



## SIGMA

### Support for Improvement in Governance and Management

A joint initiative of the OECD and the European Union, principally financed by the EU

## FORMER YUGOSLAV REPUBLIC OF MACEDONIA

### PUBLIC EXPENDITURE MANAGEMENT SYSTEM

ASSESSMENT MAY 2008

#### 1. Legal Framework

Fiscal matters in the former Yugoslav Republic of Macedonia<sup>1</sup> are regulated by the Constitution, the Rules of Procedure of the Assembly, the Law on Budgets, the Law on Accountancy, and the related secondary legislation.

The limited regulation of the budget process in the Constitution and in the Rules of Procedure means that to a large extent the regular rules apply to the treatment of the government's budget proposal in the Assembly. A peculiar feature of budgetary legislation in Macedonia, but common to countries that were previously part of former Yugoslavia, is the annual budget execution law.

The Law on Budgets regulates the procedures for preparation, adoption and execution, as well as reporting and control of the state budget, the budget of local municipalities and the budgets of the extra-budgetary funds. The Law on Budgets was updated at the end of 2007 – the main changes included the insertion of definitions of terms used in the law, the creation of a development budget as a special part of the budget, and specifications related to the budget preparation calendar, use of budget reserves and other issues. The intention to amend the organic budget law was reflected in the National Programme for the Adoption of the *acquis communautaire*, despite the fact that there is no specific *acquis* in the budget area. Finally, the adopted amendments include only one article regulating exclusively the use of EU funds. This article states that EU funds as well as national co-funding are to be presented in the budget in appropriate programmes or sub-programmes, and that the programmes covering EU funds and national co-funding are to be a consistent part of the development program plan of budget-users. In overall terms, it can be noted here that the regulation requiring the recording of EU funds and national co-funding within the budget-user's budget and within programmes (the alternative solution being the planning of one budget line for donations from revenues and one budget line respectively on the expenditure side) is a very positive direction to take in terms of budget transparency and of actual decision-making within the budget process. However, taking into account the fact that in the previous version of the law, foreign donations were already a part of the budget, the latest amendments hardly change anything related exclusively to the planning and use of EU funds. The regulations related to the use of development budget funds, including the possibility to transfer development budget funds over to the next budget year, do create better possibilities for the use of EU funds.

#### 2. Institutional Framework

The legislation regulating fiscal relations and the budget process in Macedonia provides a satisfactory division of fiscal authority between the legislature and the executive. Parliament's unequivocal right to determine public revenue and expenditure is established by the Constitution, while the government's right and obligation to propose a budget are determined by both the Constitution and the organic budget law. The relationship in fiscal matters between the legislature (the Assembly) and the executive (the government) is

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<sup>1</sup> In this report the former Yugoslav Republic of Macedonia will hereafter be referred to as "Macedonia".

fundamentally balanced, with a clear role for preparing, executing and monitoring the budget assigned to the government. The role of parliament is to scrutinise the government's budget proposal and to decide on revenue and expenditure.

The fundamental intergovernmental relations between the central government and the autonomous local governments are outlined in legislation. The Central Bank is independent from the executive, and is not allowed to finance the government (Law on the National Bank).

The Ministry of Finance is responsible for most of the fiscal issues, while the responsibility for strategic planning lies with the General Secretariat in the Department of Strategy, Planning and Supervision. The responsibility for the planning of EU funds is also in the General Secretariat, while the management of the funds as well as planning of all other state finances is in the Ministry of Finance. With a view to creating the best possible conditions for rational budgetary decision-making, it would be wise to consider gathering these responsibilities within one institution and also harmonising the processes, as it is not possible to effectively plan the use of EU funds if the responsible institution does not know where the needs are, what has to be developed, and what is already being financed by the rest of the budget.

## ***2.1 Scope and Transparency of the Budget and Quality of Budget Documentation***

From an institutional perspective, the annual budget is comprised of budget-users and spending-units. Budget-users are first-line users in legislative, executive and judicial authorities (central government), the funds (pension and disability insurance fund, health insurance fund, regional and national road fund, and employment agency) and municipalities. Spending-units are second-line budget-users that are financed by a budget-user.

