State and Region Financing, Planning and Budgeting in Myanmar

What are the Procedures and What are the Outcomes?

Roger Shotton, Zin Wlnt Yee and Khin Pwint Oo

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About the Authors

The lead author of the report, Roger Shotton, is a Bangkok-based independent consultant with 30 years of policy and field experience working on decentralization, local government, local infrastructure planning and local public financial management issues across Asia and Africa. Zin Wint Yee is a Program Officer at The Asia Foundation. Khin Pwint Oo is a Program Associate at the Renaissance Institute.

About The Asia Foundation and Renaissance Institute

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The Renaissance Institute (RI) is a policy institute that is closely assisting the government and key policymakers of Myanmar with policy recommendations and research for evidence-based policymaking. RI provides analytical support, assists government capacity-building and facilitates engagement between Myanmar's government and other relevant stakeholders. In particular, RI is supporting key policy priorities of the current government: public financial management reform and fiscal decentralization.

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Preface

Effective subnational public financial management is essential if state and region governments are to achieve their potential in addressing local and national policy development priorities, including the delivery of public services in their areas of jurisdiction. While the 2008 Constitution provides the framework for subnational governance and public financial management at the state and region level, the precise roles and responsibilities remain unclear with little guidance provided for lower levels of local government. As such, there is significant room to improve the clarity, efficiency and equity of public financial management procedures and processes, which would in turn bring real and tangible benefits to people across Myanmar.

This report provides a foundation for a better understanding of the current subnational public financial management in Myanmar. It presents an overview of the constitutional, institutional, and financing framework that determines subnational public expenditure. The report particularly focuses on assessing both how priorities and investments are determined in sectors that are now under the authority of state and region governments, and those which remain under direction from the Union level. After a rigorous review of procedures and issues in subnational public financial management, the report concludes with recommendations for improved practice in three main areas: (1) effectiveness and efficiency, (2) equity, and (3) transparency and accountability. We hope that this report will contribute to ongoing discussions of governance and reform issues that are critical to Myanmar's democratic transition and economic development.

This research paper is written by an independent researcher Mr. Roger Shotton, together with Ms. Zin Wint Yee of The Asia Foundation, and Ms. Khin Pwint Oo of the Renaissance Institute. Mr. Roger Shotton is an expert with decades of working experience in decentralization, local government and local public financial management in a number of countries; Ms. Zin Wint Yee works in the area of subnational governance with a specific emphasis on public financial management; and Ms. Khin Pwint Oo is a researcher with expertise in economics.

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Acronyms

ADT	average daily traffic
BE	budget estimate (the base budget)
CDF	Constituency Development Fund
CDG	Constituency Development Grant
CESR	Comprehensive Education Sector Review
DAO	Development Affairs Organization
DOC	Department of Construction
DBE	Department of Basic Education
DPFIC	District Plan Formulation and Implementation Committee
DRD	Department of Rural Development
FY	fiscal year
GAD	General Affairs Department (within MOHA)
GDP	gross domestic product
IFRD	Inter-governmental Fiscal Relations Department (within MOPF)
IRD	Internal Revenue Department (within MOPF)
MMK	Myanmar kyat (national currency)
MOHA	Ministry of Home Affairs
MOPF	Ministry of Planning and Finance
MP	Member of Parliament
MTFF	medium-term fiscal framework
NPC	National Planning Commission
PAC	Public Accounts Committee
PFIC	Plan Formulation and Implementation Committee
PFM	public financial management
RE	revised estimate (revised budget)
RTS	Representative Tax System
SEE	State Economic Enterprise
S/R	states/regions
SNG	subnational government
TE	Target Expenditure
TPFIC	Township Plan Formulation and Implementation Committee
VIP	very important person

Executive Summary

Introduction

This report on state and region planning and budgeting in Myanmar looks at state/region responsibility for expenditures, at how these are financed, at how expenditures are planned and budgeted, and at budget outcomes—all with special focus on investments and the capital budget. In so doing, the report identifies a number of issues which impact the quality of subnational public financial management (PFM), and then it suggests some of the ways these problems might be addressed.

The 2008 Constitution established the framework for subnational governance and PFM. It laid down the structures for administration and representation at one subnational level only—that of the 14 states and regions—and broad (though not always clear) parameters determining the responsibilities and resources of this level. However, no further legislation has been formulated or approved to translate these provisions into more detail, and by default, subnational responsibilities and arrangements are mainly governed by a range of pre-existing regulations,[1] and by established practices, which have not been fully documented.

In order to provide greater understanding of subnational public financial management, this study looked at the overall constitutional, institutional and financing framework for subnational public expenditure, at the processes for financing, planning and budgeting, and at the actual outcomes with regard to priorities actually funded or not funded. Particular attention was paid to documenting and understanding how capital investment planning and budget priorities are determined both for sectors which now fall under state/region authority and for those which remain under Union authority, notably the Department of Basic Education (DBE) and the Department of Rural Development (DRD).

The paper is based on: (i) fieldwork carried out in Myanmar in June/July 2016, during which a small team from The Asia Foundation (the Foundation) and the Renaissance Institute (RI) visited four states and regions (Shan, Ayeyarwady, Tanintharyi and Kayin); (ii) desk reviews of documentation on states/ regions;[2] and (iii) broad international experience in the area of subnational governance, PFM, finance, and service delivery.

Subnational expenditure responsibilities

Mandates and practice. These responsibilities need first to be clarified since (a) they shape the scope of subnational planning and budgeting, and (b) determine the financing needed for these functions, given the "Finance follows Function" axiom. Here, reference is usually made to Schedule 2 of the 2008 Constitution as the basis for these responsibilities, in contrast to Schedule 1, which indicates Union responsibilities. However, these two schedules are both vague and incomplete, e.g. they say little about key sectors such as education or health, and nothing about sectors such as the environment.

But, whatever the legal mandates may be, actual expenditure data suggest that the sectoral range of expenditures is very limited: roads and bridges, local administration, DAOs, and very minor expenditures in support of agriculture, irrigation, forestry, etc.; some state/region governments also make modest off-grid electricity investments.

[1] Work is underway— with World Bank support— to update the 1986 public financial management regulations.

[2] Including three earlier reports of The Asia Foundation: "State and Region Governments in Myanmar" (2013), which outlined the complex state/region subnational government institutional structures, their roles and relations with the Union Government; "Fiscal Decentralization in Myanmar" (2014), which outlined the rationale for a greater degree of fiscal decentralization and a road map for achieving this; and "State and Region Public Finances in Myanmar" (2015), which outlined subnational government revenue powers and trends, and their expenditure patterns.

Expenditure responsibilities - issues arising:

a) Inconsistent application. The distinctions in legal mandates are not always consistently applied. For example, "Union roads" are supposed to be funded from the Union budget, yet 60% of the Tanintharyi Region roads budget is spent on Union roads.

b) Anomalies and splits. There are splits in responsibility which undermine efficient PFM. For example, in the case of off-grid electricity, the capital expenditures are funded by the state/region budget, but current expenditures by the Union budget. Electricity investments themselves are split between the Electricity Department, the Department of Rural Development and, in some cases, the Department of Border Affairs. Roads expenditures are split between the Department of Highways, DRD, and the Development Affairs Organization (DAO). Such split functions are manageable if there is inter-departmental coordination in planning and budgeting, but such coordination is very weak.

c) Extreme centralization. Most fundamentally, a range of expenditures are still under Union line ministry control which would be much more efficiently and effectively managed at the state/region level: e.g. rural roads, rural water supply and sanitation, basic education facilities, basic health facilities, etc. Elsewhere in Asia, all of these are typically legally mandated to local governments that are often much smaller and less well-staffed than Myanmar's townships, let alone Myanmar's states and regions.

Table 1 Some expenditure assignments to local government elsewhere in Asia

Nepal Local Self-Governance Act (1999)	Bangladesh Union Parishad Act (2009)	Kerala State - India State Local Government Act (1994)	Cambodia Law on Commune & Sangkhat Administration (2001)
Village Development Committees *[av. pop. 10,000]*	*Union Parishads* *[av. pop. 27,000]*	*Gram Panchayats* *[av. pop. 25,000]*	*Communes* *[av. pop. 8,000]*
- drinking water - primary education facilities - primary health facilities - village roads - village irrigation	- rural roads, culverts - wells, water pumps, tanks, ponds - irrigation and drainage works - street lighting	- pre-primary, primary & upper primary schools - dispensaries and hospitals - rural water supply - waste disposal - public toilets and bathing places - day care centers	- village roads & bridges - village water supplies - village irrigation - primary school facilities - primary health care facilities

Av. pop. = average population

d) Divided loyalties of the state/region administration. State/region ministerial departments (except Development Affairs) are primarily accountable to their Union ministries, although nominally, they report to state/region government, which at times gives rise to conflicts of interest in regard to their Union and their state/region responsibilities, especially where their resources are short.

Financing of subnational plans and budgets

State/region revenues comprise: (a) own-source revenues which come from tax and other sources; and (b) fiscal transfers—a mix of shared revenues and, most importantly, grant transfers from the Union level. Together these are the resources which finance state/region plans and budgets. These financing mechanisms greatly influence not only the levels, but also the quality, of public expenditures in the states/regions. In the following section, each revenue source is discussed, in turn.

Own-source revenues

Own-source revenues - sources. State/region governments collect both tax revenues, and revenues from fees, licenses, etc., within the powers under Schedule 5 of the Constitution. The main state/ region tax revenues are property and road vehicle-related wheel taxes (collected by DAOs), excise and land taxes (collected by the Union's General Administration Department - GAD), and depending on context, fishery and forestry taxes. The main non-tax own-source revenues are licenses auctioned by the DAO for such things as slaughterhouses and ferry crossings, although some state/region governments also receive substantial revenues from other sources, e.g. Shan State receives large revenues from various projects and public-private partnerships.

Own-source revenues - patterns. Own-source revenues per capita vary greatly - e.g. in fiscal year (FY) 2016/17 they ranged from Myanmar kyat (MMK) 3,136 (Kayin) to MMK 40,127 (Yangon), and this variance has been increasing in the past five years. Across Shan, Tanintharyi and Ayeyarwady, non-tax revenues dominate own-source revenues (56-88% of the total), and these, in turn, are dominated by DAO license auction revenues. While total revenues per capita were not too different in these three states/regions, the composition varied substantially. In Ayeyarwady and Tanintharyi tax revenues per capita were almost identical (at around MMK 1,250) but were less than half that level in Shan (at MMK 540); however, in Shan the State government received various non-tax revenues (from private-public ventures and other fees accruing to the State) amounting to MMK 1,806 per capita which - together with DAO non-tax revenues - more than compensated the lower tax-revenue collection.

Table 2 Own-source revenue per capita composition - MMK (FY 2016/17)

Type of Revenue	Ayeyarwady	Shan	Tanintharyi
Part 1: State & Region Government Revenues	18	1,806	93
Part 2: Department Revenues Dept. Tax Revenues	1,223	540	1,253
Other Dept. Own Revenues	1,573	2,186	1,846
of which DAO non-tax revenues	*1,504*	*2,119*	*1,792*
Total Own-Source Revenues	2,814	4,531	3,192

Fiscal transfers

Union sharing of revenues. Starting in FY 2016/17, the Internal Revenue Department (IRD) is sharing 15% of (non-import) commercial and special goods tax revenues with state/region governments, based on area of collection. Hence, of the total estimated MMK 213.4 billion "shareable pool" for 2016/17, MMK 192.8 billion was returned to Yangon. At the state/region level, there is still some ambiguity about this arrangement. There is also a long-standing arrangement whereby the IRD shares 5% of (non-corporate) income tax, and 2% of stamp duties with DAOs, based on the township of origin. For FY 2016/17, the total pool was MMK 37.3 billion, of which MMK 25 billion reverted to Yangon, and MMK 8 billion to Mandalay. Overall these shared revenues accounted for some 14% of total transfers to the subnational level. DAO-shared revenues accounted for only some 5% of DAO revenues in the smaller towns of the areas covered by this study, though possibly it was much more in the cities (but, from FY 2017/18, these revenues will be shared directly with state/region governments and no longer earmarked for DAOs).

"Deficit" grant transfers - the legacy. These constitute the great bulk (up to 95% in some cases) of revenues in the states/regions, with the exception of Yangon and Mandalay. Traditionally, Union transfers to state/region governments have followed the negotiated "deficit grant" model, common in many ex-socialist countries, whereby state/region governments propose a budget with an inevitable deficit, and the Union government determines the extent to which these deficits will be covered by a transfer. In the process, the Union often selects specific state/region budget priorities for this additional funding. This model has had a number of negative results (also seen in many other countries). These are: i) a trend toward inflated expenditure proposals, with little prioritization; ii) weak incentives for own-source revenue collection; iii) inequitable revenue outcomes across states/regions; and, iv) an overall lack of transparency and fueling of center-local patronage relations.

"Deficit" grant transfers - medium-term fiscal framework (MTFF) reforms underway. However, thanks to the MTFF reforms, the grant transfer mechanism is also being reformed. First, since FY 2015/16, both the grant pool and the allocations to states/regions have been formula-based; second, since FY 2016/17 grant amounts have been announced to state/region governments in November, before state/region budget proposals are finalized, allowing states/regions to factor-in their budget ceiling in this process. Previously this information was only provided in January, after one or more initial budget proposals from the states/regions. As discussed in more detail in the following section, this is a very important reform.

State/region revenues - key issues

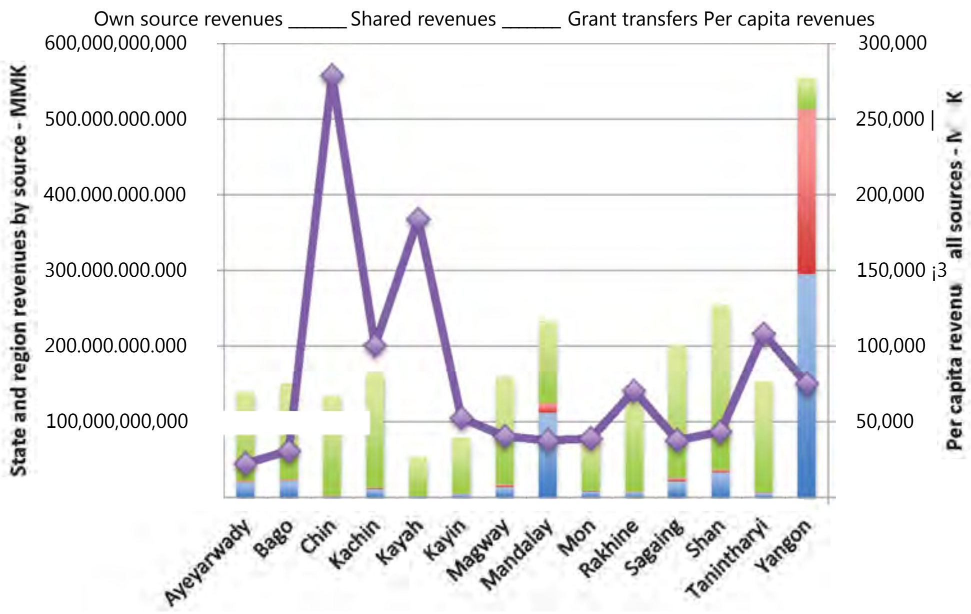
A number of features of the arrangements just outlined pose problems for state/region PFM:

a) Own-source revenues: Schedule 5 of the 2008 Constitution gives very limited revenue powers to the states/regions, but it is not unusual for the central government to retain the most productive sources of revenues (taxes on corporate incomes, profits, trade, etc.). What is more problematic is that: (i) tax rates have remained unchanged for decades (e.g. land tax is a negligible MMK 3.5 per acre), and often tax collection costs are more than the revenue collected; (ii) collection procedures are cumbersome and costly because over 20 state/region departments are engaged in revenue collection, rather than a single state/region revenue collection office; these two problems are partly due to (iii) the fact that many laws and regulations governing revenue powers have not been aligned to Schedule 5 provisions; (iv) there is no guidance or capacity support for state/region revenue collection; and (v) a potentially major state/region tax revenue source — property tax — is solely for the use of DAOs in urban areas. Further, (vi) as noted, for some years the deficit transfer model has probably undermined local fiscal effort, though this should now change, with MTFF reforms noted. Lastly (vii), it should be noted that although "excise revenue" is constitutionally assigned to states and regions, in practice it is the Union that collects this through the special goods taxes on alcohol and tobacco - possible also due to inconsistency of older laws and regulations with Schedule 5.

b) Revenue-sharing: Sharing the revenues from taxes on businesses and special goods is a positive step, but there is no obvious reason for this to be shared based on the area of tax generation. Unlike taxes earned from, for example, natural resource development or tourism, there is no local public expenditure required to manage or mitigate the effects of the commercial activity that is being taxed. It would therefore be simpler to put the shared pool into the larger grant transfer pool, for allocation by formula. Generally, information about various sharing arrangements seems to be lacking at both the state/region and the Union levels, which also prevents monitoring of the overall resource streams, and the devising of overall effective and equitable inter-governmental fiscal policy.

c) Grant transfers: The move toward rule-based allocations is a major step forward. However, there are serious problems in the formula currently used (and even in the manner of computation). As a result, the relative outcomes do not reflect relative need, and are highly inequitable, resulting in a bias toward states/regions with smaller populations such as Chin and Kayah, and bias against those with large populations, such as Ayeyarwady, Bago, or Sagaing. Figure 1 shows both total state/region revenues (grant transfers combined with shared-revenues and own-source revenues) as well as total revenues per capita, for all states and regions, for which the degree of variance is striking. Of course, differing needs mean that allocations per capita do need to vary, but the current range of 1:10, or more, seems hard to justify.[3]

Figure 1 State and region per capita revenues - all sources



The move to announce budget allocations in November is also an important improvement, as it allows state/region governments to finalize their budget proposals, based on a realistic ceiling. However, in some states/regions, the message that this is indeed a ceiling seems not to be recognized, and the old practice of submitting inflated, un-prioritized budget proposals persists. This, as discussed further, continues to undermine the quality of PFM.

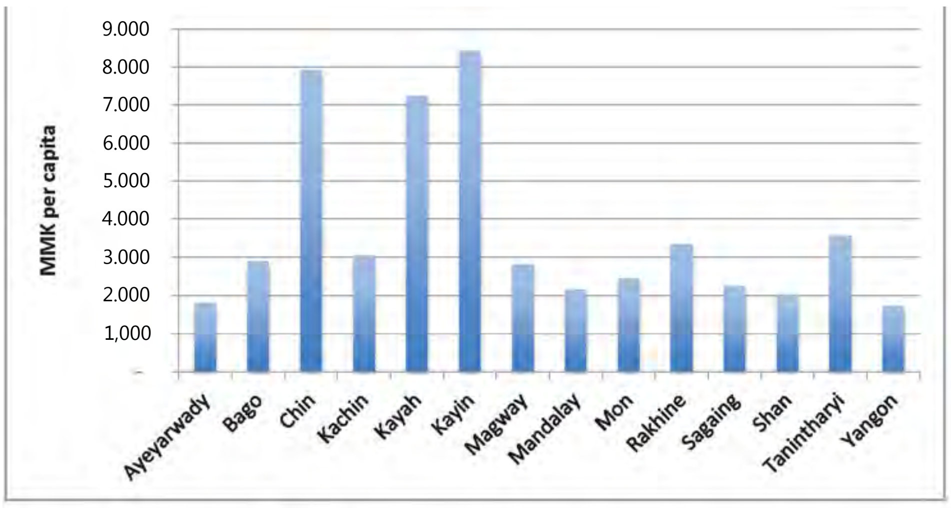
"Deconcentrated" financing

A last element in subnational financing arrangements lies in the funding for Schedule 1 expenditures undertaken by state/region line departments (Basic Education, Rural Development, etc.) using the

[3] It may be argued that these per capita variations simply compensate for greatly varying Union Government expenditures in different states/regions. However, this misses the point that Union and state/region governments each have (in theory) different sets of expenditure responsibilities (aside from the fact that no data are available on these Union expenditures by state/region).

