to capacity development and their expected contribution. If a relevant and up-to-date diagnostic exists then it should be sourced to avoid duplication of effort.

3.5. Program Duration and Budget

The PFMP is a long term partnership between the Governments of Australia and the Philippines that reflects the long term nature of improving PFM systems. The term of the PFMP is 10 years and will be implemented in five-year phases, with points of review for each phase. In this way, both governments can evaluate the impact of the program and redirect it as needed, while providing the consistent, long-term resources that are required. A mid-term review of the services provided under the Contract will take place at the beginning of the third year to decide whether the program will continue for a second two-year phase.

The proposed financing from the Australian aid program for the PFMP is up to A\$30 million for an initial five years from 2011 to 2016. Estimated program costs are based on the continuation of some priority activities funded previously under the PEGR²⁶ and the implementation of new activities as set out in the Philippines PFM Reform Roadmap. There is potential for scalability in resourcing as demand for assistance increases or decreases over time. Actual program expenditure will depend on the extent to which effective use of the funding can be demonstrated. Initially, program financing will cover the first three years (up to A\$18 million), with an extension to years four and five subject to the outcomes on an independent evaluation of the effectiveness of the program in the third year and Parliamentary appropriation.

The program's development is taking place in the Philippines election period and transition to a new Administration. As a natural part of the democratic cycle there is some uncertainty in the GOP's policy agenda. Where PFM strengthening is taken up effectively at a whole-of-government level it is anticipated that the program would be called on to provide a higher level of support. On the other hand, if the new government shows little or no sign of committing to comprehensive reform then a reduced level of support to target agencies is expected.

²⁶ The total contract value of the PEGR was A\$33.2 million over five years, 2005-2010, of which approximately 42 per cent was spent on PFM activities.

4. Implementation Arrangements

4.1. Governance and Management Structure

The governance and management arrangements outline the key decision-making bodies and their roles and responsibilities for directing and managing program resources. The program will, as much as possible, use existing government structures, but recognises that many aspects of GOP policy and interdepartmental coordination around PFM are yet to be finalised. A key challenge for the GOP and the program will be to forge a common or whole-of-government approach to PFM strengthening.

The approach to overall governance and management under the program makes two key assumptions, namely that:

- the GOP has competent and suitably empowered senior officials and technical bodies to guide the program and implement reforms; and
- the GOA has a comparative advantage in key elements of PFM in the Philippines, and can work closely with oversight agencies and service delivery departments to identify and mobilise a range of PFM expertise through diverse government, academic and industry contacts.

Program Steering Committee – this is the home of program decision-making and will provide strategic oversight of program planning and implementation, meeting three times a year in line with the program’s annual planning and reporting cycle (refer Section 4.2.1), or as needed, to consider progress and approve new or changed program inputs. It is proposed the Program Steering Committee comprise the same membership as the GOP PFM ‘core group’ that is composed of senior officials from DBM, BTr and COA, plus representation by the National Economic and Development Authority (NEDA) as the agency responsible for development planning, and AusAID. This way, program assistance will be aligned to the GOP’s own PFM reform priorities.

Philippine Technical Committees – within the PFM area there are a number of existing technical bodies that are either (i) formally established as interdepartmental committees, (ii) functional but yet to be formally established as interdepartmental committees, or (iii) established within a single oversight agency responsible for the PFM process. A key role of the PFMP will be to foster and encourage the formalisation and active participation of these groups in analysing and directing the PFM strengthening agenda in the GOP. Most relevant to the program’s objectives and focus areas are:

- *Reference Panel on ICS/IA* – an informal group established through the PEGR that considers internal audit and internal control protocols across government and is comprised of DBM, OP, Department of Finance (DOF), NEDA, COA and several line agencies.

- *OPIF Working Group* – an internal working group already operating within DBM that considers OPIF formats and data needs across government.
- *Civil society networks* – recognised networks of eminent individuals and academe are established and provide a forum for sharing of budget information and practices to improve and strengthen efforts of CSOs involved in PFM monitoring and transparency. AusAID will need to determine at implementation which network/s is best placed to support the program's objectives.

In terms of PFMP, it is proposed that these groups form a cohort of Philippine Technical Committees to provide technical advice and guidance to the program through regular engagement. The advisory and advocacy role of these Technical Committees has a higher likelihood of success than any stand-alone project in PFM within a single oversight agency and helps to avoid the complex issue of agenda-capture. If required, the program could also take an active role in facilitating the GOP's dialogue over which Technical Committee is best placed to drive initiatives.

Team Leader and Program Coordinator (AusAID) – it is proposed that the Team Leader for this program be an AusAID officer from the Manila Country Office. The program will require consistent, high-level liaison between Australia, the GOP, development partners and civil society to shape a program in support of the GOP's PFM reform agenda. It is vital that Australia presents a consistent policy position throughout this on-going dialogue, and that this message is delivered by an individual with clear authority to make that representation. Initially, the role of ensuring there is no duplication and overlap in program resources will fall to the Team Leader.

Ideally, this candidate would have a background with prior program management experience, and training in and exposure to a broad range of PFM and economic development issues. The Team Leader will have a complex liaison and representation role and will need to be supported by a Program Coordinator, also an AusAID officer at the Manila Country Office.²⁷ The Program Coordinator is likely to be an Overseas-based officer with a background in whole-of-government PFM issues. This role will provide on-going programming support as well as back-up for the Team Leader when he/she is absent. Other AusAID in-house resources may need to be sought to support program implementation.

Technical Advisory Team – it is acknowledged that no individual Team Leader or Program Coordinator has the capacity to address all the technical issues that are likely to be generated during the implementation of the PFM reform agenda. The proposed solution is to set aside funding for a Technical Advisory Team composed of a small number of experts in specific technical areas who can provide technical inputs to the program, work closely with key stakeholders, and identify and mobilise a broad range of PFM sector expertise through diverse contacts, possibly in consortia with other institutions.

²⁷ It is an internal decision for AusAID as to whether these positions are to be funded out of the Departmental or Administered Budget.

The Technical Advisory Team will be contracted at program implementation and may include full-time, part-time or periodic inputs. The types of expertise required may not be limited to the PFM field and, subject to program requirements, could include other areas such as public sector reform, capacity development and organisational management, political governance and management information systems. The technical advisers will provide advice and assistance on the programming aspects of the program, likely to include:

- assessing the feasibility of proposals for specialist technical support under the program;
- drafting of specialist Terms of Reference (TOR) for technical assistance and Scope of Services for sub-contractors;
- engaging counterpart agencies and development partners on activity implementation in their area of expertise; and
- appraising specialised technical papers/reports as part of the program's quality assurance role on behalf of the GOP.

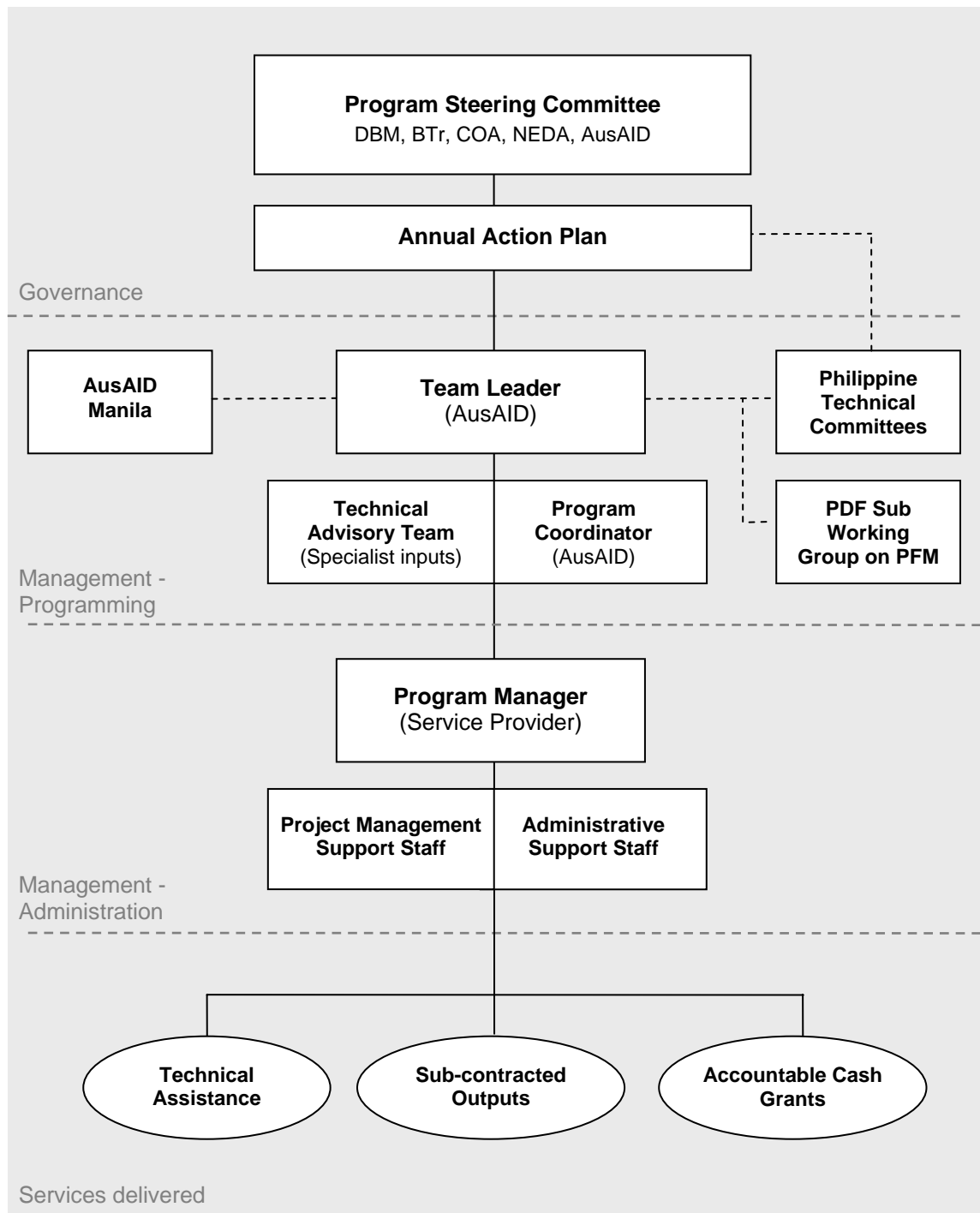
It is proposed that a full-time M&E Specialist forms part of the Technical Advisory Team to support implementation of the program's M&E framework.

