

*2 December 2012*

## Global Initiative on Fiscal Transparency

# **Towards Stronger Incentives for Increased Fiscal Transparency, Participation and Accountability**

Discussion Paper for GIFT Lead Stewards

**Murray Petrie**

**Senior Steward (GIFT)**

**iScale**

## Contents

Executive Summary	4
Abbreviations and Acronyms	8
Section I: Introduction and background	9
Section II: Incentives and causal pathways: theory and evidence	10
a) Fiscal transparency program logic	11
b) Synthesis of evidence	12
c) Strengthening the evidence base	14
Section III: Incentives and incentive mechanisms for promoting fiscal transparency, participation and accountability	
a) Fiscal transparency as executive branch self-regulation	15
b) The role of legislatures	21
c) Other actors	22
d) Global norms	22
e) Information and communications technology	29
Section IV: How GIFT can strengthen incentives for fiscal transparency, participation and accountability	
a) The GIFT theory of change	30
b) Evaluative material on the effectiveness of interventions aimed at increasing FTPA	31
c) The general literature on influencing policy outcomes	35
Section V: Conclusions and recommendations	36
References	44
Annex 1: Fiscal transparency, participation and accountability: assumed causal pathways, indicators and evidence	[separate file]

Annex 2:	Brief summaries of empirical evidence	48
Annex 3:	The Political Economy of Policy Reform (Figure 8.1, Grindle and Thomas 1991).	51
Figure 1:	FTPAs incentives logic	11
Figure 2:	Virtuous expanding cycle of fiscal transparency	[separate file]
Figure 3:	The GIFT theory of change	30
Figure 4:	GIFT Incentives Prioritization Matrix	39
Table 1:	Finnemore and Sikkink's Norm Life Cycle	23
Box 1:	Grindle and Thomas' Framework for the Political Economy of Policy Reform	18
Box 2:	Motivations and incentives for executive branch decision-makers to introduce greater FTPA	19-20
Box 3:	The recent record of international monitoring by the IMF	32
Box 4:	Kingdon's agenda setting model of influencing government policies	36

## Executive Summary

This report was commissioned by the GIFT Lead Stewards at their meeting in Washington DC in August 2012. GIFT's objective is to utilise incentive mechanisms to foster increased fiscal transparency, participation, and accountability (FTPAs) worldwide.

This report aims to deliver three results for GIFT:

- 1) A tighter and more useable shared analytical framework on incentives.
- 2) A more solid basis for selecting between potential alternative areas for action on incentives.
- 3) Recommendations on specific incentive levers on which GIFT should focus its initial efforts, and action agendas to implement them.

The question at the heart of the issue of incentives for FTPAs is: *why would governments choose to impose FTPA requirements on themselves?* A first response to this question might involve posing the further question: *what are the potential incentive-compatible levers or circumstances that GIFT should consider as potential candidates for strengthening, or as entry points for engagement?*

The report first drills down into the micro causal pathways through which FTPA-activities are assumed to impact on outcomes, and the empirical evidence on those impacts. Annex 1 contains a summary outcomes hierarchy table, including citations to the key pieces of empirical evidence (brief summaries of which appear in Annex 2).

The relevant evidence on incentives can be summarised as follows. There is case study and testimonial evidence of the impact of CSO FTPA norms and their assessment (especially graduated country rankings) on country behaviour. There is evidence of a strong impact of IFI conditionality on FTPAs in some circumstances. There is a solid body of evidence that fiscal transparency is rewarded with higher sovereign ratings and lower spreads. There is some evidence that fiscal transparency improves fiscal performance, and social and governance indicators.

Drawing on the assumed causal pathways (Annex 1), the empirical evidence on impacts (pp. 12-13), the 'stylized facts' on the political and other circumstances that create positive incentives (p. 37), and the GIFT theory of change, a prioritisation matrix has been devised which arrays the strength of the incentive mechanism or channel in one dimension, and the ability of GIFT interventions to influence on the other dimension – see table next page.

The highest potential priorities appear in segments 1 and 3 of the table, the correspondence of a clear ability of GIFT to influence, on the one hand, with negative incentives, and with strongly positive incentives respectively, on the other.

## GIFT Incentives Prioritization Matrix

*Strength of incentive mechanism or channel*

<i>Amenable to short term influence by GIFT? <sup>1</sup></i>	Negative	Moderately positive	Strongly positive
Yes	(1) *Weak oversight institutions *Weak civil society *Weak media *Gaming of FTPA assessments *Standard shopping	(2) *Standards convergence *New FTPA norms *UNGA declaration/G20 *Legislative oversight *Communication with key decision makers *FTPA TA *FTPA ICT-take up *Evidence of FTPA impacts	(3) * The Open Govt. Partnership * Sovereign bond market *FTPA country league tables *Authoritative, comparative, regular FTPA assessments of fiscal data quality *Concern over social equity and human rights
Maybe	(4) *Fiscal austerity (gimmicks) *Corruption *Under-funding of oversight institutions	(5) *Fiscal austerity (build credibility) *Donor conditionality *Business and other financial markets *Scope of FTPA Reforms (wide public impact v technocratic) *General PFM reform and capacity building	(6) *IFI conditionality *Prestige of individ. leaders *Internalization via domestic independent FTPA assessments *Central governments impose FTPA on SNGs *Use of bond rating as regulatory mechanism *Concerns over environmental outcomes *Regulation of sovereign bond market?
No  (but GIFT can be ready when opportunities arise)	(7) *Autocratic regimes *Elite capture *Secrecy culture *Business/polit. Networks	(8) *Prominence of FTPA norms	(9) *Characteristics of elites *National context *Agenda-setting circs. (regime change, crises, post-conflict) *Political pluralism * Deep regional trade agreements

<sup>1</sup> Amenable to influence by GIFT is assessed against a time frame of up to, say, 3 years, which in this field of deep institutional change, should be regarded as the short term. The medium term might be approximately 4-10 years, and the long term 10-20+ years.

Based on the above, the following specific recommendations are put forward for consideration as priority areas for GIFT to focus on to strengthen incentives for FTPA, in the next 12 months to the end of 2013:

- I. **The Open Government Partnership:** the essential challenge of the incentives issue - of executives imposing FTPA requirements on themselves - points to the great potential of the OGP as a mechanism for GIFT to work with to achieve shared objectives. Forty one of these countries have committed themselves to specific initiatives on fiscal transparency and participation.
- II. **The sovereign bond market channel (and the private financial sector and wider private sector):** The solid evidence in support of countries being rewarded for fiscal transparency with higher ratings and lower spreads, the large number of sovereign borrowers, and the widespread concerns over fiscal sustainability and transparency post-GFC all point to this as an area of significant unexploited potential.
- III. **The standards and norms agenda:** there is sufficient case-study and testimonial evidence of an effect on key decision makers through instruments such as the IMF Code and the OBI, and of an indirect impact through, for example, the strengthening of civil society and the financial market channel, to justify high priority being given to GIFT's norms agenda.
- IV. **Communicating the urgency of FTPA:** both directly to officials, and via the actors that decision makers listen to (citizens/voters, the media, business, and CSOs).

These four priority areas are intended to comprise a coherent and mutually-supporting package to strengthen incentives. There are close interconnections between the OGP agenda, the norms agenda, and GIFT's TA and ICT initiatives. There are also links between the financial market and norms agendas, while the communication agenda has the potential to reinforce and leverage all of GIFT's activities.

Suggested action agendas to implement these four priority areas in 2013 are as follows:

- a. **The Open Government Partnership:** create a GIFT-OGP Community of Practice on FTPA; work with the Co-chairs of OGP for 2013 (Indonesia and the U.K.); work with selected OGP governments/CSOs to implement their FTPA commitments, and with selected non-OGP countries on meeting OGP eligibility criteria; attract OGP members as GIFT stewards.
- b. **The sovereign bond market/financial sector actors:** conduct interviews/hold events to better understand practices and information needs, and promote the incorporation of this in the design and assessment of norms.
- c. **The standards and norms agenda:** develop and trial the Guide on Public Participation in Fiscal Policy; develop the Guide on Legislative Oversight;

provide input into reviews of existing norms to increase their incentive effects; facilitate coordination between standard setters; promote the strengthening of FTPA databases, monitoring, evaluation, and research.

- d. **Communicating the urgency of FTPA – Global Political Agenda-Setting:** more officially launch GIFT at the WB/IMF Annual Meetings in April and/or UN Meetings in September; pursue UNGA declaration and G20 opportunities; produce popular versions of the HLPs and the ‘killer facts on fiscal transparency’; progressively build relationships with the media; and develop a communications strategy.

An implication of the above agenda is that there is a need to increase the tempo of GIFT activity i.e. more engagement from Stewards’ organisations, more Working Group meetings.

Stewards should also review whether the current number and configuration of Working Groups is fit for purpose given the new action agenda.

#### **I. Proposed decisions by GIFT Stewards**

It is recommended that Stewards:

- 1) Endorse the four priority areas for GIFT action on strengthening incentives in 2013, as outlined on pp. 38-40, as being central to the rationale and motivation for GIFT.
- 2) Discuss and decide on the recommended action agendas to implement the four priorities put forward on pp. 40-42.
- 3) Review whether the current Working Group structure and process are fit for purpose given the new action agenda.
- 4) Discuss and decide in principle on the possible six priority areas for 2014 (pp. 42-43) as a basis for planning, and for review in the light of developments during 2013.

## Abbreviations and Acronyms

CoST	Construction Sector Transparency
CSO	Civil Society Organisation
EITI	Extractive Industries Transparency Initiative
FTPA	Fiscal Transparency, Participation and Accountability
G20	The Group of 20
GFC	Global financial crisis
GFS	Government Finance Statistics
GIFT	Global Initiative on Fiscal Transparency
GFMIS	Government financial management information system
GFSM2001	Government Finance Statistics Manual 2001
HLP	High Level Principles (of GIFT)
IBP	International Budget Partnership
ICT	Information and communications technology
IFAC	International Federation of Accountants
IFI	International financial institution
IMF	International Monetary Fund
IMF FTC	IMF Fiscal Transparency Code
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standards
ISO	International Standards Organisation
ISSAI	International standard of supreme audit institutions
MSI	Multi-Stakeholder Initiative
OBI	Open Budget Index
OBS	Open Budget Survey
OECD	Organization for Economic Cooperation and Development
OECD BP	OECD Best Practices in Budget Transparency
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
ROSC	Report on the Observance of Standards and Codes
SAI	Supreme Audit Institution
SDDS	Special Data Dissemination Standard
SNG	Sub-National Government
TA	Technical assistance



## **i. Introduction and background**

This report was commissioned by the GIFT Lead Stewards at their meeting in Washington DC in August 2012. GIFT's objective is to utilise incentive mechanisms to foster more transparent, participatory, and accountable fiscal decision-making processes worldwide.

To date GIFT has made remarkable progress in a short period in building consensus around a new set of High-Level Principles for Fiscal Transparency, Participation and Accountability (FTPA). They are contained in two documents: 1) a summary version of the High Level Principles, and 2) an expanded version that presents more detailed background information on each principle.

GIFT is now building on the progress achieved, by anchoring an action agenda and developing products around the High-Level Principles. These activities and products fall into four categories:

- 1) Global political agenda setting and promotion of the High Level Principles.
- 2) Drafting and promoting up-take of new norms to fill critical gaps, and addressing inconsistencies within the current normative architecture.
- 3) Sharpening the shared understanding of and strengthening the framework of incentives for advancing fiscal transparency.
- 4) Further advancing the work on technical assistance and capacity building in FTPA.

The third of these categories - work on incentives - is specifically prioritized within GIFT over the coming year, and is the subject of this report.

This report aims to deliver three results for GIFT:

1. A tighter and more useable shared analytical framework on incentives.
2. A more solid basis for selecting between potential alternative areas for action on incentives.
3. Recommendations on specific incentive levers on which GIFT should focus its initial efforts, and action agendas to implement them.

The report builds on an initial December 2011 report for GIFT lead stewards that explored the elements of an incentive regime for fiscal transparency.<sup>2</sup> That report

---

<sup>2</sup> Alejandro Litovsky, 'Assessment of an Incentive Regime for Fiscal Transparency'. Final Report, 5 December, 2011.

provided detailed information on the different stakeholders and their motivations in FTPA, and recommended three areas of focus.<sup>3</sup>

This report goes into greater detail on:

- the intervention logic – causal pathways – towards FTPA outcomes;
- the empirical evidence on impacts;
- the different types of incentive mechanisms;
- how GIFT can make a difference; and
- the implications of the above for selecting between alternative areas for action and identifying priorities for GIFT initiatives to strengthen incentives.