Union budget. Despite some suggestions that state/region line departments are given ex-ante budget allocations, this is not, in fact, the case (hence financing is not strictly deconcentrated). All budget allocations and approvals appear to be made at the Union ministry level after state/region departments (and other state/region actors) have submitted their budget proposals. In the case of the Department of Basic Education, a rough estimate of the equity of allocations can be made using population as a proxy for populations of school-age children. So in FY 2016/17 allocations per capita for states/regions varied between MMK1,730 (Yangon) and 8,439 (Kayin) — a ratio of 1:5. While much lower than the variance for general grant transfers, this range is still high. It may be that this variance does somehow reflect the relative needs or costs for basic education provision in different states and regions, although, if so, the relatively low allocation to Shan State (only MMK 2,030 per capita), for example, is surprising. It is more likely that the variance is simply the combined result of the disparate criteria applied by the Union DBE. In this regard, it seems likely that just as with general grant transfers, there is an implicit bias in the allocation mechanism towards states/regions with a smaller population (such as Chin and Kayah).

Figure 2 Financing per capita for basic education investments: FY 2016/17



Subnational planning and budgeting procedures

Overview. State/region governments and their various departments have routinely prepared Five-Year Plans, although there is agreement that the current Five-Year Plans (2016/17-20/21) reflect outdated priorities and will need to be amended. These plans are translated into annual plans, and operationalized through state/region annual budgets, which include the capital and current budgets for both the plan and other expenditures. There is an annual process for preparing these documents, which culminates in approval of an annual State/Region Budget Law and Plan Law by the state/region Hluttaw, and the signature of the chief minister, normally in March/April, at the start of Myanmar's fiscal year. The State/Region Plan Law has two Annexes listing approved investments: Volume 1 contains those investments to be funded under the state/region budget, and Volume 2 contains investments under the Union budget.

The annual process - key steps (see also Figure 3). In June each year, the State/Region Planning Department leads a review that examines the implementation of the previous year's annual plan. Subsequently, in June and July, line ministries and the Planning Department ask township and district offices to formulate plan/budget proposals for the following year, which is primarily an exercise in updating and detailing the provisions for that year that are included in the Five-Year Plan. Proposals for state/region funding are reviewed by local Plan Formulation and Implementation Committees (PFICs), and then sent to the state/region line department concerned; while proposals for Union funding bypass the PFICs, and go directly to the state/region line department. DAO plan proposals also effectively bypass the PFICs and go directly to the State/Region Development Affairs Office. State/region line departments review proposals, add their own, and consolidate the proposals. At this point, the proposals are divided into two separate "streams":

Stream I: proposals for the state/region government budget. Those proposals for funding through the state/region government budget are submitted to the State/Region Planning Department (the capital investment budget), and the State/Region Budget Department (the combined budget), and these departments may make queries or adjustments. Then, in November, the budgets are submitted to the state/region government (cabinet and chief minister) for review, and possible changes. Until FY 2016/17, the "gross", un-prioritized budget proposal was then sent to the Union level, unconstrained by a budget ceiling. At this point, the Vice-President's Office and MOPF would determine the size of the deficit transfer, and inform the state/region government. With this information, the state/region government would then proceed to "cut-down" the original proposal through rounds of negotiation with the Budget Department and state/region line departments so that the budget would fit the ceiling. Then the budget would be submitted for a second time to the Union level (some states/regions apparently even undertook a third submission). Between January and March, the final submission would then be approved by the Financial Commission, Union Government, and then the Union Hluttaw, and returned to the state/region government, which in March or April would then submit the budget to the state/region Hluttaw for approval.

But in FY 2016/17, this process was modified in an important way. The Union level informed state/region governments about their grant transfer amounts earlier (in mid-November), allowing the governments to finalize their budget proposal within the ceiling, and then make a one-time submission to the Union government. However, some states/regions still made their "gross", un-prioritized submissions, as usual, and did not interpret the grant announcement as a serious ceiling for them. In FY 2016/17, the Union government also accelerated the approval timetable in order to secure both Union and state/region approvals by January 2016 (before the government that won the election in November 2015 took office).

Stream II: proposals for the Union budget. Proposals for Union line ministry budget funding are submitted to the line ministry—in some cases directly (health), but in other cases (DBE and DRD), the proposals are first shared with the state/region government for their comments or input, but not with the state/region Hluttaw. These submissions take place between August and December, depending on the department and, in some cases, seem to involve a mix of the proposals submitted by the state/region line departments that arise from the planning process outlined above, as well as more ad hoc proposals. The latter are sponsored by various actors (very important persons, members of parliament), and channeled through the state/region line departments. Each Union line ministry reviews the proposals it receives from different state/region line departments according to the ministry's criteria, and makes final approval—which usually means substantially cutting down the original list of proposals. No consultation appears to take place with the state/region government during this process, and state/region line departments say they are simply informed of the outcomes in March.

State/region expenditure outcomes by sector. Figure 4 depicts the average breakdown in FY 2016/17 of the spending of state/region governments by sector, across Ayeyarwady, Shan and Tanintharyi. Consistently, in each of the three governments, the dominant spending category is Construction (49%)—essentially roads and bridges. The second largest category is state/region government (20%), the third is Home Affairs (11%) - essentially GAD administration - then Electricity (11%), followed by DAOs (6%). These sectors are followed by very modest expenditures in Agriculture, Livestock, Fisheries, etc. Overall, administration (state/region plus GAD) accounts for almost one third of total state and region spending, with a little over two thirds on development-related expenditures.

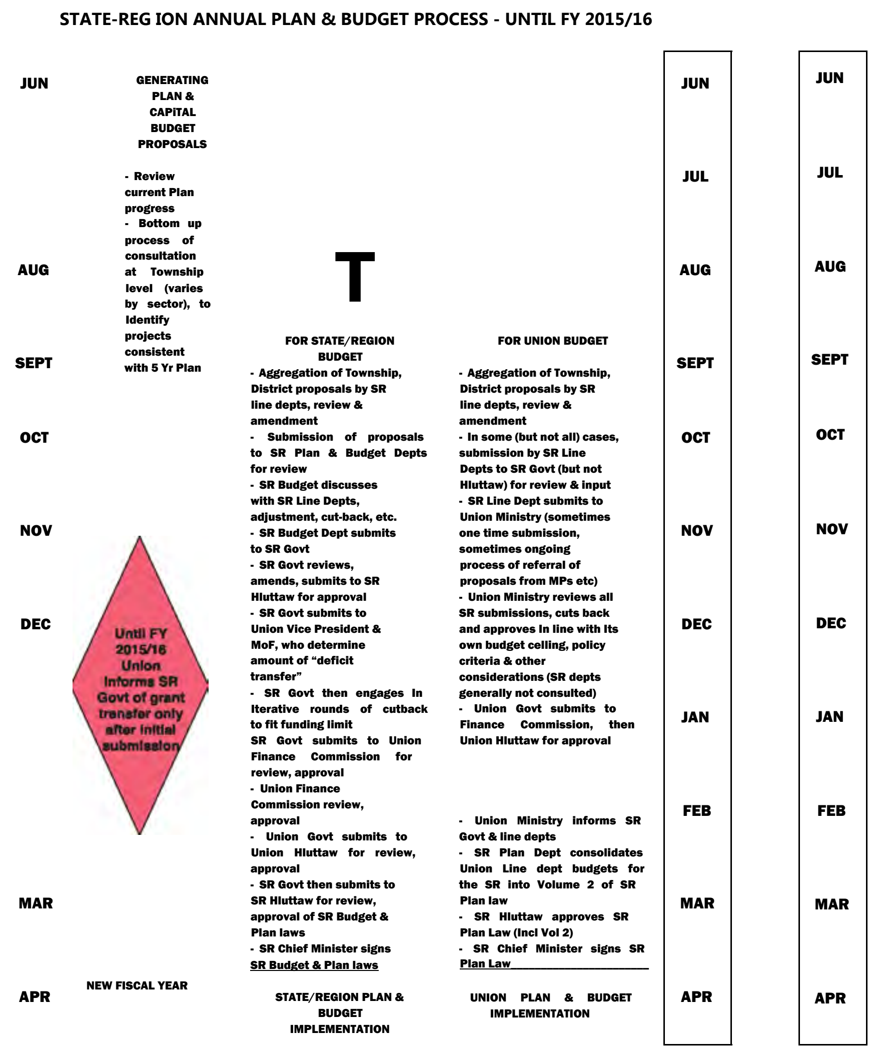


Figure 3 Annual state and region plan and budget cycle: Before and after MTFF reforms

STATE-REGION ANNUAL PLAN & BUDGET PROCESS FROM FY 2016/17

GENERATING PLAN & CAPITAL BUDGET PROPOSALS

JUN

- Review current Plan progress
- Bottom up process of consultation at Township level (varies by sector), to identify projects consistent with 5 Yr Plan

JUL

AUG

T

SEPT

FOR STATE/REGION BUDGET

- Aggregation of Township, District proposals by SR line depts, review & amendment
- Submission of proposals to SR Plan & Budget Depts for review
- SR Budget discusses with SR Line Depts, adjustment, cut-back, etc.
- SR Budget Dept submits to SR Govt
- SR Govt reviews, amends, aligns with funding ceiling - submits to SR Hluttaw for approval
- SR Govt submits to Union Finance Commission for review, approval
- Union Finance Commission review, approval
- Union Govt submits to Union Hluttaw for review, approval
- SR Govt then submits to SR Hluttaw for review, approval of SR Budget & Plan laws
- SR Chief Minister signs SR Budget & Plan laws

FOR UNION BUDGET

- Aggregation of Township, District proposals by SR line depts, review & amendment
- In some (but not all) cases, submission by SR Line Depts to SR Govt (but not Hluttaw) for review & Input
- SR Line Dept submits to Union Ministry (sometimes one time submission, sometimes ongoing process of referral of proposals from MPs etc)
- Union Ministry reviews all SR submissions, cuts back and approves In line with Its own budget ceiling, policy criteria & other considerations (SR depts generally not consulted)
- Union Govt submits to Finance Commission, then Union Hluttaw for approval
- Union Ministry informs SR Govt & line depts
- SR Plan Dept consolidates Union Line dept budgets for the SR Into Volume 2 of SR Plan law
- SR Hluttaw approves SR Plan Law (Incl Vol 2)
- SR Chief Minister signs SR Plan Law

OCT

NOV

DEC

JAN

FEB

MAR

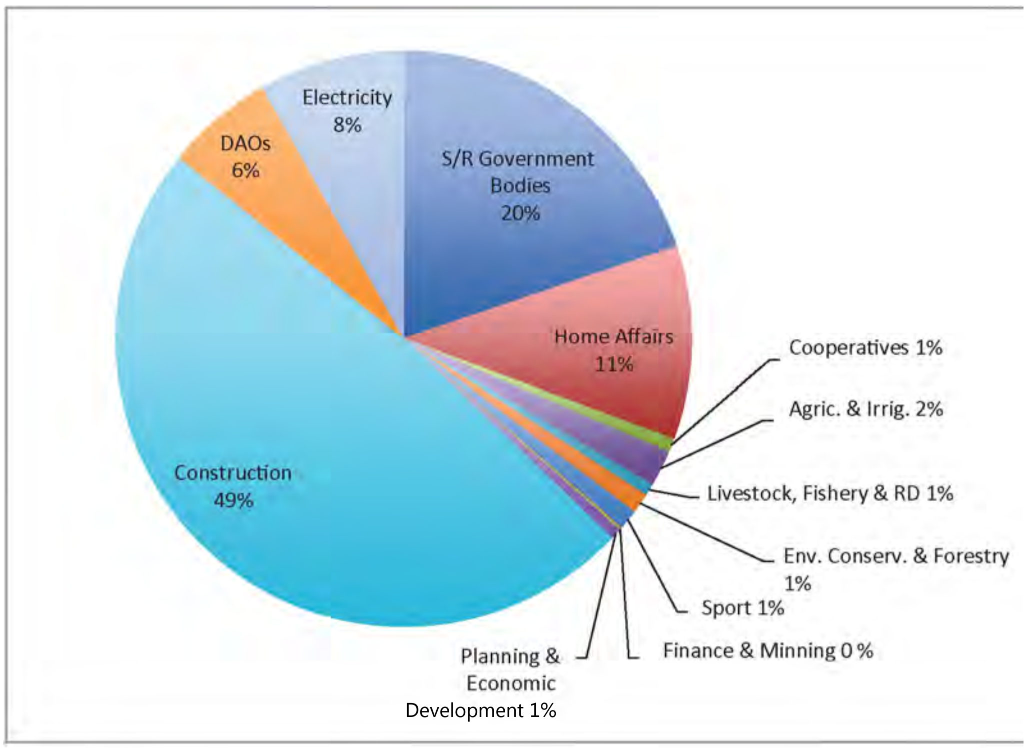
NEW FISCAL YEAR

STATE/REGION PLAN & BUDGET IMPLEMENTATION

UNION PLAN & BUDGET IMPLEMENTATION

APR

Figure 4 Average expenditure breakdown across three state/region governments (Ayeyarwady, Shan, Tanintharyi) FY 2016/17



The capital-to-current budget balance varies between 60:40 and 40:60 across the three state/region governments (although budget classification practice seems to vary).

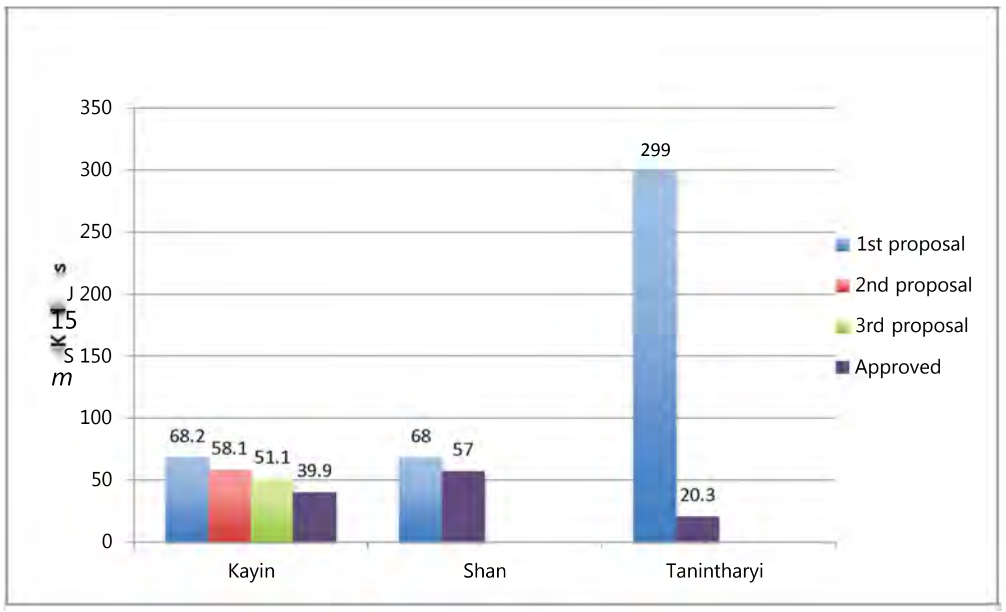
How capital expenditure priorities are determined within each sector. A number of factors come into play in determining what is, and what is not, selected for funding. As a rule, it has been necessary that all investment proposals reflect provisions already made in the Five-Year Plan, though this may change. Some individual line departments have their own technical criteria for assigning priorities (e.g. roads are sometimes rated by Average Daily Traffic data; schools are rated by three criteria—whether the school is currently unsafe, how many pupils attend the school, and the "school image"[4]). But it is not very clear how, or how consistently, such criteria are used in practice. Line departments also openly use more political criteria—proposals sponsored by "very important persons" (VIPs) or members of parliament (MPs) are officially given higher weighting. No criteria appear to be used to make any rough "net benefit" or "cost-benefit" rankings, nor to enable geographic targeting of investments to either poor areas or areas of potential (despite stated Union policy to focus on areas of deprivation).[5] Actual priorities are selected as follows:

a) Priorities for inclusion in state/region budgets. These are determined in a very short time (a matter of days, or a week or two at most) at the state/region level after the grant transfer ceiling is announced, and through negotiations between the state/region cabinet, Budget Department, and line departments (with no Hluttaw involvement). To illustrate the extent of cut-backs in three state/region governments, the percentages of road investment proposals that were actually selected were cut back to 7% (Tanintharyi), 58% (Kayin), and 84% (Shan) of the original budget submissions.

[4] This criterion was unclear, but appears to aim at factoring-in potential benefits from improved physical appearance of school facilities.

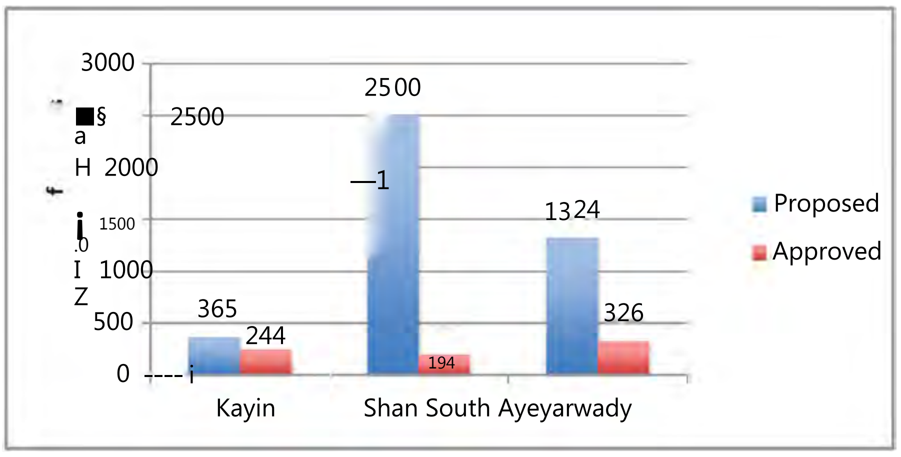
[5] For example, the national Comprehensive Education Sector Review, 2013, clearly expressed concerns about geographic and urban/rural disparities in the quality of, and access to, education.

Figure 5 Roads budgeting from department proposal to state/region approval - FY 2016/17



b) Priorities for inclusion in the line ministry budgets. This review and approval process at the Union level may take from one month (DRD) up to 4-5 months (DBE). Here too, the cut-backs are often radical: in four states/regions, the approved DBE budgets were respectively, 8%, 17%, 25%, and 67% of those proposed. In two state/region governments, the approved DRD budgets were, respectively, 18% and 48% of those proposed.

Figure 6 School investment budgeting: From state/region proposal to Union approval - FY 2016/17



Even geographic spread across townships. In the case of all subnational investments funded by either the state/region government or Union ministry budgets, there appears to be a clear bias toward "spreading" investment expenditures thinly across townships, rather than focusing on particular areas. In the case of state/region roads, for example, this means a fragmented state/region upgrading program on 1-2 kilometers of road in each township every year, rather than larger discrete investments in particular districts or townships (this incremental pattern is probably reinforced by the prevalent "force account" implementation arrangements). Similarly, DBE appears to spread school investments across all townships, regardless of relative need.

