Framework Paper

Enhancing Capabilities of Central Finance Agencies: From Diagnosis to Action

Bjoern Dressel and Jim Brumby

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ABBREVIATIONS AND ACRONYMS

AAA	Analytical and Advisory Activities
CFA	Central Finance Authority
CFAA	Country Financial Accountability Assessment
CPAR	Country Procurement Assessment Review
CPIA	Country Policy and Institutional Assessment
DFID	Department for International Development (UK)
EBF	Extra-Budgetary Funds
ESW	Economic and Sector Work
GAC	Governance and Anti-Corruption
IDA	International Development Association
IDB	Inter-American Development Bank
IFI	International Financial Institution
IFMIS	Integrated Financial Management Information System
IMF	International Monetary Fund
IT	Information Technology
LAO	Limited Access Order
MIC	Middle Income Country
MOE	Ministry of Economy
MOF	Ministry of Finance
MTEF	Medium-Term Expenditure Framework
OAG	Office of Auditor General
OAO	Open Access Order
ODI	Overseas Development Institute
PAC	Public Accounts Committee
PEFA	Public Expenditure and Financial Accountability
PER	Public Expenditure Review
PETS	Public Expenditure Tracking Survey
PFM	Public Financial Management
PIM	Public Investment Management
PPP	Public Private Partnership
PRSP	Poverty Reduction Strategy Paper
PSM	Public Sector Management
ROSC	Reports on the Observance of Standards and Codes
SAI	Supreme Audit Institution
SWAp	Sector Wide Approach
UNDP	United Nations Development Programme

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I. INTRODUCTION

Central Finance Agencies (CFA) of countries are pivotal to the Public Finance Management (PFM) reform process. Thus, the capabilities - not just capacities - of CFAs are critical to bringing about transformation. Strengthening CFA capabilities, and thereby driving government performance, is not a mere technical issue but requires a broader political economy perspective that captures the complex interactions which directly and indirectly relate to a CFA. As the World Bank continues to support PFM reform processes in various client countries across the world, a deeper understanding of the role and capabilities of CFAs as the central element in these transformations is essential. This paper proposes one such framework – one that approaches the challenge of enhancing the capabilities of CFAs through a political economy perspective.

A. CFA Roles and Functions

The central finance agency of a country, here defined as the core ministry for managing public finances, is uniquely positioned, strategically and operationally, to influence economic outcomes. Terminology and organizational structures applied to CFAs differ from country to country: some countries use the term 'Treasury,' others 'Ministry of Finance' or 'Department of Finance.' While some countries opt for a single super-ministry responsible for finance, economy, planning, and industrial policy; many others distribute accountability for fiscal and economic management among several ministries, e.g., Ministry of Finance, and Ministry of Economics. Some also separate the Ministry of Finance from the budgeting function. Thus, the term CFA is used to encompass all of these variations.

Table 1. Central Finance Agency Functions

Core Fiscal Functions	Advisory/Regulatory Functions
Macro Forecasting	
Fiscal Policy	**Oversight of SOEs**
Budget Management	**Financial Investigations**
Treasury & Cash Management	**Lottery & Gambling**
Aid & Debt and Liability Management	**Procurement**
Revenue Policy & Administration	**Financial Sector Regulations**
Financial Reporting/Internal Audit	
Intergovernmental Fiscal Relations	
Physical Asset Management	

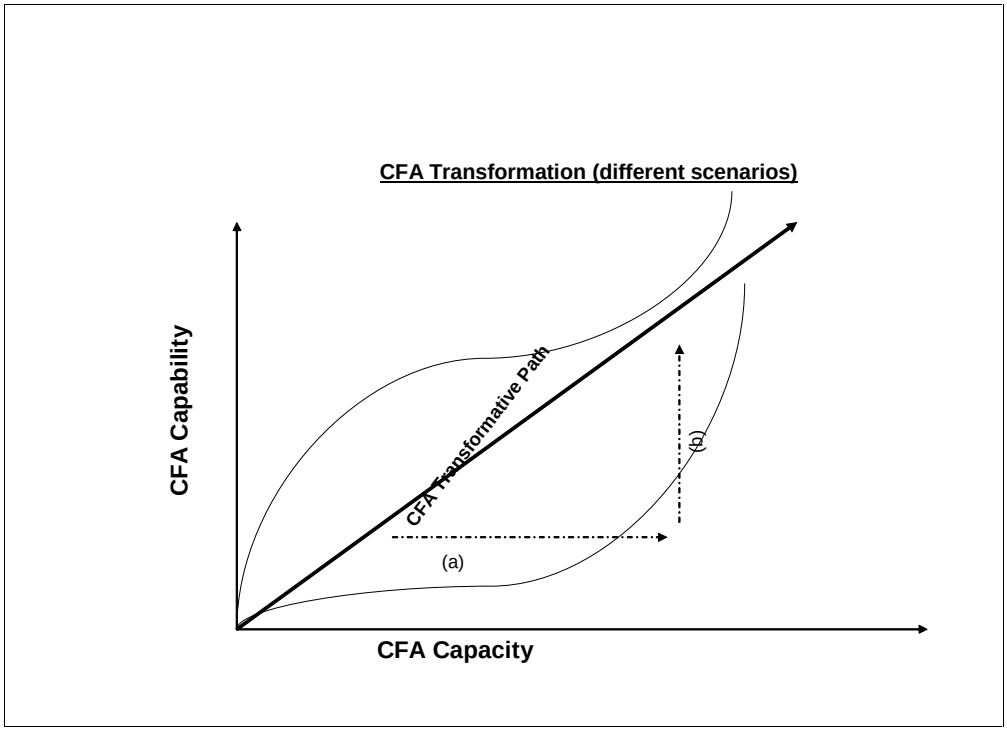
As the agency in control of public resources, the CFA marshals and deploys them to achieve desired outcomes. It also exercises guardianship over the public exchequer through its institutional roles, procedures, and administrative culture. Beyond their core fiscal responsibilities, CFAs often have numerous other roles and functions, such as regulation and oversight (see Table 1), but their primary task is to shape resource decisions and superintend public finances. CFAs are the provider of sophisticated budgetary, economic, and policy analysis and advice, the creator of norms and regulations; and stimulator of performance. Moreover, as *primus inter pares* (first among

equals) among bureaucratic agencies, and thus the nerve center of government, CFAs are central to public sector reform itself. Often their power and leadership is the critical determinant of the scope and content of reform in the public sector.

B. Capacity and Capability

Because they are so central to the functioning of the state, considerable efforts have been regularly directed to building the capacity of CFAs, particularly in developing countries, in areas such as human resources, information technology (IT), as well as accounting and budgeting. Yet, a quick look at selected low-income and middle-income countries reveals at best a mixed record for these efforts (see Appendix: Country Samples). CFAs in some countries have been successfully transformed to the point where they have exercised leadership for a wide array of public financial management (PFM) and public sector management (PSM) reforms. More often, however, despite considerable capacity building efforts, CFA transformation has either failed to unfold, proved unsustainable, or has had limited impact. Instead, in many countries, CFAs have remained ill-configured with unclear and conflicting mandates and lines of accountability.

Figure 1. CFA Transformation[1]



One argument advanced to explain these divergent outcomes is that for the most part, past efforts have focused on building *capacity*, with little consideration given to strengthening the *capabilities* of CFAs. Capacity and capability are at times used

[1] This figure is a stylized representation of the trend through time – the curved lines represent the best fit over discrete observations, i.e. i_t.

interchangeably but are distinguishable: (Further discussion of the term "capability" is in Annex 1.) The former refers to the volume or scope of CFA inputs of an appropriate quality (determined, for example, by the IT or human resource base), while the latter is about converting that volume into performance. The two are linked: where capacity is low, capabilities are also likely to be constrained. A weak configuration and/or organization of inputs, and a high-cost operating environment, perhaps marked by a lack of authority, may mean that even when capacity is high, capability may be low. There may also be cases where a CFA has low capacity, but scarce resources have been put to effective use due to a supportive operating environment, thus creating considerable capabilities. The transition of the Ugandan Ministry of Finance in the 1990s is a case in point where the Ugandan CFA started with relatively low capacity and capability. Such cases suggest a useful conceptual distinction between capacity and capability, and encourage renewed analytical focus on building capabilities in addition to capacity if CFAs are to be transformed (see Figure 1).

Building capabilities is complex, and the country context matters. The roles and functions - and thus the influence - of CFAs vary from country to country depending on institutional legacies, the role and structure of the state, the degree of economic development, and the dynamics of the political economy in which the CFA operates.

C. Rethinking CFA Reform

This paper outlines an analytical framework to assess the capabilities of CFAs in countries at different states of development - from fragile states to rapidly growing middle-income countries - and to lay a foundation for the provision of concrete guidance on how best to support positive CFA transformation. This framework is designed to assist with the diagnosis of the prevailing country situation as well as in laying a pathway to desirable transformation and greater capability. Enhancing the capabilities of CFAs will require addressing at least two dimensions: the technical, as well as the wider political and authorizing environment. For the technical dimension, the need is to assess and build up effective institutional structures, processes, and functions for CFAs that are aligned with the country situation. The political dimension, on the other hand, requires the assessment of the political economy context of institutional incentives, actors, and structural constraints on CFAs. The two dimensions complement each other: the actual roles that CFAs assume are a function of both the specified CFA arrangements, as well as how the political economy allows them to be put to effective use.

The formulation of the analytical framework is advanced by considering the following questions:

- What are the core central financial functions of government at different stages of development, and what organizational roles do these functions imply for an effective CFA? In country contexts where economic transformation would be growth-enhancing, what are the organizational and situational constraints that may prevent the conversion of capacity to capability?

- What specific political economy factors (institutional, structural, and cultural) should be considered to understand how the central finance functions work? Specifically, what critical institutional arrangements and associated incentive structures, individual and collective institutional actors and interests they pursue, and administrative cultures further or impede the transformation of CFAs to a higher level of capability?

- To stimulate positive CFA transformation, what external interventions are feasible, and in what sequence of priorities? In other words, what should CFAs do—and, more importantly, not do—and in what order?

In short, the paper addresses three distinct questions:

(i) What is the problem?
(ii) Why did the problem come about?
(iii) How do we go about reform?

Guided by these questions, the paper is structured in three main sections. The first reviews diagnostic tools that can be used to assess the effectiveness of core financial management functions in client countries and provides a rapid diagnostic template for detecting problem areas. The second section deals with the broad analytical dimensions needed to explore potential threats to CFA capabilities from a political economy viewpoint. The last section turns attention to the reform process itself, emphasizing problems related to intervention strategies and sequencing, and the importance of stakeholder analysis in building and sustaining reform coalitions.

The intent is to offer a new perspective on how to go about CFA reform, driven as much by political economy as by technical considerations. Informed by cases of CFA reforms, this framework paper offers an analysis to strengthen current Bank efforts to assess the environment for and assist in the transformation of CFAs by building a better understanding of the underlying political economy dynamics. Giving appropriate weight to the political economy considerations opens up the process to a different set of interventions, rather than simply exerting more effort to reach the same technical solutions.

II. TOWARDS A DIAGNOSTIC FRAMEWORK

The transformation of CFAs requires a problem driven approach. However, there is no single diagnostic tool currently available for carrying out assessments of problems and critical bottlenecks which constrain the enhancement of CFA capabilities, and in turn, can impede the smooth implementation of PFM reforms and achieve desired transformations. What follows is a proposed approach which builds on various existing tools used for examining other aspects of public financial management and governance, and brings a political economy perspective to the subject.

A. Approaches

There are two main approaches which can address the issue of CFA capability and the questions related to transforming capacity to capability.

The *political science* literature has traditionally taken a keen interest in the role of formal political institutions and actors in the process of managing public resources(Wildavsky and Caiden 2003; Wildavsky 1964; 1986), and it has recently been revitalized as part of the 'new institutionalist' paradigm. This paradigm, influenced not only by economics but also by sociology and history, applies a variety of approaches ranging from public choice to path dependence to explain policy processes through the lens of institutional rules, individual action and institutional change (Hall and Taylor 1996; Lowndes 1996; Peters 1999). Meanwhile, other scholars have looked at budget and PFM reforms from a wider political economy perspective. They argue that because it is inherently political, engaging in reform requires more than just a technical view; even more important is a better understanding of the complex interplay between macro political features (political regime, patronage vs. program-based politics, civil society, etc.); political agency (leadership and reform coalitions); and the major constraints emanating from the structural and cultural context (Acosta and Renzio 2007; DFID 2004; ODI 2005).

The *technical public financial management* literature contributes another stream. Influenced by some of the wider institutional debates, this approach focuses on the micro rules of budgetary governance - and thus institutional incentives - as seen often through the lens of principal-agent model, transaction costs, and management theories. It seeks to address PFM problems, often associated with aggregate expenditure control, strategic prioritization of expenditures, and operational efficiency (Alesina and Perotti 1999; Campos and Pradhan 1996; Hagen 1992a, 2005; Schick 1998). Country practice over the past several decades has seen the advent of many new PFM instruments, such as the widespread implementation of Medium-Term Expenditure Frameworks (MTEF) and performance budgeting in reformulating the budget making challenge, Integrated Financial Management Information Systems (IFMIS) focused mainly on budget execution and reporting, and the development of new diagnostic tools for assessing PFM systems such as PEFAs, PERs, CFAAs and CPARs.