The report is structured as follows:

Section II drills down into the micro causal pathways through which FTPA is assumed to impact on outcomes, and the empirical evidence on those impacts.<sup>4</sup> This section also attempts to distil key stylized facts from the empirical literature on FTPA. Annex 1 contains a summary table, including citations to the key pieces of empirical evidence on the impacts of transparency and participation. Annex 2 contains brief summaries of the citations referred to in Annex 1.

Section III discusses some of the key generic incentive mechanisms with respect to FTPA that are potentially amenable to strengthening by GIFT.

Section IV contains a brief exposition of the GIFT theory of change, and discusses GIFT's potential for strengthening incentives for FTPA.

The final section draws together conclusions from the empirical evidence, and GIFT's potential value added, to recommend a small number of incentive levers as priority areas for GIFT to initiate action on in 2013.

Proposed decisions by GIFT Stewards appear at the end of the Section V (p. 40).

## **II. Incentives and causal pathways: theory and evidence**

This section discusses the micro causal pathways through which FTPA impacts on the outcomes of interest, and the available empirical evidence on the sign and size of these impacts.

---

<sup>3</sup> The three areas were marketing fiscal transparency; developing a financial markets agenda; and coordinating fiscal transparency across other agendas, specifically aid transparency, extractive industries transparency, and quality of public service, consumer rights, and access to information.

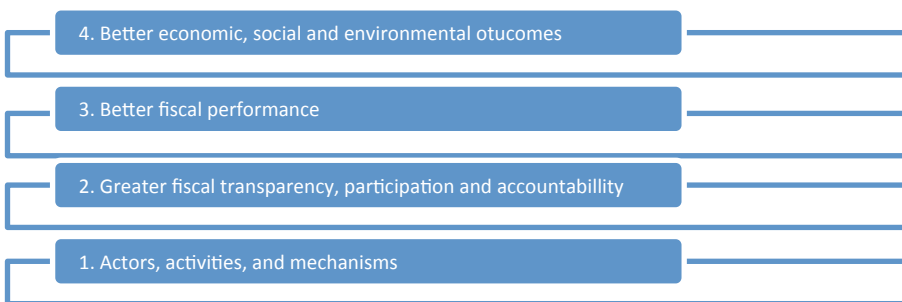
<sup>4</sup> Throughout this report the term 'impacts' is used in a general sense to refer to the effects or results of FTPA activities at all levels of the outcomes hierarchy (or results chain), from immediate and short term impacts to ultimate impacts on final outcomes.

a) *FTPAs Program Logic*

It is helpful to map out the assumed causal pathways as a check on the logic, and on the often implicit assumptions underlying the design of any initiative or program. For instance, McGee and Gaventa, in a review of the impact of citizen-led accountability and transparency initiatives note that untested assumptions and inadequate theories of change have contributed to a weak evidence base.<sup>5</sup>

The causal pathway has the following logical structure, with the direction of movement running from the bottom row upwards:

**Figure 1: FTPA Program Logic**



This is fleshed out in more detail in the table in Annex 1, which is an outcomes hierarchy running from key FTPA actors and mechanisms at level 1, through assumed immediate impacts, to intermediate outcomes, and ultimately to final outcomes (level 4). The table in Annex 1 should similarly be read from the bottom up i.e. starting at the last page and working forward.

The full outcomes hierarchy is shown, not just the lower levels that are confined to the link between actors, activities and mechanisms, on the one hand, and greater FTPA on the other. The latter is the focus of this report, in particular the incentives for key actors to introduce greater FTPA and the activities and mechanisms that may strengthen their incentives i.e. the relationships between levels 1 and 2.

However, the higher levels of the outcomes hierarchy, while obviously important of themselves, are also indirectly important for incentives to introduce FTPA. The more evidence that is marshalled on the impacts of FTPA on improving fiscal performance and/or final outcomes, the stronger is the interest in and pressure to introduce greater FTPA.

There are limitations to such linear outcomes hierarchies – as the table is drawn in Annex 1 it leaves out feedback loops and interaction effects, such as interactions

<sup>5</sup> McGee and Gaventa, 2010, pp. 6-10

between domestic oversight, market risk assessment, and external monitoring and intervention. A simple outcomes hierarchy of this type can nevertheless be a helpful way to succinctly articulate the program logic, to set down how success will or could be measured, and to locate the current evidence base.

*b) Synthesis of the evidence*

As can be seen from cursory inspection of the table in Annex 1, there is relatively limited but growing evidence to date on the impact of interventions aimed at increasing FTPA. What evidence there is, is largely confined to impacts on transparency (disclosure) rather than on participation or accountability (see the brief summaries of the citations in Annex 2). There is, however, more evidence at intermediate levels of the outcomes hierarchy.

In this sub-section, the strength of the available evidence is assessed as a combination of the strength of the relationships - between activities and FTPA or between FTPA and the relevant outcomes - from both quantitative and qualitative research, together with a judgment about how significant the finding is in a policy or practical sense. So for instance, research may have established that there is a strong causal relationship between two variables, but the outcome variable might or might not be significant to overall FTPA. It might, for instance, establish a causal relationship low on the outcomes hierarchy, confined to initial impacts rather than to better fiscal reporting or more citizen participation. Or the research finding may relate to only a small aspect of an impact or outcome, or be otherwise limited by methodology or timeliness.

The following conclusions are put forward on the strength of the evidence on the different causal pathways and mechanisms:

1. There is an accumulating and fairly solid body of evidence that the sovereign bond market channel has the assumed sign and effect i.e. after controlling for other variables, fiscal transparency is rewarded with higher sovereign ratings and lower spreads.
2. There is strong reason to believe, from publications by rating agencies on their methodology for rating sovereign bonds, that fiscal data is central to sovereign bond ratings. The rating agencies also use information on the quality of governance in a country and other softer indicators of willingness to repay and of policy sustainability, as inputs to the rating, and FTPA may also be a factor here. It also seems clear that the ratings agencies have difficulty accessing all the data they need, especially on off-budget activities, which suggests the importance of norms and standards prescribing the coverage of government fiscal reports, and authoritative published assessments of country practices against the standards. On the other

hand, rating agencies have privileged access to fiscal information from the governments they rate, and this may dilute their incentives to push for or to use published FTPA assessments.

3. There is only weak evidence that the rating agencies actually use information in published assessments of fiscal transparency and participation. The main evidence is dated (Petrie 2003). It relates to a period when fiscal ROSCs were being published in quite large numbers (2002, when the number of Fiscal ROSCs peaked at 21) prior to dwindling away (there were only 3 in 2010 and 1 in 2011). It was also prior to the 2007 amendments to the IMF Fiscal Transparency Code and ROSC; but also prior to publication of results from successive rounds of the OBI. Very recent anecdotal evidence suggests that some investment banks and rating agencies are using OBI data.

4. There is only patchy evidence to suggest that the relationship between fiscal transparency and other financial market channels (portfolio investment and FDI) has the assumed sign and effect. The evidence is dated, and was limited in coverage.

5. There is evidence that supports a positive impact of fiscal transparency on higher level outcomes, namely on fiscal performance, and to a lesser extent on performance against economic and social indicators, and on the quality of governance.

6. There is as yet little robust statistical evidence of an impact of FTPA norms and assessments on country practices. There is, however, case-study and testimonial evidence of an effect of norms on key decision makers through instruments such as the IMF Code, the OBI, and of an indirect impact through, for example, the strengthening of civil society and the financial market channel. There is also evidence of a strong impact of IFI conditionality on FTPA in some circumstances. These issues are discussed in more detail in Section IV.

7. There is, not surprisingly, limited evidence of the impact of FTPA on the perceived legitimacy of fiscal policy. This is likely due to the very late stage at which public participation has been codified as an element of fiscal transparency; for instance, there is a lack of summary cross-country data on participation in fiscal policy at the moment (see sub-section c). One study has found that greater budget transparency is associated with higher voter turnout (Benito and Bastida 2009). Multiple studies of participatory budgeting in Latin America have found it has contributed to strengthened democratic processes.<sup>6</sup>

---

<sup>6</sup> McGee and Gaventa, 2010, p. 14.

### *c) Strengthening the evidence base*

Looking ahead, as with any field of public policy, three basic types of research are needed to generate an evidence base on FTPA:

- *Basic descriptive research on the whole population of jurisdictions.* Successive bi-annual rounds of the OBS have generated a quantitative data base of a large number of countries since 2006 (94 countries in the 2010 survey) against an evolving set of questions on budget transparency and public participation in budgeting. This has yielded summary data on budget transparency practices across countries, but unfortunately there is as yet no similar summary data from the OBS on country practices with respect to public participation in fiscal policy. The IBP has also piloted the OBS at sub-national government level, and may generate a database of practices at SNG level over time.<sup>7</sup> Other sources of summary data that exist include the IMF's Fiscal ROSC data base (which is not public and is now dated given the lack of ROSCs in recent years); the IMF's Government Finance Statistics Yearbook database (institutional tables of the structure of government and the coverage of fiscal statistics); the OECD's Budget Institutions Database; and PEFA (although PEFA data is not designed or intended to be used for cross-country purposes).<sup>8</sup>
- Uncovering causal relationships on the impacts of FTPA on outcomes of interest. Agreement about the strength and form of causal relationships evolves slowly as evidence accumulates from many studies. The evidence accumulated to date is summarised in subsection b) above.
- Evaluation of policies and interventions aimed at increasing FTPA. Given the short period since the formal international fiscal transparency initiative started in 1998, this literature is in its very early stages. There is a discussion of this in Section IV. It will be important for GIFT to put in place a monitoring and evaluation framework to learn from experience with its initiatives and interventions. GIFT should also devise a research strategy, which might be confined to assessing the research efforts by GIFT

---

<sup>7</sup> [correct Paolo?].

<sup>8</sup> The OECD International Database of Budget Practices and Procedures contains results for 31 OECD member countries and 66 non-members of the 2007 OECD survey of budget practices and procedures in OECD countries, the 2008 World Bank/OECD survey of budget practices and procedures in Asia and other regions, and the 2008 CABRI/OECD survey of budget practices and procedures in Africa. The database provides data on more than 99 questions covering the entire budget cycle, and including performance information, and aid management within developing countries.

participants and others and identifying priority research areas, but which might also involve seeking to coordinate, stimulate, or even commission evaluation and research to fill key knowledge gaps. The objective of GIFT's monitoring, evaluation and research activities should be to ensure we are well placed to obtain early feedback from FTPA initiatives, and have a better idea of what works and why with respect to FTPA in 5-10 years' time.

### **III. Incentives and incentive mechanisms for promoting fiscal transparency, participation, and accountability**

#### *a) Fiscal transparency as executive branch self-regulation*

Fung et al argue that 'Public transparency policies represent a particularly promising form of information-age governance.'<sup>9</sup> These authors define public transparency policies as systems that require governments or private sector entities to publicly disclose factual information about products and practices, structured for comparability to serve a public purpose. 'At best, transparency policies advance public priorities by combining ordinary citizens' interests in making more informed choices with organizations' interests in improving their competitive position.'<sup>10</sup> They put forward a 'transparency action cycle' in which information disclosers react to information users' changing perceptions or behavior.

An adapted version of this cycle is presented in Figure 2, which is tailored to apply to FTPA, to incorporate new developments in ICT, and to illustrate an expanding 'zone' of FTPA.

#### **[Figure 2: Virtuous expanding cycle of fiscal transparency here – in separate file]**

The cycle can, of course, also operate in reverse, as a vicious cycle of progressively shrinking FTPA. For example, governments may respond to powerful interests and shift fiscal activities off budget; they may engage in fiscal gimmicks that make the reported fiscal position look better while the true fiscal position deteriorates; or public participation opportunities may be captured by narrow elites.

Sources of new perceptions, preferences and demands on the part of voters, business and markets, or civil society, could come from crises, corruption scandals, major service delivery or new policy failures, or credible external assessments of performance weaknesses. The evidence for the impact from these is discussed in the next section.

---

<sup>9</sup> Fung, Graham, Weil, and Fagotto, 2005, p. 4.

<sup>10</sup> Fung et al 2005, p. 2.

Fung et al describe transparency policies as a third wave of modern regulatory innovation, at a time of optimism about advances in information and communications technology (ICT).