Program Office (Service Provider) – a contracted Service Provider will manage the administration of the program and establish a Program Office in Manila outside of AusAID and the GOP, headed by a Program Manager. Program Office staffing will be finalised in detail once a Service Provider has been selected, but full-time resources will include the Program Manager, supported by project management and administrative staff. It is proposed that the Program Office be located centrally, in offices that are readily accessible to the GOP, AusAID, development partners and civil society. Equality of access is essential to establishing the program as a neutral, merit-based entity. The Technical Advisory Team will be located in the Program Office, and the Team Leader/Program Coordinator will need to maintain an office in this location also, to provide for structured consultation and liaison, as needed.

Under this management structure, AusAID is directly responsible for programming risk. This is the overall level of accountability that AusAID normally assumes, but the lines of responsibility are more direct in this design.

The diagram on the next page provides an overview of the governance and management arrangements for the program.

Diagram 1 – PFMP Governance and Management Structure



4.2. Planning and Management Processes

4.2.1. Management – Programming

Annual Action Plan – the principal role of the program is to lend support to the GOP’s own reform efforts. An Annual Action Plan of activities will be annually programmed through a formal process for targeting key priorities of the GOP and associated activities. The Team Leader will develop the Plan in collaboration with the Program

Steering Committee, Technical Committees and development partners; endorsement of the Plan will be the responsibility of the Program Steering Committee.

Engagement with the Philippine Technical Committees could be achieved by AusAID's participation in the regular timetable of committee meetings and/or by convening a separate committee meeting for the purpose of developing the Annual Action Plan. Each Technical Committee will need to be consulted as to which of these options is preferable. It is intended that this dialogue between the program and each of the Technical Committees also serves as a way of formally seeking assistance with key interventions.

The Annual Action Plan will need to be complemented by an out-of-cycle process to address urgent or emerging issues. A total allowance of up to 10 per cent of annual program resources is made for this. Activities financed out-of-cycle would need to follow the broad programming guidelines established for the Annual Action Plan; and be supported by a formal request and endorsed by the Team Leader. The Program Steering Committee will be informed of all out-of-cycle activities.

Three key program milestones compose the planning and reporting cycle each year:

- 1st Quarter Annual Action Plan and Annual Program Accomplishment Report (previous year) to Program Steering Committee for approval
- Mid Year Six-monthly Progress Report to Program Steering Committee
- 4th Quarter Draft Annual Action Plan prepared in consultation with Program Steering Committee and Technical Committees

The Team Leader will receive requests for assistance and appraise each on merit, requesting additional information and seeking the support of the Technical Advisory Team and Program Coordinator as needed. PFM strengthening tasks cannot be unilaterally programmed by the Team Leader or AusAID, although AusAID may expand program funding to accommodate additional requests. In the latter case, there will be a need for the program to have a capacity to be scalable over time; and this will need to be reflected in the management mechanisms that support the program. This approach will require considerable flexibility in both annual programming and subsequent implementation methods.

In complex matters of PFM with wide-ranging impact on the budgetary and accounting systems of the GOP, the program will adopt a two step process: to first help build a coalition for change on key issues; and then mobilise support for implementation of an agreed solution. In such a case, the first step is likely to begin with broad-ranging consultation between the parties to isolate and articulate the main issues, ensure that there is no duplication or overlap, and that sequencing of the initiative is consistent with overall Roadmap progress to date.

This approach is likely to need detailed technical diagnostics to provide balanced and politically neutral information to inform the stakeholders. Diagnostics will be, as much

as possible, led by government and distinguish between system-wide issues affecting an agency's performance and issues that are specific to them, as well as capacity issues crucial to reform management and performance improvement. This step will also assess whether the program can scope, source and deliver the required assistance. This may then be followed by a second step where the program mobilises the assistance required via the Service Provider.

In simpler matters of PFM support, there may be a need for a short-term technical assessment or research role that can be filled on the basis of a formal request from the Program Steering Committee or Technical Committee. The Program can then enter into a defined process to identify, seek GOP endorsement, contract, mobilise and quality assure the output needed by the GOP.

Selection of activities – in the absence of a final Philippines PFM Reform Roadmap and considering the long term outlook of the program, it is not possible to state with clarity or certainty what activities will be supported by the PFMP. However, it is important to set down selection criteria for future program activities that will assist with a consistency of approach over the 10-year term.

The selection criteria proposed for the program activities are as follows:

- Activities that fall within the scope of the program's strategic objectives, especially related to, or in direct support of, budget execution and accountability and transparency;
- Activities that better inform and/or reinforce the political economy around the Philippines PFM Reform Roadmap;
- Activities that support systemic change at either whole-of-government or agency specific level;
- Activities that build the capability of government systems, organisations and people to enable the effective provision of public goods and services;
- Activities that link-up elements of the Roadmap with shared outcomes, such as supporting GIFMIS to provide reliable financial data into OPIF;
- Activities that support other key Roadmap initiatives that are properly sequenced and ready to commence; and
- Activities that support cross-cutting issues such as gender and anti-corruption.

These criteria can be used to test proposals that come to the PFMP for funding and determine whether they can be supported or not. These criteria can be tested and re-evaluated for relevance and sustainability; and amended if needed by subsequent Annual Action Plans and formal reviews.

4.2.2. Management – Administration

Managing administration of the program will be outsourced to a Service Provider selected on a competitive international tender process. A clear distinction needs to be made between the programming role of the Team Leader and the administrative role of the Program Manager. It is not intended that the Program Manager contest program priorities or methodologies with the Team Leader, but he/she will support programming decisions taken by AusAID and the GOP. It is more likely for the Program Manager position to be awarded to an administrative specialist, rather than a development specialist. Under this structure, any direct requests for program assistance made to the Program Manager need to be formally referred to the Team Leader/Program Coordinator.

The role of the Service Provider will be to:

- source and provide the GOP with timely and value-for-money access to diverse and appropriate technical advice and expertise from within and outside of the Philippines across a range of PFM topics. In doing so, the Service Provider will aim to maximise the use and development of partner country institutions and in-country sources of expertise;
- procure and manage contracted inputs (consistent with the principles of the Commonwealth Procurement Guidelines);
- provide administrative support to all program inputs;
- manage and report on program funding;
- provide administrative secretariat services to the Program Steering Committee and Technical Committees if required; and
- develop and implement a communication and information strategy to collate and disseminate appropriate information between and across key partners and stakeholders.

It is likely that the Service Provider costs will have a fixed and a variable component. Fixed costs will be those needed to support the offices and amenities and minimum staffing establishment. These will be determined by agreement and will be fully reimbursable. This removes any commercial risk to the Service Provider and allows a clear focus on quality support and services to the program.

Variable costs will relate to the additional cost of each recruitment and/or procurement managed under a separate Tasking Note issued by the Team Leader/Program Coordinator on behalf of the Program Steering Committee. There are two components to each variable cost incurred, being the direct costs of the individual contract, and Service Provider fees for undertaking the recruitment or procurement.

In order to promote high quality recruitment and procurement, it is proposed that the direct costs of each Tasking Note also be reimbursable to the Services Provider; and that only the recruitment/procurement management fee be at performance risk. It is this payment component that would be held up, or waived, in the case of poor or unacceptable performance by the Service Provider. Performance will be assessed and determined by the Team Leader/Program Coordinator and AusAID under the terms of the Contract and the program M&E arrangements. It is anticipated that quality and responsiveness of the Service Provider will be a key appraisal criteria for AusAID.

Other administration support to AusAID – in addition to its main role of servicing the PFMP, the Service Provider may be contracted to provide administrative support directly to AusAID's operations in the Philippines in functions where the Service Provider has a comparative advantage and where there are cost advantages to AusAID. It is anticipated that any functions outsourced by AusAID to the Service Provider would be minimal initially. Details will be supplied during the tender process.

4.3. Monitoring and Evaluation Framework

M&E in the PFMP serves two equally important purposes: (i) it provides management information so program management and both governments can continually calibrate implementation to maintain progress towards objectives and to achieve the greatest impact; and (ii) it provides the basis for accountability to both parties and the citizens of both countries regarding the effectiveness of the investment in the program. In other words, the M&E arrangements ultimately seek to answer two overarching questions: Is the program being implemented as planned? And is the program having the intended positive effect (and not causing unintended negative effects)?

The M&E Framework for the PFMP builds upon the lessons of the predecessor PEGR.²⁸ It will provide management information to ensure the program is heading in the right direction. It will generate performance data to measure progress and performance of the program against agreed indicators linked to the GOP's own PFM reform targets and is anchored on the program's logic and results-orientation; it presents and elaborates a clear linkage of the indicators on inputs and outputs against outcomes and impacts. The M&E Framework will also be a mechanism for informed decision-making to increase the potential for success.

Performance indicators provide a means for day-to-day performance management, periodic monitoring and ongoing risk assessment, and contribute to the program evaluation. They will enable the program to track changes (expected and unexpected), their causes, and the implications for the program and the GOP. As the PFMP is a flexible and responsive program that will work across a range of agencies within an annually updated action plan, it is not possible to provide a concrete set of performance indicators at program design from which to monitor and assess the achievements of the

²⁸ PEGR's Performance Management Framework focuses on measuring performance of Facility Partners and Partner Contractor against key performance areas/indicators under an incentive scheme containing reward and penalty. This proved to be limited and required a complementary M&E Framework that measures the progress of reform activities against Facility objectives.

program. However, in order to foster partnership it is still important that an agreement is forged among partners at the start of the program implementation on the M&E Framework and an accompanying set of key performance indicators and processes.