It is an objective of this framework to effectively apply the complementary strengths of both streams to the concrete issue of building capabilities of CFAs and offer a resource for integrating both the technical and the political dimensions into realistic guidance for promoting a beneficial transformation in the core central finance functions of governments.

B. Available Tools

To begin to chart the path toward enhancing a CFA capability, it is useful first to diagnose the current situation by quickly locating critical capacity and the operational issues that require attention. There are no readymade analytical tools to assess central finance functions - a problem exacerbated by the fact that CFAs differ widely in organizational structure and functions.

There are, however, a number of diagnostic economic and sector work (ESW) products that the World Bank, the IMF, partner organizations and markets have developed in recent years that can help in assessing the effectiveness of central finance functions. Many of these have been associated with aspects of fiduciary interests or creditworthiness. These products fall essentially into two categories:

Non-standardized analytical assessments of a country's PFM system, using such diagnostic products as:

- **Public Expenditure Reviews (PERs),** which analyze the country's fiscal position, its expenditure policies (in particular, the extent to which they are pro-poor), and its expenditure management systems. While PERs vary considerably in coverage, they may also examine institutional arrangements for public expenditure management on national and subnational level, touch on the issues associated with the size of the civil service wage bill, and revenue policy and administration - aspects of direct relevance for CFAs.

- **Country Financial Accountability Assessments (CFAAs),** which evaluate the strengths and weaknesses of accountability arrangements for managing public resources in areas like budgeting, accounting, and audits, and also identify the risks these may pose to the use of World Bank funds. CFAAs also often analyze the role of CFAs in the country's public and private sector financial accountability framework.

- **Country Procurement Assessment Reviews (CPARs),** which examine public procurement institutions and practices in borrower countries, which in some countries might include the CFA.

- **Public Investment Management Reviews (PIM Reviews),** which examine the efficiency of the public investment management function. As of now, these have been applied in six countries, but they are likely to be applied more widely.

- **Reports on the Observance of Standards and Codes (ROSCs),** while templated, may not be prescriptively standardized. Fiscal ROSCs, as most pertinent for CFAs, may examine the clarity of roles and responsibilities in fiscal management, budget processes, as well as the disclosure and integrity of information.

- **Debt Management Diagnostic,** being piloted.

- **IMF Reports**, particularly 'Red Cover' technical assistance reports on PFM, and other reports such as safeguard assessments of central banks (to be used under confidentiality arrangements).

- **Client Country and Development Partner Reports**, which include reports from official oversight agencies in borrowing countries (such as parliament or supreme

audit institutions), as well as PFM diagnostic work undertaken by other development partners, such as the Asian Development Bank Diagnostic Study of Accounting and Auditing, European Commission ex ante assessments of country financial management, and UNDP Assessments in Accountability and Transparency (CONTACT).

- **Institutional Governance Assessments (IGAs)** that might touch on PFM and the institutional capacity of CFAs.

- **Institutional and Governance Reviews (IGRs),** which evaluate the quality of accountability, policymaking, and service-delivery institutions within a given country from a broad governance perspective and often deal with the CFA in diagnosing the shortcomings of formal PFM systems.

- **Other studies**, in which finance functions are dealt with, but may not be the core of the studies, such as Governance and Anti-Corruption (GAC) diagnostics which look at aspects of governance and occasional political economy studies, and other analytical work (see for instance, cash rationing in Zambia, political economy in Uganda.)

Standardized assessments, with a quantitative element, of a country's PFM system, intended to generate standardized benchmarks for comparative purposes, including:

- **Public Expenditure and Financial Accountability (PEFA)** indicators, a collaborative effort of seven development partners to oversee the development of a universally accepted tool to assess a country's PFM system against 28 indicators in three areas of budget credibility, comprehensiveness, transparency, and the stages of the budget process (i.e., planning, execution, reporting and audit).

- **Country Policy and Institutional Assessments (CPIAs**), which rate a country's performance against 16 criteria representing different policy and institutional dimensions of a country's poverty and growth strategy, including the quality of economic and budgetary management. [Done only for IDA countries?]

C. Rapid Assessment

Although none of the available diagnostic tools (both qualitative and quantitative) to evaluate a client country's PFM system and its related institutional arrangements deal exclusively with CFAs, the information they provide can be quite useful for an initial CFA assessment. For instance, one way to create a useful tool for assessing a CFA is to link the available diagnostic information more specifically to its fiscal core and regulatory/advisory noncore functions. That makes it possible to pinpoint specific problems in the working of CFAs. A sample analytical matrix that links specific quantitative indicators and related qualitative assessments to core and noncore functions is shown in Tables 2a and 2b.

Table 2A. CFA Diagnostic Matrix: Core Functions

Functional Areas	Tasks	Diagnostic Indicators	
Macroeconomic Management	Macro-Projections	PEFA	PI-6
		Others	ROSC, CPIA-I1 (Macroeconomic management)
	Fiscal Policy Development	PEFA	PI-12 (Multiyear perspective in fiscal planning, expenditure policy, and budgeting)
		Others	PER (aggregate fiscal outcomes, functional and economic composition of public expenditure, fiscal planning, debt sustainability analysis), CPIA-I2 (fiscal policy),
Budget Management	Budget Preparation & Analysis	PEFA	PI-5 (Classification of the budget), HIPIC-5 (Classification) PI-6 (Comprehensiveness of information included in the budget documentation) PI-7 (Extent of unreported government operations) PI-11 (Orderliness and participation in the annual budget process)
		Others	CFAA, ROSC (specified budget calendar, timeliness and orderliness); CPIA-8 (Equity of public resource use), PIM framework
	Budget Monitoring and Execution	PEFA	PI-1 (Aggregate expenditure out-turn to original approved budget) PI-2 (Composition of expenditure out-turn compared to original approved budget) PI-3 (Aggregate revenue out-turn compared to original approved budget) PI-4 (Stock and monitoring of expenditure payment arrears) P-16 (Predictability in the availability of funds for commitment of expenditures) P-18 (Effectiveness of payroll controls) PI-20 (Effectiveness of internal controls for non salary expenditure)
		Others	PER (budget out-turns, efficiency analysis), CPIA-13 (Quality of Budgetary and Financial Management), PIM framework; possibly also: QSDS (availability of information in resources received by service delivery units, satisfaction of performance); PETS (proportion of budget allocations reaching the front line); Citizen Report Cards & Community Score Cards (consumer perceptions of timeliness and responsiveness in service delivery; Absenteeism (in education)
	Intergovernmental Fiscal Relations	PEFA	PI-8 (Transparency of intergovernmental fiscal relations)
		Others	CFAA (Legal Framework), ROSC (clarity of roles and responsibilities between levels of government); PER (balance between revenue and expenditure assignments. Debt issue power by subnationals)
Treasury & Cash Management	Payment Management	PEFA	P-17 (Recording and management of cash balances, debt and guarantees)
	Revenue Management		CFAA (tax payment)
	Cash Management	PEFA	P-17 (Recording and management of cash balances, debt and guarantees)
	Financial Accounting, Recording and Reporting	PEFA	PI-22 (Timeliness and regularity of accounts reconciliation) PI-23 (Availability of information on resources received by service delivery units) PI-24 (Quality and timeliness of in year budget reports) PI-25 (Quality and timeliness of annual financial statements)
		Others	CFAA, ROSC (Data Dissemination), PIM framework

Aid & Debt and Liability Management	Aid Coordination	PEFA	D-1 (Predictability of direct budget support) D-2 (Financial information provided by donors for budgeting and reporting on project and program aid D-3 (Proportion of Aid that is managed by use of national procedures)
		PER	PER (proportion of aid, aid coordination)
	Debt Management	CPIA	I-3 (Debt Policy); also: PI-17
		Others	ROSC, CFAA (debt management)
	Liability Management	PEFA	PI-9 (Oversight from aggregate fiscal risk) P-17 (Recording and management of cash balances, debt and guarantees)
		Others	ROSC, CFAA (liability management), PER (the list or estimates of contingent liabilities)
Revenue Administration	Revenue Administration	PEFA	PI-13 (Transparency of taxpayer obligations and liabilities) PI-14 (Effectiveness of measures for taxpayer registration and tax assessment) PI-15 (Effectiveness in collection of tax payments)
		Others	CPIA-14 (Efficiency of Revenue Mobilization)
Asset Management	Public Investment Policy and Management	Others	PIM framework, PER
	Public Private Partnerships	Others	PIM framework
Internal Audit	Internal Audit	PEFAs	PI-21 (Effectiveness of Internal Audit)
		Others	CFAA

Table 2B. CFA Diagnostic Matrix: Advisory/Regulatory Functions

Functional Areas	Tasks	Diagnostic Indicator	
Oversight of SOEs		PEFA	PI-9 (Oversight of aggregate fiscal risk from other public sector entities)
		Others	ROSC, PER
Lottery and Gambling			
Financial Sector Regulation	Policy guidelines for the central bank		Possible: Financial ROSC
	Oversight of Capital Market		
	Regulation of Commercial Banks	Others	BCP (Basel Core Principles for Effective Banking Supervision)
	Financial Investigations		
Procurement	Procurement Arrangements	PEFA/	PI-19 (Competition, value for money and controls in procurement)
		Others	CPAR; HIPIC-16 (Efficiency and effectiveness of the public procurement system)
Personnel Management	Recruitment	PEFA	I-18 Effectiveness of payroll controls PI-20 Effectiveness of internal controls for non-salary expenditures
	Promotion		
	Retirement		

What emerges is a comprehensive diagnostic template for assessing central finance functions which is both versatile and operationally useful. For instance, a quick assessment might look at just the quantitative benchmark indicators, such as PEFA indicators, using a rapid assessment matrix that would allow for evaluation of problem

areas in CFA functional areas (see Table 3, which links PEFA indicators to specific core functional areas of Ghana's CFA).

This concrete example demonstrates that it is possible to quickly identify major problem areas within a country's (Ghana, in the example) CFA as a starting point for further investigation. One could, for instance, deepen the diagnosis using information presented in qualitative assessments, such as ROSCs, PERs, or CFAAs, where these are available. This should help pull together a fairly comprehensive picture of problems that should be addressed. As more use is made of the PEFA tool, it may be possible to agree on a methodology for summing the scores by function. But even with these tools, rapid diagnosis is still only the first analytical step. Most of the information revealed by the diagnostic ESWs is still technical, and as a diagnostic toolkit its primary function is to identify problems rather than inquire into their root causes. The challenge is to widen the investigation beyond the technical to the wider political economy aspects. A framework that takes on this challenge is laid out in the next section.

Table 3. Example: Rapid Assessment of CFA Core Functional Capacity in Ghana

Functional Areas	Tasks	PEFA Indicators			
		D	C	B	A
Macroeconomic Management	Macro-Projections				
	Fiscal Policy Development	**P-12**			
Budget Management	Budget Preparation & Analysis	**P-5**			
		P-6			
		P-7			
		P-11			
	Budget Monitoring and Execution	**P-1**			
		P-2			
		P-3			
		P-4			
		P-16			
		P-20			
	Intergovernmental Fiscal Relations	**P-8**			
Treasury & Cash Management	Payment Management	**P-17**			
	Revenue Management				
	Cash Management	**P-17**			
	Financial Accounting, Recording and Reporting	**P-22**			
		P-23			
		P-24			
		P-25			
Aid & Debt and Liability Management	Aid Coordination	**D-3**			
	Debt Management	**P-17**			
	Liability Management	**P-9**			
Revenue Administration	Revenue Administration	**P-13**			
		P-14			
		P-15			
Asset Management	Financial Assets				
	Non-financial Assets				
Internal Audit	Internal Audit	**P-21**			

Source: PEFA (2006)

III. POLITICAL ECONOMY OF CFA CAPABILITY BUILDING

The transformation to ensure fully effective central finance functions may be complex. Bringing CFA reform to fruition requires multiple actors, a variety of institutional settings, and considerable political will. There are no universally correct technical policies: what might work at one point in a given country might not work in a different place or in the same place at another time. Equally important, impediments to CFA capability can stem also from the external political and institutional context - the machinery of government, inadequate laws, or interest group activity. This is where political economy analysis can be insightful by taking approaches which explicitly recognize these external complexities. Such an approach may provide an entry point to locate options beyond purely technical issues in designing solutions to CFA problems. .

Such an analysis can be initiated at the institutional level, encompassing the interplay between:

- ***Institutions:*** Institutions that pertain to CFAs are the formal administrative setting and arrangements (rules, norms, procedures - both formal and informal) that guide the conduct of central finance functions.