The relevance of regulatory transparency to fiscal transparency is two-fold:

- a) Fiscal transparency, participation and accountability are essentially about the regulation of fiscal policy-making and implementation processes.
- b) From an incentives perspective, a critical element of fiscal transparency is that, to a significant extent, it represents self-regulation by the executive branch, in some countries in tandem with the legislative branch. Decisions to introduce greater FTPA must, at the end of the day, be taken by and implemented by national level officials within the executive branch of government in most countries. Legislatures can play an important role in some countries, but in many countries the executive has a majority in the legislature, and in all countries the executive possesses the information and controls most of the processes of public participation.

FTPA represents self-regulation by the executive branch except to the extent that:

- A country's Constitution imposes requirements for fiscal transparency and participation, which are then enforced by an independent judiciary;<sup>11</sup> or
- A country has entered international commitments to fiscal transparency and participation e.g. in regional groupings such as the European Community (EC) e.g. treaty commitments to the provision of fiscal statistics; or multilateral treaty commitments around transparency of border tariffs in the WTO, or to very basic elements of fiscal transparency in UNCAC; or commitments to international organizations such as the IMF e.g. to fiscal transparency as conditionality for short term financial support, or commitments to the publication of fiscal statistics in the SDDS.
- The central government has the jurisdiction and authority to impose fiscal transparency requirements on sub-national governments (SNGs).

Leaving SNGs aside, this leads directly to a question which it is suggested is at the heart of the issue of incentives for FTPA: ***why would governments choose to impose FTPA requirements on themselves?***

---

<sup>11</sup> A constitution of course is generally a form of macro, country-level self-regulation (except where it is imposed externally e.g. by the victors after a war), but can be seen as essentially a given from the perspective of an executive at any point in time. Some countries with relatively recent Constitutions contain specific provisions on fiscal transparency, public participation, and accountability e.g. South Africa, Brazil, that are not contained in older Constitutions.



A first response to this question might involve posing the further question: *what are the potential incentive-compatible levers or circumstances that GIFT should consider as potential candidates for strengthening, or as entry points for engagement?*

In answering this it is first useful to distinguish between incentives and motives. Motives are typically divided into two types: internal (or intrinsic) motivation, and external (or extrinsic) motivation.

Intrinsic motivation arises from within the individual. In the context of FTPA, intrinsic motivation might refer to an individual political leader's pursuit of greater FTPA arising from their belief in the inherent value of FTPA e.g. the pursuit of human rights to information, or the instrumental value of FTPA e.g. in raising living standards. Such motivation might also arise with respect to senior civil servants in key institutions, particularly the ministry of finance (particularly officials responsible for the budget), a Budget Office (where it is separate from the mof); the prime minister's department or the president's office, potentially the ministry of planning, and senior office holders in watch-dog agencies such as the SAI and the Ombudsman. In some situations a champion minister of a line ministry, such as education or health or infrastructure, could play an important role in starting to open up government information.

Incentives of various types – financial, winning a competition (e.g. re-election to office), prestige and recognition, and threat of sanctions - are important examples of external motivation. They are clearly of two types: positive incentives (rewards) and negative incentives (punishments). Theory suggests that certain factors increase the effectiveness of incentives, such as how close the consequence is in time, how easy it is to perform the required activity, and how specific the required activity is.

The literature also refers to the possibility of external motivation being internalised if the activity fits with an individual's values and beliefs. This would suggest a reduced need for incentives due to the ability to rely on internal motivation. With respect to FTPA, internalisation is perhaps most relevant in thinking about internalising external pressures for greater FTPA via developing domestic constituencies for FTPA, or even by building a multi-stakeholder approach to assessment, or tasking a domestic institution (e.g. the SAI) with responsibilities for assessing, reporting on and promoting FTPA.

Secondly, it is also useful to distinguish between incentives that are potentially faced directly by decision makers with the authority to introduce greater FTPA, and those that operate indirectly through other actors who interact with the first set of decision-makers.

Thirdly, it is necessary to distinguish between different degrees of ambition or scope of FTPA. At a general level, the literature distinguishes between crisis situations and 'politics as usual' (Grindle and Thomas). In a crisis, there is greater urgency to act (e.g. introducing greater fiscal transparency to try to head off a collapse in market confidence in fiscal

sustainability); higher stakes from inaction; stronger incentives; and the likely engagement of the top political leadership. Box 1 briefly describes Grindle and Thomas' wider framework for the political economy of policy reform.

**Box 1: Grindle and Thomas' framework for the political economy of policy reform**

Grindle and Thomas have put forward a useful framework for the political economy of policy reform, concentrating on developing countries (Grindle and Thomas 1991). Figure 8.1 from Grindle and Thomas is reproduced in Annex 3. They identify three broad factors:

- A. The environmental context:
  - a. The individual characteristics of policy elites: includes their ideological predispositions, their professional expertise and training, their memories of similar policy situations, their position and power resources, their political and institutional commitments and loyalties, and their personal attributes and goals.
  - b. The context of policy choice: includes societal pressures, historical context, economic conditions, international context, and administrative capacity.
- B. The agenda-setting circumstances: whether it is a crisis situation or 'politics as usual.'
- C. The policy characteristics: whether the arena of conflict is the broad public, or a less visible bureaucratic audience.

The literature also distinguishes between the scope of political conflict involved: whether the increased FTPA concerned has a direct and visible impact on large sectors of society, or is more technical and bureaucratic with limited public impact (Grindle and Thomas 1991). An example of the former might be a new and broad Fiscal Responsibility Law, while the latter might be a new GFMIS which, initially at least, may be viewed as largely a technical issue.

In Box 2 an attempt has been made to identify and classify a number of direct levers and incentives from the perspective of decision-makers within the executive branch of government. The incentive features are classified according to whether they are primarily domestic or external factors. The examples illustrate the various elements discussed above, notably internal and external motivation, and positive and negative incentives of various types.

At the same time, there are of course also powerful negative motives and incentives for executive branch actors to oppose increased FTPA or to reduce the current level of FTPA. Key ones here are:

- The desire to channel public resources or positions of influence to favoured groups or individuals in return for electoral support or campaign financing.

## **Box 2: Motivations and incentives for executive branch decision-makers to introduce greater FTPA**

Decisions to introduce greater FTPA must, at the end of the day, generally be taken by and be implemented by national level officials within the executive branch of government. A key issue for GIFT, therefore, is how to work with and strengthen the incentives that various of these officials face, or how to take advantage of opportunities to engage given the presence of particular circumstances that positively influence their motivations.

### *Domestic political factors:*

- 1) To respond to demands from a legislature with sufficient authority and, in turn incentives, to push for greater FTPA e.g. as occurred in France in 2001.
- 2) To launch a country on a new trajectory, particularly at points of regime change or change in leadership e.g. fiscal transparency and participation linked to political competition and policy contestation in a new democracy.
- 3) To respond to a wave of popular demand e.g. following a corruption scandal, or unpopular fiscal bail-outs of private financial institutions.
- 4) To entrench policies which are in line with the ideology of a political party or coalition of parties e.g. transparency of tax burdens and total public spending as a brake on the size of government, or alternatively transparency of social and environmental indicators that suggests the need for more or more effective public spending.
- 5) To be seen to respect recognized citizen rights e.g. a right to public information, a right to participate in fiscal policy decision making; or transparency over gender-based budgets.
- 6) To increase the personal reputation of individual political leaders e.g. to increase their personal political popularity or power (to be re-elected).
- 7) To embarrass the previous government of a different political composition e.g. exposing corruption or gross mismanagement, or fiscal gimmicks, and instituting new practices to ensure they do not recur e.g. the Charter of Budget Honesty Act in Australia introduced by an incoming government in 1998.
- 8) To reduce the room for manoeuvre of future governments of competing political parties e.g. transparency of spending to reduce the scope for channelling resources to favoured groups.
- 9) To head off potentially more intrusive or restrictive requirements being forced on a government by the weight of popular opinion or reaction to an incident, or by some other uncommon means i.e. damage-limitation.
- 10) To increase the attractiveness of domestic investment, so as to grow the tax base, create jobs, and improve prospects for re-election e.g. in a country where political competition is on the basis of policies that promote the general public good.
- 11) To provide higher quality public services to improve the prospect of re-election e.g. increasing public consultation over policy changes to improve the quality (and legitimacy) of policy design.
- 12) To respond to demands for greater FTPA from domestic CSOs.
- 13) To enforce transparency and accountability on sub-national governments to reduce fiscal risk to the central government, particularly following a fiscal crisis involving sub-national governments, or to respond to popular concern over corruption or mismanagement scandals at SNG level.
- 14) To prevent unproductive tax competition between sub-national jurisdictions.
- 15) In response to pressure from sub-national governments on the central government for greater transparency over inter-governmental fiscal transfers – e.g. to attempt to reduce

'leakage' between the central budget and what is eventually received into sub-national treasuries;<sup>12</sup> or to reduce the discretion of central government officials in allocating resources between SNGs; or by some SNGs to try to obtain a more equitable share compared to other SNGs.

*External factors:*

- 1) To reduce the risk of loss of market confidence in a country's public debt sustainability e.g. to head off the risk of, or respond to a rating down-grade.
- 2) To address concerns and pressures from the international donor community about the integrity and legitimacy of domestic PFM, that could lead to a loss of some development assistance or a tightening of conditionality.
- 3) To meet IFI requirements as a condition of accessing project or program financing.
- 4) To respond to pressure from neighbouring countries in deep regional trade agreements.
- 5) To obtain increased legitimacy for the government in the eyes of the international community.
- 6) To increase the personal reputation of individual political leaders e.g. to increase their future prospects for international public office, or their personal prestige.
- 7) To increase the credibility of promises or actions to increase fiscal transparency and accountability so as to increase the benefits of FTPA e.g. more credible actions are likely to receive an earlier and more favourable response from financial markets. This would require the use of particular mechanisms of fiscal transparency that are difficult to reverse, such as new Constitutional provisions, or international treaty commitments.
- 8) To prevent unproductive tax competition between countries e.g. tax transparency within international currency unions.
- 9) To prevent distortion of competitive markets in deep Free Trade Agreements e.g. transparency of state aid to industry.

- To make a government's fiscal performance look better than it is, in order to enhance the prospects of re-election, or to prevent a credit rating down-grade. This is particularly important at the moment in the context of fiscal austerity in many countries in the aftermath of the global financial crisis (GFC).

- To gain an advantage in negotiations with a legislature over the annual budget
- To hide fiscal problems or risks for a future government of a different political composition to deal with.
- To weaken the ability of civil society and/or the media to monitor government and hold it to account.
- Personal enrichment (especially grand corruption).
- Cultures of secrecy within government that inhibit the free flow of information within government let alone to the public.
- The weak capacity of the civil service, which acts as a brake on dissemination and participation, and adds to risk-averse behaviour e.g. non-disclosure as the default option.

---

<sup>12</sup> As occurred in Nigeria, for instance, with respect to oil revenue sharing and fiscal transfers within the Federation.

- Resistance to foreign norms.

### *b) The role of legislatures*

The first domestic factor in Box 1 - to respond to demands from a legislature with sufficient authority and, in turn incentives, to push for greater FTPA – raises the issue of the circumstances in which a legislature might face incentives to push for increased FTPA. These incentives could include:

- a A desire to obtain more information and accountability from the executive. While legislatures' role in fiscal policymaking has grown in recent years, many continue to lack the information, time, and powers to hold governments to account (IMF 2012).
- b A desire for more authority or say over the level or allocation of spending or over tax policies.

Countries where members of the executive are not also members of the legislature (i.e. countries that do *not* have Westminster-style systems) are probably more likely to have incentives to push for or to impose FTPA requirements on their executive branches. The separation of powers creates stronger incentives for a legislature to confront an executive, especially when the majority party(s) in the legislature is from a different party to the President.

In addition, countries where the legal framework empowers the legislature with authority over particular types of fiscal decisions, such as amending the executive's budget proposal, or changing the levels or composition of spending, seem more likely to be more assertive in exercising oversight of the executive's conduct of fiscal policy.

A recent example of an active legislature pushing for greater FTPA was in France, where the financial committees of the Assembly and Senate were the driving force behind the country's 2001 organic budget law which overhauled the budgetary and accounting rules to enhance fiscal transparency at every stage of the financial management cycle (IMF 2012).