Subnational planning and budgeting issues:

A number of issues emerge from the findings discussed above:

a) "Silo"-type local planning. [6] There is no effective local institutional platform to ensure the inter-departmental review and coordination of investment proposals—for example, coordination between rural and urban road networks, or between village and township/district roads. Planning and budgeting expenditures for each of the layers of government are largely undertaken in separate departmental "silos". This can easily lead to strategic constraints and opportunities missed, and/or to duplication.

b) Lack of adequate investment appraisal criteria. Overall, it seems there are no adequate tools used to ensure consistent screening, appraisal and ranking of competing investment proposals. Those used for ranking roads (average daily traffic) or schools (the three criteria related to school size, safety and image) appear not to be applied consistently, and in any event are inadequate (e.g. not factoring in costs). More troubling still is the weighting of proposals by the status of the proponent. All this is very unlikely to ensure that approved proposals will be the most effective and efficient and with the greatest development impact. With a move towards more "bottom-up", participatory and transparent planning, arrangements for transparent screening and prioritizing of the ever-larger flow of proposals become ever more important. Operational criteria are also needed to translate policy concerns about inequitable geographic access to basic services, which characterize many sectors, to allow geographic targeting (to areas of greatest need or greater potential), and move away from the institutional bias to spreading resources evenly, but inequitably, across all townships.

c) Lack of incentives to prioritize. Lack of a known state/region budget ceiling prior to the MTFF reform has encouraged a focus on generating an inflated volume of plan and budget proposals, with no real incentive for any serious prioritization or "weeding out" at the township, district, or state/region levels. Conversely, this inflated volume has also reduced the capacity to properly formulate investment proposals that have been developed with adequate consultation, and checked, assessed, and costed. The announcement of the grant transfer amounts in November 2016 helps to address this problem, but much better communications are needed to ensure that state/region authorities realize that they now face a hard budget constraint.

d) Inadequate time. The hurried "cutting-back" of state/region budget proposals in a matter of a week or so, mainly by the state/region cabinet, Budget Department, and line department heads so that the proposals fit the level of fiscal transfer now announced in November, has inevitably been undertaken without any thorough review of the "pros and cons" of competing options. Nor has there been adequate consultation with technical staff of the departments concerned, or with stakeholders at the local level, during this process.

Passive role of the State/Region Hluttaws. The role of the State/Region Hluttaws (and their specialized public accounts or budget committees) is also limited by the very short time allotted to them for assessing proposals. Generally, they play a fairly marginal role in the state/region budget process, and none at all in the deconcentrated budget process. They do not appear to be involved very much in the critical, initial budget preparation stages where options are reviewed, and even if they are involved at this stage, they have little time and lack expertise to provide an effective review or input. The Hluttaw review and final approval of the budget, already approved at the Union level, takes place when there is little scope to make much change.

[6] An information "silo" is a management system that shares little or no information with related management systems.

Implications for the quality of subnational PFM

The various issues just identified all have direct impact on the quality of subnational PFM and, ultimately, on public service delivery. Briefly these are impacts on:

a) Effectiveness and efficiency. Overly centralized decision-making across a range of public expenditures which are eminently "local", means that the wrong priorities will often be made. Silo-based planning misses the opportunities for synergy, and often results in duplication. Own-revenue constraints limit the resources available for public expenditure. The lack of any prioritization of proposals below the state/region government level clogs up the review process and limits the time and resources needed for proper vetting, assessment, and appraisal of options. The lack of any appraisal and ranking criteria means that the options selected may often be sub-optimal (at best) and the lack of any criteria for geographic targeting, and the resulting equal spread of expenditure, is in conflict with Union Government goals to achieve equity as well as promote economic potential.

b) Equity. Inter-state/region equity is undermined by the disparities resulting from the fiscal transfer mechanism, while intra-state/region equity is undermined by the prevalent "spreading" of investments across all townships, regardless of relative need or potential.

c) Transparency and accountability. Generally, information on plans and budgets, or on the rationale for approval of particular proposals, is very hard to access, even for a researcher, and certainly not for the general public. The role of State/Region Hluttaws in budget scrutiny and review seems very limited. Not only do they have little expertise on budget matters, they have very little time to review the submissions. At the time of final budget approval, they are faced with a *fait accompli* (accomplished fact), since approval has already been given at the Union level, and they have no role in reviewing, let alone approving, budget proposals from the state/region line departments.

Possible directions for reform

Greater clarity and decentralization of expenditure responsibilities

In the short-term, there is scope to engage with selected line ministries to explore the scope for ex-ante budget allocations to their respective state/region departments, to encourage a greater degree of deconcentration of specific functions, especially in the areas of small-scale rural, education, and health infrastructure. In the medium term, though, there is an opportunity to then switch responsibility for some of these expenditures to the state/region governments, with corresponding financing and guidance. This could all be undertaken initially on a small-scale, pilot basis, but would require very close consultations with the line ministries concerned. In parallel, a process of regular reviews of the legal and regulatory framework governing these responsibilities is needed to ensure that anomalies and inconsistencies are removed.

More effective and equitable financing

a) Own-source revenues: In the short-term, measures are needed to update tax and fee rates, harmonize revenue collection and administration, and straighten out anomalies in the way revenues are recorded. In the medium-longer term, efforts are needed to create a single state/region revenue collection and administration unit. In parallel, a program of public information would help create awareness of the importance of paying tax. An ongoing effort is also needed to re-align the details in the older legal and regulatory framework with Schedule 5 provisions.

b) Revenue-sharing: It seems important to review the current basis of allocation of shared revenues back to states and regions. This is currently based on area of collection, but a more appropriate and equitable option is to consider pooling funds, along with general grant transfer funds, and simply allocate the pool by formula. As proposals for other revenue-sharing arrangements come under review (e.g. natural resource-related revenues), for which sharing by derivation may make more sense, it will be important to keep an eye on the equity implications, given the inter-regional disparities in the tax bases for such revenues.

c) Grant transfers: It is important to build on the formula-based approach, but to revise the formula so that it better reflects relative need and fiscal constraints, and reduces the current, serious disparities generated by the current formula. One possible approach is outlined which would use "need-related" variables of population (weighted 60%), poverty incidence[7] (20%), and land area (20%) - many variations are possible in these weightings, but population should be given at least 50% weight. The fiscal constraint element would be addressed in the first year or two by factoring-in actual revenue collection in the past year, but moving toward a "Representative Tax System" approach after research has been conducted on the fiscal revenue potential of each state and region. However, any change toward a more equitable formula will mean that some states/regions (mainly the more populated ones) will gain, but others will lose, relative to the current allocation pattern, so long as the total pool is unchanged.

Strengthening planning and budgeting procedures

a) Inter-sectoral coordination. Clear directions and guidance from Planning Commissions and the Ministry of Planning and Finance to township/district planning bodies to mandate more effective inter-departmental coordination, and joint appraisal of proposals regarding their wider socioeconomic and fiscal consequences and externalities.

b) The annual cycle. Review of the annual process to both identify redundant steps, but especially to create more time for the key steps of vetting, appraisal, ranking of options, etc., by the state/ region administration, and also to create more time for the Hluttaw to play a role.

c) Assigning budget ceilings. Review the scope to: (i) advance the announcement of state/region grants even earlier than November, and (ii) assign ex ante budget ceilings to state/region departments, and possibly to townships, in order to encourage more disciplined budget prioritization. This could be done first on a pilot basis, drawing on the considerable international experience.

d) Appraisal and selection tools. Devise procedures, guidelines, and tools to aid state/region departments to make more transparent and consistent appraisal of plan and capital budget options, and to better determine the likely benefit/cost outcomes. This could be done first on a pilot basis, drawing on considerable international experience.

e) Role of the Hluttaw. Devise procedures, guidelines, and tools that Hluttaws and their specialized committees can use to engage in more informed scrutiny and assessment of plans and budget proposals, including reports on budget execution. This could be done first on a pilot basis, drawing on considerable international experience.

[7] Poverty incidence index for each state/region will need to be weighted by the relative population size of that state/region.

Introduction

Report overview

This report builds on a substantial body of recent work on subnational governance and public finance commissioned by The Asia Foundation and other agencies,[8] and aims to explore these issues further. The study looked at the overall constitutional, institutional, and financing framework for subnational public expenditure, at the processes for financing, planning, and budgeting, and at the actual outcomes with regard to priorities actually funded or not funded. Particular attention was paid to documenting and understanding how capital investment planning and budget priorities are determined both for sectors which now fall under state/region authority, and for those which remain under Union authority, notably the Department of Basic Education (DBE) and the Department of Rural Development (DRD).

The report is structured as follows:

- Section A provides a reminder of the rationale for decentralizing certain expenditure responsibilities and then provides an account of current subnational expenditure mandates (and hence planning and budgeting responsibilities) in Myanmar.
- Section B examines the mechanisms for financing these responsibilities, the financing outcomes of these mechanisms, and the implications for subnational PFM.
- Section C examines procedures for subnational planning and budgeting, roles and timetables, and then expenditure outcomes and the manner in which investment budget priorities are determined.

Each of these three sections begins with some general principles and issues on the topic, then outlines research findings, and concludes by highlighting a series of issues of broader policy concern in Myanmar, which emerged from the findings.

- Section D of the report sums up the implications of these findings, and of the issues identified, for the quality of subnational planning and budgeting, and then provides some recommendations for both Union and state/region governments, and for development partners.

Study approach

This report is based on research that was conducted over the period from April to July 2016. The research included:

- A review of the existing documentation on subnational governance and public financial management, and on service delivery in key sectors, including several key reports published by The Asia Foundation.
- A number of field visits in Myanmar. These included visits to Nay Pyi Taw and, most importantly, to Shan and Kayin States and to Ayeyarwady and Tanintharyi Regions—in all of which, the study team had extensive meetings with government officials at state/region, district, and township levels.

[8] Much of this literature has been commissioned by The Asia Foundation and MDRI-CESD, and most notably: (1) Hamish Nixon, et al., *State and Region Governments in Myanmar* (Yangon: The Asia Foundation and MDRI-CESD, 2013), which outlined the complex state/region subnational government institutional structures, their roles and relations with the Union Government; (2) Hamish Nixon and Cindy Joelene, *Fiscal Decentralization in Myanmar: Towards a Roadmap for Reform.* Discussion Paper 5 (Yangon: The Asia Foundation and MDRI-CESD, 2014), which outlined the rationale for a greater degree of fiscal decentralization and a road map for achieving this; and (3) Giles Dickenson-Jones et al. *State and Region Public Finances in Myanmar* (Yangon: The Asia Foundation and MDRI-CESD, 2015), which outlined subnational government revenue powers and trends, and their expenditure patterns. It also complements a recent review commissioned by the Japanese International Cooperation Agency (JICA): Giles Dickenson-Jones et al. *Intergovernmental Fiscal Relations in Myanmar: Current Processes and Future Priorities in Public Financial Management Reform* (Yangon: MDRI-CESD and Japan International Cooperation Agency, 2016).

The study team was able to obtain a relatively large number of planning and budgeting documents which were generously shared by several State/Region Budget and Planning Departments, and also by the Construction, Rural Development, and Basic Education Departments at the subnational level.

Limits of this report: a clarification

A final introductory remark is needed to clarify what this report is, and what it is not.

The modest aim of this report is to outline the current arrangements for the financing, planning, and budgeting of public investments at the state/region level; to identify a number of issues arising in these arrangements which appear to undermine the quality of local PFM and hence of local service delivery; and to suggest some specific areas for reform (including a greater, but still modest, degree of decentralization in some specific areas). The hope is that this may inform wider discussion of some of the important issues of policy, procedure, and practice.

This report does not aim to provide an exhaustive account of the arguments for or against 'decentralization' (for which there is a very extensive, albeit rather inconclusive body of international literature). Nor does this report aim to provide any kind of prescriptive road map to 'decentralization' in Myanmar (whatever that might mean). All of this would require far more ambitious and complex research and consultation. This would also probably not be very helpful.

In Myanmar, as everywhere, the practical policy challenge is not to press for 'wholesale decentralization' but rather to carefully determine the appropriate balance of inter-governmental responsibilities for individual public services, recognizing that certain responsibilities are best handled centrally, while others may be better handled locally, and then determine how best to finance and manage these responsibilities.

A. State and Region Expenditure Responsibilities

In this section the rationale for decentralizing certain expenditure — and hence corresponding planning and budgeting — responsibilities are reviewed. The section starts with some general considerations before looking at the assignment of responsibilities to state and region governments in Myanmar.

A.1. Preamble: General principles and issues

A.1.1. Finance follows function

The question of expenditure or functional assignments between levels of government is a very important one for several reasons:

- First, if the functional assignments of different levels of government for public services are unclear, then activities may be duplicated at different levels, or simply not undertaken at all, which undermines the efficiency of service delivery.
- Second, if functional assignments for public services are made at the wrong level, that is, 'local functions' are handled too centrally, or 'national functions' too locally, then the effectiveness, efficiency, and equity of public service delivery may also suffer.
- Third, it is very hard to hold any level of government accountable if the legal provisions about 'who is responsible for what' are vague, or contradictory. This problem of unclear expectation is faced in many places, and especially in some of the former socialist 'transition' countries.
- Finally, the critical first step in designing the intergovernmental fiscal framework is to determine which functions should be undertaken by each level of government, and therefore what the *expenditure responsibilities of each level* will be. Only when this is clear can the system of revenue assignments be designed, revenue sharing, and center-local fiscal transfers, to ensure that expenditures are adequately financed.

A 'golden rule' of public finance and inter-governmental fiscal relations is that 'finance follows function'. In other words, it can only be *after* the determination of functional spending assignments for each level, that it makes sense to determine policy on the revenues and the fiscal transfers needed by each level.

Box 1 'Finance follows function' - a cardinal rule

> "First should come the assignment of expenditure responsibility to local governments, and then the assignment of revenue responsibility should be determined. This is an important rule, for two reasons. The first is that the central government must establish expenditure needs for each level of government before tackling the question of revenue assignment. The second is that the economically efficient assignment of revenues requires knowledge of expenditure assignment. For example, services that may be priced (e.g. public utilities) should be largely financed by user charges; general services with a local area benefit should be financed by local taxes; and goods or services characterized by significant externalities should be financed by region-wide taxes and inter-governmental transfers. Governments must settle on the assignment of expenditure responsibilities to local governments [...] before they can choose an efficient mix of taxing and fiscal transfers."
>
> Roy Bahl *Implementation Rules for Fiscal Decentralization,* Working Paper 9901. International Studies Program, School of Policy Studies (Atlanta: Georgia State University, 1999).

Of course, it is also true that all too often subnational governments in many countries are given quite clear functional spending mandates but *not the required revenue powers or fiscal transfers* to meet these. This is the common problem of 'unfunded mandates', found in both industrialized countries and in the developing world. This, in turn, can result in spending responsibilities that are not carried out, or in deficit spending or excessive borrowing by local authorities.

A.1.2. Reasons for decentralizing

The potential benefits of a greater degree of fiscal decentralization in Myanmar have been argued elsewhere.[9] Very briefly, though, allowing local control of expenditures on *certain* local public goods and services may achieve the following *potential* benefits:

- Effectiveness (or allocative efficiency): Better tailoring of plans and budgets to local priorities, especially for those 'local' public goods and services associated with the needs and preferences that vary between states and regions (and often between the townships within them), and hence for which there is great value in ensuring that local knowledge and preference are fed into plan and budget allocation decisions. Decision-makers in Nay Pyi Taw may more effectively plan for major national public investments or for those sorts of national program which suit a uniform design. But these Union-level officials cannot be expected to assess the relative options for, or the merits of, different possible local school, road, or water investments any better than state/region, district, or township people. Indeed, although they may be professionally better qualified, Union officials lack the sort of 'fine-grained' local knowledge that such assessments and decisions require.

- Efficiency: Ensuring that budget implementation is undertaken more efficiently if the agency or firm mandated to execute investments is under local control, and where time delays, resource-wastage, or other forms of abuse can be much more easily spotted and addressed. Additional efficiency is gained as local control can ensure that linkages between different investments and activities are identified, simply because the control span is much narrower at the local level. Possible synergies can be leveraged (e.g. the linking of complementary public health education activities and investments in improved water supply, or of investments in the tertiary and secondary road networks in the same area); and wasteful overlaps can be identified and avoided (e.g. the possible duplication of water supply investments in the same village by different agencies).

- Equity: Better ensuring that local differences in need are properly taken into account, and that 'standard' packages are not provided uniformly across states/regions or townships, regardless of differing contexts and needs.

- Transparency and accountability: Better ensuring that plan and budget decisions are made more transparent and accountable. When local officials are made responsible for decisions, information should be more readily available to the public, and complaints or opinions should be much more easily communicated by local citizens and would-be users, and much more likely to be heard and acted upon, and much less easily deflected.

It must be stressed though that these are all potential and not automatic benefits, and are subject to adequate capacities and accountability arrangements being in place.

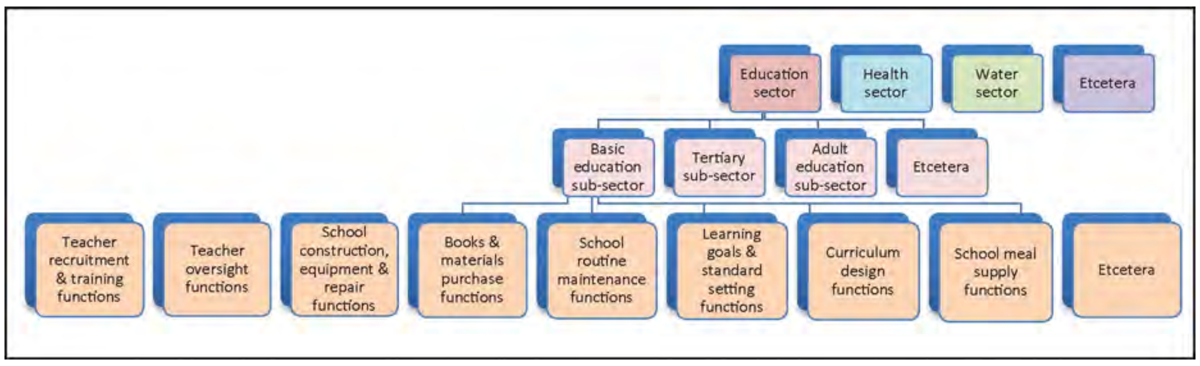
A.1.3. The importance of being clear and specific

The issue is not whether whole sectors (health, education, roads) should be decentralized—instead it needs to be specific, and to 'unbundle' each sector. For example, education is a *sector,* comprising various *sub-sectors or services,* such as basic education. The basic education *service,* in turn, comprises an array of very different *tasks or functions* that can include: setting curricula, exams and teaching standards; hiring, managing and paying teachers; in-service training of teachers; determining school design standards; building, equipping, maintaining, and repairing schools; purchasing school books;

[9] For example, Nixon and Joelene *Fiscal Decentralization in Myanmar.*

preparing school meals; undertaking school inspections and much more. The question then becomes which of these functions might best be managed at the subnational level.

Figure 7 'Unbundling sectors' into functions: The education sector as an example



The key point here is that some of these functions may best be handled locally, but others will be better handled by the central government. Consequently, the 'decentralization vs. centralization' discussion should focus on specific *tasks or functions,* not on whole services, let alone entire sectors. This unbundling is usually simpler for public services which are infrastructure-based such as roads, but can be very complex for education or health services where there are important human resource and input supply dimensions, with many complex functions involved.

A.1.4. Determining whether responsibilities might be decentralized[10]

The next step is to map out how these various functions are *currently* assigned by each level or agency of government. This will require a review of current legislation and regulations for specific sectors and services. The objective of this exercise should be to generate a 'map' of currently prescribed functions against levels or agencies of government. Using such a matrix, it is then possible to identify any problem areas (those which are unclear, inconsistent, excessively fragmented, etc.) and see whether the function is better handled more centrally or more locally.