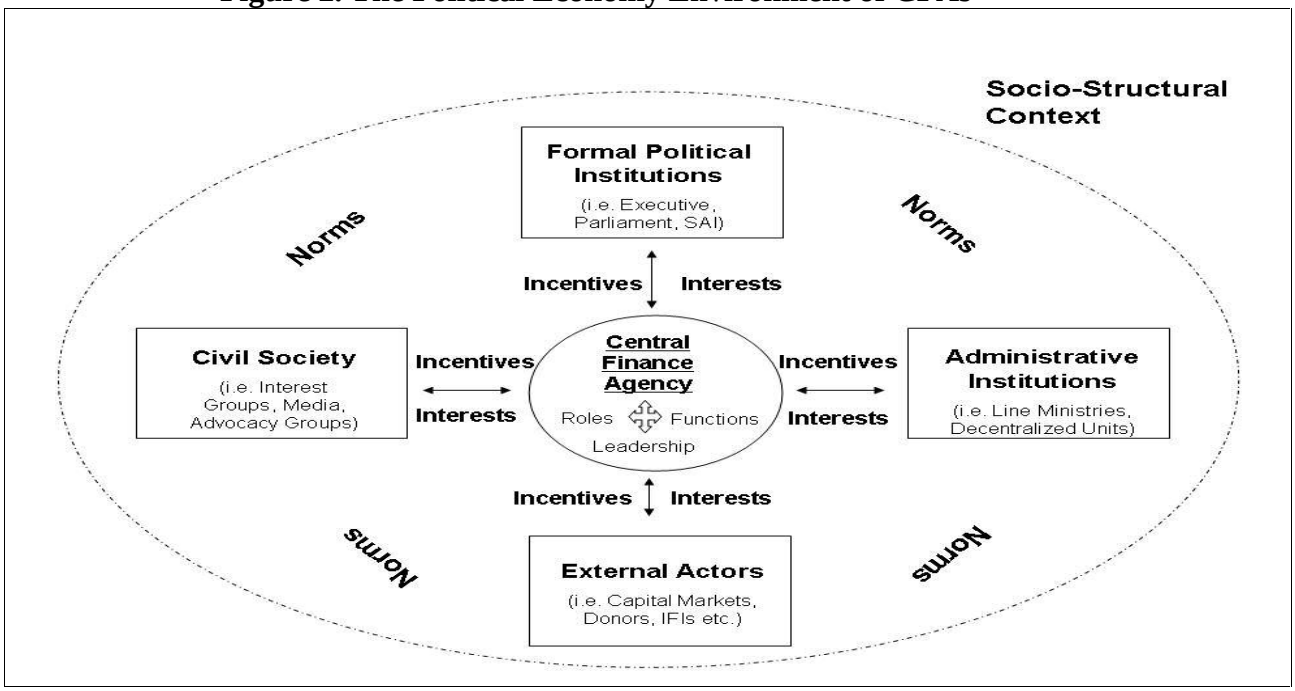
- ***Incentives***: The institutional and individual inducements that stakeholders respond to. The structure of institutional incentives includes rules, both procedural and substantive, that specify desired fiscal policy outcomes, as well as roles and information.

- ***Individual and collective actors***: The critical agents who operate both within and outside a given institution and influence its activities.

- ***Interests:*** The motivations and aims of both individual and collective actors (business, civil society, etc.), whether endogenously given or exogenously determined by the socio-structural situation, that feed into or challenge institutional structures.

These factors may be closely intertwined. How these factors interact can help explain why a particular CFA works in a certain way. Keeping track of these dynamics may be particularly challenging, however, in institutional settings where information asymmetries are persistent and the need to delegate authority might create additional misalignments. Hence, it becomes necessary to peer through the lens of principal-agent relationships and trace the signals their actions send through the accountability framework. It is also necessary to account for the environment in which the institutions are embedded, e.g., the level of development, ethnic diversity, resource abundance. Similarly, societal and intrabureaucratic norms and values (e.g., clientelism, patronage) should be considered because they provide the transmission belt between the structural and institutional levels.

Figure 2. The Political Economy Environment of CFAs



Applying these political economy perspectives to reforming the capabilities of CFAs may not be straightforward. CFAs are embedded within a complex of institutions and faced with a variety of institutional actors, incentives, and interests, both domestic and external (Figure 2).

The challenge then is to clearly dissect these institutional relationships and identify critical stakeholders. To capture these dynamics, it is important to proceed in two steps.

- *First*, to clarify some of the institutional linkages laid out in Figure 2. The intent is to highlight critical issues in each of the institutional relations from a political economy perspective that analyzes principal-agent relations and routes of accountability.
- *Second*, to then break some of these findings down to a more detailed understanding of the institutional dynamics in CFA functional areas.

A. Institutional Dynamics

The five critical institutional relationships in Figure 2 that affect the working of CFAs thus require analytical attention.

(i) CFA Internal Arrangements

The first of these relationships concerns the inner workings of the CFAs themselves. Critical actors here are the politically appointed finance minister and CFA management, and the technocrats it employs. The institutional relationship between them evidently has the principal-agent nature (See Annex 3). From a political economy perspective, their

behavior is best understood by looking at the organizational structure, the incentive system underpinned by functional roles, rules and information, and technocratic leadership.

The legal-organizational structure of the CFA has important implications for decision making across its functions. The first issue is whether there is only a single CFA or several. In general, the more hierarchical and centralized the functions are, the easier it is to use standard command and control systems. For instance, in some countries, revenue administration and treasury functions are delegated to semi-independent or fully independent agencies, which in the most extreme cases, report directly to the chief executive bypassing the CFA. A fragmented structure implies that there is also the principal-agent relationship between the CFA and autonomous agencies which may lead to various problems in the CFA operation, such as limited access to information and duplication of functions.

Box 1
Common Coordination Failures in Central Finance Functions

- *Disconnect between planning and budgeting functions*: Various planning and prioritization exercises such as the MTEF and long-term economic development plans have little influence on the annual budgeting process. Often the planning function belongs to one ministry and the budgeting function to another.
- *Replication of planning exercises and macroeconomic management*: The central finance ministry and other planning ministries have duplicating roles for formulating economic development plans and macroeconomic forecasting and monitoring.
- *Lack of coordination between capital and recurrent expenditures*: Capital and recurrent expenditures are prepared separately; the recurrent cost implications for new and existing capital assets are not considered; different priorities are applied for preparing capital and recurrent budgets.
- *Failure to take note of spending capacity in developing capital budgets*: The capital budget is generated as a wish-list with little consideration of many of the logistical and other issues associated with executing such projects.
- *Lack of coordination between revenue agencies and treasury functions*: In-year revenue collection information does not feed into the budget execution process in a timely way, thus, resulting in unfunded commitments and unnecessary stop-and-go patterns of public expenditure execution.
- *Unclear responsibilities among the CFA, ministry of local government, and sector ministries in dealing with local public finance*: Local public finance management is fragmented by multiple ministries and agencies; the role of local government in dealing with local finance is often unclear and replicating that of the ministry of finance.
- *Inappropriate status/level of influence of the CFA*: The CFA is either too vulnerable/ politicized to stand up to the unreasonable spending requests of line ministries, or is too powerful/ rigid in delegating sufficient discretion to line ministries for effective resource allocation and efficient spending (subsidiarity principle).
- *Personalized/patronized informal network that overrules formal lines of responsibilities*: Public financial management system is often personalized, depending on a number of individuals for most PFM functions; in other words, there is a tendency that PFM functions such as budgeting and treasury are concentrated in a small number of individuals, raising concerns about sustainability and checks and balance of the overall system.

Source: Various World Bank documents.

This points to the importance of the CFA coordination and oversight roles across all core functions. As CFAs are in charge of the health of the overall public finance system, they cannot fulfill their mandate without being able to ensure collaboration among various functions, establish adequate reporting requirements, and bring transparency with respect to internal processes. On the other hand, CFAs possess technical expertise that is critical

for a proper oversight. More fragmented structures therefore require greater focus on the means between organizations to achieve desirable levels of co-ordination and the appropriate recognition of the CFA authority. Fragmentation can mean that even when there is a high level of capacity, the cumbersome structures with conflicting or poorly defined roles, operating procedures, and rules for sharing information may prevent the conversion of that capacity into effective utilization, thus reducing its capabilities. Box 1 illustrates the sorts of coordination issues and problems that can typically be identified .

These various concerns about CFA internal arrangements have a direct bearing on their capability. The contexts, internal processes, reform environments, structures, and personnel management systems need to be assessed in gaining an understanding of CFA internal workings. A composite approach, based on the specific knowledge of the operations of CFAs and concerns about their capability, is shown in Table 4.

Table 4. Elements to Pursue in Internal Component of Capability Study

Broad category	No.	Name	Description
Managing context	1.	PFM Environment	• Clarity of roles and responsibilities in performing PFM tasks • Ability to co-ordinate across agencies which contribute to central finance functions
	2.	External Relations	• Ability to influence through building and maintaining positive relationships within government and with other stakeholders
Managing internal processes	3.	Corporate Planning	• Ability to plan resource use and access those resources to support business aspirations
	4.	Structure	• Ability to design and manage structures to support business objectives
	5.	Systems	• Ability to move information to where it is most valuable for monitoring and decision making • Ability to make decisions and implement in a timely fashion
Managing people	6.	Values	• Ability to manage shared values and commitment to functional objectives
	7.	Human Resources Skills	• Ability to access necessary skills to carry out functions
	8.	Performance & Accountability	• Ability to encourage better performance from individuals

(ii) CFA and Formal Political Institutions

CFAs maintain numerous linkages to the country's political institutions. The primary actors here are elected and appointed officials in the executive, legislative, and judicial branches. But it is not merely the core nature of the political system that will influence the role of the CFA but how the system operates in fact, and the degree to which the openness of the political system influences and defines the characteristics of the organization of the system of government.

The political aspects of the economic governance framework depends very much on the type of government in place. (See Annex 4 for a discussion of "limited access order" and

"open access order' systems and implications for CFAs.) The CFA's relationship to the executive branch also differs depending on whether the form of government is presidential or parliamentary (See Annex 5 for a discussion of the ramifications for CFAs for the two systems.) There are strengths and drawbacks to each. While presidential systems can provide stability, a split legislative majority can result in the slowing down of executive decisiveness and processes. Parliamentary systems can be plagued with instability, particularly if the formation of the government depends on weak coalitions. In either system, the CFA may get caught in the middle of the dynamics of political negotiations and exchanges. The CFA's relationships with the legislature (e.g., parliament) and various parliamentary committees are other aspects that need analysis within the political economic approach to CFA capability building. The Supreme Audit Institution (SAI) adds another layer of accountability to the system of public finances through external audit reports.[2]

(iii) CFA and Administrative Institutions

Whereas the CFA is an agent in the linkage between CFA and political institutions, the nature of the principal-agent relationship between CFA and administrative institutions such as *line ministries* is just the opposite. As with the internal CFA arrangements, the institutional framework of this relationship is delineated into roles, rules, and information – the three foundations that essentially underpin the incentive structure. As a principal, the CFA is charged with the responsibility for financing public policy and the services delivered by line ministries. In this capacity, it acts as rule-setter, defining procedures for resource flows and policy rules for budget aggregates; as central operating agent, establishing practices for the release of funds, financial reporting, sharing of substantive information, and debt financing; and as center of expertise, ensuring that the budget reflects the government's strategic priorities and emerging social needs.

The CFA's institutional authority and control over line ministries, however, is often challenged by the dynamics of political economy because PFM processes are often driven by the opportunistic interests of ministries and other institutional actors. This in effect makes it harder for the CFA to successfully manage public expenditures and achieve the objectives of aggregate fiscal discipline and allocative and operational efficiency. Regardless of a country's state of development, unless clear contrary incentive systems exist, line ministries will typically try to maximize their budgets in negotiations with the CFA. Sectoral ministries are often susceptible to capture by client interests and thus seek to maximize their output, attracting patronage and rents to high-level managers in corrupt environments. Asymmetry of information between CFA and sectoral ministries is also common, even in advanced countries with well-functioning PFM systems. Line ministries have a significant information advantage over the CFA since they supply the financial and substantive budget information on which the CFA relies in prioritizing

[2] The relationship between the CFA and the judicial branch, including quasi- judicial agencies of horizontal accountability, should also be considered. Due to the recent specification of socioeconomic rights and entitlements in many constitutions, courts are now more involved in the policy process where civil society actors push for constitutionally guaranteed services.

budget allocations and the volume, quality, and cost of outputs to ensure operational efficiency. In low-income countries where typically institutions are weak, the capabilities of a CFA are undermined by both domestic and external political economy factors, such as the aid process, low dispersion in the civil service pay structure, and direct political interference in management of the public finances.

Budget constraints sometimes have uneven credibility in many low income settings, and planning and budgeting are often unrealistic. In such situations, a CFA faced with a budget that cannot be implemented as approved, resorts to informal practices, such as cash rationing or strict cash limits, to control spending on a monthly or even weekly basis (See Annex 2). This situation creates ample opportunities for rent seeking through collusion between a spending agency and CFA officials. Line ministries working to maximize donor funding and thereby their total resource envelope suppress information about the actual amount of aid by operating extrabudgetary funds (see Annex 2). Project financing, which donors favor because it allows ring-fencing and a direct fiduciary accountability, fragments budget decision-making, and undermines the authority of CFAs over sectoral ministries. The weaker the CFA's hold on aid coordination, the more difficult it is to retain control and produce a reliable budget. It becomes a vicious cycle as unpredictable resource allocation forces ministries to breach formal rules to ensure that they can deliver services.

In principle, CFAs may refuse to release funds to a ministry that does not comply with financial accounting and reporting, but the political credibility of such a measure is likely to be low. Conversely, political actors in the executive in low-income countries often prefer informal practices that make it easy to protect a favored project, not seldom intended to finance a political campaign, and require the CFA to provide full financing or give priority to politically important projects through cash rationing. Thus, the CFA often operates within the web of personalized networks that overrule formal lines of responsibility and inherently limit its control over PFM systems.

