

## CHAPTER V. DEVELOPING AN ACTION PLAN: RECOMMENDATIONS FOR ACHIEVING FISCAL SUSTAINABILITY AND IMPROVING BUDGETARY MANAGEMENT IN BELARUS.

5.1 The previous chapters have focused on key issues that underpin an effective budgetary process: fiscal discipline and sustainability; effective allocation of resources and the technical efficiency of the budget process. In each area, Belarus has made important progress and strides, but in each area there are important steps that need to be taken that could significantly improve the use of public resources.

5.2 Yet managing change and improvement in fiscal and public expenditure management is a complex process that takes years to undertake. Indeed, the strongest of systems are always in the process of trying to improve themselves. This requires policymakers that are committed to the goals of improved budgetary practices. It also requires developing a strategy and managing the change properly. The starting point of developing a strategy is to identify the objectives that one seeks to achieve. The second step is to carry out a comprehensive and candid assessment of the strengths and weaknesses of the system currently in place. The previous chapters have attempted to begin this assessment.

5.3 Once the key measures have been identified, a phased action plan can be developed. Such an action plan should include the following elements<sup>1</sup>:

- The overall goal of the reforms and the specific objective of each component;
- A list of components;
- A list of activities for preparing and implementing the reforms; the deadlines for completing these activities and the milestones for accomplishing key tasks;
- Indicators to monitor the progress achieved;
- The organizational arrangements to prepare changes and supervise implementation; and some notion of the resources that will be devoted to the reform in order to obtain the required inputs.

5.4 As important to achieving success, however, is building a commitment to improving the use of public resources, both within and outside of the government. Changes will take hold only if there are champions within the government. The top management of the Ministry of Finance must be actively engaged in the process and efforts should be centered in the Ministry of Finance. To design and implement the reforms, the Ministry of Finance should work in close cooperation with line ministries, subnational governments and other key players.

5.5 Effective organizational arrangements are also necessary to implement change. Given the important and wide ranging nature of issues related to public expenditure reforms, three levels of participants are needed:

- A *Steering Group*, which consists of high level officials that provide general direction to the program of change. Typically the steering group is chaired by the Ministry of Finance. It is also important to include in the Steering Group the heads of key department in the Ministry

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<sup>1</sup> This and what follows draws on Allen and Tommasi (2001) *Managing Public Expenditure – A Reference Book for Transition Economies*. OECD.

of Finance and representatives of ministries and government agencies participating in the reforms. One of the aims of this group is to establish a consensus on the key objectives that need to be addressed.

- A *Core Unit* that is made responsible for overall management of the program of activities. This unit is most appropriately located within the Ministry of Finance and needs to have a very clear vision as to the goals and objectives to be reached. It also be given the authority to spread new practices or approaches through seminars, workshops and training activities.
- *Working groups* should be created to develop and help implement specific reforms in particular areas. These groups often undertake the detailed day-today work of developing and implementing needed changes.

Such groups will be needed to fully develop the needed changes, but also to develop a communication strategy and to assure that the proposed changes have full ownership of the Belarusian government and people.

5.6 On the basis of the analysis of the previous chapters, this final section of the report outlines suggested primary directions for economic policy in the short and medium term. We hope that these recommendations may prove useful to the Government in the elaboration of an Action Plan for improving public resource management. This Action Plan should specify concrete steps for the short and medium term, together with the agency most likely responsible, and indicators for measuring performance in reaching the given objectives. ..

5.7 But before moving to the recommendations, it is important to reiterate, what this study sees as the keys goals to be achieved for an effective budget system:

- *Maintaining Aggregate Fiscal Discipline.* Assuring that the country lives within its means is a fundamental objective for healthy budget management. In order to maintain its growth and competitiveness, Belarus must reduce the extent of explicit and implicit fiscal activities. This can start by identifying expenditures that can be cut in the short term and including the complicated array of extrabudgetary and quasi-fiscal activities into budget analysis.
- *Allocating resources to effectively meet government priorities.* Effective allocation of the Government's resources implies that specific outcomes in line with government priorities are attained. These outcomes must go beyond the financial fulfillment of an expenditure plan. They must include the actual results of service delivery ( in the form of meeting sectoral objectives). The government must seek to create a better connection between public expenditures and state objectives.
- *Promoting the efficient use of resources through sound budget processes.* The rules by which resources are allocated, distributed, monitored, evaluated and audited play a critical role in assuring that resources are being well-used. The best methods of allocation may be undermined by weak budget rules and budget management practices. In Belarus, budgetary preparation and approval lacks focus and realism and the implementation of the budget allows for too much discretion in the allocation and re-allocation of state expenditures.

5.8 For effective budget management, all of these objective must be developed over time. To focus on one aspect, while ignoring the others, is unlikely to lead to success. In this sense, efforts to improve the system must be comprehensive, so that all the complementary pieces for the system to work well are in place. In what follows, “short run” is to be interpreted as a period of 1-2 years, while medium term covers 3-4 years..

**I) The imperative of tax and expenditure reduction:**

- The size of government in Belarus is too large for the economy to meet the challenge of growing competition on world markets from producers in Russia and many other countries. While the explicit general government budget is roughly 10 per cent more of GDP than in Russia, for example, accounting for significant off-budgetary and quasi-fiscal expenditures would make this differential substantially higher. A significant overall reduction of the tax burden on Belarusian firms is needed, together with a program for achieving comparable reductions in state expenditures.