Baseline information on performance indicators is essential. It is important when undertaking diagnostics and establishing TOR and Scope of Services that baseline information on the areas requiring assistance is established. Well documented baseline information will ensure disciplined future monitoring and assessments of improvements. Where accurate baseline information is not available or suspect, agreement should be reached between parties on the most accurate description of the current performance level of the outputs and outcomes that are intended to be addressed.

Monitoring of capacity development in the program is directly linked to the performance indicators. A wide range of stakeholders and their perspectives on 'capacity' needs to be incorporated into program monitoring. This includes qualitative feedback on achieving change as well as quantitative measurement.

Progress towards the program's objectives will be influenced by a range of technical and non-technical factors; only one of which will be the support through the PFMP. A key M&E instrument will be surveys to capture implementers and recipients' satisfaction and contribution to program outcomes and capacity development. The survey instruments and sampling design will be developed at program implementation, but should contain questions that address and respond to all levels of analysis (see below) and should be evidence-based. The survey instrument should also allow triangulation to validate data and information.

The program will share the M&E reporting with stakeholders and, as much as possible, feed into the GOP specific reporting processes and systems. The M&E arrangements will also link to AusAID internal quality processes: Quality at Entry, Quality at Implementation, and Quality at Completion.

4.3.1. Levels of Analysis

The M&E arrangements for the program operate at four levels of analysis:

- *Objectives* – achieving the overall program goal and strategic objectives is not wholly within the control of the PFMP, but its efforts are intended to make a substantial contribution to achieving them. GOP programs and other donor interventions will contribute to these objectives, and their achievement will also be influenced by exogenous factors. The goal and strategic objectives have a long term horizon (5-10 years) and performance will be assessed over that timeframe.
- *Intermediate outcomes* – program outcomes will in many cases require additional customised data collection and/or analysis to provide indicators of progress. Independent evaluation at the outcome level will be undertaken. The

M&E Specialist will support others (ideally mainly in government) to do data collection, but will also facilitate data collection and analysis.

- *Outputs* – activity outputs will be specified for each activity funded by the program. Details of activities and indicators will be progressively developed over the life of the PFMP, but are included in the M&E framework as indicative so that there is program logic to the achievement of outcomes and objectives. It will be a core requirement of all activities that they clearly articulate their intended outputs, and the M&E Specialist will assist with this process.
- *Inputs* – activity inputs will be monitored throughout implementation in order to provide program management and both governments with data including on resource utilisation and cost. While inputs monitoring is of little value in determining a program's effectiveness, there is a need to be able to report the extent of use of the various modes of support, the relative costs of different inputs, and the range of sources for procurement.

4.3.2. Program Reporting

The M&E arrangements are designed to minimise formal program-specific reporting so that reporting does not become a distraction from program activities for implementers and program management. A number of regular reports are, however, necessary:

- *Annual Program Accomplishment Report* – submitted to the Program Steering Committee in the first quarter of each year and will provide an overview of annual program progress, based on agreed performance indicators. The annual report will also feed into AusAID's annual quality and performance reporting processes.
- *Six-monthly Progress Report* – prepared on the basis of exception reporting, highlighting significant achievements, areas of concern and/or opportunities. The progress report will be brief and will focus on issues, lessons, opportunities and constraints to feed into the preparation of the next Annual Action Plan. The Team Leader will provide more frequent verbal reporting to AusAID and the Program Steering Committee as needed.
- *Implementation Reports* – prepared by program implementers (e.g. advisers) and will take a similar exception reporting approach, providing brief quarterly reports to the Program Manager. They will feed into the program-level reporting and into regular meetings of the relevant committees in order to provide a complete picture of progress, risks, opportunities and lessons learned.

Regular program reporting will be supplemented and verified by external independent evaluations of the effectiveness of the program. These evaluations will be conducted at the beginning of the third and fifth years of the program (subject to program extension). The second of these evaluations forms a *Mid-Term Review* and will inform decisions about the future shape and focus of the program for a potential second five-year phase

in a ten year program, allowing enough time for any necessary re-design and any restructuring of management and/or implementation arrangements.

4.3.3. Roles and Responsibilities

The roles and responsibilities of key program actors in the implementation of the M&E arrangements are:

- *Program Steering Committee* – provides the strategic oversight of the program, approving the Annual Action Plan and monitoring program performance at the program levels (outcomes-objectives).
- *Philippine Technical Committees* – monitor progress and performance at both program levels (outcomes-objectives) and activity levels (inputs-outputs), and make recommendations and proposals about what areas the program supports.
- *Team Leader* – in partnership with the GOP and with support of the Program Coordinator, monitors the program at both program and activity levels, including through engagement with the Program Steering Committee and Technical Committees. The Team Leader has overall responsibility for program level reporting to the Program Steering Committee and AusAID.
- *M&E Specialist* – ensures the M&E Framework is appropriately managed, updated and implemented as per the Design, and enables methodologies and strategies to be consistent across the program. The M&E Specialist is responsible for the preparation of program reporting in collaboration with all parties and will coordinate the collection of evidence on the impact of the program, including information about other GOP, AusAID and donor programs operating in PFM reform. A component of the M&E Specialist's TOR will be to invest in opportunities for learning and incorporating qualitative techniques to capture the depth and breadth of change programs.
- *Program Manager* – has responsibility for the quality and timeliness of implementation reporting. The Program Manager, through the Program Office, will be responsible for developing and maintaining an information management system, website and database for easy storage, access, retrieval of information and reports. The Program Office will also provide procurement and logistical services to support independent evaluations of the program.

4.3.4. M&E Matrix

An indicative M&E matrix is at Annex 2. The matrix specifies performance indicators and data sources to form the basis for the ongoing monitoring and evaluation of program effectiveness. The matrix will need to be reviewed and updated as appropriate on mobilisation of the program so that it utilises current GOP systems to the greatest extent possible, and to maximise the value of data and reporting tools for the GOP.

4.4. Management of Risk

Sustainability and effectiveness

Risk – engagement in PFM is not guaranteed to be successful. The potential significant benefits of PFM are balanced by substantial risks. Reforming PFM systems goes to the core of government decision making, operations and opportunities for corruption. The international experience of PFM reform in developing countries indicates that change is difficult with frequent setbacks.²⁹ The Philippines system has proved resilient to change and the slow pace of progress can be difficult for development partners with short term result and reporting horizons. Progress is not impossible though as many of the reforms to PFM are technocratic in nature and selective support by donors can nurture the progressive elements of government to improve their systems.

Response – expectation of program achievement should be of modest incremental progress towards realistic long term objectives. In the early stages of the program some clear indicators will be set to measure progressive success over the short term. Ideally, the engagement between the GOP and AusAID will be a long term partnership that reflects that timeline, as major evolution in PFM can sometimes be measured in decades rather than years. As equal partners it is hoped that the Governments of Australia and the Philippines can have a robust, open debate about the best way to strengthen PFM systems. This may sometimes involve agreeing to disagree, but as long as the lines of communication are open and honest then a robust dialogue will benefit all partners.

Political and bureaucratic commitment to PFM reform

Risk – the program's design is taking place in an election period and transition to a new Administration. As a natural part of the democratic cycle there is some uncertainty in the GOP's policy agenda. If the new government were to adopt a comprehensive PFM improvement agenda as a key priority then the absorptive capacity for effective utilisation of funds would increase. Without a high quality reform agenda that links long term strategic goals with practical intermediary steps, small scale reform efforts may be poorly sequenced, inconsistent with each other and might not lead towards a long term strategic objective.

Response – the program will devote considerable up-front resources to assist the finalisation and implementation of a whole-of-government PFM reform strategy. If the GOP has adopted a strategic reform agenda that outlines the specific technocratic steps needed to reach long term objectives, this alone could be considered a significant achievement by all partners. Even in the absence of a whole-of-government PFM reform agenda there are important institutional changes that can be pursued in small steps, such as improving the financial processes and systems of the spending departments, assisting DBM with better performance information, and the roll out of internal controls and audit to key departments. It is possible for a constituency of reform

²⁹ Allan, The Challenge of Reforming Budgetary Institutions in Developing Countries, IMF Paper May 2009

amongst progressive middle level technocrats who will support intermediate steps towards greater reform.

Corruption

Risk – corruption is an issue of significant concern in the Philippines. International measurements of country efforts to control corruption generally show a long-term decline in the Philippines' performance. The World Bank Governance Indicators show a marked decline in the country's control of corruption rating over the last decade. Similarly, the 2008 Transparency International Corruption Perceptions Index showed that the Philippines ranked 141 out of 180 countries, continuing a long-term deterioration in both raw score and relative ranking to the region.

Response – the program is appropriately focused on the positive link between PFM improvement and facilitating better service delivery. However, the program is aiming to strengthening key parts of the systems that limit and control corruption, thus the program core focus could be considered in large part to be focused on anti-corruption. Improved transparency and reporting of fund use, internal control and audit and external analysis of the budget are all key anti-corruption measures. Strengthening these mechanisms within government will also facilitate the greater use of government systems by donors.

At the operational level of executing funds, there is only a moderate danger of misuse of AusAID funds as the primarily expenditure of the program will likely be technical support and not in the high corruption areas such as infrastructure or information technology hardware. The overall risk to the program of misappropriation of funds will also be mitigated as DBM has already requested that program funds remain donor executed to reduce administration burden. The program may in limited cases move to the use of partner government systems and in these cases standard AusAID fiduciary and accountability controls will apply.

Coordination with development partners

Risk – lack of coordination and cooperation between development partners can lead to duplication of effort and overburdening of GOP partners, which could undermine the program's effectiveness. Furthermore, poor donor communication can risk driving the debate towards a rushed or inappropriate agenda that suits the needs of individual development partners more than government. This risk is not as strong as in many developing countries. Total ODA to the Philippines is only 0.5 per cent of GNI so even if they wanted to development partners lack the financial clout to impose on government. However, development partners can still play a strong role in influencing the strategic agendas and providing specific technical advice.