A political economy analysis of the institutional linkages between CFA and sectoral ministries in low-income countries thus reveals that typical solutions to the principal-agent problems, in particular, aggregate budget limits, MTEFs, and annual hard budget constraints for sectoral ministries combined with some relaxation of internal controls and transparency rules, are unlikely to transform the CFA into a capable leader of PFM reforms. Only by taking a broader approach that redresses the perverse incentives usually shaped by the aid process in developing countries, reforming the civil service pay system, and direct political intervention is it possible to achieve a congruence of roles, rules, and information flows that support positive CFA transformation.

(iv) CFA and External Actors

CFAs also maintain formal linkages with external actors - international financial institutions (IFIs) such as the World Bank, the IMF, regional development banks, and multilateral and bilateral donors (USAID, DfID, GTZ, etc.) In countries with access to capital markets, there are also direct interactions with rating agencies and international

representatives of capital markets such as investment banks, and brokerage houses. IFIs and other donors matter particularly for the work of CFAs in fragile states, low-income countries, and some middle income countries because they are the main providers of technical assistance and other activities aimed at building capacity.

Given the important role of external actors in such settings, there are complex issues from a political economy perspective. External actors sometimes tend to push for difficult reforms that can overburden the country's capabilities and thus create new capacity challenges - a problem that can be worsened by the lack of coordination and prioritization among donor agencies. Similarly, despite the recent positive shift toward general budget support that should enhance the country's capacity to plan, prioritize, and manage public resources, financial aid inflows can be unpredictable and otherwise problematic. Aid inflows can lead to a substitution effect: they can reduce the incentives for governments to raise their own revenues, which in turn can diminish government accountability to domestic actors and create a moral hazard. Moreover, where institutions are weak, aid inflows tend to shift the balance of power within government agencies to increase the executive's discretion and spending power, thus often fostering patronage and corruption.

(v) CFA and Civil Society

A final institutional link to consider is that between the CFA and civil society at large. Civil society is defined here as the range of social actors between family and state, as diverse as trade unions, business associations, and the media, to name only a few. The role of civil society has greatly increased in many countries over the last two decades, in part to the opening up of the political space, and the diminishing role of the state in public affairs following structural reforms. There has also been a notable shift toward donor support for civil society actors. These developments affect CFAs, which now face not only new requirements for transparency but also increasing demands of civil society actors for involvement in the budget process. A good example for this new cooperation is the formal setting for the Poverty Reduction Strategy Paper (PRSP) process, which aims to bring civil and state actors together to achieve consensus on public policy choices. In other instances, civil society groups have begun to monitor public service delivery and track government spending, thus highlighting their role in enforcing accountability within the political system.

This positive trend of the increasing role of civil societies also has its own complex political economy dynamics. Much of the positive impact of civil society also depends on the strength of the institutions in place, that is, the ability of the state to channel civil society activities (e.g., lobbying, campaign contributions, protests) within the institutional realm. Although approaches differ (some countries prefer corporatist arrangements that require apex or umbrella associations to form, others prefer a pluralist system in which various organizations compete for influence), firm institutional boundaries are needed. There is a risk of special interest capture of the state, or incentives for such illegal activities as corruption. Similarly, while in many instances social protest movements have been of critical effect in initiating institutional reforms and policy changes, in cases

where social protest has become the primary venue for change, these movements have weakened rather than strengthened institutions.

The relationship between CFA and civil society is often fragile: civil society actors may be in flux; bureaucrats may be reluctant to engage in greater dialogue with civil society, particularly in areas that are considered to require technocratic expertise. What is needed, then, is not simply a change of the institutional avenues but also a change in bureaucratic culture - something far more difficult to achieve. Hence, much in this relationship will depend on the breadth and depth of civil society, the institutions in place, and the willingness of bureaucrats to engage with civil society. Capturing these dynamics and tracing their impact on the work of the CFA is an important part of any political economy analysis of CFA reform.

B. Structural Context

In addition to the institutional linkages described, it is necessary to take into account the socio-structural context in which they are embedded. Structural constraints, such as climate, level of development, degree of ethnic fragmentation, and availability of natural resources, constitute boundaries within which political economy dynamics unfold. For instance, a narrow economic base or lack of economic opportunities may considerably constrain capacity-building efforts. The fact that many developing countries are still primarily rural is something else to consider. In these societies citizens identify so strongly with their place of residence that they define their relationship with the state (their political interests) primarily in terms of their local community.

These considerations have far-reaching political economy consequences. For instance, political competition and conflict may be organized mainly around place, ethnicity, and language rather than class or ideology. And there is regular conflict over distribution of resources rather than over ideological frontiers, particularly where resources are abundant. Also, political mobilization occurs mainly on a local and clientelist basis. Networks are held together by relationships between superordinates and subordinates cemented by patronage. In these settings the weakness of formal institutions, such as parties, reinforces a political culture based more on informal than on formal relations.

In many low-income countries, political expression of these dynamics at the macro-level is best captured by the concept of *neopatrimonialism*, a term derived from Weber's concepts of patrimonialism and legal-rational bureaucracy (Weber 1978, 1980) that describes hybrid regimes in which the customs and patterns of patrimonialism coexist with rational legal institutions. For instance, while in patrimonial situations all power relations between ruler and ruled - political as well as administrative relations - are personal (there is no differentiation between the private and the public realm), in a neopatrimonial setting the distinction between private and public is at least formally accepted, though clearly in practice these spheres permeate each other, with the patrimonial penetrating the legal-rational sphere. As a result, actions by state institutions or state agents often become incalculable; formal state institutions fail to serve the public welfare (thus further eroding state legitimacy); and informal patterns become so

persistent that there is good reason to speak of a new political culture. The effects are most dramatic in public administration where meritocracy and public interest principles are gradually replaced by political clientelism and prebendalist behavior among those in power. CFAs cannot escape the structural constraints in which they are embedded. It is therefore important that a political economy analysis accounts for such structural parameters as well, as detailed in Table 4.

Table 5. Summary: Political Economy Aspects: Institutional/ Structural

Institutional Routes	Political Economy Aspects		
	Principal Actors	**Institutional Arrangements/ Incentives**	**Structural Constraints**
Internal CFA Arrangements	• Bureaucrats (within CFA) • Politicians (minister, executive)	• Organizational structure, including fractionalization of the CFA (e.g., reporting to different politicians, senior bureaucrats) • Recruitment, pay structure, promotion rules, and performance measurement/reward	• Personal rule/Neo-patrimonial arrangement • Corruption • Clientelism • State capture • Human resource base • Fiscal transparency traditions
CFA and Political Institutions	• Politicians (i.e., executive, parliament) • Appointed officials in judicial and quasi judicial agencies	• Constitutional arrangements • Electoral rules • Fiscal rules	
CFA and Administrative Institutions (e.g., Line Ministries)	• Bureaucrats (in line ministry and CFA) • Political leaders (in line ministry and CFA)	• M&E rules • Contractual agreements • Budget rules	
CFA and External Actors	• Donors • IFIs • INGOs • MNCs • Rating agencies	• Aid agreements • Capital market rules	• Aid dependency • Donor competition
CFA and Civil Society	• Interest groups • Social movements	• Corporate/ pluralist structures	• Social cleavages (e.g., religious, ethnic, etc.)

IV. DESIGNING CFA REFORMS: FROM DIAGNOSIS TO ACTION

Once there is an understanding of the political economy and the dynamics in which CFAs operate, the challenge is to translate the findings into operationally useful interventions. The practical relevance of political economy analysis is often hampered by the fact that it may not be clear who should act upon the findings in the first place. The actors that form a major stumbling block may not perceive it to be in their interest to support reform, and others may not be able to implement reform on their own. Hence, despite considerable efforts in the political economy field to craft tools in areas like PFM, there is still considerable uncertainty about how to make political economy analysis useful for operational work.

These issues are addressed in the following three steps and it is hoped that this sequence will help to clarify how to translate political economy analysis into viable reform strategies for CFA capacity building in low- and middle-income countries.

- A closer examination of the design of country-wide development strategies and how that may help in identifying strategic entry points for CFA reforms.
- The settings where CFA capacity-building reforms are likely to be of high relevance, and how these reforms are best prioritized in light of numerous reform needs and political economy constraints.
- How to build and sustain reform coalitions for building CFA capacity, including the involvement of tools from stakeholder analysis.

A. Evaluating Opportunities for CFA Reform

An examination of the design of a country-level development strategy can help in defining objectives and clarify what might prevent their achievement and how the constraints may be nullified. If that proves difficult, the exercise could consider how energies may be redirected to goals that are more achievable. In the context of CFA capacity building, a strategic approach involves careful evaluation of whether CFA reform even makes sense given the country's political economy constraints, and if so, which specific CFA reforms would best lend themselves to the chosen development trajectory.

Fukuyama and Levy (2007) provide an interesting point of departure. The authors argue that development dynamics are best understood in terms of four closely related dimensions: economic growth, civil society, state building, and the existing liberal democratic political institutions. Because these dimensions are intertwined, the authors argue that the appropriate development strategy will take a comprehensive view of their interaction to identify strategic entry points to break the low-growth trap and unleash virtuous spirals of cumulative change. The authors offer four ideal-type reform paths based on different entry points resulting from different political economy constraints.

- **Sequence I: State Capacity Building**. Where there is space for institutional reform, developmental momentum is best injected by starting with building the

capacities and concomitantly or subsequently, the capabilities needed to transform state dysfunction into state effectiveness.

- **Sequence II: Transformational Governance**. Here change begins with the transformation of political institutions (e.g., parliament, rule of law, and rights regime) to initiate developmental momentum. This entry point is strategically desirable when state institutions lack credibility or political leaders are unable or unwilling to engage in institutional reform.

- **Sequence III: Just Enough Governance**. In settings where the political economy in effect prevents comprehensive institutional reform, the strategic focus should be on growth-centered incremental reforms at the margin. In highly constrained settings where institutions are weak, limited second-best reforms aimed at growth might be a viable short-term strategy.

- **Sequence IV: Bottom-Up Development**. In this scenario, virtually all channels are blocked except for civil society. This is likely where there is little or no growth, administrative and political capacity is weak, and the elites have little political will to change the status quo.

Arguably, these are descriptions of ideal-type situations, and clear distinctions between them are not easy to make. Also, many of these strategic considerations relate especially to low-income environments where growth is stagnant, institutional capacity is limited, and there is little momentum for change. Because middle-income countries generally exhibit a certain level of institutional capacity, political accountability, and civil society activism, there the environment for reform is far more dynamic and can often generate sufficient internal momentum to recalibrate institutional dynamics.

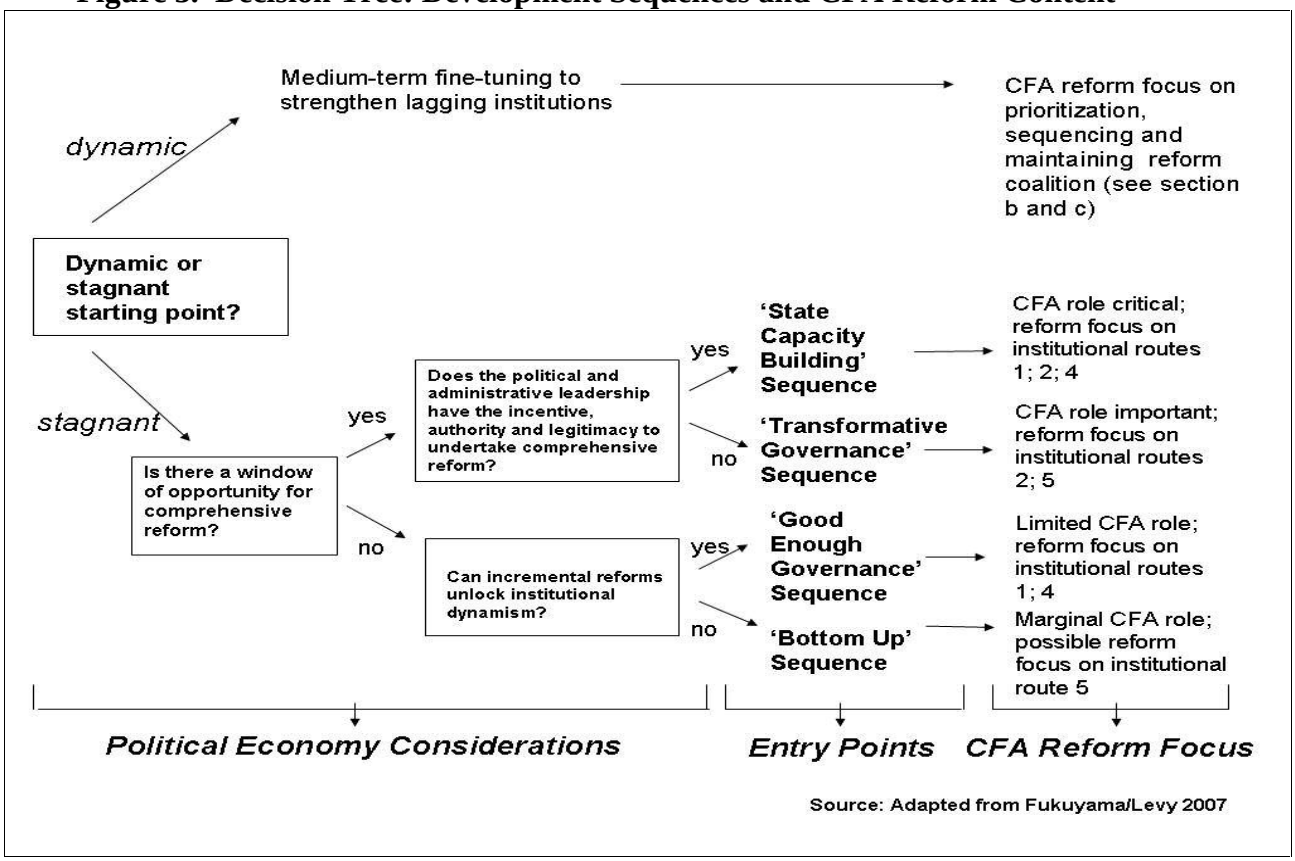
Table 6. Country Level Development Strategy and CFA Reform

Entry Points/Sequence	Reform Focus	CFA Reform Role
'Building State Capacity' (Sequence I)	Administrative Institutions, Investment Regime	High
'Transformative Governance' (Sequence II)	Political Institutions, Political Liberalization/Incentives	Medium
'Just Enough Governance' (Sequence III)	Growth oriented, incremental institutional reforms	Low/Medium
'Bottom up Development' (Sequence IV)	Civil society development	Low

These strategic approaches have useful implications for the CFA capability-building agenda. The strategic entry point chosen will affect the scope for CFA capability building reforms. For instance, where the political economy demonstrates little room for institutional reform but instead implies the need for a strategic focus on civil society support, the value added of building CFA capacity and capability might be limited. However, in an environment where the reform strategy is focused on administrative strengthening, CFAs are likely to be critical to the process and thus often claim considerable capacity building efforts for themselves.

