PER Annual Progress Report

In 2014, the Public Expenditure Review (PER) process has continued to produce useful outputs which are used to improve fiscal policy formulation and management. Four studies were approved for implementation in 2014. These include the following topics: Contingent Liabilities, Government Pension Obligations and Contingent Liabilities, Prevention and Management of Payment Arrears and an Assessment of Non-Tax Revenue Potential in Tanzania. There were also two ongoing studies which were approved in 2013; these are the Public Investment Management Operational Manual and the Public-Private-Partnership (PPP) study. This note provides a short update on each of the studies. It will also provide updates on the implementation of the recommendations for the studies completed in 2013. All studies include an inception meeting and a technical meeting.

Tax Exemptions Study

**Status: Completed in October 2013, Action Plan Drafted in February 2014**

The report examines the tax exemptions provided in Tanzania and analyses the effectiveness and efficiency of the exemptions issued over the last decade. The study’s empirical evidence shows that offering tax exemptions to corporations has no significant impact on attracting investments. Based on international best practice, it was suggested to minimize unnecessary losses of revenue resulting from the application of tax exemptions and proposes reforms to increase tax revenue. An action plan for implementation of the study findings has been developed and additional work to assess the cost and benefit of tax exemptions in Tanzania has been completed. Many of the recommendations for reducing tax exemptions have been adopted in the recent 2014/15 budget speech by the Minister for Finance. Other recommendations have been implemented through the VAT Act. enacted by Parliament in November, 2014. Moreover, tax exemptions granted from January, 2010 to September, 2014 have been uploaded on the MoF website in order to improve transparency. Steps will be taken to ensure that tax exemptions are uploaded on the MoF website quarterly.

**Next steps:**

- Final version of the tax exemptions action plan is circulated to the PER Champions.

National Agriculture Input Voucher Scheme

**Status: Completed in March 2014, Action Plan Drafted in September 2014**

The study on the National Agriculture Input Voucher Scheme assessed the performance of the agricultural National Inputs Voucher Scheme (NAIVS) and looked at how the program contributed to increased production, productivity and profitability of the Tanzanian farming/agriculture and the sustainability of these investments. The report concludes that on average the NAIVS program has offered a positive return on investment for the average maize producer in some of the regions where data were
collected but the returns to the rice subsidy are more variable and lower. Further, the report revealed that the returns are still little based on domestic farm gate prices for grain surplus households. NAIVS has contributed to some degree to improving the adoption of improved seed and fertilizer, based on continuing purchases after graduation. The report also highlighted a number of implementation challenges including delays in printing and distributing vouchers, delays in delivery of inputs, delays in payment of suppliers and misallocation of about 1% of vouchers. An action plan for implementation of the study findings has been developed. As part of implementation of the findings, the Government has decided to replace the NAIVS with an agricultural credit mechanism.

**Next steps:**

- Final version of the NAIVS action plan is circulated to the PER Champions.

**Fiscal Inequities Study**

**Status: Completed in April 2014, Action Plan Drafted in September 2014**

The key objective of the fiscal inequities study was to analyse progress, achievements and challenges of the current strategies for addressing inequalities of recurrent grant allocations across LGAs. The findings of the report suggest that, LGA financing is characterised by an increasing wage share and reduced operational funding. The patterns of inequality and inequity between LGAs have remained very significant over the last 6 year period. They are driven by PE allocation across sectors, particularly education and health. There also exists substantial fiscal inequity within LGAs, often more than inequity between LGAs. The study suggests that shifting incremental resources to the worst served areas is likely to improve service delivery. Furthermore, better management of staff inputs within LGAs could also lead to significant improvements in service delivery. Well-targeted incentive schemes were also recommended as alternative options that can make a substantial difference to local service delivery. An action plan for implementation of the study findings has been developed.

**Next steps:**

- Final version of the NAIVS action plan is circulated to the PER Champions

**Prevention and Management of Payment Arrears**

**Status: Completed in November 2014**

The arrears study aims to find solutions to avoid accumulation of payment arrears in order to improve the credibility of budget execution. Regular reporting by the Accountant General’s Department suggest the scale of government arrears to have increased from TSh. 485 billion to TSh. 1,301 billion (i.e. from 1.4% to 2.3% of GDP) over the period since December 2010. The report suggests that, deterioration in compliance to financial rules and regulations, budget discipline and lack of effective
enforcement have contributed to or failed to prevent the accumulation of payment arrears exist at each stage in the budget cycle. The report recommended various measures to be adopted by the Government to clear the existing stock of arrears and prevent their re-occurrence. Some of the recommended measures include: Government to issue an updated guideline on the definition and reporting of payment arrears and provide associated training; update and disseminate the financial regulations and other instructional materials to support the revised legal framework; improve revenue forecasting capacity and expand the role of the independent assessment of revenue forecasts; and to prepare and publish arrears clearance strategy and timeframe. In response to the consultant’s recommendations, the Government has prepared a strategy for clearance and prevention of arrears.