Response – the program's activities will all require sign off from relevant government officials. Ongoing collaboration and coordination will be sought through the PDF Sub-working Group on PFM, which AusAID co-chairs with DBM. AusAID has also collaborated closely with the World Bank on a strategic priority paper for the new

Administration. Co-financing or collaborative analytical work should be actively pursued between development partners under the new program.

Performance and effectiveness of technical assistance personnel

Risk – the quality of technical assistance personnel used by the PFMP is central to the overall effectiveness of the program. Technical inputs that are unsatisfactory and not in accordance with the PFMP design or suited to the Philippines context may put in jeopardy the good standing of the program and AusAID.

Response – the PFMP recruitment strategy will be implemented in partnership with the GOP and agency partners and stakeholders. Ongoing strategic management of technical assistance personnel is a core element of the program and will be monitored as part of the ongoing assessment of aid effectiveness through the M&E Framework and contractor performance.

Management of the program by AusAID

Risk – AusAID's decision to directly manage the program requires that it has appropriate in-house skills and experience in program management, and training in and exposure to a broad range of public financial management and economic development issues. Failure by AusAID to provide overall strategic direction and management is a risk to the success of the program.

Response – AusAID has been engaged in supporting PFM strengthening and broader economic development in the Philippines, and in the region more broadly, for many years. Australia has undergone significant reforms of its own PFM systems and is able to draw on this experience, as well as internationally, when implementing development assistance programs. Australia continues to be a lead donor in the PFM field and as such has had an opportunity to learn from the successes and challenges of that assistance. There are suitably qualified candidates for the Team Leader and Program Coordinator roles within AusAID, but as a fallback other Australian Government agencies could be approached to fill these positions if required. Ensuring effective succession arrangements from one AusAID Team Leader or Coordinator to the next will be a task for AusAID Manila to manage.

4.5. Gender and Development

The Philippines is well-advanced in promoting gender equality as an integral element of development. It ranks ninth among 134 nations in the 2009 World Economic Forum gender gap index in providing equal opportunities and resources for women. Although this means that the country is three notches down from its 2007 record, it is still way ahead being the only Asian nation in the top 10. The presence of legal, policy and institutional infrastructure facilitates gender mainstreaming in public administration and governance to ensure women and men equally contribute to and benefit from development. Civil society also plays an active role in advocating for and monitoring the country's progress and compliance vis-à-vis its national and global commitments in advancing gender equality such as Women in Development and Nation-Building Act

(RA 7192), Beijing Platform for Action, Millennium Development Goals, among others.

The Philippine Commission on Women (formerly the National Commission on the Role of Filipino Women) serves as the oversight agency in coordinating, implementing, and reviewing gender mainstreaming efforts in the bureaucracy. In partnership with NEDA and the Official Development Assistance Gender and Development Network, the Commission formulated the Harmonized GAD Guidelines. The Guidelines provide donor, government and other stakeholders with an instrument to enable the gender responsiveness of programs and projects.

A landmark legislation on gender budgeting was passed in 1992 which requires all government agencies and LGUs to allocate a minimum of five per cent of their total budgets to GAD-responsive programs and projects. This policy has been integrated in the annual budgeting process of the government. However, challenges remain in terms of the quality of implementation and compliance which stem from poor gender analysis at the initial stages of project development, including expertise in identifying gender issues and resources needed to gather sex-disaggregated data.

The systemic failure of enforcement of the GAD and other legislated appropriation stems not from a lack of good intentions but fundamental constraint in Philippines that any system of policy based budgeting requires a foundation of sound and transparent cash management to implement. A more meaningful gender budgeting requires a PFM system with sufficient capacity to pursue and attribute discrete policy objectives and outcomes to government expenditures.

4.5.1. PFMP and Gender Budgeting

All Australian development assistance should be provided in a manner that advances gender equality and empowers women, particularly through supporting country-led priorities for gender empowerment, engaging with both men and women to advance gender equality, strengthening accountability mechanisms and supporting the collection and analysis of information to increase gender equality and improve results.³⁰

The Australian Government supports the Philippines' efforts on gender equality. In terms of improving gender budgeting, this is a long-term development agenda that requires careful sequencing of reform activities. Fundamentally, a meaningful system of gender budgeting is best served by AusAID's PFM assistance targeting the basic accountability measures within the key social services agencies to make resource use more transparent and accountable.

AusAID, in consultation with the GOP, will also support the practical integration of a gender dimension within the OPIF framework. The PFMP will pilot test the feasibility of developing gender-responsive and performance-based budgeting through the OPIF in key agencies such as DepEd and DSWD. The program will explore meaningful ways of

³⁰ Gender equality in Australia's aid program – why and how, AusAID, 2007

mainstreaming gender in the OPIF formulation to make the MFOs gender aware and/or developing gender-responsive performance indicators.

The intended benefits of this approach are two-pronged. By understanding the nature of inequality through the performance indicators, the GOP will have an informed decision in allocating its limited resources. On the other hand, increasing transparency and promoting gender-responsive information through the OPIF will help various stakeholders in analysing the gender implication of budget allocation. The OPIF information can also guide review of whether programs and activities address gender gaps and issues.

Annex 1. Background Note on Information Systems

Design Team consultations with several GOP agencies have indicated two main information deficiencies preventing proper analysis of public services delivery. They are: (i) central agency evidence that departments report inaccurately and late; and (ii) departmental evidence that funding of Budgets is delayed and incomplete.

In a largely manual bookkeeping process, such as that prevailing in GOP, it is resource-intensive and time-consuming to bring about changes to reporting formats. Major resources are employed simply in keeping books and records of account, without considering error clearing and then reporting. In the past decade, these manual public expenditure management tools have been significantly impacted by the following GOP reforms:

- In 2001, the GOP introduced accrual accounting across all 430 reporting entities in government. This resulted in an entirely new approach being taken to bookkeeping in the form of additional subsidiary ledgers to record Accounts Receivable and Payable, Assets and Liabilities and other provisions such as Annual Leave and Retirement Entitlements.
- In 2005, the introduction of an OPIF required the preparation of detailed financial reporting to match up to physical reporting using the Program, Project and Activity format set out in each Budget. This called for all manual Budget Registries to be fully up to date each quarter, a major additional demand on resources given the large volume of physical documents and Registries involved; and the large carried forward balances of unreconciled items evident in most Registries. Many of the bigger departments have invested in automated accounting tools of various designs to assist with financial and performance reporting.
- In 2009, the introduction of monthly Notice of Cash Allocations (NCAs), while allowing for quicker, more reliable release by Treasury resulted in the workload around maintaining Budget Registries increasing by a factor of three, from quarterly to monthly.

The combined impact of these prior changes has been for departmental budget and accounting personnel interviewed by the Design Team to call for stabilisation of the public expenditure management systems; and not for greater reforms.

Role of COA

The practical improvement of information systems falls under the responsibility of COA for designing and approving automated accounting tools for use by GOP.³¹ In 2004, aware of the additional bookkeeping burden that accrual accounting and performance

³¹ The design team is aware that in the past there has been some debate about ideal mandate of COA and their responsibility under the Constitution. The design team is assuming CoA will retain a strong mandate in accounting policy and execution in the short to medium term.

reporting would impose on existing manual systems, COA designed a suite of accounting software that could assist departments to automate their bookkeeping functions. This comprised two applications, with others proposed; these were:

- Electronic New Government Accounting System (e-NGAS) – to automate bookkeeping in the General Ledger, Subsidiary Ledgers and preparation of Financial Statements; and
- Electronic Budgets (e- Budgets) – to automate maintenance of all Budgetary Accounting Registries.

These tools have had a limited roll-out into departments since their release by COA. A number of factors have affected the adoption of these automated tools in the GOP:

- e-Budgets was suspended in 2005, primarily due to an internal debate within COA about the effectiveness this application as a stand-alone module compared to integrating it into a future release of e-NGAS;
- e-NGAS has been rolled out to 52 (12 per cent) of 436 reporting entities at 2007, but the roll-out program was also suspended in mid-2008 due to disagreements within COA regarding the need to integrate e-Budgets and IPSAS into a revised version of e-NGAS at some later date;
- resistance from major departments who have already invested in automated accounting tools of various designs to assist with OPIF and financial reporting and do not wish to see that investment disrupted or superseded. Further, a lack of web-based links between existing departmental records and e-NGAS renders it less user friendly than departments require, so alternative solutions are being sought;
- the cost of e-NGAS implementation by COA, reported to the Design Team to be PHP70,000 per site, per month for the duration of the installation up to the acceptance of the software by implementing agencies; and
- the absence of a clear roll-out plan for e-NGAS and e-Budgets that has high-level support and a well-designed communications plan to manage HR concerns in budget and accounting officers as the public expenditure management process is automated.

The Design Team considers that this long-delayed automation of public expenditure management tools is largely a result of under-resourcing of the accounting side of COA's mandate. COA advised that it has 9,000 auditors and 150 accounting specialists' positions, of which only 70 are currently filled. This is indicative of the respective effort that COA can bring to bear on the automation of public accounting, compared to its audit role.

Designing and then implementing a major public expenditure automation project requires strong, obvious leadership. In most jurisdictions an “Accounting Czar” would be appointed; given broad and independent authority; and then adequately resourced to achieve the process within a responsible time-frame.

There is no structural impediment to the Commission Proper making such an appointment; conferring the required independence and authority on that office; and then resourcing that function adequately. Doing so would achieve two objectives simultaneously. Firstly, it would allow COA to begin to take a first step to establish a truly independent audit function, without being constrained by the accounting responsibilities required in the Constitution in any practical sense. The next step could be to seek a formal separation of these two discrete constitutional roles, as appropriate.

Secondly, such a Commission Proper decision and appointment would give the necessary gravitas and resourcing to automation of the public expenditure system. This streamlining of the public expenditure system is needed to keep up with the GOP’s growing demand for information as it continues to implement its often-stated policy of performance management in the public sector.