The funds are listed as first-line budget-users, in accordance with the amendments to the Law on Budgets, and therefore common regulations exist for the funds and for all of the other budget-users. This means that none of the funds referred to as extra-budgetary funds should exist anymore, but attempts are still being made to incorporate these funds into the overall state financial management process and also to clarify the status of the funds. The existence of extra-budgetary funds is indeed not just a budgetary issue, but also a question of actual decision-making and policy implementation (changing the structure of the annual budget and bringing the funds into the Treasury is not in itself much of an improvement, unless the decision-making process for planning the funds' budget is also changed).

The budget is set up according to administrative, economic and programme classifications. Foreign donations, own revenues, and inflows from loans as well as the use of these funds (according to administrative and economic classifications) on the expenditure side are part of the annual budget, but the actual capacity to plan these revenues and their intended use has been relatively weak – for example, the actual collection of foreign donations in 2007 was less than 50% of the figure initially planned; furthermore, the revenue prognosis of foreign donations in the second revised budget had even increased in comparison with the initial prognosis. In these kinds of circumstances, it is crucial to ensure the existence of strict control mechanisms so that budget-users are not able to spend more than the actual collection of revenues would allow.

In overall terms, the structure of the budget is very detailed, especially with regard to economic classification, which in practice creates problems for budget-users during the budget execution. In order to provide a certain flexibility, it is allowed to change 15% of every budget item during the budgetary year. For the sake of budget transparency, it would be rational to consider decreasing the number of items in the budget on the one hand, and on the other, making the reallocation rules stricter. This would allow better control of the initially planned budget and would also, among other benefits, provide a better basis for budgetary discussions in parliament.

The 2008 budget documentation also includes background information on programmes, including a description of achievements in 2007 and indicators for 2008. However, the programme classification currently used provides very little added-value due to the fact that not all of the programmes are actually sets of related activities and projects aimed at the realisation of a common goal(s) – which is how the term “programme” is defined in the latest amendments to the Law on Budgets – and therefore currently it is also not possible to set meaningful indicators. Furthermore, the targets set are not in line with budget limitations. Incorporating the information on programmes and their intended results into the budget documentation is a good step forward, but considerable efforts need to be made to make the programme classification and indicators meaningful and usable in the actual policy-planning process.

Although steps have been taken in relatively sophisticated directions (such as programme budgeting) the current budget documentation still lacks some of the basic information required by international standards and good practice. For example, the comparative budgetary information is provided only with the previous budget year, and no prognosis is provided on the impacts of current budget decisions on the budgets of future years. The gradual introduction of a medium-term fiscal framework is an important instrument for assessing future financial liabilities. For this to be effective, however, it is important that medium-term projections be realistic and reliable, which would require enhanced capacity in both the Ministry of Finance and line ministries. There is also virtually no presentation of fiscal risks, including contingent liabilities, in the budget documents.

## **2.2. *The Planning Process***

The Law on Budgets outlines a medium-term process with top-down elements, based on fiscal policy objectives and macroeconomic projections. In overall terms, the budget preparation process is relatively adequate – the main strengths relate to the steps taken in creating a co-ordinated strategic planning system in the entire administration (which is probably one of the most, or even the most, advanced system in the region) and the intention to create a logical linkage between strategic planning and annual budget preparation (however, steps need to be taken to fully harmonise the processes in practice and also to ensure the existence of relevant responsibilities).

### **2.2.1. *Medium-Term Expenditure Framework***

There is a clear ambition to move towards a medium-term expenditure framework in Macedonia. The process starts with the definition of the government's strategic priorities, which must be completed by 15 April at the latest. By 31 May the government is required to adopt a medium-term fiscal strategy, in which revenue and appropriations for the next three-year period are projected. Investments are planned in a three-year rolling framework. A medium-term baseline projection of revenue and appropriations should also be included in the government's budget proposal to parliament. Although clearly indispensable for sound fiscal management, the usefulness of medium-term projections is dependent on the quality of strategic planning and the capability to prepare revenue and expenditure forecasts. There appears to be room for improving the capacity of line ministries and of the Ministry of Finance to make reliable medium-term forecasts. One important element in improving expenditure forecasting is the development of a computerised budget management system. A new software package for budget management was developed and used for the preparation of the 2008 budget.