On the other hand, a legislature may also have perverse incentives to try to blame the executive for poor fiscal outcomes for which the legislature itself is at least partly responsible. So while the legislature in countries with a strict separation from the executive may have stronger incentives to oversee the executive, its mixed incentives, and its measure of joint authority over the budget can make it harder for the public to hold either branch accountable for fiscal management. In a Westminster system, an executive might want to introduce greater FTPA to increase the credibility of fiscal policy, with stronger incentives to do so due to the clearer accountability of the executive for fiscal policy. Examples would include the UK (e.g. the establishment of the Office for Budget Responsibility in 2011), Australia (the 1998 Charter of Budget Honesty Act) and New Zealand (the Fiscal Responsibility Act 1993).

Finally, where a key legislative committee, such as a budget committee or a public accounts committee, is chaired by a member of the parliamentary opposition who is politically motivated to contest the executive, it is more likely that the committee will scrutinise government and seek to hold it accountable for fiscal management. More generally, Wehner and de Renzio (2011) find, in an 85 country data set, that partisan fragmentation of the legislature is associated with higher levels of budget disclosure.

#### *c) Other actors*

Briefly, the motivations and incentives faced by a limited number of other actors are also important. These include:

- The business community, which is not homogenous and should be disaggregated at least into the financial sector (which in turn needs disaggregation), the international trade sector, direct investment (domestic and international), and organised business lobby groups. The business community is primarily motivated by private profit, and is not necessarily in favour of increased FTPA where it is seen to conflict with private profit e.g. from the possession of private information or privileged access to elites. However, there are potential areas where competitive advantage is advanced through FTPA e.g. by levelling the playing field, or by increasing pressure to cut taxes, provide better public goods important to business, and reduce waste.
- The media, which is primarily motivated by profit, and which may pursue FTPA stories as a means to increase circulation. In addition, individual editors and journalists may be motivated to pursue FTPA stories by the desire for prestige, or from a personal commitment to social justice, human rights and so on.
- CSOs, which are often motivated by the personal agendas of founders or leaders, and/or by objectives related to social equity, human rights or the environment. The ICT revolution has greatly increased the ability of CSOs to form domestic and trans-national networks, to share experience and research, and to monitor and lobby government.

#### *d) Global norms*

The previous sub-sections have considered incentives from the perspective of the main institutional *actors*. In this and the next sub-section some generic incentive *mechanisms* will be considered that impact across many actors: global norms, including assessments of performance against standards and norms; and information and communication technology (ICT).

Norms and standards are rules of appropriate behaviour that are specific to a particular actor or entity. The terms are often used interchangeably, although a standard is generally viewed as being more specific, authoritative and binding, while a norm is more general and

less binding. In this paper the term norm is often used generically to include standards, but is at times also differentiated from standard, as in this sub-section.

A key issue for norms as an incentive mechanism is the conditions that affect the take-up and impact of different norms. The international relations literature suggests the following conditions under which norms matter:

- Legitimation – states that seek international legitimacy will adopt norms.
- Prominence – norms held by successful states are likely to spread.
- Intrinsic characteristics – clear, specific and enduring norms that make universalistic claims are likely to spread. There is debate over whether norms embodying an instrumental logic or a logic of appropriateness are more effective.
- ‘Fit’ with existing norms – the better the ‘fit’ the more effective is a norm.
- World time-context – norms that fit with the current world historical context are more effective.

A second important issue with respect to norms and incentives is the dynamics of norm uptake. How are norms disseminated and taken up? Are there non-linearities and ‘tipping points’? The international relations literature refers to a ‘norm life cycle’ and ‘norm cascades’ (Finnemore and Sikkink). Table 1 illustrates a posited three-stage life cycle, with actors, motives, and dominant mechanisms. In this model, in stage 1 states adopt norms for domestic political reasons. If enough states adopt the norm a tipping point is reached, leading to stage 2. Empirically, the tipping point is about one-third of states.<sup>13</sup> In Stage 2 states adopt norms in response to international pressure, while in stage 3 norms are internalized through codification.

**Table 1: Finnemore and Sikkink’s Norm Life Cycle<sup>14</sup>**

	<i>Stage 1: Norm emergence</i>	<i>Stage 2: Norm Cascade</i>	<i>Stage 3: Internalization</i>
<i>Actors</i>	Norm entrepreneurs with organizational platforms	States, international organizations, networks	Law, professions, bureaucracy
<i>Motives</i>	Altruism, empathy, ideational, commitment	Legitimacy, reputation, esteem	Conformity
<i>Dominant mechanisms</i>	Persuasion	Socialization, institutionalization, demonstration	Habit, institutionalization

On a long historical plane, Acemoglu and Robinson posit the presence of either extractive or inclusive political institutions that determine the prosperity of nations. The key element is decisions by the ruling elite on how they will organize a country’s political and economic

<sup>13</sup> See Sikkink and Khagram, ‘Restructuring World Politics – Transnational Movements, Networks and Norms.’

<sup>14</sup> Finnemore and Sikkink, 1998, p. 258.

institutions. Acemoglu and Robinson posit ‘critical junctures’ in the history of nations in which a new distribution of power and wealth upsets elite control and results in some governments becoming more accountable and responsive to their people. They also point to positive feedback loops that can create a virtuous cycle that prevents elites from overcoming inclusive institutions. A pre-condition for a virtuous circle is political pluralism.

Transparency and public participation are advanced forms of democratic pluralism. This analysis suggests that in many cases a pre-condition for political elites to face incentives to initiate or accept more FTPA is some basic level of political contestability. Transparency and direct public participation may also be important in creating incentives against rent extraction, by providing the population with information to monitor elite performance. This interacts with a free media, to help ensure the population is empowered with information.

Finally, two general political economy situations have been identified in the literature as offering promise as potential points of entry for FTPA reforms:<sup>15</sup>

- A post-conflict situation, when the political situation is unusually fluid, and the constraints of pre-existing rent allocations and institutional arrangements have been torn down. Collier (2007) identifies this as an opportunity for the international community to provide very large but time-limited TA inputs – although the multiplicity of actors and the confused environment can create problems of coherence, sustainability and consistency of approach. Collier was writing about capacity building very generally, but the point seems likely to apply to FTPA, and country experience, for instance in Liberia and Timor Leste, supports the proposition.
- Early in the natural resource cycle in a resource dependent state, when the allocation of ‘rents’ has not yet ossified. East Timor provides an example of the sort of advanced transparency around natural resource exploitation and fiscal policy that is possible early in the resource cycle.

### *Incentives and norm design*

In the fiscal transparency space there are, broadly speaking, at least five main types of norm systems, and these create different incentives for countries and decision-makers within countries. The five main types are:

- 1) Instruments that have the legal force of standards e.g. IPSASs, ISSAIs. These can have powerful and enduring incentives where compliance is assessed by an independent and competent domestic attestation body on a routine basis. IFAC and associated bodies promulgate international public sector accounting standards, international standards on auditing, operate a member body compliance program in-country, and

---

<sup>15</sup> Petrie, forthcoming.



provide adoption and implementation support. INTOSAI promulgates international standards for SAIs, and country practices are assessed by SAIs in each country.

- 2) Norms that generate a binary outcome: meets standard/fails to meet the standard e.g. EITI (and, beyond FTPA, ISO certification more generally). Depending where the bar is set, these can create strong incentives to improve performance for those countries that are currently just below the standard, or to maintain performance for countries at or just above the standard. However, if the bar is set too low, it may provide only weak incentives and could actually be counterproductive by legitimising weak performance and compromising efforts to improve performance. This has arguably been the case with EITI, where the standard has been set by consensus amongst participants.<sup>16</sup> In addition, for countries that are well below the standard, or that have already achieved it, binary systems produce weak incentives. They also fail to distinguish between a country that only just achieves the standard, and a country that exceeds the standard by a large margin – which limits the ability of information users to discriminate between good and strong performers (or alternatively, between weak and very weak performers).
- 3) Normative systems where country practices or outcomes are scored against carefully defined ordinal indices of performance across multiple dimensions, but which are not designed to produce a single aggregate score for a country, let-alone cross-country scores e.g. PEFA. These systems define practices from international good practice down to weak practices. They can be relevant for countries at all levels of performance, and can provide incentives for year-on-year improvements, although they may or may not produce strong incentives for any particular country. They are more ‘developmental’ in that by disaggregating performance levels they can make it clearer to a country and to external parties (such as donors) what practical steps need to be taken to improve performance to the next level. PEFA is in fact intended to facilitate dialogue between governments and their development partners over the design and implementation of PFM reforms.
- 4) Country rating systems, which aggregate quantitative scores across individual indicators to produce a composite country score and a ‘league table’ of country scores e.g. the OBI; sovereign credit ratings. To the extent that countries are motivated to improve their standing relative to other countries, this can produce quite strong incentives. Where a country’s rating is perceived to be linked to access to finance, or to regulatory requirements – as is the case with bond ratings - the incentives created can be powerful (see the evidence cited in Section IV). With respect to the OBI, while there is no clear evidence to date of a link between OBI scores and access to financing, there are aspects to the way in which the OBI is designed and delivered that are intended to increase its impact, including:
  - a. The Survey shows, in a practical way, specifically what each government would need to do to improve its score on most questions e.g. to score an ‘a’

---

<sup>16</sup> See ‘Evaluation of Extractive Industries Transparency Initiative’, Final Report, p. 48.

instead of a 'b' for timeliness of publication of the year-end report, a government would need to publish the report within six months of the end of the year, instead of 6-12 months.

- b. The Surveys for many countries demonstrate that the relevant information or data is already produced and is available within government, making it a relatively short step technically to place the data in the public domain.
  - c. The Survey results are released in regional events designed to generate peer pressure among neighbouring countries.
  - d. Governments that have improved their scores from the previous round(s) are recognized with favourable publicity, while poor or deteriorating performers are singled out for adverse publicity.
  - e. The IBP provides technical assistance to countries wishing to increase FTPA through a mentoring program.<sup>17</sup>
- 5) Systems that produce only a qualitative assessment of performance, or that incorporate only a general and imprecise rating of performance against individual elements in the norm but not an aggregate score e.g. the Fiscal ROSC post-2007. However, the potential linkages between the ROSC, IMF surveillance, IMF program design and conditionality, and IMF TA all represent possible mechanisms to leverage the incentive effects of the Fiscal ROSC. In addition, the Fiscal ROSC also has the potential to provide financial markets with a clearer indication of shortcomings in the coverage and quality of fiscal data, which could also leverage its incentive effects. The IMF is considering these issues in the context of updating the Fiscal Transparency Code and Manual and strengthening the Fund's relationship with other international standard-setters in 2013. Findings from a recent evaluation of ROSCs are discussed in Section IV. The Fund intends to adopt a more graduated, accessible, and risk-based approach to IMF evaluations of fiscal transparency practices.<sup>18</sup>

Strong incentives can be created when the requirement for an assessment or the outcome of an assessment of practices is used as part of a regulatory system. For example, the requirement for a minimum sovereign credit rating before institutional investors may invest in government bonds strengthens the incentive effects of credit ratings. The requirement in the Dodd-Frank Wall Street Reform Act for companies listed on the US stock exchange to

---

<sup>17</sup> See <http://internationalbudget.org/what-we-do/mentoring-gov-program/> The Mentoring Government Program's objectives are to: a) help governments identify and understand the specific information needs of CSOs and the public, particularly the poor; b) assist governments in their efforts to build information systems for disclosing information and to translate the budget information they produce into formats that the public can use to effectively monitor the budget process; and c) mentor government efforts to improve their relationships with nongovernmental actors and establish trust in the process and institutions, in order to encourage social participation and enhance the impact of policies, particularly those aimed at reducing poverty. A summary of the work that the Mentoring Government Program has done in the Dominican Republic, Egypt, El Salvador, Ghana, Guatemala, Honduras, Mali, Tunisia, and Zambia is available at the web site above.

<sup>18</sup> See IMF 2012, p. 36.

report detailed data on their payments to governments is expected to put pressure on governments to improve their reporting of natural resource revenues.

In the fiscal transparency space, an example of this kind of mechanism is:

- DfID's requirement that a PEFA assessment be undertaken before it will consider providing budget support. The EU is reportedly considering introducing a similar requirement.
- The World Bank's announcement in 2011 that the Bank will not lend directly to finance budgets in countries that do not publish their budgets.
- The IFIs also require that a country drawing on their resources submit to a safeguards assessment to ensure the member's resources are protected when lent to a government or central bank. However, a safeguards assessment is not in the public domain, although it could be.
- The California Retirement Pension Fund (CALPERS) at one point included an assessment of a country's fiscal transparency against the IMF FTC as an element in its investment criteria in deciding on country asset allocations.<sup>19</sup> It is not clear whether this is still the case, or whether any other private financial institutions are using fiscal transparency assessments in a similar way (although very recent anecdotal evidence suggests that some investment banks are using OBI data in some way as an input to their investment analysis).

