DOCUMENT OF
THE WORLD BANK

REPUBLIC OF YEMEN

PUBLIC EXPENDITURE FINANCIAL ACCOUNTABILITY ASSESSMENT

PEFA ASSESSMENT

June 2008

Social and Economic Development Group
Middle East and North Africa Region
The World Bank

Abbreviations and Acronyms

Acronym	Full Title
AFMIS	Accounting and Finanical Management Information System
ASYCUDA	Automated System for Customs Documentation and Administration
CBY	Central Bank of Yemen
CFAA	Country Financial Accountability Assessment
CG	Central Government
COCA	Central Organization for Control and Auditing
COFOG	Classification of Functions of Government
CPAR	Country Procurement Accountability Review
DFID	Department for International Development - UK
DG	Director General
DMFAS	Debt Management annd Financial Analsyis System
DPPR	The Socio-Economic Development Plan for Poverty Reduction
DSA	Debt Sustainability Analysis
EC	European Commission
EU	European Union
FY	Fiscal Year
GDP	Gross Domestic Product
GFS	Government Financial Statistics
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
IIA	International Internal Audit Standards
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standards
M&E	Monitoring and Evaluation
MDA	Ministries, Departments and Agencies
MOF	Ministry of Finance
MoP	Ministry of Planning and International Cooperation
MTEF	Medium Term Expenditure Framework
PAC	Public Accounts Committee
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
PSIP	Public Sector Investment Program
RIC	Regional Information Centre
TIN	Tax Identification Number
UNDP	United Nations Development Program
USAID	United States Agency for International Development
WB	World Bank
YR	Yemeni Rials

Regional Vice President	Daniela Gressani
Sector Director	Ritva S. Reinikka
Country Director	Emmanuel Mbi
Sector Manager	Miria A. Pigato
Country Manager	Mustapha Rouis
Task Team Leader	Arun Arya

Acknowledgements

The PEFA Assessment of Republic of Yemen was conducted by a core team led by: Mr. Arun Arya, Senior Public Sector Management Specialist and Task Team Leader (MNSED), and comprising Mmes/Messrs. Ronald Quist, Consultant (MNSED), Franck Bessette, Public Sector Specialist (PEFA Secretariat), Pierre Prosper Messali, Senior Financial Management Specialist (MNAFM), David Biggs, Senior Public Sector Specialist (MNSED), Mikael Mengesha, Senior Procurement Specialist (MNAPR), Akram Al Shorbagi, Senior Financial Management Specialist (MNAFM) and Saad Al Geradi, Consultant (MNSED). Ms. Abeer Yahia Aleryani, Team Assistant (MNCYE) provided the necessary administrative and technical support. Mr. Robert P. Beschel, Lead Public Sector Specialist (MNSED) provided the necessary guidance to the team. We wish to thank our peer reviewers, Mr. Salvatore Schiavo-Campo, Consultant (MNSED) and Mr. David Shand, Consultant (EAPCO) for providing their valuable insights and guidance to the draft report.

The draft report was presented before the National Stakeholders' Workshop on November 5, 2007 in which key government officials and donors actively participated. Considering the recommendations of the workshop and peer reviewers' comments, the report was revised. The government of Yemen, Ministry of Finance, constituted a PEFA Task Force under the chair of Mr. Jalal Yaqoub, Deputy Finance Minister to carefully scrutinise the revised report. The PEFA Task Force had several meetings from December 2007 to May 2008 and made its recommendations to the PEFA Secretariat in June 2008. The PEFA Task Force examined these recommendations and gave its findings as per the PEFA Guidelines. Based on recommendations of the PEFA Task Force and findings of PEFA Secretariat, the PEFA Report was finalised in June 2008 by the team.

We wish to thank the Government of Yemen, especially, His Excellency Mr. Noaman Al-Sohaibi, Minister of Finance, for taking the decision to carry out this assessment for measuring the state of present performance of the PFM Systems for setting the baseline for future PFM reforms; Mr. Anwar Kamrani, the then National PFM Coordinator, for both extensively and intensively contributing to the deliberations of all the PEFA Team meetings; Mr. Ali Shatter Mothana, Deputy Finance Minister, to chair the deliberations of the national stakeholder's workshop and firming up its conclusions and recommendations; Mr. Jalal Yaqoub, Deputy Finance Minister for chairing the PEFA Task Force and carefully scrutinising the draft PEFA Report in light of recommendations of the national stakeholder's workshop; and, Mr. Tarek Al Sharafi for anchoring and actively contributing to all the PEFA Task Force meetings. We would also like to thank different PFM institutions within the Ministry of Finance who provided their valuable time and much assistance along with the information for assessing the indicators presented in this report.

Special acknowledgment is reserved for the PEFA Secretariat who observed part of the field mission, carefully reviewed two draft versions of this report and provided some very useful suggestions that have resulted in an improved final report. A number of Government Officials and Donors carefully reviewed the Draft Report and provided very useful comments and inputs. Special mention must go to the following for their singular contributions; the Ministry of Local Authorities, the Department of Planning, Statistics and Follow up (within Ministry of Finance), Department of International Financial Relations (within Ministry of Finance), the Tax Authority, Department for Final Accounts, the Internal Audit Department and the Debt Department ((within Ministry of Finance); the Netherlands, DFID, and UNDP.

The report has benefited immensely from the active participation of many Government officials with public finance management responsibility who participated in a review workshop and discussed fully the indicator scorings.

Currency and Exchange Rates

Currency Unit – Yemen Riyals (YR)
US$1 = YR 196

Fiscal Year

January 1 to December 31

PEFA Assessment Period

The PEFA Assessment covers the period FY 2004, FY 2005, FY 2006. In accordance with the PEFA Manual, where not explicitly specified the most recent completed budget cycle at the time of the assessment was used in the case of periodic events. In the case of status indicators such as PI-10 the current year (2007) was used.

YEMEN PEFA ASSESSMENT

TABLE OF CONTENTS

EXECUTIVE SUMMARY

This Public Expenditure and Financial Accountability (PEFA) assessment was sponsored by the World Bank. The terms of reference were reviewed by the Government and all donors active in supporting Public Finance Management in Yemen. It has been undertaken in agreement with the Government of Yemen and with the assistance of the Ministry of Finance.

The assessment was prepared on the basis of:

1. The Public Financial Management Performance Measurement Framework issued by the PEFA multi-donor programme in June 2005; and

2. The demonstrated observable public finance management (PFM) practices in Yemen at the time of the assessment as determined through interviews and reviews and analysis of translated official documents.

Corroborating evidence was sought from a variety of sources wherever possible. Discussions were held with stakeholders to determine the appropriate scoring for each indicator. A field mission exit workshop and a final review workshop of the indicator scorings issued in the draft report were held in which a full representation of Government officials and Donors actively participated. Final discussions were held with Government officials and additional documentation reviewed for indicators for which differences of opinion remained. All comments received were carefully considered and used to clarify further or amend the draft report.

The purpose of the PFM Performance Report is to assess the status of the public finance management system at a given point in time[1]. It should serve as a comprehensive and holistic measure of current PFM systems operating in Yemen identifying both areas of ***strength*** and ***weakness***. It is important to emphasize that the objective of the assessment has not been to evaluate and score the performance of specific institutions or PFM officials, but rather to assess the performance of the PFM systems themselves. Its purpose has not been to report on the intent, or forecast the outcome of a number of projects carried out in the area of PFM.

Through this, the first PEFA Assessment carried out for Yemen, a baseline is to be set for the continued use and assessment of the set of 31 high-level indicators of the PEFA Performance Measurement Framework. It is anticipated that such PEFA Assessments shall be carried out every three years or so, and in so doing provide a clear and accessible basis for monitoring PFM progress over the long term. Given that purpose, the ready availability of the final report on the Internet and through other outlets, shall be necessary for guiding PFM dialogue, reform and management.

While this report, by design, neither articulates specific recommendations for PFM reform, nor details an action plan, it is anticipated that the analysis and results shall assist the Government in leading with respect to defining its PFM reform priorities and detail the subsequent reform activity sequencing and pacing schedule. Further, it should serve as a useful basis for supporting dialogue pertaining to the adoption of a strengthened approach in providing harmonized and aligned Donor support of the Government's PFM reform efforts.

INTEGRATED ASSESSMENT OF PFM PERFORMANCE

1. Credibility of the Budget

The revenue out-turn well surpasses the budget revenue estimates for all three years assessed. In principle robust revenue achievements provide a sound starting point for achieving a

[1] For most of the indicators assessed this would correspond to the budget year 2006.

credible budget. Approximately 75% of Government revenues derive from oil production. Given that, as well as the price volatility of oil, the Government adopts a conservative posture on revenue estimates to shield the budget process from excessive revenue swings[2]. This policy posture on the revenue budget however, has not been coupled with a firm articulated fiscal policy that seeks to systematically and predictably address the application of any excess revenues over such conservative revenue estimates[3]. Consequently, much of the surplus has been directed to primary recurrent expenditure and thus undermining budget credibility on the expenditure side. The current policy of subsidising domestic petroleum consumption means that with increasing oil prices and the subsequent increase in Government revenues, subsidy payments (categorised under recurrent expenditure) automatically increase. An analysis of the increased expenditures shows that even when the domestic petroleum subsidies are excluded, the increase of expenditure over original budget estimates is still substantial and to a degree that undermines the credibility of the budget[4].

There have been substantial tax reforms since 2001 including a shift to a self assessment basis for major and medium tax payers and the implementation of improved Customs systems which have translated into healthier tax revenue streams[5].

The poor matching of aggregate expenditure out-turn figures to the budget estimates reflect a lack of strict fiscal discipline exercised in budget execution. The lack of predictability in budget releases; the weak cash management in spite of many requisite elements for sound cash management being present; the non uniformly implemented commitment controls; the less than fully effective salary expenditure controls; and the non-achievement of value-for-money in procurement; the practice of ex-post approval of the supplementary budget by parliament; along with the accumulation of arrears without proper and complete tracking upon which to base their effective management and reduction all contribute to undermining the PFM capacity for achieving aggregate fiscal discipline, and consequently improving the credibility of the budget.

When one considers the variance of expenditure out-turn for the budget entities up and above aggregate expenditure deviation from aggregate budget estimates there is some evidence of the PFM systems ability to allocate resources (at least at the level of budget head) in accordance with budgetary objectives. This suggests some capacity of the PFM systems to deliver on the strategic allocation of resources, if such strategic consideration were to be incorporated into the budget.

The budget process, while it occurs within a pre-announced resource envelope based upon fiscal forecasts and takes into account policy considerations and inputs, does not reflect strong bottom-up elements within the budget entities. This is apparently due to weak reporting capacities of the budget entities to properly inform the budget process. Yemen is taking the first steps towards implementing a multi-year framework for budget estimates but this process still needs as a pre-requisite to develop stronger links with the sector development plans. The

[2] While conservative, the current budget price adopted for oil of 55 USD exceeds some other oil producing countries including Iraq and Nigeria.

[3] A number of countries, on the justification of both economic impacts as well as specific PFM considerations have opted to apply such excess revenues over budget revenue to debt reduction and/or reserves.

[4] The IMF Article IV Concluding Statement, June 2007 recommends that the phased reduction of fuel subsidies should be resumed and carried out in conjunction with improved targeting of the benefits provided by the Social Welfare Fund, as envisaged in the new draft Law on Social Welfare and currently piloted in several governorates. At the same time, part of the savings from reducing fuel subsidies should be used to increase benefit levels and the number of beneficiaries.

[5] There are still some collection difficulties encountered with small tax payers who are assessed a lump sum, however a recent joint tax collection programme with the Chamber of Commerce shows encouraging early signs.

PFM systems are capable of delivering predictable and well controlled virement procedures. Any budgetary adjustments by Line Ministries take place with clear guidelines and cannot be undertaken informally add to the credibility of the budget. However, there are considerable adjustments made above the level of Line Ministries to budget appropriations and this practice tends to undermine the credibility of the budget.

While the first four indicators (PI-1 to PI-4) focus upon a primary expenditure analysis, the issue of the credibility of the budget must take into account the whole budget including that portion which is financed by international loans and grants (see indicators PI-7 and D-2). The lack of a standard for definitions such as pledges, available funding, commitments along with clear and consistent methods for determining Donor funded budget estimates has left the Ministry of Planning in the position of largely guessing what such investment is likely to be. In response to that the Ministry of Planning has tended to adopt an extremely conservative posture which has sometimes led to projects being left out of the budget estimates[6]. These practices tend to undermine the credibility of the budget.

2. Comprehensiveness and Transparency

Yemen has evolved a fairly comprehensive budgetary process with budget documentation amounting to 38 separate volumes presented to parliament. This includes a macro-fiscal policy statement, details on expenditure and revenues for special funds, local authorities as well as the Line Ministries. The budget currently adopts an economic and administrative classification. The budget structure is being revised to reflect a functional and programmatic structure based upon GFS/COFOG standards. Fiscal forecasts are realistic even if better integration into the budget process is required. There are effective debt management controls with the Minister of Planning and International Cooperation being the sole authority for entering into loan agreements. All loans also require the Minister of Finance's endorsement and the parliament's ratification. There is a careful monitoring of the debt stock and a new debt management bill is currently being considered which includes debt ceilings as a ratio of GDP.

The Central Bank of Yemen (CBY) operates a Treasury Single Account with regular reconciliation of all transactions. The full effectiveness of the Treasury Single Account would require closer management by the Ministry of Finance. There are some amounts of extra-budgetary operations emanating out of internally generated funds held in special accounts by some of the Line Ministries though these remain an insignificant ratio of total expenditure. All revenues generated directly by Line Ministries and Revenue Agencies, including the Oil Ministry, are transferred to the Consolidated Fund, and all expenditure is made through a centralised payments system. So all domestic revenues and expenditures, save for the small amounts of internally generated funds, are transacted through the CBY Treasury Single Account. It should be noted though that while the majority of donor funds operate under a mechanism which includes the deposit of funds in the CBY, which are regularly monitored using the Debt Management Financial Analysis System (DMFAS), there are a number of major Donors who do not adhere to this arrangement and where the tracking of project implementation is less regular or timely.

A review of the mechanisms for the horizontal allocation of resources across Local Authorities reveals budget processes and financial reporting procedures that are well integrated into the central government procedures. In particular the recurrent expenditure allocations to local authorities are managed in the same way as the allocations to Line Ministries are. There has been significant reform in recent years with respect to the Local Authorities and the Local Authorities Law, 2001 provides for a rule based horizontal allocation of central government disbursements, however without a full operationalization of

[6] For example USAID reports omissions of projects in the Education sector that were excluded because these projects were not governed by a specific financing agreement.

the law and effective monitoring and evaluation mechanisms, the rule based allocation of resources has only been partially put into effect.

There have been dramatic changes in attitudes to transparency in recent years. Public access with regards to budget and other fiscal documentation remains lacking with respect to such outlets as a Government bookshop, libraries and other physical outlets. There have though been significant improvements with respect to the amount of budgetary and fiscal information that is being placed on Government websites.

3. Policy-Based Budgeting

The first steps towards implementing a multi-year budgetary framework have been undertaken. The GoY has issued a medium term national development framework (DPPR) that clearly states the medium term policy objectives. It was developed within a macro-fiscal framework though not fully costed; inclusive of recurrent cost implications. A macro-fiscal analysis is performed each year, but without sectoral work being undertaken, before budget preparation begins. Debt sustainability analysis is regularly undertaken and the debt stock is monitored and reconciled on an on-going and regular basis. Forecast of fiscal aggregates on the basis of economic classifications are prepared for three years on a rolling basis. Statements of sector strategies exist for just a few sectors. These are not all fully costed, and where that is done costings are not in line with aggregate fiscal forecasts – hence the need to negotiate retrospectively with the MoP as part of the budget process.

The budget cycle is well defined and the call circular issues clear guidelines that provide a sound context for the budget process. The budget process encompasses policy input both at the beginning through cabinet approved sector ceilings, as well as at the end by way of parliamentary debate. The executive completes its budget submissions prior to the start of the fiscal year after allowing for two and half months of budget preparation by the Line Ministries and subjected to a full negotiation process. The Parliament approves the appropriations before the start of the fiscal year after subjecting the budget proposals to vigorous debate over a two month period. The budget documents are quite detailed and appropriately address many of the requirements both for meaningful budgetary oversight and to properly guide implementation. However, there remain some issues of transparency and clarity as to how parliamentary recommendations are incorporated into budgetary implementation. While a written parliamentary recommendation is included in the appropriations law, along with an undertaking to implement such recommendations signed by the Minister of Finance there is no opportunity to directly track the implementation of the parliamentary recommendations. There would be greater transparency with regards to the inclusion of parliamentary budget policy inputs, if an approved budget prepared by the Ministry of Finance as derived from the parliamentary recommendations, was also included in the budget documents.

4. Predictability and Control in Budget Execution

There are three main sources for domestic revenue in Yemen. These are (1) oil revenues (accounting for about 75% of revenue) arising through royalties, income tax and government shares of oil production (2) income taxes, both company and individual, and (3) customs revenues. The oil revenues are governed by Production Share Agreements (PSAs) entered into with 12 oil producing companies. Actual revenue out-turn far surpasses the revenue budget and so the budget is shielded from the extreme volatility of oil prices as a result of the conservative posture adopted. While daily payments of tax receipts into the Consolidated Revenue Fund along with regular reconciliations are carried out by the Tax Agencies, regular reconciliations by the Oil Ministry are not. There are significant tax arrears, dominated by a large uncollectible component which is under consideration to be written off or addressed in some other suitable way. The collection ratio of tax arrears remains low.

The adoption of a six-month general warrant for the authority to incur recurrent expenditure, as well as the three-month general warrant for capital expenditure suggests a sound basis for predictability in budget execution. Unfortunately, at the present time, this is not coupled with pro forma revenue cash flows, or expenditure cash flows fully informed by procurement plans and implementation schedules. So in spite of in principle access to a number of requisite elements for effective cash management such as debt maturity profiles, and up to date cash balances there is no cash management currently being carried out to ensure predictable budget releases. This system of cash disbursements against an absence of cash management almost certainly leads to inefficiencies arising from having to resort to short term borrowings to a greater degree than would be necessary if cash management were appropriately applied[7]. The problem is further compounded by the practice of making adjustments from time to time to the general warrant ceilings on a basis that appears to occur principally above the level of the Line Ministries.

Virement control is strong. Virement control over transfers between budgetary chapters and sub-chapters are made at the level of the Ministry of Finance. The sub-account structure of the Treasury Single Account mirroring the chapter and sub-chapter ceilings facilitates effective virement control. AFMIS is currently being piloted in four ministries. It is hoped that its implementation will improve the level of budget execution control. However, while a commitment control module exists it has not been implemented as yet. Manual commitment control systems[8] are not uniformly implemented across all ministries. The weak commitment controls along with the updates of the General Warrant ceilings all contribute to the effects of weak credibility of the budget outlined in the first section.

Yemen, for the most part, uses a centralised payments system out of the Consolidated Fund held in the CBY and operated as a Treasury Single Account which facilitates daily bank balance consolidation that informs and controls payments. In principle such an arrangement should facilitate the prompt payment of all cheques. The lack of effective commitment controls though have led to very slow payments and what appears to be, though not verifiable, a high level of arrears.

There has been substantial reform in the area of procurement by way of the passing in July, 2007 of a new Tender Law. This is an important first step towards tackling what remains a serious challenge to achieving effective control in budget execution. The previous law did not facilitate an authority responsible for procurement policy and regulatory oversight nor did it facilitate an independent procurement appeals mechanism. These have been effectively addressed in the new law. The Central Organization for Control and Auditing (COCA) and Chamber of Commerce paint a troubling picture of procurement practice. The picture is presented as one rife with fake competition, abuse of contract variations with subsequent project overruns, non transparent tender evaluations, the too often use of direct procurement methods, the use of slicing to by pass procurement and authorisation thresholds.

The management of payroll is another area where control appears to be less than satisfactory. There has been a Civil Service Modernization Project started in 1998 which included the establishment of a clean personnel database by 2001. The project was restarted in 2005 with a re-visitation of the clean up exercise (principally of double dippers and ghosts) through a new database that includes biometric control data. When measured by the number of

[7] The MoF does not engage in any cash management at this time. It might be argued that the CBY does it. However, it should be noted that it earns a commission of 1% for issuing Government Debt instruments and so does not have the same incentives as the Treasury would have to keep debt costs to a minimum.

[8] In Yemen, it appears that the conventional wisdom with respect to both commitments and arrears is that these have no place in a cash accounting based budgetary system. Indeed this seems to be much of the impetus for wishing to adopt an accrual accounting basis. It would be quite straight forward to add commitment and arrears monitoring under the current cash basis reporting systems.

irregularities[9] uncovered through the cleanups, both exercises were highly successful. The clean up exercise covers approximately 50% of all Government employees. Not yet included at this time is a significant portion of the Ministry of Education staff, the judiciary, and the ministries of Defence and Internal Affairs. These successes though have not yet been coupled with effective direct database links between the cleaned personnel database and the payroll. There are still less than adequate reconciliation controls for the addition, termination and modification of personnel records in the fragmented payroll files. Until the completion of the implementation of effective database control links between a personnel database with full integrity and the payroll files, or adopting effective regular reconciliations between the two this leaves the payrolls vulnerable to ghosts and double dippers creeping back over time as indeed occurred with the first database created under the project..

There are two main components of internal audit in Yemen. The first, resident in all Line Ministries limits its audit activities to operational audits. The Ministry of Finance also has an Internal Audit Unit with jurisdiction over all Line Ministries, Local Authorities and Public Corporations. This unit carries out in addition to financial audits, limited systems and value for money audits. They prepare annual work plans using a risk based approach to identifying areas of focus and report regularly to the Line Minister and Minister of Finance on their findings with copies of reports submitted to COCA and the Cabinet. However, with only a full time professional staff of 16, their effectiveness is limited. There is also only limited follow up on the audit findings of the Internal Audit. The Head of the Public Entity is accountable for the management of public funds. There is a Follow Up Department within the Ministry of Finance responsible for the implementation of corrective measures and audit recommendations. Finally, within the Finance Offices of each Line Ministry are Inspectors and Controllers. Their primary role is quality assurance of expenditure procedures through the application of pre-audit methods.

5. Accounting, Recording and Reporting

Government accounting standards are applied across all ministries consistently. While the appropriations accounts adopt a few of the mandatory standards of IPSAS such as comparison between budget and actuals; the inclusion of financial assets and liabilities and the details of revenues and expenditure, not all of the mandatory standards are met. The CBY submits monthly budget Release Reports to the Ministry of Finance, based upon payments[10] made. The Final Accounts Directorate of the Ministry of Finance consolidates the accounts prepared by the Line Ministries. The financial reporting is challenged by a number of Donors not providing complete or timely financial expenditure data to the Government especially with respect to those expenditures they execute directly on behalf of their projects. The consolidated government accounts are prepared annually with revenue and expenditure information as well as a table of financial assets and liabilities. These are typically completed within nine months after the close of the fiscal year but outside of the six month requirement of the Finance Law.

The Line Ministries submit Monthly Budget Execution Returns; however these are submitted on average 12 weeks after the close of the period. These do not distinguish between commitments and expenditure. They however distinguish advances and payments and allow direct comparison of budget implementation to the original budget. The reporting format accommodates for Line Ministries to report on accrued arrears but this is often not adhered to. With the delays in the submission of the Monthly and Quarterly Budget Execution Reports their effectiveness as a management tool is undermined. There is a consolidation, though

[9] It is reported that through the clean up exercise it has been revealed as much as 14% of the database reflects double dippers and ghosts. Some officials place that figure as high as 30%.

[10] Note that such payments do not distinguish between advances, imprests and fully acquitted expenditures.

delayed, of Budget Entity submissions to an aggregate budget implementation profile which enhances the information available for policy decisions.

There have been assessments carried out on the level of expenditure carried out at the level of front-line facilities in the past three years including a Public Expenditure Tracking Survey in the Ministry of Education carried out by the World Bank, a Public Expenditure Review covering Health carried out by USAID and a Public Expenditure Tracking Survey in the Ministry of Health carried with support from DFID. These pointed to difficulties with salary payments and weak bottom up budget preparation procedures leading to a misalignment of resources.

6. External Scrutiny and Audit

Yemen is characterised by a well structured and vibrant parliamentary oversight of the government's budget estimates approval process that addresses in addition to details of the revenue and expenditure estimates reviews and debates fiscal policy. It appears though to have been less involved in actual expenditure achievements or of the quality of expenditure management in the years 2004 to 2006. The picture appears to be dramatically different in 2007. The parliament has almost completed a three volume 350 page review of the audit findings which included interviewing a number of Government officials responsible for the audit findings. The submission of the audit reports and audited financial statements from COCA is timely.

COCA has undertaken to adopt many of the INTOSAI standards but is probably best characterised as a work in progress. A draft audit bill has been completed and is currently under consideration of the President to address amongst other things the independence of the President of COCA as well as the organization. There is significant follow up on Audit findings by COCA and it has clear procedures for managing the follow up and ensuring that audit recommendations are carried out.

ASSESSMENT OF THE IMPACT OF PFM WEAKNESSES

When viewed from the perspective of the three main objectives of a sound PFM system, namely aggregate fiscal discipline, strategic allocation of resources and the efficient delivery of services, Yemen in spite of many elements that could assure that it does, has not scored very well with respect to aggregate fiscal discipline. With respect to the strategic allocation of resources its budget performance demonstrates some ability in being able to allocate resources in accordance with budgetary intent at least to the level of budget head. On the other hand smaller ministries tended to get allocated even lower that original budget estimates in spite of large aggregate expenditure excesses over original budget estimate. The efficient delivery of services remains challenged by difficulties in the area of salary controls and procurement management. Many specific individual functions of PFM are carried out very well; however it is important to keep in mind the importance of linkages between PFM activities and the tendency for a PFM system to deliver overall at a level influenced significantly by the weakest links in the activity chain. There are three main factors that colour PFM in Yemen:

1. *The large oil component of revenue*: Approximately 75% of Government revenues derive from oil. This coupled with the high price volatility means that medium and long term revenue forecasts present a special challenge to budgetary and macro-fiscal forecasts. The issue of a large oil component of the revenue budget introduces even further complexity given that Yemen's proven oil reserves are on the decline.

2. *Capacity constraints:* While there is considerable capacity in many areas of Public Finance Management, the great majority of spending units spread across the country within the districts and line ministries are operated on a manual basis

and do not have adequately trained personnel. For that reason, the Inspectors and Controllers within the Finance Units of the Line Ministries serve to provide quality assurance for the execution of expenditure management. The recent decentralization efforts that have moved much more responsibility directly to the Local Authorities appear to have further exacerbated the capacity challenges.

3. *It is currently undergoing the substantial reform of its legal and regulatory framework*: In the past five years or so Yemen has undergone a tremendous amount of reform by way of its legal and regulatory framework which has sometimes meant a reform of the institutional arrangements responsible for delivering on public finance management. This has meant that this assessment was often forced to assess works in progress.

Aggregate Fiscal Discipline: With respect to aggregate fiscal discipline Yemen's robust revenue performance, well developed debt monitoring and credible three year fiscal forecasts along and a comprehensive and policy-capable budget process schedule all point to the ability to deliver on aggregate fiscal discipline (see PI-2, PI-3, PI-9, PI-11and PI-17). However, there remain important challenges towards meeting this objective including the absence of an effective cash management system to support predictable budget releases and weaknesses in the application of commitment control systems. Also, the evidence points to significant losses both with salary payments and procurement.

Strategic Allocation of Resources: Yemen has taken a number of important initial steps towards achieving a number of pre-requisites for a budgetary process that is fully capable of the strategic allocation of resources (see PI-5, PI-6, PI-11 and PI-12); however there are still a number of important steps that remain to be implemented. The budget schedule in Yemen well supports policy inputs in to the budgeting process. On the other hand the practice of justifying supplemental budgets ex-post undermines the achievement of a strong strategic element to actual budgetary achievements.

The Government of Yemen issued the DPPR to serve as its national development framework which includes a clear articulation of its development policy objectives. The DPPR development objectives rely heavily upon Donor inputs and so will require close alignment of donor grants and loans with the budget. Eventually, after achieving all of the pre-requisites necessary for a successful implementation, Yemen intends to implement a Medium Term Expenditure Framework (MTEF) to serve as a translation mechanism for Government policy and strategic planning into a budgetary instrument. An MTEF would also serve as a focal point for Donor alignment with Government policy in its support of the budget.

Efficient Service Delivery: The apparently high levels of arrears (see PI-4) and weaknesses in the procurement systems (PI-19) as well as in controlling payroll (PI-18) all point to value for money not yet an outcome of Yemen's PFM systems. Procurement planning would go a long way towards improving efficiency. Yemen has not yet achieved sufficient efficiency in it service delivery. It is apparent that while top down discipline remains strong a stronger bottom-up participation in the budget preparation process would introduce opportunities to better align the budget with actual needs.

PROSPECTS FOR REFORM PLANNING AND IMPLEMENTATION

The Government of Yemen has adopted a comprehensive PFM Reform strategy approved by Cabinet in 2005. The strategy identifies six main objectives. These are: to improve the level of priority setting and basis for decision-making; improve budget execution; develop public finance management information systems; enhance control and financial accountability; improve the system of bidding and procurement; and improve capacity and skills of public finance staff.

There have already been a number of PFM reforms that have recently been implemented, some of which have already shown measurable impact on PFM performance. These include:

- The reform of taxation with the implementation of the self assessment basis. The adoption of ASYCUDA ++ for customs processing and the move to ASYCUDA World being supported by USAID;
- The enactment of a number of laws including the Anti-Corruption Law, the Tender Law and the Local Authorities Law;
- The adoption of the GFS/COFOG budget classification standard which will see functional budget classification by the 2009 budget submission;
- The cleaning up of the personnel rolls and the introduction of a biometric identification system under the Public Service Modernisation Project, managed by the Civil Service Ministry and supported by the World Bank; and
- The testing[11] and piloting of an integrated financial management system (AFMIS) in four ministries, namely the Ministries of Finance, Education, Health and Public Works.

The PFM Reform Programme in Yemen has political championship at the very highest levels. The institutional arrangements for implementation of the PFM Reform Programme start with the overall responsibility for implementation being vested in the Ministerial PFM Reform Committee. A PFM Reform Task Force headed by the Deputy Minister of Finance in charge of Budget is responsible for overseeing the implementation of the reforms. There are a number of Technical Committees that have responsibility for specific PFM Reform activities. At the present time there has been no clear structure set up to directly manage PFM Reform. Specifically, no clear components have been defined for the PFM Reform pillar, with specific component managers tasked with clear roles and responsibilities each with a clear set of activities, targeted outputs, fully costed inputs, monitoring indicators and reviewable milestones. There are no arrangements to coordinate linkages between different PFM reform components, a key to managing PFM reforms, and no specific arrangements for managing the implementation of the reforms within the Line Ministries. The PFM reform programme, started in 2005, was only integrated as a separate programme within the Ministry of Finance budget in 2007. The lack of due consideration given to recurrent expenditure consequences of the PFM reforms raises questions about sustainability. It should be noted that most of the reforms have centred upon MoF and Civil Service Ministry activities rather than distributed activities rolled out to all the Line Ministries.

The PFM Reform effort has attracted substantial Donor support and at this time there is a very active Donor Harmonization Group specifically for PFM Reform in Yemen. There is indication that such support would yield even better results if there was closer and stronger alignment with Government reform plans and implementation, and more cognizance of capacity constraints in attempting to implement all of the PFM Reforms simultaneously without careful consideration given to prioritization and out roll out schedules.

[11] The AFMIS outputs are being tested by KPMG Cairo to ensure accuracy and reliability.

Table 1
Summary of PFM Performance Scores

PFM Performance Indicator	Score	Method
A. Credibility of the Budget		
1. Aggregate expenditure out-turn compared to original approved budget	**D**	M1
2. Composition of expenditure out-turn compared to original approved budget	**C**	M1
3. Aggregate revenue out-turn compared to original approved budget	**A**	M1
4. Stock and monitoring of expenditure payment arrears	**<NS>**	M1
B. Comprehensiveness and Transparency		
5. Classification of the budget	**C**	M1
6. Comprehensiveness of information included in budget documentation	**A**	M1
7. Extent of unreported government operations	**B+**	M1
8. Transparency of Inter-Governmental Fiscal Relations	**A**	M2
9. Oversight of aggregate fiscal risk from other public sector entities.	**C**	M1
10. Public Access to key fiscal information	**C**	M1
C (i) Policy-Based Budgeting		
11. Orderliness and participation in the annual budget process	**A**	M2
12. Multi-year perspective in fiscal planning, expenditure policy and budgeting	**B**	M2
C (ii) Predictability and Control in Budget Execution		
13. Transparency of taxpayer obligations and liabilities	**B**	M2
14. Effectiveness of measures for taxpayer registration and tax assessment	**B**	M2
15. Effectiveness in collection of tax payments	**D+**	M1
16. Predictability in the availability of funds for commitment of expenditures	**D+**	M1
17. Recording and management of cash balances, debt and guarantees	**B+**	M2
18. Effectiveness of payroll controls	**D+**	M1
19. Competition, value for money and controls in procurement	**D+**	M2
20. Effectiveness of internal controls for non-salary expenditure	**D+**	M1
21. Effectiveness of internal audit	**D+**	M1
C (iii) Accounting, Recording and Reporting		
22. Timeliness and regularity of accounts reconciliation	**B**	M2
23. Availability of information on resources received by service delivery units	**B**	M1
24. Quality and timeliness of in-year budget reports	**D+**	M1
25. Quality and timeliness of annual financial statements	**C+**	M1
C (iv) External Scrutiny and Audit		
26. Scope, nature and follow-up of external audit	**B+**	M1
27. Legislative scrutiny of the annual budget law	**C+**	M1
28. Legislative scrutiny of external audit reports	**D+**	M1
D. Donor Practices		
D-1 Predictability of Direct Budget Support	**D**	M1
D-2 Financial information provided by donors for budgeting and reporting on project and program aid	**D+**	M1
D-3 Proportion of aid that is managed by use of national procedures	**D**	M1

M1 scorings are based upon the lowest scored dimension making up that indicator
M2 scorings represent an aggregate scoring of the dimensions making up that indicator
<NS> indicator could not be scored due to unavailability of data or the lack of reliable data.