Annex 2. Monitoring and Evaluation Matrix

Performance Indicator	Baseline Information	Intermediate Outcomes	Means of Verification
PROGRAM GOAL – Improvement in the efficiency, accountability and transparency of public fund use in the Philippines to enable better service delivery			
A. Government efficiency of allocating public resources for development is improved	Despite comprehensive budget documentation, there is weak planning-budgeting nexus, frequent delays in approving the budget, extensive in-year reallocations of the approved budget, and difficulty in tracking budget allocations; each of these factors undermines the credibility of the budget	<ul style="list-style-type: none"> a. Annual budget is delivered within a fixed budget calendar b. Ability of government to monitor implementation of the agreed annual budget is improved c. OPIF is more effective as an agency performance management and resource allocation tool 	Annual budget documents; OPIF Book; COA Annual Audit Reports; Annual Financial Statements of government; diagnostic studies (PEFA, PERs); Government/DP sector program reports; President's Budget Message; Legislative Budget hearings; third party assessments (SEPO, CPBD, CSOs, Academe)
B. Government efficiency of delivering public goods and services is improved	Lack of interdepartmental coordination combined with uncertainty around budget execution procedures and a complex system of budget and accounting reporting results in a highly labour intensive PFM system	<ul style="list-style-type: none"> a. Comprehensive PFM reform program is launched by government b. Key budget execution systems and procedures are improved c. Internal controls systems and internal audit are strengthened 	Annual budget documents; OPIF Book; COA Annual Audit Reports; Annual Financial Statements of government; budget execution documents and reports; diagnostic studies (PEFA, PERs, PETS); third party assessments (SEPO, CPBD, CSOs, Academe)
C. Government accountability and transparency of appropriated funds is improved	Sub-par external reporting is exacerbated by fragmented data and unconnected manual and electronic PFM information management systems, as well as significant portions of approved appropriations being outside spending agencies and normal accountability mechanisms	<ul style="list-style-type: none"> a. More timely and reliable public expenditure information better informs government and the public b. More capable civil society builds demand for improved accountability and transparency c. Budget oversight role of Congress improves 	Annual budget documents; OPIF Book; COA Annual Audit Reports; Annual Financial Statements of government; President's Budget Message; diagnostic studies (PEFA, PERs, PETS); Legislative Budget hearings; third party assessments (SEPO, CPBD, CSOs, Academe)

Performance Indicator	Baseline Information	Intermediate Outcomes	Means of Verification
OBJECTIVE 1 – Increase the efficiency and effectiveness of the allocation, utilisation and reporting of budgeted funds by oversight agencies			
A. Whole-of-government coordination for implementing PFM reforms is improved	An agreed whole-of-government PFM reform strategy or program does not exist	<ul style="list-style-type: none"> a. Government PFM Reform Roadmap is agreed, costed, and appropriately prioritised and sequenced b. Interdepartmental information flows and reporting is improved through better coordination amongst oversight agencies c. PFM ‘core group’ implements ‘quick win’ reforms 	Strategy or reform document which is publicly available; Executive and Congress are willing to support PFM reforms; President’s Budget Message
B. Systems and procedures for budget formulation are improved, including the timeliness, presentation and communication of the budget	Budget documents are comprehensive but presentation of data is not user friendly and the complex appropriation structure, combined with re-enacted budgets, prohibits a reliable and efficient means of calculating out-turn budgetary information	<ul style="list-style-type: none"> a. Public version of the PBS is prepared in a timely manner to explain budget decisions in terms of government policy b. Format of budget documentation is improved and/or a simplified budget brief is prepared to communicate key budget outcomes c. Options developed to simplify the appropriation structure of the budget, especially the reporting of automatic appropriations, and improve procedures for agencies to manage re-enacted budgets 	Budget documentation; PBS; official budget Guidelines and Circulars; Executive Orders; OPIF Book
C. Systems and procedures for budget execution are improved so there is predictability in the availability of funds and better reporting of utilisation of public	Budget execution procedures such as cash management and in-year budget reporting are cumbersome and resource intensive for agencies, with low	<ul style="list-style-type: none"> a. Complete a government PFM manual to provide a common understanding of budget execution laws, regulations and procedures 	Budget documentation; budget execution documents and reports (ABM, SAROs, NCAs, SAOB); Monthly Cash Program; official budget Guidelines and Circulars; Executive Orders; MDS guidelines; PFM

Performance Indicator	Baseline Information	Intermediate Outcomes	Means of Verification
funds	compliance in some areas	<ul style="list-style-type: none"> b. Options developed to streamline interdepartmental cash management and release procedures, in-year budget processes and reporting c. Controls and monitoring of MDS accounts and bank reconciliation system is improved 	manual
OBJECTIVE 2 – Improve PFM capability in select departments to enable more efficient utilisation and accountability of public funds for service delivery			
A. Budget execution in select agencies is improved, leading to the removal of PFM-related blockages to service delivery	Most large spending agencies received either qualified or adverse opinions by COA	<ul style="list-style-type: none"> a. PFM reforms are included as a key component of sectoral programs of government and DPs b. Budget and finance offices in select agencies improve capability to utilise and account for government funds c. Some expenditure monitoring and reporting processes are improved in select agencies 	OPIF Book; COA Annual Audit Reports; Annual Financial Reports; Agency Performance Reviews; Budget Performance Assessment Reports
B. Internal control systems in select agencies is improved	Internal control systems exist in most large spending agencies but non compliance is routine and widespread	<ul style="list-style-type: none"> a. Management Divisions (or equivalent units) of select agencies improve capability to monitor and assess internal controls b. NGICS applied in and tailored to select agencies 	OPIF Book; Agency Performance Reviews; Budget Performance Assessment Reports; COA Annual Audit Reports; risk management plans and reporting; ICS operating manuals
C. Coverage and quality of internal audits by select agencies is improved, and attests to agency performance reporting	Internal Audit Units are established in most large spending agencies, but capability and the quality of internal audit reports is generally sub-par, and	<ul style="list-style-type: none"> a. Internal Audit Units of select agencies improve capability to undertake quality internal audits b. PGIAM applied in and tailored to 	Review of PGIAM; agency audit plans; quality of internal audit reports and links to Agency Performance Reviews; Budget Performance Assessment Reports; COA

Performance Indicator	Baseline Information	Intermediate Outcomes	Means of Verification
	responses to audit finding are often delayed	select agencies	Annual Audit Reports; management responses to audit findings; IA operating manuals
OBJECTIVE 3 – Generate more timely, reliable and accessible public expenditure management information			
A. Usage of OPIF as a tool for agency performance management and resource allocation decisions is increased	OPIF Book of Outputs is produced annually and has full coverage of government agencies, but the quality of financial and performance information needs to be verified and improved in some cases	<ul style="list-style-type: none"> a. Finalise and roll-out OPIF guidelines to provide clear standards for linking MFOs and performance indicators, and for identifying more robust performance information b. Reporting of PAPs expenditures is improved for major spending agencies and can be verified by DBM 	OPIF Book; OPIF guidelines; budget documentation; Agency Performance Reviews; Budget Performance Assessment Reports; records of Budget Hearings in the Legislature; President's Budget Message
B. Core systems and processes for reporting of budgeted funds are improved	Currently there is a lack of coherence between the classification system used for budget formulation, execution and reporting	<ul style="list-style-type: none"> a. Concrete steps taken to improve coherence between the format DBM formulates the budget in and the one COA reports on 	Budget documentation; OPIF Book; Agency Performance Reviews; Budget Performance Assessment; Annual Financial Reports of government; COA Annual Audit Reports; Annual Report on Allotments, Obligations and Disbursements; GIFMIS implementation plan
C. Transparency of in-year and out-turn reporting on government expenditures is improved	Public reporting of budget execution is limited, with little in-year reporting, and out-turn reporting compromised by different classification systems between DBM and COA	<ul style="list-style-type: none"> a. Make in-year budget reporting, such as a consolidated SAOB, readily available to the public b. Concrete steps are taken to improve the alignment of out-turn budget reporting with the GAA and improve the timeliness of reports 	Budget documentation; in-year budget reporting (BEDs, BARs, SAOB, Monthly Report of Disbursements), Annual Financial Reports of government; COA Annual Audit Reports; Annual Report on Allotments, Obligations and Disbursements; GIFMIS implementation plan

Performance Indicator	Baseline Information	Intermediate Outcomes	Means of Verification
OBJECTIVE 4 – Strengthen external oversight of public expenditure management linked to physical performance information			
A. Constructive engagement between CSOs and government on budget analysis and monitoring is increased	Analysis of budget execution and performance by civil society is limited and no formal channels for cooperation with government exist	<ul style="list-style-type: none"> a. Recognised research body or ‘think tank’ on budget analysis is formalised by credible CSOs and academe b. Capacity of CSOs to provide an objective measure of government budget execution and performance is improved c. Forum for cooperation between government and select CSOs is agreed 	Government websites; civil society reports/websites; media evidence of CSOs and academe reports influencing decision making; Congress/Legislative Budget hearings
B. Quality research and analysis by CSOs and academe is used by government to monitor and report on public service delivery	Civil society analysis and monitoring of government expenditure for service delivery is limited	<ul style="list-style-type: none"> a. Preparation of key pieces of analysis by civil society, which is publicly available and utilised by key stakeholders b. Oversight agencies use civil society reports in budget planning and formulation 	Government websites; civil society reports/websites; media evidence of CSOs and academe reports influencing decision making; Legislative Budget hearings
C. Capacity of Congress in its budget oversight function is improved	Despite having a constitutional mandate to oversight budget execution, this is scarcely practiced by either Houses of Congress	<ul style="list-style-type: none"> a. Congressional budget oversight role is more widely understood b. Tools for conducting budget oversight are provided to Congressional staff and technical offices 	Legislative Budget hearings