The guiding principle is that of 'subsidiarity'. As far as possible, the level of government responsibility should correspond to the population catchment area benefitting from a particular service. This means that:

- Responsibility for services which serve large population catchment areas should be located at higher levels of subnational government or with the central government, depending on the size of the country. This could include, for example, universities and national museums.
- Responsibility for services which serve small, local population catchment areas should be located with lower-level subnational governments corresponding to those local populations. This could include, for example, kindergartens, primary/secondary schools, and rural water supplies.

But there are important exceptions to the subsidiarity principle:

- *Externalities and spillovers:* There are instances where service delivery decisions in one area directly or indirectly affect the population in another area. For example, the delivery of immunization services in one region, but not others, may affect neighboring populations through the risk of spreading illness. Similarly, the construction of a new provincial hospital may reduce demand for

[10] A good review of the methodological issues in this section is provided in "Functional Assignment in Multi-Level Government, Vols 1 & 2", GTZ, 2009.

the services of an already under-used hospital in a nearby small province, and/or it may increase the number of patients referred up to the national hospital, choking its capacity. In such cases, overall responsibility for the provision of functions may be better assigned to a higher, even central, level to ensure that these consequences are taken into account when planning and managing that service.

- *Economies of scale:* There may be some functions which generate economies of scale and so can be handled more cost-effectively at a higher level. For example, organizing teacher training, or procuring school books, or administering teacher payroll processes.
- *Equity and national uniformity:* There is always a trade-off between the desire to allow local choice and the need for national uniformity and equity. Concern for national uniformity and equity usually means that broad policy and standard setting functions should be assigned to the central government. Similarly, where the service in question must be delivered in a standard fashion, or according to a fixed 'protocol', then *if it is decentralized* to subnational levels, it is best done through a delegated arrangement, allowing no variation between localities. For example, if responsibilities for birth and death registrations, or for immunization were decentralized, this would best be done through *delegation,* and not through *devolution.* It would *not* be desirable for each subnational government to devise their own procedures and certificates for civic registration, or to determine which vaccines to administer and how.

Lastly, a common misconception should be noted. The own-source revenue capacity of subnational governments should *not* be a factor in determining whether to assign functions to them or not. In other words, when functional assignment issues are under discussion, it is sometimes said that a particular expenditure responsibility cannot be entrusted to the local level because that level does not have adequate fiscal resources. But this is to turn the logic of public finance around. If, for reasons of efficiency, responsiveness, and local accountability, it is believed to be appropriate to assign a function to the subnational government, then the central government must ensure some form of fiscal transfer to compensate for the inevitably limited local revenues. Again, 'finance follows function'.

This is not to say that all public expenditure responsibilities should be decentralized, which is quite the contrary. Very many expenditure responsibilities, along with most policy and regulatory functions are best handled at the central level. However, in regard to expenditures on a specific range of local public goods and services, decentralization of responsibility can potentially greatly improve the effectiveness, efficiency, equity, and accountability of their planning, budgeting, and delivery.

A.2. What are subnational expenditure responsibilities in Myanmar?

Box 2 Two main forms of decentralizing expenditure responsibilities[11]

- 'Devolved' expenditures: These are expenditures which are formally mandated as state/region responsibilities, are financed within state/region budgets, from the state/region's own revenues, and therefore, are supposedly subject to final approval by state/region authorities. This is the most important set of decentralized responsibilities for two reasons: (i) since it involves full local control, it potentially allows the greatest potential benefits in the quality of decision-making and public service delivery; and (ii) it requires that states/regions have adequate financing from their budgets.

- 'Deconcentrated' expenditures: These are expenditures undertaken within the states/regions, but financed from the Union ministry budget and with Union revenues. However, state/region line departments (and even state/region governments) have some degree of input or control over planning and budgeting. Thus, strictly speaking, referring to these as 'deconcentrated' expenditures in the current Myanmar context is misleading. State/region line departments have virtually no discretionary authority over local ministry spending in Myanmar.

A.2.1. "Devolved" expenditure responsibilities in Myanmar

The legal mandates

It is conventional to point to Schedules 1 and 2,[12] of the 2008 Constitution as setting out the respective expenditure mandates of Union and state/region governments. However, for several reasons, it must be said that these schedules do not provide a very clear basis for distinguishing their mandates:

The content of these two schedules is often vague and inconsistent, and key service functions are not always explicitly assigned to either level. To illustrate, neither education nor health are mentioned at all in Schedule 2, and even Schedule 1 does not provide much guidance:

- Section 9 of Schedule 1 only refers to Union Education responsibilities as comprising "(a) Educational curricula, syllabus, teaching methodology, research, plans, projects, standards; (b) Universities, degree colleges, institutes and other institutions of higher learning; (c) examinations prescribed by the Union; (d) private schools and training..." In other words, there is no explicit mention in either Schedules 1 or 2 of responsibilities for basic education schooling which is a key education sub-sector and which accounts for the great bulk of the education budget. Due to lack of any explicit mention, it seems to be assumed that the intent is Union-level responsibility.
- Similar inconsistency applies to the treatment of health. Schedule 1 hardly mentions the provision of basic health services at all.

    Other critical sectors such as the environment appear to get no mention at all in either schedule.

- Indeed, strictly speaking, Schedule 2 simply does not appear to intend to define state/region service functions or mandates per se:

- Article 188 of the 2008 Constitution states that "the Region or State Hluttaw shall have the right to enact laws [....] related to matters prescribed in Schedule 2 ..." This seems to suggest that the two schedules intend to distinguish between the spheres of policymaking, legislative, and regulatory competence of the Hluttaws at the Union and subnational levels, rather than between areas of

[11] There is a third way of decentralizing expenditure responsibility through "Delegation", but this does not usually account for a significant share of subnational expenditures.

[12] See Annex 1 for Schedule 2 of the 2008 Constitution.

their functional or expenditure responsibility.

- This is supported by the language of Schedule 2 which often appears to be 'circular'. For example, with regard to roads, irrigation, and electricity, Schedule 2 indicates state/region responsibilities as being for roads and bridges, dams and irrigation works, and electricity generation and distribution ".having the right to be managed by the Region or State". It must therefore be inferred that these constitutional schedules are not intended to be the final arbiter for subnational mandates, and that other legislation or convention needs to be looked to.

There are currently some proposed amendments to Schedule 2 of the Constitution, which if approved, and subject to subsequent Union legislation, could expand the scope of state/region responsibilities. Although, again, the proposals appear to conflate regulatory responsibilities with expenditure responsibilities.

Box 3 Proposed amendments to Schedule 2

Current proposed amendments would seem to allow state/region authorities to intervene in a range of new areas, including:

- *Hotels and tourism*
- *Small scale mining and mineral extraction*
- *Industrial zones*
- *Renovation and development of water courses and resources*
- *Air transport*
- *Basic education schools*
- *Private clinics and hospitals*
- *Social relief and rehabilitation*

However, even if approved, all this is subject to Union legislation in each case. Moreover, it is not clear if the emphasis is primarily on empowering states/regions with regulatory oversight, or on also mandating them with some public expenditure responsibilities in these areas.

The mandates in practice

Whatever the regulatory basis may be, in practice, the actual devolved functions seem to be very limited indeed. Looking at how state/region governments actually spend money (see also Section C.4), these expenditures come down to capital and current expenditures associated with:

- The state/region government's own administrative apparatus (Hluttaw, Court, etc.).
- The General Administration Department (GAD) of the Ministry of Home Affairs, which ensures general government administration from the state/region, down through the district, township, and ward/village tract levels.
- The state/region road and bridge network (as distinct from the Union roads and bridges in states/regions) as so classified by the Department of Construction.[13]
- Development Affairs Organizations (DAOs), which finance urban roads, waste disposal, and water systems.
- Off-grid electric power and distribution.
- Minor expenditure functions in support of agriculture and irrigation, environmental protection, forestry, etc.

[13] To illustrate, in Ayeyarwady, there are 77 state roads (equiv. to 1,872 km), versus 14 Union roads (equiv. to 709 km); in Kayin, there are 34 state roads (equiv. to 1,090 km) versus 22 Union roads (equiv. to 852 km).

A.2.2. 'Deconcentrated' expenditure responsibilities in Myanmar

A wide range of expenditures are also undertaken within the state/region but managed by subnational offices of Union line ministries, and financed from the Union budget with Union revenues. Although these expenditures are not subnational responsibilities, and are not included in state/region budgets (and not subject to review and approval by state/region Hluttaws), they are determined to a greater or lesser degree by the subnational planning process. To illustrate:

- Education. The Ministry of Education budget for basic education (school investments, salaries, maintenance, etc.) in each state/region is finalized and approved at the Union level, but this is based on annual capital and current budget proposals and priorities from the State/Region Education Department, as well as proposals from other actors.
- Rural Development. Similarly, the Ministry of Livestock, Fisheries and Rural Development budget for rural infrastructure, capacity-building, etc. is finalized and approved at the Union level, but is also based on annual capital and current budget proposals from the State/Region Rural Development Department.

The budgets of other Union ministries (Health, Agriculture and Irrigation, etc.) are similarly shaped to a greater or lesser degree by proposals from their state/region departments.

A.3. Expenditure assignments: Issues arising

A.3.1. Inconsistencies in application and other anomalies

In actual practice, the distinctions between even the rather unclear devolved mandates outlined in the 2008 Constitution are not always consistently applied. Generally, there are a number of anomalies in the institutional responsibilities for key sectors such as:

Roads and bridges

The national road network (as in most countries) is classified by 'levels' as follows:[14]

- A primary Union highway network (some 19,500 km) is under the authority of the Union Highways and Bridges Departments of the Ministry of Construction.
- A secondary network of district and township roads (some 16,000 km) is supposedly under the responsibility of state/region governments through the State/Region Highways and Bridges Departments of the State/Region Departments of Construction.
- A tertiary rural network of village roads and tracks (some 82,000 km) is mainly under the authority of the Union-level Department for Rural Development. In border areas, the Ministry of Border Affairs also appears to assume responsibilities.
- A tertiary urban road network within the cities and towns (some 27,000 km) is under the authority of DAOs, or of the Yangon, Mandalay, or Nay Pyi Taw City Development Committees.

That there are such different institutional planning and expenditure responsibilities for different 'layers' of the road network is quite normal. However, in Myanmar, some challenges arise. Although the 'layers' of the network seem to be clearly defined, responsibilities appear to be mixed or shared in practice. To illustrate:

- In Tanintharyi, some 60% of the FY 2016-17 region investment budget for roads (total of MMK

[14] Details reported are based on a Ministry of Construction presentation on the national road network, and on discussions with senior officials from the Departments of Highways and Bridges at the Union Ministry of Construction.

20.3 billion) was actually allocated to expenditure on Union highways in the region.[15]

- In a similar manner, the Department of Rural Development in Kayin State indicated that on occasion, it co-financed road investments in sub-townships because DAOs, which are nominally responsible for these roads, lacked the resources to complete their projects.

This practice may be seen as evidence of pragmatism and flexibility. But there are two serious risks from such blurring of responsibilities: (a) it becomes impossible to estimate clearly the expenditure responsibilities of each institutional level, and hence to design appropriate mechanisms to finance these responsibilities; and (b) it can easily lead to avoidance of managerial or political accountability for inadequate investment or poor management and maintenance.

Electricity

State/region governments sometimes assume responsibility for investment in electricity generation and transmission networks in urban areas which are not connected to the national power grid. However, it appears that the current budget responsibilities for operating and maintaining these networks lie with the Union Electricity Department. This split between investment and current expenditure planning and budgeting responsibilities risks undermining the efficient allocation of resources and getting the right spending balance between the creation of new assets and the operation and maintenance of existing assets.

That aside, even the investment budgeting responsibilities for electricity are split. While investment in the urban areas is handled by the State/Region Electricity Department, investment in electricity distribution in rural areas lies mainly under the authority of the Union-level Department for Rural Development,[16] although in some border townships, the Ministry of Border Affairs also engages in investments in rural power.

There is certainly a rationale for maintaining a separation between expenditure and planning responsibilities for the national power grid and local off-grid power systems. But, among others, the fragmented functional responsibilities within the local off-grid system, risk undermining the coherence and efficiency of planning and budgeting within the state/region, and encouraging duplication and overlap, and inconsistent standards. This problem is compounded by 'silo-type' planning at the local level.

A.3.2. High degree of centralization

Only very modest devolved mandates…

Despite provisions of the 2008 Constitution for the establishment of a subnational government tier at the state/region level, Myanmar remains a highly centralized country, where the Union government still controls the majority of all spending decisions related to the delivery of public goods and services, and an even greater share of national revenues. The potential benefits of a greater degree of fiscal decentralization in Myanmar have been argued elsewhere.[17] Overall, apart from the inconsistencies and anomalies in expenditure responsibilities noted above, the extremely limited devolution is striking. So is the very high Union-level control over certain public expenditures and, by extension, over the corresponding planning and budgeting functions which could be much better handled at the

[15] When this apparent anomaly was raised during this study, it was said that "Union highway infrastructure investment is a top priority for the region and the regional budget also needs to be supportive of these strategic priorities". The Union Department of Highways confirmed that such expenditure on the Union road network in state/region budgets is quite common practice.

[16] DRD is implementing the rural off-grid electrification component of a major program funded by the World Bank—the National Electrification Project.

[17] See, for example, Nixon and Joelene *Fiscal Decentralization in Myanmar*.

subnational level. For example:

- The sorts of small-scale rural infrastructure funded by DRD (village roads and tracks, village water supplies, solar electricity installations, etc.) are all small-scale investments. Their 'impact area' lies well within a township, and often even within a single village tract area, and for these there are generally no wider indirect impacts which might require 'higher level' review and approval, as suggested under A.1.4.
- Similarly, in the social sectors, individual school and health facility investments (new, renovated, or expanded facilities), where local knowledge is key to setting the right priorities and making decisions would be more appropriately mandated to the subnational level. However, the responsibility for education and health policy matters, or for staff payroll management and many other functions, is usually best retained by the Ministries of Education and Health at the Union level.

Indeed, in most countries such small/medium investment expenditure functions are decentralized to subnational governments with a much smaller population than even the township level in Myanmar (average population, 150,000), and are often closer to the population size at the village tract level. Table 3 provides an illustration of some responsibilities assigned to the lowest local government tiers elsewhere in Asia.[18] In all cases, these tiers in Myanmar, are: (a) smaller units (in population size), and (b) have far fewer government officials (i.e. 'weaker staffing capacities') to handle planning and oversight, than do townships (let alone states or regions).

Table 3 Illustration of devolved investment mandates elsewhere in Asia

Nepal Local Self-Governance Act (1999)	Bangladesh Union Parishad Act (2009)	Kerala State - India State Local Government Act (1994)	Cambodia Law on Commune & Sangkhat Administration (2001)
Village Development Committees [av. pop. 10,000]	*Union Parishads [av. pop. 27,000]*	*Gram Panchayats [av. pop. 25,000]*	*Communes [av. pop. 8,000]*
- drinking water - primary education facilities - primary health facilities - village roads - village irrigation	- rural roads, culverts - wells, water pumps, tanks, ponds - irrigation and drainage works - street lighting	- pre-primary, primary & upper primary schools - dispensaries and hospitals - rural water supply - waste disposal - public toilets and bathing places - day care centers	- village roads & bridges - village water supplies - village irrigation - primary school facilities - primary health care facilities

Av. pop. = average population

...and little deconcentration of budget authority.

Similarly, the degree to which Union line ministries allow their state/region departments any

[18] A review of the mandates of higher subnational levels in these countries—such as District Development Committees in Nepal, Upazila Parishads in Bangladesh, the District Parishads in Kerala, etc.—reveals a much larger set of functions assigned to those levels.

discretionary authority over budgets also seems very limited. Indeed, no Union ministry appears to genuinely 'deconcentrate' much budgeting authority, and all continue to withhold final budget allocation and approval under their own authority. This review found no case where a Union ministry actually allocates an investment budget to its state/region department directors, or allows them full subnational discretionary authority.[19]

The procedures whereby subnational ministerial departments undertake planning and budgeting will be explored in more detail under Section C.

A.3.3. Unclear institutional accountabilities

Lastly, aside from the lack of division of expenditure responsibilities between Union and subnational levels, there is also an issue about the accountabilities of subnational sector departments in regard to these two sets of responsibilities.

In each state/region, there are some 20-25 Union ministerial departments. As noted above, several of these departments (e.g. Construction, Electricity, Fisheries) are engaged in planning and managing expenditures, both for the state/region government, as well as for their Union ministry. With the exception of the state/region Ministries of Development Affairs overseeing the DAOs, the heads and staff of all these departments are Union officials who are primarily under Union ministry control. Although these departments do have a formal reporting line to one of the state/region ministers, the fact that their departmental accountability is primarily to their Union ministry may lead at times to some conflict of interest and loyalty. Thus, for example, if the Union Construction Ministry places high priority on improvement of a Union highway in the state/region, but has insufficient budgetary resources, there may be understandable pressure on the State/Region Construction Department head to energetically argue for the state/region government to use its funds for the Union highway. This, thereby, moves resources away from the state/region highway investments that the state/region government is supposed to deliver. Similarly, where the department is short-staffed or otherwise constrained, it is possible that Union responsibilities will be accorded greater priority than state/region responsibilities.

If there is to be greater decentralization of responsibility to state/region governments, these accountability issues will need to be addressed to ensure that both the state/region government and its Hluttaw can exact greater accountability from the various line departments concerned.

[19] The Union Ministry of Education suggested to this study team that it allocates 'budget ceilings' to State/Region Departments of Basic Education at the start of the annual budget cycle, indicating a degree of deconcentrated budget authority. However, interviews with State/Region Education Departments, and analysis of plan proposals and approvals, indicated that this was not the case. The Department of Rural Development comes closest to assigning budgetary authority to the subnational level, but even here the final budget allocation decision, and final approval of expenditures, rests at Union level.

B. How are Subnational Expenditures Financed

In the preceding section subnational expenditure responsibilities are examined. In this section, the arrangements for financing these expenditures, and their implications are examined, starting with some general considerations and then looking at subnational financing in Myanmar and issues arising.

B.1. Preamble: General principles and issues[20]

There are two sources of financing for subnational government (SNG) expenditure responsibilities: i) own-source revenues, and ii) fiscal transfers. Borrowing or use of capital markets to raise extra revenues is not really an option for subnational governments in developing countries, with the exception of the governments of large, prosperous metropolitan areas.

B.1.1. Own-source revenues: Always limited

These revenues are derived from: *non-tax revenues* such as water user charges, market or business license fees, or fines; and *tax revenues,* such as property tax, land tax, personal and business taxes, or taxes on trade. But in most countries, subnational governments have extremely limited own-source revenues, and there are essentially two reasons for this.

First, as a rule, subnational governments are assigned only modest revenue-raising powers. This is largely for good economic reasons. Economic principles dictate that subnational governments should not be assigned revenue sources that are likely to vary greatly between regions, such as import duties, taxes on large business entities, or on natural resources. Further, they should not be assigned revenue sources that may discourage production and trade, or cause businesses to move to avoid a local tax. Similarly, it is important to avoid assigning local taxes that are hard to collect, that are more efficient to collect at a national level, that are not stable, or are not likely to increase as local incomes increase. Second, central governments will always be reluctant to give away control of revenue sources, even the property tax, which is in principle considered a good candidate for a local tax.

B.1.2. Addressing the 'vertical gap': Need for fiscal transfers

There is, then, a *basic structural issue* for subnational governments in most countries—that is that the level of spending which they are expected to undertake far exceeds the level of revenue which they can raise locally. This basic asymmetry leads to what is known as the 'vertical gap'. In order to fill this 'vertical gap' central government has to provide 'fiscal transfers' - through revenue sharing and/or grants.