1. INTRODUCTION

1.1 OBJECTIVE OF THE PUBLIC FINANCIAL MANAGEMENT PERFORMANCE REPORT

1.1.1.1 The purpose of this Public Expenditure and Financial Accountability (PEFA) Assessment has been to assess the current status of the Yemen's Public Finance Management (PFM) systems based on the PEFA indicators; a set of **28** high level performance indicators that measure the Central Government's PFM systems **plus 3** more high level performance indicators that measure the performance of Donors involved in the Government's budgetary processes. This assessment is being carried out in order to set a baseline for the continued use and assessment of these indicators. The performance indicators is presented along with a narrative to provide a brief description of the PFM processes and procedures adopted by the Government, and also to support and explain the scorings. In addition to the performance indicators the PFM performance report reviews the Yemen economic context in which such PFM is carried out, the legal and regulatory framework, the institutional arrangements and an assessment of the PFM reforms being undertaken in Yemen.

1.1.1.2 This evaluation is in keeping with the Strengthened Approach to supporting PFM reform[12]. It aims to achieve better public financial management systems in countries through effective engagement and support over PFM reforms – reducing the transaction costs of some practices and focusing on reform results rather than inputs and activities. The three main objectives of the Strengthened Approach for Yemen are:

- *Adopting a country-led agenda for PFM reform in Yemen* which is fully cognizant of its capacity constraints and being willing to accept second-best reform alternatives should that be the price to ensure Government leadership in undertaking the PFM reform process.
- *Promoting a coordinated program of Donor support and alignment around Yemen's PFM reform agenda* through a dialogue between government and donors operating as a harmonised group, and incorporating analytical and advisory work, technical assistance, funding support and training which are appropriately phased over a medium term time frame.
- *Monitoring Yemen's PFM reform results through a common information pool*; This Performance Measurement Report is intended to serve as a common information pool on PFM performance in Yemen for government, donors and other stakeholders at country level. The report set out below will also serve as one element for the monitoring and evaluation on a long term basis the outcomes of the PFM reform.

1.1.1.3 The immediate impetus for carrying out this PEFA Assessment as identified in the Terms of Reference (ToR) is to enhance implementation of the PFM Action Plan through more efficient and effective resource allocation and utilization by assessing the status and evolution of performance indicators in public finance management. It states as its immediate objectives to be to provide Government and the Donors with an assessment of the current quality of PFM in the country and provide a status of the situation as at the end of 2006. In keeping with the Strengthened Approach and hence adopting a harmonised approach, it was agreed to conduct a full PFM assessment in accordance with the Performance Measurement Framework developed by the PEFA Secretariat[13]. It is

[12] For more information on the Strengthened Approach to supporting PFM reforms see for example Issues Paper No. 1 available off the PEFA Secretariat website at www.pefa.org.

[13] PEFA is a multi-agency partnership program sponsored by: the World Bank, the International Monetary Fund, the European Commission, the United Kingdom's Department for International Development, the French Ministry of Foreign Affairs, the Royal Norwegian Ministry of Foreign Affairs, the Swiss State Secretariat for Economic Affairs, and the Strategic Partnership with Africa.

important to emphasize that the purpose of this evaluation has not been to evaluate and score particular institutions or responsible individuals in the Government. The focus of the PFM Performance Measurement Framework both with respect to intent and execution is solely on the PFM systems.

1.2 PROCESS OF PREPARING THE PFM-PR

1.2.1.1 This PEFA assessment was sponsored by the World Bank which prepared the terms of reference (ToR)[14]. The ToR was circulated to a number of development partners and to the Government for comment. Several weeks prior to the start of the mission a review of previous PFM assessments was made and a work plan prepared by the Consultant. The plan foresaw three field missions.

- In the first, a week long mission, two one-day training workshops on the PEFA methodology were carried out for Government Officials as well as Donors. Also during this mission a detailed work plan was developed along with a list of required documents and a requested schedule of meetings spanning the four week second field mission and shared with Government and Donors. Some documentation available electronically was obtained prior to the start of the second mission.

- The second mission was for four weeks and involved primarily the interviewing of government and donor officials as well as the review and analysis of budget and other PFM documentation. There was excellent cooperation from Government officials in terms of making time available; sometimes on short notice in spite of pressing simultaneous budget process demands. Officials were fully engaging during meetings. Often information requested was provided promptly, but in a few instances some officials were reluctant to provide information due to concerns that might cause them some difficulty. An exit briefing was carried out at the end of the second field mission at which time an exit draft was presented. The draft PEFA Report was circulated to Government Officials and to the Donors for review and comment. A copy was also sent to the PEFA Secretariat for review and compliance testing with the PEFA standards, report formats and methodological approach.

- The third field mission was for a week and included a workshop where the final PEFA Report scorings were presented and fully discussed. Final exit meetings were carried out to discuss scorings review additional material and to clarify statements in the narrative so as to address remaining differences of opinion.

1.3 METHODOLOGY FOR THE PEFA EVALUATION

1.3.1.1 The PEFA evaluation was carried out between June 18th and November 5th, 2007[15]. Meetings were arranged with the assistance of the PFM Coordinator. The PEFA evaluation involved:

- Reviewing previous PFM diagnostics and studies performed on Yemen including: the Country Financial Accountability Assessment (CFAA) 2004, Country Procurement Assessment (CPAR) 2003, and the IMF Article IV Report January 2005.
- Reviewing documentation posted on Government websites including www.yemencustoms.gov.ye, www.tax.gov.ye, www.coca.gov.ye, www.afmis.gov.ye and www.mof.gov.ye.
- Assessing the requirements for further analysis and evaluation of PFM practice in Yemen based upon interviews with Government Officials, donors and private sector

[14] See Appendix II

[15] The evaluation was carried out by Ron Quist , Saad Geradi under contract to the World Bank and Franck Bessette from the PEFA Secretariat assisted from a methodological and procedural point of view.

organizations; quantitative analysis of official financial and budgetary data; reviews and assessment of legal and regulatory documentation; assessments of PFM procedures and systems; and the application of professional judgement

1.4 SCOPE OF THE ASSESSMENT

1.4.1.1 The assessment of Yemen's PFM covers the fiscal years 2004, 2005 and 2006[16]. The assessment of Yemen's PFM covers all public expenditures of the central Government and the institutions responsible for such. Public expenditure in Yemen is highly centralised, and the central government's budget covers approximately 43% of public sector expenditure. The public sector is made up of the Central Government made up of 34 ministries and departments and 22 Governorates, 5 Autonomous Government Agencies and 14 Special Funds, Public and mixed sector (Public-Private Sector) Corporations and 303 Local Authorities.

Table 1.1
Table of Public Expenditure Segregated by Government Classification

	2004		2005	
	Amount	**%**	**Amount**	**%**
Central Government	764,368,101,656	38%	1,041,441,615,739	37%
AGA's	73,142,279,198	4%	98,295,536,054	4%
Special Funds	80,586,578,629	4%	103,918,632,255	4%
Local Governemt	128,837,000,000	6%	155,112,000,000	6%
Public Corporations	973,326,000,000	48%	1,401,575,000,000	50%
Total	**2,020,259,959,483**	**100%**	**2,800,342,784,048**	**100%**

Central Government, AGAs and Special Funds data obtained from final accounts submitted to parliament, Local Government data obtained from the Budget Directorate and Public Corporations data obtained from the Planning, Statistics and Follow Up Department. Note the Public Corporations data includes expenditure of public-private corporations.

1.4.1.2 The structure of the rest of the evaluation report is as follows:

- Section 2 provides background information and the economic and fiscal context for the evaluation;
- Section 3 explains the scores for the 31 individual performance indicators;
- Section 4 describes the government's reform programme; and
- A series of appendices provides more detailed reference information, including a summary of the PEFA scoring calibration (Appendix 1), the ToR for the evaluation (Appendix 2), and a list of the stakeholders visited by the team (Appendix 3), and a list of the documentation reviewed (Appendix 4). Comments on the draft report and the responses are presented in Appendix 5. In Appendix 6 is presented an organigram of the Ministry of Finance.

[16] Note that there are a number of specific indicators that do not refer to all three years of the time frame and may refer to the most recent two or the most recent i.e. 2006. The PEFA manual specifies which year or years are to be applied.

2. COUNTRY BACKGROUND INFORMATION

2.1 DESCRIPTION OF COUNTRY ECONOMIC SITUATION

2.1.1.1 Yemen is a developing country with a per capita GDP of approximately US$ 930 reported in 2006. It is evolving its democratic traditions and institutions. The legal and institutional framework for fiscal management has seen extensive reform in recent years. Its economy relies heavily on oil, services and agriculture. In 2004, oil accounted for 72% of government revenue, more than 86% of export earnings and 35.1% of GDP. This dependence leaves Yemen's external and fiscal accounts vulnerable to fluctuations in international oil prices. The proven oil reserves of Yemen, divided between nine oilfields, are on the decline; even though exploration efforts continue.

2.1.1.2 Yemen has a high illiteracy rate, a severe water shortage problem and with the majority of the population under the age of 24 years. Yemen with a population of approximately 19.4 million people in 2004, most of whom live in the rural areas and a population growth rate in recent decades among the highest in the world, faces special socio-political challenges with respect to high unemployment and extreme scarcity of natural resources such as water.

2.1.1.3 The over-arching framework for medium-term economic programmes is the five-year Socio-Economic Development Plan for Poverty Reduction (DPPR) covering the period 2006 to 2010 and incorporating as its policy focus the Millennium Development Goals (MDGs). Specifically, the DPPR aims at strengthening democratisation, improving governance, deepening citizens' participation in development processes and enhancing the people's standard of living. The DPPR acknowledges high population growth, water shortages, high unemployment, low human resources development and fragile infrastructure as major challenges. The long term goals set by the government are: to move Yemen from the Low to the Middle Human Development Group by 2025, to sustain higher economic growth (beyond 7%) and to halve poverty by 2015 (from 1998 levels). The development framework targets an average real GDP growth rate of 7.1 percent for the period, a deficit not to exceed 3 percent of GDP and central government debt below 60% of GDP. It targets investment spending to increase to 30% of expenditure with an inflation rate held below 13.8 percent.

Table 2.1
Selected Economic Indicators 2001 to 2006

Year	2001	2002	2003	2004	2005	2006
1. Population						
Population (Millions)	17.7	18.3	18.8	19.4	20.6	
Growth (%)	3.00%	3.00%	3.00%	3.00%	3.00%	
2. National Accounts						
Real GDP Growth Rate	3.8%	3.9%	3.7%	4.0%	5.6%	3.2%
Per Capita GNP (US$)	520	544	574	649	761	869
3. Domestic Saving and Investment						
Gross National Savings/GDP (%)	20.39%	16.80%	16.20%	13.90%	15.80%	18.40%
Gross Domestic Investment/GDP (%)	19.6%	18.5%	20.7%	20.0%	18.5%	16.40
4. Overall Balance(Deficit) (US$ million)	274.6	77.3	493.2	299.5	305.1	146.9
Overall Balance (Deficit) as Share of GDP	2.79	- 0.72	- 4.19	- 2.15	- 1.81	0.79
5. Average annual inflation rate (%)	11.9%	12.2%	10.8%	12.5%	11.8%	18.5%
6. Average Exchange Rate (YR/US$)	168.69	175.62	183.45	184.78	191.52	197.05

Sources: Government Finance Statistics, IMF Article IV – Yemen 2004, The Macro Economic Framework of the 2008 Draft Budget prepared by the MoF :Planning, Statistics and Follow UP Sector

2.1.1.4 Table 2.1 presents selected economic indicators. It shows a steady GDP growth rate between 3.2% and 5.6% through 2005 with a slowing down in 2006. Only in 2006 was there a positive overall balance, after several years of overall deficit in spite of robust oil revenues. Inflation showed a marked increase to 18.5% in 2006 after several years between 10% and 12%. The ratio of external debt to GDP stands at approximately 39%. Foreign exchange reserves can ensure 16 months of imports but they are threatened by the negative trend in the current account balance; this despite the increases in oil prices. Official unemployment was at 16.5% in 2004, but, according to unofficial estimates it could be double that and is expected to grow because 50% of the population is under 15.

2.1.1.5 In 2006 Transparency International ranked Yemen 119th on its Corruption Perception Index. That is above Pakistan (147th), and Russia (127th), and below Libya (107th), Egypt (73rd) and Turkey (60th).

2.1.2 Overall Government Reform Program

2.1.2.1 The overall government reform program as articulated in the DPPR (summarised above in 2.1.1.3) defines a national development strategy focused on five pillars premised upon achieving a sustained economic growth of 7% over the medium term, with a focus on agriculture, fisheries, energy and water. As a result, infrastructural development and an increased emphasis on education and training are major aspects of the economic growth strategy. Yemen's poverty reduction strategy focuses upon the promotion of economic growth and job creation, the development of skills, providing quality healthcare and the alleviation of severe poverty through direct interventions. This will require basic health and education services as well as utilities (e.g. water, electricity, and road access) and the maximising of the effectiveness of government financial resources allocated for poverty reduction programmes.

2.1.3 Rationale for PFM Reforms

2.1.3.1 The overall government reform program serves as the rationale for PFM reforms. The Government has a development plan. In order to deliver on that plan it requires a budget formulation process for translating the plan into budgetary outcomes. It needs to have a budget that has an appropriate policy based classification structure to deliver on its poverty reduction programmes and the capacity for the efficient delivery of services to ensure effectiveness of its financial resources allocated for poverty reduction programmes. Sound PFM systems, achieved through PFM reform, will provide it with a budget instrument with the capacity to deliver on its policy objectives; to deliver on its plan.

2.2 DESCRIPTION OF BUDGETARY OUTCOMES

2.2.1 Fiscal Performance

2.2.1.1 Yemen's ability to mobilize domestic resources has been impressive over the last three years with revenues increasing between 32% and 38% over the three year period reviewed leading to primary surpluses increasing from 1.5% in 2004 to 4.5% in 2006. This has resulted primarily from increases in oil prices. These results have enabled the country to achieve a sustainable fiscal framework, as defined by a decreasing overall balance. There has been an increase in recurrent expenditures arising out of increases in the wage bill and subsidies at the expense of the development budget. Such a continuing trend shall pose a challenge to the Government's objective of meeting the Millennium Development Goals. Table 2.2 below provides a summary of the central government's fiscal operations.

Table 2.2
Summary of Central Government Fiscal Operations expressed as a percentage of GDP

Fiscal Year	2004	2005	2006
Revenue and Grants	**31.7**	**34.6**	**38.3**
Expenditure	**32.3**	**34.5**	**36.1**
Recurrent Expenditure	24.1	26.6	28.4
Wages and Salaries	9.2	9.1	10.3
Other Recurrent Expenditures	4.2	4.0	4.5
Transfers and Subsidies	8.5	11.4	11.2
Interest	2.1	2.2	2.4
Development Expenditure	8.2	7.9	7.7
Fiscal Balance (Exclusive of Ammortization)	**- 0.6**	**0.1**	**2.2**
Primary Surplus/Deficit	**1.5**	**2.3**	**4.6**

Source: Derived from tables presented in The Macro Economic Framework of the 2008 Draft Budget prepared by the Planning, Statistics and Follow-up Sector of the Ministry of Finance.

2.2.2 Allocation of Resources

2.2.2.1 On considering the ratios of personnel emoluments, other recurrent transactions and capital expenditure to primary expenditure (exclusive of interest and amortization payments) one observes a personnel emolument ratio having stayed steady and averaged 30% during the period of PEFA assessment. The results of the calculated budgetary ratios are presented in Table 2.3. The figures depict a decreasing ratio in capital expenditure. As shown in Table 2.3, the composition of expenditure by economic classification is still highly skewed towards recurrent items despite the restructuring efforts. Approximately 25 per cent of total expenditure is available to finance development activities. Salaries and wages, interest payments and pension payments continue to rise, keeping recurrent expenditures high. The continuing policy on subsidizing domestic petroleum consumption also gives rise to increases in recurrent expenditure.

Table 2.3
Expenditure Ratios of Personnel Emoluments,
Other Recurrent Charges and Capital Expenditure

Fiscal Year	2004	2005	2006
Personnel Emoluments Ratio	30%	28%	31%
Other Recurrent Charges Ratio	14%	12%	13%
Transfers and Subsidies	28%	35%	33%
Capital Expenditure Ratio	27%	24%	23%
Totals	100%	100%	100%

Ratios derived from Table 2.2

2.2.2.2 There is, broadly speaking, some conformity with the DDPR by way of focus on the social sectors; however during the period of the PEFA assessment this sector has evidenced significant declines. It would appear that much of the reason for the decline has been the increased oil subsidies (reflected in the MoF expenditure) on domestic petroleum consumption. Agriculture and Fisheries which are identified as areas of growth in the DPPR have also seen a decline.

Table 2.4
Estimated and Actual Primary Expenditure Allocations by Budget Head

	2004		2005		2006	
Budget Head	**Estimate**	**Actual**	**Estimate**	**Actual**	**Estimate**	**Actual**
Presidential House	2.3%	2.7%	2.3%	2.3%	1.9%	2.2%
Parliament	0.4%	0.3%	0.4%	0.3%	0.3%	0.4%
Judiciary Authority	1.4%	2.3%	1.6%	2.1%	1.2%	1.1%
Supreme Com. For Elections	0.1%	0.0%	0.1%	0.1%	0.0%	0.1%
Ministerial Cabinet	0.7%	0.5%	0.7%	0.6%	0.6%	0.7%
Ministry of Foreign Affairs	1.6%	1.3%	1.6%	1.1%	1.1%	0.9%
Ministry of Emmigrants	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Ministry of Human Rights	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Ministry of Legal Affairs	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Ministry of Planning & Int.Cop	1.3%	0.4%	1.2%	0.5%	1.0%	0.2%
Ministry of Civil Service	0.6%	0.6%	1.2%	0.5%	0.7%	0.4%
Ministry of Finance	22.6%	29.8%	15.4%	33.6%	29.5%	34.3%
Ministry of Local Administr.	1.1%	0.9%	1.4%	0.9%	1.5%	1.1%
Ministry of Internal Affairs	5.8%	6.4%	7.0%	5.7%	6.8%	6.8%
Central Org. for Polit. Security	0.8%	0.8%	0.8%	0.7%	0.8%	0.7%
Ministry of Defence	18.1%	17.2%	18.9%	15.8%	17.4%	18.6%
Ministry of Education	19.6%	15.2%	20.4%	14.1%	15.1%	13.5%
Ministry of Higher Ed.&Resear	4.7%	3.2%	4.5%	2.9%	3.7%	2.8%
Ministry of Vocational Training	1.0%	0.5%	1.3%	0.5%	1.2%	0.7%
Ministry of Health & Populat.	5.1%	5.3%	6.0%	4.3%	4.8%	3.8%
Ministry of Soc.Affairs &Lab.	0.3%	0.2%	0.4%	0.2%	0.2%	0.2%
Ministry of Youth &Sports	0.7%	0.4%	0.6%	0.2%	0.5%	0.4%
Ministry of Culture &Tourism	0.4%	0.2%	0.4%	0.3%	0.3%	0.2%
Ministry of Information	1.1%	0.9%	1.1%	0.8%	1.0%	0.8%
Ministry of Pub.Works &Roads	5.7%	8.9%	7.7%	9.8%	6.9%	8.5%
Ministry of Agriculture	2.0%	1.1%	2.0%	1.2%	0.8%	0.8%
Ministry of Fisheries	0.2%	0.2%	0.3%	0.3%	0.2%	0.1%
Ministry of Oil &Min.Resource	0.2%	0.1%	0.2%	0.1%	0.2%	0.2%
Ministry of Electricity	0.1%	0.0%	0.1%	0.0%	0.1%	0.0%
Ministry of Water & Environment	1.5%	0.3%	1.8%	0.9%	1.8%	0.1%
Min. of Com.&Inf.Techn.	0.0%	0.0%	0.0%	0.0%	0.1%	0.0%
Ministry of Transportation	0.1%	0.1%	0.1%	0.0%	0.1%	0.0%
Ministry of Trade&Industry	0.4%	0.2%	0.3%	0.2%	0.2%	0.2%
Orientation & Guid. Sector	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%
Total	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**

2.2.3 Support to Yemen's Macroeconomic Reform Programme and Public Financial Management (PFM)

2.2.3.1 The DPPR, (2006-2010) is the second in a series of national plans designed to fulfil Yemen's Strategic Vision 2025. Its genesis lies in the national Poverty Reduction Strategy (PRS) for 2003-2005 and serves as the central theme for cooperation and partnership with the international community. Targeted budget support from the Netherlands has been provided on the basis of the status of Public Financial Management systems in place in Yemen and the progress made in improving those systems. Other International Development Partners active in supporting Yemen include the World Bank, the Arab Fund for Social and Economic Development, Germany, DFID, EC, Netherlands, USAID, France and JICA. Yemen's is currently preparing for its candidacy to the US Millennium Challenge Account (MCA) Threshold Programme.

2.2.3.2 Over the last few years, several assessments have been undertaken in the field of PFM, most notably the World Bank's CFAA (Country Financial Accountability

Assessment) of 2004, USAID Public Expenditure Reviews in 2006 and the World Bank Country Procurement Assessment Report (CPAR) 2003. These assessments provide a basis for further donor harmonization.

2.3 LEGAL AND INSTITUTIONAL FRAMEWORK FOR PFM

2.3.1 Legal Framework

2.3.1.1 *The Constitution:* The Constitution of the Republic of Yemen provides the basis of PFM in Yemen. It sets out the broad parameters for PFM. The Constitution establishes Parliament as the supreme authority in matters of public funds' management and also provides for a supreme audit function. It lays down the basis for the functioning of the President of the Central Organisation of Audit and protects against any restrictions on access to information on public finance or in the exercise of his audit functions. It states that funds can only be spent in line with the Constitution or as authorised by an appropriation law. The Constitution stipulates that the Minister shall prepare and lay before the parliament the estimates of the revenues and expenditure of Yemen for that financial year.

2.3.1.2 *Finance Law 1990 (amended 1999):* This act and its regulations detail the management of the main elements of PFM in Yemen including payments and withdrawals from the consolidated fund, the management of contingencies and also the administration of Government accounts and loans. It stipulates that all revenues must be deposited into the Central Bank. It lays down financial management procedures covering the budget process, cash and debt management, accounting, reporting, internal controls and the audit and legislative oversight to be exercised over these functions. The Minister of Finance is responsible for supervising the government's finances and ensuring a full accounting to Parliament. The Finance Law stipulates that the Ministry of Finance shall within nine months of the close of each financial year submit accounts showing fully the financial position of the State to the Council of Ministers and then to Parliament.

2.3.1.3 *The Tender Law (1997):* served as the legal instrument for the management of auctions, procurement and stores during the period of the review. The procurement regulations are outdated and do not include many of the requirements of a sound public procurement system including efficiency, fairness and transparency and the institution of an independent public procurement oversight authority responsible for policy, regulation and inspection nor does it accommodate the institution of a public complaints review board. *The Tender Law (2007):* enacted in July 2007 is a modern procurement law that focuses on transparency and accountability and properly addresses public procurement oversight as well as administrative review and appeal.

2.3.1.4 *Central Organization for Control and Auditing (1992) Act*: outlines the role and responsibilities of the Central Organization for Control and Auditing (COCA) and facilitates a degree of financial independence as its budget is not subject to review by the Ministry of Finance.

2.3.1.5 *The Civil Service Law:* governs the procedures for initiating and terminating employment within the public sector and the general management of the public service. It outlines the procedures and authorities for setting the establishment for the public service.

2.3.1.6 *Yemen Budget Implementation Guidelines:* governs budget classification and the control of virement across budget sub chapters, items or sub items. It addresses the rate at which budget releases shall be made for personnel emoluments as well as other recurrent costs. Each administrative unit shall have its own accounting unit. This unit shall be responsible for executing all financial and accounting operations.

The accounting unit shall prepare the monthly, periodical, and final account statements.

2.3.1.7 *Draft Legislation*: Work has begun on a Procurement Bill, a new Finance Bill, a Tax Bill a Customs Bill, Debt Management Bill and a Loans and Guarantees Bill.

2.3.2 Institutional Framework for PFM

2.3.2.1 Following unification in May 1990, Yemen has evolved as a democratic state based on a multiparty parliamentary system. The executive branch comprises the President and the Council of Ministers. The President is elected by direct popular vote and the Presidential term of office is seven years. The Council of Ministers is appointed by the President upon the advice of the Prime Minister. The parliament is unicameral. The 301 deputies of the House of Representatives are elected by direct popular vote every six years. The 111 members of the *Shura* are appointed by the president and serve as an advisory council.

2.3.2.2 *The Executive:* Executive authority is established in the office of the President. The Prime Minister is responsible for the day to day running of government affairs. The Minister of Finance is responsible for the management of public finances. The Minister appoints Accounting Officers to each ministry and department with responsibility for safeguarding of public funds; ensuring the application of funds as intended by Parliament and in accordance with approved policy, responding to all information requests required by the Minister of Finance and the President of COCA; maintain financial records in accordance with the financial regulations; maintain an efficient system of internal controls and submit the financial, accounting and stores records to the President of COCA. The Central Government adopts a public administration institutional framework that extends over 22 Governorates.

2.3.2.3 *The Legislature*: The Parliament is unicameral. The Parliament votes on the budget but has no authority to directly amend budget lines. The Public Accounts Committee is responsible for oversight of the management of all public funds. The Secretary General of the House serves as Clerk of the House.

2.3.2.4 *Judiciary:* The judiciary is constitutionally independent from the other two branches of government. It includes an appeals court.

2.3.2.5 *The President and Cabinet:* serve as the highest policy and authorization body of government. It serves as the highest executive body in the management of public finance in Yemen.

2.3.2.6 *Minister of Finance:* The Minister of Finance is responsible to the Cabinet and Parliament for ensuring compliance by the Ministry of Finance with its responsibilities under the Republic of Yemen Finance Law. These include the formulation of national economic policies and managing and co-ordinating the collection of national revenues and the distribution of the Government's financial resources.

2.3.2.7 *The Ministry of Planning:* is responsible for the preparation of the investment budget. The Minister of Plannins and has the sole authority for signing loan agreements.

2.3.2.8 *President of Central Organization of Control and Audit (COCA):* The President of COCA's mandate comes not from a specific act but rather from the Constitution, the Finance Law (1990) and various sundry pieces of legislation. In addition to its audit duties, it also conducts special investigations for the Cabinet, the Minister of Finance, and the PAC. The Constitution provides a degree of independence for its operations including budgetary and operational independence.

2.3.2.9 *The Supreme Government Tender and Auction Committee:* The Supreme Tender Committee is responsible for the endorsement of tenders over given thresholds that are evaluated as winning. Each Line Ministry constitutes a Tender Committee to address bid selections below the Supreme Tender Committee thresholds. The Ministry of Public Works is responsible for the registration of contractors for Government procurement.

2.3.2.10 *The Economic Unit, Ministry of Finance :* is responsible for the financial oversight of public corporations and other self financing public bodies. The operational oversight is the responsibility of individual Line Ministries to which they are assigned.

2.3.2.11 *Line Ministries and Sub National Levels of Government:* Accounting Officers are appointed for each Ministry. This assigns specific responsibilities including compliance with the Republic of Yemen Finance Law as well as sound economic and expenditure management of the Ministry's affairs. The Accounting Officer serves as the custodian of public funds.

2.3.2.12 *Finance Officers within Line Ministries:* Within the Line Ministries, finance officers, accounts officers, cashiers, and procurement officers report functionally to the Ministry of Finance. They however report administratively to the accounting officer of the line ministry in which they serve.

2.3.2.13 *Sub National Levels of Government:* There are two main tiers of sub national government in Yemen. The first is at the Governorate level (22) whose executive is headed by a Governor, with the rank of a minister and appointed by republican decree. There is a local council whose members are elected by the districts. The second tier are made up of the district councils (303) headed by a council chairman. Both tiers have the right to raise revenues..

2.3.2.14 *The Anti Corruption Commission:* An eleven member body voted by parliament and operational since June 2007 is responsible for oversight of all public bodies and for the prosecution before the courts of all identified instances of corruption.

2.3.2.15 *Summary of Institutional Responsibilities*: Table 2.5 presents a matrix of institutional responsibilities for the different PFM functions including the institutional arrangements for carrying out PFM reform. It provides an "at a glance" view of the institutional arrangements under which public finance management is governed in Yemen. The table also includes the oversight role of parliament and depicts the integral role that the Donors play in PFM in Yemen.

2.3.2.16 *Absent Features from the Institutional Arrangements:* The institutional arrangements do not include a public procurement oversight authority, a public procurement complaints board, procurement investigations unit, audit committees or an Internal Auditor General, or an Accountant General. Payments are carried out by the Accounting Officers of the Line Ministries and Departments. Line Ministries are responsible for preparing annual accounts which are consolidated by the Final Accounts Department within the Ministry of Finance. There are no Audit Committees set up within Line Ministries to address the follow up of audit findings. Audit follow ups are addressed through the Follow Up Department within the Ministry of Finance and through meetings held by the relevant officials.

<u>Table 2.5</u> Matrix of Institutional Responsibilities for PFM Functions

		Ministry of Finance												MoP	MoO	Line Ministry								
PFM Function	**Cabinet**	**FM**	**Budget Dep.**	**BE**	**PD**	**DM**	**PSIP**	**GAD**	**NTC**	**PFM Ref.**	**Customs**	**TRA**	**IA**			**LM**	**TC**	**ICI**	**Act**	**CSM**	**COCA**	**CBoY**	**Parliament**	**Donors**
Policy Elaboration and Planning																								
Policy/Budget Approvals	✓	✓												✓		✓				✓				
Loan Approvals	Endorse	✓												✓									✓	
Supplemental Budgets	✓	✓														✓							✓	
National Development Plan (DPPR)	✓	✓														✓								Consult
Sector Development Plans	✓															✓								Consult
Budget Formulation/Preparation																								
MTEF(under development)			✓		✓									✓		✓				✓		✓		Consult
Budget Speech		✓																						
Macro-Fiscal Framework	✓	✓			✓									✓										
Annual Budget Estimates	✓	✓	✓				✓							✓	✓	✓				✓		✓		Consult
Revenue Administration/Collections																								
Tax Revenue											✓	✓												
Royalties															✓									
Grants/Loans	✓	✓				✓																		✓
Budget Execution																								
Debt Management						✓																✓		
Budget Allocation/Cash Management			✓																			✓		
Virement - Chapter Level		✓	✓	✓																		✓		
Establishment Control			Consult													✓				✓				
Personnel Rolls																✓				✓				
Payroll																✓				✓				
Procurement/Supply Chain									✓							✓	✓							
Non-Salary Recurrent Expenditure																✓								
Capital Expenditure			✓		✓											✓								✓
Payments																✓			✓			✓		
Financial Reporting							✓									✓			✓			✓		✓
Accounting								✓											✓					
Internal Audit/Control											✓	✓	✓					✓						
External Scrutiny/ Budget Oversight																								
External Audit		✓																			✓			
Budget Oversight																							✓	
Expenditure/Audit Oversight																							✓	
PFM Reform																								
Reform Policy/Approval	✓																							Consult
Reform Coordination/Monitoring										✓														✓

FM: Finance Minister; **BE**: Budget Execution Department, **PD**: Planning Directorate (MoF); **DM**: Debt Management Department, **PSIP**: Public Sector Investment Program; **GAD**: General Accounts Directorate **NTC**: National Tender Committee; **TRA**: Tax Revenue Authority; **PFM**: PFM Reform Unit; IA: Internal Audit; **ICI**: Internal Control and Inspection; **LM**: Line Minister; **AO**: Accounting Officer; **TC**: Tender Committee; **MoP**: Ministry of Planning; **MoO**: Ministry of Oil and Minerals, **CSM**: Civil Service Ministry; **COCA**; Central Organization of Control and Audit; **CBoY**: Central Bank of Yemen.

2.3.3 The Key Features of the PFM system

2.3.3.1 The financial year for central government and local authorities in Yemen is from January 1 to December 31. The budget process begins in May. Usually the draft budget is submitted in early October with the Budget Speech to parliament late October. The annual appropriations law is typically passed by parliament between the second and third week of December and enacted into law by the signature of the president the last week in December. Authority to incur expenditure is facilitated through a General Warrant issued on the strength of the enactment into law of the Appropriation Bill.