**Next steps:**
- Arrears action plan is drafted.
- Strategy on arrears and contingent liabilities is shared with PER Champions.

**Public Investment Management Operational Manual**

**Status: Completed in February 2015**

The Public Investment Management Operational Manual was finalized in February 2015. The key purpose of the manual is to provide strategic guidance on the selection of projects and development of project proposals for financing at the central and local government levels. The manual will serve as a capacity strengthening tool and reference for government officials on standard procedures and methods for project appraisal. The budget guidelines for 2015/16 ask for officials to use the manual for all new projects. The manual will be shared with a wide range of stakeholders both in hard and soft copies.

**Next steps:**
- PIM manual training is completed in 2015.

**Contingent Liabilities**

**Status: Completed in December 2014**

This study looks at the management of contingent liabilities in Tanzania, an essential component of fiscal risk management. The study identified and estimated contingent liabilities in different categories; one-off guarantees, standardized guarantees, pension guarantees, PPP guarantees, litigations and on-lending that includes credit risks (the final borrower is responsible for repaying the loan). The total contingent liabilities (explicit) with on-lending (credit risk) was estimated to be TSh. 9,333 billion, comprising Pension arrears and actuarial deficit to PSPF (TSh. 4,800 billion), One-off and standardized guarantees (TSh. 2,116 billion), Litigations (TSh. 1,855 billion) and On-lending with credit risk (TSh. 562 billion). The report provides a series of recommendations. These include: the need to set a properly defined debt limit and
prepare guidelines and procedures based on a credit rating methodology for the issuance of guarantees; disclosure and reporting of guarantees should adhere to relevant IPSAS and IFRS standards and the verified debt from transformation of provident funds to pension funds, which have immediate implication to the government’s fiscal policy, to be restructured into long term maturities and acknowledged through Consolidated Financial Statement.

Next steps:
- Contingent liabilities action plan is drafted.
- Strategy on arrears and contingent liabilities is shared with PER Champions.

**Government Pension Obligations and Contingent Liabilities**

**Status: Completed in February, 2015**

This study looks at the pension system in Tanzania and aims to assess its sustainability. The study revealed that the Government pension liabilities consist of two streams – obligations to repay the PSPF for pre-1999 benefit payments made on its behalf and contingent liabilities of all funds whereby government would make benefit payments should the funds not be in a position to do so. Further, the report suggested that, if the pensions new harmonization rules are applied in full the Government contingent pension liabilities is estimated to TSh. 12.0 trillion. PSPF is the main liability both in the short and the long term. To secure the financial position of the PSPF will require both a reduction in outstanding liabilities and increased payments from the Government. A merger of funds would reduce government contingent pension liabilities in future and should allow for efficiency gains. A further option is to reduce Government pension liabilities going forward by gradually increasing the retirement age. The Government has prepared a strategy for clearing pensions’ liabilities especially the pre 1999 PSPF liabilities.

Next steps:
- Pensions action plan is drafted.
- Strategy on pensions is submitted to Cabinet.

**Rapid Budget Analysis**

**Status: Completed in February 2015**

The RBA exercise is carried out on an annual basis. The overall objective of the RBA is to review actual and budgeted expenditure patterns to inform strategic resource allocation and thereby make recommendations to accelerate economic growth and poverty reduction.

Between 2012/13 and 2013/14, the Tanzanian Government was able to reduce the fiscal deficit from 5 to 3.3 percent of GDP, and so stabilize the level of public debt to around 32 percent of GDP. Those positive developments were welcomed after the fiscal
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slippage observed in 2012/13 and the rapid increase in the public debt level over the past few years.

However, this fiscal consolidation, while commendable, was achieved at some costs, including the accumulation of arrears and significant expenditure cuts in the range of 2.5 percent of GDP during the year. At end June 2014, the level of arrears accumulated by the Government with contractors and pension funds was approximately six percent of GDP. While public spending was cut across the board, the implementation of the development budget suffered most, with an execution rate of only 62 percent. As a result, public spending on development was only 4.8 percent of GDP, the lowest level in the last five years, and in sharp contradiction with the objectives stated in the recent Big Results Now initiative. Expenditure cuts also impacted on LGA’s capacity to deliver social services, particularly in the health and education sectors. The fundamental reason behind those cuts was the over-optimistic revenue projections adopted by the Government in the approved budget, which forced the authorities to reduce their spending even though their tax performance was slightly better in 2013/14 than in 2012/13.