In order to be able to make a well-informed decision on the development of government finances, it is of crucial importance to have access to good macroeconomic forecasts over the medium term. Since 2001 the Macroeconomic Policy Department in the Ministry of Finance has been responsible for these forecasts. Early in the year, this department makes a forecast of all relevant macroeconomic parameters, which serves as the basis for the government's Fiscal Strategy. The macroeconomic framework is then updated on a quarterly basis to ensure that the budget proposal is based on the best available information. The forecasting has been strengthened through model development and the hiring of additional economists – however, so far it has been relatively easy to prepare the prognosis due to the fact that no significant changes occurred, whereas recently there have been turning-points in economic indicators. In a less stable economic situation, the quality of projections and the need to further develop capabilities are more apparent (as in general models do not work well and therefore do not help very much in periods of significant change).

No other national institution produces macroeconomic forecasts. The economic assumptions are routinely discussed with the IMF and the Central Bank in accordance with the IMF-Macedonian Standby Agreement, which clearly contributes to the quality of the forecasts. In due course, consideration could be given to the creation of an independent forecasting body.

**The clear ambition to include medium-term expenditure and revenue projections in the budget preparation phase is a positive sign. However, work still needs to be done in this area. Assessing the new model for macroeconomic forecasting is premature, but clearly the capacity of the government in this area still has to be a priority. A second issue for consideration is the need to make the actual ministerial budget projections beyond the upcoming fiscal years as realistic as possible.**

### 2.2.2. Annual Budget Process

The annual budget process in Macedonia is regulated in a relatively detailed manner with the Law on Budgets – recent amendments to the law also included changes to the budget preparation calendar, but the main stages and characteristics of the process have remained unchanged.

The process is initiated with the government's adoption of its main strategic priorities in mid-April. Subsequently an assessment and forecast of central macroeconomic parameters are to be used as input for the Fiscal Strategy, which is adopted by the government by 31 May at the latest. The Fiscal Strategy also includes a division of the budget into expenditure ceilings for about 30 quasi-functionally defined areas of the budget and for each of the four funds. An explicit attempt is made to take into account factors that affect expenditure, such as macroeconomic parameters, volumes of entitlement systems, legislation not yet in effect, or expected policy proposals. The sequencing of these steps and the procedures for setting overall expenditure restrictions do not appear to be fully consistent with a top-down approach to budgeting, where available resources determine the scope for government policy. Furthermore, budget ceilings set early on may be altered in the course of the preparation process due to political pressure to increase spending or as the result of increased expenditure projections resulting from macroeconomic development.

Based on the government's strategic priorities, the Fiscal Strategy and budget ceilings for budget areas and extra-budgetary funds, the Ministry of Finance distributes by 15 June at the latest a circular to approximately 30 budget-users with an overall responsibility for quasi-functionally defined areas of the budget and to the funds. In addition to the budget ceilings, which are to be divided between budget-users under the respective quasi-functional classifications, the circular includes macroeconomic forecasts, the government's strategic priorities, and technical issues concerning the preparation of draft budget requests. A high degree of discretion is given to the heads of the quasi-functional areas in dividing the budget between subordinate budget-users and in deciding how to allocate available resources. Except for some expenditure categories, such as staff expenditures, the Budget Department does not take a lead role in dividing between items in the budget. This autonomy with regard to budget allocation also applies to investment procedures, where budget-users are responsible for the allocation between investment projects and current expenditures. Based on the directives in the circular, heads of functional areas and extra-budgetary funds are required to submit draft budget requests to the Ministry of Finance by 1 September (with the latest amendments to the Law on Budgets, the deadline has been postponed from 15 August). These budget requests should also include strategic plans of each institution, covering programmes and activities for the realisation of the government's strategic priorities as well as the goals and priorities of the budget-user. Although the requests must provide information in a medium-term perspective, projections beyond the upcoming fiscal year are of insufficient quality (including the methodological quality of the strategic plans). The Ministry of Finance then scrutinises the requests, makes adjustments in the draft budgets of budget-users, and prepares a draft budget proposal, which is sent to the Council of Ministers by 1 November. After having adopted the draft budget, the government submits the budget proposal to parliament by 15 November, where it is discussed for a minimum of 20 days before it is adopted in December.