Strong incentives can also be created when consumers are enlisted to make purchasing decisions on the basis of public policy causes. For example, some consumers respond to product certification stating that particular products have been produced in an environmentally sustainable manner. There might conceivably be scope in future to enlist this type of incentive mechanism with respect to FTPA, with a country's sovereign bonds being certified e.g. by a CSO; or even enlisting consumers to boycott products of companies headquartered in countries with weak FTPA practices e.g. where the rights to fiscal information or to public participation are seriously violated; or where fiscal policies impose serious damage on the environment (e.g. subsidies for greenhouse gas-producing activities, deforestation).

There is also the issue of who does the assessment of country practices. At one extreme, an international entity assesses practices on a regular or irregular basis, by invitation – or at least consent - from the authorities e.g. sovereign ratings; Fiscal ROSC; PEFA.

At the other extreme, the assessment is performed regularly as part of the standard operating procedure by a domestic entity e.g. the annual attestation audit by the Supreme Audit Institution, which assesses compliance with appropriations, and in the case of financial statements, compliance with applicable accounting standards.

---

<sup>19</sup> See Petrie 2003.

In between are assessments commissioned by external entities but incorporating some element of local involvement e.g. some PEFA assessments, EITI.

Depending on its nature, an external assessment can generate strong incentives if, due to its objectivity or authoritativeness, it is perceived by the government to impact on the perceptions of important actors e.g. financial market participants and investors, or, potentially, domestic oversight agencies such as the legislature, or the media and general public. However, an external assessment that receives little exposure domestically or in the public arena may have very little impact and therefore no incentive effect – unless it impacts on the decisions or behaviour of official actors such as donors or IFIs.

The desirability of internalising the norms, and ideally making them part of the standard operating procedures of actors within countries, suggests the desirability of assessments being conducted by domestic entities, not by external actors such as international organisations or international CSOs. The potential to internalise more of the fiscal transparency assessment process, through domestic multi-stakeholder processes or the SAI, should be investigated.

Some current norms and guidelines may be creating negative incentives for FTPA. For instance, rules for resolution of sovereign bond defaults provide that certain information provided by a debtor to a creditor committee, such as information on its economic program and financing proposals, should remain confidential. There are also restrictions on the type of information a debtor can publish ahead of an offering, associated with insider trading concerns.<sup>20</sup> There may well be good public policy reasons for these restrictions, but it may be worth reviewing them from an FTPA perspective. Interestingly, in a recent article in the Economist, the suggestion was made that ‘the tendency of investors to rely on ratings is reinforced by the privileged access that [rating] agencies have to information about issuers...It would help if regulators forced issuers of bonds and other rated securities to provide more public information.’<sup>21</sup>

Finally, it is necessary to consider the possibility of perverse incentives and ‘gaming’ of the FTPA system and FTPA assessments. The stronger the incentives created by a standard or norm, the stronger are the incentives to game the system. This can take the form of:

- Shifting fiscal activities outside the scope of the standard or norm
- Publishing data but hiding it in hard to access formats or disparate (and inactive) web sites
- Standard-shopping e.g. cherry picking the lowest hurdles across overlapping and inconsistent standards

---

<sup>20</sup> See Report of the Principles Consultative Group on 2012 Implementation of the Principles for Stable Capital Flows and Fair Debt Restructuring, Annex VI, Best Practices For Formation And Operation Of Creditor Committees, Institute of International Finance, Washington DC, October 2012.

<sup>21</sup> ‘Crisis in ratings land?’ The Economist, November 10, 2012, pp. 72-73.

- Under-funding fiscal oversight institutions

To the extent possible, these perverse incentive effects need to be recognized and allowed for in the design of a standard or norm at the outset.

For example, if the scope of FTPA was shifted from the government sector to the public sector, the ability of a government to shift fiscal activities outside the scope would be less – because private sector entities have much stronger incentives to resist interference in their operations or transfers of obligations to them without at least matching compensation.<sup>22</sup>

#### e) Information and communications technology

Finally, the coincidence in time of an upsurge in transparency-as-governance with the ICT revolution is not accidental. ICT changes should be seen as an important enabler of greater FTPA

On the supply side, ICT changes have greatly reduced the cost and increased the effectiveness of:

- a) Compiling and reporting fiscal data viz. new GFMS's in many countries.
- b) Publicly disseminating data and reports viz. the ubiquity of rapid low cost dissemination via web sites.
- c) Engaging directly with citizens over policy design and policy implementation viz. web surveys or feedback mechanisms, mobile phone reporting.

The impact of ICT - enabled citizen/government interaction is still in its early days, but the impact of a) and b) above is evident from the ninety four countries included in the 2010 OBI: 90% of all these countries' budget reports are on-line and only 10% are published in hard copy. Furthermore, these governments are producing internally 42% of all the reports they are not publishing, so that rapid gains in transparency are very easy from a technical and practical point of view if not politically. The potential here has been demonstrated by the rapid increases in their OBI scores achieved by countries such as Liberia, Mongolia and Uganda in recent years. On the demand side, ICT changes have greatly reduced the cost and increased the effectiveness of:

- a) Oversight and audit agencies interacting directly with CSOs and citizens.
- b) Citizens interacting directly with agencies delivering public services.
- c) Civil society organizations mobilizing and coordinating with each other within-country and trans-nationally.
- d) CSOs interacting directly with citizens.

The ICT revolution should therefore be viewed as a key enabler of increased FTPA. For a given level of incentives on governments and non-government actors to increase

---

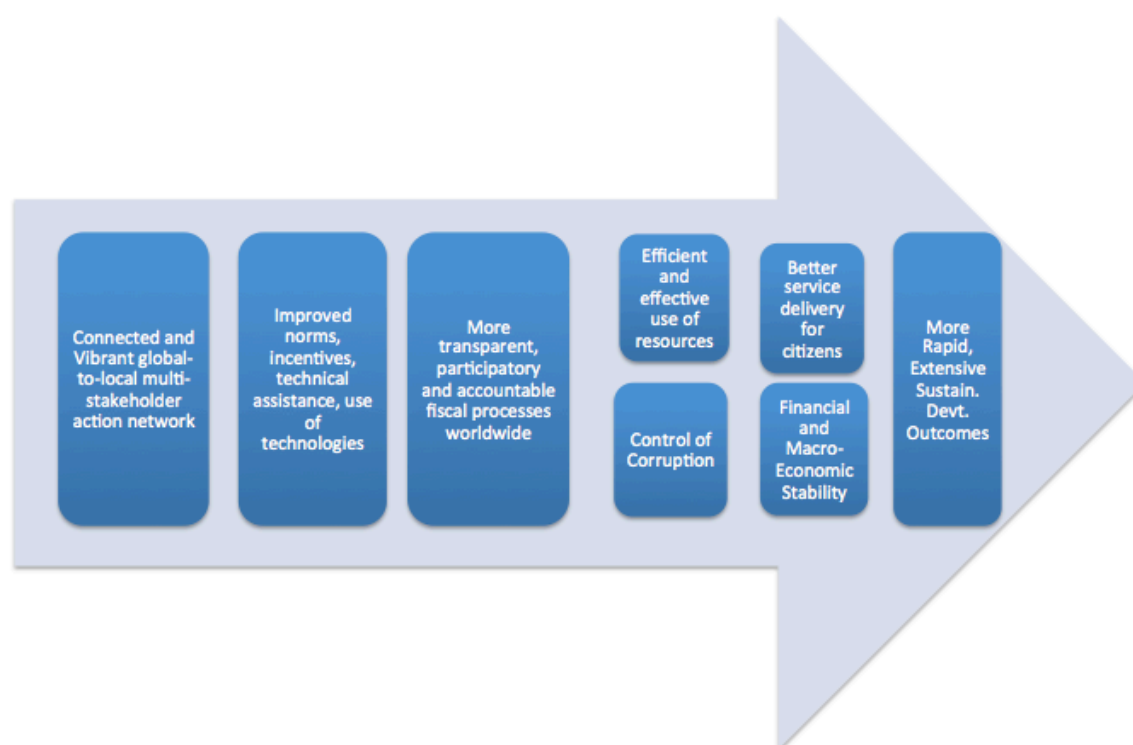
<sup>22</sup> IMF 2012, p.

transparency or to lobby for it, the ICT revolution is likely to have resulted in more FTPA activity, and seems likely to continue to do so.

#### **IV. How GIFT can strengthen incentives for fiscal transparency, participation and accountability**

##### *a) The GIFT Theory of Change*

Figure 3 presents the diagrammatic exposition of GIFT's theory of change.



**Figure 3: The GIFT theory of change**

Key components of the theory of change are:

- Global to local networks, recognizing that while global norms and external finance and pressures can play a role, ultimately the critical actions are at the country level. Empowering country level actors inside and outside government is a key lever for GIFT.
- A multi-stakeholder initiative (MSI), representing a recent innovation bringing together governments, international institutions, civil society groups and the private sector all aiming to increase FTPA in a specific sphere (e.g. EITI, CoST) or more generally (e.g. GIFT).

- Use of a mix of approaches, from standards and norm development and new approaches to the assessment of country practices; to technical support and capacity building for the implementation of transparency and accountability; use of new technologies as an enabler; and strengthening incentives for FTPA.

GIFT is now in the ‘launching’ phase of the life cycle of an MSI, and the key functions include developing an action agenda, and putting monitoring and learning mechanisms in place.<sup>23</sup>

Strengthening incentives has been viewed as a critical element of GIFT’s action agenda by many of GIFT’s stakeholders. As noted, this paper is intended to help develop an action agenda around incentives.

*b) Evaluative material on effectiveness of interventions aimed at increasing FTPA*

As noted in Section II, there is a relatively limited but growing body of empirical evidence on the impacts of policies and interventions aimed at increasing FTPA, that GIFT can draw on in developing an action agenda around incentives.

The main evidence is:

- The IMF’s recent review of fiscal transparency practices, standards, and assessments following the GFC (IMF 2012). The review focused on the first level of the outcomes hierarchy – the quality of the FTC and the fiscal ROSCs – rather than whether the ROSCs were used by external parties or had an impact on behaviour. It found that the GFC has revealed three main areas of shortcoming:<sup>24</sup>
  - First, fiscal transparency standards need to be updated to address gaps in and inconsistencies between those standards. In particular, the standards need to ensure that published fiscal reports (i) cover a wider range of public sector institutions; (ii) capture a broader range of direct and contingent assets and liabilities; (iii) recognize a wider range of transactions and flows; (iv) be published in a more timely manner; (v) take a more rigorous approach to fiscal forecasting and risk analysis; and (vi) present forecast and actual fiscal data on a consistent basis. Some standards also need to be supplemented by guidance on their implementation.
  - Second, the IMF needs to adopt a more modular, analytical, and calibrated approach to evaluating country compliance with fiscal transparency standards. Analysis of the Fiscal ROSCs for nine of the ten countries that experienced the largest increase in government liabilities during the GFC revealed a mixed record in identifying key problems – see Box 3. This requires revisions to the Fiscal Transparency Code and Manual, to provide a set of achievable milestones on the way to full compliance with those standards (a

<sup>23</sup> The four phases of an MSI have been characterised as catalysing; launching; enhancing; and transitioning.

<sup>24</sup> Copied from the Executive Summary of IMF 2012, p. 3.

graduated approach); a more focused and substantive fiscal ROSC catering for modular assessments focused on key areas, including an assessment of the quality of fiscal data, and providing a comparable and actionable final report.

- Third, national, regional, and international institutions need to strengthen incentives for improvements in fiscal transparency practices. This could be done by: (i) fostering national and regional constituencies for transparency, (ii) strengthening the institutional relationships among international standard-setters; and (iii) providing regular updates on the state of fiscal transparency practices across countries.

### **Box 3: The recent record of international monitoring by the IMF<sup>25</sup>**

The fiscal transparency ROSC's record in identifying problems that contributed to or exacerbated the fiscal impact of the GFC was mixed. Of the ten countries that experienced the largest increase in government liabilities during the crisis, nine had undergone a ROSC within the previous eight years. These reports identified some but not all of the key transparency problems revealed by the crisis. The reports were most effective in identifying inadequate coverage of fiscal reports, lack of medium-term fiscal forecasts, and weak controls over budget execution. However, issues such as the need for fiscal risk analysis to explore a broader range of output scenarios or better surveillance of exposure to financial sector risks were generally not explored. Even where shortcomings were identified, their relative seriousness was generally not quantified and they were not always given due prominence in the summary recommendations.