Consideration of some concrete cases could be helpful. Uganda in the late 1980s/early 1990s might be a good illustration of wider developmental state ambitions supported, above all, by reform of state capacity (sequence I). Given the strategic focus of the reforms, the CFA led by Tumusiime-Mutebile took the lead in the transformation with the help of considerable support from internal and external actors. Post-apartheid South Africa (1996- present), on the other hand, is a good example for how developmental momentum was unleashed (sequence II) primarily by political institutions (elections, constitutional reform) and then was quickly extended to the treasury which, guided by Trevor Manuel, emerged as the technical lead agency for the developmental ambitions of the new state. By contrast, cases of incremental, selective institutional reforms (sequence III) may be found in some of the technocratic agencies of Thailand and the Philippines where, despite difficult reform environments in the early 1990s, technocratic insulation allowed for some incremental technical reforms, often with the CFA at its core. However, where civil society has remained the primary driver for change (sequence IV), CFAs in the short term had only marginal roles at best, with some scope for expansion over the medium term when collective pressures begin to move the entity to a developmental trajectory more appropriate to sequences I and II. Thus, the strategic approach suggests that careful consideration be given first to what the developmental trajectory is and whether CFA reform would or would not add value.

Figure 3. Decision Tree: Development Sequences and CFA Reform Content



Once general considerations about how developmental strategies frame the *scope* for CFA reform, the next step would be to contemplate specifically about the *content* of CFA capacity building reforms, including what specific elements should be reformed over others. The strategic implications are captured in the following decision tree (Figure 3).

Political economy considerations might be helpful not only to clarify how priorities for development reform might vary, but also lead to distinct institutional aspects of CFA capacity building. For instance, the first fork in the decision tree distinguishes among countries according to whether their developmental performance is dynamic or stagnant. If dynamic, the challenge is mainly to sustain current momentum and ensure that reforms are sensibly sequenced. Low-income countries that are stagnating offer quite a different challenge. As the second fork indicates, in some cases there may be a unique window of opportunity for comprehensive reform (new leadership, external shock, etc.). If not, an incremental reform approach is the only likely option. The earlier description of the political economy environment of CFAs highlighted five distinct institutional routes: internal to the CFA (route 1); and between the CFA and political institutions (route 2), administrative institutions such as line ministries (route 3), external actors (route 4), and civil society (route 5).

From a strategic point of view, each of these sequences has different implications for each of the entry points. For instance, building state capacity (sequence I) is likely to focus more on the dynamics within the CFA and between the CFA and line ministries/donors than the transformative governance path (sequence II) which would deal more with the CFA and political institutions or civil society in order to build political impetus for change. By contrast, a bottom-up approach (sequence IV) would, at best, suggest a focus on the role of civil society in the PFM process and possibly its linkages to the CFA.

Hence, it is suggested that a strategic approach informed by the country context should be a first step in guiding the CFA capability building agenda. Once it is determined that CFA reform is a sensible objective to pursue, it becomes possible to choose which institutional aspects should be emphasized in the reform design. These strategic considerations should be kept in mind while moving on to address issues of prioritization and sequencing.

B. Prioritizing and Sequencing

Once the decision is made that CFA reform would provide strategic propulsion for the developmental trajectory, the question becomes how to prioritize and sequence the interventions in designing CFA reform. These concerns are important from the practitioners' perspective for the following reasons:

- It is likely that the CFA diagnosis and analysis will have revealed multiple reform needs all of which urgently require attention.
- Given the inherent complexities of CFA capacity-building, one reform measure is often a prerequisite for another.

- Given demands for reform from both internal and external actors and recognizing the undoubtedly limited resources of the CFA itself, decisions need to be made regarding which interventions will have the highest impact. Otherwise, there is a considerable risk that the CFA will suffer from reform 'overload.'

The question about sequencing is not easy to answer, and there is a continuing debate (Levy and Kpundeh 2004; Rodrick 2008; World Bank 2008). However, two separate literature streams may help to inform the thinking.

"Good enough governance" approach

The "good enough governance" stream argues the need to align capacity building efforts with country-specific realities, allowing the context to inform decision making. Governance interventions are not introduced in a vacuum, but are built on some foundation of existing capacity, even if the capacity is low. The issue of what to build on depends on identifying the strengths and weaknesses of the particular state in order to find matching interventions. In less institutionalized settings, the type of CFA reform is also likely to be more critical - with potential for not only significant gains but considerable risk of failure - than in more institutionalized settings where change might be easier to induce but reform is also likely to be more incremental. For maximum impact, it is thus necessary to align CFA reform to the institutional context.

PFM platform approach

The second stream springs from the PFM literature, particularly the current debate about a "platform approach" for PFM reform that builds on earlier debates about whether to get the basics in place first or to leapfrog. This approach attempts to disaggregate an overall governance output or objective (e.g., better PFM) into the characteristics that contribute to that objective and target specific actions to achieving such characteristics. The PFM reform program in Cambodia demonstrates how the approach might proceed in two steps:

- Lay out a common vision for reform and define the critical building blocks (platforms) for achieving it. For Cambodia, these are: a credible budget (PF1); effective financial accountability (PF2); an affordable policy agenda through policy budget links (PF3); and effective program accountability (PF4).
- Define an action plan in terms of specific measures in support of each of these platforms.

The platform choice in Cambodia illustrates a logical sequence driven by the fact that: (i) each stage is a prerequisite for the next; (ii) the sequence is manageable for the implementing staff, given limited capacity; and (iii) it allows for continuous reform momentum while also providing time for internalization. Specific activities in support of each platform further reflect this logic.

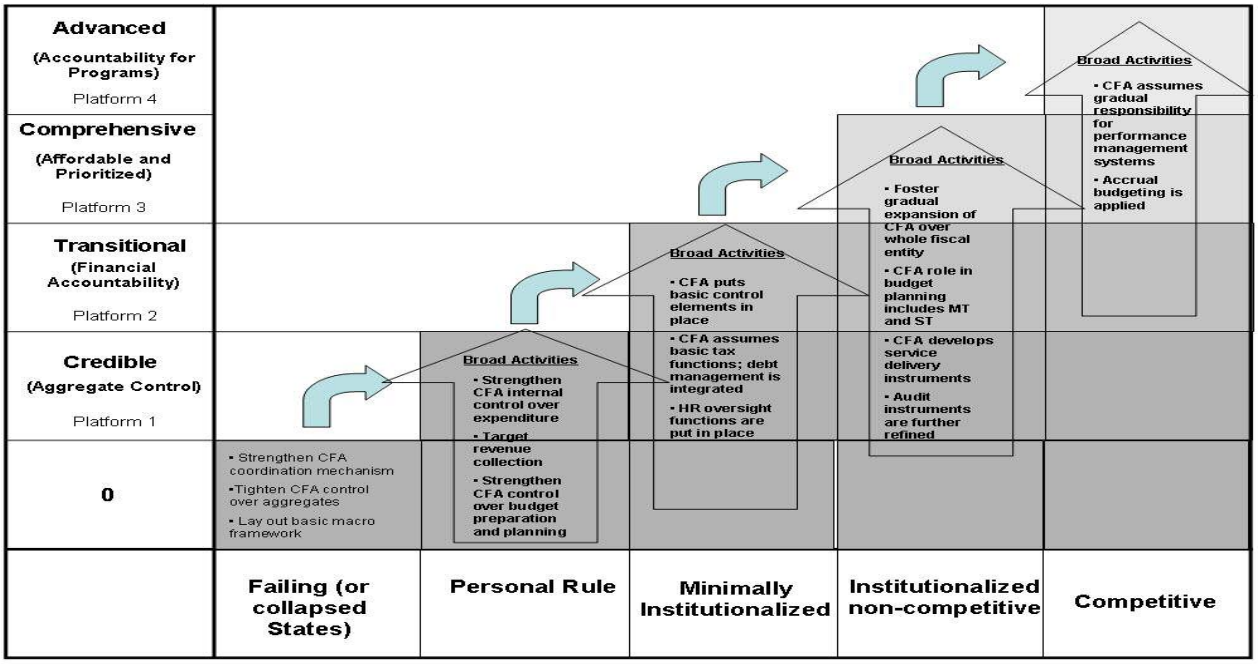
The platform approach has direct implications for a CFA capacity building agenda. It suggests that the design of a logical platform sequence in support of a chosen CFA reform agenda take the context into account. It also urges a careful consideration of the supportive measures for each of the CFA platforms chosen, which ideally should not just reflect standard technical interventions but also activities that address the incentive issues discussed earlier. The ease or difficulty of each of these activities (in terms of organizational and logistical complexity, budgetary requirements, behavioral changes required, etc.) should be guiding principles for ranking activities for each platform.

These two streams provide useful insights into how to structure the thinking about sequencing different types of CFA capacity reforms.

- First, adjust CFA capability-building goals to the institutional context.
- Then, define the logical building blocks for achieving the desired outputs.
- Finally, design specific actions, reflective of the political economy dynamics, in support of the platforms, rank-ordered by their ease or difficulty.

Figure 4 illustrates in a generalized fashion how such an approach would help to ensure that the interventions chosen are relevant, feasible, and directed at the roots of a specific problem. In such a sequenced roadmap of CFA capability building reform , the contextual setting is carefully matched with a logical sequence of reforms.

Figure 4. Sequencing and Prioritizing CFA Reform



Source: Adapted from Grindle (2007)

C. Sustaining CFA Reform: Stakeholder Analysis

Building capability in CFAs - that is, to formulate a reform vision and agree on concrete steps to achieve it - requires building and sustaining coalitions for reform. This brings into focus the fundamental roles of agents and agencies - leaders, elites, and coalitions - in the reform process. The challenge is how to muster support for CFA reform and ensure that reform momentum is sustained over time. Achieving reforms is complex, and often what look like simple technical changes turn out to be difficult to implement politically. Most reforms have distributive consequences that will lead different groups to organize to protect their incomes and rents. Hence, a critical aspect of reform management involves reorganizing interests, expanding the weight of coalitions that benefit from the reforms, and either marginalizing or compensating the losers.

It has been argued that the fate of any reform hinges on the balance of power between winners and losers in the reform effort. The various discussions focus on the role of interest groups (stakeholders) in the reform process and analyze the preferences and political realities that shape the incentives stakeholders have for reform. The salient observations include the following:

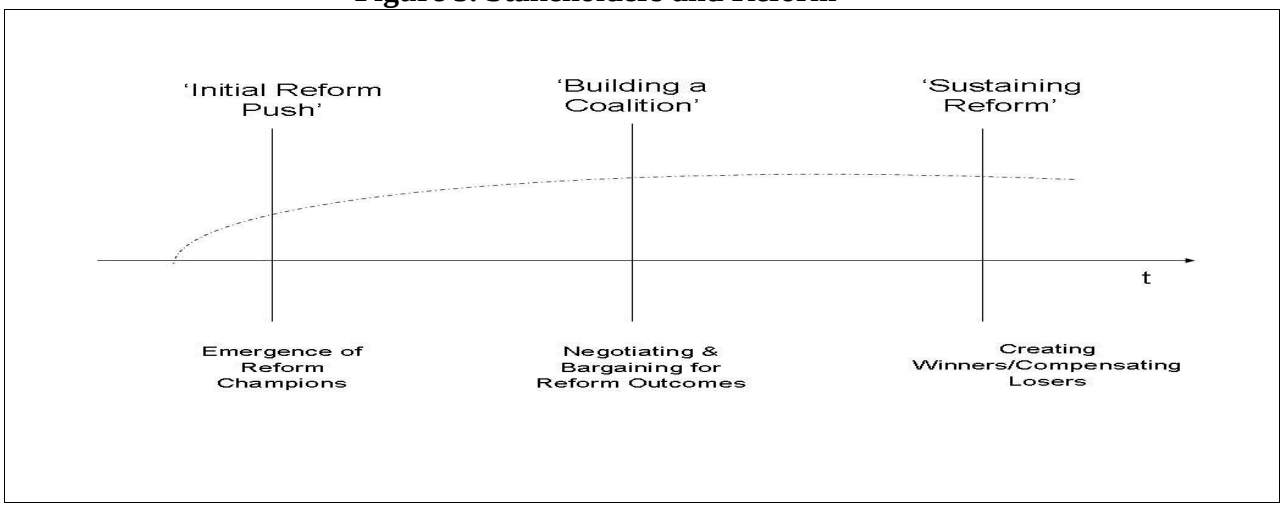
- Politicians respond to constituent pressures because they seek to remain in office, and they trade policy distortions for political support. As a result, the commitment to reform of politicians tends to follow political-business cycles, driven by careful calculations about the expected benefits of reform, particularly if information asymmetries are high. However, institutional structures often mute or magnify these effects. For instance, the structure of the party system, the stability of the cabinet, or how support and opposition are organized in parliament, are institutional factors that may affect the behavior of the executive and its ability to get decisive action on reform.