2.3.3.2 While Yemen has adopted a national development plan - the Socio-Economic Development Plan for Poverty Reduction (DPPR), and has developed sector strategies for some of the major sectors it does not yet have in place many of the pre-requisites for the successful implementation of a Medium Term Expenditure Framework.

2.3.3.3 Yemen has a distributed payments and accounting system operated out of a single consolidated fund account set up in the CBY. Over the past few years the Yemen Government has been gradually rolling out a standardised (across the whole of government) financial management information system (AFMIS). The Government has implemented an integrated financial management information system (AFMIS) across four ministries at the headquarters level. It is based upon proprietary software developed in Yemen. The payroll systems are managed and operated independently by each of the Line Ministries but using standard software across all ministries.

2.3.3.4 The Government of Yemen adopts a strict cash accounting basis for the preparation of its accounts. The final accounts are prepared by the Line Ministries and consolidated by the Ministry of Finance.

2.3.3.5 COCA has jurisdiction over all government entities including public and statutory bodies. The Financial Law and Audit Law authorise COCA the requisite independence and jurisdiction to receive all documentation necessary to carry out his work and places no restrictions on the publication of his findings. The Head of the Public Entity is responsible and held accountable for implementing any recommendations emanating out of an audit.

2.3.3.6 At this time the PFM systems in Yemen does not include a public procurement oversight body responsible for policy and regulatory oversight; neither does it have a procurement complaints or appeals body even though these are included in the newly passed Tender Law (July 2007) which is yet to be operationalized by the issuance of the associated regulations.

3. ASSESSMENT OF PFM SYSTEMS, PROCESSES AND INSTITUTIONS

3.1 PFM OUTTURNS: CREDIBILITY OF THE BUDGET

3.1.1 Aggregate expenditure out-turn compared to original approved budget

3.1.1.1 The PEFA assessment covers the fiscal years 2004, 2005 and 2006; 2006 being the most recent completed budget year at the time of the assessment. The reporting formats of the budget documentation permit an identification of debt service elements and donor contributions and so make it possible to identify and measure primary expenditure[17] estimates as well as primary recurrent expenditure achievements. The budget documentation also permits a segregation of primary capital expenditure achievements. The recurrent expenditure estimates and actuals presented in Table 3.1 were derived from the published appropriations accounts and the *proposed* budgets submitted to Parliament. At the present time the Ministry of Finance does not separately publish parliamentary *approved* budget estimates. The outcomes of the parliamentary debate on the budget proposals are a separate budget document that includes all of the parliamentary recommendations and a signed undertaking that the Minister of Finance shall carry out such recommendations. However, the Ministry of Finance does not specifically adjust the budget proposal figures accordingly. By constitution, the parliament is not authorised to directly amend the budget figures. No changes are made to the aggregate budget figure, but recommendations can give rise to reallocations between budget heads. The Ministry of Finance states that it incorporates the consequences of the parliament's recommendation in the budget releases and demonstrates to the parliament through the supplemental budget process that such recommendations have been carried out. The parliament suggests that such a process remains opaque. The upshot of this is that there is no clear and direct evidence how the parliamentary recommendations are reflected in the budget process

3.1.1.2 The Government of Yemen has adopted a strict cash accounting basis for its Public Accounts with the fiscal year defined as January 1 to December 31st. Outstanding commitments for goods, works and services (open purchase orders) not delivered by the 31st of the last month of the fiscal year (except for emergencies) are cancelled. Un-cleared cheques are not honoured and must be reissued in the next fiscal year[18]. This therefore results in any unspent funds at the close of the fiscal year being lost by the Line Ministry. One consequence of the implementation of the cash accounting system is that it does not strictly match expenditure periods to budget estimate periods as would be the case for modified cash accounting[19] with a consequence of slightly biasing downwards the measure of actual expenditure to original budget estimate.

3.1.1.3 The estimates and actuals presented in Table 3.1 exclude interest payments and capital projects funded by grants and loans. For all three fiscal years reviewed, the aggregate actual expenditures far exceed the original budget estimates reaching a mismatch of 40% in 2005. In all three years revenues greatly exceeded budget estimates (see indicator PI-3). In response to approximately 75% of its revenues being based on oil exports, coupled with oil price volatility, Yemen adopts a conservative posture on revenue forecasts which in turn translate into conservative original budget estimates. Without clearly articulated fiscal policies to address any revenue excesses over budget estimates the consequence of surplus revenue is the significantly increased actual expenditure over budget estimate. In practice the excess of revenue over budget estimates goes principally to domestic petroleum subsidies, to additional recurrent expenditure and to some additional capital expenditure. When the poor cash management, weak commitment controls along with ex-post supplemental budget procedures (see PI-27) and rather non-transparent budget revision

[17] Primary Expenditure excludes debt service payments and donor and loan funded project expenditure.

[18] Officials of the CBY indicate that under very special circumstances, and only under instruction from the Ministry of Finance, they shall permit cheques to be cleared for expenditures incurred in the previous fiscal year.

[19] This mismatch of expenditure period with budget estimates period could in principle lead to some bias introduced in the application of the rating method for indicators P1 and P2.

procedures that occur above the level of the Line Ministries are considered, it leads to a conclusion that a significant portion of expenditure is not subjected to full budgetary preparation control and approval rigour. Estimates of the proportion of recurrent expenditure increases due to domestic petroleum consumption subsidies show that approximately 70%, 62% and 44% of recurrent expenditure increases over original budget estimates for the years 2004, 2005 and 2006 respectively were applied to domestic petroleum subsidies. Therefore the increases in non-petroleum subsidy recurrent expenditure were 7%, 8% and 18% for the years 2004, 2005 and 2006 respectively. It should be noted that if the increases in total aggregate expenditure over original budget estimate is calculated excluding increases in expenditure due to domestic petroleum subsidies the results show excesses of 5% 32% and 17% respectively[20].

3.1.1.4 The comparison of primary expenditure estimates to actual primary expenditure is premised upon the availability of accurate financial data. There is reason to believe the accuracy and reliability of the audited expenditure data used for this analysis is not completely reliable. The budget documentation shows widely varying data for actual expenditure data as reported under the summary tables versus the detail entries questions the accuracy of expenditure data reported. In discussions with COCA officials they indicated that they were aware of the difficulties with the reported expenditure data. This also points to weakness in the reconciliation procedures used to prepare the budget documentation.

3.1.1.5 While the PI-1 indicator focuses upon a primary budget estimate and expenditure analysis, it is significant to note that there are also mismatches between budget estimate and out-turn for that portion of which is financed by international loans and grants which is not captured in Table 3.1 (see indicators PI-7 and D-2).

Table 3.1

Comparison of Original Budget Estimates against Actuals (Primary Expenditure)

	2004		2005		2006	
	Estimates	Actual	Estimates	Actual	Estimates	Actual
Original Primary Expenditure						
Recurrent Expenditure	501,020,034	624,562,539	582,832,285	862,011,815	870,960,454	1,073,853,274
Interest Payments	38,187,697	53,976,110	52,226,664	69,071,550	84,791,740	88,896,434
Primary Recurrent Expenditure	462,832,337	570,586,429	530,605,621	792,940,265	786,168,714	984,956,840
Capital Expenditure (Govt. Funded)	189,427,748	210,558,131	196,045,548	254,366,924	236,141,953	242,468,510
Total Original Primary Expenditure	**652,260,085**	**781,144,560**	**726,651,169**	**1,047,307,189**	**1,022,310,667**	**1,227,425,351**
Primary Expediture Deviation	**19.8%**		**44.1%**		**20.1%**	

Amounts are in 1000's of Yemeni Riyals. The data has was extracted from the Budget Books for 2004, 2005 and 2006 and for the appropriation accounts for 2004, 2005 and 2006.

3.1.2 Composition of expenditure out-turn compared to original approved budget

3.1.2.1 Given the high levels of actual expenditure over original budget estimate, the composition of expenditure out-turn to original approved budget becomes a very important measure. Large deviations would suggest significant distortions to the original policy objectives captured in the original budget estimates. To obtain a measure of how much the reallocations between budget lines have contributed to variance up and above the deviations in the overall levels of expenditure, an analysis of budget deviations between budget estimates and actual out-turns by budget head was performed for the years 2004, 2005 and 2006.

3.1.2.2 Table 3.2 shows the results of the analysis applied to the data presented in Table 3.3. The analysis of the total expenditure deviation less the total expenditure variance shows

[20] Even if the impact of the domestic petroleum subsidies on excess expenditure over original budget estimate are excluded from the analysis the indicator scoring for PI-1 with two years exceeding 15% would still result in a D.

deviations in excess expenditure deviation over total expenditure variance between 13.6% and 6.9%.

Table 3.2
Analysis of Budgeted to Actual Expenditure Variance of Budget Head to Total Budget Deviation

Year	2004	2005	2006
Total Expenditure Deviation	33.36%	51.0%	27.4%
Total Expenditure Variance	19.76%	44.1%	20.1%
Deviation in Excess over Total Variance	**13.60%**	**6.90%**	**7.36%**

Data derived from Table 3.3

3.1.2.3 The budget to expenditure deviations for each Budget Head is presented in Table 3.3. These deviations are substantial and are consistent with the lack of appropriate ex-ante consideration and budgetary process in the supplemental budget procedures observed (see PI-27); the incidence of adjustments to the six-month appropriation releases issued to the Line Ministries made by the Ministry of Finance; and to a lesser degree the lack of proper budgetary and expenditure reflection of internally generated funds (see PI-8).

3.1.2.4 The variations shown in Table 3.3 is evidence of a less than strong coupling between the original budget and the budget execution process brought about through repeated variations made to the budget releases allocations as well as weak commitment control processes. It raises questions about Yemen's PFM systems being able to deliver fully on the strategic intent of its budget and ensuring that budget implementation is ultimately in line with the policy objectives set out in its national development framework, the DPPR.

3.1.2.5 Inspection of the data presented in Table 3.3[21] shows that in spite of substantial increases in expenditure over original budget estimates, some ministries received less than their original budget estimates. Some examples include the Ministries of Education and Higher Education. Further it is noted that the smaller ministries (consolidated into a single line titled aggregate) show less expenditure than originally budgeted in the years 2004 and 2005 in spite of the substantial aggregate excess expenditure over original budget; which may suggest that the actual allocation of resources reflects the strength and influence of the specific ministries rather than a reflection of the policy objectives embedded into the original budget allocations.

[21] Note the minor discrepancies in the totals of Table 3.2 and Table 3.1. While the data was obtained from the same Budget and Appropriation Accounts they were obtained from different sections and point to inconsistencies in these reports. The issue was raised in interviews with COCA who indicated that they are aware of discrepancies in the reports. No reasons for the discrepancies could be provided by Government officials but a possible reason for discrepancies in actual expenditures may be that the detailed budget head figures include extrabudgetary expenditures. The discrepancy amounts are of the extrabudgetray expenditures estimated.

Table 3.3
Comparison of Original Budget Estimates and Actual Expenditure by Head

	Budget Head	2004 Budget		Budget Head	2005 Budget		Budget Head	2006 Budget	
		Estimate	Actual		Estimate	Actual		Estimate	Actual
1	Ministry of Finance	146,631,976	234,840,715	Ministry of Finance	156,114,702	400,682,491	Ministry of Finance	359,204,192	479,155,080
2	Ministry of Education	127,260,558	119,704,368	Ministry of Education	137,555,723	138,928,660	Ministry of Defence	161,830,500	211,219,237
3	Ministry of Defence	117,030,346	135,899,259	Ministry of Defence	127,253,667	156,149,893	Ministry of Education	140,015,559	154,083,721
4	Ministry of Internal Affairs	37,389,838	50,414,900	Ministry of Pub.Works &Roads	51,719,101	96,503,952	Ministry of Pub.Works &Roads	63,878,151	96,592,047
5	Ministry of Pub.Works &Roads	37,187,542	69,932,128	Ministry of Internal Affairs	47,499,499	56,655,548	Ministry of Internal Affairs	63,419,131	76,987,709
6	Ministry of Health & Populat.	32,811,836	41,944,866	Ministry of Health & Populat.	40,330,815	42,361,009	Ministry of Health & Populat.	44,346,064	43,057,382
7	Ministry of Higher Ed.&Resear	30,408,331	25,417,840	Ministry of Higher Ed.&Resear	30,217,531	28,357,546	Ministry of Higher Ed.&Resear	34,068,953	32,164,096
8	Presidential House	14,711,333	21,148,300	Presidential House	15,277,368	22,702,631	Presidential House	18,074,124	24,999,308
9	Ministry of Agriculture	12,638,849	8,372,296	Ministry of Agriculture	13,298,592	11,433,968	Ministry of Water & Environment	16,779,997	1,332,373
10	Ministry of Foreign Affairs	10,282,691	10,407,288	Ministry of Water & Environment	12,020,269	8,992,510	Ministry of Local Administr.	14,331,845	12,308,442
11	Ministry of Water & Environment	9,529,793	2,044,767	Ministry of Foreign Affairs	10,890,271	10,606,214	Ministry of Vocational Training	11,575,985	7,644,783
12	Judiciary Authority	9,247,504	18,127,545	Judiciary Authority	10,789,748	20,481,705	Judiciary Authority	10,963,730	12,013,020
13	Ministry of Planning & Int.Cop	8,368,417	3,403,384	Ministry of Local Administr.	9,309,471	9,323,521	Ministry of Foreign Affairs	9,997,634	10,274,956
14	Ministry of Local Administr.	7,069,733	7,333,636	Ministry of Vocational Training	8,759,194	5,075,368	Ministry of Planning & Int.Cop	9,269,763	2,439,044
15	Ministry of Information	6,906,999	6,735,158	Ministry of Civil Service	8,396,402	4,907,145	Ministry of Information	9,000,964	9,065,891
16	Ministry of Vocational Training	6,668,703	3,627,992	Ministry of Planning & Int.Cop	7,921,069	4,783,078	Ministry of Agriculture	7,856,765	9,539,118
17	Central Org. for Polit. Security	5,250,600	6,033,978	Ministry of Information	7,573,889	7,482,658	Central Org. for Polit. Security	7,846,760	8,510,448
18	Ministerial Cabinet	4,370,395	4,156,864	Central Org. for Polit. Security	5,663,779	7,068,731	Ministry of Civil Service	6,189,063	4,710,125
19	Ministry of Youth &Sports	4,351,615	2,873,706	Ministerial Cabinet	4,902,931	6,105,434	Ministerial Cabinet	5,179,207	8,051,739
20	Ministry of Civil Service	3,999,125	4,366,189	Ministry of Youth &Sports	4,128,837	2,291,298	Ministry of Youth &Sports	4,384,947	4,966,660
21	Aggregate	15,653,326	12,536,936	Aggregate	16,436,571	15,795,675	Aggregate	16,753,889	18,344,579
	Total	**647,769,510**	**789,322,117**	**Total**	**726,059,429**	**1,056,689,035**	**Total**	**1,014,967,223**	**1,227,459,759**

Amounts are in 1000's of Yemeni Riyals. The data has was extracted from the Budget Books for 2004, 2005 and 2006 and for the appropriation accounts for 2004, 2005 and 2006. We note that the totals, derived from the detailed budget Head entries do not precisely match the totals shown in Table 3.1 which were derived from summary figures reported in the Budget Books and Appropriations Accounts. Such discrepancy points to some inaccuracy in the budget book data.

3.1.3 Aggregate revenue out-turn compared to original approved budget

3.1.3.1 The principal sources of domestic revenue are from oil production share arrangements and royalties on oil production, taxes on international trade and transactions, and income tax. There is no value added tax imposed in Yemen. The oil revenues represent approximately 75% of domestic government revenue, which due to the high volatility in oil prices on the world market in turn leads to highly unpredictable revenues. Yemen, as part of its fiscal policy posture, adopts a conservative position with respect to revenue budgets.

3.1.3.2 The revenue estimates and actual receipts are classified as Taxation Revenue, Non-Tax Revenue and Capital Revenue (sales of assets and of stocks). A comparison of budgeted versus actual domestic revenues demonstrates actual revenues exceeding revenue estimates in 2004, 2005 and 2006 by between 30% and 61% (see Table 3.4). While such robust revenue results can contribute to the credibility of the budget they may however limit strategic allocation considerations if such are based upon estimates that substantially underestimated the availability of resources. A countervailing factor is that oil price volatility in the past few years has been high and thus excludes the possibility of very accurate revenue forecasts. A conservative revenue budget shields the budget from volatility. Yemen's revenue budget is based upon an oil price higher than some other oil producing countries including Iraq and Nigeria.

3.1.3.3 In addressing volatility in revenues through a conservative posture on revenue budgeting, it is important to also address the consequences on budget execution that arises as a consequence of likely excess revenues. Where revenue excesses over revenue budget estimates are very large as is the case in Yemen it can undermine aggregate fiscal discipline. This is the case where the excess funds are channelled into recurrent expenditure without clear policy constraints and with only weak supplemental budgetary procedures to serve as oversight. As discussed above in 3.1.1.3, for the most part excess revenues have been applied to recurrent expenditures which subsequent negative impacts on indicator scoring PI-1.

3.1.3.4 In the three fiscal years reviewed there were no natural disasters experienced nor were there any other external shocks experienced that may have adversely affected revenues. The volatility of oil prices in world markets, coupled with its dominance in revenue contributions shall keep Yemen vulnerable to market down turns.

Table 3.4
Comparison of Budgeted and Actual Revenue Receipts (Domestic)

	2004			2005			2006		
	Estimate	Actual	% A/E	Estimate	Actual	% A/E	Estimate	Actual (provisional)	% A/E
Revenue (in 1000's of Yemeni Rials)									
Recurrent Revenue									
Tax Revenues	168,354,022	186,538,372	110.8%	190,966,431	234,894,407	123.0%	256,431,676	266,050,369	103.8%
Oil Royalties	449,757,147	615,040,891	136.7%	495,606,200	869,554,041	175.5%	708,770,990	1,177,482,731	166.1%
Total Recurrent Revenues	**618,111,169**	**801,579,263**	**129.7%**	**686,572,631**	**1,104,448,448**	**160.9%**	**965,202,666**	**1,443,533,100**	**149.6%**
Capital Revenues									
Sale of Assets	143,440	143,440		2,522,358	3,103,082		-	3,456,887	
Sale of Stocks	-	119,349		-	399,444		649,275	1,555,831	
Total Capital Revenues	**143,440**	**262,789**	**183.2%**	**2,522,358**	**3,502,526**	**138.9%**	**649,275**	**5,012,719**	**772.0%**
Total Revenue	**618,373,958**	**801,842,052**	**129.7%**	**689,094,989**	**1,107,950,974**	**160.8%**	**965,851,941**	**1,448,545,819**	**150.0%**

Amounts are in 1000's of Yemeni Riyals. The data has was extracted from the Budget Books for 2004, 2005 and 2006 and for the appropriation accounts for 2004, 2005 and 2006.

3.1.4 Arrears

3.1.4.1 Arrears are defined as payments that remain unpaid thirty days after the date of invoice verification. Payments for expenditure arrears are sourced from the next year's budget. While the Monthly Budget Execution Returns format, submitted by Line Ministries to the Ministry of Finance, accommodates entries for accrued arrears many Line Ministries do not report on them and neither does the Ministry of Finance consolidate these elements to obtain a national arrears figure. Indeed it would appear that much of the impetus for wishing to adopt accrual accounting as part of the PFM reform effort has been to better report on and monitor the level of arrears. During the deliberations of the national stakeholder's workshop Director Budget informed that the Finance Ministry does have information on Payment Arrears and that each line ministry while submitting their budget proposals to the Finance Ministry, also submit their statements on ***'Old Commitments',*** which include **'Payment Arrears'.** However, the PEFA Task Force discovered that preparation of these statements was a one-time annual exercise used for issuing sanctions with supporting documents. But there was no regular monitoring of payment arrears by Finance or any other ministry. It was not possible to get a statement of ministry wise payment arrears at a given point of time. Thus, although respective spending units might be having information of payment arrears with them, it is not compiled and regularly monitored at the country level by Ministry of Finance at the moment. There is, therefore, a need to create a system of taking stock and monitoring of payment arrears.

3.1.4.2 In discussions with the officials of COCA arrears were characterized to be at significant levels. In their view the high prices paid by government entities, as demonstrated in value-for-money audits carried out, is in part due to high levels of arrears. The practice of using middle men in contracts, where the party responsible for actual contract implementation is different from the party awarded the contract is the other reason for not achieving value-for-money. There are weaknesses in the commitment control systems implemented which would also point to the accrual of substantial arrears – but without reported data, this cannot be substantiated. Without reliable data compiled for accrued arrears it is not possible to precisely state the seriousness of the problem, nor report on whether it is decreasing or increasing over time. In general there are a number of possible causative factors for the high levels of arrears accrued such as the weak links between the budget formulation processes and budget execution; the absence of a budget preparation process characterised by the reconciliation of top-down resource discipline and bottom-up inputs and the lack of effective commitment control systems.

Indicator /Dimension	Score	Brief Explanation
PI-1 Aggregate expenditure out-turn compared to original approved budget	**D**	Deviations between approved budget primary expenditure and provisional actual expenditure were: for 2004 =19.8%, 2005 = 44.1% and 2006 = 20.1%.
PI-2 Composition of expenditure out-turn compared to original approved budget.	**C**	The average variances in excess of overall deviations were: 2004 = 13.6%, 2005 = 6.9% and 2006 = 7.4%
PI-3 Aggregate revenue out-turn compared to original approved budget	**A**	Domestic revenue collection exceeded 97% in all three of the last three budget years.
PI-4 Stock and monitoring of expenditure Payment arrears	**<NS>**	
(i) Stock of expenditure payment arrears (as a percentage of actual total expenditure for the corresponding fiscal year) and a recent change in the stock	<NS>	There is no monitoring of arrears being undertaken so the arrears cannot be quantified. There are however indications, including through COCA's audit activities, that suggest that the arrears may be substantial.
(ii) Availability of data for monitoring the stock payment arrears	D	There is no reliable data maintained on the level of arrears available from the past two years.

3.2 COMPREHENSIVENESS AND TRANSPARENCY

3.2.1 Classification of the Budget

3.2.1.1 Currently the fiscal framework is presented on a cash accounting basis employing only economic and administrative classifications. Starting with the 2009 budget year the central government intends to adopt a budget based on economic, administrative and functional classification for formulation, execution and reporting. The Government Financial Statistics, a quarterly report (in English and Arabic) put out by the Department of Planning, Statistics and Follow-Up, Ministry of Finance includes summary percentage distribution data using the 10 main COFOG functional classifications. However, functional classifications have not yet been integrated directly into the budget process. The chart of accounts for the Central Government budget monitoring is consistent with GFS standards even though the 2001 GFS standard is yet to be fully adopted. Budget execution is not yet based upon a COFOG/GFS standard, but it is intended that this will become so as the AFMIS system is rolled out to all budget entities.

Indicator	Score	Brief Explanation
B. Comprehensiveness and Transparency		
PI-5 Classification of the Budget	**C▲**	The budget formulation and execution is based on economic and administrative classification. There have been recent efforts made towards adopting functional classifications within the budget process however budget formulation and execution is not yet based on a functional classification. There is the intention to implement it in the 2009 Budget. At this time there is evidence supported by informal internal documents and the Government Financial Statistics Bulletin that show functional distribution ratio tables.

3.2.2 Comprehensiveness of the Budget Documentation

3.2.2.1 Only proposed budgets are prepared and published. A specific approved budget is not published. However any recommendations made by Parliament are reported in a separate attachment to the budget volumes. The Ministry of Finance does not publish any quantitative impact analysis of the parliament's recommendations or make any adjustments to the proposed budget to reflect parliament's recommendations. Ministry of Finance officials explain that the parliamentary recommendations are taken into consideration during budget execution in the setting of budget releases. However, Line Ministry officials state that they are unaware of any modifications that specifically reflect parliamentary adjustments in the appropriations they receive. This suggests that at the very least if such parliamentary adjustments are carried out, they are not transparent to the entities responsible for carrying out budget execution.

3.2.2.2 The budget submissions to parliament include 38 separate volumes and attachments and are also submitted electronically on a CD. The budget format includes estimates, the proposed estimates for the previous years and actual expenditure data for two previous years. The appropriations accounts for the previous year are submitted at approximately the same time as the Budget documents are submitted allowing parliamentarians to review both during the budget review process. The format of the appropriations accounts includes actual expenditure data of the Budget Year-2 and the revised budget data of the Budget Year-2. Budget documentation is comprehensive, and consists of the following main components and elements:

- The Budget Speech by the Minister of Finance that contains Government policy and the estimated impacts of new policy on the budget;
- The Estimates of Expenditure as proposed but without approved estimates for the previous budget year;
- Actual Expenditures for budget year-2, and budget year-3;
- Summary revenue estimates for the budget year and the current year (budget year-1);
- Debt Service Estimates (in attachment)
- The Debt Stock listing individual creditors (in attachment);
- Statement of Financial Assets and Liabilities (two years prior to the budget year);
- Selected economic data upon which the budget estimates are based.

3.2.2.3 The budget speech underscores the policy priorities for the respective budget year and contains the information pertaining to the overall macroeconomic and fiscal framework in their various sections. It also includes an analysis of budget impacts of new government policies. The Estimates of Expenditure provides a breakdown by economic and administrative classification. The table below summarises the availability of budget information. The Budget documents are comprehensive but these documents are undermined by not including approved budget data even in subsequent budget submittals. It raises the question how well budget implementation reflects parliamentary approvals and modifications.

Table 3.5
Summary of Budget Documentation

Elements of budget documentation	Availability	Notes
1. Macro-economic assumptions, incl. at least estimates of aggregate growth, inflation and exchange rate	Yes	Macroeconomic assumptions are included in the Budget Speech. In 2005 and 2006 these included GDP growth rate, population growth rates, the inflation rate and the exchange rate. The government however has made the conscious decision to exclude the exchange rate in future budgets because it adversely affects the foreign exchange markets.
2. Fiscal deficit, defined according to GFS or other internationally recognised standard	Yes	Fiscal deficit is defined and presented in the "Budget Speech"
3. Deficit financing, describing anticipated composition	Yes	A table is included that provides information on how the deficit is to be financed.
4. Debt stock, incl. details at least for the beginning of the current year	Yes	There is a reasonably detailed statement of outstanding public debt included as an attachment to the Budget Speech.
5. Financial assets, incl. details at least for the beginning of the current year	Yes	Information on financial assets is included in attachments submitted along with the budget documents; however it is not clear if or how comprehensive the listed financial assets are.
6. Prior year's budget out-turn, presented in the same format as the budget proposal	Yes	Budget year -2, out-turn is included in the same format as the budget (where prior year is defined as BY-2)
7. Current year's budget (revised budget or estimated out-turn), presented in the same format as the budget proposal	No	The revised budget for budget year-2 is included in the appropriations accounts which are also submitted as part of the budget documentation submitted to parliament; however there are no revised budgets or estimated out-turns for the current year.
8. Summarised budget data for both revenue and expenditure according to the main heads of the classification used, incl. data for current and previous year	Yes	The budget does include summarised data according to the main heads of classification for both revenue and expenditure.
9. Explanation of budget implications of new policy initiatives, with estimates of the budgetary impact of all major revenue policy changes and/or some major changes to expenditure programs	Yes	The Budget Speech includes an analysis of budget impacts of new government policies

Indicator	Score	Brief Explanation
B. Comprehensiveness and Transparency		
PI-6 Comprehensiveness of information included in budget documentation	**A**	Budget documentation fulfils 8 out of 9 benchmarks. The Budget documents are comprehensive but these documents would be made more transparent by including approved budget data even in subsequent budget submittals. Government officials state that parliamentary modifications are taken into consideration at the time of execution. It still raises the question how well budget implementation reflects parliamentary approvals and modifications.

3.2.3 Extent of Unreported Government Operations

3.2.3.1 One element of government operations which affects the efficient allocation of resources is the existence of unreported government operations. In general, given their nature, it is difficult to quantify accurately the extent of unreported government operations. In Yemen there is complete and regular reporting on Special Funds such as the Roads Fund, the Medical Supplies and Drugs Fund and the Social Care Fund both to the Ministry of Finance in its oversight capacity as well as to the Parliament. The Government operates a single treasury consolidated fund in the CBY where all revenues are deposited except for internally generated funds. These are deposited in Special Accounts that are controlled directly by the Line Ministries. There are twelve Line Ministries that receive internally generated funds, five of which transfer all their funds to the consolidated fund and seven of which transfer differing proportions of their collections. Only recently have there been efforts to consider internal generated funds separately within the budget and also report on their expenditure separately. The 2007 Budget identifies Special Account Revenues to be 8,931,709,000 Yemen Riyals out of a total budget of 1.4 trillion Yemen Riyals, corresponding to 0.6% of total expenditure. This represents a reasonable proxy for unreported and not fully reported Government Operations for the period considered FYs 2004, 2005 and 2006 and suggests that the amount of extra-budgetary expenditure is insignificant. In the COCA Audit Report for 2005 it states that a number of units resort to putting aside part of their revenues in special accounts to fund part of their expenditures outside the budget framework in violation of the provisions of Financial Law No. 8, 1990. The ascertained total amount of these is estimated at YR 6.3 billion. This is consistent with the estimates used in the 2007 Budget and corroborates the conclusion that extra-budgetary expenditure is less than 1%.

3.2.3.2 Budget documentation includes details of projects showing both Donor contributions as well as Government counterpart fund contributions. A number of Donors do not provide complete financial expenditure data to the Government especially with respect to those expenditures they execute directly on behalf of the project as well as due to either the non submission or the late submission of financial statements for consolidation into the government's consolidated appropriations accounts. The consequence of poor donor financed investment budget estimates coupled with incomplete and delayed financial reporting leads to inaccuracies in the reported implementation of investment projects. Many of the major donors provide basic income and expenditure reports to the Ministry of Planning and the Line Ministry under which the project is carried out. For most projects the funding is deposited in the CBY. This provides the Government with an opportunity to track project implementation by monitoring actual disbursements. This, while a reasonable proxy, is not a substitute for actual expenditure reporting. The Appropriations Accounts include grant expenditure reports for a number of the major grant aid Donors including USAID, Japan, UNDP, DFID the EU and Netherlands which would suggest that greater than 50% is reported upon. However, there have been difficulties on reporting on some grants from USAID, Germany and Netherlands. Further, it is apparent (see D-2) that even where there is financial reporting, this is not always complete. It is difficult to determine precisely how much remains unreported, but discussions with officials and Donors suggest the amount to be significant. For example in one year USAID alone reported 15 Million USD being omitted where the overall grant aid disbursed for the six largest grant donors contributed about 120 Million USD.

Indicator	Score	Brief Explanation
PI-7 Extent of Unreported government Operations	**B+**	
(i) level of unreported extra-budgetary expenditure	A	All revenues generated directly by the MDAs are transferred to the Consolidated Fund except for internally generated funds which are deposited in Special Accounts. An assessment of internally generated funds in 2007 suggests that the amounts are insignificant (less than 1%). There is very close oversight of all of the Special Funds which must report regularly to the Ministry of Finance as well as to Parliament

(ii) Income/Expenditure information on donor-funded projects	B	Income/expenditure data of donor funded projects (loan funded) are submitted to the Ministry of Planning as well as the Line Ministry to be included in fiscal reports but there appear to remain issues with timeliness and completeness. Over 50% of the grant funded projects are reported on.

3.2.4 Transparency of Inter-governmental Fiscal Relations

3.2.4.1 Since the enactment of the Local Authority Law 4, 2001 there has been a substantial transfer of responsibility from the Line Ministries to the Local Authorities at the district level. The Line Ministries maintain offices in the districts to provide supervision and technical assistance to the Local Authorities for the operations of facilities within their jurisdiction. However, the budget estimates and expenditure formats maintain all health and education expenditure within the respective Line Ministry budget heads[22]. Officials report that due to lack of capacity of the majority of the Local Authorities such transfer of responsibility has not been implemented. Under the new arrangement, in addition to town planning, community amenities, maintenance of minor roads and water supply systems the local authorities are responsible for basic and secondary education as well as health. There are 303 local authorities spread over 22 Governorates.

3.2.4.2 There are four main sources of funds available to Local Authorities. These are:

- Own Revenues which include business licence fees, levies and local taxes;
- Joint Revenues which include vehicle registration fees, building permit fees and property taxes) which are shared 50% to other districts, 25% to the Governorate and 25% kept within the Local Authority
- Central Government Budget transfers which cover recurrent expenditures which are managed in the same way as Line Ministry recurrent budgets; and
- Public Revenues (also transferred from the Central Government Budget), which include 30% of the Fisheries Fund, the Agricultural Fund and the Sports Fund

3.2.4.3 The Local Authorities share the same financial year as the central government and participate directly in the budget process with respect to their recurrent budgets which are funded fully by the Central Government. Both the budget document and the appropriations accounts directly integrate all the fiscal data for the local authorities. Therefore, central government recurrent expenditure contributions are known at the start of the budget process typically in May. The horizontal allocation of the public revenues is based upon six criteria that are outlined in the Local Authorities Law No. 4, 2001. These are: the population density; level of own resources; level of social and economic growth rates as well as level of deprivation; level of competence of the Local Authority; ability to collect financial recourses and the soundness of their expenditure; and any other fundamentals and criteria determined by the Cabinet.