For 2014/15, the Government has projected a fiscal deficit of around 3.7 percent of GDP, in line with the IMF program. This target assumes an improvement in revenue collection, up by 0.5 percent of GDP, and controlled public expenditures. The authorities are also planning a shift from current to development expenditures, in the range of 1.5 percent of GDP, to support the rapid implementation of the BRN initiative and other national development strategies.

During the first semester of 2014/15, the implementation of the budget faced significant challenges. The first challenge, not new, was that revenue targets were missed again by about 10 percent, notably in VAT and income tax collection. This financing gap was exacerbated by the slow disbursement of external aid, notably budget support in the context of the IPTL scandal, even though it was partly compensated by increased commercial borrowing on the domestic and international markets. The second challenge remained the high level of arrears, which compromises the relationship between the Government and its contractors as well as the financial stability of the pension system. The Government, being aware of those challenges, has initiated some actions, which should be implemented with a sense of urgency, including:

• Improve revenue collection, notably through the implementation of the recently approved VAT Act and the Tax Administration Act as well as further efforts in reducing the use of tax exemptions.
• Address properly the IPTL corruption scandal to restore budget support and reduce the reliance on commercial borrowing.
• Develop and implement an action plan to address and eliminate the level of arrears accumulated with contractors, notably in the transport sector.
• Adopt reforms in the pension system to address the level of arrears accumulated with pension funds and limit the Government’s future financial obligations.

These actions are necessary to increase the level of public revenues and restore the confidence with private contractors as well as with pension funds in both the short and medium terms. Their implementation will also guide how much the authorities will have to adjust their expenditures during the rest of the fiscal year, which might difficult in the context of the forthcoming General Elections, so that they can meet their fiscal target of 3.7 percent of GDP at the end of 2014/15. These actions are also important in view of the rapid increase in the public debt service (excluding amortization of domestic debt), which is projected to absorb approximately 12 percent of total domestic revenues in 2014/15 against only seven percent in 2011/12. While Tanzania’s debt distress remains low, this last figure emphasizes the need for the Government to resist to the temptation to borrow excessively at non-concessional terms on both the domestic and international markets as its fiscal space has been considerably reduced in the last few years.

Next steps:
- RBA is discussed with MoF and key action points are agreed.

An Assessment of Non-Tax Revenue Potential in Tanzania

Status: Ongoing

Non-Tax Revenues form an important component of the domestic revenue base. However, the contributions in Tanzania remain consistently low. The non-tax revenues study will examine how to improve non-tax revenues by estimating their potential and assessing the possibility to expand the non-tax revenue base whilst maximizing economic benefits. It will estimate the non-tax revenue potential in natural resources and public and statutory corporations. It will also propose measures for increasing the collection of non-tax revenues in these two areas whilst maximizing the economic benefits of non-tax revenues.

Next steps:
- MoF submit their comments to DFID.
- The consultants finalise the report.

PPP

Status: In Procurement Stage

PPP is an important instrument for the Government to attract public private investment and to improve public services. The PPP study aims to inform decision makers on the potential pipeline of PPP projects in the transport sector and how best public funds can be used to support them. It will look at how scarce resources can be used most
effectively to leverage private investment and to provide value for money. The study will examine how PPP projects should be selected, how to fast track procurement, criteria to allocate public funding and the decision process for allocation. The study will be based on best practices and tools which can be adopted to prioritize PPP projects, specifically in the transport sector.

**Next steps:**
- PPP study consultant is chosen and work starts.

**Future Pipeline**

Four studies have been proposed for implementation in 2015. These are: efficiency gains in infrastructure investment projects; implications of the GDP rebasing on macroeconomic, fiscal and the public expenditure planning; social protection and environment and climate change. The proposals will be presented for approval to the PER Champions Group meeting scheduled in February, 2015. A maximum of three will be selected.

**Next steps:**
- ToRs are drawn up for the selected studies and consultants appointed.

**PER Newsletter**

The quarterly PER newsletters highlighting key PER activities being implemented in each quarter have been produced for information sharing with stakeholders. The newsletters have been posted on the MOF website (http://www.mof.go.tz/index.php?option=com_content&view=article&id=750&Itemid=268) and DPG website (http://www.tzdpg.or.tz/index.php?id=1229).