- The most substantial opposition to change often comes not from interest groups, legislators, or voters, but from ministers and bureaucrats. This is particularly true for technical reforms, which rely on dedicated reformers within the bureaucracy or on politicians delegating decision-making authority to units within government that are insulated from routine administrative processes and interest group pressures. In many low-income countries, donors facilitate the process by helping build bureaucratic capacity. In the long run, however, a wider base of support is needed to sustain reform so that insulated technocratic agencies do not become politically isolated and programs are vulnerable to reversal.

- The ability of business, labor, and social movements to spearhead collective action outside routine political channels (through, for example, strikes, demonstrations, or capital flight) is often critical to sustaining, or undermining, the reform process.

Over the long term, reform is thus often best understood as a process of gradual coalition building: groups of leaders (stakeholders) come together to achieve certain goals that each could not achieve alone. One way to think about reform, then, is to view it as a staged process that ideally brings in a widening array of stakeholders, producing political settlements or equilibria along the way.

Figure 5. Stakeholders and Reform



The challenge then is how coalitions can be made operationally useful. Answers are beginning to emerge from recent pilot work within the Bank on mapping the preferences and behavior of stakeholders in the reform process using the Expected Utility Stakeholder Model (Nunberg 2004). Combining rigorous data collection with sophisticated information processing, this quantitative modeling exercise aims to place critical stakeholder positions along the continuum of reform options in order to simulate eventual negotiations between the stakeholders and predict likely support for a reform position. The model cannot yet be applied widely because not only are considerable resources required, but it also depends on timely and accurate information, and is often politically sensitive. Nevertheless, the basic idea behind the model can be useful: conceptually mapping actors, stakeholder positions, and their relative power so as to evaluate the potential and scope for reform (see Table 7 below). The model also applies in general to CFA reform, but that also entails specific challenges because in general CFA reform is both highly technical and very political.

Supply-side-driven technocratic leadership is often critical for the success of CFA reform; political leadership in its support may be simply passive rather than active. However, there is an array of stakeholders who might also be actively interested in supporting or blocking CFA reform given their various relationships with the CFA and their particular interests. Depending on their resources, strengths, and nature of the power balance, they may also form consensus blocs or coalitions either in support of or in opposition to proposed changes. Because demand from stakeholders outside government (e.g., civil society) is less likely to be focused on concrete technical reforms than on broader governance issues (such as corruption, service delivery, etc.), considerable scope is left for bureaucratic discretion. However, the likely visible impact of certain CFA

reforms in areas of macroeconomic stability, procurement, etc. also offers considerable potential for widening buy-in to a broader group of stakeholders. That may explain why, despite general disagreement over priorities, there has been an increasing number of alliances between technocrats and civil society groups in support of CFA reform.

Table 7. Stakeholder Analysis: Sample Format

Stakeholders	
Central Government	**Others**
Executive Legislature CFA Staff Civil Service Line Ministries	Business Community Decentralized Government Entities External Actors (including Donors) Civil Society

Stakeholder Issues to Consider for Each Stakeholder Category
Placing the Stakeholder
• Policy stance (along the reform continuum) • Relative power (resources of stakeholders to defend their positions) • Importance each stakeholder attaches to reform • Potential for reform consensus (e.g., pacts, coalitions)
Relationships Between Stakeholders and CFA
• Nature of relationship with CFA • Level of support for PFM reform • Nature of political economy factors explaining level of support • Avenues for developing consensus around reform

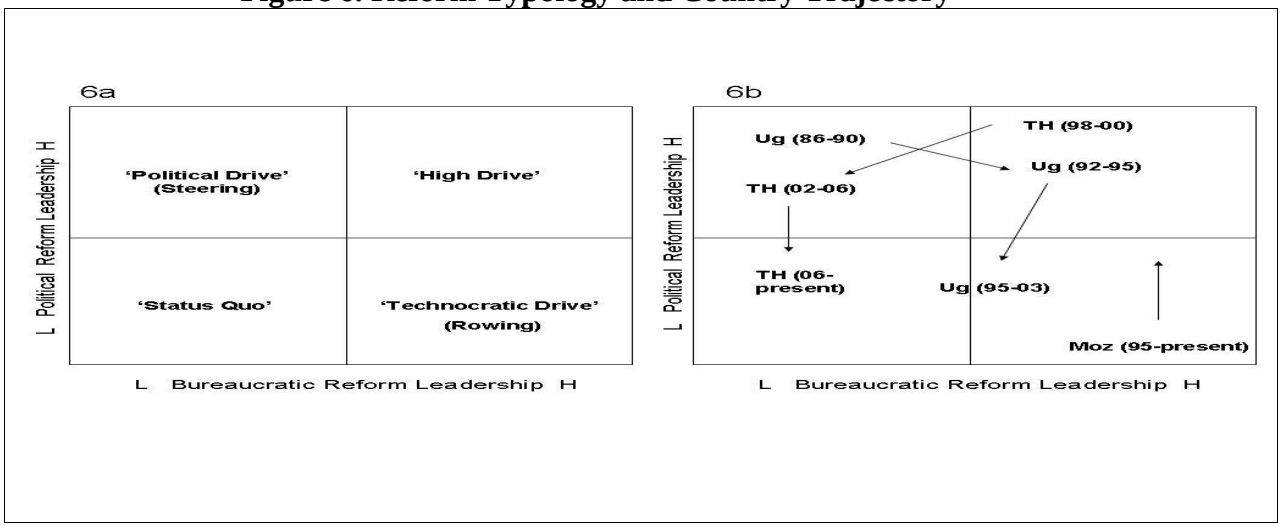
Source: Adapted from Nunberg (2004)

The technical nature of CFA reform is not likely to depoliticize the exercise as it is closely linked to the public resource process - and rents and other arrangements that traditionally benefited political and bureaucratic elites are directly at stake (e.g., extra-budgetary financing, or, treasury single accounts), thus generating considerable resistance to reform among those stakeholders. In addition to lending technical advice, donors may be able to provide incentives for reform by shifting resources to certain reform constituencies within government, thus altering the power balance.

Momentum for CFA reform can be unleashed from a variety of angles. In Chile and Mozambique, it has been driven primarily by technocratic leadership; in Thailand and Tanzania, by political leadership; in Uganda and Cambodia by both together. Leadership stories known from Uganda (Tumusiime-Mutebile) and Afghanistan (Ghani) are reminders of the impact individual champions can make. Yet they should also be viewed warily: they generally reflect a weak institutional environment and considerable donor

support. Uganda's case is particularly instructive. It offers a reminder that donor support might help strengthen technical leadership but that if political support wanes and domestic coalitions for reform are weak, there is a risk that CFA reform will be primarily addressed to the international community and have little domestic impact.

Figure 6. Reform Typology and Country Trajectory



In general, CFA reforms seem to be particularly successful where political and bureaucratic leaders work together, and there is both internal and external support. In terms of a typology of CFA reform (though this is generally not a static process), countries move over time along the reform trajectory (see Figure 6).

Building CFA capacity cannot begin without considerable reflection about the interests of the stakeholders and their ability and willingness to form coalitions for reform. This should be done in the context of the country's broad development strategy and with an understanding of priorities and reasonable sequencing. Thus, stakeholder analysis is the final component in moving the CFA reform agenda from diagnosis to action.

V. CONCLUSIONS

Well-functioning CFAs are central to the public financial management process. Yet, it is rarely clear how to enhance their capability effectively. What at times look like clear-cut technical solutions to CFA capability issues often fail to unfold; at other times, reform is achieved suddenly. But even then, there is a concern about how to make these reforms lasting and transformational.

Given such empirical paradoxes, this framework paper has moved beyond the traditional purely technical view to take a wider political economy perspective on CFA capacity and capability building. It has proceeded in three analytical steps, starting from an initial diagnosis of CFA functions and roles ("What is the problem?"), moving to analysis of the political economy environment in which CFAs operate ("Why did the problem come

about?”), and finally, taking into account strategic considerations that need to inform capacity building interventions (“How to go about reform?”). It is hoped that together these steps can advance current World Bank efforts to assess the environment for and assist in the transformation of CFAs by building a better understanding of underlying political economy dynamics.

There are essentially three major aspects of this discussion to highlight:

- It is necessary to analyze carefully the roles and functions of CFAs. There are a number of diagnostic economic and sector work (ESW) products available within the Bank and elsewhere to support institutional analysis, but none has yet dealt specifically with CFAs. The analytical template presented here deals specifically with CFA functions (core and noncore); it should allow for more rapid assessment of CFA capacity and capability issues. While further work needs to be done to integrate other dynamic aspects into the template, having a CFA template at all is a critical starting point for any problem-driven analysis.

- Understanding the dynamics of CFA capability building from a political economy perspective depends on a comprehensive awareness of the interplay between the institutions, incentives, interests, and individual actors that are directly and indirectly related to a CFA, and of the sociostructural environment in which it operates. There are critical institutional linkages to consider at the macro level, which, when applied to specific CFA issues, help shed light on the dynamics of CFA reform. Besides fostering a better understanding of the sociostructural constraints, the contribution of a political economy analysis is to disassemble [deconstruct?] these complex dynamics so that specific impediments to change can be targeted and reform momentum built. To do that, incentive and interest structures need to be aligned with the goals of CFA reform.

- Finally, the challenge is to translate political economy findings into effective interventions: reform does not happen in a vacuum; the context matters. The political economy approach strongly suggests positioning CFA capability building within the context of a country’s entire development strategy, thinking carefully about issues of prioritization and sequencing in the light of country realities, and giving careful attention to coalition building as a means of sustaining reforms. It requires strategic consideration in deciding how and when to approach interventions with a specific CFA.

While integrating political economy analysis into the CFA capability building agenda requires considerable effort, the effort can generate substantial benefits. The effect of integrating political economy analysis into the agenda is not necessarily to change the nature of traditional technical interventions; rather, it can help clarify when, and even whether, reforms should be undertaken, how to choose among reform options, and how to design reforms to get maximum buy-in from critical stakeholders. Taken together, this implies not simply more analysis but instead a distinctly different way of engaging with CFA reform issues.

Annex 1. Operationalization of the Internal Aspects of Capability Approach

The challenge becomes to take related but different approaches to developing or sustaining capability, and providing a mode to employ these for development partners and countries. A pragmatically synthetic approach is proposed by making use of the existing literature and drawing out the most essential elements, given the environment.

A. Core Capabilities

Peter Morgan, in his very thoughtful deconstruction of the term, attempts to redefine 'capacity' in a development context. He notes that the lack of a shared understanding or a common frame of reference about capacity is not an abstract point without operational implications. He says: "International development agencies harmonizing their resources in a sector-wide approach (SWAp) to support capacity development means coordinating to do what exactly? Strategies for capacity development add up to a focus on what activities? Does monitoring that looks at short-term changes to structure and performance at a point in time but ignores issues to do with process, relationships and legitimacy tell us anything significant about capacity? When we evaluate capacity, what is it we think we are looking at?"(Morgan 2006, pp. 2-3)

We have taken the view that the meaningfulness of the expression in a development context is broken, and cannot be fixed. Indeed, we would argue that Morgan is really seeking to define aggregate capability, rather than capacity. His five dimensions are each listed as a capability, but then when summed, they are termed capacity. His five capabilities are as follows (p.8):

- the capability to act;
- the capability to generate development results;
- the capability to relate;
- the capability to adapt; and
- the capability to integrate.

These dimensions in turn have 19 component parts as shown in Annex Table 1 below.

Capacity is by its nature a term that relates to the inputs available, rather than the outputs produced. Whereas, we see capability as the ability to marshal combinations of inputs and influence the external environment to yield production. Not surprisingly then, one way of interpreting capability is to argue that it relates directly to the economic notion of a production function. The CFA functions yield an outcome, which are captured by various measures such as PEFA.