3.2.4.4 At the present time the horizontal allocation of public revenues is the responsibility of a Committee made up of representatives of the Ministries of Finance, Local Authorities and Planning[23]. However, without fully developed quantifiable and measurable indicators not all six criteria laid out in the law are applied. However, even with only a partial implementation of the law the allocations remain rule based. Thus with both categories of transfers being rule based over 90% of the horizontal allocations from Central Government is determined by transparent

[22]The transfer of basic education and health responsibilities along with corresponding budget transfers constitute part of central government transfers. No data was available that quantified these transfers and so were not included in the analysis. A committee (Finance, Planning and Local Authorities) is responsible for allocating these amounts to the Governorates, which in turn allocate to the local authorities.

[23] At the present time the Committee consider in arriving at the horizontal allocation of resources using population, level of deprivation and level of own revenues.

rules and permit a clear basis for the Local Authorities to forecast their revenues and plan their budgets.

Table 3.6
Segregation of Central Government Transfers into Recurrent Expenditures and Public Revenues for FYs 2004, 2005, and 2006

Year	2004		2005		2006	
	Amount	%	Amount	%	Amount	%
Central Government Transfers	125,611,000,000	97%	152,985,000,000	99%	178,273,000,000	99%
Public Revenues	3,226,000,000	3%	2,127,000,000	1%	2,392,000,000	1%
Total	**128,837,000,000**	100%	**155,112,000,000**	100%	**180,665,000,000**	100%

Amounts are Yemeni Riyals. Data obtained from the Budget Directorate, Ministry of Finance

3.2.4.5 As part of the main budgetary process, the Local Authorities along with the Line Ministries receive their budgetary allocation ceilings in May. They then prepare their recurrent budgets and submit them to the Ministry of Finance in August. They also participate in the Budget Negotiation procedures. The Local Authorities submit financial reports to the Ministry of Local Authorities on a quarterly basis typically within 30 days of the end of the quarter. Final accounts are submitted to the Ministry of Finance to be consolidated into a set of national appropriations accounts. The consolidated local authority financial statements are prepared in a structure consistent with the Central Governments financial reports and included with the final appropriations accounts submitted typically 9 to 10 months after the close of the Fiscal Year (see PI-25).

Indicator	Score	Brief Explanation
PI-8 Transparency of Inter-governmental fiscal relations	**A**	
(i) Transparent and objectivity in the horizontal allocation among SN government	A	The central government transfers for recurrent expenditure of the Local Authorities are based upon the same budget procedures as for the Line Ministries and so are transparent and subject to set procedures and rules. While the Public Revenues, also transferred from the Central Government, are subject to horizontal allocation procedures enshrined in law, not all of the factors are currently applied. However, these allocations are rule based. The effect is to make over 90 % of the horizontal allocations transparent and rules based.
(ii)Timeliness of reliable information to SN government on their allocations	A	Local Authorities are provided the budget ceilings at the start of the budget process in May along with the Line Ministries.
(iii) Extent of consolidation of fiscal data for government according to sectoral categories	A	All Local Authorities provide quarterly financial statements to the Ministry of Local Authorities. On an annual basis the Local Authorities submit final accounts that are included in the national appropriations accounts when they are presented to the COCA 9 to 10 months after the close of the Fiscal Year.

3.2.5 Oversight of Aggregate Fiscal Risk from Other Public Sector Entities

3.2.5.1 The Yemen Government manages oversight of the public enterprises under the guidance of the Public Corporations Law 35, 1991. There are 5 active AGAs and 11 Special Funds registered. The Economics Department of the Ministry of Finance provides oversight and guidance to the Public Enterprises. Its Monitoring and Performance Evaluation Unit monitors and evaluates the performance of the Public Enterprises. Where Public Enterprises are found not to be in compliance with the requirements of the law or where anomalies are identified these may be reported on and forwarded to the Minister of Finance and to COCA.

3.2.5.2 Public Enterprises submit quarterly financial statements to the Economics Department and submit audited financial statements annually. By law all Public Enterprises adopt a January 1st to December 31st fiscal year and adopt an accrual accounting basis for their financial reporting. The financial reporting standard along with accounting notes provides a basis for assessing fiscal risk. Public Enterprises can borrow upon approval of their respective board of directors. The Ministry of Finance consolidates the Public Enterprise financial statements and submits revenue and expenditures documents to the Cabinet and Parliament each year. It is important, however, that the Central Government consolidates ***fiscal risk issues*** like debt service default (with or without guarantees issued by central government); operational losses caused by unfunded quasi-fiscal operations; expenditure payment arrears and unfunded pension obligations; into a report at least annually. The PEFA Task Force examined the latest Annual Report and discovered that fiscal risk issues were not consolidated in a separate section of this report.

3.2.5.3 As a matter of policy, the Government has tended to subsidize loss making Public Enterprises; however these for the most part have been planned and reflected in budgets. The Monitoring and Performance Evaluation Unit within the Economics Department has been particularly effective in providing an early warning mechanism for Public Enterprises that develop financial difficulties.

3.2.5.4 Local Authorities are directly supervised by the Ministry of Local Government. They have to provide annual budgets for the funds received from the Government of Yemen and their self-raised funds. They submit quarterly statements of revenue and expenditure for all revenue and expenditure. They have no borrowing authority, cannot issue guarantees and are subject to the government financial management regulations and instructions. Fiscal risk associated with the accrual of expenditure arrears, like is the case for Line Ministries, remains an area of concern. The Local Authorities do not submit regular information on expenditure arrears to the Ministry of Finance.

Indicator	Score	Brief Explanation
PI-9 Oversight of Aggregate Fiscal Risk	**C+**	
(i)Extent of central government monitoring of AGAs/PEs	C	Law 35, 1991 provides the legal authority for control and oversight to the MoF. The Economic Department within the MoF is dedicated to oversight of the Public Enterprises. Quarterly reports are submitted to the MoFP. MoFP reports to the Parliament annually and present a summarised financial report. The accrual basis along with accounting notes provides a basis for assessing fiscal risk. However, fiscal risk issues like debt service default (with or without guarantees issued by central government); operational losses caused by unfunded quasi-fiscal operations; expenditure payment arrears and unfunded pension obligations; are not being consolidated into a separate report.
(ii) Extent of central government monitoring of SN governments' fiscal position	A	The Local Authorities are monitored by the Ministry of Local Authorities through their annual budget process and through monthly budget implementation reports. They are unable to borrow directly.

3.2.6 Public Access to Fiscal Information

3.2.6.1 Transparency will depend on whether timely information on the budget and its execution by the government is made available and is readily accessible to the general public and other stakeholders in the budget process. Such transparency requires that the Government make relevant information widely available in a timely fashion, and selects outlets that are readily accessible by a wide section of the population. There is much information pertaining to public finance management laws now available in summary formats on official websites. Further the COCA has a website and puts out a newsletter that reports on important audit findings.

3.2.6.2 The Ministry of Finance does not employ newspapers or other media to present budget release data for different budget heads and programmes. Budget documentation including the Budget Speech is available from the Ministry of Finance, but these are often not available in sufficient quantity to provide or sell to the public. Circulation is limited principally to Members of Parliament, Governorates (5 sets each) and Line Ministries. In practice only consultants, academic researchers and some journalists have access to printed budgetary information. These must make special requests to receive such information and so such access may be restrictive.

3.2.6.3 The High Tender Board maintains a list of contracts above 125 Million Yemeni Riyals that were procured under the open tender method. However, none of these lists are published or made available to the public. There is still in many instances a reluctance to share government information by some officials[24].

3.2.6.4 Officials cite as an example where greater attention to transparency has resulted in dramatic improvements the provision of information on budgetary allocations to facilities. A recent budget release program carried out by the Ministry of Finance supported by DFID, and based upon increased transparency in budget information, has proven very effective in ensuring budget releases to the level of health facilities. The Ministry of Finance provides direct budget information to heads of health facilities on the releases that have been provided to health facilities with copies to respective Governors and heads of local authorities. This has considerably improved upon the actual funds received by these facilities. This effort is now being extended to the education sector, even though that effort is proving more difficult to implement than was the case for the health facilities.

3.2.6.5 Table 3.7 provides a summary of the elements to which public access is essential.

Table 3.7
Public Access to Information

Elements of information for public access	Availability and means
Annual budget documentation when submitted to the legislature	Yes - is made available to the public only through researchers, journalists and consultants at the time of submission of budget documents to the parliament. Since 2007 summary budget information has been available on the MoF website, but only after the approval of the budget by the Parliament. (www.mof.gov.ye).
In-year budget execution reports within one month of their completion	No – these are not made available to the public
Year-end financial statements within 6 months of completed audit	Yes – these are made available in printed reports approximately nine months after the close of the fiscal year and two to three months after the completion of the audit. They are available to researchers, consultants and journalists. Summary financial reports are currently available on the MoF website (www.mof.gov.ye).
External audit reports within 6 months of completed audit	No – these are not generally available to the public and are not yet available on the COCA website.
Contract awards (app. USD 100,000 equiv.) published at least quarterly	No – contract awards are not published
Resources available to primary service unit at least annually	No – these are not made available to the public

[24] On many occasions officials were reluctant to provide documentation (especially where not already printed) to the PEFA Assessment team due to concerns that doing so might get them in trouble with higher ups. It is important to note that many officials directly involved with PFM reform demonstrated a strikingly different attitude about providing information to the PEFA Assessment team.

Indicator	Score	Brief Explanation
PI-10 Public Access to Fiscal Information	**C**	Currently (2007) the Government has made available a number of fiscal reports available on its reports. This includes the annual budget documentation and year end financial statements. Access of budget documentation at the time of submission to parliament and year end financial statements are available only to researchers, consultants and journalists. The Government makes available 2 of the listed types of information.

3.2.7 Orderliness and Participation

3.2.7.1 The budget preparation process is clearly articulated in the legislative and regulatory framework of Yemen. The Finance Law spells out the roles and responsibilities of different players in the budget process. The budget ceilings are determined by the MoF in accordance with policy and cognizant of resource envelope constraints. Under the current budget preparation procedures a committee whose members include the Ministry of Finance, the Ministry of Planning, the Tax Authorities, the Ministry for Oil, and the Central Bank of Yemen is responsible for setting the total budget envelope and the allocation across main budget heads. These budget ceilings are then approved by a Cabinet sub-committee – the Committee of Policies, Economics and Fiscal Data. The budget ceilings are set on the basis of macroeconomic indicators and to a certain extent take into account the government's policy objectives. However, the budget process does not yet fully incorporate strategic elements introduced through a direct consideration of sector strategies nor is there a direct and literal with the National Development Framework – DPPR.

3.2.7.2 The Budget Call Circular, including ceilings by budget head, is distributed to Line Ministries no later than May 15th. These ceilings are also submitted to the broader cabinet but not to the parliament. It is the responsibility of the Line Ministries to prepare their budgets within their overall ceiling and submit their budget proposals within the first week of August – leaving them over two months to prepare their budgets. The budgets are then presented to and negotiated with the Ministry of Finance where estimates exceed ceilings. The Line Ministries submit and negotiate their recurrent and capital budgets separately. The Local Authorities also present their recurrent budgets directly to the Ministry of Finance. These are funded through direct Central Government transfers. Any modifications agreed as a result of the negotiations are allowed three days to complete the amendments.

3.2.7.3 The completed budgets are presented to the Minister of Finance by the second week of September, who upon approval submits it to Cabinet no later than the second week of October. The proposed budget is then submitted to Parliament in the last week of October which usually completes the budgetary debates and passing of the annual appropriations bill no later than the third week in December. So typically it has about 8 weeks in which to review and pass the appropriations bill. The President signs the appropriations bill into law the last week of December.

3.2.7.4 The budget calendar which begins in early May of each year, allows reasonable (approximately ten weeks) for the Line Ministries to prepare their budget submissions. Line Ministries describe the budget call circulars as having clear instructions and guidelines. The Budget preparation process is principally a top-down process. The main factors that affect the weaknesses in bottom–up participation is the poor to non-existent data available on personnel, and the poor available information on the investment budget to facilitate meaningful recurrent expenditure estimates emanating out of the investment budget. Line Ministries characterise the budget circular instructions as too restrictive and they do not properly account for shifting national priorities. They identify essential operation and maintenance expenditures as not being properly budgeted for. In addition, capital projects appear not to be linked to a long-term strategy for essential capital investment necessary for delivery of services, neither is there adequate linkage between the capital investments and the recurrent expenditure consequences.

3.2.7.5 In the past three years, the budget has always received its final approval from parliament before the start of the new budget year. In practice enactment of the budget into law by the President occurs in the last week of the year. All expenditure must be preceded by an authority to incur expenditure through the issuance of a General Warrant upon approval of the appropriations bill.

Indicator	Score	Brief Explanation
C(i) Policy-Based Budgeting		
PI-11 Orderliness and participation in the annual budget process (M2)	**A**	
(i)Existence of, and adherence to, a fixed budget calendar	A	The budget process is clearly set out. On the basis of the ceilings provided by MoF and approved by a Cabinet Sub-Committee, the Line Ministries have about 10 weeks to prepare their submissions.
(ii) Guidance on the Preparation of budget submissions.	A	The MoF issues comprehensive and clear budget circulars. The Budget ceilings/circulars for the last three years were approved by a Cabinet Sub Committee before the distribution of the circular to Line Ministries. There is some concern about the level of alignment between budget ceilings and actual requirements. The budget preparation procedure appears to be principally top-down.
(iii) timely budget approval by the legislature	A	The legislature has in the past three years always approved the budget prior to the start of the new fiscal year

3.2.8 Multi-Year Perspective

3.2.8.1 Yemen has taken the very first steps towards instituting a multi-year perspective to its budget formulation. The Government adopts a conventional macroeconomic framework as the basis for its forecasts on revenue, expenditure and deficit projections, and its budget preparation does incorporate some elements of its broad policy objectives. The Planning Department within the MoF employs a forecasting model which captures many of the key factors even though there may be some question about the model input assumptions. The UNDP is providing technical assistance to the development of the macro-fiscal framework as part of the implementation of the PFM Reform Action Plan. At the present time though, the budget preparation process does not employ or integrate these macro-fiscal forecasts. There is therefore no direct link between multi-year estimates and the subsequent annual budget ceilings set. Only recently has there been a committee set up to ensure that uniform forecast oil prices are adopted by the Ministry of Planning, Ministry of Oil, CBY and the Ministry of Finance. The revenue forecasts adopt a conservative posture for grants and only include inputs where there are already signed financial agreements. This is a particularly conservative posture for a Multi-year perspective. This may be in part due to the weak coordination between donor budget estimates for project support and the Government budgetary process (see D-2).

3.2.8.2 The Government introduced a five year medium-term Socio-Economic Development Plan for Poverty Reduction (DPPR) in 2006 which highlights measures to improve economic growth and reduce poverty and incorporates the Millennium Development Goals along with other targets. The DPPR was developed within forecast macro-fiscal aggregates and its investment requirements are costed but exclude any recurrent expenditure impacts. At present, fiscal forecasts of revenue and expenditure aggregates are prepared for three year horizons following the budget year based on GFS standards. The link between forward macro-fiscal estimates and subsequent budget ceilings are not yet in place. The MoF publishes no independent material on the fiscal forecasts and all forecasts remain internal documents. Given the capacity constraints, there is some question as to whether the scope and depth of macro-fiscal analysis as well as policy engagement currently being undertaken can effectively guide the budget process.

3.2.8.3 The Public Investment Program (PIP) contains fully costed sector strategy for all sectors. It has investment expenditure estimates but not the recurrent expenditure estimates. The PEFA Task Force assessed the total expenditure in Education, Agriculture, Water, Health and Electricity sectors during the year 2007, which have fully costed sector strategies, and compared that with the total government expenditure in that year. It discovered that total expenditure-both investment and recurrent-in above mentioned sectors was 38.59 % of the total primary expenditure. Their sector plans however are not prepared within a macro-fiscal framework. For example, the National Strategy for the Development of Basic Education in the Republic of Yemen (2003-2015) neither has its planning horizon or update schedule aligned with the National Development Framework[25]. In contrast the National General Secondary Education Strategy is fully costed with forward recurrent expenditure impacts considered. The PFM Reform Action Plan does not include the full costing of investment and recurrent expenditure.

3.2.8.4 Most of the important investment decisions are selected after analysis from the Ministry of Planning. The Public Investment Program contains fully costed sector strategies for all sectors regarding investment expenditure. The recurrent cost implications are not directly taken into account. However, Investment Budget and Recurrent Budget are surely linked for Electricity, Agriculture, Water, Health and Education sectors, all of which have fully costed sector strategies. However, outside budget investments like SFD are not linked to the recurrent budget. Thus, a link to the forward expenditure estimates does exist for above mentioned major sectors. Thus, investment decisions related with aforesaid sectors have links (although weak) to their sector strategies and their recurrent cost implications are also included in forward budget estimates for the sector.

3.2.8.5 The first rudimentary steps towards the implementation of a Medium Term Expenditure Framework (MTEF) that have been taken, however the budget documents include almost no elements of an MTEF such as forward estimates or any sectoral, programmatic or functional classification summaries. The PFM Reform Action Plan anticipates that the 2009 Budget documents shall introduce the first nascent elements of an MTEF; however there is still some reservation with some Government officials as to the preparedness of the Yemen PFM systems to undertake a full blown implementation of MTEF within such a short time frame.

3.2.8.6 Part of a credible macro-fiscal framework would be a clear debt management policy. Yemen has not yet established a clear debt management policy. A draft Debt Management Bill prepared in 2005 is currently under consideration. Article 5 of this bill requires the creation of a Committee chaired by the Ministry of Finance to put the general framework of the policies and strategies for administrating public debt and to determine clear debt management targets. The Bill also limits total debt not to exceed 60% of GDP. At the present time the Cabinet sets domestic debt ceilings (both fiscal and monetary) within which the Central Bank is to operate. In practice the Central Bank rolls over its stock of domestic stock and has broadly maintained the levels of domestic debt at the levels slightly above the previous year. There are Debt Management Regulations, Cabinet Resolution 296, 2000 which serves to guide the management and forecasting of debt levels.

3.2.8.7 The Central Bank employs the UNCTAD Debt Management Financial Analysis System (DMFAS) to register and track its external debt. The Ministries of Finance and Planning both have direct data access to the CBY server. Debt sustainability analysis is performed on a semi-annual basis and the reports submitted to Cabinet. The debt stock is reconciled on a monthly basis by the Ministry of Finance and the debt stock is published quarterly in the Government Financial Statistics as well as posted on the Ministry of Finance website.

3.2.8.8 The process for obtaining approval for inclusion of a project in the Government investment program needs to derive from a more robust strategic planning process based upon fully costed sector plans well aligned with the national development framework, DPPR. In practice, however

---

[25] A medium term expenditure framework (MTEF) for the Basic Education Sector derived from the National Strategy for the Development of Basic Education in the Republic of Yemen (2003-2015) (without integration into a national MTEF) was prepared in 2007 for the years 2007 to 2011. While the investments are costed the recurrent expenditure impacts are not. The sector MTEF has not been developed within national multi year fiscal forecasts.

actual selection is based principally on analysis by the Ministries of Planning and Finance, and also on donor and political willingness to fund them - rather than a prioritisation of investment plans according to strategic priority, resource availability and recurrent cost implications.

Indicator	Score	Brief Explanation
C(i) Policy-Based Budgeting		
PI-12 Multi-year perspective in fiscal planning, expenditure Policy and budgeting	**B**	
(i) multi-year fiscal forecast and functional Allocations	C	Forecasts of fiscal aggregates are prepared for three years, including the budget year. The forecasts are not linked to subsequent budget ceilings.
(ii) scope and frequency of debt sustainability Analysis	A	DSA for external and domestic debt is carried out semi-annually and submitted to the Cabinet.
(iii) existence of costed sector strategies	B	The Public Investment Program (PIP) contains fully costed sector strategy for all sectors. It has investment expenditure estimates but not the recurrent expenditure estimates. The total expenditure in Education, Agriculture, Water, Health and Electricity sectors (which have fully costed sector strategies) was 38.59 % of the total primary expenditure during the year 2007.
(iv) linkages between investment budgets and forward expenditure estimates	C	Most of the important investment decisions are selected after analysis from the Ministry of Planning. The Public Investment Program contains fully costed sector strategies for all sectors regarding investment expenditure. The recurrent cost implications are not directly taken into account. However, Investment Budget and Recurrent Budget are surely linked for Electricity, Agriculture, Water, Health and Education sectors, all of which have fully costed sector strategies. However, outside budget investments like SFD are not linked to the recurrent budget. Thus, a link to the forward expenditure estimates does exist for above mentioned major sectors. Thus, investment decisions related with aforesaid sectors have links (although weak) to their sector strategies and their recurrent cost implications are also included in forward budget estimates for the sector.

3.3 PREDICTABILITY AND CONTROL IN BUDGET EXECUTION

3.3.1 Transparency and Taxpayer Obligations and Liabilities

3.3.1.1 There are three primary sources of domestic revenue for the Government of Yemen. These are Oil Revenues (approximately 75%), and tax revenues (approximately 19% - with income and sales tax making up approximately 15% and customs and excise taxes making up approximately 4%). Should Yemen's oil revenues (or a substantial part of them) be considered along with tax revenue? How it be considered is important with respect to the PEFA Assessment since indicators PI-13, PI-14 and PI-15 pertain specifically to tax payers and tax revenue. Of course irrespective of such classification all Government Revenue should adhere to sound Public Finance management principles such as being subjected to sound control, applying frequent reconciliation procedures and instituting functioning appeals mechanisms. Oil Revenues are subject to Production Share Agreements (PSAs) signed between oil production company and the Ministry of Oil and Mineral Resources. These PSAs are approved by Parliament and enacted into law by the signature of the President. Article 9 of Annex F (Accenting Procedures) of the PSA addresses taxes. Specifically Article 9.1.2 defines and specifies the calculation of the Contractor's taxable income. In Article 9.1.2 it further designates that the Oil Ministry "*shall assume, pay and discharge on behalf of the Contractor, the Contractor's Income Taxes out of the Ministry's share of crude oil*." It requires that within 150 days of the close of the tax year the Tax Authority provide tax receipts directly indicating the amount of taxes paid by Contractor. This suggests that the Contractor pays taxes through the Oil share it provides the Government with very specific terms for calculating the taxes. Consequently this arrangement makes a portion of the oil revenues tax revenue[26].

<u>The Ministry of Oil and Mineral Resources</u>

3.3.1.2 There are 22 Oil Companies operating in Yemen, 12 of which are currently in production accounting for approximately 474,000 barrels production per day. The oil revenues including the portion designated as fixed tax and income tax is regulated by the PSA as well as Income Tax Regulation Law 31, 1991 along with its amendments. While the Tax Law amendment adopted in 2004 and requires all taxable entities operating in Yemen to file their tax declarations no later than the end of the first quarter after the fiscal year, the PSA designates the Ministry of Oil and Mineral Resources to file on behalf of the contractor. According to the PSA the taxable income is based upon production quantities adjusted for allowable costs which include (i) operational costs, (ii) recoverable amortised development costs, and (iii) recoverable amortised pre-operational exploration and development costs. These costs are verified by quarterly reviews and an annual audit carried out by Deloitte and Touche in collaboration with the staff of the Petroleum Accounts Department within the Ministry of Oil. The costs are converted to oil quantities, as per the terms of the PSA, based upon a weighted average price of oil for a given quarter and subtracted by the inventory adjusted oil production figures for that month which are provided by the Contractor and independently verified by the Petroleum Exploration Authority. The taxes (along with the Government's oil share and royalties) are then provided in oil which is sold directly by the Marketing Department of the Oil Ministry on the world market. The sale price of the Government's share is overseen by a ministerial Committee for Marketing Oil that usually meets once a month. The members of this committee include the Minister of Oil, the Minister of Finance, the Minister of Trade and Industry, the Governor of the CBY, the General Director for the Oil and Gas Company, with the Manager of the Oil Marketing Department acting as Secretary. The price is based upon the quality of the oil (there are two main qualities) benchmarked on 60 day forward Brent Crude Oil prices, and adjusted for discounts determined on the basis of the average price for the 5 days after the issuance of the bill of lading. Invoicing (and payments) are made on the basis of each crude oil shipment and are due within 30 days of invoice date.

3.3.1.3 The PSA provides information the tax calculations but is unclear on the tax obligations pertaining to penalties. There are no clear guidelines as to applicable penalties as might arise as a consequence of overstating allowable costs, that are only subsequently revealed upon a quarterly review or audit by the external auditor along with the Petroleum Accounting Department. The issue is made even more obscure by the designation of the Oil Ministry to pay and discharge on behalf of the Contractor his tax obligation. Officials for the Tax Authority state that they have had difficulties attempting to apply penalties to the oil producing companies.

3.3.1.4 The procedure for a tax appeal begins when a taxpayer wishes to appeal a tax assessment that differs from the contractor's own Government share determination. It is then submitted to the Settlement Committee which is made up of the General Manager for the Petroleum Accounting Department, a representative of Deloitte and Touche, a representative of the Tax Authority and a representative of the Company. This Committee meets with the appealing taxpayer in an

[26] The two most recent PSA models do not specifically calculate taxes. In some ways the PSAs may be interpreted as making the Contractor tax exempt, with an arrangement with the Ministry of Oil that indemnifies them against any tax liabilities. Indeed this arrangement appears to have evolved as a direct consequence of contractors negotiating against double taxation, both in Yemen and in their host countries. The attempt to meet this objective may have obscured some of the obligations and liabilities of contractors.

attempt to reconcile and resolve any differences. If the appellant is not satisfied with the outcome, then it is forwarded to the Minister of Oil and a senior representative of the Company. If no resolution is obtained then it is submitted to arbitration before the Commercial Court in Paris.

The Tax Revenue Authority

3.3.1.5 The Tax Revenue Authority is regulated by Income Tax Regulation Law 31, 1991 along with its amendments. The Self-Assessment Taxation scheme was adopted in 2004 and requires all taxable entities operating in Yemen to file their tax declarations no later than the end of the first quarter after the fiscal year. Each tax filing is checked for compliance with the filing requirements. More detailed review of filings is based upon the following criteria: whether the taxpayer made a loss; whether there has been a reduction in tax liability over the previous year; or whether there has been a rapid increase in expenditure or a decrease in expenditure.

3.3.1.6 The Tax Revenue Authority provides information to the public on taxpayer obligations and liabilities through joint programmes with the Chamber of Commerce in each of the 22 Governorates. The Tax Revenue Authority publishes a number of pamphlets that explain taxpayer obligations and liabilities. It also maintains a website where such information may be obtained. They carry out tax education campaigns every year using television, radio and newspapers. They also run workshops each year for the six largest governorates. The General Directorate for Tax Payer Services maintain a hotline to answer questions on tax obligations and preparations and also caters for walk in traffic. Officials are available to the public to explain tax registration and filing procedures.

3.3.1.7 The procedure for a tax appeal begins when a taxpayer wishes to appeal a tax assessment that differs from the taxpayer's filed tax declaration. It is submitted to the General Directorate for Appeals where it is screened for completion of submitted supporting documentation and arithmetic consistency. It is then submitted to the Reconciliation Committee for Tax Appeals which is made up of Tax Authority Staff. This Committee meets with the appealing taxpayer in an attempt to reconcile and resolve any differences. If the appellant is not satisfied with the outcome, then he or she may appeal within 30 days to the Tax Appeal Committee whose membership is made up of an independent external auditor as chairman, two members of the Chamber of Commerce and two members of the Tax Authority. The Tax Appeal Committee must make a ruling within 60 days of the filing of the appeal. It is restricted to either accept or reject the recommendation of the Reconciliation Committee for Tax Appeals. The tax appellant has a right to appeal further to a tax court if unsatisfied with the ruling. In the six month period January to June 2007 under the category of major tax payers there were a total of 280 cases submitted to the Reconciliation Committee for Tax Appeals of which 6 were brought before the Tax Appeal Committee. When tax assessments are carried out the final tax audit findings are submitted to the Taxpayer using Form 50. On this form the rights and procedures for appeal of the findings of the tax assessment are spelled out.

The Customs Department

3.3.1.8 The Customs Authority is regulated by the Customs Law 41, Amended 2005. The customs department employs Automated System for Customs Documentation and Administration (ASYCUDA++). This system has been networked to integrate all customs points in the country except four remote locations. The Government is working with USAID along with UNCTAD to upgrade this system to ASYCUDA World. One benefit expected is a more independent and standardised valuation system. Officials report that Customs documentation typically takes 48 hours to process, even though they acknowledge there are delays often experienced for large consignments. Customs assessments are based largely on self assessments. This though is complimented by physical inspections applied on a random sampling basis and an independent valuation of the cost of goods. At this time 8 x-ray machines have been installed to scan the contents of containers. In some points electronic manifests are submitted prior to the arrival of the ships.

3.3.1.9 Extensive training was carried out on the ASYCUDA++ procedures to clearing agents and customs brokers, as well as to the customs officers and business representatives. Three workshops were held at each of the customs points across the country. There have also been workshops held for the general public on the customs law, tariffs and smuggling. The Customs Department posts its laws and procedure guidelines on its website at www.customs.gov.ye. The website includes a help link. The Customs Department publishes a quarterly newsletter and has published a user's guide. There is a Follow Up Department which serves as a help desk to the general public and has its number published in newspapers. Officials are available to the public to explain customs procedures.

3.3.1.10 The procedure for a customs valuation appeals begins with the head of the particular customs point where the goods are to be cleared. A Values Committee has been established to receive appeals made pertaining to valuation. If no resolution can be arrived at the appeal is forwarded to the Chairman of the Customs Department. Form C4 sets the final valuation. Included on this form is a statement on the importers right to appeal. There are substantial discretionary powers by the Heads of Customs Points in the setting of import values even though there have been recent efforts to harmonise such valuations. Specifically there have been set values defined for 30 common import items. Further a Values Committee has been set to receive appeals made on valuations. Customs Forms C4 and G3 that address valuation include a notification on the importers right to appeal valuations. Customs penalties may be applied, but in accordance with Article 206 of the Customs Law the Chairman of Customs may negotiate the penalty, if that is leads to an unsatisfactory outcome it may be referred to the Minister who is also empowered to negotiate the penalty.

Indicator	Score	Brief Explanation
PI-13. Transparency of taxpayer obligations and liabilities (M2)	**B**	
(i) Clarity and comprehensiveness of tax liabilities	C	Legislation and procedures for all major taxes exist in the laws and in guidelines. These are clear and comprehensive. The discretionary powers in the case of the Customs Department both for valuations as well as for penalties applied remain substantial. In the case of the taxes on oil producing companies there is lack of clarity as to if and how late payment penalties may be applied.
(ii) Taxpayer access to information on tax liabilities and administrative procedures	A	The taxpayer access to information is widely available through pamphlets, a website, educational workshops, a hotline and walk in assistance. There are also promotional programmes in print and electronic media. The Tax Authority carries out annual education campaigns jointly with the Chamber of Commerce. The Oil Producing Companies have clear instruction on tax liabilities and procedures (charged to the Oil Ministry) included in the Production Share Agreements.
(iii) Existence and functioning of a tax appeals mechanism	B	Tax appeal comprises three main levels: objection, appeal and the law courts. These are set out in the Tax Acts and guidelines provided with each tax assessment made. They are implemented across all governorates and appear to be functioning well in the case of the Tax Authority. They are also spelled out clearly for the Oil Producing Companies. In the case of the Customs Department while there is a clear tax appeals system there remains some question on the effectiveness of checks and balances incorporated into the appeals procedures given the level of discretion over penalty negotiations exercised by both the Commissioner of Customs as well as the Minister of Finance.

3.3.2 Effectiveness of Measures for Taxpayer Registration and Tax assessment

The Tax Revenue Authority

3.3.2.1 Tax management has been computerised and a Tax Identification Number (TIN) is used to uniquely identify each registered tax payer. Uniqueness is ensured by including an identification number (such as passport number or national ID card number for individuals) and making checks against names and other data fields prior to registering a new taxpayer. The same TIN is used for sales tax and for customs. It is a requirement to complete business registration procedures and so in this way links business registration with tax registration. It is a requirement for participation in public tenders.

3.3.2.2 No specific penalties for-non compliance with tax registration exists however late payment penalties are applied retroactively when tax payers register late and are treated as tax evasion cases which draw a penalty of 50% to 150% per annum. Officials state that tax evasion and late registration, when discovered, are prosecuted to the full extent of the law. The value of penalties collected in 2006 was YR 209,870,034. Full compliance with Tax Registration Requirements is assured by periodic inspections of commercial entities. Late income tax payment not paid by the date upon which it becomes due and payable attracts interest at the rate of one and a half per-cent (1.5%) per month or part thereof for the period during which it remains unpaid. With commercial lending rates currently between 12% and 15% the up to 150% penalty serves should serve as a serious late registration disincentive. However it is not clear that the differential between late payment penalties and current commercial lending rates serves as an effective deterrent to late tax payments. The current penalty rates, given the extent to which they have been applied, should act as an effective disincentive.

3.3.2.3 Tax assessment and audits are selected on a risk assessment basis informed by incomplete or absent filings, recorded losses, and significant reductions in declared tax liabilities from one year to the next. The selection is also considers significant increases in expenditures or late payments have been more than 24 hours after the filing of the tax declaration.