Box 4 The essential asymmetry of center-local fiscal relations and the fiscal gap

> Almost everywhere, the volume of expenditures that can desirably be decentralized to subnational authorities is inevitably much greater than the volume of revenue that is technically or politically feasible to decentralize to subnational authorities. This creates a fiscal gap that needs to be 'filled' by a fiscal transfer. Exactly how this fiscal transfer is designed is critical.

Inter-governmental revenue sharing

In many countries, certain taxes are shared between the central government and subnational governments. The actual collection of the tax may be by either level. In many countries, there is a

[20] General coverage of the issues in this section can be found in: "The Oxford Handbook of State and Local Government Finance", ed. Ebel & Petersen, 2012; "Handbook of Fiscal Federalism", ed. Ahmad and Brosio, 2006; "Inter-Governmental Fiscal Transfers: Principles & Practice", ed. Boadway and Shah, World Bank, 2007.

range of such shared taxes: income and payroll taxes, value added tax, fuel taxes, and natural resource taxes. Generally, subnational governments are allowed discretion in the use of these revenues. In principle, any national tax could be shared, although it only makes sense to do so for taxes of some significant size, and for which it is feasible to assign the shared revenue to a specific subnational government. As with locally assigned revenues, a key guiding principle for avoiding major inequities, is that revenues shared between the national and subnational levels are from tax bases that do not vary much across SNGs.

There are two key 'variables' in a revenue sharing mechanism: (a) the proportion of the tax revenue that is assigned to subnational governments, and (b) whether this is shared with subnational governments according to where it was generated—that is, by 'area of derivation'—or whether it is pooled and shared by a formula.

Finally, it is worth noting a variant on revenue-sharing: 'piggybacking'. This is when subnational governments apply extra percentage points on a national tax or fee, which they then retain, or which is remitted to them by the central government for their own use. Where the subnational government establishes the rate for this surcharge, then this is effectively a local levy, or own-source revenue. Where, instead, the rules for the surcharge are set by the central government, then it approximates a form of inter-governmental transfer.

Inter-governmental fiscal grants

A second, and often the major approach to close the 'vertical gap', is through fiscal grant transfers to subnational governments. These transfers can be of several kinds.

Box 5 Typology of grant transfers

- *Unconditional, general purpose, or block grants.* These are transfers to subnational governments for a range of expenditure types mandated to subnational governments, and that usually allow them a degree of flexibility in their use. In almost all countries with subnational governments, there is some general grant of this type. The great value in such transfers is that—thanks to their discretionary nature—these transfers are a very strong incentive for local participation and consultation in determining how they should be used.
- *Equalization grants.* These are transfers to subnational governments that aim to compensate for varying own-source revenue capacities and to 'equalize' total fiscal resources across subnational governments. Very often, however, this policy goal is implemented via block grants.
- *Conditional, categorical, or sector grants.* These are transfers to subnational governments that are tied to a subsector such as basic education, or even to specific services or functions within a service, such as school meals or girls' scholarships, and these grants allow very limited flexibility. Whether such grants are established, depends on the degree to which specific service delivery functions have been devolved, and corresponding line departments are placed under subnational government control.
- *Other targeted transfers.* These are transfers to subnational governments that are often of a more ad hoc nature. Examples include transfers to address the specific problems of selected remote or poor areas, to address short-term unemployment, or to deal with the aftermath of a natural disaster. Typically, these funds can only be used for centrally prescribed expenditures.
- *Cost-reimbursement transfers.* These are transfers to offset the costs of delegated functions, such as registering births, and where reimbursement is made to subnational governments on an 'as is' basis, or according to unit cost guidelines. Therefore, there is hardly any flexibility in the use of such funds.

In addition to determining how the funds should be used, there are two other key 'design variables' to be established for each kind of grant transfer: (a) how much money should be allocated in total to the fund 'pool', and (b) how the resulting 'pool' of funds should be distributed across subnational governments. For the latter, the logic will depend on the *purpose* of each type of grant or transfer.

Block or equalization grants will need to be guided by considerations of general equity, though weighted by the relative need or poverty of different areas. For these grants to ensure such equity, allocation should be governed largely by the relative population sizes of subnational governments—something that is often under-appreciated. Allocations may be further adjusted, by simple measures of relative poverty, providing that updated and reliable data are available.

The other issue that attracts less attention, but is equally important, is exactly how in the annual government budget the *total pool for each grant* is constituted. Clearly these grant pools should reflect some estimate of the desired aggregate levels of expenditure for each instrument. For example, the pool for a grant for rural water supply improvements should reflect the total desired levels of expenditure for rural water supply. This, in turn, might be based on the central ministry's historic levels of spending for rural water supply, prior to decentralization of this function. However, in practice, all too often these are residual allocations, determined after the central ministries have gained their shares of the overall budget 'cake'. They also vary considerably and unpredictably year-by-year, thus creating uncertainty for subnational governments, and undermining local planning and budgeting for a critical service such as water supply.

Other center-local fund flows

Finally, it should be noted that aside from these sorts of fiscal transfers from the central government to subnational governments, there are a number of other fiscal flows from the center to localities. The three main ones are:

- Central sector ministries may transfer very substantial funding to their subnational units, or even right down to the school or hospital level to cover the costs of administration and service delivery. These flows will usually dwarf the volume of transfers to subnational governments.
- In a number of countries, constituency funds are transferred to the local accounts controlled by national members of parliament. This allows MPs to spend on local development.
- Donor agencies and non-government organizations also often transfer funds to local project management units.

When these funds are managed outside of the subnational government's planning and budgeting framework, as they often are, they can cause serious inefficiencies, inequities and overlaps, and undermine SNG accountability.

B.2. Own-source revenues in Myanmar

In this section, the state/region own-revenue sources, how revenues are recorded, the patterns and trends, and key issues arising are examined.

B.2.1. Own revenue sources

Budget account format

Before exploring own-source revenues, it is important to look at the accounting format used by state/region governments to record revenues. This is divided into three parts (denoting the state/ region entities to which revenues accrue), and four columns (denoting the type of revenues accruing to each entity).

Table 4 State/region budget format for classifying revenues

State/region Collecting Entity	Tax Receipts	Other Current Receipts	Capital Receipts	Receipts from Union
Part 1 State/region government entities				
Part 2 State/region departments (GAD, Forestry, etc.)				
Part 3 State economic enterprises				
TOTAL				

Within this format, Parts 1 and 2, and Tax Receipts, Other Current Receipts, and Receipts from the Union contain the most significant own-source revenues for states/regions. By contrast, state economic enterprise (SEE) revenues and revenues under the capital account seem to be negligible.

Part 1: State/region government revenues

'Part 1' of the budget report refers to those revenues that accrue to the various branches of the state/ region government (the Administration, Hluttaw, Court, etc.), rather than to the various ministerial departments in the state/region. In Shan State, for example, these include: revenues associated with various fees (e.g. for border crossings and for forms of access to Inle Lake); charges, fines, etc. levied by various state/region entities; and Other Current Receipts accruing to state/region government, e.g. from special projects, development zones, etc.

Table 5 Shan State part 1: State-government current revenues

Current receipts - BE FY 2016/17	MMK millions
State Administration	10,417.0
Hydropower fees	3QQ.Q
Border Crossing Fees	3QQ.Q
Muse Development Project	5,700.0
Inle Zone Collection Fees	1,500.0
105 Registration from Hotel Zone	1,800.0
Cherry Myaing Construction Project	765.Q
Other Revenue (water Source, irrigation, TV)	52.0
State Hluttaw	-
State Court	100.0
State Attorney General	0.6
State Auditor General	0.6

Total Part 1 State government own-revenues	**10,518.2**

However, 'Part 1: Other Current Receipts' also seems to include fiscal transfers from the Union government. The 15% share of commercial and special goods tax allocated to the Shan State government in FY 2016/17 is recorded under 'Other Current Receipts' (not under 'Union Receipts'), and is then totaled along with the various own-revenues listed in Table 5. In the case of Shan State, this was MMK 1,400 million, which somewhat misleadingly increased the 'current receipt' total to MMK 11,918 million, together with various ad hoc transfers from the Union government (other than the main fiscal 'deficit' transfer, recorded under 'Part 2')—something which is potentially confusing.

Other transfers seem to be properly recorded under the Receipts from the Union column of 'Part 1': e.g. the Constituency Development Fund. However, the budget data on state/region own-revenues which are provided by the Intergovernmental Fiscal Relations Division (IFRD) appear to 'net out' the fiscal transfers provided to the Budget Department under 'Part 2', but still include the various Union transfers and revenue-sharing, which are recorded as revenues for the various branches of the state/ region government under Part 1. In other words, while clearly recorded as transfers in individual state/ region budgets, these transfers seem to be included within IFRD's aggregation of all state/region own-revenues.

Part 2: State/region departmental revenues

States and regions raise own-revenues through levying various taxes, fees, and charges, and through the miscellaneous sale or rental of various assets, goods, and services. These are collected by individual departments, and are recorded under 'Part 2'.

Taxes, fees and charges

The tax and fee-raising powers of state/region governments are set out in Schedule 5 of the 2008 Constitution:

Box 6 Schedule 5 of the 2008 Constitution: Taxes and fees collected by region or state

1. Land revenue.
2. Excise revenue.
3. Water tax and embankment tax based on dams and reservoirs managed by the Region or State and tax on use of electricity generated by such facilities managed by the Region or State.
4. Toll fees from using roads and bridges managed by the Region or State.
5. Royalty collected on fresh water fisheries and on marine fisheries within the permitted range of territorial water.
6. Taxes collected on vehicles on road transport and vessels on inland waterway transport, in accord with law, in a Region or a State.
7. Proceeds, rent fees and other profits from those properties owned by a Region or a State.
8. Fees, taxes and other revenues collected on services enterprises by a Region or a State.
9. Fines imposed by judicial courts in a Region or a State including Region Taya hluttaw or State Taya hluttaw and taxes collected on service provision and other revenues.
10. Interests from disbursed by a Region or State.
11. Profits returned from investment of a Region or State.

12. Taxes collected on extraction of the following items from the forests in a Region or a State: on all woods except teak and other restricted hardwoods; on firewood, charcoal, rattan, bamboo, birdnests, cutch, thanetkha, turpentine, eaglewood and honey-based products.
13. Registration fees.
14. Taxes on entertainments.
15. Salt tax.
16. Revenue received from the Union Fund Account.
17. Contributions by Development Affairs Organisations in a Region or State concerned.
18. Unclaimed cash and property.
19. Treasure trove.

By implication, Schedule 5 clearly indicates that states/regions have no powers with regard to income, profit, or sales tax revenues (although there is limited sharing of some of these revenues). Of the current Schedule 5 revenue sources, the most significant are generally Property and Wheel taxes (collected by DAOs), and Excise and Land taxes (collected by GAD). Depending on local context, natural resource-related taxes such as those on forestry (collected by the Forestry Department), or on fisheries (collected by the Fisheries Department) may also be important.

However, there are a number of potentially important proposed amendments to Schedule 5, which (if approved) could greatly expand the range of state/region revenue powers, subject to subsequent Union legislation.

Box 7 Current proposed amendments to Schedule 5

States/Regions shall be empowered to raise taxes and fees related to the following activities "in accord with the law enacted by the Union": "*Investment, Insurance, income, trading, customs, hotels & lodging, tourism, registration of documents, coastal fisheries, petroleum & natural gas, minerals & mines, gemstones, teak and hardwoods, industries, boat construction, air transport, housing, private education establishments, private clinics, literature, films & videos.*"

Other current receipts

States/region departments are also empowered to raise a variety of other revenues through lease or sale of assets and other goods and services. By far, the most important of these other current revenue sources are those managed by the DAOs and, of these, revenues from various license auctions (markets, slaughterhouses, ferries, etc.) constitute the bulk. Combined, these other current sources constitute the bulk of all state/region own-source revenues, and greatly outweigh tax revenues.

State/region governments also raise some revenues from the disposal of capital assets, which are recorded under 'Capital Receipts', but these proved negligible in the four state/region governments included in the study.

B.2.2. Own-source revenues: Patterns and trends

Own-source revenue composition

The table in Annex 2 illustrates the composition of own-source revenues for three states/regions. A few features stand out:

- Tax revenues constitute the minor share of all own-source revenues, accounting at most for 44% of all state/region revenues in Ayeyarwady, but as little as 20% in Shan. The composition of these tax revenues varies considerably, with natural resource-related and excise tax revenues playing an important part, but with land tax revenues being very modest.

- The bulk of all own-source revenues are non-tax current revenues, of which the great part is collected by DAOs. DAOs collect from 54% of all state/region own-source revenues in Ayeyarwady, and 78% of all revenues in Shan.

Trends in total own-source revenues

Table 6 portrays the trends in own revenues over the past five years for all state/region governments. As noted earlier, these 'own-source revenues' are somewhat inflated by inclusion of some ad hoc transfers, project financing revenues, and shared revenues.

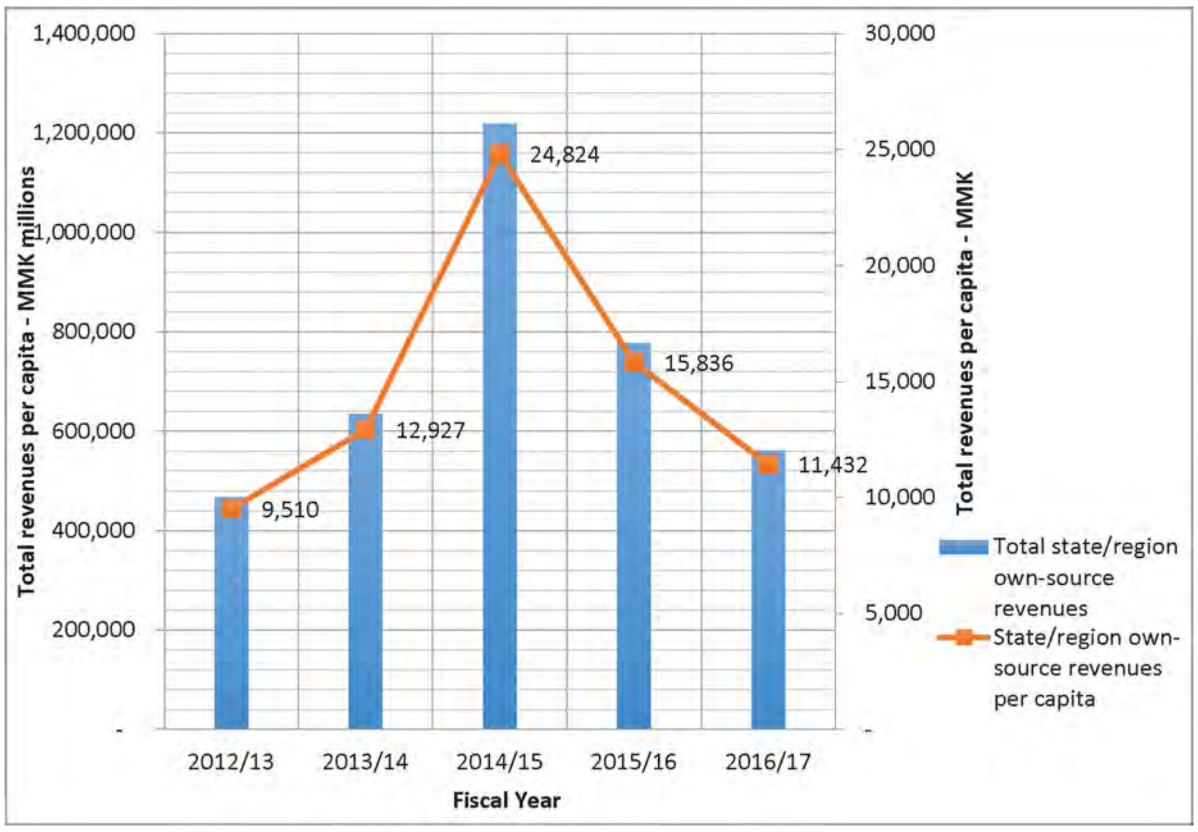
Table 6 State and region own-source revenues - MMK millions

State/Region	2012-13 Actual	2013-14 Actual	2014-15 Provisional Actual	2015-16 Revised Estimate	2016-17 BE
Ayeyarwady	41,377	54,929	82,221	27,136	20,544
Bago	19,315	31,443	50,289	36,288	22,251
Chin	8,649	13,921	45,246	7,170	1,713
Kachin	19,318	28,597	117,380	14,996	11,721
Kayah	3,564	11,190	11,312	7,135	2,194
Kayin	10,424	16,434	35,660	8,218	4,718
Magway	33,730	37,686	71,197	19,987	14,112
Mandalay	59,810	82,641	124,718	136,987	112,567
Mon	14,799	21,549	30,121	12,831	8,306
Rakhine	20,164	26,072	48,783	11,759	6,857
Sagaing	33,437	48,114	79,461	26,465	21,842
Shan	48,398	78,365	145,161	43,591	33,293
Tanintharyi	17,389	20,429	64,573	9,021	6,034
Yangon	136,767	163,597	313,205	416,289	295,361
TOTAL	467,142	634,967	1,219,325	777,872	561,512

Source: Data from the Budget Department, MOPF.

What is quite striking in Table 6, is the almost three-fold increase in total own-source revenues from FY 2Q12/13 to FY 2Q14/15, but then the sharp decline in FY 2Q16/2Q17, such that total revenues in this fiscal year are not much more than they were in FY 2Q12/13. Figure 8 illustrates this trajectory very clearly—both in regard to total own-source revenues (left axis), and also to the average levels of own-source revenues per capita (right axis).

Figure 8 Trends in state/region own-source revenues



Source: Data from the Budget Department, MOPF.

This increase and then decline seems to have affected all states/regions to a greater or lesser degree. It appears that there are two main explanations for this 'spike':[21]

First, until 2015, the Ministry of Construction had a separate Public Works Department at Union and state/region levels, which oversaw the Roads and Bridges Construction Enterprises deployed across the states/regions. Road and bridge expenditures in the Highways and Bridges Departments are generally implemented by these enterprises and, consequently, are also recorded as revenues for these enterprises. Supposedly, in FY 2014/15, there was a sharp expansion in state/region construction expenditures (probably due, in part, to the establishment of state/region administration facilities, housing, etc., as provided for in the 2008 Constitution) and, consequently in the revenues recorded by the state/region Public Works Departments. In 2015, however, the Public Works and Highways Departments were merged, and the Roads and Bridges Construction Enterprises were folded into the Highways and Bridge Department budgets, such that road and bridge expenditures were no longer recorded as enterprise revenues. In other words, the apparent spike in state/region own-revenues is largely the result of a change in accounting arrangements.

Secondly, it also appears that a number of special transfers were made to some states/ regions in FY 2014/15 due to various natural disasters that occurred that year. Given the practice of recording them under 'Part 1' of the state/region budget, and that the Union Budget Department included these in the estimates of state/region own-revenues, this may also have contributed to the apparent 'spike' in own-revenues that year.

Another possible reason might be that the sharp increase in fiscal transfers over the last 2-3 years has led to a reduction in own-revenue collection incentives and effort by states/regions over the past 2

[21] Based on discussions with Union Ministry of Planning and Finance staff.

years. However, in this study, it was not possible to explore this hypothesis.

Trends and variations in per capita own-source revenues

It is revealing to translate these own-source revenues into *per capita terms.* State/region governments vary hugely in economy, size, and population, and so their own-source revenue bases will also be expected to vary accordingly. Examination of own-source revenues *per capita* helps to provide a more meaningful basis for comparisons over time and across states and regions. Table 7 shows that behind the overall trends noted in the previous section, there are also very substantial differences in the levels of own-source revenue per capita - over the 5-year period, and across states/regions.