The timetable for the government's submission – and parliament's treatment – of the budget proposal is still an issue for concern. It is generally recommended, for the sake of better transparency, that the government's budget proposal be submitted to parliament at least three months prior to the start of the fiscal year (for example, as recommended in the OECD's *Best Practices for Budget Transparency*). This timetable is considered necessary to allow sufficient time for a thorough review of the budget proposal.

Neither the Constitution nor the parliamentary Rules of Procedure contain any detailed regulation of the procedures for reviewing the budget proposal in parliament. Except for the requirement that a debate on the budget be held in the chamber and for the fact that members of parliament may request a review of a specific section of the budget, the regular procedures for adopting government proposals apply. To strengthen parliament's interest in fiscal matters and to enhance the government's accountability for the budget, a more detailed regulation of voting procedures could be considered. Such a reform could include an introduction of a top-down voting scheme for the state budget. Parliament's power to make changes in the government's budget proposal is adequately limited by the Law on Budgets (article 30), which requires proposals for additional expenditures to be accompanied by measures that will decrease other expenditures by an equal amount.

The structure and sequencing of the budget preparation process is clear and rational, with an explicit responsibility for dividing more aggregate budget ceilings between lower-level entities devolved to the 30 or so heads of the quasi-functional areas. Although there is sufficient time between each step in the preparation

process, the budget process is initiated quite late in the year, which is probably explained by the late submission of the government's budget proposal to parliament. Attention should be given to the classification of the quasi-functional areas to ensure that the process of prioritising between different areas of the budget is not gridlocked in the organisational structure of the government sector. The overall expenditure ceiling and the division between quasi-functional areas set in May are not final and may be increased when the budget is negotiated in the autumn. This arrangement may undermine fiscal discipline.

**The structure and sequencing of the budget preparation process largely follows international good practice. However, the regulation of procedures for passing the budget proposal in parliament, including voting procedures, could nevertheless be enhanced and more time given for parliamentary discussion of the budget. In addition, the budget preparation process could be somewhat restructured to strengthen top-down elements. The expenditure ceilings set in the early stages of the budget process should follow a more purely functional division to facilitate the process of making political priorities between areas, and should not be negotiable at a later stage due to increased expenditure pressure. So that budget-users better assume responsibility for their budget proposals, the capacity for analysing and compiling financial aspects should be improved, with regard to both the next fiscal year and the medium term. At the same time, the capacity for performance-oriented evaluation should be improved – both at the level of the budget-user and in the Ministry of Finance.**

### *2.2.3. Budget Management of Public Investments*

Appropriations for investment purposes are presented in the state budget. However, the evaluation of capital investment projects are for the most part separated from the process of preparing the budget items for administrative purposes and for transfer payments. The risk of such a fragmentation is a sub-optimal division between capital expenditure and current expenditure. In addition, there is a danger of underestimating the current costs directly associated with the investment project.

One of the recent developments in the area is the introduction of a development programme plan replacing the former Public Investment Programme, which was probably the most influential change made with the recent amendments to the Law on Budgets. According to the Law on Budgets, budget-users are responsible for preparing their draft development plans and submitting them for approval to the government by 15 July at the latest. The government is to approve the development plan by 15 August.

It should be noted here that this change (from the former Public Investment Programme to the preparation of a development programme plan) has not resolved the problems faced previously, and the process as it is currently planned does not support the budgetary process. For example, according to the Law on Budgets, there is a requirement that the draft development plans submitted by budget-users be harmonised with their strategic plans, but in view of the budget calendar this requirement would be impossible to fulfill.