Annex 3. PEFA Performance Indicator Summary³²

A. PFM-OUT-TURNS: Credibility of the Budget			
PI-1	Aggregate expenditure out-turn compared to original approved budget	Not Rated	It is not possible to calculate the expenditure out-turn ratio because of the unavailability of the ex ante figures for continuing appropriations in the budget documents.
PI-2	Composition of expenditure out-turn compared to original approved budget	Not Rated	It is not possible to calculate the variance in expenditure composition relative to overall deviation in primary expenditure because of the unavailability of the ex ante figures for continuing appropriations in the budget documents.
PI-3	Aggregate revenue out-turn compared to original budget	C	The 2006 revenue out-turn was significantly lower than projected.
PI-4	Stock and monitoring of expenditure payment arrears	D+	Arrears are overstated, not being reduced and not well managed
B. KEY CROSSCUTTING ISSUES: Comprehensiveness and Transparency			
PI-5	Classification of the budget	D	The execution and reporting system does not use the budget classification.
PI-6	Comprehensiveness of information included in budget documentation	B	Budget documentation includes economic forecasts, prior year data, policy initiatives and debt level.
PI-7	Extent of unreported government operations	A	E.O. 292 imposes use of “one-fund” concept. Revolving fund and trust fund transactions remain off budget but are not material.
PI-8	Transparency of inter-governmental fiscal relations	B	Internal Revenue allotments are determined by reference to revenues collected and a formula based on land area and population. However, there is a lag in the availability of the annual LGU fiscal reports, sectoral classifications used between the BLGF reports and the BESF are inconsistent and ex-ante budgetary data are excluded.
PI-9	Oversight of aggregate fiscal risk from other public sector entities.	C+	Although COA and DOF-CAG monitor most of the GOCCs, the failure to conduct valuation of contingent liabilities and consolidated analysis of performance and risks leaves reporting incomplete. Fiscal risk of LGUs is not documented.
PI-10	Public access to key fiscal information	C	The GOP discloses fiscal and budget information through various agencies’ websites. However, posting of budget execution, contract awards, COA audit reports and availability of resources to service delivery units is not timely and are most of the time incomplete.

³² The PEFA assessment report in the Philippines is not yet publicly available but was accepted by the GOP in late 2009. The results may be selectively used as a baseline for future assistance subject to agreement by the GOP. COA furnished the Design Team with comments and corrections on the PEFA performance indicator summary which are included for information. These are marked in italics.

C. BUDGET CYCLE			
C(i) Policy Based Budgeting			
PI-11	Orderliness and participation in the annual budget process	B	Although the executive always submits budget documentation on time in accordance with a budgetary timetable, the budget law is passed with a 3-4 month delay or is sometimes not passed at all.
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting	D+	Development of Forward Estimates covering two forward years started in 2006, but the link to annual budget ceilings has yet to be firmly established.
C(ii) Predictability and Control in Budget Execution			
PI-13	Transparency of taxpayer obligations and liabilities	C	The basic guide available from BIR and the internet site is very clear. However, tax codes and the BIR-issued regulations and rulings especially for income tax are highly complex, unclear, and sometimes technically inaccurate.
PI-14	Effectiveness of measures for taxpayer registration and tax assessment	C	BIR Registration process is sound and is associated with some data sharing. Penalties tend to be written off to secure collections. Customs is less advanced.
PI-15	Effectiveness in collection of tax payments	D+	Collections are not reconciled with receipts and cash at bank
PI-16	Predictability in the availability of funds for commitment of expenditures	D+	DBM controls commitments (obligations) by issuing general or special allotment release orders. Poor reporting on budget execution makes it difficult to establish the actual extent of budget re-alignment (re-allocation).
PI-17	Recording and management of cash balances, debt and guarantees	B	BTr actively manages debt and consolidates cash balances but does not sweep interest, idle funds and other account balances from MDAs. RA 4860 sets the ceilings for foreign borrowings and guarantees. <i>RA 8182, on the other hand, provides for the exclusion of ODA loans from the foreign debt limit, amending Paragraph 1, Section 2 of RA 4860, as amended.</i>
PI-18	Effectiveness of payroll controls	C+	Human Resource records are not in place in all MDAs. Audit reports indicate overpayments are common.
PI-19	Competition, value for money and controls in procurement	B	Use of limited source procurement or shopping does not exceed 10% of the value of the contracts under the Annual Procurement Plan (APP) in 5 out of 10 agencies surveyed. However, audit reports still indicate that compliance with RA 9184 needs improvement.
PI-20	Effectiveness of internal controls for non-salary expenditure	D+	COA audit reports reveal that reporting and post purchase order controls are lacking. Vast majority of COA AAR opinions for

			national government agencies are either qualified or adverse.
PI21	Effectiveness of internal audit	D+	Internal audit has not commenced in most MDAs
C(iii) Accounting, Recording and Reporting			
PI-22	Timeliness and regularity of accounts reconciliation	D	Un-reconciled discrepancy in BTR's NG book and bank balances amounting to Php5.65 billion and absence of complete/updated BRS. Overdue un-liquidated cash advances outstanding in every MDA per COA Annual Audit reports.
PI-23	Availability of information on resources received by service delivery units	D	Reporting on resource usage by service delivery units is not done.
PI-24	Quality and timeliness of in-year budget reports	D	Although there are a lot of reports required to be submitted by the line departments, these data are not consolidated by the DBM.
PI-25	Quality and timeliness of annual financial statements	D+	COA Annual Financial Report provides relatively complete information for national and local governments and GOCCs. The financial audit report for BTr-National Government books and line departments highlights problems with underlying data, however.
C(iv) External Scrutiny and Audit			
PI-26	Scope, nature and follow up of external audit	D+	<p>Quality financial audits are performed across Government. Reports are not formally submitted to the legislature. Many recommendations are not implemented.</p> <p><i>In line with its constitutional mandate, the Commission on Audit submits copies of audit reports to the executive and legislative branches of government. As provided in Item 11 of COA Memorandum No. 2002-047 dated August 13, 2002, the COA Chairman shall transmit the AAR to the following heads of oversight bodies:</i></p> <ol style="list-style-type: none"> <i>1. President of the Philippines</i> <i>2. Vice President of the Philippines</i> <i>3. President of the Senate</i> <i>4. Chairman, Senate Finance Committee</i> <i>5. Speaker of the House of Representatives</i> <i>6. Chairman, Appropriations Committee</i> <i>7. Secretary, Department of Budget and Management</i> <p><i>COA is also mandated under Section 8(c) of RA 8182 to report to Congress not later than June 30 of each year the result of audit on each ongoing and completed ODA project.</i></p>

PI-27	Legislative scrutiny of the annual budget law	C+	Procedures for congressional reviews of the executive's budget proposal are clearly established and generally respected. Although executive has consistently submitted its budget proposal, approval of the GAA was delayed or in some years was not passed.
PI-28	Legislative scrutiny of external audit reports	D	<p>There is no process in place for the legislature to systematically receive, scrutinize, and review audit reports and monitor the implementation of findings.</p> <p><i>In coordination with the Congressional Planning and Budget Department of the House of Representatives, beginning CY 2009, the COA has conducted audit briefing for the Office of the House Speaker particularly on issues that focus on the implementation of the Appropriation Laws, as follows:</i></p> <ol style="list-style-type: none"> 1. <i>Disbursements without appropriations cover</i> 2. <i>Unreleased appropriations</i> 3. <i>Realignment of funds</i> 4. <i>Accumulation of arrears</i> 5. <i>Unliquidated cash advances</i> 6. <i>Build-up of receivables</i> 7. <i>Low absorptive capacity of agencies</i> 8. <i>Utilisation of continuing appropriations.</i>
D. Donor Practices			
D-1	Predictability of Direct Budget Support	Not rated	Not applicable as direct budgetary support not in place during the years under review.
D-2	Financial information provided by donors for budgeting/reporting on project and program aid	D	Information tends to be provided on a project by project basis and forward estimates tend not be provided by donors.
D-3	Proportion of aid that is managed by use of national procedures	D	National procedures are used for local purchases but all ICBs are managed through bilateral or multilateral agency's procurement and procedures framework.

Source: World Bank 2007

Annex 4. Aide Memoire: PFM Design Mission

November 10

Disclaimer: the views expressed in this document are the draft findings of the mission team and are subject to confirmation with the Governments of the Philippines and Australia. The full analysis and context, program description and implementation arrangements will be provided in the design document.

Executive Summary

Improving public financial management (PFM)³³ is a key for the Philippines' progress towards its development goals. Strengthening PFM is also a shared priority of both the Government of the Philippines (GoP) and Australia (GoA). The Philippines' PFM systems could be considered a work in progress with functional capacity unevenly distributed over different components of the system. There is ample evidence that there is significant potential for efficiency and improvement, although lessons indicate gains will be hard won and gradual. Effective coordination of effort across the key Central Agencies is essential.

The mission team proposes to support a PFM Project Team in the strengthening of the PFM systems and practices of the Philippines Government. Core areas of engagement would be: (i) information and financial management systems (ii) internal controls strengthening; (iii) continued support to performance information (OPIF); (iv) cash management; and (v) support to the production of high quality, constructive and practical analysis on PFM, including civil society and academia. Key Government counterparts would be the PFM oversight bodies: Department of Budget Management (DBM), the Commission on Audit (CoA), Bureau of Treasury as well as key spending departments. The organization of the government Inter-Agency Committee on PFM currently underway would provide an ideal mechanism for consultation and would be a strong statement of intent by the Government towards the PFM improvement agenda. It is proposed that the technical assistance would run for an initial two years with the intention that if it is gaining traction it will develop into a long term relationship.

Background

The Government of the Philippines (GoP) has identified strengthening of PFM as a priority through various avenues, including the Medium Term Philippine Development Plan, annual Budget messages and various policy documents released by the Government oversight authorities such as the DBM and CoA. Reflecting the GoP's priority, the jointly agreed Australia-Philippines Development Assistance Strategy 2007-11 includes as an objective "Government agencies are better able to implement transparent and efficient budgets". In practice Australia has supported GoP PFM improvements through a number of mechanisms. The most recent and substantial of these has been the Partnership for Economic Governance Reforms (PEGR) which,

³³ The mission team is using the term public financial management for consistency but the program is focused on public expenditure management.

between 2005 and its completion in April 2010, will have invested approximately 600 million Pesos into PFM -related reform in the Philippines. Some PFM reforms of GoP supported by Australia include: establishment of a medium term expenditure framework; Organisational Performance Indicator Framework (OPIF); roll out of internal audit/internal control systems in key spending departments; and introduction of a performance audit methodology for CoA.