**II) Measures aimed at achieving overall financial stability and discipline.**

**a) Increase the sphere of the budget to include significant expenditures that are currently off budget or quasi-fiscal.**

- For the short term: Incorporate Innovation Funds into the budget with full separate classifications for current and capital expenditures. Introduce full accounting for all remaining off-budgetary sources of state finance, including own funds of ministries. Cease directed commercial credits and other political pressures on commercial banks to make loans or hold government debt. Continue reducing subsidies and cross-subsidies in energy, supplemented by budgetary support for poorer families. Take inventory of all other remaining quasi-fiscal sources of finance.
- For the medium term: Incorporate all extrabudgetary funds other than the Social Protection Fund into the government budget. Continue reducing quasi-fiscal sources of finance according to established benchmarks.

**b) Calculate and reduce risks associated with contingent liabilities.**

- For the short and medium term: Identify the most important contingent liabilities for the government budget. Given an account of these liabilities in the state budget, develop facilities to monitor contingent liabilities effectively and calculate the corresponding risks. Develop a strategy for controlling and reducing risks from government guarantees and other contingent liabilities.

**c) Eliminate individual tax exemptions. Reduce sharply other tax exemptions.**

- For the short term: Identify and evaluate existing tax exemptions. Eliminate tax exemptions granted on an individual basis. Develop a strategy to reduce remaining tax exemptions according to explicit targets.

- For the medium term: Achieve reduction in the amount of granted tax exemptions according to explicit targets.

**d) Improve and tighten conditions for financing the government budget deficit.**

- For the short term: Cease direct National Bank finance of the budget deficit. Establish conditions for placing state securities on the basis of transparent competitive auctions. Fulfill all state debt obligations according to contract (no unilateral restructuring or rollovers).
- For the medium term: Uphold commitment to these practices.

**e) Rationalize utility pricing**

- For the short and medium term: Continue the program for reducing indirect subsidies and cross-subsidies, while introducing a transparent methodology that relates utility prices to long-run marginal costs. Develop parallel program to compensate poorer households directly from the budget.

**f) The creation of an effective and sustainable pension system**

- For the short term: Identify the primary risks in the pension system. Cease the funding of non-pension or insurance-related expenditures from the Social Protection Fund. Increase minimum pension age. Consider reform options to ensure effectiveness and sustainability of the pension system.
- For the medium term: Accelerate preparation of the pension reform.

**g) Improve cooperation between the Ministry of Finance and the Central Bank.**

- Promote a greater sharing of economic information, data, perspectives, and projections. Create joint committees for the examination of questions pertaining to macroeconomic policy of concern to both the National Bank and the Ministry of Finance (Government debt and guarantees, for example).

**III) Measures aimed at strengthening the link between government objectives and expenditures.**

**a) Develop effective methodology for regulating wages in the state sector.**

- For the short and medium-term: Work out an effective methodology for regulating and restraining wage growth in the state sector in a manner consistent with state objectives and the imperative of reducing state expenditures.

**b) Develop sector strategies to link budgetary expenditures with state objectives.**

- For the short-term: Work out strategies in various sectors that assess and modify existing programs and expenditures with the underlying goal of achieving specific government objectives. Introduce a more ambitious strategy, including a sector envelope approach to budgeting, in a pilot sector.
- For the medium-term: Continue to develop and expand sector strategies. Spread the practice of envelopes to other sectors.

**c) Improve practices of state-financed fixed capital investment.**

- For the short term: Develop clear criteria for the cost-benefit evaluation of investment projects. Take inventory of existing investment projects and their degree of completion with the goal of eliminating ineffective or non-financed programs. Clarify a proper division of capital and current expenditures in the budget.
- For the medium term: A full scale implementation of the new approach to capital expenditure budgeting.

**d) Take full inventory of state subsidies to the productive sector and ensure their steady reduction.**

- For the short term: Take inventory of the quantities of various direct and indirect subsidies given to producers, and develop a strategy to reduce subsidies over time according to well-defined benchmarks.
- For the medium term: Realize the subsidy reduction program according to given benchmarks.

**e) Limit the use of protected items in the budget.**

- For the short and medium term: Evaluate the opportunity costs associated with protected items in the budget and develop a strategy for their reduction, along with the introduction of a more comprehensive system of financial planning and commitment control.

**f) Improve budgetary preparation**

- For the short and medium term: Base budgetary preparation on more realistic and consistent economic projections. Develop increased capacity for such forecasting. Review the role of budgetary organizations in budgetary preparation, with a view toward greater decentralization and accountability.

**IV) Measures aimed at increasing efficiency in the use of budgetary resources.**

**a) Improve the legal and normative base for budgetary preparation and execution.**

- For the short-term: Strengthen the legal foundation of the planned budget by requiring the approval of Parliament for substantial revisions. Draft and submit the Budget Code to Parliament.
- For the medium-term: Implementation of the Budget Code. Realize a greater commitment to upholding the planned budget.

**b) Increase the scope and effectiveness of the state treasury.**

- For the short-term: Develop a program for the expansion of the state treasury to include all ministerial revenues, funds, and accounts, including those of the power ministries. Develop a system of short-term forecasting for more effective cash management and commitment control.
- For the medium-term: Realize the expansion of the treasury and more effective cash management and commitment control according to explicit targets.

**c) Internal and external monitoring and control.**

- For the short term: Demarcate responsibilities for internal controls between the SCC and Ministry of Finance in a clear and precise fashion. Begin plans for introducing performance-based audits. Prepare for creation of an external auditing agency.

For the medium term: Begin introducing performance-based audits. Progress in the creation of an external audit