Administrative procedures for initiating investment projects, including procurement procedures, are cumbersome, which partly explains the low level of execution of capital budgets in the past. To remedy the underperformance of capital investments, budget-users are required to spend at least 30% of the annual capital budget in the first half of the year – a regulation which in fact could incite budget-users to make inefficient expenditures in order not to lose the funds budgeted; it would be better to improve the patterns of management (including planning) of capital investment funds rather than trying to regulate them. Also, funds for investments from the development programme plan may be used during the first half of the next budget year – prior to the 2007 amendments to the Law on Budgets such transfers of funds were not allowed. The possibility of carrying funds over to the next budget year was required mainly to facilitate the more efficient use of EU funds. In addition, there is a need to further develop staff capacity in running investment projects and in liaising with donors.

**In spite of recent developments, investments should still be better integrated into the budget process, and efforts should be made to strengthen the capacity of the Budget Department to prepare the budget for investment purposes (transferring the function of investment planning from the Macroeconomic Policy Department to the Budget Department creates a positive basis for such efforts) alongside the budget for current expenditure and based on the set of strategic plans. Such an arrangement would have the potential of enhancing the effectiveness of capital investments at the same time as overall fiscal control increases.**

### **2.3. Budget Execution and Monitoring**

Budget execution is thoroughly regulated by the budget law, the annual budget execution law, and the guidelines for Treasury operations. The execution of the budget is based on the apportionment of the annual budget for each budget-user, which is reflected in the quarterly financial plan that each budget-user is required to submit to the competent line ministry or first-line budget-user. The budget-users are then obliged to consolidate these financial plans, which are submitted to the Ministry of Finance. These financial plans may be revised during the year. Budget-users should also prepare a monthly financial plan (based on the quarterly financial plan) according to budget classification, which is submitted to the Treasury for approval before the beginning of the quarter. The quarterly financial plans may be changed within the limits approved for the respective quarter.

The general rules for reallocation (since the adoption of the amendments to the Law on Budgets) during the budgetary year specify that a maximum of 15% of line-item appropriations, with Ministry of Finance approval, may be redistributed and that salaries may not be increased by more than 10%. Above that limit – or between central government budget-users and the funds – the approval of parliament is required. There are complaints that reallocation is excessive and that it ties up a considerable amount of personnel resources in the Treasury and in the Ministry of Finance. An estimated 5% of total expenditure is subject to reallocation during the year, which seems high but is not dramatically so. The need for extensive reallocation is linked to a lack of planning capacity in the first and second-line budget-users. This situation should improve with the introduction of the new budget and accounting software, which was initially expected to be operational in 2007, but was in fact finalised in 2008; this software would probably allow the work force to devote more time to analytical and planning activities.

The budget execution process is heavily focused on expenditure control through a consolidated Treasury Single Account. In addition, a commitment ledger, in which budget-users are required to register financial commitments in advance, has been put in place (the commitment threshold is 3000 EUR). The centralised control of individual payments reduces flexibility at the level of budget-users and may come at the cost of a decreased operational efficiency in the government administration. Nonetheless, current budget execution practice may be the most appropriate for Macedonia, given the relatively weak internal financial control systems in budget-users. Before the stringent treasury control mechanisms are reduced, it is of crucial importance that sufficient control of financial resources is ensured by alternative control systems.

When a payment is due, the respective budget-user issues a payment request and send it, either electronically or in paper format, to one of the 17 regional offices of the Treasury. The Treasury verifies whether a requested payment is in line with the submitted payment plan, corresponds to what has been entered in the commitment ledger, and matches the purpose stated in the budget. It also verifies whether there is a sufficient balance in the appropriate account. If the request is approved, the Treasury sends a payment order to the Central Bank, which is responsible for the payment system. Executed payments are registered in the Treasury General Ledger.

By concentrating available liquidity in the Treasury Single Account, the Ministry of Finance is able to benefit from the economies of scale of cash management in the government sector and to limit the need for cash and thus the costs of borrowing. All government entities, including the four funds and the municipalities, are incorporated in the Treasury Single Account. Through cash planning, based on the historical dynamics of payments and the information in the commitments ledger, the Treasury has a reasonably good picture of its cash position – however, liquidity could in practice create obstacles for incurring expenditures and therefore restrict the implementation of government policies. As a result of Macedonia's strong economic performance, the government has built up reserves in the Central Bank, which could yield higher returns if managed more effectively, but this would have to be balanced against maintaining a sufficient balance in the Central Bank.