This and other evaluations of the ROSC program highlighted a number of shortcomings in the design of the fiscal ROSC itself that may have reduced its impact:

- the methodology is one-size-fits-all and makes no allowance for different levels of institutional capacity or economic development. This makes it difficult for countries at a lower level of observance to use the ROSC to chart a sequenced reform path from their current practice to the best practices set out in the Code and Manual;
- the assessment places equal weight on compliance with all elements of the Code and focuses on verifying the existence of formal institutions rather than validating the quality of their output. This gives the evaluation the flavor of a —box ticking exercise which can overlook examples of both good and bad informal practices and fails to distinguish between more or less serious deficiencies in terms of implications for the quality of published information;
- while the reports tend to be exhaustive and qualitative in presenting the results of the evaluation, they lack a clear and accessible summary of a country's performance both relative to the absolute standards set by the Code and to other comparable country groupings; and
- the recommendations are not always integrated into Article IV consultations and surveillance, nor always followed-up by the countries themselves. However, they often inform the setting of structural conditionality for countries with IMF programs.

<sup>25</sup> The material in this box is from IMF 2012, pp. 34-36.



In addition, the Fund noted that the fiscal ROSC did not benefit from an explicit link with access to IMF or other official external financing (although they were often an input to the design of structural conditionality in IMF programs). The paper also indicated that there was a good case to expand IMF TA, traditionally focused on the ministry of finance, to build capacity in independent national institutions that promote FTPA, including independent fiscal agencies, parliamentary budget and accounts committees, national statistics agencies, and SAIs.

- At an intermediate level in the causal chain, a number of governments have issued statements referring to their country's ranking on the OBI, or have indicated an intention to take action to improve their country's score on the OBI, or have implemented enhanced FTPA measures following an OBI assessment.<sup>26</sup> These include:
  - There appears to be a direct link between the OBS and the subsequent publication of Citizens' Budgets in Egypt, Mexico and Brazil.
  - In some countries, IBP technical consultants have produced first drafts of Citizen's Budgets that have subsequently been adapted and published by governments e.g. Guatemala, Honduras, and Mali.<sup>27</sup>
  - After the international and national releases of the 2010 OBS several governments committed to specific measures to increase budget transparency and participation in their country, including Afghanistan, Bulgaria, Guatemala, and Jordan.
  - The government of Guatemala agreed to receive TA from the IBP through the IBP Mentoring Governments Program. It took credit for earning a 2010 OBI score that was above the regional average for Latin America.
  - The governments of South Africa and Mexico have included in their budget documents statements referring to their country's OBI ranking.
  
- There is similar anecdotal evidence in support of a positive incentive effect of FTPA at sub-national level in Mexico, where the States' Transparency and Tax Information Availability Index (ITDIF), developed by the consultancy Aregional, and the State Budget Information Index, produced by the Mexican think tank IMCO, are the main points of reference for sub-national governments on the topic. In some cases, senior public servants have approached both organizations in search of guidance on how to improve their performance and position in the ranking.<sup>28</sup>
  
- In Kenya the re-election of an MP has been attributed to a significant extent to his pioneering opening of the books on expenditure from his constituency development

---

<sup>26</sup> See <http://internationalbudget.org/what-we-do/open-budget-survey/advocacy/government-responses/>

<sup>27</sup> See the summary of the IBP mentoring program in pilot countries at <http://internationalbudget.org/what-we-do/mentoring-gov-program/>

<sup>28</sup> Ethos Fundacion, Transparency of Tax Expenditure Reporting: The Mexican Case. October, 2012. Draft

fund.<sup>29</sup>

- In 2002 rating agency analysts were surveyed and interviewed on their knowledge and use of Fiscal ROSCs.<sup>30</sup> In response to a question on how significant an impact a fiscal ROSC had had on a country risk assessment, on a scale of 1-5 (1 indicating no impact, 5 indicating a major impact) the mean response was 2.3. Analysts said they would most like to see more quantitative data in fiscal ROSCs, and, to a lesser extent, a quantitative rating of fiscal transparency. This data is dated, however. It was compiled at the time when Fiscal ROSCs were being published at the rate of 10-20 per year. Since 2005, the number of Fiscal ROSCs has progressively fallen, and in 2011 there was only one published. There is a need to re-engage with rating agencies on their current needs for data and information on FTPA. Very recent anecdotal evidence suggests that some rating agencies and investment banks are using OBI data, but it is not clear how they are using it or how widespread this is.
- There is clear evidence that IFI conditionality can have strong impacts on country FTPA practices in specific circumstances. For example, Greece's program with the IMF and EU contained structural benchmarks on fiscal reporting. Substantial TA has also been provided, and there has been a significant improvement in Greece's fiscal reporting practices. This is true to a lesser extent in some of the other programs with European countries. Conditionality relating to FTPA has also featured in other programs, although there are no details to hand.
- It seems clear that the conditions attached to EC membership create strong incentives for changes to the legal framework regulating PFM, including fiscal transparency requirements, in order to attain the credibility of EU membership, be eligible to receive EC fiscal transfers, and to remain a member of the club. This applies both to the pre-accession phase, where candidate countries must progressively adopt the EC legal framework, and to members, where fiscal transparency requirements have been progressively strengthened as a result of the requirements of deeper economic integration. However, this form of incentive mechanism does not seem amenable to intervention by GIFT.<sup>31</sup>

---

<sup>29</sup> See <http://internationalbudget.org/publications/social-audits-in-kenya-budget-transparency-and-accountability/>

<sup>30</sup> Petrie 2003.

<sup>31</sup> At a shallow level of regional peer pressure, the IBP is working with the Collaborative African Budget Reform Initiative (CABRI) to support senior budget officials in four countries in defining specific plans for increasing FTPA, and in developing a wider constituency for reform in these countries.

### *c) The general literature on influencing policy outcomes*

In the absence of further evidence on the effectiveness of interventions promoting FTPA, one lens to view this issue through is that of the general international literature on influencing policy outcomes. Key lessons from that literature include:<sup>32</sup>

- The need for an explicit intent to influence, and defining explicitly at the outset what influence is being aimed at and how it will be achieved.
- The importance of persistence, including designing coherent programmes of related initiatives rather than unrelated isolated initiatives.
- Person-to-person communication in various forms as the primary channel for transmitting information and the results of research to policy-makers e.g. conferences, workshops, one-on-one meetings.<sup>33</sup>
- Communication and dissemination (including the need to build costs for these activities into project budgets, and recognition of the fact that informal relationships and contacts are often more effective in influencing policy).
- Capacity building, including capacity to communicate findings to decision-makers.
- A feeling of ownership by the target policy community.

Kingdon's agenda-setting model, which views the policy process as primarily a political process, has been influential and seems relevant to designing initiatives aimed at increasing FTPA. It is outlined in Box 4.

Kingdon's model points to specific elements as likely to be critically important to GIFT's ability to influence decisions to increase FTPA. These include:

- GIFT's ability to function as a trans-national policy entrepreneur, working to re-frame salient issues of the day as FTPA issues, and being ready to 'hook solutions to problems, proposals to political momentum'.

GIFT's claim to a hearing based on its perceived legitimacy and technical authority.

---

<sup>32</sup> See Carden 2004. Policy influence can be viewed as being on a continuum running from direct impact on a specific policy decision, at one end, to indirect influence through changing a prevailing paradigm, at the other end (Neilson, 2004). It is important to note that policy influence is not necessarily desirable; it depends on a value judgment about the nature of the policies being promoted by an individual or organisation. The ability to influence policy is also highly context-dependent, with different political systems, constitutions, public management systems, and the extent and nature of alternative sources of policy advice from inside and outside government all having independent impacts.

<sup>33</sup> Maxwell, cited in IDRC, 2004.

#### **Box 4: Kingdon's agenda setting model of influencing government policies**

Kingdon identifies the following means that policy entrepreneurs use to promote their proposals or ideas:

*Problems:* "getting people to see new problems, or to see old problems in one way rather than another, is a major conceptual and political accomplishment." Entrepreneurs try to do this by highlighting indicators through press releases, hearing testimony, speeches etc. They try to bring problems into the personal experience of important people by giving them a first-hand look. They make a point of generating feedback in the form of letters and visits to decision-makers.

*Policies:* entrepreneurs 'soften up' policy communities and the public (both specialized and general publics), often over a period of years, by getting them used to new ideas and building acceptance of their proposals, so that when the 'policy window' opens (often only for a short time), their proposals are ready to go.<sup>34</sup> The means they use to do this include introducing a bill into the legislature to get people talking; civil servant speeches; issuing of reports etc; and floating trial balloons e.g. testing out new ideas in a speech to see the reaction.

*Joining the streams:* entrepreneurs "hook solutions to problems, proposals to political momentum, and political events to policy problems." They seize crises as opportunities, fit their proposals to a new government's programme, and market their proposal as the solution to a newly prominent problem.

Policy entrepreneurs engage in both advocacy and brokerage. Kingdon identifies three qualities they need to possess:

- 1) A claim to a hearing, based on either expertise, an ability to speak for others, or an authoritative decision-making position.
- 2) A reputation for political connections or negotiating skill.
- 3) Probably most importantly, persistence. "Tenacity pays off".

## **V. Conclusions and Recommendations**

Because political economy lies at the heart of incentives for FTPA, the issues are inevitably messy and imprecise. There is a need to recognize the complexity of actor motivations and political context, the strength of inertial and opposing forces, and the difficulty both of achieving and of demonstrating results. The possibility of perverse incentives and gaming, of mechanistic compliance that is not internalised or sustained, and of unintended consequences, must be recognised. GIFT should not promise too much in terms of strengthening incentives for FTPA. On the other hand, neither should GIFT offer too little, nor be too vague about what it is trying to achieve in this area and how it intends to achieve it.

There are some macro-level, conjunctural factors supporting incentives for FTPA that suggest this is a time of real opportunity for major and sustained advances. These are the predominance of democratic regimes amongst the dominant powers and largest economies

---

<sup>34</sup> Lindquist, 2001, p. 19, has stated that, with respect to achieving policy influence: 'Readiness, rather than achieving impact with each event or study, may be a more important goal.'

(albeit allowing for the rise of China and of course Russia); the wave of transitions from closed regimes; and the ICT revolution as an enabler of both supply of and demand for greater FTPA.

In the other direction, elite dominance in democracies, the emergence of numerous hybrid regimes with mixes of openness and opacity (partial democratization) and the persistence of many non-democratic regimes continue to present formidable obstacles to FTPA. In addition, the GFC and its aftermath of fiscal austerity is creating strong incentives for fiscal obfuscation and gimmickry by governments. It is also leading to claims by governments that budgets of programs or institutions that ensure public access to official information cannot be maintained.

However, the GFC is at the same time demonstrating the critical importance of the ability of countries to win the trust of their citizens if they are to generate a social consensus around how to manage through a period of prolonged fiscal austerity and return to fiscal sustainability. And there is public anger that a lack of transparency was a major contributor to the GFC in the first place, and at the perceived inequity of bailing out bankers.

Beyond these broad considerations, the following appear as 'stylized facts' from the available evidence on incentives, windows of opportunity, and triggers that contribute to FTPA:<sup>35</sup>

- Fiscal crises.
- Major public sector corruption scandals.
- Political transitions and major regime changes including post-conflict situations.  
Democratic transitions, more specifically:
  - A motivated legislature with capacity.
  - Political competition on the basis of public policy platforms (generally political parties as opposed to the politics of personality, family or group).
  - An independent and active media.
  - An organized and vibrant civil society focused on FTPA.
- Sovereign borrowing on international bond markets.
- Broader private financial sector incentives, especially from investors of various kinds.
- International donor and aid practices that promote rather than undermine FTPA.
- Global norms and assessments of country practices against them, especially those that involve scoring and ranking of countries and that are authoritative and regular
- A perceived need for domestic and international legitimacy in terms of good governance and sound fiscal management generally, and often democratic practices and respect for human rights as well.

The importance of democracy, in turn, suggests that the electoral cycle, in which political parties regularly re-visit their agendas, is an important 'business-as-usual' opportunity

---

<sup>35</sup> These draw extensively on Khagram, de Renzio and Fung, forthcoming.

where political elites in some countries have incentives to be sympathetic to calls for more FTPA. This is second order, however, to democratic transitions or regime change.