The Ministry of Oil and Mineral Resources

3.3.2.4 Each of the oil companies has been assigned a Tax Identification Number (TIN). While the tax laws accommodate for late payment penalties, in the case of the oil producing companies these are not applied[27]. Tax Authority officials state that they have attempted to apply penalties but have been responded to by oil producing companies that all tax payments due are incorporated in the oil shares provided to the Government.

3.3.2.5 Officials of the Tax Authority state that upon the authority of minutes signed by the Ministers of Finance and Oil, the Tax Authority have been instructed to accept the Oil Company filings and that they are not subject to assessment or audit by the authority. Their assessments are limited to taxes on wages and salaries.

The Customs Department

3.3.2.6 Customs registration has been computerised and a Tax Identification Number (TIN) is used to uniquely identify each registered tax payer. The Tax Authority and the Customs systems are directly linked and direct links are planned to the Ministry of Trade and Industry, the Quality and Standards Board, the Central Statistics Organization, the Ministry of Finance and the Higher Council for Exports.

3.3.2.7 The nature of the customs procedures does not provide much opportunity for accruing late payment penalties. However in accordance with the Customs Manual penalties between 100% to 300% of the value of the imported goods plus 100% of the customs levy may be applied for misstated valued that on audit are discovered. There is an Audit and Verification Department

[27] In particular when self assessments of Government shares are shown to be understated through independent audit and reported two years later, any short fall in payments are made but without consideration of penalties that may be due given the portion of late payment that pertains to taxes.

that is responsible for pre-audit of customs documentation. There are plans to set up a post audit section but these plans are yet to be implemented.

Indicator	Score	Brief Explanation
PI-14. Effectiveness of measures for taxpayer registration and tax assessment	**B**	
(i) Controls in taxpayer registration system	B	Taxpayers are registered using a unique Tax Identification Number (TIN) maintained in a database. The TIN is required by other administrations thus supporting the registration process.
(ii) Effectiveness of penalties for non-compliance with registration and declaration obligations	C	In the case of the Tax Authority and the Customs Department high penalties along with the risk of imprisonment should serve as an effective deterrent to non tax registration. Effectiveness is assured due to the vigorous application of the penalties to tax evaders who are discovered. However late payment penalties probably do not serve as fully effective disincentives given the commercial lending rates pertaining in Yemen currently. In the case of the Oil Producing Companies it is not really clear what penalties if any are applicable.
(iii) Planning and monitoring of tax audit and fraud investigation programs	B	Planning and monitoring of tax audit and fraud investigation programmes is carried out and managed using a selection basis derived from risk assessment. In the case of the 12 oil producing companies all are reviewed and audited on an on-going basis. The Customs Department plans to institute a risk basis for audit and fraud investigations but these have not yet been instituted.

3.3.3 Effectiveness in Collection of Tax Payments

The Tax Revenue Authority

3.3.3.1 The level of income tax arrears in Yemen as a ratio of income tax collections was significant and averaged 3.6% (weighted average) in the 2005 and 2006 fiscal years. These figures include 3.7 Billion YR, which the Tax Authority classifies as uncollectible due to these companies having declared bankruptcies. There has been a request to have the uncollectible amount written off or otherwise suitably treated but which is yet to be carried out by the Ministry of Finance[28]. Tax arrears collection rates averaged less than 60% in 2006 as indicated in Table 3.8. This table provides a summary of income tax revenue collection arrears in proportion to tax arrears stock levels. The ratio of the collection of arrears to tax arrears stock is 6%, 72% and 16% for the three years assessed.

Table 3.8
Tax Arrears Stocks and Collection for FY 04, FY 05 and FY 06

		2004	2005	2006
1	Opening Balance	3,760,360,511	4,290,556,643	4,991,739,593
2	Uncollectable (write off requested)	3,700,000,000	3,700,000,000	3,700,000,000
3	Adjusted Opening Balance	3,760,360,511	4,290,556,643	4,991,739,593
4	Added during the year	763,893,667	3,801,405,027	228,023,580
5	Total Arrears	4,524,254,178	8,091,961,670	5,219,763,173
6	Arrears recovered during the year	233,697,535	3,100,222,077	808,501,015
7	Closing balance 31/12	4,290,556,643	4,991,739,593	4,411,262,158
8	% Recovered (excluding current assesments)(6/5)	5%	38%	15%
9	% Recovered (including current assesments)(6/3)	6%	72%	16%
10	Total Income Tax Revenues	116,632,158,659	153,741,827,622	219,537,136,454
11	% Areears (5/10)	3.9%	5.3%	2.4%
12	**Average % Total Tax Arears/Total Collections for 2005 and 2006**			**3.6%**

Data obtained from Tax Collection Department. All amounts in Yemeni Riyals[29].

[28] When the analysis is repeated assuming that the requested amount of 3.7 Billion Yemeni Riyals have been written off, the % of tax arrears falls to 1.6% and would thus warrant a score of A. However, such formal write off, has not been implemented to date.

[29] Note that the Tax Revenue presented in PI-3 include other than income tax revenue.

3.3.3.2 Tax collected is transferred daily to the Consolidated Fund and transfer advices are sent to the Ministry of Finance supported by copies of bank deposit slips. On a monthly basis the paid in deposits are reported and reconciled with the CBY within 10 days of the close of the month using Form 57. Quarterly reporting and reconciliations are done on a quarterly basis using Form 58. The results of Tax Assessments are not reported to the Ministry of Finance neither are payment arrears. With regards to tax arrears, these are not reported to the Ministry of Finance.

The Customs Department

3.3.3.3 In the case of customs tax arrears arise as a result of internal audit findings of payment discrepancies for which recovery procedures have been initiated and for any fines levied by the Customs Department arising from payment discrepancies arising from improper or incomplete customs declarations. Customs arrears are stated to be a very small proportion of custom's revenue collection. No collection data on customs tax arrears collection was available during the field assessment.

3.3.3.4 Customs duties collected is transferred directly on collection to the Consolidated Fund given that the CBY has representatives at every Customs collection point. Daily reconciliations are performed on a country wide consolidated basis. Daily reconciliations are submitted to the Ministry of Finance and also monthly summaries reconciled by the daily transfer confirmation slips are prepared and submitted to the Ministry of Finance.

The Ministry of Oil and Mineral Resources

3.3.3.5 The arrangements for review and audit of oil producing companies does not facilitate a determination of any arrears for up to two years after the close of the fiscal year. When unpaid amounts are owed the Government as determined from the review or audit basis, no penalties are applied. Future oil shares are adjusted to compensate for any arrears that may have accrued due to underpayments that have been made.

3.3.3.6 All payments are made directly to the CBY and typically are received within 30 days of invoice date. However, there are no reconciliation procedures in place even though officials of the Petroleum Accounting Department indicate that they intend to institute such procedures presently. Although this is an issue to be looked into by the government, but considering that Oil Share is not included in the definition of Tax for the purpose of PEFA methodology, only the effectiveness of Tax collection is to be borne in mind for this set of indicators.

Indicator	Score	Brief Explanation
PI-15. Effectiveness in collection of tax payments (M1)	**D+**	
(i) Collection ratio for gross tax arrears, being percentage of tax arrears at the beginning of a fiscal year, which was collected during that fiscal year	D	There are significant tax arrears in Yemen (>2%) with an average ratio for 2005 and 2006 that was 3.6%. The Tax Authority has requested to write off 3.7 Billion YR of uncollected taxes due to declared bankruptcies by the companies owing them. The collection ratios were 6%, 72% and 16% for the three years covered. There are not significant amounts of customs duties arrears. Given the mechanism for addressing past underpayments of Government oil shares there are no arrears on oil shares.
(ii) Effectiveness of transfer of tax collections to the Treasury by the revenue administration	A	Taxes are collected and paid into the Consolidated Fund are made daily on the next day after collection. The same arrangements exist for Customs duties. All payments for the Government oil share are paid directly into the Consolidated Revenue Fund.
(iii) Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the Treasury	A	Reconciliations of tax assessments, collections, arrears and transfers are done monthly within 15 days or so after the end of the month. A similar arrangement exists for Customs duties.

3.3.4 Predictability in the Availability of Funds for Commitment of Expenditures

3.3.4.1 The Ministry of Finance issues a six-monthly general warrant (authority to incur expenditure) that sets the cash withdrawal ceilings within which Line Ministries may incur expenditure. It does so by instructing the Central Bank of Yemen on expenditure ceilings for each of the Line Ministries and Local Authorities. These allocations therefore serve as the basis for commitment control. In the case of recurrent expenditure the Ministry of Finance authorises each Line Ministry to withdraw up to 1/6th of the general warrant appropriation per month. For capital expenditure allocations are on a quarterly basis. Any balances are automatically rolled over to the next month until the end of the year in the case of Line Ministries. Local Authority balances are carried over to the next year. All accounts are closed at the end of the year; any un-cleared cheques must be re-issued in the new budget year. The CBY maintains for each Line Ministry a single expenditure account with a sub-account structure that is coincident with the chapters and sub chapters of the budget. This therefore serves as a useful mechanism for controlling virement. There is no cash management carried out; this in spite of available information on pro forma revenue flows for oil revenues making up approximately 75% of the Government revenues and timely data on deposits from income and sales taxes, as well as customs duties. Line Ministries are not requested to prepare procurement plans from which cash flow projections may be derived and submitted to the Ministry of Finance. Lastly, the CBY operates a Treasury Single Account that provides fully reconciled bank balances for all Line Ministries down to the Governorate level. The Ministry of Finance operates timely and up to date tracking of its debt status. With these four elements in place, the Government of Yemen would be in position to operate a sound cash management programme to more efficiently meet its budget release objectives.

3.3.4.2 Currently there is no explicit cash management function carried out by the Ministry of Finance. The Central Bank of Yemen is responsible for ensuring cash availability, and does so on the basis of maintaining fully reconciled daily consolidated cash balances. However, without specific cash management tied to the availability of cash, it may lead to the Central Bank resorting to inefficient short term borrowing. Further, the CBY does not report on Treasury instruments so as to distinguish between fiscal and monetary treasury instruments. This blurs the lines between monetary and fiscal policy and can impact negatively on macroeconomic stability. Further, ignoring cash flow considerations both of Line Ministry requirements as well as revenue patterns and adhering to a mechanistic monthly allocation of 1/6th of the six-monthly general warrant can lead to inefficiencies where idle funds accrue in periods of low aggregate Line Ministry cash demand, and borrowings must be undertaken in periods of high cash demand.

3.3.4.3 No pro-forma Cash Flows are prepared by the MDAs. Budget releases are based solely on the proposed budget estimates submitted and issued at the beginning of each fiscal year. The six-monthly general warrant is updated frequently during the six-month period to take into account actual revenue achievements or of Line Ministries that do not spend their full allocations. This practice helps to undermine the credibility of the six month budget release general warrant and its usefulness as a predictor of available funds. In spite of revenue forecasts being readily derivable from oil sale invoices within a 30 day profile, no such forecasts are carried out to serve as a basis for preparing pro forma revenue cash flows to support effective cash management.

3.3.4.4 All payments are made directly out of the Consolidated Fund held with the Central Bank of Yemen. The Ministry of Finance also maintains Project Accounts through which loan and grant funds that are required to implement projects are placed. In addition the Line Ministries may in some cases control donor funds directly. The Central Bank of Yemen has twenty branches to cover all 22 Governorates as well as Sana'a. It is able to consolidate a treasury single account and reconciles the balance with the cash book on a daily basis at the end of each day. The CBY submits monthly expenditure reports to the Ministry of Finance on a monthly basis.

3.3.4.5 It may be of some interest to point out that the CBY does not carry out an accounting function even though some have characterised it as doing so, and the General Accounts Division of the

Ministry of Finance uses its monthly expenditure reports to reconcile its own accounts. The monthly expenditure reports can only measure the payments made out of a Line Ministry's account and does not distinguish between fully acquitted expenditures and advances. Consequently, the CBY expenditure reports are merely measuring budget releases and not actual expenditure.

3.3.4.6 Adjustments to budgetary allocations should be made by normal ex-ante virement procedures; or possibly by issuing a Supplementary Budget, once or so within the year; or alternatively it may occur by ex-post regularisation of unauthorised spending. In Yemen, only virements within sub-chapters of the budget may be authorised by the Line Minister. All other virements must be approved by the Minister of Finance. The Minister is further authorised to make advances from the Consolidated Fund for meeting urgent and unforeseen needs for public expenditure. The amounts advanced must be subsequently standardised by Supplementary Appropriation Laws. The Budget Implementation Guidelines mention the conditions in which in-year budget adjustments can be made by the government and who is authorized to grant approval to these adjustments.

Indicator	Score	Brief Explanation
PI-16 Predictability in the availability of funds for commitment of expenditures (M1)	**D+**	
(i) Extent to which cash flows are forecast and monitored	D	No Cash flow forecasts are prepared by the MDAS. The budget release mechanism does not include any expenditure cash flows even though it may take into account actual revenue achievements to adjust the six-monthly general warrant that sets cash withdrawal ceilings. No revenue forecasts are made even though the pro forma revenue profiles from oil share sales can readily be determined over a thirty day horizon.
(ii) Reliability and horizon of periodic in-year information to Line Ministries on ceilings for expenditure commitment.	B	MDAs are provided with six-monthly general warrants by the Ministry of Finance which serve as the commitment ceilings against which expenditure is made. At this time these six-monthly general warrants (translated into expenditure allocation ceilings) are updated within the six month period and so may dilute the predictability and reliability of the six-month authorities to incur expenditure. While no detailed data was available on updates, their 6 month rolling nature and discussions with Government officials suggest that MDAs are provided reliable commitment ceilings quarterly in advance.
(iii) Frequency and transparency of adjustment to budget allocations, which are decided above the management of Line Ministries	C	All significant virements must be made subject to the approval of the Ministry of Finance and the CBY account structure support a strict application of virement control. However the frequent updates of the budget release appropriations by the Ministry of Finance are not done in a transparent way. The Budget Implementation Guidelines mention the conditions in which in-year budget adjustments can be made by the government and who is authorized to grant approval to these adjustments.

3.3.5 Recording and Management of Cash Balances, Debt and Guarantees

3.3.5.1 The Minister of Planning is the sole authority for the contracting of loans, after consultation with the Line Minister on whose behalf the loan is being contracted, the Minister of Finance, and subject to the endorsement of the Cabinet and the approval of parliament and enactment into law of the financing agreement. While not yet enacted into law, a newly completed Debt Management Bill specifies debts stock to GDP ratio ceilings (60%). The objective for managing the debt is to keep it sustainable; sustainability being interpreted as maintaining a debt to GDP ratio below the ceiling. The debt to GDP ratio in Yemen remains low and in recent years this target has been met or exceeded. When statutory bodies contract loans that require a Government guarantee, the Government borrows on its behalf and onward lends to the statutory body. The procedures are subject to the same controls and procedures for the Government contracting a loan. All loan guarantees must be authorised by the Minister of Finance endorsed by the Cabinet and approved by parliament.

3.3.5.2 It should be noted that in spite of the stated strategic objective of limiting borrowing, there remains potential risks that threaten to undermine the debt management strategy. These primarily derive from the possible bail outs by the Government of loss making Public Enterprises. While it has been government policy to in some cases subsidize Public Enterprises, a fairly effective oversight mechanism for aggregate fiscal risk from Public Enterprises should mitigate this risk (see PI-9).

3.3.5.3 The Debt Management Unit uses the UNCTAD Debt Management Financial Analysis System (DMFAS). Comprehensive records on domestic and external debt are compiled and are updated and reconciled on a monthly basis. The server is housed in the Central Bank of Yemen with on-line workstations in the Ministry of Finance and the Ministry of Planning. The reconciliation is done on the basis of internal consistency checks, comparisons with the Central Bank as well as reconciliation with the bank statements from the lending institutions. Note that while many submit monthly bank statements, there are others that submit only on a quarterly basis or a six monthly basis. Comprehensive statistical reports providing information on debt stocks, debt service and debt management operations are prepared monthly and submitted to the Planning Division of the Ministry of Finance. The Planning Department of the Ministry of Finance publishes a quarterly finance statistics report on a quarterly basis. There are three levels of reconciliation performed. First are internal consistency checks to guard against mistaken entries or data corruption; the second are reconciliations done against lending agency bank account statements and the third is done against CBY data.

3.3.5.4 The recording and management of cash balances is carried out by the Central Bank of Yemen and reported to the Ministry of Finance. This role provides a critical component both for managing budget allocations to the Line Ministries as well as serving as an important information input to the function of managing borrowings carried out by the Debt Management Unit within the Ministry of Finance. The Debt Management Unit monitors all domestic (Domestic Loans Department) and external debt (External Loans Department, Grants Department). It reports comprehensively on debt stock levels, debt maturity profiles, and creditor, rate and currency compositions.

3.3.5.5 The payments system utilizes the Consolidated Fund for all payments on Government expenditure (except for grant and loan funded project accounts). This facilitates a monitoring mechanism that reports and reconciles the account on a daily basis. All active project accounts are held in the Central bank of Yemen and reconciled on a daily basis. There are small amounts held in Special Accounts directly by Line Ministries (estimated to be less than 1% of expenditure) that are not reconciled daily and remain outside this arrangement.

Indicator	Score	Brief Explanation
PI-17 Recording and management of cash balances, debt and guarantees	**B+**	
(i)Quality of debt recording and reporting	A	Comprehensive records on domestic and external debt are compiled and are updated and reconciled on a monthly basis. Comprehensive statistical reports providing information on debt stocks, debt service and debt management operations are prepared quarterly.
(ii) Extent of consolidation of the Government's cash balances	B	The payments system utilizes the Consolidated Fund for all payments on Government expenditure (except

Indicator	Score	Brief Explanation
		for grant and loan funded project accounts). This facilitates a monitoring mechanism that reports and reconciles the account on a daily basis. All active project accounts are held in the Central bank of Yemen and reconciled on a daily basis. There are small amounts held in Special Accounts directly by Line Ministries (estimated to be less than 1% of expenditure) that are not reconciled daily and remain outside this arrangement.
(iii) Systems for contracting loans and issuance of guarantees	B	The systems for contracting loans and issuing guarantees are bound by transparent procedures set within the legal and regulatory framework. Clear loan level ceilings are defined.

3.3.6 Effectiveness of Payroll Controls

3.3.6.1 The personnel emolument amounts to approximately 30% of the primary expenditures. There is a total a work force of approximately 460,000 public servants in Central Government even though the precise number remains unknown[30]. Human resources management is decentralised. The Civil Service Ministry serves as the oversight body responsible for setting the establishment ceilings and for monitoring personnel levels. The Civil Service Law, 1991 governs employment in the public sector. A Labour Strategy was approved by Cabinet in 2005 that governs the reform of the Civil Service. In July 2005 Wage Law was enacted which seeks to directly address the curbing ghosts. This reform effort is being supported by the World Bank.

3.3.6.2 Given the lack of reliable information on the actual personnel roles; the establishment which is used for preparing wage and salary budgetary estimates is based upon a 1998 assessment of the personnel rolls which included a census. Since then the establishment figure employed has been determined by assigning annual increases between 9% and 11% and further allocating 75% of the assigned increase to the social sectors. This approach to budget preparation has assured that the process is principally top-down and not based upon bottom up personnel roll estimates.

3.3.6.3 At the current time personnel roles remain highly fragmented. The Civil Service Ministry operates Oracle based databases implemented at the headquarters and the information centres located in 18 of the 22 Governorates. These databases are not directly linked neither do they have implemented in all cases, the regular updates of these databases to reflect new hires, terminations, retirements, and transfers etc. One consequence of such fragmentation of the personnel database has been the inclusion of multiple entries of a single individual permitting the payment of multiple salaries to the individual. Recent clean up exercises of the personnel databases bases upon the comparison of signed attendance sheets with payroll lists have identified a great many such cases of individuals receiving multiple salaries. In one case the person was collecting 24 salaries.

3.3.6.4 The Civil Service Ministry has developed standardised payroll software that has been made available to units with computer hardware and staffing capability to operate the software. However, not many Spending Units run this software. A number of Spending Units use the Regional Information Centres (RICs) as payroll service bureaus. They submit their payroll lists to the RICs who enter the information and run the payroll on their behalf. Under this arrangement there is a reconciliation made between the submitted payroll list submitted by the Spending Unit and the payroll run by the RICs. This still leaves some public entities where electronic spreadsheets and manual systems are used to manage payroll. Such a system is prone to errors and does not permit easy data queries. The payrolls run by the RICs are further reconciled with the Employee Database, but this has not been fully cleaned to date and so

[30] There are two personnel databases. The first includes all ministries, but through a clean up exercise has been shown to have a substantial number of ghosts and double dippers. The second, which includes biometric data controls, is still being developed and excludes the staff of the Ministry of Defence, the Ministry of Interior, the Judiciary and a substantial proportion of the Ministry of Education. Upon completion of the clean up exercise, it is anticipated that a comprehensive public servant database with full integrity will have been achieved.

questions the effectiveness of such a reconciliation process. The Civil Service ministry also follows a manual system to reconcile nominal roll with the payroll. It issues *Fatwa* to make changes in the nominal roll. Based on this *Fatwa*, Ministry of Finance effects change in the payroll. As per civil service ministry estimates, the average time taken in effecting this change is 15 days and the maximum time is one month. Even if one considers this to be an overestimate, the evidence suggests that the time taken is not more than six months.

3.3.6.5 The civil service ministry governs only about 30-35 % staff, and the bulk of staff is handled by their respective ministries, departments and agencies independently and the impact of a change in the nominal roll is within their own domain and immediate. The Civil Service Ministry handles public sector ministries like Education, Health, Transport, etc., for which Personnel Directors of those ministries are authorized to issue orders to make changes in the personnel records kept at the RICs. The officials of the General Department of Expenditure are authorized to make changes in the payroll. Audit Trails in the form of files with note-sheets and orders are maintained. Other ministries, departments and agencies including the army, COCA, parliament, police, election authority, judges, do not require fatwa to make changes in the nominal roll to be issued by civil service ministry and do not require ministry of finance to effect a change in the payroll.

3.3.6.6 The Vice Minister Civil Services informed the PEFA Task Force that his ministry issues *Fatwa* to make changes in the nominal roll, and based on that *Fatwa*, Ministry of Finance effects changes in the payroll. In certain cases, the changes are done within 24 hours and in some cases 2-3 days. But on an average, the time taken is 15 days. If the fatwa is issued by his ministry before the 15th of the month, the changes are effected within next month's payroll. However, if the fatwa is issued after the 15th, the impact on the payroll could be the month after. But in no case the time taken is more than 3 months. He also said that the retroactive changes required were in less than 5 % cases. However, it wasn't clear whether the issuance of *fatwas* is systematic and comprehensive. He also informed that the civil service ministry governs only about 30-35 % staff, and the bulk of staff is handled by their respective ministries, departments and agencies independently and the impact of a change in the nominal roll is within their own domain and immediate, for which, the timeliness of changes to payroll in respect of changes in personnel database could not be ascertained.

3.3.6.7 The Civil Service Ministry handles public sector ministries like Education, Health, Transport, etc., for which Personnel Directors of those ministries are authorized to issue orders to make changes in the personnel records kept at the RICs. The officials of the General Department of Expenditure are authorized to make changes in the payroll. Audit Trails in the form of files with note-sheets and orders are maintained. Other ministries, departments and agencies including the army, COCA, parliament, police, election authority, judges, do not require fatwa to make changes in the nominal roll to be issued by civil service ministry and do not require ministry of finance to effect a change in the payroll. However, no extra evidence could be deduced that "authority and basis for changes were clear" across government.

3.3.6.8 The Ministry of Education, which is responsible for about 240,000 employees or approximately 50% of the total number of public personnel employs a computerised payroll system however it is not based upon a single control personnel database that includes all of the teaching staff in the approximately 15,000 facilities. As reported in a Basic Education Tracking Survey carried out by the World Bank published in December 2006 there are substantial delays and inconsistencies in salary delivery. It points to a common practice of uncertain salary deduction by principals. The report notes that field surveys found that teachers never see their pay stubs and they never know how much they are supposed to receive for a particular month.

3.3.6.9 There is currently a programme being carried out by the Technical Unit, a joint effort of the Ministry of Finance and the Civil Service Ministry to clean up the payroll lists. This has been done by suspending all allowances payments and checking payroll lists against attendance sheets. However, without any simultaneous development of a linked database that is regularly updated it is unlikely that any gains in cleaning up the personnel rolls can be sustained. Still the credit goes to the ministry of civil service to ensure that Payroll and Attendance Sheets are cross-verified. Last it was done in July 2005, on the basis of which 27,000 ghost workers were removed from the payroll. A payroll audit was also carried out in August 2007, results of which are being compiled. However, these payroll audit were not covering 'all' central government entities, which should be done in future.

3.3.6.10 The payroll is audited by the Internal Audit Unit of each MDA. However, for the Line Ministries visited, it appears that the internal auditors typically perform one annual audit on a sample basis. Given the level of fragmentation of the personnel management and in absence of an integrated personnel management database, even at the level of the MDAs, including establishment and payroll, sample audits are not fully effective control tools. The Auditor General audits the payroll every year as part of its statutory audit. Its reports contain findings on payroll such as overpayments, advances and unpaid arrears of statutory deductions made to employees' salaries, albeit in a small proportion. There is no dedicated payroll audit carried out regularly but the Research and Establishment Control Unit perform regular operational audits of the MDAs' human resource management.

Indicator	Score	Brief Explanation
PI-18 Effectiveness of Payroll Controls	**D+**	
(i)Degree of integration and Reconciliation between personnel Records and payroll data	C	A computerized personnel data base exists for the civil services on the basis of which capturing of biometric details of all civil service employees is completed. However, this personnel database is fragmented and not fully maintained. It is also not linked to the Payroll database. But a manual system exists whereby civil service ministry issues a *fatwa* for any changes in the nominal roll. Based on this *Fatwa*, Ministry of Finance effects changes in the payroll. Reconciliation of the payroll with personnel records through this process is taking place at least every 6 months.
(ii) Timeliness of changes to Personnel records and the payroll	D	The civil service ministry issues *Fatwa* to make changes in the nominal roll, and based on that *Fatwa*, ministry of finance effects changes in the payroll. On an average, the time taken is 15 days. However, it is not clear whether the issuance of *fatwas* is systematic and comprehensive. With such fragmentation of personnel databases and no clearly defined systems for updating changes in personnel rolls, actual changes to personnel rolls is estimated to be longer than 3 months.
(iii) Internal controls of changes to personnel records and the payroll	D	There are some payroll controls but their effectiveness is undermined by the fragmentation and irregular updating of personnel rolls. There is evidence of substantial abuse of the payroll systems in the clean up exercise.
(iv)Existence of payroll audits to identify control weaknesses and /or ghost workers.	C	A partial payroll audit is being carried out by the Technical Unit by comparing attendance sheets to payroll lists.

3.3.7 Competition, Value for Money and Controls in Procurement

3.3.7.1 The Republic of Yemen in July of 2007 passed a new Tender Law that addresses a number of modern public procurement management features including a public procurement oversight authority and an administrative review board, as well as providing sanctions for non-compliance. Civil Society including such bodies as the Chamber of Commerce paint a rather troubling picture of public procurement in Yemen. Public Procurement in Yemen is characterised as not being transparent, and wrought with too many instances of fake competition, the use of middlemen to obtain contract awards and then selling them to other contractors for actual implementation, cases of the abuse of contract variations to inflate contract sums during implementation. Tender evaluations are described as arbitrary with no indicating of the evaluation criteria to be used provided on bidding documents.

3.3.7.2 COCA's findings on procurement are consistent with the Chamber of Commerce's description. It states that procurement is generally uneconomical and lacks transparency. It describes prices as exaggerated. It observes that procurement procedures are ignored and the lack of application of effective sanctions. It also mentions the practice of slicing as a way to keep procurement amounts below a given threshold and in so doing avoid the controls and authorisations required of a given procurement method.

3.3.7.3 The Government of Yemen is required to maintain data on public contracts awarded in individual Line Ministries and for all public tenders above 125 Million YR that was carried out using the Open Tender Method in the Supreme Tender Committee[31]. In August 2006 the Ministry of Finance issued a circular requiring Government Agencies to file lists of all contract awards, which was to be published on the website www.yemen-nic.com, however by October 2006 less than half of the Government Agencies were filing such procurement information. The PEFA Task Force tried to collect information from Public Works, Agriculture, Education and Health ministries on the kind of information they maintain (in specific registers) regarding all procurements above 125 million Yemeni riyals. Information from these ministries was received and reviewed but it was not possible to assess the percentage of procurements above 125 million Yemeni Riyals being either through open competition, direct offers or restricted tenders. Thus, it is not practically possible to make an assessment at the country level. There is thus insufficient data available to assess the proportion of contracts above the threshold which were carried out using the Open Tender Method.

3.3.7.4 Article 85 of the Tender Law provides the justification for less competitive methods. It provides for limited bidding, competitive bidding as well as direct purchase but does not provide clear and unambiguous guidance on the circumstances or procedures for use of the other methods. For example there is no reference to the exclusion of urgent circumstances that have arisen out of the dilatory conduct of a Procuring Entity the promotion. Employing a direct purchasing method justified on the basis of dilatory conduct would undermine effective competition.

Indicator	Score	Brief Explanation
PI-19: Competition, value for money and controls in procurement (M2)	**D+**	
(i) Use of open competition for award of contracts that exceed the nationally established threshold for small purchases	D	The Government of Yemen maintains data on public contracts awarded in individual Line Ministries and for all public tenders above 125 Million Yemen Riyals that was carried out using the Open Tender Method in the Supreme Tender Committee. There is insufficient data available to assess the proportion of contracts above the threshold which were carried out using the Open Tender Method.
(ii) Justification for use of less competitive procurement methods	C	The Tender Law establishes the open tender method as the preferred method and provides justification for less competitive procurement methods but is rather ambiguous in the application of the direct purchase method.
(iii) Existence and operation of a procurement complaints mechanism	D▲	While there is an Administrative Review Board to be created under the terms of the new tender law enacted in July 2007, the law in force for the period 2004 to 2006 did not facilitate addressing complaints regarding the implementation of a particular procurement process.

[31] A review of the Supreme Tender Committee list showed it to be only partial and did not include contracts awarded using procurement methods other than open tender. When the ledgers for the Ministry of Public Works were reviewed, they only contained lists of bidders, and did not include contract award data nor procurement method.

3.3.8 Effectiveness of Internal Controls for Non-salary Expenditure

3.3.8.1 As described in PI-16, six month (recurrent expenditure) and three month (capital expenditure) warrants are prepared on the basis of the budget allocations and used as the basis for setting the withdrawal ceilings for MDAs. Expenditure commitment control can only be based upon timely and accurate projections on the availability of funds. However, as described in PI-16 the practice of adjusting the budget release ceilings after the issuance of the original six monthly profiles undermines commitment control implementation as spending ceilings themselves become unpredictable over the intended six-month time frame. This thus undermines the effectiveness of internal controls for non-salary expenditure.

3.3.8.2 A number of MDAs use ledgers to operate commitment control ledgers but it is not certain that these are universally applied across all spending units across all Governorates or that they are fully integrated into the procurement/expenditure cycle for all non-salary expenditure. While there is a commitment control feature available on AFMIS, and consequently to the four ministries where it is currently under bet testing, the feature is not yet activated. The structure of the Treasury Single Account (Consolidated Fund) made to reflect the chapter and sub-chapter structure of the budget provides a sound basis for effecting virement control at that level based upon authorization from the Ministry of Finance.

3.3.8.3 The expenditure management rules and procedures are clear and accessible through manuals. Interviews with a wide variety of officials left an impression that there was familiarity with the rules and procedures. Each year the MoF issues Notes on the Budget Implementation to the Finance Officers in the Line Ministries that highlight areas of weakness in the previous year's budget implementation. However, in practice there are excessive delays. These may come about due to excessive duplication and possible rent seeking behaviour. These procedures begin with the Initial Purchase Request, where the availability of the goods is first checked for as available in inventory prior to initiating a procurement procedure. Tender Committees supported by technical specification and evaluation committees are responsible for bid announcement and vendor selection. Commitments are entered into with contracts or purchase orders which specify the goods, works or services required, the amounts to be paid and the delivery time. Inspection Committees are set up to inspect and accept goods, works and services and to ensure full compliance with the specifications and quantities committed to. All payments must be supported by Initial Purchase Requisitions, the Purchase Order, Minutes of the Tender Committee indicating vendor selection, the inspection report and the Goods or Services Received note or Interim Certificate. All expenditure documentation are reviewed for completeness and accuracy by the Inspection and Control Officers with authority to pass or reject but not to amend or modify.

Indicator	Score	Brief explanation
PI-20: Effectiveness of internal controls for non-salary expenditure (M1)	**D+**	
(i) Effectiveness of expenditure commitment controls	D	Commitment control ledgers are not maintained universally across all Spending Units. The AFMIS system under beta testing in four ministries does not have the commitment control module activated.
(ii) Comprehensiveness, relevance and understanding of other internal control rules/ procedures	B	Financial management rules and procedures exist and are documented and well understood. However there is much delay in practice which may be due to excessive duplication
(iii) Degree of compliance with rules for processing and recording transactions	C	Primarily due to the compliance checks that are carried out, compliance with rules pertaining to expenditure documentation is fairly high but there remain instances of emergency procedures that are used without adequate justification.