The Treasury produces reports on the cash execution of the budget with virtually no delay. Daily reports showing payments and the balance on sub-accounts in the Treasury Single Account are sent to the Minister of Finance and to the Prime Minister. Monthly reports are produced and distributed to the government within 30 days after the end of the month. These reports are also published on the Ministry of Finance's website. A semi-annual report on the budget execution is sent to the government and published no later than 31 July.

**With the amendments to the Law on Budgets, no fundamental changes were foreseen with regard to the budget execution function – therefore, the main features in this process have remained unchanged over the past few years. Centralised budget execution through the Treasury provides a solid control of payments and makes it possible to closely monitor adherence to the detailed line-item specification in**

**the budget. Given the budget-users' mandate to make reallocations at the most detailed level of economic classification and the relatively smooth process of reallocating funds between line-items where the approval of the Ministry of Finance or the government is required, there seems to be some leeway for operational efficiency. As performance-oriented budgeting, management and control develop, the number of lines in the budget could gradually be decreased and the tight, centralised payment control relaxed. To avoid a situation of cash rationing, liquidity management and the access to liquidity markets should be further developed.**

#### **2.4. Accounting and Reporting**

Budget accounting is centralised in the Treasury and is based on cash payments registered in the Treasury General Ledger. Budget-users are also required to keep their own accounts.

The centralisation of budget accounting facilitates the production of budget execution reports, which can be used to monitor the development of in-year revenue and expenditure. Since the chart of accounts is identical for all budget-users, it is simple to compile aggregated information on government finances. The chart of accounts is based on the IMF General Finance Statistics (GFS) 86, with a certain modification of the updated GFS 2001. Work is currently underway to move to GFS 2001 to make the chart of accounts compatible with the European System of Accounts (ESA) 95.

A working group has been established to change the Law on Accountancy. However, as the department co-ordinating the process is not responsible for the budget accounting function in general, very practical problems may emerge during the process. It would therefore be rational to bring the two responsibilities into a single department.

According to the Accounting Law, the final accounts are to be submitted to the State Audit Office and the Central Registry by 1 February. According to the Law on Budgets, the Minister of Finance is required to submit to the government by 31 May the final accounts of the previous year's budget, together with the audit report of the State Audit Office. This report, however, does not relate to a consolidated set of accounts, or to the cash execution of the budget, but is rather a summarised compilation of the results of each separate audit of budget-users, and as such its bearing is limited. After approval by the government, the final accounts are to be submitted to parliament no later than 30 June. The audited accounts should be submitted to parliament earlier than 30 June to enable a discussion of the previous year's budget outcome prior to the initiation of discussions of the next year's budget, but in practice there is very little discussion of the outcomes or of the final accounts in general. The government is not required to submit a half-year report on the budget execution to parliament, although this report is available to the public. There is no formal parliamentary debate associated with the publication of the report, but it is used in the monthly "question time" of the Minister of Finance.

Finally, a strengthening of the government's ability to make outputs transparent and to evaluate the performance of programmes and staff is necessary. This will undoubtedly be easier with the introduction of the new budget management system, but a determined and strategic effort is needed. A strengthened focus on performance reporting should not entail a massive complication of the reporting procedures. Rather, the focus should be on a few simple overall performance measures. As in most OECD countries, performance information should be aimed at informing, rather than determining, the allocation of resources.

**The current practice of accounting, both in the Treasury and at the level of budget-users, cannot be sustained in the long term. A long-term strategy for government sector accounting, where the organisation and responsibility for accounting is clarified, could be considered. In such a strategy, the accounting base should be discussed. For the purpose of monitoring budget execution, cash-based accounting is clearly appropriate. However, such an accounting base may not be sufficient for the management requirements at the level of budget-users. The issue of the government's submission of the final accounts to parliament needs to be examined. A half-year budget execution report to parliament should be introduced. In addition, the focus on a transparent measurement of outputs needs to be strengthened.**

### **3. Capacity to Further Develop the System**

Although the system for managing public expenditure is fundamentally adequate, there is a need to further develop legislation and regulation, the organisational division of functions and responsibilities, technical

financial management systems, and capacity and competence in order to reach good international practice. Currently, the success of the development of public financial management is dependent on a small but competent core of specialists supporting strategic initiatives for change. One of the key future challenges is to widen the foundation of competence in the central administration. Even more urgent is enhancing appropriate qualifications of staff in line ministries and budget-users. Without a substantial improvement in the remuneration of civil servants, it may be difficult to recruit and keep the required competence.