Table 7 Own-source revenues per capita - MMK millions

State/Region	2012-13 Actual	2013-14 Actual	2014-15 Provisional Actual	2015-16 Revised Estimate	2016-17 BE
Ayeyarwady	6,690	8,881	13,294	4,388	3,322
Bago	3,968	6,460	10,332	7,455	4,572
Chin	18,064	29,074	94,498	14,974	3,577
Kachin	11,759	17,407	71,449	9,128	7,134
Kayah	12,435	39,042	39,465	24,892	7,656
Kayin	6,929	10,925	23,705	5,463	3,136
Magway	8,611	9,621	18,176	5,102	3,603
Mandalay	9,700	13,403	20,228	22,217	18,257
Mon	7,204	10,489	14,662	6,246	4,043
Rakhine	9,607	12,422	23,243	5,603	3,267
Sagaing	6,279	9,035	14,921	4,970	4,102
Shan	8,309	13,455	24,923	7,484	5,716
Tanintharyi	12,347	14,505	45,848	6,405	4,284
Yangon	18,581	22,226	42,551	56,556	40,127
Average	9,510	12,926	24,823	15,836	11,432

Source: Data from the Budget Department, MOPF.

Not surprisingly, Yangon generates high levels per capita, although in some years other states/regions have generated even higher levels - e.g. Chin, Kachin, and Kayah have recorded exceptionally high levels in some years, notably in FY 2014/15. These high levels may have been due to various factors: to the issue related to accounting for revenues of the construction enterprises noted earlier; to revenues associated with special development zones (as seen for Shan in FY 2016/17); to misclassification of some fiscal transfers which spiked that year; or to some sort of 'windfall' revenues, e.g. sale of state assets.

Table 8 depicts the variance in own-source revenues per capita—variance that has steadily increased over the five years, despite the recent decline in average levels. Thus:

- In FY 2012/13, the lowest level of own-revenues per capita was MMK 3,968 (Bago), and the highest was MMK 18,581 (Yangon)—a Max:Min ratio of 4.7.
- In FY 2016/17, the lowest level of own-revenues per capita is MMK 3,136 (Kayin), and the highest is MMK 40,127 (also Yangon)—a Max:Min ratio of 12.8.

Thus, over the 5-year period, the spread between the lowest and the highest per capita levels has increased by three times.

Table 8 Variance in own-source revenues per capita - MMK millions

MIN/MAX	2012-13 Actual	2013-14 Actual	2014-15 Provisional Actual	2015-16 Revised Estimate	2016-17 BE
MINIMUM VALUE	3,968	6,460	10,332	4,388	3,136
Lowest three	*Bago*	*Bago*	*Bago*	*Ayeyarwady*	*Kayin*
	Sagaing	*Ayeyarwady*	*Ayeyarwady*	*Sagaing*	*Ayeyarwady*
	Ayeyarwady	*Sagaing*	*Mon*	*Magway*	*Rakhine*
MAXIMUM VALUE	18,581	39,042	94,498	56,556	40,127
Highest three	*Yangon*	*Kayah*	*Chin*	*Yangon*	*Yangon*
	Chin	*Chin*	*Kachin*	*Kayah*	*Mandalay*
	Kayah	*Yangon*	*Tanintharyi*	*Mandalay*	*Kayah*
MAX: MIN RATIO	*4.70*	*6.00*	*9.00*	*12.90*	*12.80*

Source: Data from the Budget Department, MOPF.

The reasons for the very substantial variations and the increasing spread of per capita revenues between states and regions are unclear, especially given the anomalies in revenue classification. But two issues need to be noted:

- What these variations mean is that different states/regions enjoy very different abilities to finance their expenditure mandates from their various 'own-source revenues'. It therefore lies with the Union government to ensure that such differences are, as far as possible, 'leveled' through fiscal transfers in order to ensure the necessary equity in subnational public financial resources and basic service delivery.
- At the same time, it would also be very helpful if the states/regions' own-revenue classification was amended, in order to more clearly distinguish between what are genuine 'own revenues' and what are various other transfers or shared revenues from the Union level. This would make for more effective monitoring and design of fiscal transfer arrangements by the Ministry of Planning and Finance.

Composition of Per Capita Own-Source Revenues

There are significant variations between states/regions in the composition of own-source revenues raised per capita. Shan State recorded notably low tax revenues per capita, but more than compensated by much higher other revenue collection efforts, and especially by the very high levels of revenues accruing specifically to the state government (largely associated with a number of special development zones in the state, where Chinese funding is very significant).

Table 9 Own-source revenues per capita: Composition - MMK billions (FY 2016/17)

Type of Revenue	Ayeyarwady	Shan	Tanintharyi
State & Region Gov't Revenues	18	1,806	93
Dept. Tax Revenues	1,223	540	1,253
Other Dept. Own Revenues	1,573	2,186	1,846
Total Own-source Revenues	2,814	4,531	3,192

Source: State/region Budget Departments

These differences may be due to structural variations in their respective revenue bases, or to different levels of collection effort/efficiency, or to both.

B.3. Fiscal transfers in Myanmar

The Union government has used a number of fiscal transfer instruments to help address the vertical fiscal gap faced by state/region governments. Table 10 provides an overview of the current instruments in FY 2016/17, the basis for their allocation between states/regions, and how they are recorded as revenues in state/region budgets:

Table 10 Types of fiscal transfer

Type of Transfer	Basis of Allocation between States/ Regions	How Recorded under State/Region Budget Account	FY 2016/17 Total Pool MMK millions
Grant Transfers			
General purpose 'deficit grant' (longstanding)	Both pool & allocation now rule-based (previously Union discretion or negotiation)	Part 2 - Dept. of Budget: Receipts from the Union	1,688,220
Constituency Fund Grant (longstanding)	MMK 100 million per township	Part 1 - State/Region Hluttaw: Receipts from the Union	33,00
Various ad hoc grants for disasters etc.	Ad hoc	Depends on the implementing department	NA
Sharing of Union Tax Revenues			

Commercial Tax (net of tax on imported goods) shared with the state/region government (begun FY 2016/17)	15% by state/region of collection	Part 1 - State/Region Administration: other Current Receipts	134,183
Special Commodity Tax (net of tax on imported goods) with the state/region government (begun FY 2016/17)	15% by state/region of collection	Part 1 - State/Region Administration: other Current Receipts	79,282
Individual Income Tax (currently shared with DAOs, but from Sept 2016 to be shared with the states/regions)	5% by township of collection	Part 2 - DAO: Other Current Receipts (but in future will be recorded under Part 1 - State/Region Administration)	28,634
Stamp Duties on 3 instruments (currently shared with DAOs but from FY 2017/18 with states/regions)	2% by township of collection	Part 2 - DAO: Other Current Receipts (but in future will be recorded under Part 1 - State/Region Administration)	8,683

Source: Union Budget and Internal Revenue Departments

Other grant instruments (such as the Regional Development and Poverty Alleviation Fund, the Township Development and Management Fund, the Green Emerald Fund, etc.) have been in place for one or more years since 2012, but have been discontinued as of FY 2016/17.

B.3.1. Union tax sharing with states/regions

In several Asian countries (for example in Lao PDR, Vietnam, the People's Republic of China, Mongolia, and the Central Asian states) revenues are shared in multiple ways between the national and subnational governments. Such sharing can provide important sources of subnational revenue, but are sometimes very complex, can create problems of transparency, efficiency, and horizontal equity, but can be hard to reform. However, in Myanmar, happily, very few taxes are shared from the Union level down to the subnational governments and arrangements are quite simple.

Commercial and special goods tax sharing

Box 8 Union Tax Law (2016)

'Commercial taxes' are to be levied as 5% of the sales price for all goods sold, and as 3% of the sales price for buildings.
'Special goods taxes' are to be levied on a range of 'special goods' (tobacco, alcohol, timber, fuel, vehicles, etc.) at varying rates (Note these rates are to be levied on the total value of the sale, including excise tax); on a range of commercial services, at rates from 3% to 5%; and on a range of export items, at rates from 5% to 50%.

Starting in FY 2016/17, 15% of the commercial tax and special goods tax collected by IRD for the Union government is being shared with state/region governments. IRD will share these revenues by putting them into the State/Region Fund account, and the revenues will be recorded among 'other current receipts' in 'Part 1' of the Budget. These funds are not 'earmarked'—they can be used by the state/ region governments as they wish, within their legal expenditure mandates. This sharing applies to taxes on domestically traded goods and services, and excludes tax revenues on imported goods. Sharing with states/regions is undertaken on the basis of 'derivation'—i.e. according to the state/ region where the taxes were collected.

Table 11 Revenue sharing with states and regions - MMK billions - FY 2016/17

State/Region	Commercial Tax Sharing (15%)	Special Goods Tax Sharing (15%)	Total
Ayeyarwady	1,050.000	461.755	1,511.755
Bago	1,211.517	52.500	1,264.017
Chin	1,035.000	-	1,035.000
Kachin	1,065.000	0.540	1,065.540
Kayah	71.075	-	71.075
Kayin	357.500	0.695	358.195
Magway	2,741.963	15.250	2,757.213
Mandalay	4,195.334	382.236	4,577.570
Mon	325.711	5.800	331.511
Rakhine	985.238	0.880	986.118
Sagaing	2,397.732	1,059.000	3,456.732
Shan	2,031.000	330.000	2,361.000
Tanintharyi	819.324	51.225	870.549
Yangon	115,896.762	76,922.193	192,818.955
TOTAL	134,183.156	79,282.074	213,465.230

Source: Data from the Budget Department, MOPF.

When compared to grant transfers, which are examined in the next subsection, the sharing of these tax revenues is of little significance for most states and regions in changing revenue patterns. This is not surprising since the total pool allocated in FY 2016/17 is only MMK 213 billion—only 12% of the grant transfer pool of MMK 1,700 billion. However, in the case of Yangon Region, the shared revenue of MMK 192.8 billion dwarfs the grant transfer of MMK 40.9 billion. This is simply because the great bulk of commercial and special goods tax revenues are generated in Yangon.

This policy initiative is new, and so the procedures are not yet well defined. In the first year of implementation (FY 2016/17), the process for tax sharing was as follows:

- By November 2015, actual tax revenue data for FY 2014/15 were compiled by each State/Region Internal Revenue Department and sent to the Union IRD (actual data for FY 2015/16 were not yet complete at that time).
- The Union IRD subtracted the import tax element for each state/region, computed the 15% share of the net amount, and submitted the sharing proposal for each state/region to the Union Budget

Department for approval (since sharing by the Union IRD is recorded as an 'expenditure', it needs this approval).

- After approval, the Union IRD then transfers the amounts approved to each state/region fund account on a quarterly basis.

Other Union tax sharing with the local level

Currently, the Union IRD shares two types of taxes with the municipal DAOs: i) 5% of income tax revenues from taxes on individuals, not businesses, and ii) 2% of the stamp duty,[22] which is levied on three specific transactions: conveyances, gifts, and mortgage deeds. Based on derivation, these revenues are also shared with the township where they are collected.

Table 12 Revenue sharing with DAOs through states and regions - MMK billions - FY 2016/17

State/Region	Income Tax 5 %	Stamp Tax 2%	Total
Ayeyarwady	355.000	115.448	470.448
Bago	265.104	93.160	358.264
Chin	16.000	0.975	16.975
Kachin	155.390	55.000	210.390
Kayah	32.820	16.950	49.770
Kayin	78.390	20.300	98.690
Magway	235.596	70.735	306.331
Mandalay	6,452.101	1,512.886	7,964.987
Mon	297.120	138.400	435.520
Rakhine	60.364	-	60.364
Sagaing	369.003	12.326	381.329
Shan	1,077.606	455.553	1,533.159
Tanintharyi	278.823	91.120	369.943
Yangon	18,960.526	6,100.000	25,060.526
TOTAL	2B,633.B43	B,6B2.B53	37,316.696

Source: Data from the Budget Department, MOPF.

These shared revenues constitute a relatively small portion of total revenues for the DAOs that were included in this study,[23] although they may be relatively much more important for large urban DAOs, or for the Yangon, Mandalay, and Nay Pyi Taw Development Committees, where income tax revenues are much more significant than in smaller towns.

[22] This sharing of stamp duty has distant origins, starting with the 1920 Rangoon Development Trust Act which mandated such sharing in the, then, Rangoon municipal area. This was extended to Mandalay in 2009, and across all DAOs nation-wide in 2014.

[23] For example, in FY 2016/17, shared revenues account for less than 4% of total revenues for all DAOs in Ayeyarwady, and some 6% for Dawei Township.

As with other DAO revenues, this is recorded as current revenue in the state/region government budget, but so far has been effectively 'firewalled' only to finance DAO expenditures.

However, these arrangements are changing. It was recently announced that both shared revenues are about to be transferred directly from the Union IRD to the state/region government account, and are no longer earmarked for DAOs. This change has already taken effect (as of September 2016) for income tax revenues. The new arrangement for stamp duty revenues will take place in FY 2017/18.

B.3.2. General 'deficit' grant transfers

From deficit transfers to formula-based grants: The legacy

Previously, in Myanmar, general grant transfers from the Union level to state/region governments were conceived as 'deficit financing', similar to arrangements in a number of other countries across Asia and elsewhere, and notably the former socialist countries. Indeed, transfers are often still referred to as 'deficit transfers', despite the changes which have recently been made. See the section *Move to formula-based grants.*

Under this model, state/region governments made an annual submission of their projected expenditures and their (inevitably lower) projected revenues to the Union government. The Union government then reviewed these proposed budgets and the associated 'financing gaps', and determined, given the total funds available for this purpose, to what extent it could provide funding to each state/region government to cover these gaps. The extent to which these gaps could be covered was typically a result of applying various norms, based on historical precedent (maintenance of capital, current or inter-sectoral ratios, technical cost norms, etc.) but also of lobbying by various agencies and individuals.

Superficially, this may appear to be a reasonable approach to covering the vertical fiscal gap, but it actually causes major problems for the quality of subnational PFM since, for lack of a clear up-front budget ceiling, state/region governments:

- Have little incentive to make adequate effort to forecast or mobilize own-source revenues, in the hope that they can offset this through greater transfers;
- Have an incentive to inflate their expenditure proposals, in the hope that a longer list of proposals will attract a larger volume of transfers;

- Relatedly, have little incentive to make difficult local prioritization decisions, which can be difficult for subnational authorities (since it means refusing some and accepting other local proposals), given that the responsibility for setting the budget constraint lies at the Union level.

There are also further problems:

- The cumulative outcome of many different bilateral 'gap-filling' financing agreements can be unpredictable and may result in greatly varying levels of revenues and expenditure per capita across states/regions, so that the overall outcomes are inequitable.[24]
- Insofar as the Union government also determines which specific expenditures will, and will not be financed, then it may do so with very imperfect knowledge of the local context, and the relative merits of different options, resulting in budget outcomes which are ineffective and/or inefficient.
- The process itself is prone to a lack of transparency and, at least a perception of, arbitrariness and

[24] Here it should be noted that, despite suggestions made elsewhere that there is some correlation between grant transfers and the poverty or GDP levels of states and regions, there are, in fact, serious equity issues emerging from these allocations in Myanmar over the years. These are examined further in this section.

favoritism,[25] which can erode overall faith in the system.

All these problems have manifested in Myanmar, and have seriously compromised the effectiveness, equity, and efficiency of subnational PFM.26

The move to formula-based grants

Since FY 2015/16, under the Medium-Term Fiscal Framework (MTFF) being adopted as part of broader public financial management reforms, the Union government has been moving towards a 'rule-based' financing model, inspired by international best practice.

Determining the total pool

First, the annual total fiscal transfer pool was determined for FY 2015/16 and, accordingly, was set at MMK 1,706 billion. Then, for FY 2016/17, this total transfer pool was increased by a factor of 1.077 to follow the expected 7.7% annual growth of Gross Domestic Product (GDP), thereby increasing to MMK 1,787 billion. This total represents the sum of both general grants and shared commercial tax revenues to be provided to state/region governments. Given that the commercial tax sharing resources were estimated at MMK 98.17 billion, the pool for general grants is therefore MMK 1,688 billion, which is rather less than in FY 2015/16. For FY 2017/18, it is unclear what the annual growth factor will be, and whether it will apply to the entire pool, or only to the grant transfer element. That aside, this pre-determination of at least the grant transfer pool has the great advantage of allowing stability and predictability for both Union and state/region governments.

The allocation formula

Secondly, starting in FY 2015/16, allocations from the pool to state/region governments are now rule-based, rather than based on the more ad hoc and negotiated arrangements which prevailed earlier. The use of a formula aimed at reflecting both relative expenditure needs and fiscal constraints has proceeded in phases:

The method used

The criteria outlined above are used to determine allocations to state/region governments as follows:

- Step 1. For each state/region:
  - For needs-related criteria, the value for each criterion is divided by the average value for all states/regions for that criterion.
  - For fiscal constraint-related criteria, the inverse of the value for each criterion is divided by the average value of the inverse for all states/regions for that criterion.
  - Then, the average value is computed across each of these six ratios.

- Step 2. The total pool is then divided among states/regions according to their relative average ratios for the six criteria previously listed in the box. This provides the estimated total transfers to each state/region.

[25] Here it should be noted that, despite suggestions made elsewhere that there is some correlation between grant transfers and the poverty or GDP levels of states and regions, there are, in fact, serious equity issues emerging from these allocations in Myanmar over the years. These are examined further in this section.

[26] Similar problems have been widely documented in many other (especially socialist) countries where deficit-financing transfers have long been a key element in inter-governmental fiscal relations. See for example: (1) Bird, R. et al., Eds. *Decentralization of the Socialist State: Intergovernmental Finance in Transition Economies* (Washington, DC: World Bank, 1995); (2) Jorge Martinez-Vasquez & Jameson Boex *Budgeting & Fiscal Management in Transition Countries,* WP 00-6, Andrew Young School of Policy Studies (Atlanta: Georgia State University, 2000); (3) E-D Norris et al. Eds "Making Decentralization Work: The Case of Russia, Ukraine and Kazakhstan", Conference Paper, *Fiscal Decentralization* (Washington, DC: International Monetary Fund, November 2000); and (4) World Bank "Kazakhstan - Reforming intergovernmental fiscal relations", Public expenditure review (PER). Report No. 33709-KZ (Washington, DC: World Bank, 2006).

• Step 3. From the estimated total transfer amount, the state/region share in commercial tax revenue is subtracted, and the difference is the amount to be provided as a general deficit grant.

This use of an allocation formula is also a major advance, and provides potential for much greater equity and transparency. However, as the formula is currently constructed, there are a number of serious problems that arise, suggesting the need for review and further development of the formula approach. See *Fiscal transfers: Issues.*

Box 9 Development of the grant transfer formula [27]

The criteria used in FY 2015/16 were:

- State/Region Population - based on the national population census, 2014 (Development Needs).
- State/Region Poverty Index - based on the Integrated Household Living Condition Assessment, 2009/10 (Development needs).
- State/Region per Capita GDP - based on Planning Department estimates (Fiscal Constraint).