Annex 1 Table 1. Aspects of Morgan's Five Capabilities

Dimension of Capability	Aspects of the Capability
The capability to act	Degree to which decisions are implemented Degree and use of operational autonomy Action orientation within the system Integrity of the organization, its leadership and staff Effective human, institutional and financial resource mobilization
The capability to generate development results	Strengthening public institutions and services Generating substantive outcomes such as better health and education Improving sustainability of development results
The capability to relate	Degree of legitimacy in the eyes of its supporters an stakeholders Ability to protect the core interests of the system Operational autonomy
The capability to adapt	Adaptive management culture Ability, opportunity and discipline to learn Confidence to change Ability to balance stability and change
The capability to integrate	Integrating structures inside the system A well-defined set of simple rules that govern operations A leadership intent on achieving coherence A shared vision of the intent of the organization

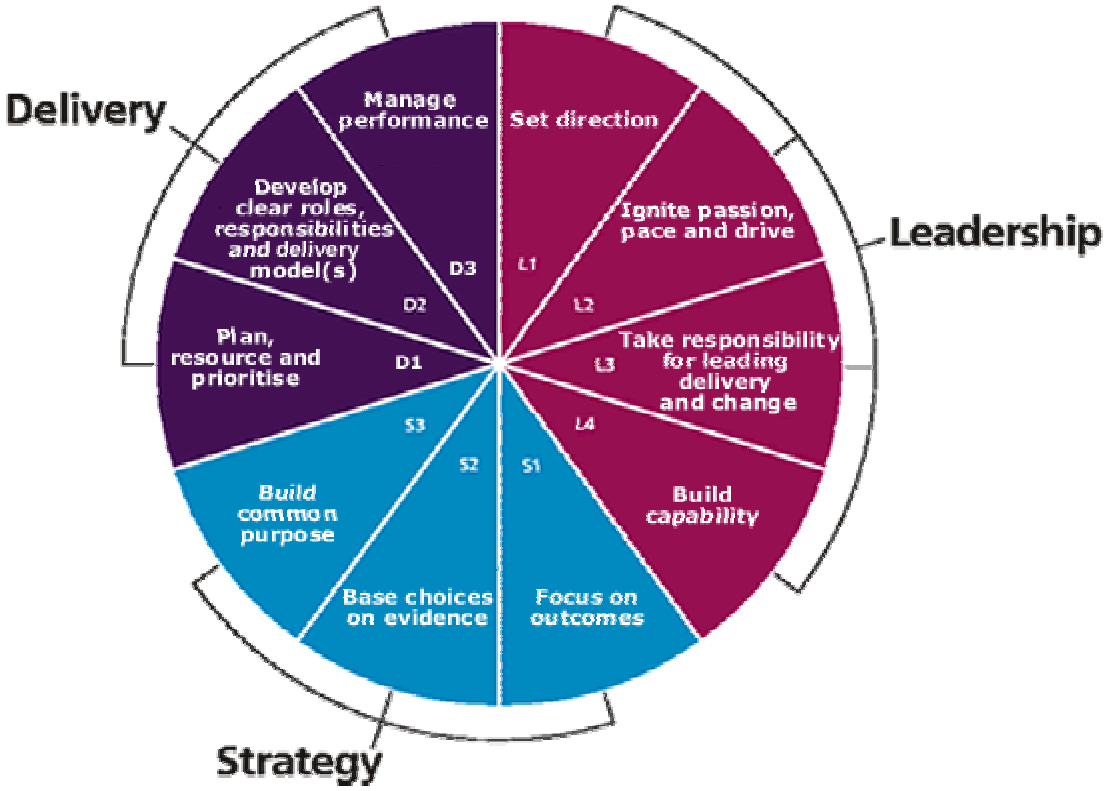
Source: Morgan, 2006

B. UK Capability Model

The British Government has developed a capability model that it applies in reviewing the performance of various government departments. In this approach, capability is comprised of leadership, strategy and delivery, and is represented by the diagram below.

The model of capability has been designed specifically for the UK Capability Reviews. It was developed through consultation with senior leaders in Whitehall and external experts. The model is deliberately selective and designed to focus on the most crucial areas of capability in the context of the British civil service.

Annex 1 Figure 1. The UK Capability Model



C. New Zealand Treasury

On his exit from the job as Secretary to the Treasury in New Zealand in 1992, Graham Scott wrote of his experiences in a short booklet titled "Reflections on Managing the Treasury". This highly readable account provides an insight into the turnaround that occurred in managing the New Zealand Treasury during the most active period of public sector and economic reforms in New Zealand. Scott organizes his paper into seven main headings, with his main point on each.

- *The Treasury's tradition*: Innovation should flourish; ideas, not people, should get kicked around, and a senior person's ideas were not necessarily better than a junior person's ideas.
- *Leadership:* Leadership is a core competence that is encouraged; this means risking failure and personal distress because of the commitment to broader values and a drive for results.
- *Managing people*: Values and various management systems need to be mutually reinforcing.

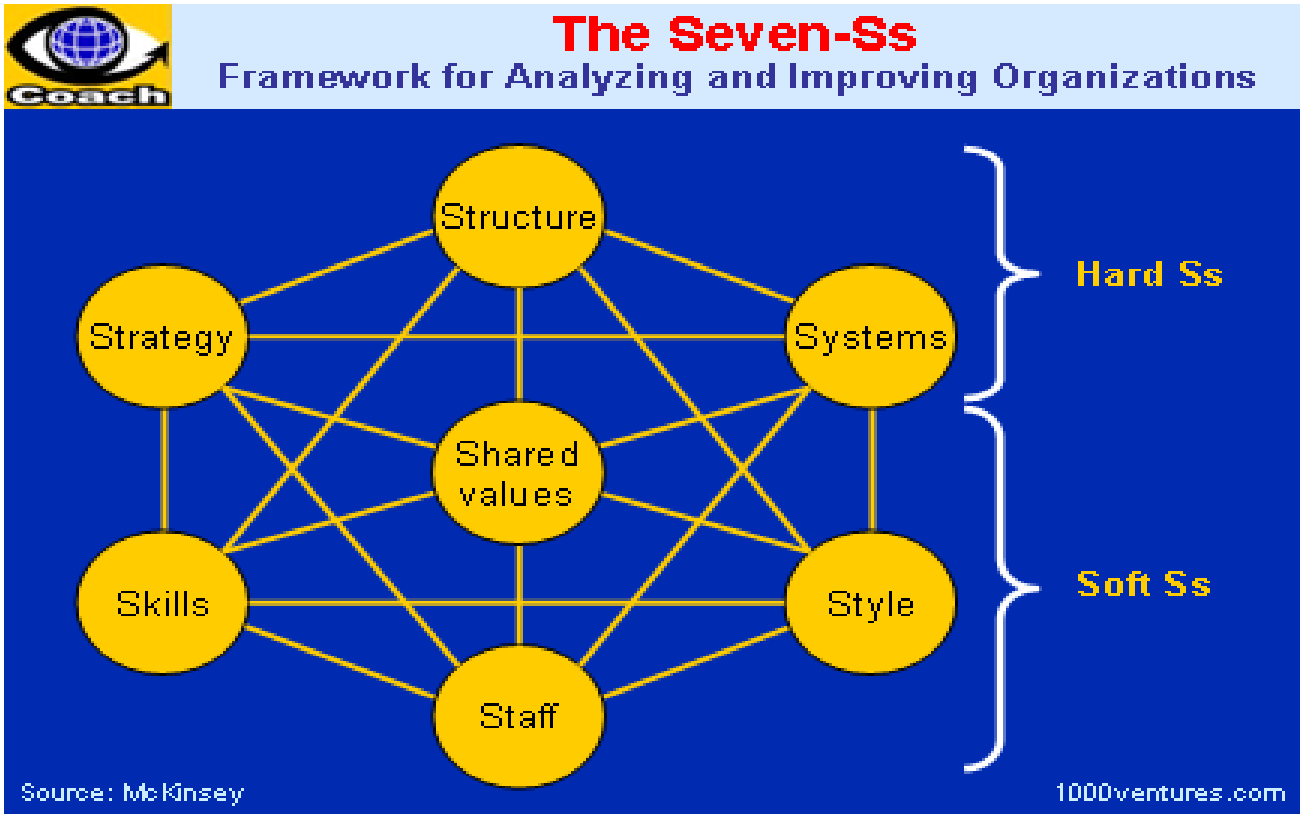
- *Managing performance*: The system for assessing staff's performance and planning for improvement is a key aspect of managing the Treasury.
- *Quality*: By modeling the philosophy and techniques of total quality management, procedures and policies will become a formality.
- *External relations*: Although often employed for their analytical skills, to be successful, treasury analysts have to be able to build and maintain positive external relationships.
- *Corporate planning*: There is a need to be ruthless in asking whether things are being done out of habit or necessity.

Source: Scott 1992.

D. Management Consulting

The world's major management consulting companies apply set frameworks in providing advice to corporations and others in making organizational transformations. Probably the best known is the McKinsey seven "s" approach, which is represented below.

Annex 1 Figure 2. The Seven-Ss of McKinsey]



One distinctive feature of this approach is that of the seven 's' all but strategy are inwardly focused. The IMF has had some success in applying a framework based on the seven 's' in its work with tax administration organizations.

Annex 2. Political Economy Analysis of Some CFA Issues

Arguably, many of the political economy aspects described apply to the macro level and so can be of only limited use for operational work. The challenge, however, is to link political economy aspects to concrete areas for CFA reform. This is not easy as most problems are context-specific, and generalizations will depend on careful analysis of individual cases. Several selected common problems in PFM/CFA reform are used to illustrate how a political economy analysis can be useful in capacity building. The critical aspect to highlight here is again how the institutional dynamics - the complex interplay of institutions, interests, incentives, and individuals (the four I's) relate to the wider structural environment. Hopefully, the following case studies of three common CFA problem areas will provide instructive political economy insights into areas highlighted in the diagnosis section.

Example 1: Budget Formulation and Off-Budget Items

Off-budget funds and transactions are a major concern in many developing countries, despite considerable efforts by the IFIs and donor community to promote transparency and accountability by encouraging the passage of new finance laws. These informal practices have sometimes become so dominant that some observers are convinced that the formal budget process is no more than a façade (Killick 2004; Rakner et al 2004). A political economy analysis may provide a different perspective on some of the dynamics driving extra-budgetary funds (EBF). Such an analysis would start by looking at the critical actors driving the process - here bureaucrats, politicians, and external actors - and their interests. Often they have good reason, in their own minds, to create or maintain EBFs. For example, ministry officials may want to create an EBF if government pay scales are deficient and the EBF funds might be translated into salary enhancements; they might also use direct donor financing of projects as a way to escape budget discipline in the form of competition from other priorities. Politicians, on the other hand, may press for EBFs if they have little confidence that the budget will fund their political objectives.

In other instances, the CFA may not be able to impose hard budget constraints or insist on transparency because of interference from the executive branch, or even outright collusion between politicians and bureaucrats to expropriate public funds, a scenario that is not uncommon in poorly institutionalized neopatrimonial settings. Dysfunctional dynamics are numerous in the area of EBF and not easily fixed by traditional interventions such as new organic finance laws. A political economy analysis may open the way to formulation of different interventions that would be more effective in altering negative behavior or incentives.

Example 2: Budget Implementation and Cash Budgeting

Budgets are seldom implemented as planned in many developing countries because they are curtailed by cash limitations, often related to the cash release system at the treasury. Instead of releasing money at regular and predictable intervals, cash is often forthcoming only when the treasury is sufficiently liquid. As a result, funds are released according to

priorities that may place statutory charges such as debt servicing ahead of voted expenditures, a wage bill ahead of pensions, etc. On the capital side, funds are often released selectively to projects that are deemed politically important or to secure aid disbursements.

These practices then lead to the creation of a situation of dual budgets: the real operating budget is the cash release budget, the real capital budget is the aid disbursement (Stevens 2004). Conventional prescriptions like MTEFs and better cash management often fall short of solving the issue for political economy reasons. For instance, politicians may prefer arrangements that respond to day-to-day political needs. Bureaucrats, on the other hand, might view cash budgeting as a way to create rents and enhance their power (analogous to when contractors pay bribes to get funds released). Institutional incentives and constraints add to this practice. Moreover, IFI pressure to achieve fiscal targets and adhere to the PRSP process might make cash budgeting inevitable, particularly if spending patterns are not flexible and the government budget institutions are inadequate. Also, where the executive dominates and the CFA role is seen to be simply that of "finding money," the CFA may not have the political power to impose realistic budgets on the line ministries. Instead, it will try to impose another budget through cash limits.

The political dynamics are often similar in countries where the legislature has the power to change the budget and thus may add expenditures that cannot be financed. This leaves the executive no alternative but to implement the budget through a cash release system on the political calculation that, for example, vetoing the appropriations could trigger impeachment procedures. In other cases where bureaucracies are highly fragmented, the CFA may simply not trust line ministries and agencies to spend according to published budgets and thus prefers to control spending month to month, especially if the CFA lacks the political clout to make line ministries comply with the fiscal reporting standards that are necessary for effective cash flow management.

There are again wider political economy dynamics that are not properly addressed by standard CFA capacity reform efforts. The challenge is to use the political economy analysis to identify innovative interventions that would change the negative dynamics described.

Example 3: Public Private Partnerships

Public private partnerships (PPPs) provide an opportunity for governments to secure public infrastructure services without the large up-front investment that characterizes traditional public investment.[3] The ability to postpone government liabilities [costs?] is a key reason why politicians are attracted to PPPs. Another common motivation is the perception that outcomes can be improved by private sector participation in aspects of the

[3] There is no consensus on a definition of PPPs: generally speaking, they refer to arrangements with the following characteristics: (i) private execution and financing of public investment; (ii) an emphasis on both investment and service provision by the private sector; and, (iii) an appropriate risk sharing between the government and the private sector.

project (e.g., financing, service delivery, user fee collection, and maintenance) that traditionally have been handled by the public sector.