Mission Purpose

The purpose of the mission was to produce a draft design of a Program to deliver assistance to GoP's agenda to strengthen PFM in the Philippines. The goal of the new Program is to capitalise on areas of success from past engagement while expanding in assistance in areas that are increasingly apparent as emerging priorities. In particular reflecting the greater emphasis within oversight agencies that a greater focus is required on 'budget execution and budget accountability', i.e. improvements to systems, processes and accountability on the use of public funds. The abbreviated Terms of Reference for the mission are attached.

The mission consulted widely with Government Partners at both the oversight level and in spending departments. Also consulted were members of academia, civil society, the Senate and Congress Budget offices, Development Partners and experts in the field. A full list of partners consulted is attached and the team is grateful to all those who gave their time and technical inputs. The mission also drew on past analytical work such as the PEFA diagnostic, the IMF's Cash Management Mission Report and various reports produced by GoP, PEGR and other development partners.

Context

The strengths and weaknesses of Philippines' PFM systems has been well documented in a number of diagnostics. The mission wanted to build on that work by testing a few assumptions for the purpose of seeing where assistance is best targeted. A brief summary of these observations of the mission is provided below and will be fleshed out in the design document.

Improving PFM is a key for the Philippines' progress towards its development goals. The Philippines' PFM systems could be considered a work in progress with functional capacity unevenly distributed over generally fragmented components of PFM systems. Many of the procedures around financial use and reporting are basically sound. However, in practice procedures are often inconsistent between agencies and not fully documented. This means that while experienced senior staff understands how the system operates, this knowledge is not equally shared across the bureaucracy and application of process is reportedly not always consistent.

Similarly, financial use and reporting systems are often sound in isolation but do not always connect with each other. This means that the various actors in the systems lack reliable data, or have to go to great effort to find the data necessary to fulfil their mandate. For example, while the Government is able to track total disbursements from

the Treasury on a monthly basis, data on budget obligations by composition of spending based on approved appropriations components are not regularly available, precluding sound analysis of value for money.

The PFM systems of the Government in many procedures remain mainly manual and paper based, which limits the capacity of finance managers to produce timely and accurate data. Thus decision-makers do not always have reliable information to manage public finance adequately. Unfortunately it is also the case that in the absence of information, people inside and outside the Government can assume the worse, which erodes public trust in Government.

At a practical level, significant benefits could be gained with improved reporting through the computerization of manual Government financial processes. Some Government Departments are required to manage over a million paper documents a year to keep internal financial records. The administrative burden from huge amounts of manually recorded transactions is difficult to manage for even highly competent finance staff. CoA has a strong mandate to strengthen PFM systems in the Philippines, and has developed several tools that would allow greater automation of financial transactions. At the time of this mission, the roll out of these tools has been paused on the electronic New Government Accounting System (e-NGAS) or still in the beta phase (eBudget). Whatever electronic platform is chosen by the government, it is clear that considerable efficiency gains can be the pursuit of more accurate and timely reporting process. If full automation occurs it could release qualified staff from basic bookkeeping functions for use in higher value-adding roles. A stumbling block to automation is the fragmentation of the different systems currently in operation.

Discussion with Government partners of the history of PFM reform, such as the medium term expenditure frameworks, OPIF or the roll out of eNGAS signals that change requires a long period of incubation and progress is slow. The Philippines is hardly unique in this aspect; the pace of PFM reform is often frustrating in many developed and developing countries, although the status quo does appear particularly well entrenched in the Philippines. This means that fatigue can set in as reforms have been discussed for many years, but often the benefit from implementation has yet to be fully realized.

In an environment where change is slow, new reforms should be embarked on cautiously and the case may be made that implementation and improvement of existing systems is the best way forward, 'not letting the perfect get in the way of the good'. For a development partner this also means that our commitment needs to be long term and sensitive to the likelihood that the pace of change will likely be gradual rather than in leaps and bounds. Accepting that the end goal is far away and will require an even greater focus, it is important to go on strategic prioritization and sequencing in the PFM improvement Program to ensure the numerous incremental steps are leading towards long term sustainability.

Proposed Program

The design team is proposing:

A Program that supports the strengthening of the PFM systems and practices of the Philippines Government.

The Program would be a mechanism through which the key expenditure management, oversight and execution bodies could access high quality technical assistance and assistance on core PFM issues. Recognising the highly specialised and technical nature of PFM and that for a program of limited size needs to develop a core area of expertise, the Program will specialise on a number of components. It is proposed that the Program has five key areas of focus:

- Information and financial management systems both at the oversight level and for the implementation in key line departments;
- Internal controls system-strengthening in spending departments;
- Continued support to performance information agenda (OPIF), to make it more functional for planning and budgeting purposes;
- Cash management and programming; and
- Support to the production of high quality, practical and constructive analytical work on PFM issues, including work by civil society and academia.

The first stage of assistance in these areas will be developed further in the design and with program implementation. The type of assistance offered could include: diagnostics around key aspects of the PFM systems, for example system, such as cash allocation policies or key financial management systems; long term or short term technical assistance to help in the implementation of programs from both local and international advisors; and the production of regular ‘hot topic’ papers that inform the internal policy debate within Government; and finally, support to the ‘demand side of Governance’ through academia and civil society that can work constructively with the bureaucracy and/or the legislature to encourage well informed and rigorous debate on PFM issues.

It is proposed that AusAID will make an initial two-year commitment towards the Program. Subject to Government approval from both the Philippines and Australia, AusAID could initially commit grant financing of up to approximately 400 million Pesos for an initial two years of the Program between 2010 and 2012. In the early stages of the Program, some clear indicators will be set to measure progressive success over the short term. At the end of the two-year period, a Program review will take place of the Program and the GoP and the Australian Government will decide whether the Program will continue for a further two years.

The Program design is taking place in the election period and as a natural part of the democratic cycle there is some uncertainty in the GoP’s policy agenda. If post-election

the Government were to adopt a comprehensive PFM improvement agenda as a key priority then the absorptive capacity for effective utilization of funds would increase. Ideally, the engagement between GoP and AusAID will be long term partnership that reflects that timeline for major evolution in PFM can sometimes be measured in decades rather than years. As partners in a mature relationship, it is hoped that the Governments of Australia and the Philippines can have a robust and open debate about the best way to strengthen PFM systems. This may sometimes involve agreeing to disagree, but as long as the lines of communication are open and honest then a robust dialogue will benefit all partners.

Consultation

In line with Paris Declaration Principals consultation with Government oversight will ideally be provided by the relevant technical committees of the Government. Subject to GoP agreement, the proposed key Government Counterparts of the Program would be the key agencies involved in expenditure management and reporting: DBM, Commission on Audit, Bureau of Treasury and selected large expenditure departments. If government pushes through with the signing of the Memorandum of Agreement that will formalize the creation of an interagency PFM Interagency Committee, that would be an ideal vehicle for providing strategic direction towards the proposed AusAID Program. To achieve oversight while avoiding zero sum games across different activities, it is proposed that the Program will have:

- a clearly defined list of core engagement areas;
- a governance mechanism that selects and funds concepts on merit; and
- a budget framework that is flexible depending on the strength of progress of the activities that can be programmed each year as a rolling design.

It was expressed by key recipients of AusAID assistance that they appreciated the close consultation at the meaningful points of strategic formulation, progress and output of technical assistance. However, due to their heavy work burden of their regular jobs in busy oversight departments within Government they were grateful that historically AusAID in the past has not required them to administer the day -to -day operation of the technical assistance. It is therefore proposed the Program continues this practice.

It is the belief of the design team that AusAID has the potential to develop a core competitive advantage in delivering some aspects of PFM assistance. However the scope of PFM issues that GoP deals with is far beyond the capacity of a single bilateral donor to engage in successfully conceptually and financially. For example, support to 'hard' infrastructure such as the physical infrastructure of departments or software licences is beyond the financial scope of AusAID's ability to support. Similarly there are many thematic areas, such as revenue, sub -national governments, Government Corporation Oversight and debt management that are outside the reasonable area of focus of this Program.

Other Development Partners

Strong links have already been built with development partners through the shared roll out of core government programs such as OPIF and Internal, internal audit and controls and the production of analytical products. In line with Paris/Accra principles and to reduce the management burden of Government, AusAID would to continue to explore opportunities for collaboration with other Development Partners that are highly active in the field, including both the Development Banks and other bilateral donors. One of the primary mechanisms for doing this could be the Governance sub-working group of the Philippines' Development Forum.

During design consultations, both development banks indicated their willingness to fund larger scale PFM systemic improvements, as needed by GoP. The capacity to extend donor assistance funding into government-wide initiatives is an important back-stop to the initial consensus building and analytical work of the PFM Resource Centre.

Where the relevant GoP technical committee endorses a larger scale PFM activity for funding, this initiative can be carried into the Philippines' Development Forum to mobilise the needed resources through donor assistance channels.