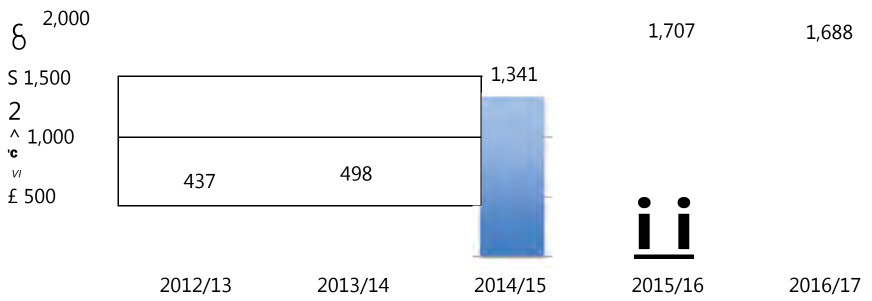
Then in FY 2016/17, three more criteria were added:

- State/Region Land Area - based on the national population census, 2014 (Development needs).
- State/Region Urban Population as a percentage of the total state population - based on the national population census, 2014 (fiscal constraint).
- Per Capita tax collection - based on the actual tax revenue collected in the fiscal year N-1 (Fiscal constraint).[27]

The trends and patterns in grant transfers

As Figure 9 illustrates, from FY 2012/13 to FY 2015/16, the total volume of fiscal transfers has increased by 4 times, though the level has now stabilized at around MMK 1,700 billion. This is equivalent to an increase in per capita transfers from MMK 8,897 (FY 2012/13) to MMK 34,370 (FY 2016/17), or from $7.4 million to $28.6 million.

Figure 9 Trends in total grant transfers, all states and regions - MMK billions



Source: Data from the Budget Department, MOPF.

Figure 9 and table 13 provide details of allocations to state/region governments over the past five years.

[27] FY N-1 denotes the fiscal year preceding the fiscal year (FY N) for which the grant is to be allocated.

Table 13 Trends in total grant transfers and their variance - MMK billions

State/Region	*Pop.*	2012/13 PA	2013/14 RE	2014/15 BE	2015/16 BE	2016/17 BE
Ayeyarwady	*6,184,829*	41.30	47.70	85.63	110.38	116.20
Bago	*4,867,373*	17.80	42.60	78.59	120.94	126.37
Chin	*478,801*	9.00	31.60	95.16	122.84	130.74
Kachin	*1,642,841*	18.90	31.70	157.10	146.76	152.29
Kayah	*286,627*	5.40	16.90	43.21	46.92	50.44
Kayin	*1,504,326*	11.20	20.40	60.50	68.46	73.90
Magway	*3,917,055*	52.10	97.50	139.63	136.37	141.53
Mandalay	*6,165,723*	21.80	33.50	53.36	108.36	107.23
Mon	*2,054,393*	11.50	16.60	35.50	70.35	70.97
Rakhine	*2,098,807*	44.60	69.60	147.28	133.96	140.41
Sagaing	*5,325,347*	43.40	67.50	170.45	170.41	175.51
Shan	*5,824,432*	55.10	87.40	219.33	208.02	216.41
Tanintharyi	*1,408,401*	19.80	31.20	125.55	142.08	145.39
Yangon	*7,360,703*	84.90	32.00	58.44	120.67	40.86
TOTAL	*49,119,658*	436.80	626.20	1,469.73	1,706.53	1,688.22
MINIMUM VALUE		*5.40*	*16.60*	*35.50*	*46.92*	*40.86*
LOWEST THREE		*Kayah*	*Mon*	*Mon*	*Kayah*	*Yangon*
Chin		*Kayah*	*Mon*	*Kayah*		
Kayah Kayin Kayin		*Mandalay*	*Kayin*	*Mon*		
MAXIMUM VALUE		*84.90*	*97.50*	*219.33*	*208.02*	*216.41*
HIGHEST THREE		*Yangon*	*Magway*	*Shan*	*Shan*	*Shan*
Shan		*Sagaing*	*Sagaing*	*Sagaing*		
Shan Magway Rakhine		*Kachin*	*Kachin*	*Kachin*		
RATIO MAX:MIN		*15.7*	*5.9*	*6.2*	*4.4*	*5.3*

Source: Data from the Budget Department, MOPF.

From figure 9 and table 13, two points are striking:

- The relative shares of each state/region government seem to have been fairly consistent, with the same sub-set of state/region governments quite consistently getting relatively small or relatively large allocations. This suggests a degree of consistency in the manner in which the deficit transfers were estimated year-by-year. However, Yangon is a notable exception, having earlier gained the greatest share, but in later years has received very low shares (quite appropriately, in view of its large own revenues). Since the allocations were only made by formula starting in FY 2015/16, this consistency seems surprising.

- Very oddly, the degree of spread between total grant transfers has reduced, despite the increased pool—from a maximum-to-minimum range of 15.7 in FY 2012/13, down to around 5 in recent years.

The equity angle: Grant transfers per capita

However, what is more significant are the patterns seen from a *per capita* angle. Only when the relative populations of states/regions are factored in, can grant transfers be seen as equitable. This is not to say that fiscal transfers per capita should be equal across states/regions, but they should not be very different. Table 14 presents the patterns and trends in per capita fiscal transfers to states/regions.

Table 14 Grant transfers per capita and variance - MMK

State/ Region	*Pop.*	2012/13	2013/14	2014/15	2015/16	2016/17
		PA	RE	UBL	UBL	UBL
Ayeyarwady	*6,184,829*	6,678	7,712	13,845	17,847	18,788
Bago	*4,867,373*	3,657	8,752	16,146	24,847	25,962
Chin	*478,801*	18,797	65,998	198,746	256,557	273,055
Kachin	*1,642,841*	11,504	19,296	95,627	89,335	92,699
Kayah	*286,627*	18,840	58,962	150,753	163,688	175,971
Kayin	*1,504,326*	7,445	13,561	40,217	45,510	49,124
Magway	*3,917,055*	13,301	24,891	35,647	34,813	36,130
Mandalay	*6,165,723*	3,536	5,433	8,654	17,575	17,390
Mon	*2,054,393*	5,598	8,080	17,280	34,244	34,544
Rakhine	*2,098,807*	21,250	33,162	70,173	63,826	66,899
Sagaing	*5,325,347*	8,150	12,675	32,007	32,000	32,957
Shan	*5,824,432*	9,460	15,006	37,657	35,715	37,155
Tanintharyi	*1,408,401*	14,058	22,153	89,144	100,877	103,231
Yangon	*7,360,703*	11,534	4,347	7,939	16,394	5,551
TOTAL	*49,119,658*	8,893	12,748	29,921	34,742	34,370
MINIMUM VALUE		*3,536*	*4,347*	*7,939*	*16,394*	*5,551*
LOWEST THREE		*Mandalay*	*Yangon*	*Yangon*	*Yangon*	*Yangon*
Bago		*Mandalay*	*Mandalay*	*Mandalay*	*Mandalay*	
Mon		*Ayeyarwady*	*Ayeyarwady*	*Ayeyarwady*	*Ayeyarwady*	
MAXIMUM VALUE		*21,250*	*65,998*	*198,746*	*256,557*	*273,055*
HIGHEST THREE		*Rakhine*	*Chin*	*Chin*	*Chin*	*Chin*
Kayah		*Kayah*	*Kayah*	*Kayah*	*Kayah*	
Chin		*Magway*	*Tanintharyi*	*Tanintharyi*	*Tanintharyi*	

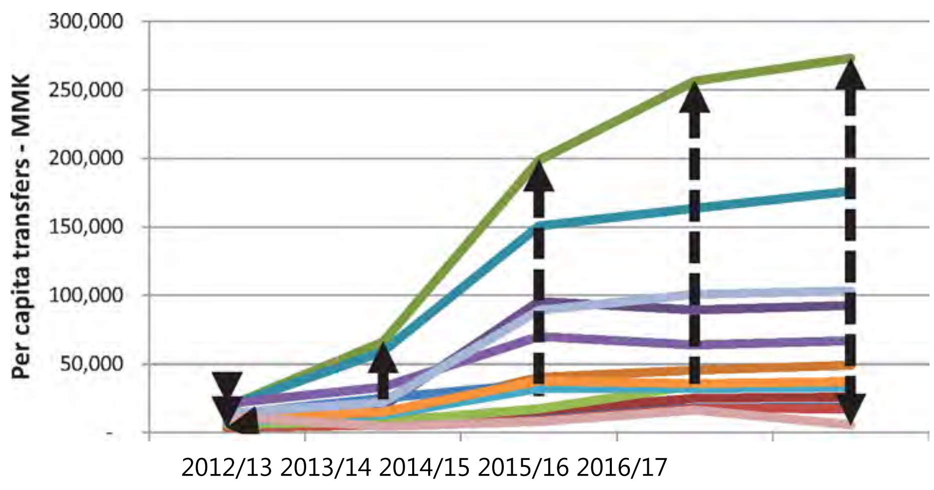
RATIO MAX:MIN	*6.0*	*15.2*	*25.0*	*15.6*	*49.2*

Source: Data from the Budget Department, MOPF.

A number of issues emerge in table 14. In general, behind the steady growth of national average grant transfers per capita, there is a very wide variation each year in the per capita transfers across states/ regions. For example, in FY 2016/17, Chin and Kayah received MMK 271,055 and MMK 175,971, per capita, respectively. Yangon and Mandalay, however, received only MMK 5,551 and MMK 17,390, respectively. Yangon and Mandalay, of course, enjoy much higher own-source revenues per capita than other states/regions. As such, on equity grounds, it makes sense that they receive correspondingly lower transfers. But then many other states/regions (e.g. Ayeyarwady, Bago, Magway, Sagaing, and Shan) that do not enjoy especially high own-source revenues, receive only little more than Mandalay, and a small fraction of the amounts enjoyed by some other states/regions.

This range between the lowest and highest value of transfers per capita has been expanding over the years as the volume of transfers has increased: from a ratio of 6.0 in FY 2012/13 to the current ratio of 49.2 in FY 2016/17.

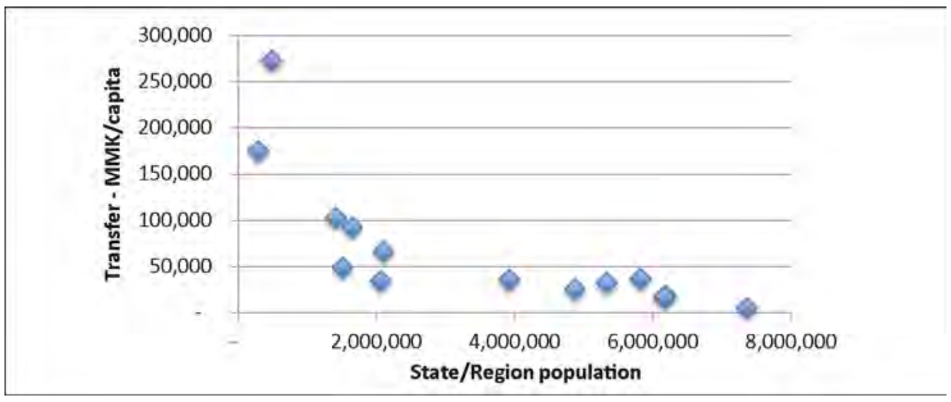
Figure 10 Visualizing growing variance in grants per capita



Source: Data from the Budget Department, MOPF.

In general, the less-populated states/regions appear to receive much more generous allocations per capita than the more-populated ones. The following chart portrays a clear negative correlation between state/region population size and the level of transfer per capita.

Figure 11 Plotting grants per capita against state/region population, FY 2016/17



Source: Data from the Budget Department, MOPF.

Once again, it should be stressed that there is no necessary reason that fiscal transfers per capita should be equal across states/regions if, for example, there are also substantial differences in state/region own-source revenues, such that varying per capita transfers allow equalization of revenues per capita, or in their per-capita expenditure responsibilities. The implications of all this are examined further under B 5.

B.3.3. Constituency Development Fund (CDF)[28]

Alongside the general grant transfer just examined, the only specific inter-governmental grant transfer now remaining is the CDF, which was established in FY 2013/14 as an instrument managed under the authority of the Union Hluttaw to provide annual Constituency Development Grants (CDGs) to townships, but channeled through state/region Hluttaws (to whose account funds are transferred). CDGs are grants earmarked for small infrastructure and other investments, selected through a planning process managed under the various township committees.

The annual volume of the CDF is MMK 33 billion, or only about 2% of the overall fiscal transfers from Union to states/regions. CDGs are allocated equally as MMK 100 million grants to each of the 330 townships. Given that township populations vary between some 2,000 persons to over 400,000 persons, there is very considerable difference in the funds provided, when measured on a per capita basis. Per capita allocations range from a meager MMK 250 in highly populated townships, to MMK 50,000 in the small townships in the hill areas - a range of 1:200.

B.4. Financing 'deconcentrated' expenditures: Basic education

There are no fiscal transfers to finance Basic Education expenditures at the state/region level, since these are not funded from the state/region budget. There are, supposedly, notional 'budget allocations' to State/Region Departments of Basic Education but: (a) it is not clear how they are determined, (b) states/regions are never informed of budget allocations at the time they formulate their budget proposals, and (c) final approval within these ceilings is kept at the Union level. Hence, strictly speaking, it is misleading to refer to this as 'deconcentrated' funding.

Table 15 shows the actual approved allocations to State/Region Departments of Basic Education (DBE) for FY 2016/17, by type of investment, and by proponent. Further details are provided in Annex 6.

The equity issues arising from these allocations are examined further under B.5.3.

[28] Details of the Constituency Fund in this sub-section are largely drawn from the report by Bart Robertson et al. *Local Development Funds in Myanmar: An Initial Review.* Discussion Paper No. 9 (Yangon: The Asia Foundation and MDRI-CESD, 2015).

Table 15 DBE capital budget by state/region and investment proponent - MMK millions - FY 2016/17

State/Region	Proponent								Other		Total
	'High authorities'		S/R Hluttaw members		State/Region DBE		Union DBE (science labs)				MMK millions
	MMK millions	**Percentage**	**MMK millions**	**Percentage**	**MMK millions**	**Percentage**	**MMK mil-lions**	**Percent-age**	**MMK millions**	**Percent-age**	
Ayeyarwady	288.00	3%	5,297.40	47%	4,116.30	37%	351.00	3%	1,111.30	10%	11,164.00
Bago (East)	*1,024.20*	*13%*	*1,704.90*	*22%*	*3,600.00*	*47%*	*351.00*	*5%*	*982.80*	*13%*	*7,662.90*
Bago (West)	*401.70*	*6%*	*3,557.70*	*56%*	*1,164.90*	*18%*	*351.00*	*6%*	*889.20*	*14%*	*6,364.50*
Bago (Total)	1,425.90	10%	5,262.60	*38%*	4,764.90	34%	702.00	5%	1,872.00	*13%*	14,027.40
Chin	-		2,624.40	*69%*	648.00	17%	432.00	11%	90.43	*2%*	3,794.83
Kachin	60.00	*1%*	2,523.30	51%	2,034.00	41%	351.00	7%	23.40	0%	4,991.70
Kayah	31.20	*2%*	1,041.30	50%	807.60	39%	140.40	7%	53.89	3%	2,074.39
Kayin	156.00	*1%*	743.40	6%	10,194.00	80%	315.90	2%	1,285.01	10%	12,694.31
Magway	638.70	*6%*	3,872.40	35%	5,946.00	54%	351.00	3%	161.66	1%	10,969.76
Mandalay	81.90	*1%*	3,229.80	24%	9,531.90	71%	351.00	3%	144.90	1%	13,339.50
Mon	156.00	*3%*	946.50	19%	2,701.80	54%	175.50	3%	1,063.70	21%	5,043.50
Nay Pyi Taw	336.00	*2%*	66.30	0%	1,794.60	13%	105.30	1%	12,045.40	84%	14,347.60
Rakhine	168.00	*2%*	2,351.70	33%	2,076.00	30%	351.00	5%	2,084.96	30%	7,031.66
Sagaing	828.00	7%	3,846.60	32%	6,952.20	58%	351.00	3%	-	-	11,977.80
Shan (East)	*119.05*	*8%*	*81.90*	*6%*	*1,143.00*	*81%*	*70.20*	*5%*	-	-	*1,414.15*
Shan (North)	*833.30*	*21%*	*765.00*	*19%*	*2,242.20*	*56%*	*140.40*	*4%*	-	-	*3,980.90*
Shan (South)	*783.12*	*12%*	*1,961.40*	*31%*	*3,310.50*	*51%*	*351.00*	*5%*	*23.40*	*0%*	*6,429.42*
Shan (Total)	1,735.47	15%	2,808.30	24%	6,695.70	57%	561.60	5%	23.40	0%	11,824.47
Tanintharyi	322.80	6%	418.80	8%	3,002.10	60%	351.00	7%	912.60	18%	5,007.30
Yangon	144.00	1%	-	0%	10,653.44	84%	351.00	3%	1,586.70	12%	12,735.14
TOTAL	6,371.97	5%	35,032.80	25%	71,918.54	51%	5,240.70	4%	22,459.34	16%	141,023.35

Source: Union Department of Basic Education

B.5. Financing: Issues arising

B.5.1. Own-source revenues: Issues

It was noted earlier that the tax sources assigned to states/regions are ones with only modest yield. Those that are buoyant and high yield tax sources, such as income, profit, and sales taxes, are all retained for the Union government. This is not, in itself, too problematic, and there are good reasons that such revenues are under Union government control. The Schedule 5 amendment of the 2008 Constitution may increase the range of state/region revenue powers, but it is important that any new powers (e.g. related to natural resources) will not cause major disparity between state/region own-source revenues[29]. Or if they do cause disparity, the fiscal transfer mechanism will then need to be reviewed to find ways to compensate for this. That aside, the scope for states/regions to raise own-source revenues is weakened by a number of factors:

Limited powers and inflexible rates

In many cases, the rates on state/region taxes were set decades ago and have not been adjusted upwards in line with inflation. For example, the Land Tax collected by GAD on behalf of states/regions is a mere MMK 3.5 ($ 0.003) per acre. The collection of such taxes costs much more than the revenue raised. In that regard, according to one State Budget Director "some village tract administrators often find it more expedient to remit the meager land tax proceeds from their own pocket to the GAD, rather than attempt to tour their area to collect from villagers."

State/region governments seem to have little or no discretion in setting or changing the tax rates for these various levying powers - partly because the various laws and regulations governing these powers have not yet been re-aligned with Schedule 5 provisions. However, normally, such discretion (within limits) goes together with the 'tax revenue power'. Reportedly, a proposal to raise the Land Tax is being discussed now, but only at the Union level.[30]

Weak incentives

The 'deficit transfer' funding arrangements in place, until very recently, have very likely undermined the incentive for state/region governments to maximize their own-revenue collection effort. The soft budget constraint inherent in this arrangement has placed the main resource-mobilization focus on lobbying 'upwards' for increased transfers from the Union government, rather than on leveraging their own-source revenue base. This, however, should now change as Medium Term Fiscal Framework reforms are introduced, bringing in a harder budget constraint.

Lack of guidance and support

There is little or no practical guidance for state/region governments regarding how to: collect these taxes consistently and efficiently; assess the tax base and taxable values; assess the amounts due; manage tax billing and administer the tax in a consistent and transparent manner; deal with delays and defaults; provide incentives for prompt payment; and so on.

Cumbersome local revenue administration

At the same time, local tax administration is inherently complex in Myanmar. State/region taxes are

[29] For comparative international experience and potential problems see "Natural Resource Revenue Sharing", Natural Resource Governance Institute & UNDP, 2016.