PPPs are often pushed as a way to expand investment in the delivery of public services without having to rely on the state meeting the initial expenditures. For this reason, PPPs are strongly supported by construction companies, financial institutions, and many others in the private sector. They often attract to their corner line ministries that are interested in addressing urgent infrastructure needs. CFAs tend to be warier: they recognize that whether PPPs are preferable over traditional investment depends on whether they lower the cost over the entire project cycle. Since this may require assessment of uncertain liabilities over a very long time, PPPs tend to come with significant risks that are difficult to incorporate into fiscal decision making. The risks are enhanced by the contingent nature of many PPP-related liabilities. For example, the government may agree to supplement a PPP contractor's revenues from a toll road if traffic falls short of a pre-set benchmark.

IFI advice has been directed to ensure that decision making on PPP projects is not distorted by systematic underestimation of the fiscal risks and the long-term costs of PPPs (IMF 2007). The basic principle is to frame the process in such a way that the options of traditional investment and investment through PPPs are weighed on a comparable basis. This would prevent PPPs from being used to circumvent the budget constraint, which could jeopardize fiscal sustainability and undermine the efficiency of public investment. Typical elements of advice are that the CFA should have a decisive voice in decision making on PPP projects; the true fiscal costs of PPPs should be reflected in government accounts and budgeted to the extent possible; PPP-related contingent liabilities should be fully disclosed; and PPPs should only be undertaken if they address a priority need and offer value for money relative to traditional provision of infrastructure through the public sector.

This advice has been tailored based on examples of governments with a capable CFA (e.g., South Africa, Victoria State in Australia, and the U.K.); it may be difficult to apply in other cases where CFAs are less competent. In countries where the cabinet has a key role in budget decisions, attempts to depoliticize PPPs are likely to be ineffective and perhaps lead to risks not being clearly acknowledged. Another issue is that proper management of PPPs requires considerable strengthening of institutions (advice typically includes setting up a high-quality PPP unit within government, but may also extend to investment planning, accounting, and reporting, and changing the legal framework). Countries with limited administrative capacity find it difficult to follow such advice and may also question how it relates to the need to upgrade the administrative capacity in other areas, such as tax administration and procurement.

Annex 3. The Principal-Agent Relationship in CFA Internal Arrangements

The principal-agent linkages between the finance minister and CFA management on one side, and lower rank technocrats on the other side, depend upon whether the latter have proper technical skills to do their task and whether they are provided incentives to perform. Incentives involve aspects of recruitment, pay structure, and the way promotions are exercised. Some have argued that first-generation civil service reforms emphasizing retrenchment and growing opportunities in the private sector have considerably weakened CFA technical capacity in many countries (Stevens and Teggemann 2004). The resulting shortage of skills, particularly in low income settings, has created a formidable challenge for CFA leadership and donors alike to implement PFM reforms. The means to attract and retain competent personnel and manage their performance are also necessary if civil servants are to perform effectively and efficiently. Using semi-autonomous or fully autonomous agencies indeed have been often the way to enhance available skills and performance of a few critical CFA functions. A special status allows these agencies to introduce better remuneration and promotion scales, and thus bring in the most qualified. Also, combined with the legal foundations, performance arrangements are often critical in shaping how much autonomy CFAs can claim. However, many CFA functions are usually subject to general civil service regulations, and CFA leadership needs to go through a Civil Service Commission if they want to increase compensations in order to attract better skills and manage performance. Autonomy is often simply a reflection of the ability to build an independent and professional civil service whose esprit de corps creates conditions that can make it an island of excellence among bureaucratic agencies.

The cultural aspect is closely related to leadership. Often, transformative changes take place only when institutional structures are transformed by "reform entrepreneurs" at the center who have a clear vision and mobilize internal constituencies for far reaching reforms.[4] And yet, while leadership - the ability to promote achievement of certain goals effectively - is often associated with strong personalities, it can rarely be attributed to a single person alone. Instead, functional leadership is marked by the mobilization of multiple leaders within organizations who facilitate cooperation and intertemporal bargains to build institutional capacity. Dysfunctional leadership, on the other hand, is often personal and charismatic. It deinstitutionalizes formal arrangements over time (IDB 2006). Another important aspect of leadership relevant for CFAs is institutional leadership. The strategic position at the center of government provides CFAs with a unique advantage to champion reforms in PFM as well as broader public sector governance which are critical for the effective functioning of line ministries and the overall public sector.

[4] Well-known cases are the leadership of Tumusiime-Mutebile at the Ministry of Finance in Uganda, and Ashraf Ghani in Afghanistan.

Annex 4. Limited Access Order, Open Access Order Systems, and CFAs

North et al (2007) and others make the point strongly that economic governance is a heavily political management process. They describe this process as one of moving from a "limited access order"(LAO) to an "open access order" (OAO) society. A LAO is a nation state where the political system manipulates the economy to create rents as a means of solving the problem of violence. This is a natural response of societies to the threat or use of internal or external violence: the LAO reduces violence by containing all individuals and groups (or polities) with sufficient access to violence that can or do create disorder in the state, within a "dominant coalition". This coalition creates cooperation and order by limiting access to valuable resources - land, labor and capital - to elite groups, and creates economic rents they will lose if the elites return to using violence. In other words, the fruits of an economy are distributed unevenly and probably corruptly. The success of an LAO in preserving stability and avoiding violence is measured by the ability of the political rather than the economic governance structures to maintain societal control to avoid violence.

This insight helps explain why concentrating on the economic governance framework alone is not likely to be sustainable in any context, let alone in an aid context. The implications for the CFA are also clear: in a LAO, the CFA may be expected to act as an instrument of the ruling polity's rent seeking apparatus.

There are many degrees of LAO, and fragile states are at one extreme because of their ability to collapse back into conflict given the fragility of the dominant coalition in government. In contrast, an OAO is sustained by competition, where no particular polity has access to violence (with the exception of criminal polities which are expected to be controlled by the rule of law). Political and economic competition balances interests and rent-seeking behavior, so resorting to violence to secure a particular benefit or grievance is either unnecessary (the institutional structure delivers acceptable redress), or discouraged (by the existence of property rights or non-discriminatory rule of law), or prevented by the state with legitimate and accountable use of force.

North et al (2007) note that, "Open access is sustainable when a society is able to produce three outcomes: (i) Entry into economic, political, religious, and educational activities is open to all citizens without restraint; (ii) Support for organizational forms in each of those activities that are open to all citizens; and, (iii) Rule of law enforced impartially for all citizens."

Annex 5. The CFA's Role Within Dominant Form of Government

The relationship of the CFA to the executive branch to which it belongs and to which it is primarily accountable is foremost. With some exceptions, executive arrangements worldwide can be typically characterized as either *presidential* or *parliamentary*. The difference between the two lies in the structure of accountability. Presidential systems are generally characterized by an executive directly elected by the people whose term is fixed and independent of that of parliament (which thus has a separate origin and survival). Parliamentary systems by contrast elect their executive (prime minister, chancellor, etc.) from the parliament, which requires that the prime minister (PM) stay in power and keep a majority in parliament. Combined with the choice of the electoral system - plurality (PL) or proportional (PR) - which determines the type, size, and number of parties, there are essentially four different arrangements: Parliamentary-PR; Parliamentary-PL; Presidential-PL; and Presidential-PR. Each has very different political dynamics and trade-offs (see Haggard and McCubbins 2001; Lijphart 1992; Sartori 1994).

Both presidential and parliamentary systems have their strengths and drawbacks. For instance, a presidential system might provide more stability than a parliamentary system due to the fixed presidential term. Yet, gridlock and stasis are common features in presidential systems, particularly when the executive has to face a split majority in the legislature (Mainwaring and Shugart 1997). Similarly, parliamentary systems might suffer from weak coalitional governments if there are many parties in parliament, none of them strong enough to form a cabinet on its own (Lijphart 1992). But the likelihood of cabinet instability is also somewhat mitigated through incentives to negotiate and seek consensus at the cabinet level (Lijphart 1999). In short, both executive arrangements come with trade-offs, most of which can be captured from a policy angle on the continuum between decisiveness (the ability to get a decision) and resoluteness (the ability to hold to a decision), depending on the number of institutional veto players involved (Haggard and McCubbins 2001; Tsebelis 2002).

The implications for CFAs are complex. For instance, in a presidential system, the CFA is officially accountable to just one person - the president - but the political dynamics that come with the separation of power (veto powers, committee structures) also mean that the CFA will often have to be deeply involved in the political negotiations between the executive and legislature during the budget process (Wildavsky and Caiden 2003). Also, for an agency directly anchored to the executive branch, executive interference might at times considerably reduce the technocratic insulation of CFAs, particularly in less institutionalized settings.

Parliamentary systems pose different but equal challenges for CFAs. While in Westminster-type systems with a strong executive and clear majorities in parliament CFAs might often function as the technical nerve center of government and exert 'treasury dominance' over the cabinet and line ministries (see Thain and Wright 1995; Chapman 1997), coalitional parliamentary systems typically give the CFA a more

subdued role as a 'consensus seeker' and 'cabinet advisor,' reflecting the protracted negotiations and political vulnerabilities facing the government (Hagen 2007).

These types of observations have spurred an emerging quantitative literature suggesting that presidential systems might be more conducive to fiscal discipline but cabinet systems may produce more equitable policies (see Persson, Roland, and Tabellini 2000b; Persson and Tabellini 2000a). However, such suggestions should be treated with caution. For one thing, many political systems, particularly in less institutionalized settings, do not fall clearly into either category. They are best described as hybrids that combine elements of both presidential and parliamentary systems. Equally important, most policy choices are not the result of executive arrangements alone; they are also shaped by the electoral system which determines how many parties are represented in parliament, how programmatic these parties are, and whether MPs are likely to pursue particularistic or universal interests. It is necessary to analyze electoral rules and executive arrangements in combination to understand the dynamics between a CFA and the executive branch.

The linkage between the CFA and parliament is also worth attention. Parliament holds the power of the purse as it approves the budget and decide on taxation. It also has a critical oversight function, for instance, when it follows up on audit reports or holds individual members of the cabinet or the bureaucracy accountable (Krafchik and Wehner 1998; Stapenhurst and Pelizzo 2002). Constitutional, parliamentary, and budgetary rules critically determine the relationship between parliament and the CFA. In some cases, parliament is constitutionally empowered to increase the executive budget; in others, it can only modify the budget within the given ceiling. The powers of the Public Accounts Committee (PAC) also differ depending on the formal rules in place, how effectively they are applied, what informal rules seem to be operational, and how the country's party system plays out. The political realities as much as the institutional arrangements matter profoundly for the work of CFAs.

The budget process is a good illustration of this dynamic. For instance, the more committees there are within the legislature - the more institutional veto gates - the more will a CFA be forced to assist in the engagement of negotiating and horse trading with members of parliament, more often than not through the aegis of the political leader of the CFA, to get the budget passed (Weingast, Shepsle, and Johnson 1981). Also, depending on the electoral system, members of parliament might be more inclined to pursue particularistic over universal interests, which by providing incentives for pork barrel spending undermines the ability of the CFA to honor long- term plans and control fiscal discipline (Baron 1991; Bradbury and Cain 2001). Often, hierarchical arrangements that give greater powers to the CFA (or executive branch more broadly) are better suited to ensure aggregate discipline than those that are less hierarchical (see Alesina and Perotti 1999; Ferejohn and Krehbiel 1987; Hagen 1992b). It should facilitate discipline, but that is not always the result if the president chooses to be reckless.
However, institutional arrangements that promote executive dominance also come with trade-offs with regard to political accountability, particularly if institutions are weak. A comprehensive evaluation therefore requires dissecting executive-legislative dynamics, especially the rules guiding the interaction between the CFA and parliament.

Appendix: Country Samples

Category	Country Classification			Country Cases
Past Cases of Success (i.e., transformative role of CFA with measurable economic success)	**Middle Income**		Resource Rich	Botswana
			Resource Poor	South Africa (1996-2000), Namibia (1990s)
	IDA	Institutional-Stable		Uganda (1992-95); Ghana (1981-1990); Mozambique. (1992-); Cambodia (1992-);
		Fragile States	Resource Rich	Nigeria (2003-2006)
			Resource Poor	Eritrea (1991-95); East Timor (1999-2002); Afghanistan (2002-)
Mixed Outcomes/Failures (i.e., potential control cases)	**Middle Income**		Resource Rich	Angola ?
			Resource Poor	Turkey ?
	IDA	Institutional Stable		Rwanda (1990s); Mali (1987-97); Kenya (1980s-1990s); Zambia (1990s); Malawi (1995-??)
		Fragile States	Resource Rich	Nigeria (1990s-); Cote d'Ivoire (1990s); DRC, Iraq
			Resource Poor	Tajikistan (1990s)?; Ethiopia (1991-)
Opportunities (i.e., strong country demand/window of opportunity)	**Middle Income**			Thailand, Malaysia
	IDA	Institutional Stable		Indonesia, Tanzania
		Fragile States	Resource Rich	Nigeria, Liberia, Sierra Leone
			Resource Poor	Niger; East Timor

Source: ICRs, PERs, CABRI case studies, interviews

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