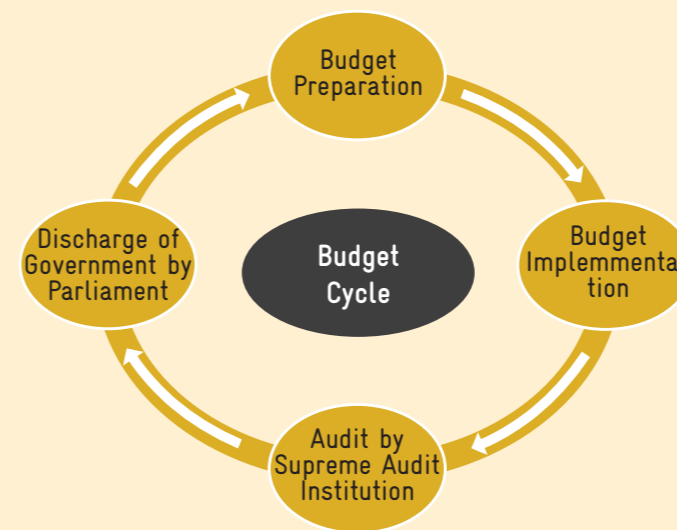


# Public Financial Management in the South Caucasus

Targeted, effective and transparent use of public funds



Commissioned by: German Federal Ministry for Economic Cooperation and Development (BMZ),  
European Union (EU) in Armenia  
Partners: ministries of finance, parliaments, supreme audit institutions  
Current commission: April 2017 to March 2020  
Budget: EUR 5.75 million, including EUR 1 million provided by the EU  
Countries: Armenia, Georgia



## ◀ An example from the field – how we achieve results:

Internal financial control is a key area of public policy reform in the South Caucasus. Facilitated by the project, the finance ministries of Armenia and Georgia have therefore jointly drawn up a plan of action for the introduction of a concept for European standards in this field – – the Public Internal Financial Control (PIFC) system. As a result of implementing the plan of action, the following results have been achieved since 2014:

PIFC has been enshrined in law as an instrument for the independent and objective auditing of public institutions. Thirteen pilot audits have been carried out on the basis of the new standards. The findings have led to more detailed market analyses ahead of public procurements, to procurement control reforms, and to the optimisation of internal processes. The lessons learned from the pilot audits have been discussed with other public institutions in order to maximise impact across the public administration apparatus. Georgia's guidelines for system audits were adapted to the Armenian country context and are now being used by internal auditors in Armenia.

## ◀ Challenges:

To be able to provide their citizens with public services, Armenia and Georgia need to raise, use and control public funds fairly, efficiently and transparently as well as in a results-oriented manner. To ensure this foundation for a viable relationship between citizens and the state, our partners are currently undergoing a complex transformation process that affects fundamental aspects of the interplay between government, parliament and supreme audit institution in the budget cycle.

## ◀ Objectives:

The objective is to align the use of public funds more closely with national development strategies by introducing European and international standards while maintaining transparency and efficiency and improving accountability.

## ◀ Activities:

We are advising our partners on introducing results-oriented budget management, on improving internal, external and parliamentary control mechanisms, as well as on taxation and customs regulations. European standards are the yardstick. To help make the change process sustainable, we are training the actors involved and fostering cooperation between the key stakeholders.

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For the first time in its history, the Georgian parliament has systematically debated 18 State Audit Office audit reports in a rule-based process since 2013. 13 of these reports were performance audits, five of which were supported by the project as an on-the-job training measure.

900 employees of public institutions in Georgia and Armenia have been trained in effective revenue management, results-based expenditure management, and external and parliamentary financial control. They are now contributing towards a transparent and results-based use of public funds in the two countries.

Also in Georgia, a model for negotiating double taxation agreements was developed (based on OECD rules) that has already been used to negotiate or renegotiate five agreements. The model also strengthens Georgia's position in such negotiations as well as the application of international standards.

## Results: ➡

The most recent constitutional reform in Armenia provides for an amendment to the definition of roles and responsibilities of the Government, Parliament and Chamber of Control (CoC) in the budget cycle, bringing them into line with international standards. These changes are to be incorporated into Armenia's new law on the CoC.

The Armenian Parliament has decided to make a complete switch to a results-based budget. The Government, Parliament and CoC have agreed on a joint implementation strategy for the period to 2018.

## Our contribution in Georgia

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Partners: Ministry of Finance, Parliament, State Audit Office

#### ◀ A country-specific example

*One work stream involves advising on the performance audits of public institutions conducted by the State Audit Office. In this regard - among others - the National Forestry Agency was audited in 2015 in close consultation with the German development cooperation project 'Integrated Biodiversity Management, South Caucasus'. Methodological support was provided by a staff member from Germany's supreme audit institution, the Bundesrechnungshof.*

*The audit results identify deficits in the current practice of awarding timber concessions, which are impacting negatively on the national budget and causing environmental damage in Georgia. The audit report was discussed in Parliament. The recommendations made in the report are now being implemented by the audited body, the Ministry of Environment and Natural Resources Protection. In the biodiversity project, these recommendations are being used to jointly identify key areas of forest sector reform, such as the revision of legislation relating to forests.*

#### ◀ Intervention area: Accountability

- » The project is supporting the State Audit Office in introducing performance audits and improving the quality of reporting. Through dialogue forums, Parliament is also being made more keenly aware of its role when cooperating with the State Audit Office. This support has helped increase the number of Audit Office reports discussed in parliament from one in 2013 to the current total of 18, 13 of which were performance audit reports.
- » The independence of the State Audit Office is also being enshrined in law with the help of legal advice, and has been underpinned by the revision of Georgia's State Audit Office Law (Article 35).
- » With regard to results-based budgeting, the project is supporting the development and application of a methodological approach for programme budgeting. This has resulted in substantial progress regarding the definition of objectives and indicators for the programmes, as confirmed by Transparency International Georgia in its 'Brief Assessment of the 2016 Budget'.
- » Concerning the public internal financial control (PIFC) approach, the project is supporting coordination of the reform process, as well as the conduct of training measures and pilot audits. These measures have provided training for more than 50% of the country's internal auditors. As a result, two of the three pillars of the PIFC approach have been successfully implemented, namely the establishment of a Central Harmonisation Unit at the Ministry of Finance and a sound internal auditing system in the sectoral ministries.

#### ◀ Intervention area: Public financial management reforms

- » The project supported a customs policy reform provided for in the EU Association Agreement by drafting new customs legislation. Independent reports by the EU note that extensive progress has been made in this area.



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