Annex 5. Consultation List

During the design mission the Design Team met with the following officials from GOP, donor agencies, civil society organisations, and PEGR management and consultants:

Government of Philippines

Bureau of the Treasury (BTr)

National Treasurer Roberto Tan
Deputy Treasurer Christine Sanchez
Deputy Treasurer Gisela Lood

Commission on Audit (COA)

Assistant Commissioner Arcadio Cuenco, Jr.
Assistant Commissioner Carmela Perez
Assistant Commissioner Emma Espina
Assistant Commissioner Gloria Cornejo

Congressional Planning and Budget Office (CPBO)

Director General Rodolfo Vicera
Executive Director Romulo Miral
Director Novel Bangsal
Director Dina Pasaqui
Ms Pamela Diaz Manalo
Ms Elsie Gutierrez

Department of Budget and Management (DBM)

Secretary Rolando Andaya, Jr.
Undersecretary Laura Pascua
Undersecretary Evelyn Guerrero
Director Nora Oliveros
Director Amelita Castillo
Director Tina Canda
Ms Tessie Gregorio

Department of Education (DepEd)

Undersecretary Jesus Galvan
Assistant Secretary Jesus Mateo

Department of Finance (DOF)

Undersecretary Gil Beltran
Director Joji Cruz

Department of Health (DOH)

Undersecretary Lydia Fernandez
Mr Laureano Cruz
Ms Ma. Carolina Taiño
Ms Ma. Vida Gomez

Department of Public Works and Highways (DPWH)

Director Aristeo Reyes
Ms Marie Palafox
Ms Marciana Herrera

Department of Social Welfare and Development (DSWD)

Assistant Secretary Mateo Montaña
Assistant Secretary Florita Villar
Director Desiree Fajardo
Ms Victoria Navida

National Economic and Development Authority (NEDA)

Deputy Director General Rolando Tungpalan
Director Jonathan Uy
Director Jocelyn Reyes
OIC Assistant Director Myrna Clara Asuncion
Ms Ameta Benjamin
Ms Jenneth Taja
Mr Reno Joseph Cantre

Office of the President (OP)

Deputy Executive Secretary Alberto Bernardo

Senate Legislative Budget Reporting and Monitoring Office

Director Yolanda Dublon

Donor Agencies**Asian Development Bank (ADB)**

Ms Claudia Buentjen
Mr Kelly Bird
Ms Heidi Mendoza

European Union

Mr Nick Taylor
Ms Anja Bauer
Ms Rita Bustamante
Dr Mitch Majini
Mr Jeff Byrne

International Monetary Fund (IMF)

Resident Representative Dennis Botman

United States Agency for International Development (USAID)

Mr Tyler Holt
Ms Ria Orca

World Bank

Ms Marysse Gautier
Mr Matthew James Keir Stephens
Ms Preselyn Abella
Mr Eric Le Borgne

Civil Society Organisations

Procurement Watch – Mr Amador Astudillo and Ms Ma. Caroline Belisario
Makati Business Club – Executive Director Alberto Lim
Transparency and Accountability Network (TAN) – Executive Director Vincent Lazatin
University of the Philippines National College of Public Administration & Government - Dean Alex Brillantes
De La Salle University School of Government – Dean Francisco Magno

The Asia Foundation – Dr Steven Rood

PEGR Management and Consultants

Mr Ian Porter

Ms Susan Bulan

Mr Joel Lasam

Mr Ronnie Tamangan

Ms Corazon Jose

Ms Teresita Pascual

Mr Ephrem Cortes

Dr Ed Gonzales, Advisory and Quality Assurance Group (AQAG)

Mr Jun Miral, AQAG

Mr Vir Ignacio, AQAG

Ms Rebecca Sarmenta, AQAG

Mr Bill Cox, Team Leader, Reform Agenda (RA) on Contingent Liabilities Management

Ms Helen Martin, Member, RA on Contingent Liabilities Management

Mr Ian Collins, Team Leader, RA on OPIF

Mr Peter Fane, International Expert, RA on PFM/OPIF

Ms Thuy Mellor, Team Leader, RA on Strengthening DepEd Internal Control System/Internal Audit (ICS/IA)

Mr Mike Cleary, Team Leader, RA on Strengthening DPWH FM

Mr Rafino Malgapo, Team Leader, RA on Strengthening DPWH ICS/IA

Ms Nelia Villeza, Member, RA on Strengthening GOP ICS

Annex 6. Terms of Reference for Key Personnel

Team Leader

The Team Leader will have overall responsibility for programming and program implementation and will provide a mix of strategic, technical and managerial input to the program. The Team Leader will engage in high-level liaison between Australia, the GOP, development partners and civil society to shape a program in support of the GOP's PFM reform agenda. It is vital that Australia presents a consistent policy position throughout this on-going dialogue, and that this message is delivered by an individual with clear authority to make that representation. For this reason it is proposed the Team Leader be an AusAID officer from the Manila Country Office.

The Team Leader will report to the AusAID Minister Counsellor and to the Counsellor Economic Growth on a day-to-day basis. The Team Leader will be co-located in AusAID's Country Office and the Program Office to facilitate a close working relationship with the Program Coordinator, Program Manager and Technical Advisory Team.

Key responsibilities:

- provide strategic guidance and advice on PFM reform issues to AusAID and the GOP, particularly as they relate to the implementation of the PFMP;
- work closely with program stakeholders to prepare the Annual Action Plan and enable coherence of program priorities and activities with the GOP;
- enable coordination and coherence of PFM reform priorities and activities with other relevant AusAID programs and development partners;
- report on program performance in collaboration with the Program Coordinator, M&E Specialist and Program Manager;
- provide technical inputs, particularly related to evaluation of proposals and quality assurance of program outputs;
- manage key program personnel including the Program Coordinator, Program Manager and Technical Advisory Team;
- establish professional networks and relationships across domestic and international organisations involved in PFM strengthening and economic development;
- operate in accordance with the principles of aid effectiveness, including using and supporting GOP systems; and
- work in a way that promotes gender equality and principles of good governance.

Skills, knowledge and experience:

- understanding of the role and functions of PFM in a modern democracy;
- ability to provide high quality advice and strategic guidance on PFM reform issues in a developing country context;
- experience with developing country PFM systems and organisations to manage and implement public resources to deliver services;
- program management experience and ability to manage diverse forms of support and personnel from varied professional and cultural backgrounds;
- training in and exposure to a broad range of PFM and/or economic development issues;
- knowledge and experience of development assistance programs and ability to apply the principles of aid effectiveness;
- strong interpersonal and communication skills, including the ability to convey concepts clearly and to understand and meet the needs of a range of stakeholders; and
- understanding and commitment to principles of gender equality and good governance.

Program Coordinator

The Program Coordinator will support the Team Leader in programming and program implementation in collaboration with the GOP, development partners and civil society. The Program Coordinator will be an AusAID officer at the Manila Country Office and is likely to be a locally engaged officer with a background in whole-of-government PFM issues. This role will provide back-up for the Team Leader when he/she is absent. The Program Coordinator will be located AusAID's Country Office and will report to the Team Leader.

Key responsibilities:

- support programming and program implementation, including liaison with the GOP, development partners and civil society;
- work closely with other relevant AusAID programs and development partners to enable coordination and coherence of PFM reform priorities and activities;
- work closely with the Team Leader, M&E Specialist and Program Manager to support program reporting and monitoring;

- provide technical inputs, particularly related to screening of proposals and quality assurance of program outputs;
- manage performance of the Service Provider in accordance with contractual arrangements;
- manage AusAID's internal activity management process;
- enable professional networks and relationships with organisations involved in PFM strengthening and economic development in the Philippines; and
- promote gender equality and principles of good governance.

Skills, knowledge and experience:

- experience with PFM systems and organisations in the Philippines to manage and implement public resources to deliver services;
- program management (including contract management) experience and ability to manage diverse forms of support and personnel from varied professional and cultural backgrounds;
- knowledge and experience of development assistance programs and ability to apply the principles of aid effectiveness;
- understanding of the range of capacity development approaches and their applicability to different contexts and needs;
- strong interpersonal and communication skills, including the ability to understand and meet the needs of a range of stakeholders; and
- understanding and commitment to principles of gender equality and good governance.

Program Manager

The Program Manager is responsible for the administration of the program and for managing the Program Office in support of the programming decisions taken by AusAID and the GOP. The Program Manager will be under contract with, and be accountable to, the Service Provider, while also supporting the Team Leader/Program Coordinator on a day-to-day basis. The Program Manager is a full-time position based in the Program Office.

Key responsibilities:

- work closely with the Team Leader/Program Coordinator and the GOP to provide timely, high quality and value-for-money assistance through the program;

- provide advice and guidance on operational issues in the implementation of the program, including managing risk;
- manage and report on program funding, and oversee the disbursement of program funds in accordance with agreed procedures;
- ensure the quality and timeliness of implementation reporting by contracted inputs;
- maintain constructive working relationships with the Team Leader/Program Coordinator and the GOP;
- establish and provide quality control for all plans, reports, systems, outputs and contract management;
- manage all advisory placements, including initial induction and orientation, ongoing support and training, trouble shooting, and counselling for performance;
- manage a communication and information strategy to collate and disseminate appropriate information between and across key partners and stakeholders; and

Skills, knowledge and experience:

- program management experience including the leadership of a large program comprising diverse forms of support and personnel from varied professional and cultural backgrounds;
- knowledge and experience of development assistance programs and ability to apply the principles of aid effectiveness;
- understanding of the range of capacity development approaches and their applicability to different contexts and needs;
- counselling, mediation and problem solving experience in complex environments;
- high level interpersonal, communication and cross-cultural skills, including the ability to understand and meet the needs of a range of stakeholders; and
- understanding and commitment to gender equity in human resource practices.

M&E Specialist

The M&E Specialist will support both governments' increasing commitment to managing for development results and greater performance orientation, while also investing in opportunities for learning and incorporating qualitative techniques to capture the depth and breadth of change programs. The M&E Specialist will enable M&E methodologies and strategies to be consistent across the program. This is a full-

time position based in the Program Office and forms part of the Technical Advisory Team.

Key responsibilities:

- ensure the M&E Framework is appropriately managed, updated and implemented as per the Design;
- develop and update the methodology for measuring program performance and progress towards achieving objectives and outcomes;
- coordinate the collection of all evidence on the impact of the program with information about other GOP, AusAID and donor programs also operating in PFM reform;
- support the Team Leader/Program Coordinator with all monitoring, evaluation and reporting activities;
- provide targeted and agreed technical support to the GOP, such as management and implementation of issues-based evaluation studies, and monitoring of the government's PFM reform program if requested;
- enable the program to meet all AusAID and GOP reporting requirements; and
- ensure M&E strategies and opportunities enhance gender equity outcomes within the overall context of the program.

Skills, knowledge and experience:

- experience and understanding of contemporary M&E strategies and systems;
- strong understanding and/or experience of the M&E needs of partner government agencies in a development context;
- high level interpersonal, communication and cross-cultural skills, including the ability to convey concepts clearly and to understand and meet the needs of a range of stakeholders; and
- commitment to gender equity within an M&E context.