3.3.9 Effectiveness of Internal Audit

3.3.9.1 The jurisdiction of the Internal Audit function extends to all Line Ministries, Local Authorities and Public Enterprises. The internal audit function is carried out by two separate organizations. The first is the General Directorate for Internal Audit which is housed within the Ministry of Finance and headed by a General Director and currently has a staff of 21[32], 16 of whom are financial auditors. They carry out ex-ante, transactional and ex-poste audits. The second are the Inspectorate Directorates housed directly within the Line Ministries which carry out operational audits. In addition to these two audit functions, is an Inspector and Controller within the Finance Department of each line ministry who reports to the Finance Officer and is primarily responsible for pre-audit and compliance checks.

3.3.9.2 The General Directorate for Internal Audit carries out ex-post audits that focus primarily on financial audits with some systems audits[33] and only occasional value-for-money audits. The only performance audits carried out are specifically for the Ministry of Finance based upon annual work plans and set targets. It prepares Annual Audit Work Programmes and employs a risk based approach to the selection of public entities to be included in the audit work plan. The auditors carry out their audits on the basis of an audit manual that detail the methodologies to be applied. The selection is based upon expenditure volume, primary activity, previous audit findings and COCA reports. While the Internal Audit covers all functions of central government, operations however are restricted by staffing and budgetary constraints and so in practice Internal Audit Units are unable to fulfil effectively their full responsibilities and coverage. With a full time professional staff level of only 16, 34 Line Ministries, 22 Governorates and 303 Local Authorities can hardly be fully addressed. The focus is usually the Ministries of Health, Education, Public Works, Agriculture and Finance and the Electricity Corporation and the Special Funds. The security ministries and agencies are never included.

3.3.9.3 The General Directorate for Internal Audit reports regularly on its audit findings and submits these reports to the Minister of Finance, and to the respective Line Ministries or Local Authorities; with copies to COCA and the Cabinet. COCA takes into account the Internal Audit reports in developing its annual audit plans.

3.3.9.4 Head of Procuring Entities are responsible for carrying out recommended corrective measures. The management response to audit queries in general appears to be varied as officials report. No specific Audit Committees have been set up within Line Ministries to follow up on audit findings and ensure management responses and actions; however, within the Ministry of Finance is a Follow Up Department whose responsibility it is to follow up on audit recommendations carried out by the Line Ministries.

3.3.9.5 The Inspectors within the Finance Departments housed directly within the Line Ministry serve the primary purpose of quality assurance of the procurement and expenditure documentation and on the quality and completeness of recording in financial ledgers. This would appear to be an important element to assuring the effectiveness of internal controls. However, their pre-audit role raises two concerns: the first is the issue of independence since might become a part the expenditure cycle upon which they are to report, and the second is the opportunities for rent seeking that may be introduced by de-facto making payments subject to the internal auditor's "approval". Yemen has attempted to address both concerns by limiting the Inspector's role to a stop order to be reported to the Finance Officer for action rather than an "authorisation" role and limiting to a limited period (1 to 3 days) the time in which to issue a stop order.

[32] In addition it has access to 32 other auditors in other departments within the Ministry of Finance.

[33] The Audit Work Plans do not present information in which to determine what proportion of man-days is allocated to systems audits. Even after much discussion with officials of the Internal Audit Department, none could provide estimates. In two separate interviews with two previous DGs for Internal Audit both with tenures during the period of review they stated that the system audits took up a very small percentage of audit time. In one's opinion there was no more than 10% of audit time spent on systems audits. The other expressed it as being between 5% and 10%.

PI-21. Effectiveness of Internal Audit	D+	Brief Explanation
(i) Coverage and quality of the internal audit function	D	The internal audit function covers all MDAs, executive agencies and public bodies. Operations however are restricted by staffing constraints and so in practice the Internal Audit Unit is unable to fulfil effectively its full responsibilities and coverage. Very little audit time is spent on systems audits, and though not possible to verify based upon audit work plans, an officer in charge of Internal Audit estimated the amount of time to be no more than 10%.
(ii) Frequency and distribution of reports	B	The reports are issued regularly for most audited entities and distributed to the respective Line Ministry, the Ministry of Finance with copies to COCA and the Cabinet.
(iii) Extent of management response to internal audit findings	C	The management response to audit queries in general appears to be varied as Officials report. The head of the public entity is responsible for carrying out the auditor's recommended corrective measures. No Audit Committees have been set up to follow up on audit findings and obtain management responses and actions.

3.4 ACCOUNTING, RECORDING AND REPORTING

3.4.1 Timeliness and Regularity of Accounts Reconciliation

3.4.1.1 The Central Bank has 20 Branches which have responsibility for all 22 Governorates. It maintains the Consolidated Fund as a treasury single account which assigns a single main account for each Line Ministry but with a sub-account structure that reflects the chapter and subchapter structure of the budget. The CBY monitors and reconciles the Consolidated Fund account on a daily basis and so is in a position to determine the current status of bank balances for the entire Government on a next-day basis. The CBY submits fully reconciled Monthly Budget Release Returns to the Ministry of Finance within 10 days of the close of the month. There are a few Central Government Accounts, including the Special Accounts held by some Line Ministries (less than 1% of expenditure – see PI-7) and certain Government accounts held off shore (e.g. Tokyo Mitsubishi Bank for Japan Aid) which are not reconciled each month within four weeks of the close of the month.

3.4.1.2 There are appears to be a widespread notion that the CBY carries out expenditure management and accounting functions for the Ministry of Finance. This is not quite accurate. A more accurate characterisation would be that the CBY carries out a very effective budget release control function. It is based on the achievement of an all encompassing treasury single account that permits the CBY to establish a consolidated cash balance whose accuracy is ensured through daily bank balance reconciliations. Further, the CBY presents monthly budget release reports that accurately and in a timely manner report on the payments (withdrawals) made by each Line Ministry.

3.4.1.3 However, the full potential of this powerful facility is not achieved in the execution of the budget because the Ministry of Finance does not base its budget releases on cash flow projections to ensure that not only are budget releases predictable (based on the six-monthly general warrants that instruct the CBY on the cash withdrawal ceilings for each Line Ministry) but that they match expenditures to actual needs and cash availability in order to minimize the need to resort to short term borrowing. It appears the mechanistic approach of assigning 1/6th of the appropriation each month takes away any flexibility for effective cash management. This seems to have led to the Ministry of Finance ignoring its responsibility for fiscal management and the CBY obscuring the lines between monetary and fiscal considerations in the issuance of domestic debt instruments.

3.4.1.4 The General Accounts Directorate of the Ministry of Finance is responsible for the consolidation of the final accounts submitted by the Line Ministries. In practice it converts all suspense account entries to expenditure at the close of each year and so achieves a simple direct and literal reconciliation with the CBY figures. This practice, while somewhat unconventional[34], also includes the reporting of temporary advances and other suspense account balances allows a complete financial picture if even distorting the expenditure profile. Suspense accounts are monitored and tracked during the year based upon monthly and quarterly submissions of budget execution reports submitted by the Line Ministries. The Regulation Department is responsible for monitoring and reconciling suspense accounts on a quarterly basis; however some accounts have un-cleared balances brought forward.

Indicator	Score	Brief Explanation
PI-22 Timeliness and regularity of accounts reconciliation (M2)	**B**	
(i)Regularity of Bank reconciliations	B	It maintains the Consolidated Fund as a treasury single account which assigns a single main account for each Line Ministry but with a sub-account structure that reflects the chapter and subchapter structure of the budget. The CBY monitors and reconciles the Consolidated Fund account on a daily basis. The CBY provides a reconciled monthly disbursement report to the MoF within 10 days of the end of the month. However as already noted in PI-7 and D3 there are a few special accounts and project accounts that remain outside this arrangement.
(ii) Regularity of reconciliation and clearance of suspense accounts and advances	B	Suspense accounts are monitored and reconciled on a quarterly basis based upon monthly and quarterly submissions of budget execution reports submitted by the Line Ministries. However, some accounts have uncleared balances brought forward.

3.4.2 Availability of Information on Resources Received by Service Delivery Units

3.4.2.1 A Basic Education Tracking Survey Report, sponsored by the World Bank, was published in December 2006. The study identifies ghost workers and teacher absenteeism as two of the challenges facing the delivery of services at the point of the front-line delivery service units. One recent survey carried out with support from DFID on the health sector was carried out in 2005 that demonstrated the level of resource actually received by health facilities across the country. In 2006 a Public Expenditure Review (PER), sponsored by USAID, was carried out for the health sector for the period 1999 to 2003. The PER included an assessment of the investment resources that were actually received by the primary health clinics.

Indicator	Score	Brief Explanation
PI-23 Availability of information on resources received by service delivery units	**B**	A survey was undertaken in 2006 on Health and 2005 on Basic Education that reviewed the actual resources received by health and education facilities across the country. A PER carried out in 2006 referenced the period 1999 to 2003.

[34] There is double counting of entries since the supplemental entries are transferred to expenditure as well as reported as temporary advances and credits.

3.4.3 Quality and Timeliness of in-year Budget Reports

3.4.3.1 The Budget Implementation reporting system requires the Line Ministries to submit fully reconciled Monthly Budget Execution Returns by the 15^{th} of each month. The Line Ministries submit the monthly Budget Execution Reports emanating out of the Consolidated Fund transactions to the General Accounting Directorate within the Ministry of Finance using Form 57 for the Monthly Budget Execution Returns and Form 58 for the Quarterly Submissions. In practice the actual submittals occur much later. An analysis for 2006 indicates an average submittal delay of 10 weeks beyond the required 15 day time allotment for Monthly Budget Execution Reports, and a 9 week delay for quarterly reports. The monthly statements of expenditure are reported in the same classifications as the budget is presented, receipts and payments, and a summary of balances held in imprest accounts. The General Accounts Division reviews the Monthly Expenditure Returns and reconciles them against CBY Monthly Budget Release Reports on a monthly basis. The Monthly Expenditure Returns format is fully consistent with the budget format and facilitates expenditure statements by budget head and economic classification. It does not provide any information on commitments (authorised expenditure).

3.4.3.2 There are boxes in the reporting format for arrears; however some of the actual submissions that were reviewed included no actual expenditure arrears data. Further, the Ministry of Finance does not attempt to consolidate and report on the national aggregate of arrears. COCA reports that the amount of arrears is substantial. Suspense accounts are monitored and reconciled on a quarterly basis based upon monthly and quarterly submissions of budget execution reports of Line Ministries. However, some accounts have uncleared balances brought forward. Inspection of the actual expenditure reports showed inconsistencies between detail accounts and summary figures. COCA reported that they were cognizant of accuracy difficulties with the financial statements. Thus, although there are some concerns about accuracy, but data issues are generally highlighted in reports and do not compromise overall consistency/ usefulness.

Indicator	Score	Brief Explanation
PI-24 Quality and Timeliness of in-year budget reports	**D+**	
(i)Scope of reports in terms of coverage and compatibility with budget estimates	C	The Monthly Expenditure Returns allow a direct comparison of budget implementation to the original budget. Only expenditures are covered, not commitments. Information included covers all of the budget estimates items.
(ii) Timeliness of the issue of reports	D	Reports are prepared monthly and quarterly and on average are submitted after more than 8 weeks after the close of each month.
(iii) Quality of information	B	Ministry of Finance does not attempt to consolidate and report on the national aggregate of arrears. COCA reports that the amount of arrears is substantial. There are some inconsistencies between detail accounts and summary figures. Although there are some concerns about accuracy, but data issues do not compromise overall consistency and usefulness.

3.4.4 Quality and Timeliness of Annual Financial Statements

3.4.4.1 Under the cash accounting system the source document for accounting entries is the payment voucher. Entries are dated using the date on the cheque. A single consolidated account held with the CBY is used for making all Government funded payments out of the Treasury. The Ministry of Finance prepares consolidated final accounts annually. Consolidated government accounts are prepared with revenue and expenditure information as well as a table of financial assets and liabilities.

3.4.4.2 The Line Ministries are responsible for preparing the final accounts. The Minister of Finance on the basis of these submissions prepares a single consolidated financial statement for submission to the Cabinet and COCA. The Finance Law states that within six months of the close of the fiscal year the Ministry of Finance shall submit to COCA the consolidated final accounts. In practice, as evidenced by the schedule of submittals of financial statements to COCA presented in Table 3.9, the Finance Ministry has submitted the statement for external audit within 10 months of the close of the fiscal year for all of the years considered for this assessment.

Table 3.9

Schedule of Submission of Financial Statements to COCA

Fiscal Year	2004	2005	2006
Approved by Cabinet	14/09/2004	13/09/2005	10/09/2006
Date of Submission to COCA	27/09/2004	25/09/2005	10/10/2006
Months after Close of Fiscal Year	9 Months	9 Months	10 Months
Date of Submission to Parliament	27/09/2004	25/09/2005	10/10/2006

3.4.4.3 The Government of Yemen employs a cash based accounting system and has adopted a standard set of accounting standards for all public service institutions. Standard and consistent formats have been adopted and are used across all Line Ministries.

Indicator	Score	Brief Explanation
PI-25 Quality and timeliness of annual financial statements	**C+**	
(i) Completeness of the financial statements	B	The Ministry of Finance prepares consolidated final accounts annually. Consolidated government accounts are prepared with revenue and expenditure information as well as a table of financial assets and liabilities. However, the financial statements do not include any expenditure or tax arrears.
(ii) Timeliness of submission of the Financial statements	B	Financial statements are submitted within 10 months of the end of the fiscal year
(iii)Accounting standards used	C	A set of accounting standards developed and financial statements are presented in a consistent format for the years reviewed.

3.5 EXTERNAL SCRUTINY AND AUDIT

3.5.1.1 Both the President and the Office of COCA demonstrate some elements of independence. The President of COCA's position is enshrined in the Financial Law and the External Audit Law No. 39, 1992. By the standards of independence set by INTOSAI for supreme audit institutions there are two areas in which the Auditor General falls short of complete independence. The appointment of the President of COCA is on the authority of the President of the Republic; but is not guaranteed by fixed tenor and may be terminated on the sole decision of the President. The budget estimates for COCA are independent of Ministry of Finance budget negotiations and is approved directly by the President. However, the COCA budget is not charged directly to the Consolidated Fund nor does it constitute a statutory budgetary item. Consequently, actual budget disbursement is subject to the control of the Ministry of Finance. The hiring and termination of COCA staff is solely at the discretion of the President of COCA (subject to labour laws and protections) and so independent of the Ministry of Civil Service and has allowed COCA a fair amount of control over the quality and fit of its staff.

3.5.1.2 An External Audit Bill has been prepared as part of the PFM reform effort being undertaken. It has been submitted to the President for approval. Under this Bill greater independence is proposed for COCA to bring it more in line with INTOSAI standards. Specific proposals include the appointment based upon nomination by the President and approval by parliaments and fixing of the term of tenure of the President of COCA to no more than two terms each for five years with the only possibility for early termination being court established mental incompetence. The COCA budget would by direct charge to the Consolidated Fund to ensure full budgetary independence.

3.5.1.3 COCA, in accordance with law has full and complete jurisdiction over all public entities including local authorities and public corporations for which the Government has more than a 50% ownership stake. It has jurisdiction over all security ministries, departments and agencies (under some security clearance controls) and is not restricted as to what, whom or where it can report its findings. In addition to it legal requirement to submit audit reports to the parliament, COCA has recently initiated a newsletter and a website in which it intends to disseminate it findings to a wider audience. COCA comprises 1,800 staff of which approximately 60% are assigned to the 22 Governorates. There are approximately 800 staff that are designated technical. Of these approximately 80% possess an accounting or auditing accreditation. There are also a number of legal and administrative staff. In addition COCA sometimes contracts out to specialists such as engineers, pharmacists, and computer specialists to assist in the case of specialized audits. With staffing limitations, not all central government entities, public enterprises and local authorities are audited every year. The annual audit work programme suggests that approximately 80% (by expenditure volume) are audited annually. The sample selection adopts a risk based approach which includes such factors as volume, capacity of the respective internal audit units, type of activity (such as project expenditure) and responsiveness to previous audit findings. The scope of audit performed pertains to financial audits and compliance audits. In very limited cases performance and value-for-money audits have been undertaken. Specifically a manual for performance audits has been prepared and such audits carried out for the Roads Authority Funds, the Universities and the Electricity Corporation. Auditors work under the guidance of an External Audit Manual which indicate and prioritise risk factors as a basis for guiding audit focus. While not yet fully achieved, there are efforts to comply with INTOSAI standards and the reform efforts being undertaken are being guided by the INTOSAI standards.

3.5.1.4 In accordance with the Finance Law, the audited financial statements have to be submitted to the Parliament within three months of receiving the final consolidated appropriations accounts from the Ministry of Finance, which in turn should be submitted to COCA within 6 months of the end of the fiscal year – January 1st to December 31st. The audited financial statements and audit reports are submitted to Parliament and to the President of the Republic. The financial statements have to be submitted to the Auditor General by 31st July of the financial year ending 31st March.

Table 3.10

Statistics on Annual Financial Statements Submissions to COCA and their Certification by COCA for 2004; 2005; 2006

Fiscal Year	2004	2005	2006
Approved by Cabinet	14/09/2004	13/09/2005	10/09/2006
Financial Statements			
Date of Submission to COCA	27/09/2004	25/09/2005	10/10/2006
Months after Close of Fiscal Year	9 Months	9 Months	10 Months
Date of Submission by COCA to Parliament	30/12/2004	31/12/2005	25/12/2006
Months after receiving Financial Statements	3 Months	3 Months	2 Months
Audit Reports			
Date of Submission by COCA to Parliament	January	January	February
Months after close of fiscal year	1 Month	1 Month	2 Months

3.5.1.5 When the external auditor prepares an audit report the findings are discussed and agreed by the auditor with the head of the Public Entity. Within thirty days after the completion of the audit, COCA submits a formal letter to the Head of the Procuring Entity outlining the findings and recommending corrective measures to be carried out. The Head of the Procuring Entity is responsible and held accountable for instituting the corrective measures. In accordance with the Audit Law, the Head of the Procuring Entity is allowed 30 days within which to respond indicating agreement with the findings and acceptance of the responsibility to institute the audit recommendations. Where Procuring Entities fail to respond, COCA meets the Head of the

Procuring Entity to investigate any reasons for not responding. Minutes of these meetings are kept and both parties sign. The audit work plans include as the first item of business to follow upon the previous year's audit recommendations. For corrective measures that are persistently ignored, the individual auditor reports this to COCA and the Head of Procuring Entity is called in to a meeting. Where the problem persists the issue is forwarded to the President. Officials of COCA indicate that this has been very effective in ensuring the complete and timely implementation of COCA recommended corrective measures.

Indicator	Score	Brief Explanation
PI-26. Scope, nature and follow-up of external audit	**B+**	
(i) Scope/nature of audit performed (incl. adherence to auditing standards)	B	Most central government entities are audited annually. It is estimated that about 80% of expenditure is audited annually. The audits cover mainly financial statements and compliance audit including revenues and expenditure. Value-for-money and performance audits have been performed to a limited extent. The audits, guided by an audit manual, focus on significant and systemic issues. There are efforts to conform to the INTOSAI standards.
(ii) Timeliness of submission of audit reports to the legislature	A	The COCA audit report is submitted within two months of the close of the fiscal year the Parliament every year. The certification of the annual financial statements is submitted by the end of December each year and no more than 3 months after the receipt of the consolidated financial statements.
(iii) Evidence of follow-up on audit recommendations	A	There a clear and actively followed procedure for follow-up on the audit recommendations. The procedures are time-bound and are generally adhered to. The implementation of corrective measures is followed up through successive audits

3.5.2 Legislative Scrutiny of the Annual Budget Law

3.5.2.1 The parliament is unicameral. There are 301 deputies of the House of Representatives are elected by direct popular vote every six years. The annual budget legislative review, in practice, usually begins with the tabling before parliament of the appropriations bill along with the draft estimates between the middle and the end of October. A budget address date is pre-announced and given typically two weeks to three weeks after the tabling of the appropriations bill in order to allow time for each member to carefully review the details of the revenue and expenditure estimates. The budget speech usually occurs the second or third week in October. Debates primarily focus on the detailed revenue and expenditure estimates even though there is some discussion of the Government's fiscal policy framework after review by the sub-committee on Fiscal Policy. The medium term fiscal framework is not yet an element of the budgetary debate.

3.5.2.2 The Budget is reviewed and discussed in detail by the Budget Committee made up of approximately 55 members. The Budget Committee has available to it a technical support staff made up of approximately 50 professionals including economists and accountants. The membership is made up of the members of the finance committee, heads of the political parties, and heads of other parliamentary committees. The Budget Committee divides up into six Sub-committees. These are the Fiscal Policies Sub-Committee, the Local Authorities Sub-Committee, the Central Accounting Sub-Committee, the Special Funds Sub-Committee, the Public Corporations Sub-Committee, and the Financial Sub-Committee.

3.5.2.3 The Budget Committee is given 30 days within which to complete its review and prepare its recommendations. During such consideration the Minister of Finance and any of the Line Ministers may be called to defend their budgets. After consideration, the Budget Committee prepares its recommendations along with notes of all of the meetings with public officials that were held. The general parliament is given three days to review the recommendations and then subject it to debate. The budgetary debate is cast live on television and radio and can take up to two weeks. The budget, along with the parliamentary recommendations, is approved by the last week of December and enacted into law by signature of the President before December 31st. Consequently the entire legislative review of the budget typically takes between ten and twelve weeks and allows for passing of the budget to occur before the start of the financial year. The Minister of Finance signs a written undertaking that the Parliaments recommendations shall be implemented and is circulated as an attachment to the appropriations law. The constitution does not permit the parliament to adjust budgetary figures directly. It may either reject or approve the Government's proposed budget.

3.5.2.4 According to some members, in practice parliamentary recommendations are not fully implemented. It is reported that a number of Line Ministries complain to the parliament that recommendations are not carried out. The Ministry of Finance states that these budgetary adjustments are reflected in the general warrant that allocates budget releases. Line Ministry officials stated that they were unaware of such adjustments. The apparently contradictory statements may be a matter of lack of transparency. The Budget Documents do not include a column of approved budget estimates arrived at by the Ministry of Finance after consideration of the financial impact of the parliamentary recommendations that can serve as the budgetary guide to Line Ministries for their implementation, and also communicate to all stakeholders the actual budget to be implemented. Such an arrangement would ensure that the parliamentary policy inputs were reflected in the budget and would enhance the predictability of budget execution since the guiding budget instrument would be the approved budget (proposed plus recommendations) rather than the current arrangements that only reflects the proposed budget.

3.5.2.5 The Supplementary Budget Estimates presented by the Minister of Finance and voted by typically once a year. The Finance Law provides clear guidelines on the passing of Supplemental Budgets. In particular the law requires that any supplementary budget expenditure be approved prior to expenditure. The procedures are similar to that described above for the passage of the budget into law. The Minister of Finance submits a Schedule of Supplementary Estimates to the house which details the additional expenditure and source of funding broken down by budget head and programme. In practice the supplemental budget submission serves to justify expenditure that has already occurred. Parliamentary members state that the Ministry of Finance in the last five years has justified such practice on the basis of emergencies such as the recent implementation of wage increases. This is in contrast to the Civil Service Ministry statements that such wage increases were foreseen and incorporated in to the original budget estimates.

Indicator	Score	Brief Explanation
PI-27 Legislative Scrutiny of the Annual Budget Law	**C+**	
(i)Scope of the legislature's scrutiny	B	The Legislature mainly reviews the, details of expenditure and revenues, and only addresses fiscal policy as the context in which the detailed expenditure and revenues are discussed.
(ii)Extent to which the legislature's procedures are well-established and respected	C	The procedures for budget review are well established and the practices of the House and the Senate are well enshrined. The Budget Committee, a sub-committee of parliament, is itself supported by 6 sub- committees and 50 technical support staff. The Budget Documents do not include a column of approved budget estimates arrived at by the Ministry of Finance after consideration of the financial impact of the parliamentary recommendations. The legislature's procedures for budget review are therefore well established but not fully respected.
(iii)Adequacy of time for the legislature to provide a response to budget proposals both the	A	The Legislature has slightly over two months in total to review the budget proposals.

Indicator	Score	Brief Explanation
detailed estimates and, where applicable, for proposals on macro-fiscal aggregates earlier in the budget preparation cycle (time allowed in practice for all stages combined)		
(iv)Rules for in-year Amendments to the budget without Ex-ante approval by the legislature.	C	Rules for the in-year amendments exist but in practice there are extensive administrative re-allocations as well as expansions without ex-ante approval by the parliament.

3.5.3 Legislative Scrutiny of External Audit Reports

3.5.3.1 COCA submits its annual audit report by February of each year (see PI-26) and the financial statements by November. Further, quarterly audit reports are submitted to the Secretary General of the parliament. This allows the House to review both the audit report and the audited financial statements as part of the budget debate. The parliament may use the Audit Report and audited financial statements along with the Budget documents for the debates and when they question the public officials. Any Member of Parliament may address any findings of any audit reports by calling the head of the public entity.

3.5.3.2 There is a Committee for the Review of Audit Reports and Financial Accounts made up of members of the Financial Committee, the heads of political parties and the heads of other Committees. This committee is currently reviewing the 2005 financial accounts and have prepared a 350 page report in three volumes which includes recommendations to prosecute the cases of corruption. Concerned officials were called in to discuss the findings. In contrast, for the years 2004, 2005 and 2006 there were no hearings held or follow up on the audit reports.

Indicator	Score	Brief Explanation
PI-28. Legislative scrutiny of external audit reports (M1)	**D+**	
(i) Timeliness of examination of audit reports by legislature (for reports received with the last three years)	D	The Public Accounts Committee (Financial Committee) is currently reviewing the audit report for 2005 but did not review the audit report for 2004 and has not yet reviewed the audit report for 2006.
(ii) Extent of hearings on key findings undertaken by legislature	C▲	There appear to have been only ad hoc hearings on the key findings of the audit reports carried out in 2004, 2005 and 2006. However, in 2007 a far more systematic and comprehensive approach is being employed.
(iii) Issuance of recommended actions by the legislature and implementation by the executive	B	No actions were recommended by the Parliament in the years 2004, 2005 and 2006. However, in 2007, the Parliament has issued a 350-page report recommending actions on the basis of COCA's Annual Audit Report for 2005 accounts. Some of these recommendations have been also acted upon by the government.

3.6 DONOR PRACTICES

3.6.1 Predictability of Direct Budget Support

3.6.1.1 The Netherlands is the only donor currently providing targeted budget support to Yemen. In 2005 and 2006 Yemen was provided targeted budget support[35] in the water sector. The total amount committed in 2005 was 4 Million Euros, two million of which was disbursed upon signature of the financing agreement in the third quarter, and a further one million was disbursed in November of 2006 corresponding to a 75% disbursement ratio. A total of 3.6 Million Euro

[35] Targeted budget support refers to budget support channelled through a special account and targeting specific application within the budget and subject to all of the government budget systems, controls and reporting. It might be described as direct budget support with conditionalities attached to ensure full funding of particular budget lines.

was forecast and committed in the fourth quarter of 2006; all of which was disbursed in the same quarter corresponding to a 100% disbursement ratio. There are plans to continue to provide budget support in the water sector through till 2009. In the case of the 2005 direct budget support commitment weighted disbursement delay[36] was 75% and for 2006 it was 0%.

3.6.1.2 As regards to the schedule of agreements in neither of the two years in which direct budget support was provided were the financing agreements entered into prior to or at the beginning of the fiscal year in which they were disbursed.

Table 3.11
Direct Budget Support for the Period 2004 to 2006

	2005				2006			
Direct Budget Support	**Qtr 1**	**Qtr2**	**Qtr 3**	**Qtr 4**	**Qtr 1**	**Qtr2**	**Qtr 3**	**Qtr 4**
Forecast			4,000,000					
Disbursement				2,000,000				1,000,000
Forecast								3,600,000
Disbursement								3,600,000

All amounts are in Euros

3.6.2 Financial information provided by Donors for Budgeting and Reporting on Project and Program Aid

3.6.2.1 In recent years, the major donors providing project and programme aid in Yemen have been the IDA, the Arabic Fund for Development, the UN Agencies, Japan, the Saudi Fund, USAID, EU, and Netherlands. Both DFID and USAID foresee dramatic increases in their aid activities over the coming years. A number of Donors indicate that there has not been a standardised utilization of terms in the communication to the Government on annual budget estimates of aid funded projects and programmes. There is inconsistency in the proxies used for budget estimates including pledges, multi year versus single year commitments, and available funding. A number of Donors indicate disbursement estimates are not informed by fully developed procurement plans and absorptive capacities pertaining to realistic schedules of project implementation. The lack of a standard for definitions has left the Ministry of Planning in the position of largely guessing what the budget estimates for donor funded investment is likely to be, and responding to that by adopting an extremely conservative posture[37].

3.6.2.2 In turn, the Government provides no clear guidelines as to budget estimate submissions or a time table or format or budgetary classification of cost estimates and work plans. The Yemen Budget is based upon an economic and administrative classification and does not yet reflect a functional or programmatic classification. Many Donors submit estimates as well as financial reporting on a programmatic basis. The Ministry of Planning reports that it has had to employ simple mapping tools to translate Donor Reports into the national budget. The Yemen budgetary process follows a very strict schedule of preparation (see PI-11) and so there should be an opportunity to align Donor budgets with that cycle. Project design and financial forecasts are based mainly on donors own financial years – only some of which correspond to the Government financial calendar. Project implementation formats are not consistent across all donors. Currently for many Donors there is no attempt to synchronise the project budgetary schedules with the Government's fiscal year. A number of Donors pointed out the difficulties faced in doing so, given the strict restrictions about communicating aid flows prior to their own national budget approvals. However, a number also pointed out that their intended moves to a

[36] The weighted disbursement delay is determined as the percent of funds delayed multiplied by the number of quarters of delay, corresponding to a 40% measure of weighted disbursement delay for each year of delay of the full amount of direct budget support funds.

[37] Ministry of Planning Officials have illustrated the point by describing how after a Donor's conference in London earlier this year the estimate for the investment budget for 2008 was originally set at 853 Billion Yemeni Riyals based upon the pledges made, and after more careful assessments and the realization that the pledge figures included existing commitments and reflected very little new funding have had to revise their budget estimates for 2008 downwards to a little over 50% of the original estimate. Even where commitment figures are used, these can serve as unreliable proxies of actual disbursement. By way of illustration in 2004 DFID disbursed 74% of its commitments and in 2005 it disbursed 91% of its commitments.

multi-year donor aid framework would place them in a better position to provide improved budget estimates to the Government. At the present, a number of the major Donors including the EU, USAID, Netherlands, Japan and DFID are among Donors unable to provide budget estimates for the coming fiscal year three months prior the start of the fiscal year given their own national budget cycles.

3.6.2.3 With respect to the financial reporting there are a wide variety of arrangements. Some Donors provide quarterly reports, others semi-annual and still others provide only annual financial reports. There appears to be some lack of clarity as to the roles and responsibilities of Donors versus the Government with respect to financial reporting. Given that many projects employ independent management units (PMUs, PIUs, PCUs etc.) often located within the Line Ministry and they are responsible for preparing project implementation reports that include expenditure statements with copies circulated to Government, it is presumed that this serves as the full requirement for financial reporting. As a number of Donors indicated, sometimes they carried out expenditure directly on behalf of the project which the project management unit would not necessarily have information about[38]. Further, the financial reports were often subject to audit by the Donors and might adjust financial reports to reflect ineligible expenditure. The upshot of this is that often Government does not receive the full and complete expenditure picture on projects to properly report on project expenditure within the national appropriation accounts. In the case where the Donors manage expenditure directly such as is the case with USAID and Japan, the risk of the Government not receiving complete expenditure data remains substantial. The timing of project implementation reports is also an important consideration. By law, Line Ministries must submit their final financial statements three months after the close of the fiscal year to the Ministry of Finance for consolidation into the national appropriations accounts. A number of Donors indicated that they did not provide final statements before that date. The inescapable conclusion to be drawn is that the national appropriations accounts are based upon incomplete financial data.

3.6.2.4 For loan funded projects that deposit the amounts within the CBY the monitoring of disbursements through DMFAS provides a basis for the timely monitoring of project disbursements. While such disbursements do not necessarily equate to actual project expenditure they provide for timely estimates. These external loans, including IDA and Arabic Fund for Development, represent for more than 50% of the project disbursements for projects included in the budget.

3.6.3 Proportion of aid that is managed by use of national procedures

3.6.3.1 While the project funds are often placed in Government accounts held in the Central Bank there are a number of Donors including Japan, the United States and Germany that do not deposit AID funds in the Central Bank. This diminishes the capacity of the Government to monitor actual disbursements and so closely monitor project implementation. For Donors that do not deposit funds in the Central Bank they voiced concerns about the funds not being diverted to other applications. Japan and the United States indicated that all disbursements were subject to Government approval and in the case of Japan that the Government received copies of bank statements (usually Tokyo Mitsubishi Bank) and so felt there remained an opportunity for Government to monitor disbursements closely. By way of the use of Government systems, the procurement, financial management and reporting, accounting and external audit are rarely carried with respect to national procedures and systems. As indicated in Table 3.12, in most cases they adopt the procedures of the Donor. This diverts capacity away from managing the national systems and where strong and synchronised coordination is lacking between the Donor systems and the Government systems can contribute to a weakening of the Government budgeting and financial reporting systems. USAID indicates instances where projects were not reflected in the Government Budget which occurred as a result of donor support forged directly with Line Ministries that was not supported by a formal project agreement signed by the

[38] A number of Donors interviewed sated that this was especially the case for Technical Assistance contracts where they were concerned that greater transparency with respect to the rates that International Consultants were paid could lead to complications in implementing projects.