Drawing on the assumed causal pathways, the empirical evidence, the 'stylized facts' on incentives, and the GIFT theory of change, a prioritisation matrix has been devised which arrays the strength of the incentive mechanism or channel in one dimension, and the ability of GIFT interventions to influence on the other dimension – see **Figure 4 (next page)**.

The highest potential priorities appear in segments 1 and 3 of the table, the correspondence of negative incentives, and of strong incentives respectively, with a clear ability of GIFT to influence.

Based on Figure 4, the following specific recommendations are put forward for consideration as priority areas for GIFT to focus on to strengthen incentives for FTPA, in the next 12 months to the end of 2013:

- 1) **The Open Government Partnership:** the essential challenge of the incentives issue - of executives imposing FTPA requirements on themselves - points to the great potential of the OGP as a mechanism for GIFT to work with to achieve shared objectives. The OGP is a self-selected group of fifty seven governments that have committed themselves to improvements in openness, and to involving civil society in the design and monitoring of their commitments, in order to enhance domestic and international legitimacy.<sup>36</sup> Forty one of these countries have committed themselves to specific initiatives on fiscal transparency and participation.<sup>37</sup> GIFT Lead Stewards are leaders in the OGP. If the OGP had not been invented, GIFT could only have dreamt of such an opportunity! On the other side of the coin, GIFT can help OGP leverage its resources through providing TA to help OGP governments implement their FTPA commitments; building a community of practice amongst OGP governments; and working with countries ineligible to join OGP to meet the FTPA eligibility criteria.

---

<sup>36</sup> As at 26 October 2012, 47 countries have delivered (i.e. indicated) their OGP commitments and 10 are developing their commitments. Source: OGP web site, <http://www.opengovpartnership.org/countries?page=4>

<sup>37</sup> A quick analysis of these commitments by Randall Kemp (iScale) suggests the following areas of commitment: Procurement 12 countries; Citizen Participation 11; Extractive Resources 9; Foreign Assistance 8; Public Servant Assets 8; "Portal" 7; Expenditures 7; Tax Information 7; Contracts/Tenders 6; Generic Transparency 6; Publish Budget 6; Citizen Budget 5; Sub-National Transparency 5; Unified Information System 5; Monitor Transparency 4; Budgets for NGOs 3.

**Figure 4: GIFT Incentives Prioritization Matrix**

*Strength of incentive mechanism or channel*

<i>Amenable to short term influence by GIFT?</i> <sup>38</sup>	Negative	Moderate	Strong
Yes	(1) *Weak oversight institutions *Weak civil society *Weak media *Gaming of FTPA assessments *Standard shopping	(2) *Standards convergence *New FTPA norms *UNGA declaration/G20 *Legislative oversight *Communication with key decision makers *FTPA TA *FTPA ICT-take up *Evidence of FTPA impacts	(3) * The OGP * Sovereign bond market *FTPA country league tables *Authoritative, comparative, regular FTPA assessments of fiscal data quality *Concern over social equity and human rights
Maybe	(4) *Fiscal austerity (gimmicks) *Corruption *Under-funding of oversight institutions	(5) *Fiscal austerity (build credibility) *Donor conditionality *Business and other financial markets *Scope of FTPA Reforms (wide public impact v technocratic) *General PFM reform and capacity building	(6) *IFI conditionality *Media pressure *Prestige of individ. leaders *Internalization via domestic independent FTPA assessments *Central governments impose FTPA on SNGs *Use of bond rating as regulatory mechanism *Concerns over environmental outcomes *Regulation of sovereign bond market?
No  (but GIFT can be ready when opportunities arise)	(7) *Autocratic regimes *Elite capture *Culture of secrecy *Business/political networks	(8) *Prominence of FTPA norms	(9) *Characteristics of elites *National context *Agenda-setting circls. (regime change, crises, post-conflict) *Political pluralism * Deep regional trade agreements

<sup>38</sup> Amenable to influence by GIFT is assessed against a time frame of up to, say, 3 years, which in this field of deep institutional change, should be regarded as the short term. The medium term might be approximately 4-10 years, and the long term 10-20+ years.

- II) **The sovereign bond market channel (and the private financial sector and wider private sector):** The solid evidence in support of countries being rewarded for fiscal transparency with higher ratings and lower spreads, the large number of sovereign borrowers, and the widespread concerns over fiscal sustainability and transparency post-GFC all point to this as an area of significant unexploited potential. There is also evidence of potential in the broader financial sector and private investment and business channels.
- III) **The standards and norms agenda:** while there is as yet little robust statistical evidence of an impact of FTPA norms and assessments on country practices, there is sufficient case-study and testimonial evidence of an effect on key decision makers through instruments such as the IMF Code, the OBI, and of an indirect impact through, for example, the strengthening of civil society and the financial market channel, to justify high priority being given to GIFT's norms agenda.
- IV) **Communicating the urgency of FTPA to officials and the general public:** the literature on influencing public policy outcomes suggests the need to bridge the gap between the 'technical policy wonks' and decision makers in the executive and legislative branch, both directly, and via the actors that decision makers listen to (citizens/voters, the media, business, and CSOs).

These four priority areas are intended to comprise a coherent and mutually-supporting package. There are close interconnections between the OGP agenda, the norms agenda, and GIFT's TA and ICT initiatives. There are also links between the financial market and norms agendas, while the communication agenda has the potential to reinforce and leverage all of GIFT's activities.

Suggested action agendas to implement these four priority areas are as follows:

**The Open Government Partnership:**

- a Submit a formal proposal to the OGP for a GIFT-OGP Community of Practice on FTPA.
- b Work intensively with the Co-chairs of OGP for 2013 (Indonesia and the U.K.).
- c Work with the OGP and selected individual OGP governments and CSOs to design, implement and monitor their FTPA commitments.<sup>39</sup>

---

<sup>39</sup> The need to support the introduction of FTPA by ministers and ministries of finance, planning and budget and potentially legislatures, suggests it could be worth considering going outside normal aid channels and attempting to broker direct technician-to-technician interactions with OGP countries, for example through MOF-to-MOF cooperation (e.g. twinning relationships), and inter-parliamentary relationships. Innovative mechanisms could be considered, such as by giving a reformist minister of finance more control over the TA budget rather than the usual mediation through aid agencies with the risk of supply-driven activities. There



- d Explore the possibility of the OGP formally endorsing the GIFT HLPs.
- e Identify and invite non-OGP countries as candidates to work with on meeting the OGP FTPA eligibility criteria.
- f Assess the possibility of trialling GIFT-developed FTPA instruments in a selected OGP country(s), such as the Participation Guide.<sup>40</sup>
- g Use the OGP as a means to expand the number of governments that are stewards of GIFT.
- h Create a direct link between the OGP and GIFT's capacity building, ICT, and norms agendas.

**The sovereign bond market/financial sector actors:**

- a Conduct interviews with rating agencies, investors of various kinds, and governments to gather evidence and ideas about their perceptions and practices, followed by an event to engage these actors in GIFT incentives work. WEF has already agreed to co-host this meeting, and the Institute of International Finance has also been engaged.
- b Aim to generate a better understanding of what rating agencies and financial sector actors are looking for in fiscal transparency assessments, and incorporate this both in the design of normative instruments and in the assessment of country practices.
- c Assess the scope for altering practices of financial actors players to strengthen FTPA incentives. If scope exists, translate into an action-agenda in partnership with champions in these sub-sectors.
- d This agenda should be coordinated with the IMF's review, over the same time period, of the Fiscal Transparency Code and ROSC, an important target 'market' for which is likely to be financial market participants; and with the review of the OBI, and PEFA.

**The standards and norms agenda:**

- a Complete a further version of the Expanded HLPs.
- b Develop the Guide on Public Participation in Fiscal Policy and trial it in 2013: synthesize and generate evidence, experience and lessons; assemble a multi-disciplinary working group of GIFT stewards, and demand and supply-side budget actors to engage on the issue; and consult with a broad range of stakeholders.
- c Develop the Guide on Legislative Oversight of Fiscal Policy: seek collaboration with Inter-Parliamentary Union and other global and regional parliamentary bodies; consult with experts and stakeholders; develop the Guide through building relationships with other actors in the field in 2013.

---

may also be a role for GIFT to broker or disseminate emerging new practices in the use of ICT to promote FTPA in selected OGP countries.

<sup>40</sup> The Guide on Legislative Oversight of Fiscal Policy might potentially be trialled if developed sufficiently during 2013.

- d Continue to explore with relevant actors the possible development of an open data standard.
- e Explore the possibility of mutual recognition of elements of normative instruments, and of coordinated or joint assessments of practice against norms.
- f Provide input into reviews of existing norms (chiefly the IMF Fiscal Transparency Code and ROSC; the OBI and OBI Plus; and PEFA) to increase their incentive effects (including through introducing a more graduated and quantitative approach); facilitate discussion and coordination between standard setters to reduce inconsistencies and promote convergence; promote the strengthening of FTPA databases, monitoring, evaluation, and research.

**Communicating the urgency of FTPA – Global Political Agenda-Setting:**

- a More officially launch GIFT at the WB/IMF Annual Meetings in April and/or UN Meetings in September.
- b Legitimization and universalization of the HLPs through an UNGA declaration; and through promotion via key global groupings such as the G20.
- c Engage communications experts to help produce popular versions of the HLPs, and then the Expanded HLPs.
- d Revise and develop a popular version of the ‘killer facts on fiscal transparency’.
- e Progressively build relationships with the media, and develop a communications strategy for 2014 and beyond.

An implication of the above agenda is that there is a need to increase the tempo of GIFT activity. This is likely to require both increased engagement from Stewards and their organisations, and a need for each GIFT Working Group to start holding at least one virtual meeting in between the Stewards meetings.

Stewards should also review whether the current number and configuration of Working Groups is fit for purpose given the new action agenda.

For the following 12 month period (January to December 2014), depending on developments and progress, GIFT priorities for strengthening incentives could be:

- I. Following through on and deepening of the OGP initiative, and approaching additional non-OGP governments.
- II. Norms: disseminate the new norms on public participation, and on legislative oversight through enlisting champions and finding institutional ‘homes’ for them, and supporting their implementation through capacity building; build a technical coalition to develop a norm on fiscal policy and environmental issues; promote mutual recognition of FTPA assessments between institutions; explore possible leveraging of FTPA assessments through linkage with donor financing, and financial

market channels; and explore the possibility of internalising parts of FTPA assessment through domestic mechanisms.

- III. Further develop the relationships with the media, and with academics: encourage investigative journalism on FTPA; over time aim to achieve consensus and internalise a 'policy narrative' around FTPA.<sup>41</sup>
- IV. Assess the possibility of instituting personal incentives for ministers of finance or prime ministers/presidents leading FTPA reforms e.g. 'The Peoples' Minister of Finance of the year.' Create a prize for FTPA Leadership.

#### **V. Proposed decisions by GIFT Stewards**

It is recommended that Stewards:

- 1) Endorse the four priority areas for GIFT action on strengthening incentives in 2013, as outlined on pp. 38-40, as being central to the rationale and motivation for GIFT.
- 2) Discuss and decide on the recommended action agendas to implement the four priorities put forward on pp. 40-42.
- 3) Review whether the current Working Group structure and process are fit for purpose given the new action agenda.
- 4) Discuss and decide in principle on the possible six priority areas for 2014 (pp. 42-43) as a basis for planning, and for review in the light of developments during 2013.

---

<sup>41</sup> 'Policy narratives' are stories describing in highly simplified form how very complex policy processes work in a specific setting, that have attained the status of conventional wisdom (even in the face of conflicting evidence), and that help to underpin the assumptions used in decision-making. An example cited is that of "the tragedy of the commons." See Neilson, 2001, pp. 37-40. Pollard and Court, 2005, suggest that civil society organisations can influence agenda setting by crystallising a body of evidence as a policy narrative to create a window for policy change.