Another key challenge involves improving the co-operation between policy departments and departments responsible for financial management – currently, developments in public expenditure management are carried forward without any real internal demand for these changes, and therefore the public expenditure management system does not support the actual decision-making process. The recommendation made in the context of public internal financial control in Macedonia<sup>2</sup> to upgrade the financial function in budget institutions may contribute to improving this situation.

Previous reforms have been ambitious and have produced results. The Macedonian authorities have assumed responsibility for modernising expenditure management and are clearly committed to a reform agenda. To continue such improvements, consideration should be given to elaborating strategic plans in some key areas, such as accounting, financial management systems and budgeting, management and control. Such initiatives would benefit from political commitment, the assignment of responsibility and mandate to a task group in charge of the reform programme, sufficient and unambiguous financing for projects, and a structured sequence of reform steps. The role and scope of technical assistance should be clearly spelled out.

**Reform in the area of fiscal management has benefited from the support of multilateral organisations, such as the World Bank, the International Monetary Fund and the European Commission, as well as from bilateral technical assistance programmes. To optimise the resources offered to the Macedonian administration, it is important to co-ordinate these projects and – in the worst case – to avoid any conflicting advice.**

#### **4. Summary and Next Steps**

The system for public expenditure management in Macedonia provides some of the essential preconditions for an effective and efficient administration characterised by a high level of fiscal discipline and control of public funds. Nonetheless, Sigma's baseline requirements are only partially fulfilled, and further development in some key areas is highly recommended.

- 1. Parliament's role in the budget process should be strengthened.** This includes a more thorough regulation of parliament's approval of the budget proposal, including a possible introduction of top-down voting procedures. To allow sufficient time for review, the government's budget proposal should be submitted to parliament earlier than 15 November – preferably no later than end-September. The introduction of a pre-budget statement, outlining some main parameters of the government's fiscal and budget policies early in the budget process, should be considered. Consideration could also be given to obliging the government to submit mid-year and end-of-year reports on the budget execution to parliament.
- 2. The budget preparation process should be developed to strengthen fiscal discipline, facilitate the process of prioritising between main policy areas, and improve expenditure and revenue projections.** To enable an earlier submission of the budget proposal to parliament, the budget preparation process should be initiated earlier in the year. Parallel to this adjustment, top-down procedures could be strengthened through the introduction of medium-term fiscal targets and a reduction of the scope for the adjustment of ceilings for individual areas in the budget to expenditure pressure. Fiscal risks should be analysed and presented in the budget documents. Medium-term projections of revenue and expenditure should be improved and linked to the strategic planning process, including a systematic update of the macroeconomic framework during the preparation phase, with a clear procedure for taking into account policy initiatives so as to ensure consistency between the budget and macroeconomic projections. Models for expenditure and revenue estimates also need to be improved

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<sup>2</sup> See Sigma's 2008 assessment of Public Internal Financial Control in the former Yugoslav Republic of Macedonia.

3. **The central government budget should be made more comprehensive through the further integration of the funds into the budget and the elimination of some earmarked revenue.**
4. **The preparation of investment expenditure should be better linked to the strategic planning process and co-ordinated with the planning of current expenditure.**
5. **A comprehensive strategy for developing government sector accounting and reporting should be elaborated.** The current system of dual accounting, with separate accounting bases for Treasury accounting and budget-user accounting, appears to be inefficient. With the aim of satisfying the need at both central and decentralised levels for information on government sector financial operations, the elaboration of a medium-term plan for accounting development should be set as a priority. In addition, the focus on a transparent measurement of outputs needs to be strengthened.