Ministry of Planning and International Cooperation, and hence there was no opportunity for the Government record or track project implementation within it national budgetary and financial reporting systems. The independent Donor systems used for managing project funds being applied in Yemen, while possibly well justified on the basis of a political or governance rationale, nevertheless have contributed to undermining the accuracy of budget estimates and introducing substantial inaccuracies in financial reporting.

3.6.3.2 The methodology used in determining the proportion of donor funds that are managed through Government systems is based on obtaining information from the donors by programme types on whether they use each of the four categories of Government procedures listed in Table 3.12. A percentage of usage of the government system is thus calculated (using a weighting factor of 0.25 for each of the four factors) and applied to the disbursements recorded for 2004, 2005 and 2006. This calculation provides an aggregate proportion of funds being disbursed, utilised and reported on using government procedures (see Table 3.12). As demonstrated in the table, considerably less than 50% of aid funds to the central government are managed through national procedures.

Table 3.12
Use of Government Systems for the Period 2004 to 2006

	Use of Government Systems					2004	2005	2006	2004	2005	2006
Donor	**Procurement**	**Payment/Accounting**	**Financial Reporting**	**Auditing**	**Type of Support**	**USD**	**USD**	**USD**	**% Use of Systems**		
EU	No	No	No	No	Programme/Project	15	31	21			
Netherlands	**Yes**	**Yes**	**Yes**	**Yes**	Targeted Budget	-	5	5		1.2%	1.1%
	No	No	No	No	Programme/Project	24	21	23			
DFID	No	No	No	No	Programme/Project	13	22	-			
UNDP	No	No	No	No	Programme/Project	7	8	13	2.2%	2.1%	2.9%
UNDP (Nex)	**Yes**	**Yes**	**Yes**	**Yes**	Programme/Project	3	4	5			
USAID- USDA	**Yes**	**Yes**	**Yes**	**Yes**	Programme/Project	26	-	11	8.1%		2.3%
USAID-Projects	No	No	No	No	Programme/Project	11	15	8			
Japan	No	No	No	No	Programme/Project	33	18	26			
IDA	No	No	No	**Yes**	Programme/Project	92	129	160	7.2%	7.9%	8.9%
IFAD	No	No	No	No	Programme/Project	6	5	1			
OPEC Fund	No	No	No	No	Programme/Project	5	5	7			
Arabic Fund for Development	No	No	No	No	Programme/Project	35	64	103			
The Saudi Fund	No	No	No	No	Programme/Project	23	20	24			
Islamic Fund for Development	No	No	No	No	Programme/Project	17	15	14			
Spanish Kingdom - Governmental	No	No	No	No	Programme/Project	3	0	-			
Spanish Fund - Commercial	No	No	No	No	Programme/Project	1	0	-			
China Developmental	No	No	No	No	Programme/Project	9	19	22			
Korea	No	No	No	No	Programme/Project	-	23	7			
Total						**323**	**407**	**450**	17.5%	11.2%	15.2%

Indicator	Score	Brief Explanation
D-1 Predictability of Direct Budget Support	**D**	
(i) Annual deviation of actual budget support from the forecast provided by the donor agencies at least six weeks prior to the government submitting its budget proposals to the legislature (or equivalent approving body).	*D*	No timely and comprehensive forecast was provided by the donor agency providing direct budget support in either of the two years in which direct budget support was provided.

Indicator	Score	Brief Explanation
(ii) In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates	*D*	The actual disbursement delays were 75% and 0% for 2005 and 2006 respectively, however in both years the agreements were made after the second quarter of the fiscal year in which they were disbursed..
D-2 Financial information provided by donors for budgeting and reporting on project and program aid (M1)	**D+**	
(i) Completeness and timeliness of budget estimates by donors for project support.	D	Many major Donors do not adhere to the Yemen budget cycle. There is the expectation as a number of major donors move to multi-year frameworks that they will be better able to align their budget estimates submissions with the Government's budget cycle.
(ii) Frequency and coverage of reporting by donors on actual donor flows for project support.	C	Not all Donors provide quarterly reports on actual disbursements to the Government but for those who deposit project funds with the CBY, tracking using DMFAS facilitates the timely tracking of disbursements and thus indirectly project implementation. . Many of the PMUs also report on project implementation quarterly and typically do so within 45 days of the end of the quarter. There are a number of difficulties that remain as to the accuracy as well as completeness of financial reports. These external loans, including IDA and Arabic Fund for Development, represent for more than 50% of the project disbursements for projects included in the budget.
D-3 Proportion of aid that is managed by use of national procedures	**D**	
(i) Overall proportion of aid funds to central government that are managed through national procedures.	D	Although many of the major projects use bank accounts monitored and located in the CBY and project management units sometimes directly located within the Line Ministries the systems employed for audit, reporting and accounting, and procurement for the most part are done as per the systems of the Development Partners. Less than 50% of aid funds are procured, accounted for, reported on or audited by national procedures and financial management systems.

4. GOVERNMENT REFORM PROCESS

4.1 GENERAL DESCRIPTION OF RECENT AND ON-GOING REFORMS

4.1.1.1 The Government of Yemen has embarked upon a programme of Public Finance Management Reform as part of a broader National Reform Agenda[39]. In early 2006, Yemen embarked on a set of ambitious and interconnected reform measures named the National Reform Agenda (NRA), with the support and coordination of international development partners. The President and Government of Yemen have defined combating corruption as the foremost priority of their reform strategy. Among the recent milestones achieved have been:

- The National Anti-Corruption Awareness Campaign an intensive media campaign carried out over two months in 2006;
- The enactment of the Financial Disclosure Law which requires the highest accountable officers for public finance management including the president to file a financial disclosure statement;
- The adoption of a Procurement Manual and Standard Bidding Documents developed by international procurement consultants and the implementation of a procurement training programme for 80 procurement officers;
- The adoption of an Anti-Corruption law which creates the Anti-Corruption Commission which was passed in 2007;
- The implementation of a Biometric ID system aimed at eliminating “double dippers” and ghost workers from Government payrolls;
- A presidential campaign commitment to enhance the independence of the Central Organisation for Control and Audit (COCA);
- Agreeing to subject itself to the Extractive Industries Transparency Initiative (EITI) reviews; and
- The adoption of a Public Finance Management Reform Strategy inaugurated in May 2006. A PFM Reform Action Plan and Partnership Agreement were signed between the Government and a number of participating Donors[40] to support the implementation of the reform strategy.

4.1.1.2 The Public Finance Management Reform Strategy was developed with assistance from DFID, adopted and approved by Cabinet Resolution No. 253 on August 9, 2005. The strategy incorporates six prime components. These are to: improve the level of priority setting and basis for decision-making; improve budget execution; develop public finance management information systems; enhance control and financial accountability; improve the system of bidding and procurement; and improve capacity and skills of public finance staff.

4.1.1.3 The Government with support from UNDP has undertaken a two and a quarter year project for the Implementation of the Public Financial Management Reform Action Plan. The project is supported under a pooled funding mechanism with participation from GTZ, UNDP, DFID and the Netherlands: demonstrating the will to make Donor Coordination a reality in Yemen. The project amount is $3.6 Million. Its objectives are coincident with the PFM Reform Strategy; however the project does not specify measurable time bound targets, nor any reviewable milestones. There is no distinction made between pilot activities, roll out activities be it to just the Line Ministry Headquarters or to all Spending Units within the 22 Governorates. There are

[39] In early 2006, Yemen embarked on a set of ambitious and interconnected reform measures named the National Reform Agenda (NRA), with the support and coordination of international development partners. The overall objective of this agenda was improving Yemen's investment climate and strengthening democratic institutions. This strong commitment to adopting far-reaching political, economic and institutional reforms stems from a clear understanding on the part of the GoY that these reform measures are vital to development.

[40] The signatories of the Partnership Agreement between the Government of Yemen and the Donor Community on Public Financial Management Reform include the United Kingdom, the United States, Netherlands, Germany, UNDP and the World Bank. The agreement is open to additional Donors subject to the agreement of the partners.

no activity linkages identified nor any institutional arrangements proposed to coordinate the PFM Reform Activities. Further there is no specific reform activity sequencing tables, or any platforms defined to guide the initial focus of reform. The costing are partial in that they provide no indication of the recurrent expenditure implications and so do not assure sustainability of the reforms. Further, it would appear that many of the activities are grossly underestimated and leave a skewed perception of what the requirements are for implementing such activities[41].

4.1.1.4 The Partnership Agreement within the broader PFM reform context identifies four areas of special importance. These are: improving the transparency of the budget; strengthening the accountability institutions with a special focus on COCA; enabling the Government to set policy priorities and using the budget process to deliver them efficiently and effectively; and achieving improved delivery service at both the national and the sub-national levels. While there is clearly overlap between the PFM reform objectives outlined in the DPPR, the PFM Action Plan and the Partnership Agreement, they are not identical. While the National Development Framework (DPPR) identifies a Civil Service Modernisation Strategy, it does not specify the PFM Reform Strategy, nor does it outline its objectives. The Partnership Agreement introduces improved transparency and efficiency in the delivery of services that are not included in the PFM Reform Strategy.

4.1.1.5 The PFM reform programme adopted by Yemen has been informed by a number of studies carried out by the World Bank and the IMF including a Country Financial and Accountability Assessment (2004), and a Country Procurement Assessment Report (2003). The Public Finance Management Reform Programme is comprehensive and contains many elements of a sound PFM Reform programme. It includes a list of dated milestones but is not clear to distinguish activity start as well as end dates, and whether pilot programs are to be employed or not. Further, the reform activities outlined in the PFM Action Plan do not appear to be defined within a single coordinated multi-year expenditure framework with a single coordinated funding framework to ensure that the requisite sequencing and scheduling of reform activities can be appropriately supported. Further the reform activities are not fully costed nor does it ensure the close coordination of PFM reform activities necessary for the management of the activity linkages, the paced roll out of activities throughout the different levels of Government, or the sequencing and pacing of reform activities.

4.1.1.6 There have already been a number of PFM reforms that have recently been implemented, some of which have already shown measurable impact on PFM performance. These include:

- The reform of taxation with the implementation of the self assessment basis for major and medium sized tax payers. The adoption of ASYCUDA ++ for customs processing and the move to ASYCUDA World being supported by USAID;
- The enactment of a number of laws including the Anti-Corruption Law, the Tender Law and the Local Authorities Law;
- The adoption of the GFS/COFOG budget classification standard which will see functional budget classification by the 2009 budget submission;
- The cleaning up of the personnel rolls and the introduction of a biometric identification system. This is part of the Public Service Modernisation Project, managed by the Civil Service Ministry and supported by the World Bank and initiated in 1998; and
- The testing[42] and piloting of an integrated financial management system (AFMIS) in four ministries, namely the Ministries of Finance, Education, Health and Public Works. The AFMIS project constitutes the second main component of the Public Service Modernisation Project and is managed by the Ministry of Finance. The piloting has incorporated training

[41] For example it estimates the cost of establishing a computerised PFM information system, establishing a user friendly financial information system, and the rolling out of AFMIS to presumably 34 Ministries and 303 Local Authorities (Network financial reporting for all central and local budget units) including the cost of training, implementation, hardware and software to be $344,000.

[42] The AFMIS outputs are being tested by KPMG Cairo to ensure accuracy and reliability.

for 500 users responsible for budget preparation, and is expected to train 500 more users responsible for budget execution. Beyond the pilot stage, it is anticipated that the second phase will involve the roll out to all Line Ministry Headquarters and the final stage will see a roll out to all 22 Governorates. While the current configuration is client/server based, it is anticipated that the roll out to the Governorates will be based upon a web enabled version of the AFMIS software, developed by a local software developer.

4.2 INSTITUTIONAL FACTORS AFFECTING REFORM PLANNING AND IMPLEMENTATION

4.2.1.1 The PFM Reform Programme in Yemen has political championship at the very highest levels. The institutional arrangements for implementation of the PFM Reform Programme start with the overall responsibility for implementation being vested in the Ministerial PFM Reform Committee which meets annually and is responsible for the implementation of the strategy and achievement of the desired reform outcomes. The Committee is made up of the Minister and Vice Minister of Finance, the Minister of Planning, the Minister for Civil Service, the Minister for Local Authorities and the Governor of the Central Bank. A PFM Reform Task Force headed by the Deputy Minister of Finance in Charge of Budget has been set up which is responsible for overseeing the implementation of the reforms. There are a number of Technical Committees that have responsibility for specific PFM Reform activities. These are the Committee on Functional Classification, the Committee on the Accounting Manual, the Committee on the Treasury System, the Committee on Cash Management, the Committee on Internal Audit, and the Committee on Institutional Restructuring and Capacity Building

4.2.1.2 Notably, the AFMIS project is not represented within the PFM Reform Task Force which represents a risk as to whether the computerisation effort will reflect the specific requirements of the reformed PFM. The Technical Committees are supposed to report to the Follow-Up Committee on a Quarterly Basis but in practice this is not adhered to diligently. On the other hand there is no representation from COCA or the Internal Audit Unit of the Ministry of Finance on the AFMIS Task Force. This raises questions about whether the level of AFMIS transaction and reporting controls are fully compliant with the PFM requirements. It also suggests that there is little coordination between the AFMIS Project and these audit institutions with respect to the development of effective audit techniques for auditing public finance management implemented on the AFMIS platform.

4.2.1.3 Responsibility for the detailed implementation of each of the reform pillars is delegated to the relevant Ministry to be led by the Accounting Officer. At the present time there has been no clear structure set up to manage PFM Reform within the Ministry of Finance. While components have been defined for the Technical Committees, each currently developing a clear set of activities to be specified in Terms of References, there are still no targeted outputs, fully costed inputs, monitoring indicators and reviewable milestones. The PFM reform programme has not been integrated as a separate programme within the Ministry of Finance budget. A large part of the reason for the absence of these important elements to PFM reform appears to be the rather severe capacity constraints. With limited capacity to address the pressing issues of the day job, it is hardly surprising that no distinct formal structure can be set up and managed to deliver on PFM Reforms. Having said that, the past few years have demonstrated some progress in addressing the first element of sound PFM practice; i.e. the achievement of aggregate fiscal discipline. However it should be noted that most of the reforms have centred upon MoF and Civil Service Ministry activities rather than distributed activities rolled out to all the Line Ministries. For example the PEFA assessment shows the management of expenditure with respect to pro forma cash flows and the institution of effective commitment controls to be weak even with respect to aggregate fiscal discipline and may be a precursor to the challenges of progress through the next steps of PFM Reform that will almost certainly require greater emphasis on reform prioritisation, sequencing and coordination.

4.2.1.4 While the PFM Reform effort has attracted substantial Donor support and at this time there is a very active Donor Harmonization Group specifically for PFM Reform in Yemen, there is evidence that such support would yield even better results if there was closer and stronger alignment with Government reform plans and implementation, and more cognizance of capacity constraints in implementing all of the PFM Reforms simultaneously.

4.2.1.5 The centrality of sound PFM to Public Sector Reform emanates from its fundamental role in facilitating the business of Government across all of its core functions. The achievement of sound PFM serves as the enabler, the necessary condition, for a well functioning public sector. Effective PFM reform requires a holistic and comprehensive perspective. There are many specific functions of public finance management that are inter-linked so that a carefully managed sequencing of reform steps, fully cognizant of the inter-linkages, serves as a pre-requisite for effective PFM reform. Consequently, any reform programme that does not address PFM in a holistic and comprehensive way, but just encompasses a single core element of sound public finance management is unlikely to live up to its full promise. While there are a number of important cross-cutting reform objectives (with respect to public finance management reform) embarked upon it falls short of defining a strategic framework that specifically targets and prioritises the achievement of all three core elements of a sound Public Finance Management (PFM) system and seeks to implement activities in a carefully coordinated and sequenced manner . A sound PFM system should have the capability of providing aggregate fiscal discipline, the strategic allocation of resources, and the efficient delivery of services and value for money. However, it may be necessary to embark on each of these objectives one at a time, looking to consolidate a particular “platform” before fully embarking on the next. The PEFA Assessment suggests that predictability and control remain challenges to Yemen’s PFM. There remain significant losses with payroll management and procurement. Budget preparation would benefit from a stronger bottom up dimension. These areas may require first priority, before focus on a more output approach to budgeting, or a focus on efficiency improvements.

4.2.1.6 The introduction of a single coordinated funding framework supporting a comprehensive and consolidated set of work plans and fully costed estimates developed within a multi-year reform programme expenditure framework, implemented through institutional arrangements that well facilitate the close coordination of reform activity implementation, and monitored through a consolidated programme monitoring and evaluation framework made up of both verifiable milestones and PFM outcomes would allow closer alignment of implementation with the Government’s strategy’s approach and could greatly enhance the impact of PFM reform. Such an approach would more readily facilitate a strengthened approach to donor support of the PFM reforms based upon donor harmonization working with a single pool of reform information.

Appendix 1

Indicator /Dimension	Score	Brief Explanation
PI-1 Aggregate expenditure out-turn compared to original approved budget	**D**	Deviations between approved budget primary expenditure and provisional actual expenditure were: for 2004 =19.8%, 2005 = 44.1% and 2006 = 20.1%.
PI-2 Composition of expenditure out-turn compared to original approved budget.	**C**	The average variances in excess of overall deviations were: 2004 = 13.6%, 2005 = 6.9% and 2006 = 7.4%
PI-3 Aggregate revenue out-turn compared to original approved budget	**A**	Domestic revenue collection exceeded 97% in all three of the last three budget years.
PI-4 Stock and monitoring of expenditure Payment arrears	**<NS>**	
(i) Stock of expenditure payment arrears (as a percentage of actual total expenditure for the corresponding fiscal year) and a recent change in the stock	<NS>	There is no monitoring of arrears being undertaken so the arrears cannot be quantified. There are however indications, including through COCA's audit activities, that suggest that the arrears may be substantial.
(ii) Availability of data for monitoring the stock payment arrears	D	There is no reliable data maintained on the level of arrears available from the past two years.
Indicator	**Score**	**Brief Explanation**
B. Comprehensiveness and Transparency		
PI-5 Classification of the Budget	**C▲**	The budget formulation and execution is based on economic and administrative classification. There have been recent efforts made towards adopting functional classifications within the budget process however budget formulation and execution is not yet based on a functional classification. There is the intention to implement it in the 2009 Budget. At this time there is evidence supported by informal internal documents and the Government Financial Statistics Bulletin that show functional distribution ratio tables.
Indicator	**Score**	**Brief Explanation**
B. Comprehensiveness and Transparency		
PI-6 Comprehensiveness of information included in budget documentation	**A**	Budget documentation fulfils 8 out of 9 benchmarks. The Budget documents are comprehensive but these documents would be made more transparent by including approved budget data even in subsequent budget submittals. Government officials state that parliamentary modifications are taken into consideration at the time of execution. It still raises the question how well budget implementation reflects parliamentary approvals and modifications.
Indicator	**Score**	**Brief Explanation**
PI-7 Extent of Unreported government Operations	**B+**	
(i) level of unreported extra-budgetary expenditure	A	All revenues generated directly by the MDAs are transferred to the Consolidated Fund except for internally generated funds which are deposited in Special Accounts. An assessment of internally generated funds in 2007 suggests that the amounts are insignificant (less than 1%). There is very close oversight of all of the Special Funds which must report regularly to the Ministry of Finance as well as to Parliament

Indicator /Dimension	Score	Brief Explanation
(ii) Income/Expenditure information on donor-funded projects	B	Income/expenditure data of donor funded projects (loan funded) are submitted to the Ministry of Planning as well as the Line Ministry to be included in fiscal reports but there appear to remain issues with timeliness and completeness. Over 50% of the grant funded projects are reported on.

Indicator	Score	Brief Explanation
PI-8 Transparency of Inter-governmental fiscal relations	**A**	
(i) Transparent and objectivity in the horizontal allocation among SN government	A	The central government transfers for recurrent expenditure of the Local Authorities are based upon the same budget procedures as for the Line Ministries and so are transparent and subject to set procedures and rules. While the Public Revenues, also transferred from the Central Government, are subject to horizontal allocation procedures enshrined in law, not all of the factors are currently applied. However, these allocations are rule based. The effect is to make over 90 % of the horizontal allocations transparent and rules based.
(ii)Timeliness of reliable information to SN government on their allocations	A	Local Authorities are provided the budget ceilings at the start of the budget process in May along with the Line Ministries.
(iii) Extent of consolidation of fiscal data for government according to sectoral categories	A	All Local Authorities provide quarterly financial statements to the Ministry of Local Authorities. On an annual basis the Local Authorities submit final accounts that are included in the national appropriations accounts when they are presented to the COCA 9 to 10 months after the close of the Fiscal Year.

Indicator	Score	Brief Explanation
PI-9 Oversight of Aggregate Fiscal Risk	**C+**	
(i)Extent of central government monitoring of AGAs/PEs	C	Law 35, 1991 provides the legal authority for control and oversight to the MoF. The Economic Department within the MoF is dedicated to oversight of the Public Enterprises. Quarterly reports are submitted to the MoFP. MoFP reports to the Parliament annually and present a summarised financial report. The accrual basis along with accounting notes provides a basis for assessing fiscal risk. However, fiscal risk issues like debt service default (with or without guarantees issued by central government); operational losses caused by unfunded quasi-fiscal operations; expenditure payment arrears and unfunded pension obligations; are not being consolidated into a separate report.
(ii) Extent of central government monitoring of SN governments' fiscal position	A	The Local Authorities are monitored by the Ministry of Local Authorities through their annual budget process and through monthly budget implementation reports. They are unable to borrow directly.

Indicator	Score	Brief Explanation
PI-10 Public Access to Fiscal Information	**C**	Currently (2007) the Government has made available a number of fiscal reports available on its reports. This includes the annual budget documentation and year end

		financial statements. Access of budget documentation at the time of submission to parliament and year end financial statements are available to researchers, consultants and journalists. The Government makes available 2 of the listed types of information.

Indicator	Score	Brief Explanation
C(i) Policy-Based Budgeting		
PI-11 Orderliness and participation in the annual budget process (M2)	**A**	
(i)Existence of, and adherence to, a fixed budget calendar	A	The budget process is clearly set out. On the basis of the ceilings provided by MoF and approved by a Cabinet Sub-Committee, the Line Ministries have about 10 weeks to prepare their submissions.
(ii) Guidance on the Preparation of budget submissions.	A	The MoF issues comprehensive and clear budget circulars. The Budget ceilings/circulars for the last three years were approved by a Cabinet Sub Committee before the distribution of the circular to Line Ministries. There is some concern about the level of alignment between budget ceilings and actual requirements. The budget preparation procedure appears to be principally top-down.
(iii) timely budget approval by the legislature	A	The legislature has in the past three years always approved the budget prior to the start of the new fiscal year

Indicator	Score	Brief Explanation
C(i) Policy-Based Budgeting		
PI-12 Multi-year perspective in fiscal planning, expenditure Policy and budgeting	**B**	
(i) multi-year fiscal forecast and functional Allocations	C	Forecasts of fiscal aggregates are prepared for three years, including the budget year. The forecasts are not linked to subsequent budget ceilings.
(ii) scope and frequency of debt sustainability Analysis	A	DSA for external and domestic debt is carried out semi-annually and submitted to the Cabinet.
(iii) existence of costed sector strategies	B	The Public Investment Program (PIP) contains fully costed sector strategy for all sectors. It has investment expenditure estimates but not the recurrent expenditure estimates. The total expenditure in Education, Agriculture, Water, Health and Electricity sectors (which have fully costed sector strategies) was 38.59 % of the total primary expenditure during the year 2007.
(iv) linkages between investment budgets and forward expenditure estimates	C	Most of the important investment decisions are selected after analysis from the Ministry of Planning. The Public Investment Program contains fully costed sector strategies for all sectors regarding investment expenditure. The recurrent cost implications are not directly taken into account. However, Investment Budget and Recurrent Budget are surely linked for Electricity, Agriculture, Water, Health and Education sectors, all of which have fully costed sector strategies. However, outside budget investments like SFD are not linked to the recurrent budget. Thus, a link to the forward expenditure estimates does exist for

Indicator	Score	Brief Explanation
		above mentioned major sectors. Thus, investment decisions related with aforesaid sectors have links (although weak) to their sector strategies and their recurrent cost implications are also included in forward budget estimates for the sector.
PI-13. Transparency of taxpayer obligations and liabilities (M2)	**B**	
(i) Clarity and comprehensiveness of tax liabilities	C	Legislation and procedures for all major taxes exist in the laws and in guidelines. These are clear and comprehensive. The discretionary powers in the case of the Customs Department both for valuations as well as for penalties applied remain substantial. In the case of the taxes on oil producing companies there is lack of clarity as to if and how late payment penalties may be applied.
(ii) Taxpayer access to information on tax liabilities and administrative procedures	A	The taxpayer access to information is widely available through pamphlets, a website, educational workshops, a hotline and walk in assistance. There are also promotional programmes in print and electronic media. The Tax Authority carries out annual education campaigns jointly with the Chamber of Commerce. The Oil Producing Companies have clear instruction on tax liabilities and procedures (charged to the Oil Ministry) included in the Production Share Agreements.
(iii) Existence and functioning of a tax appeals mechanism	B	Tax appeal comprises three main levels: objection, appeal and the law courts. These are set out in the Tax Acts and guidelines provided with each tax assessment made. They are implemented across all governorates and appear to be functioning well in the case of the Tax Authority. They are also spelled out clearly for the Oil Producing Companies. In the case of the Customs Department while there is a clear tax appeals system there remains some question on the effectiveness of checks and balances incorporated into the appeals procedures given the level of discretion over penalty negotiations exercised by both the Commissioner of Customs as well as the Minister of Finance.
PI-14. Effectiveness of measures for taxpayer registration and tax assessment	**B**	
(i) Controls in taxpayer registration system	B	Taxpayers are registered using a unique Tax Identification Number (TIN) maintained in a database. The TIN is required by other administrations thus supporting the registration process.
(ii) Effectiveness of penalties for non-compliance with registration and declaration obligations	C	In the case of the Tax Authority and the Customs Department high penalties along with the risk of imprisonment should serve as an effective deterrent to non tax registration. Effectiveness is assured due to the vigorous application of the penalties to tax evaders who are discovered. However late payment penalties probably do not serve as fully effective disincentives given the commercial lending rates pertaining in Yemen currently. In the case of the Oil Producing Companies it is not really clear what penalties if any are applicable.
(iii) Planning and monitoring of tax audit and fraud investigation programs	B	Planning and monitoring of tax audit and fraud investigation programmes is carried out and managed using a selection basis derived from risk assessment. In the case of the 12 oil producing companies all are reviewed and audited on an on-going basis. The Customs Department plans to institute a risk basis for audit and fraud investigations but these have not yet

Indicator	Score	Brief Explanation
		been instituted.
PI-15. Effectiveness in collection of tax payments (M1)	**D+**	
(i) Collection ratio for gross tax arrears, being percentage of tax arrears at the beginning of a fiscal year, which was collected during that fiscal year	D	There are significant tax arrears in Yemen (>2%) with an average ratio for 2005 and 2006 that was 3.6%. The Tax Authority has requested to write off 3.7 Billion YR of uncollected taxes due to declared bankruptcies by the companies owing them. The collection ratios were 6%, 72% and 16% for the three years covered. There are not significant amounts of customs duties arrears. Given the mechanism for addressing past underpayments of Government oil shares there are no arrears on oil shares.
(ii) Effectiveness of transfer of tax collections to the Treasury by the revenue administration	A	Taxes are collected and paid into the Consolidated Fund are made daily on the next day after collection. The same arrangements exist for Customs duties. All payments for the Government oil share are paid directly into the Consolidated Revenue Fund.
(iii) Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the Treasury	A	Reconciliations of tax assessments, collections, arrears and transfers are done monthly within 15 days or so after the end of the month. A similar arrangement exists for Customs duties.
PI-16 Predictability in the availability of funds for commitment of expenditures (M1)	**D+**	
(i) Extent to which cash flows are forecast and monitored	D	No Cash flow forecasts are prepared by the MDAS. The budget release mechanism does not include any expenditure cash flows even though it may take into account actual revenue achievements to adjust the six-monthly general warrant that sets cash withdrawal ceilings. No revenue forecasts are made even though the pro forma revenue profiles from oil share sales can readily be determined over a thirty day horizon.
(ii) Reliability and horizon of periodic in-year information to Line Ministries on ceilings for expenditure commitment.	B	MDAs are provided with six-monthly general warrants by the Ministry of Finance which serve as the commitment ceilings against which expenditure is made. At this time these six-monthly general warrants (translated into expenditure allocation ceilings) are updated within the six month period and so may dilute the predictability and reliability of the six-month authorities to incur expenditure. While no detailed data was available on updates, their 6 month rolling nature and discussions with Government officials suggest that MDAs are provided reliable commitment ceilings quarterly in advance.
(iii) Frequency and transparency of adjustment to budget allocations, which are decided above the management of Line Ministries	C	All significant virements must be made subject to the approval of the Ministry of Finance and the CBY account structure support a strict application of virement control. However the frequent updates of the budget release appropriations by the Ministry of Finance are not done in a transparent way. The Budget Implementation Guidelines mention the conditions in which in-year budget adjustments can be made by the government and who is authorized to grant approval to these adjustments.
PI-17 Recording and management of cash balances, debt and guarantees	**B+**	
(i)Quality of debt recording and reporting	A	Comprehensive records on domestic and external debt are compiled and are updated and reconciled on a monthly basis. Comprehensive statistical reports providing information on debt stocks, debt service and

Indicator	Score	Brief Explanation
		debt management operations are prepared quarterly.
(ii) Extent of consolidation of the Government's cash balances	B	The payments system utilizes the Consolidated Fund for all payments on Government expenditure (except for grant and loan funded project accounts). This facilitates a monitoring mechanism that reports and reconciles the account on a daily basis. All active project accounts are held in the Central bank of Yemen and reconciled on a daily basis. There are small amounts held in Special Accounts directly by Line Ministries (estimated to be less than 1% of expenditure) that are not reconciled daily and remain outside this arrangement.
(iii) Systems for contracting loans and issuance of guarantees	B	The systems for contracting loans and issuing guarantees are bound by transparent procedures set within the legal and regulatory framework. Clear loan level ceilings are defined.
PI-18 Effectiveness of Payroll Controls	**D+**	
(i)Degree of integration and Reconciliation between personnel Records and payroll data	C	A computerized personnel data base exists for the civil services on the basis of which capturing of biometric details of all civil service employees is completed. However, this personnel database is fragmented and not fully maintained. It is also not linked to the Payroll database. But a manual system exists whereby civil service ministry issues a *fatwa* for any changes in the nominal roll. Based on this *Fatwa*, Ministry of Finance effects changes in the payroll. Reconciliation of the payroll with personnel records through this process is taking place at least every 6 months.
(ii) Timeliness of changes to Personnel records and the payroll	D	The civil service ministry issues *Fatwa* to make changes in the nominal roll, and based on that *Fatwa*, ministry of finance effects changes in the payroll. On an average, the time taken is 15 days. However, it is not clear whether the issuance of *fatwas* is systematic and comprehensive. With such fragmentation of personnel databases and no clearly defined systems for updating changes in personnel rolls, actual changes to personnel rolls is estimated to be longer than 3 months.
(iii) Internal controls of changes to personnel records and the payroll	D	There are some payroll controls but their effectiveness is undermined by the fragmentation and irregular updating of personnel rolls. There is evidence of substantial abuse of the payroll systems in the clean up exercise.
(iv)Existence of payroll audits to identify control weaknesses and /or ghost workers.	C	A partial payroll audit is being carried out by the Technical Unit by comparing attendance sheets to payroll lists.
PI-19: Competition, value for money and controls in procurement (M2)	**D+**	
(i) Use of open competition for award of contracts that exceed the nationally established threshold for small purchases	D	The Government of Yemen maintains data on public contracts awarded in individual Line Ministries and for all public tenders above 125 Million Yemen Riyals that was carried out using the Open Tender Method in the Supreme Tender Committee. There is insufficient data available to assess the proportion of contracts above the threshold which were carried out using the Open Tender Method.
(ii) Justification for use of less competitive procurement methods	C	The Tender Law establishes the open tender method as the preferred method and provides justification for less competitive procurement methods but is rather ambiguous in the application of the direct purchase method.
(iii) Existence and operation of a procurement complaints mechanism	D▲	While there is an Administrative Review Board to be created under the terms of the new tender law enacted in July 2007, the law in force for the period 2004 to 2006 did not facilitate addressing complaints regarding the implementation of a particular procurement process.