## References

- Acemoglu, Daron and James Robinson, 2012. *Why Nations Fail*. Crown Business New York.
- Alt and Lassen, 2006. *Fiscal transparency, political parties, and debt in OECD countries*. *European Economic Review*, Elsevier, vol. 50(6), pp. 1403-1439, August.
- Beath, Christia, and Enikokpov, 2012. *Direct Democracy and Resource Allocation: Experimental Evidence from Afghanistan*. World Bank Policy research Working Paper 6133, July 2012.
- Benito and Bastida, 2009. *Budget Transparency, Fiscal Performance and Political Turnout: An International Approach*. *Public Administration Review* 69(3): 403-417.
- Bernoeth and Wolff (2008)
- Carden F, 2004, *Issues in assessing the policy influence of research*, available on the web site of the International Development Research Centre, [www.idrc.ca/evaluation](http://www.idrc.ca/evaluation)
- Collier, Paul, 2007. *The Bottom Billion: Why the Poorest Countries are Failing and What Can Be Done About It*.
- Dabla-Norris, E., and others, 2010. *Budget Institutions and Fiscal Performance in Low-Income Countries*. IMF Working Paper No. 10/80. Washington: International Monetary Fund.
- EITI Evaluation Report... 'Evaluation of Extractive Industries Transparency Initiative', Final Report,
- Finnemore, M. and K. Sikkink, 1998. *International Norm Dynamics and Political Change*. [International Organization](http://www.internationalorganization.org) / Volume 52 / Issue 04 / September 1998, pp 887-917.
- Fukuda-Parr, Guyer and Lawson-Remer, 2011. *Does Budget Transparency Lead to Stronger Human Development Outcomes and Commitments to Economic and Social Rights?* IBP Working Paper Number 4: December 2011.
- Fung, Graham, Weil, and Fagotto, 2005
- Gelos, R. Gaston and Shang-Jin Wei, 2002. *Transparency and International Investor Behavior*. International Monetary Fund, IMF Working Paper 02/174. October 2002.
- Glennerster and Shin, 2003. *Is Transparency Good for You and Can the IMF Help?* IMF Working Papers 03/132, International Monetary Fund, Washington.
- Grindle, M and J. Thomas, 1991. *Public Choices and Policy Change: The Political Economy of Reform in Developing Countries*.
- Hameed, Farhan, 2011. *Budget Transparency and Financial Markets*. IBP Working Paper Number 1: December 2011.

Hameed, Farhan, 2005. *Fiscal Transparency and Economic Outcomes*. IMF Working Paper 05/225, International Monetary Fund, Washington.

Hashimoto, Yuko and K. Wacker (2012). *The Role of Risk and Information for International Capital Flows: New Evidence from the SDDS*. IMF Working Paper WP/12/242.

Institute of International Finance, 2012. *Report of the Principles Consultative Group on 2012 Implementation of the Principles for Stable Capital Flows and Fair Debt Restructuring*. Annex VI, Best Practices For Formation And Operation Of Creditor Committees. Washington DC, October 2012.

International Budget Partnership, undated. <http://internationalbudget.org/what-we-do/open-budget-survey/advocacy/government-responses/>

International Development Research Centre, (IDRC), 200. *Snapshots: Making the Most of Research*, from "Research Influence on Policy: A Forum", June 21, 2004, Ottawa, Canada, available at [www.idrc.ca/evaluation](http://www.idrc.ca/evaluation)

International Monetary Fund, 2012. *Fiscal Transparency, Accountability, and Risk*. August 7, 2012.

International Monetary Fund, 2008. *Fiscal Risks: Sources, Disclosure, and Management*. Cebotari, Davis, Lusinyan, Mati, Mauro, Petrie, and Velloso.

Islam, R, 2003. *Do More Transparent Governments Govern Better?* World Bank Policy Research Working Paper 3077. Washington, DC: World Bank.

Kaufman, D and A. Bellver, 2005. *Transparenting Transparency: Initial Empirics and Policy Applications*. World Bank Policy Research Paper. Washington DC: World Bank.

Kingdon, J, 2003, *Agendas, Alternatives, and Public Policies*, Longman, New York, Second Edition.

Khagram, de Renzio and Fung, forthcoming. *The Political Economy of Fiscal Transparency, Participation and Accountability*.

Lindquist, E, 2001, *Discerning Policy Influence: Framework for a Strategic Evaluation of IDRC-Supported Research*, available on the IDRC web site at [www.idrc.ca/evaluation](http://www.idrc.ca/evaluation)

Litovsky, Alejandro. *Assessment of an Incentive Regime for Fiscal Transparency*. Final Report, 5 December, 2011. GIFT.

Lowry and Alt (2001). *A Visible Hand? Bond Markets, Political Parties, Balanced Budget Laws, and State Government Debt*. Economics and Politics, 13 (1), pp.49-72.

McGee, Rosemary and John Gaventa, 2010. *Review of Impact and Effectiveness of Accountability and Transparency Initiatives: Synthesis Report*. Institute of Development Studies, October 2010.

Neilson, S, 2001, *Knowledge Utilization and Public Policy Processes: A Literature Review*, IDRC Evaluation Unit, December 2001, available at [www.idrc.ca/evaluation](http://www.idrc.ca/evaluation)

Petrie, M, forthcoming. *Public investment management reform: a synthesis of country experiences*. Chapter 3 in 'Investing to Invest: Building the Foundations for Effective Public Investment Management', World Bank.

Petrie, M, 2003. *Promoting Fiscal Transparency: The Complementary Roles of the IMF, Financial Markets and Civil Society*. IMF Working Paper WP/03/199.

Pollard, A, and Court, J, 2005. *How Civil Society Organisations Use Evidence to Influence Policy Processes: A literature review*, Overseas Development Institute, London, July 2005.

Poterba, J, and K. Rueben, 1999. *State Fiscal Institutions and the U.S. Municipal Bond Market*.

Robinson, M, 2006. *Budget Analysis and Policy Advocacy: The Role of Non-governmental Public Action*. IDS Working Paper 279. Brighton, UK: Institute of Development Studies.

Sikkink and Khagram, 2002. *Restructuring World Politics – Transnational Movements, Networks and Norms*.

Weber, Anke, 2012. *Stock-Flow Adjustments and Fiscal Transparency: A Cross-Country Comparison*. IMF Working Paper No. 12/39. Washington: International Monetary Fund.

Wehner, J, and Paolo de Renzio, 2011. *Citizens, legislators, and executive disclosure: The political determinants of fiscal transparency*. IBP Working Paper Number 3; December 2011.

**Annex 1:** Fiscal transparency, participation and accountability: assumed causal pathways, indicators and evidence

[separate file]

## **Annex 2: Brief summaries of empirical evidence**

Alt and Lassen (2006): use a career concerns political economy model to show that fiscal transparency reduces public debt and deficits, even after controlling for political variables like common law history, political competition, and presidential system.

Beath, Christia and Enikolopov (2012): Used RCT across 250 villages in Afghanistan to compare the outcomes from secret ballot referenda against normal community consultation processes. Found that elites exert influence over consultation outcomes but not referenda outcomes, which are driven primarily by citizen preferences. Referenda are also found to improve public satisfaction and legitimacy.

Benito and Bastida (2009): the authors build a comprehensive index of budget transparency encompassing 40 budget features based on international standards for a sample of 41 countries. They find a positive relationship between national government fiscal balance and budget transparency: The more information the budget discloses, the less the politicians can use fiscal deficits to achieve opportunistic goals. They also find evidence that greater budget transparency is associated with higher voter turnout.

Bernoth and Wolff (2008): using three different measures of transparency, find that fiscal transparency reduces risk premia while creative accounting increases the spread. The increase in risk premium is stronger if financial markets are unsure of the true extent of creative accounting.

Dabla-Norris, and others (2010): This paper presents multi-dimensional indices of the quality of budget institutions in low-income countries. The indices allow for benchmarking against the performance of middle-income countries, across regions, and according to different institutional arrangements that deliver good fiscal performance. Using the constructed indices, the paper provides preliminary empirical support for the hypotheses that strong budget institutions help improve fiscal balances and public external debt outcomes; and countries with stronger fiscal institutions have better scope to conduct countercyclical policies.

Fukuda-Parr et al (2011): found that countries that exhibit high levels of budget transparency also tend to achieve positive development outcomes, realize the economic and social rights of their citizens more fully, and to be more democratic. However, the regression analysis shows that, when differences in per capita income and region are held constant, budget transparency retains a significant statistical association with only a few variables, namely infant and child survival, the percentage of the population using improved drinking water, and public health expenditure levels.

Gelos and Wei (2002): using various indices of government and corporate transparency, show



that emerging market equity funds hold fewer assets in less transparent countries, and herding among funds is somewhat less prevalent in more transparent countries.

Glennerster and Shin (2003): find that sovereign spreads decline following the adoption of transparency-related reforms such as publication of IMF country surveillance reports as well as release of various reports on compliance with standards.

Hameed, (2011): using 2008 OBI data, the paper finds that more transparent countries, after controlling for various economic variables, have higher credit ratings and lower spreads. Further, for countries with similar credit ratings, higher transparency is associated with lower spreads. Limited evidence is found that more transparent countries are less likely to be downgraded given excessively high spreads. Finally, the change in spreads is smaller for more transparent countries compared to less transparent countries.

Hameed (2010): using OBI 2008 data, the paper finds that budget transparency matters for financial markets. In particular, more transparent countries, after controlling for various economic variables, have higher credit ratings and lower spreads. Further, for countries with similar credit ratings, higher transparency is associated with lower spreads. There is limited evidence that more transparent countries are less likely to be downgraded given excessively high spreads. Finally, the change in spreads is smaller for more transparent countries compared to less transparent countries.

Hameed (2005): finds that after controlling for other socio-economic variables, more transparent countries have better credit ratings.

Hashimoto (2012): investigates whether better information about the macroeconomic environment of an economy has a positive impact on its capital inflows (portfolio and FDI). For FDI, finds statistically significant and robust support for this hypothesis: SDDS subscription increased inflows by an economically relevant magnitude of about 60 per cent. It is not clear what role the publication of fiscal data had here, as fiscal data is one of four macroeconomic data sets incorporated in the SDDS.

IMF 2008 Fiscal Risks (2008): fiscal transparency, particularly fiscal risk disclosure, is associated with better sovereign bond ratings and greater access to international capital markets. The estimated coefficients on fiscal risk disclosure suggest that countries moving from no disclosure of macrofiscal risks, contingent liabilities, and quasi-fiscal activities to providing even partial information on all these areas would improve their credit ratings on average by a full notch (e.g., from Baa1 to 3A on Moody's ratings).

Islam (2003): finds evidence that greater budget transparency is associated with better quality governance.

Kaufman and Bellver (2005): find evidence that greater budget transparency is associated with better socio-economic and human development indicators, higher competitiveness, and

reduced corruption.

McGee, Rosemary and John Gaventa (2010): This report distils findings from reviews of transparency and accountability initiatives (TAIs) in the areas of public service delivery, budget processes, freedom of information, natural resource governance and aid transparency. The evidence base on these initiatives' effectiveness is weak, uneven, and sometimes contradictory. While few meta-level studies exist, micro-level studies suggest that in some conditions, TAIs can contribute to positive outcomes. Success factors seem to include coalitions of both state actors and citizens that bridge the demand and supply sides of accountability. It is important to understand accountability and transparency not only as formal mechanisms, but as relationships involving power dynamics across state and society.

Petrie (2003): on the basis of surveys of and interviews with rating agency analysts, found considerable use of IMF Fiscal ROSCs. Also found use of ROSCs by some in the US international investment community (but not outside the US); and some other evidence of market demand for information on fiscal transparency.

Poterba and Reuben (1999, 2011): consider the impact of fiscal institutions on US municipal bond interest rates. Their findings suggest that institutions matter i.e. fiscal institutions affect interest rates beyond their indirect effect through fiscal outcomes. Similarly, Lowry and Alt (2001) observed that fiscal institutions in American states have an impact on bond rates.

Robinson (2006): in a study of six organisations in six countries CSOs were found to have been effective in interpreting and disseminating budget information to enable broader civil society and other actors to engage with the budget process in more meaningful ways, and impacted on the level of pro-poor allocations and results.

Wehner and de Renzio (2011): Empirical evidence on the beneficial effects of fiscal transparency ranges from improved budgetary outcomes, to lower sovereign borrowing costs and decreased corruption. Despite this, hardly any effort has been invested in exploring the determinants of fiscal transparency. Using a new 85-country dataset, we focus on two important sources of domestic demand for open budgeting: citizens and legislators. Our results suggest that free and fair elections have a significant direct effect on budgetary disclosure, and that they dampen the adverse effect on fiscal transparency of dependence on natural resource revenues. We also find that partisan fragmentation in the legislature is associated with higher levels of budgetary disclosure.

# Annex 3: The Political Economy of Policy Reform

Figure 8.1, Grindle and Thomas 1991.