Indicator	Score	Brief Explanation
PI-20: Effectiveness of internal controls for non-salary expenditure (M1)	**D+**	
(i) Effectiveness of expenditure commitment controls	D	Commitment control ledgers are not maintained universally across all Spending Units. The AFMIS system under beta testing in four ministries does not have the commitment control module activated.
(ii) Comprehensiveness, relevance and understanding of other internal control rules/ procedures	B	Financial management rules and procedures exist and are documented and well understood. However there is much delay in practice which may be due to excessive duplication
(iii) Degree of compliance with rules for processing and recording transactions	C	Primarily due to the compliance checks that are carried out, compliance with rules pertaining to expenditure documentation is fairly high but there remain instances of emergency procedures that are used without adequate justification.
PI-21. Effectiveness of Internal Audit	**D+**	
(i) Coverage and quality of the internal audit function	D	The internal audit function covers all MDAs, executive agencies and public bodies. Operations however are restricted by staffing constraints and so in practice the Internal Audit Unit is unable to fulfil effectively its full responsibilities and coverage. Very little audit time is spent on systems audits, and though not possible to verify based upon audit work plans, an officer in charge of Internal Audit estimated the amount of time to be no more than 10%.
(ii) Frequency and distribution of reports	B	The reports are issued regularly for most audited entities and distributed to the respective Line Ministry, the Ministry of Finance with copies to COCA and the Cabinet.
(iii) Extent of management response to internal audit findings	C	The management response to audit queries in general appears to be varied as Officials report. The head of the public entity is responsible for carrying out the auditor's recommended corrective measures. No Audit Committees have been set up to follow up on audit findings and obtain management responses and actions.
PI-22 Timeliness and regularity of accounts reconciliation (M2)	**B**	
(i)Regularity of Bank reconciliations	B	It maintains the Consolidated Fund as a treasury single account which assigns a single main account for each Line Ministry but with a sub-account structure that reflects the chapter and subchapter structure of the budget. The CBY monitors and reconciles the Consolidated Fund account on a daily basis. The CBY provides a reconciled monthly disbursement report to the MoF within 10 days of the end of the month. However as already noted in PI-7 and D3 there are a few special accounts and project accounts that remain outside this arrangement.
(ii) Regularity of reconciliation and clearance of suspense accounts and advances	B	Suspense accounts are monitored and reconciled on a quarterly basis based upon monthly and quarterly submissions of budget execution reports submitted by the Line Ministries. However, some accounts have uncleared balances brought forward.
PI-23 Availability of information on resources received by service delivery units	**B**	A survey was undertaken in 2006 on Health and 2005 on Basic Education that reviewed the actual resources received by health and education facilities across the country. A PER carried out in 2006 referenced the period 1999 to 2003.
PI-24 Quality and Timeliness of in-year budget reports	**D+**	

Indicator	Score	Brief Explanation
(i)Scope of reports in terms of coverage and compatibility with budget estimates	C	The Monthly Expenditure Returns allow a direct comparison of budget implementation to the original budget. Only expenditures are covered, not commitments. Information included covers all of the budget estimates items.
(ii) Timeliness of the issue of reports	D	Reports are prepared monthly and quarterly and on average are submitted after more than 8 weeks after the close of each month.
(iii) Quality of information	B	Ministry of Finance does not attempt to consolidate and report on the national aggregate of arrears. COCA reports that the amount of arrears is substantial. There are some inconsistencies between detail accounts and summary figures. Although there are some concerns about accuracy, but data issues do not compromise overall consistency and usefulness.
PI-25 Quality and timeliness of annual financial statements	**C+**	
(i) Completeness of the financial statements	B	The Ministry of Finance prepares consolidated final accounts annually. Consolidated government accounts are prepared with revenue and expenditure information as well as a table of financial assets and liabilities. However, the financial statements do not include any expenditure or tax arrears.
(ii) Timeliness of submission of the Financial statements	B	Financial statements are submitted within 10 months of the end of the fiscal year
(iii)Accounting standards used	C	A set of accounting standards developed and financial statements are presented in a consistent format for the years reviewed.
PI-26. Scope, nature and follow-up of external audit	**B+**	
(i) Scope/nature of audit performed (incl. adherence to auditing standards)	B	Most central government entities are audited annually. It is estimated that about 80% of expenditure is audited annually. The audits cover mainly financial statements and compliance audit including revenues and expenditure. Value-for-money and performance audits have been performed to a limited extent. The audits, guided by an audit manual, focus on significant and systemic issues. There are efforts to conform to the INTOSAI standards.
(ii) Timeliness of submission of audit reports to the legislature	A	The COCA audit report is submitted within two months of the close of the fiscal year the Parliament every year. The certification of the annual financial statements is submitted by the end of December each year and no more than 3 months after the receipt of the consolidated financial statements.
(iii) Evidence of follow-up on audit recommendations	A	There a clear and actively followed procedure for follow-up on the audit recommendations. The procedures are time-bound and are generally adhered to. The implementation of corrective measures is followed up through successive audits
PI-27 Legislative Scrutiny of the Annual Budget Law	**C+**	
(i)Scope of the legislature's scrutiny	B	The Legislature mainly reviews the, details of expenditure and revenues, and only addresses fiscal policy as the context in which the detailed expenditure and revenues are discussed.
(ii)Extent to which the legislature's procedures are well-established and respected	C	The procedures for budget review are well established and the practices of the House and the Senate are well enshrined. The Budget

Indicator	Score	Brief Explanation
		Committee, a sub-committee of parliament, is itself supported by 6 sub- committees and 50 technical support staff. The Budget Documents do not include a column of approved budget estimates arrived at by the Ministry of Finance after consideration of the financial impact of the parliamentary recommendations. The legislature's procedures for budget review are therefore well established but not fully respected.
(iii)Adequacy of time for the legislature to provide a response to budget proposals both the detailed estimates and, where applicable, for proposals on macro-fiscal aggregates earlier in the budget preparation cycle (time allowed in practice for all stages combined)	A	The Legislature has slightly over two months in total to review the budget proposals.
(iv)Rules for in-year Amendments to the budget without Ex-ante approval by the legislature.	C	Rules for the in-year amendments exist but in practice there are extensive administrative re-allocations as well as expansions without ex-ante approval by the parliament.
PI-28. Legislative scrutiny of external audit reports (M1)	**D+**	
(i) Timeliness of examination of audit reports by legislature (for reports received with the last three years)	D	The Public Accounts Committee (Financial Committee) is currently reviewing the audit report for 2005 but did not review the audit report for 2004 and has not yet reviewed the audit report for 2006.
(ii) Extent of hearings on key findings undertaken by legislature	C	There appear to have been only ad hoc hearings on the key findings of the audit reports carried out in 2004, 2005 and 2006. However, in 2007 a far more systematic and comprehensive approach is being employed.
(iii) Issuance of recommended actions by the legislature and implementation by the executive	B	No actions were recommended by the Parliament in the years 2004, 2005 and 2006. However, in 2007, the Parliament has issued a 350-page report recommending actions on the basis of COCA's Annual Audit Report for 2005 accounts. Some of these recommendations have been also acted upon by the government.
D-1 Predictability of Direct Budget Support	**D**	
(i) Annual deviation of actual budget support from the forecast provided by the donor agencies at least six weeks prior to the government submitting its budget proposals to the legislature (or equivalent approving body).	*D*	No timely and comprehensive forecast was provided by the donor agency providing direct budget support in either of the two years in which direct budget support was provided.
(ii) In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates	*D*	The actual disbursement delays were 75% and 0% for 2005 and 2006 respectively, however in both years the agreements were made after the second quarter of the fiscal year in which they were disbursed.
D-2 Financial information provided by donors for budgeting and reporting on project and program aid (M1)	**D+**	
(i) Completeness and timeliness of budget estimates by donors for project support.	D	Several major Donors to not adhere to the Yemen budget cycle. There is the expectation as a number of major donors move to multi-year frameworks that they will be better able to align their budget estimates submissions with the Government's budget cycle.
(ii) Frequency and coverage of reporting by donors on actual donor flows for project	C	Not all Donors provide quarterly reports on actual disbursements to the Government but for those who

Indicator	Score	Brief Explanation
support.		deposit project funds with the CBY, tracking using DMFAS facilitates the timely tracking of disbursements and thus indirectly project implementation. . Many of the PMUs also report on project implementation quarterly and typically do so within 45 days of the end of the quarter. There are a number of difficulties that remain as to the accuracy as well as completeness of financial reports. These external loans, including IDA and Arabic Fund for Development, represent for more than 50% of the project disbursements for projects included in the budget.
D-3 Proportion of aid that is managed by use of national procedures	**D**	
(i) Overall proportion of aid funds to central government that are managed through national procedures.	D	Although many of the major projects use bank accounts monitored and located in the CBY and project management units sometimes directly located within the Line Ministries the systems employed for audit, reporting and accounting, and procurement for the most part are done as per the systems of the Development Partners. Less than 50% of aid funds are procured, accounted for, reported on or audited by national procedures and financial management systems.

Appendix 2

Terms of Reference for the Assessment of Public Finance Management in Republic of Yemen

1. ***Background and Context***

In the past few years, several diagnostic reviews of the Public Financial Management (PFM) system of Yemen have been carried out by the World Bank, the IMF and other donors. These have led to a broad degree of consensus between the donors and the Government of Yemen about the need for reform and the main priority areas. In addition, several donors are providing technical assistance and financial support to the Government in a range of projects and activities to promote improvements in PFM.

On August 9, 2005, in Cabinet Resolution No. 253 of 2005, the Cabinet approved the Public Finance Management Reform Strategy and resolved to establish a Ministerial committee chaired by the Deputy Prime Minister, Minister of Finance and members to include Deputy Prime Minister, Minister of Planning and International Co-operation, Minister of Local Administration, Minister of Civil Service and Social Security, Governor of the Central Bank of Yemen and the Vice Minister of Finance. The committee (which has not yet become operational) was charged with the responsibility of overseeing public finance reform and the Cabinet endorsed the components of Public Finance Management Reform outlined below:

1. General Budget Reform – Preparation, Execution and Information systems
2. Enhancing Control and Financial Accountability
3. Reforming the system of bids and procurement, and
4. Improving competence and skills

An Action Plan has been formulated on the basis of above Strategy, which has been divided into two phases. The first phase is to be implemented in the years 2006, 2007 and 2008. The activities under this Plan have been prioritized and sequenced in order to provide the best use of limited donor resources. The basic **Objectives** of this Action Plan, in the first phase, are as follows:

1. Adoption of modern Government budgeting principles
2. Enhancing Control and financial accountability
3. Reduce resource leakage
4. Improved financial reporting integrity and timeliness
5. Improved transparency

The **Outputs** that are to be achieved by the end of 2008 are as follows:

1. Introduction of Medium-Term Expenditure Framework
2. GFS Economic reporting of revenues and expenditures
3. GFS Functional reporting of expenditures
4. Supplementary statements of all off-budget transactions
5. Reduced resource leakage

The basic **Components** of this Action Plan in the first phase are as follows:

1. Improve Budget Classification, Preparation and introduce forward estimates
2. Improve Budget Execution
3. Roll out of the public finance management information system (AFMIS)
4. Improving capacity in budgeting, procurement and auditing
5. Adopt Internal Control concepts and framework
6. Improve Compliance
7. Improve Financial Reporting including budget coverage
8. Implementation of reformed system of bidding and procurement

A Partnership Agreement was signed in May 2006 between Government of Yemen, represented by the Ministry of Finance and Ministry of Planning, and, Donors, represented by the World Bank, UNDP, European Commission, Royal Netherlands Embassy, DFID, US Embassy, German Embassy, GTZ and Denmark, to implement the PFM Reform Strategy. The donor community declared their commitment to work together and in partnership with the Government of Yemen in designing and implementing key reforms that will build the capacity of the state to perform core PFM functions, contributing to good governance and poverty reduction for the country's citizens. The Government of Yemen similarly declared its commitment to the reform of PFM, to working in partnership with the donors, and to making effective use of the technical assistance and financial support provided by the donors for this purpose. Following this, a Project Agreement titled 'Implementation of Public Financial Management Reform Action Plan' was signed between UNDP and Government of Yemen in September 2006 with an objective of supporting Ministry of Finance to implement Public Finance Management as per its Action Plan. The Project Cost is US $ 3.662 Million with duration of October 2006 to December 2008. The project cost is shared by DFID, UNDP, Netherlands and GTZ/Germany.

2. Purpose of Assessment

The purpose of this assessment is to measure the present performance of the PFM function using an internationally accepted framework – the Public Expenditure and Financial Accountability (PEFA) Performance Measurement Framework. This framework identifies a set of critical objectives of a PFM system, and a standard set of high-level PFM indicators on PFM System Out-turns, Cross-cutting features of PFM System, Budget cycle and Donor practices, to assess performance against those objectives. The purpose is to produce a Baseline PFM Performance Measurement, against which the direction and extent of future progress can be measured overtime. This Performance Measurement would identify areas of low and high performances and, therefore, assist in the determination of those priority areas that need corrective and curative actions.

This assessment would enable the performance of PFM system to be regularly monitored against a baseline. In doing so, it would allow progress over time to be demonstrated by looking at the trends of the selected indicators. It would also allow for a wide international acceptability, international comparisons and would facilitate harmonization. Jointly undertaken with the Government, it would finally allow for increasing Government's capacity in PFM assessment and ownership of responses to identified weaknesses.

3. Objectives of Assessment

The ***general objective*** of this PEFA Assessment is to enhance implementation of the PFM Action Plan through more efficient and effective resource allocation and utilization by assessing the status and evolution of performance indicators in public finance management.
The ***immediate objectives*** of this assessment are to provide Government and the Donors with:
(a) An assessment of the current quality of PFM in the country and provide a status of the situation as at the end of 2006;
(b) Strengthen the capacity of MOF in conducting self assessment and targeting internal reforms

4. Scope of Assessment

The Assessment would be for the Central Government Budget only and would not include the Budget of Local Governments. The Consultant will use the guidelines contained in the latest publication of PEFA PFM Performance Measurement Framework, published by the PEFA Secretariat, in the World Bank, for this assessment. The Consultant would rank the PFM system over a set of following High-Level Performance indicators, as per given Guidelines:

A. PFM-OUT-TURNS: Credibility of the budget	
PI-1	Aggregate expenditure out-turn compared 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

B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency	
PI-5	Classification of the budget
PI-6	Comprehensiveness of information included in budget documentation
PI-7	Extent of unreported government operations
PI-8	Transparency of inter-governmental fiscal relations
PI-9	Oversight of aggregate fiscal risk from other public sector entities.
PI-10	Public access to key fiscal information
C. BUDGET CYCLE	
C(i) Policy-Based Budgeting	
PI-11	Orderliness and participation in the annual budget process
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting
C(ii) Predictability and Control in Budget Execution	
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
PI-16	Predictability in the availability of funds for commitment of expenditures
PI-17	Recording and management of cash balances, debt and guarantees
PI-18	Effectiveness of payroll controls
PI-19	Competition, value for money and controls in procurement
PI-20	Effectiveness of internal controls for non-salary expenditure
PI-21	Effectiveness of internal audit
C(iii) Accounting, Recording and Reporting	
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
C(iv) External Scrutiny and Audit	
PI-26	Scope, nature and follow-up of external audit
PI-27	Legislative scrutiny of the annual budget law
PI-28	Legislative scrutiny of external audit reports
D. DONOR PRACTICES	
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

Apart from ranking of PFM System on above indicators, the Consultant will in particular provide a documented analytical part:

(i) Justifying the benchmark value to be given on each of above indicators for 2006, giving the reasons for the rating, i.e. the circumstances that explain how the country got or stayed there. The ratings should be traceable and supporting evidence provided in the narrative.

(ii) More particularly, analysing any evolution during 2006, even if there is no change of the ranking itself. In this regard, kindly refer to Page 61 and 62 of aforesaid PEFA Guidelines, which deal with "reporting of progress" and of the use of upward arrows.

(iii) A structure for future PFM assessments should also be provided for in the report. The future PFM assessments could be in a cycle of every two or three years. This could be coupled with an annual review in areas of specific weaknesses, or for which a particular reform effort has been conducted. This structure should include the kind of roles and participation that would be expected from national and international actors, processes to be followed, and a calendar. This proposal should be built on Government views.

5. *Expected outputs of Assignment*

(i) A final report answering to the objectives and scope referred to above and

(ii) An enhanced capacity to conduct PFM assessments within relevant government offices involved in this exercise.

6. *Methodology for undertaking the assessment*

The detailed methodology to be used will consist of the following steps:

1. Use of the PEFA PFM Performance Measurement Framework:

As indicated before, the Consultant will use the latest publication of PEFA PFM Performance Measurement Framework, published by the PEFA Secretariat, in the World Bank. S/He will be required to apply the Framework guidance contained in the Framework's **Annex 1** for the PFM High-Level Performance Indicator Set and **Annex 2** for the format of the PFM Performance Report.

2. Preparation of inception report:

a. The consultants' work will begin with the drafting of an inception report, with the objective of presenting the methodology to be used based on analysing key policy documents, previous information on PFM in Yemen and interviews with key informants. In this report, the consultants will submit a detailed plan for activities and schedules, including the list of stakeholders to be interviewed, questionnaires and any other tool of analysis applied. The inception report should be submitted at the end of the first week of the field work to the Ministry of Finance, the World Bank Country Office in Sana'a and the Public Finance Management Advisory Unit (PFMAU).

b. Feedback will be given by the Government, PFMAU, the World Bank Public Sector team in Yemen and at headquarters and the PEFA Secretariat on the Inception Report within one week (five working days). Based on this feedback, the Inception Report will be finalized.

3. Preparatory workshop for national stakeholders

The consultant team will give a preliminary workshop for all stakeholders involved, in order to explain the concept of PFM and its importance for public sector development in Yemen, the Standardized Assessment approach and the PFM Performance Measurement Framework. The workshop will have the objective to address specific technical issues that government staff may raise. This workshop should help the government to have a cooperative attitude during this exercise. The minutes of this meeting will be prepared by the consultants.

4. Interviews with key stakeholders and key documentation analysis

5. Draft report

The draft report will include outcomes of interviews and seminar with stakeholders, results from data collection and main constraints identified. The draft report should be submitted one week after the end of the one month field mission.

6. Comments

Comments would also be sought from all stakeholders and development partners involved in this assessment, along with the Public Sector team in Yemen and at headquarters; and, the PEFA Secretariat at the World Bank headquarters. The written comments to the draft report would be required as soon as possible and in any case within one month after the delivery of the draft report.

7. Final Workshop on draft report findings and conclusions/ Comments

a- A workshop will be organised one month after the delivery of the draft report to discuss with all interested parties the draft report conclusions. This workshop will be facilitated by the consultants, who will be also responsible for preparing the minutes of this meeting.

b- In the event of differences of opinion on the consultant's findings with the Government's institutions involved, which may have been detected before the workshop, the consultants must report them in full during the discussion, and take note of any disagreement that may persist at the end of the workshop.

8. Submission of Final Report

One week is foreseen for the finalisation of the report after the conclusion of the Workshop. A final report will be externally prepared by the consultants.
Without undermining the independent nature of this assessment and the necessary objectivity of the ranking exercise, the consultants will consider feedback from stakeholders, development partners, the PEFA Secretariat and the Bank's team in Yemen and at headquarters into the report, as long as they have been remitted within the time limits. However, in case of persistent differences of opinion, the consultants will express their independent analysis in the report, and will inform separately, in a specific annex, of eventual differences of opinion expressed.

7. Involvement of Stakeholders in the assessment

It is extremely important that all major stakeholders are duly consulted in the assessment process. The major stakeholders in Yemen are:

1. Ministry of Finance: including the Minister, Deputy Minister and Director Generals.

2. Members of Inter-Ministerial Committee: set up by Cabinet Decision No. 134 of 2005 to oversee implementation of PFM Reform Strategy. The Committee is under chairmanship of Finance Minister and includes as members, representatives of Ministries of Planning, Local Administration, Legal Affairs, Civil Services and Pensions, Governor of Central Bank and Vice Minister of Finance.

3. Members of Technical Committee: set up by Ministry of Finance's Decree No. 430 of 2005 to review and follow-up Working Group in implementation of PFM Reform Strategy. The Committee is chaired by Vice Minister of Finance and includes as members representatives of government organizations that are members of inter-ministerial committee, Dean of Finance Institute, representative of Donors and the PFM expert.

4. Members of Working Group: set up to oversee detailed implementation of different components of PFM Reform Action Plan, under chairmanship of Deputy Ministers of Ministry of Finance.

5. Central Organization for Control and Auditing (COCA) - the Supreme Audit Institution responsible for external audit.

6. The National Project Director (NPD) to be appointed by Government of Yemen for ensuring implementation of PFM Project inputs, outputs and activities.

7. PFM Expert in the PFM Advisory Unit

8. AFMIS Expert in the Ministry of Finance

9. Donors: Netherlands, DFID, UNDP, World Bank, GTZ, USAID, Germans and Denmark.

The main Government partner for this exercise is the Ministry of Finance (MoF). The MoF will be responsible for liaising with other actors, informing them on this exercise, providing all the necessary information and requiring their respective cooperation.
Due to its specific role in the PFM area as an external auditor, it is particularly important that the COCA, which works in an independent manner from the Government, would be informed at an appropriate time, would provide the relevant information and participate in the discussions about the preliminary findings.
Generally, all services that are to be affected by the findings and recommendations of the assessment should be invited by MoF to participate in the workshops and to react to conclusions.
It is important that this work be undertaken through a more participatory approach, without however compromising a professionally sound and objective assessment. After having reached an agreement on the present terms of reference, the involvement of the Government can be seen at three level: (1) operationally in the provision of the information from specific services along the field work phase; (2) technically in discussing the preliminary findings of the draft report; (3) finally through an annex of the final report expressing eventual divergence of Government's opinions from the consultants' analysis.

8. Human resources

The consultancy team will consist of two consultants: one international and one local, both with excellent capacity in PFM area, knowledge of PEFA approach, preferably fluent in Arabic language with solid work experience in Yemen. These two consultants would be supported by staff inputs from Arun Arya and David Biggs, Senior Public Sector Specialists, in the World Bank, based at Yemen and Washington DC, respectively.

9. Calendar

S. No.	Task	Target Date
1.	Start of Assignment	June 23, 2007
2.	Submission of Inception Report	July 2, 2007
3.	Submission of Comments to Inception Report	July 9, 2007
4.	Finalization of Inception Report	July 17, 2007
5.	Field Work	August 7 to September 4, 2007
6.	Submission of Draft Report	September 9, 2007
6.	Comments on Draft Report	September 29, 2007
7.	Workshop	October 12, 2007
8.	Final Report	October 20, 2007

10. Presentation of the reports

All reports should be sent both in English and Arabic, both in paper and in electronic version, to the World Bank Country Office in Sana'a, Yemen, Ministry of Finance, the PFMAU and the PEFA Secretariat.

Appendix 3

List of Stakeholders Interviewed

No	Name of the Person		Ministry/Agency
1	Abdul Rahman Ali,	Dep. Minister, Final Accounts	MOF
2	Abdul Raqeeb Al Shargabi,	DG, Control of Budget Allocations	MOF
3	Ali Yahia Al Yajouri,	Director of Final Accounts	MOF
4	Ali Hassan Dhaiban,	Director Capital Expenditures	MOF
5	Hani Abdul Rahman Enan,	Director of External Loans	MOF
6	Nasr Al Harbi,	Deputy Minister for Public Corporations	MOF
7	Mr. Azez Othman,	Director General of Public Corporations	MOF
8	Mohamed Al Suroori,	Director for Public Corporations	MOF
9	Ali Jubran Al Shamahi,	DG for Budget Preparation	MOF
10	Tarek Abdul Raqeeb Rashed,	DG of Budget Release	MOF
11	Kaid Ahmed Mohamed,	Director of Budget Release	MOF
12	Nagi Ali Jaber,	Director of Budget Release	MOF
13	Ghaleb M. Ahmed,	Budget Release	MOF
14	Ahmed Taher Nage,	DG for Audit and Control	MOF
15	Farez Taher Al Ma'amary,	Director for Audit and Control	MOF
16	Anwar Kamarani,	PFM Coordinator	MOF
17	Dr. Ali S. Mothanna,	Deputy M. For Planning and Statistics	MOF
18	Ahmed Mohamed Hajar,	Ass. Deputy of Planning & Statistics	MOF
19	Abdul Galeel Al Dar,	Director of Planning & Statistics	MOF
20	Dr. Nabeel Al Sohaibi,	AFMIS Project Director	MOF
21	Mr. Abldul K. Al Raie,	Sub Governor, Domestic Banking	CBY
22	Ahmed Yahia Al Washali		CBY
23	Fadhl Abdul W. Al Ameri,	DG for Domestic Debts	CBY
24	Mohamed Al Sanhani,	Deputy DG for Budget Preparation	Ministry of Local Administration
25	Abdul Razak Mutair,	Director of Financial Affairs	Ministry of Local Administration
26	Sadek Ali Hassan,	Procurement Officer	Ministry of Local Administration
27	Abdul Malik Al Kaderi,	Director of Financial Affairs	Ministry of Local Administration
28	Ismael Abdul Moghni,	DG for Financial Affairs	Ministry of Education
29	Raweh Noaman Saeed,	Director for Budget Preparation	Ministry of Education
30	Rajeh Ahmed Al Zoraiki,	Director of Accounting	Ministry of Education
31	Jamal Al Haimy,	DG for Internal Audit and Control	Ministry of Education

No	Name of the Person		Ministry/Agency
32	Ahmed Hamoud,	Director of Internal Audit	Ministry of Education
33	Mohamed Issa,	Director for Procurement	Ministry of Education
34	Faisal Ahmed Ghaleb,	Director for Human Resources	Ministry of Education
35	Ahmed A. Ghaleb,	Chairman of Tax Authority	Tax Authority
36	Ahmed Al Taieb,	GD for Internal Audit & Control	Tax Authority
37	Ahmed Al Barakani,	GD for Tax Appeal	Tax Authority
38	Tarek Al Barrag,	GD for Accounting	Tax Authority
39	Ziad Saleh Rowaishan,	Director for Taxpayer Registration	Tax Authority
40	Yahia Al Ashwal,	Chairman of Technical Committee	Supreme Council for Gov. Tenders
41	Anam Yahia Al Shah,	Secretary General	Supreme Council for Gov. Tenders
42	Dr. Abdalla Al Sanafi,	President (Chairman)	COCA
43	Dr. Mansour Al Butani,	Deputy President for the Admin.Sector	COCA
44	Mohamed Saif Al Mikhlafi,	DG for Final Accounts	COCA
45	Ahlam Bagatian,	Deputy Director of Technical Cooperation	COCA
46	Mohamed Zohra,	Deputy President	COCA
47	Abdul Salam M. Al Samawi,	Director of Legal Affairs Dept.	Chamber of Commerce & Industry
48	Mohamed Saba’a Al Gabri,	International Dept. Director	Chamber of Commerce & Industry
49	Dr. Ali Ali Al Zobaidi,	Chairman of Custom Authority	Custom Authority
50	Faisal Mohamed Moajam,	DG of Planning & Statistics	Custom Authority
51	Fadhl Mohsin Alban,	DG of Inspection	Custom Authority
52	Mohamed Ali Al Mahfadi,	DG of Custom Revenue	Custom Authority
53	Adnan Abdul Jabar,	DG of Labour Force	Ministry of Civil Service
54	Mohamed Naser Al Janad,	Dep. Minister, Oil Revenue Sector	MOF
55	Abdul Salam A. Shoalan,	DG of Oil Revenue Sector	MOF
56	Ahmed Ali Al Samawi,	DG of Exemptions, Oil Revenue Sector	MOF
57	Saleh Abdul Noor ,	DG of Custom & Tax, Oil Revenue Sector	MOF
58	Jehan Abdul Ghafour,	Assistant of DFID Director	DFID
59	Mohammad Pournick,	Economic & Governance Advisor	UNDP
60	Mike E. Sarhan,	Mission Director	USAID
61	Brian J. McGrath,	Political & Economic Officer	US Embassy
62	Ton Negenman,	First Secretary for Water & Sanitation	Netherlands Embassy
63	Laurence,	Financial & Admin. Advisor	Netherlands Embassy
64	Mary Horvers,	Development Cooperation Attaché	European Union
65	Mohamed Naser Al Janad,	Dep. Minister for Oil Revenue	MOF
66	Abdul Salam A. Shoalan,	DG for Oil Revenue	MOF
67	Saleh A. Hashem,	DG for Tax and Customs	MOF

No	Name of the Person		Ministry/Agency
68	Ahmed A. Al Samawi,	DG for Exemptions	MOF
70	Ashraf Faisal Al Maktari,	Oil Revenue Auditor	MOF
71	Abdulla Mohamed Sufan,	Secretary General	Parliament
72	Zakaria Saeed Al Zikri,	Dep. Chairman, Financial Committee	Parliament
73	Shaikh Mohamed M. Al Bakri,	Member of Finan. Committee	Parliament
74	Abdo Mohamed Radman,	Member of Finance Committee	Parliament
75	Ahmed Al Nowairah,	Member of Financial Committee	Parliament
76	Abdul Salam Y. Al Mohowtari,	Member of F. Committee	Parliament
77	Abdulla Hassan Al Sharttar,	Dep. Minister for Projects Program	Ministry of Planning & Int Cooper.
78	Ahmed Hazza Asad,	DG for Projects Program	Ministry of Planning & Int Cooper.
79	Dr. Saeed Al Shamasi,	DG for Petroleum Accounting	Ministry of Oil
80	Mohamed Y. Al Mashari,	Assets & Materials Director	Ministry of Oil
81	Khaled Shamsan,	Director of Petroleum Accounting	Ministry of Oil
82	Majid Al Sharafi,	IT Manager	Ministry of Oil
83	Shukria Mojahed H. Ghaleb,	DG for Internal Audit	Ministry of Oil
84	Abdul Hameed Abdul Rab,	Director of Crude Oil Marketing	Ministry of Oil
85	Fikri Abdul Wahed,	Former DG for Internal Audit	MOF
86	Hilmi Jaber,	DG for Domestic Debts	MOF
87	Hassan Mana,	DG for Grants	MOF
88	Nabel A. Shamsan,	Deputy Minister for Labour Force	Civil Service Ministry
89	Mohamed S. Al Hindi,	DG for Data Base and Biometrics	Civil Service Ministry
90	Steeve Laberge,	Consultant, Solution Technology	Civil Service Ministry
91	Abdul Rakeeb Sifyan,	Director of Information Centre	Civil Service Ministry
92	Hussain Mohamed Bukair,	Director of Tech. Support Network	Civil Service Ministry
93	Abdul Salam Al Mikhlafi,	Director of Int. Audit	Civil Service Ministry
94	Yoji Hattori,	First Secretary	Japanese Embassy
95	Ali A.W. Al Wajih,	Director of Crude Oil Marketing Depart.	Ministry of Oil

Appendix 4
Documents Received for Assessment of the PFM in Yemen

No.	Documents Received	Language
1	Constitution of Yemen	Arabic
2	Finance Law of 1990 amended 1999	English
3	Tender Law (1997) Newly Revised Tender Law	English Arabic & English
4	Civil Service Law (1980)	Arabic
5	Income Tax Law Tax Legislations	Arabic & English Arabic
6	Customs Revenue Law	Arabic
7	Conceptual Design for AFMIS Project	English
8	Central Organization for Control and Auditing (1992) Act	Arabic
9	General Auditor's Report on 2005 Budget Execution	Arabic (Translated)
10	Budget Call Circular 2006	Arabic
11	Budget Speech 2006	English
12	Budget Implementation Guidelines (207)	English
13	Strategic Educational Plan	English
14	National Development Framework (DPPR)	English
15	Debt Management Law and debt stock (External & Domes.)	English
16	Macro Fiscal Framework (July 2007)	English
17	Local Authority Law	Arabic and English
18	Partnership Agreement and Project Document	English
19	Budget estimates Volume 1 for 2004, 2005 & 2006	Arabic
20	Final Accounts(Budget execution)for 2004, 05 & 06 Volume I & II	Arabic
21	Final Accounts for Public Corporate and special funds For 2004 & 2005	Arabic
22	Central Support and Public Revenues for the local Authority for the years 2004, 05 & 06	Arabic
23	Country Financial Accountability Assessment (CFAA June 2005)	English
24	Monthly and Quarterly reports on budget execution from the line ministries	Arabic
25	Tax Authority Plan	Arabic
26	Sales Tax Law	Arabic
27	Law No of 2000 concerning on local Authority	Arabic and English
28	Cabinet Decree No. 383 for the Year 2001 on Public and Internal Revenues	Arabic
29	Secondary School Strategy (2007 – 2015)	English
30	Basic Education Strategy (2003 – 2015)	English
31	External Debts Stock as June 30, 2007	English and Arabic
32	Domestic Debts Stock as of July 31, 2007	Arabic
33	Central Bank Law	English and Arabic
34	Annual Internal Audit Plan for the year 2006	Arabic
35	Local Authority Actual Expenditures for 2005, 05 & 06	Arabic
36	Law No. 35 for the year 1991 on Public Corporations	Arabic
37	Actual Disbursements of External Debts for 2004, 2005 and 2006	Arabic
38	Financial Policies for the Central Budget Draft for the For the year 2008	English
39	Review of Official Development Assistance of Japan to Yemen over the last 3 decades.	English
40	European Union – Yemen Corporation – Disbursements For years 2004, 2005 and 2006	English
41	USAID Disbursements 2004, 2005 and 2006	English
43	PFM Reform Strategy	English

Appendix 5
Organigram for the Ministry of Finance