[30] The schedules of taxes, charges, and fines are apparently being adjusted upwards at the Union level. For example, fines for violation of the Excise Law were recently adjusted upwards, from MMK 1,000 up to MMK 1 million, an increase of 1,000 times. This is inevitably a gradual and piecemeal process.

collected not by a single tax revenue office (as is common in many countries), but by a range of up to 20-25 different state/region departments, each with its own staff and its own procedures for assessment, billing, collection, dealing with defaults, etc., and for reporting and remitting proceeds to the state/region fund account. This greatly increases the costs of tax administration (which for some departments may actually be greater than the proceeds collected), and also increases the risks of 'leakage' and abuse. It makes it very hard as well to implement the sort of revenue-collection capacity-building program that is needed or, indeed, to create an image of 'tax transparency' for Myanmar citizens who have to deal with so many different agencies and procedures. Here too, the continued proliferation of arrangements and procedures for revenue collection is in part a reflection of the fact that laws and regulations pre-dating the 2008 Constitution have not been fully re-aligned with Schedule 5 provisions.

Key revenue sources pre-empted by DAOs

It should also be underlined that one tax source which is often assigned to subnational government is property tax (immoveable assets are very well suited for local taxation). To date, property tax revenues in Myanmar have been assigned very specifically to DAOs and City Development Committees to be used for spending in urban areas only. This 'firewalling' of property tax revenue - its use reserved only for the urban population (some 35% of the total) - deprives the governments of states and regions of a potentially important revenue source which could instead be used flexibly for expenditures across the entire territory, whether in an urban or rural area, where it can have greatest impact.

Own-revenue classification and monitoring

There are two related problems here. First, the current revenue classification scheme used by state/ region government seems to be potentially misleading. Shared revenues are recorded together with genuine own-revenues under 'Other Current Receipts', even though they are transfers—they should, instead, be recorded as 'Receipts from the Union'. Second, it appears that in estimating state/region total own-revenues, the Union Budget Department takes the total revenues estimated by state/region governments, and subtracts only the general deficit transfer, such that the net 'own revenue' figure still includes both shared revenues and possibly various other grants.

These practices generate misleading information about genuine own-revenues, and can complicate and undermine self-monitoring by the state/region governments, and higher-level monitoring by the MOPF. This, in turn, may lead to lack of clarity about the overall trends and patterns in genuine 'own-source revenues', and undermine the formulation of appropriate fiscal transfer arrangements.

Excise revenue: Are states and regions missing out?

Last, it is worth noting that, although Schedule 5 assigns 'Excise Revenue' to state/region government, what is actually collected by GAD appears simply to be the annual license fee for running liquor-making or retail businesses. Yet, 'excise revenue' in English ("YiMyo" in Myanmar) denotes a fiscal levy which has a much broader base than just license fees, whether judged by international convention, or even apparently by Myanmar's own legal precedents.

Box 10 Excise revenue: Myanmar legal precedent and international convention

The Burma Excise Act (1917):

Article 2 (h): "Excise-revenue means revenue derived or derivable from any duty, fee, tax [...] relating to alcoholic liquor or intoxicating drugs."

Wikipedia - a general definition of Excise tax:

"An excise tax (sometimes called a special excise duty) is an inland tax on the sale, or production for sale, of specific goods, or a tax on a good produced for sale, or sold, within a country, or licenses for specific activities. Excises are distinguished from customs duties, which are taxes on importation. Excises are *inland* taxes, whereas customs duties are *border* taxes. ... An excise [tax] is typically a per unit tax, costing a specific amount for a volume or unit of the item purchased, whereas a sales tax or VAT is an *ad valorem* tax and proportional to the price of the good. Typical examples of excise duties are taxes on gasoline and other fuels, and taxes on tobacco and alcohol (sometimes referred to as sin tax)."

Under the Union Tax Law of 2016, on behalf of the Union government, the Internal Revenue Department collects 'special goods taxes' on alcohol and tobacco which, based on international convention and on Myanmar's own legislative precedent, would appear to be 'excise revenues', and hence to be under the authority of state/region government to collect, rather than the Union government. There may be some legal or regulatory reason why such taxes are not being, or cannot be, collected by states/regions, and instead are collected by the Union government, due, for example, to Union laws or regulations not having been re-aligned to Schedule 5 provisions; or this may simply be an oversight needing to be rectified; or it is just a mistranslation of terms between Myanmar and English.

B.5.2. Fiscal transfers: Issues

Revenue sharing

The rationale for sharing various tax revenues by area of derivation is unclear, since neither commercial nor special goods tax revenues obviously correspond to an economic activity which requires special state/region expenditure to manage or to mitigate externalities (e.g. as might be the case with tourism or natural resource extraction). Allocating by area of derivation also obviously poses an equity issue. Ninety percent of this shared revenue is (not surprisingly) allocated to the Yangon Region where most commercial activity takes place. This requires adjustment of the 'deficit grants' to compensate (for these, the pool is far greater). The alternative approach is simply to add the total tax-share pool to the deficit grant pool, and allocate the entire amount to states/regions according to the formula, which would appear to be simpler.

At the state/region level, there seems to be little awareness of this new fiscal instrument, and probably some uncertainty as to whether it is a temporary arrangement or will continue. One state/region Minister for Planning and Finance interviewed for this study did not know about the arrangement at all.

A final issue relates to the practice of state/region governments recording this revenue as one of the 'Other Current Receipts' under Part 1 of the budget where, as noted earlier, it is 'hidden' alongside state/region own-source current revenues, and misleadingly inflates the total. The rationale seems to be that since these revenues are collected locally, then they should be recorded as 'own-source revenues'. But it would seem to be less misleading and more useful to record it separately, under the Union Receipts column. Being a Union revenue at origin, the sharing is a form of Union transfer.

Grant transfers

Total revenue per capita outcomes

Table 16 Variance of state/region revenues FY 2016/17

Measure	MMK per capita
Average total per capita revenues	50,907
Minimum total per capita revenues-	22,430
Maximum total per capita revenues -	278,829
Maximum: Minimum Ratio	12.4
Standard Deviation	71,428.5

Previously, the disparities in fiscal transfers between states/regions when measured on a per capita basis were noted. A key consequence seems to be that fiscal transfers do not lead to equity of total subnational resources for public spending. Table 16, on state/region revenues per capita by source, and the charts in the following pages depict revenues per capita enjoyed by state/region governments over the past two years from own-source revenues, deficit grants and revenue sharing. What emerges is that:

- The variance in total revenues per capita across states/regions is less extreme than for fiscal transfers per capita alone, but is still very large. In FY 2016/17, variance ranges from MMK 22,430 for Ayeyarwady to MMK 278,829 for Chin, a ratio of 12.4.
- The allocation of fiscal transfers has not played an 'equalization' function. Instead of 'leveling' the variations in own-source revenues per capita, fiscal transfers seem to have been weighted excessively towards states/regions with the lower levels of own-source revenue per capita, such that these now receive in total much more per capita than those states/regions with higher own-source revenue levels.

Table 17 State/Region revenues per capita by source - MMK millions - FY 2015/16 and 2016/17

States & Regions	FY 2015/16			FY 2016/17			
	Own Revenue	Grant Transfer	Grand Total	Own Revenue	Shared Tax Revenues	Grant Transfer	Grand Total
Ayeyarwady	4,388	17,847	22,235	3,322	320	18,788	22,430
Bago	7,455	24,847	32,302	4,572	333	25,962	30,866
Chin	14,974	256,557	271,532	3,577	2,197	273,055	278,829
Kachin	9,128	89,335	98,463	7,134	777	92,699	100,610
Kayah	24,892	163,688	188,580	7,656	422	175,971	184,048
Kayin	5,463	45,510	50,974	3,136	304	49,124	52,564
Magway	5,102	34,813	39,916	3,603	782	36,130	40,515
Mandalay	22,217	17,575	39,792	18,257	2,034	17,390	37,682
Mon	6,246	34,244	40,490	4,043	373	34,544	38,960
Rakhine	5,603	63,826	69,429	3,267	499	66,899	70,665
Sagaing	4,970	32,000	36,970	4,102	721	32,957	37,779
Shan	7,484	35,715	43,200	5,716	669	37,155	43,540
Tanintharyi	6,405	100,877	107,282	4,284	881	103,231	108,396
Yangon	56,556	16,394	72,950	40,127	29,600	5,551	75,278
Average	15,836	34,742	50,578	11,432	5,106	34,370	50,907

Source: Data from the Budget Department, MOPF.

Figure 12 State and region revenues per capita by source - FY 2015/16

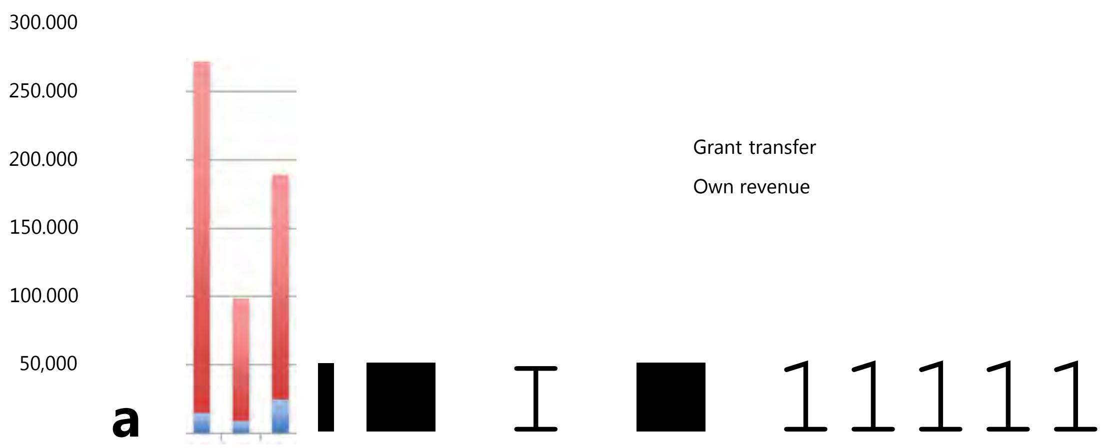
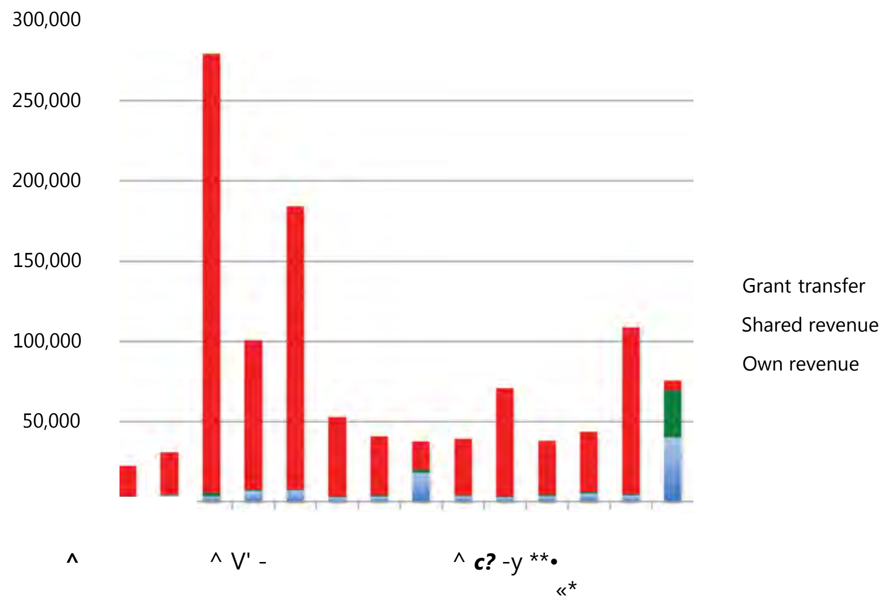


Figure 13 State and region revenues per capita by source - FY 2016/17

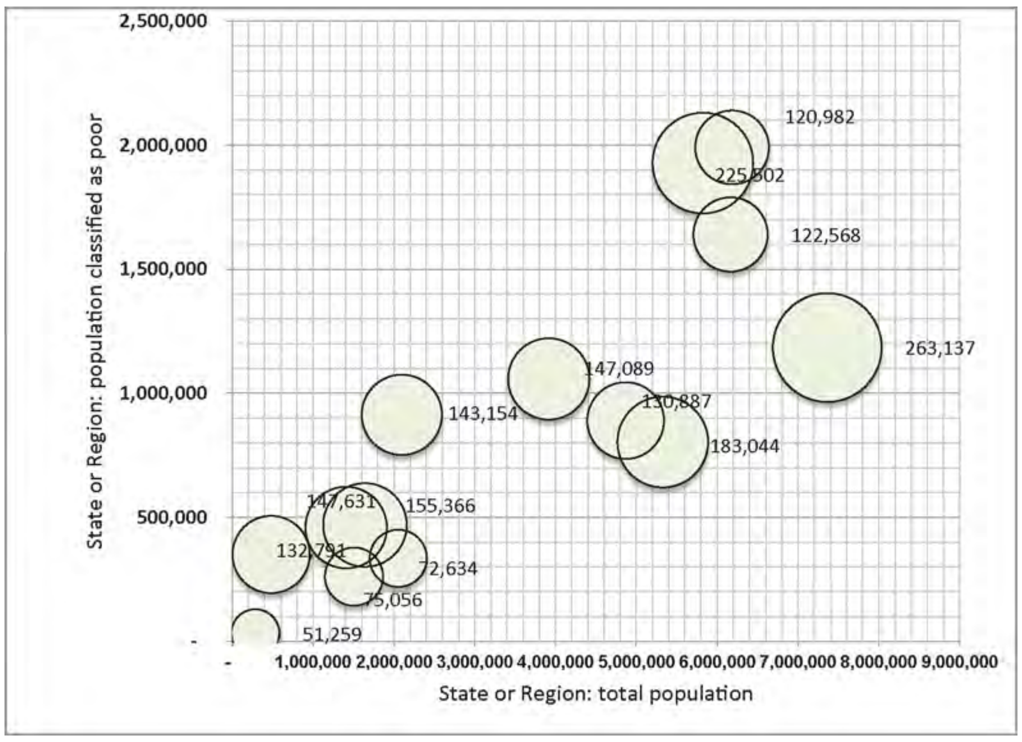


What all this means is that there is a very wide variance of total public expenditure levels per capita between states/regions, and which appears not to be justified by any corresponding variance in relative need.[31] Figure 14 locates the 14 states/regions against the two main "need" indicators: total state/region population (horizontal axis) and the number of people in each state/region below the poverty line (vertical axis).[32] The level of public expenditures is indicated by the size of the bubble for each state/region.

[31] Of course Union budget expenditures per capita will vary across states/regions, but these are, in principle, a different set of expenditure responsibilities, and so it cannot be claimed that they might somehow 'compensate' for state/region expenditure variance.

[32] This is computed by applying the state/region poverty incidence values to the state/region populations, using the same data used by MOPF for the grant transfer allocations.

Figure 14 Charting total state/region revenues/expenditures in MMK millions against total population and population classified as poor



It is clear that states/regions on similar coordinates - i.e. which have both very similar total population levels and poor population levels - often enjoy very different levels of revenue/expenditure (e.g. of the two with the highest levels of poor population, and which have very similar total population, one state/region enjoys MMK 225,502 million while the other enjoys only MMK 122,568 million - little more than half); and, similarly, that some states/regions with higher total population and poor population levels enjoy much lower revenue/expenditure levels than other states/regions with lower total and poor population levels. In other words, there is no correlation of revenue/expenditure levels with the two principal need indicators.

The grant transfer allocation formula

Institution of the formula has been a very positive move towards a more transparent and predictable funding mechanism and, potentially, one that can help introduce the much greater equity that is badly needed in the allocation of resources to states and regions. However, the formula, as currently designed and implemented, has a number of problematic features which compromise these objectives, and which also underlie the lack of correlation of state/region revenue/expenditure levels and relative need, which was just highlighted.

- ***Calibrating for different expenditure needs.*** As noted, if allocation of public resources across subnational units is to be equitable, then these resources per person should tend towards similar levels, allowing for some difference in local context and need. This does not mean that they should be equal, but neither should levels be dramatically different. Yet, allocations per capita are currently quite dramatically different across states/regions, and even more so since the introduction of a formula. This appears to be due to several 'technical' anomalies in the formula:

- Weighting. In all allocation formulae, the criteria will have, by design or by default, a 'weighting'. This means that the total pool is split into sub-pools so that the allocations for each of the criteria are made from the corresponding sub-pool. If a 10% (or 0.1 factor) weighting to a criterion is given, this means that 10% of the total pool will be allocated according to the relative values of each

state/region for that particular criterion.

Since no explicit weights seem to have been given to the six criteria by default, each of the six variables appears to be given equally, 1/6 (or 17%) importance in the allocations. This means that:

- Population, which is the most important of all the criteria, has only 17% weighting, which is very low. Mathematically, this means that transfers per capita generated by the formula are likely to be very different, and unlikely to correlate with relative population size.
- All need criteria combined account for only 3/6 (50%) of the pool. This gives far too little importance to relative expenditure needs.

• ***Computation of the poverty incidence factor.*** The relative poverty incidence of states/regions is an important variable to moderate allocations, and ensure that per capita allocations in poorer areas are appropriately greater than those allocations in less-poor areas. However, the poverty incidence criterion appears to be included as an absolute number in the formula. Instead, this number needs to be weighted by the relative populations of states/regions, otherwise it introduces a serious distortion and, other things being equal, will tend to give larger allocations to states/ regions with smaller populations.

• ***Calibrating for local fiscal constraint.*** There are three variables that have been used to provide a measure of relative 'fiscal poverty' for states/regions.

- ***Tax revenues per capita.*** It is unclear whether historic actual tax revenues or future estimates were used. Using estimated revenues can be problematic since this can provide a disincentive to state/region governments to mobilize own-revenues if they believe this will lead to a reduction in the level of transfers. An alternative approach to calibrating for local revenue potential is discussed under Section D.2.2.
- ***GDP per capita.*** Use of GDP per capita is problematic for two reasons: (i) because the methodological basis for estimating subnational GDP values is very questionable (not only in Myanmar, but generally), and hence the numbers are of doubtful value; (ii) that aside, the rationale for its inclusion is presumably that it serves as a proxy measure for relative state/ region 'fiscal potential'. But given that most important tax powers related to income and wealth are Union taxes, the GDP criterion is actually a measure with little relevance.
- ***Urban share of population.*** Use of the urban population share of total population is also rather problematic, being a weak proxy for fiscal potential.
- ***Weighting.*** As noted, by default, the three criteria account for the other 50% of the pool. This is far too much weighting, especially considering that, nationally, the volume of own-source revenues is so small, at only about 20% of total state/region revenues. This is in addition to the more general problems of using any fiscal constraint-related criteria in such a formula.

Timing and Information

Much attention is usually given to the technical details of the allocation formula for fiscal transfers. But one dimension of the fiscal transfer mechanism which is typically neglected is the information about transfers that is communicated to subnational levels; i.e. what is communicated, and when.

Previously, the amount of the fiscal transfer was only communicated to state/region governments after they had made their budget submissions, usually in January. This then required one or more rounds of iteration through which state/region governments would engage in last-minute 'cutting down' of their original budget proposal to a level that could be financed with the available funds. This iteration was a source of problems and undermined the quality of the planning and budgeting process.

Starting in FY 2016/17, the Union government began informing state/region governments of the size of the transfer in mid-November. This is an extremely positive reform, and allows state/region governments to finalize their budget proposal according to the availability of funds before submitting the budget to the Financial Commission. This means there is no need for further iteration and cutting down. But this is only an advantage if it is made clear to state/region governments that the amount of the transfer announced in November is final and not subject to further negotiation. This has not always been the understanding at the state/region level.

B.5.3. Financing deconcentrated expenditures: Issues

It is not known what criteria are used by the Union Department of Basic Education to make the relative state/region allocations in Table 18. A ***post-facto*** assessment of the equity of these allocations, however, can be made by calculating them on a per capita basis (using total state/region populations as a proxy for numbers of pupils or school-age children, for which data are unavailable). This suggests that there is a substantial variance in the average MMK 3,690 per capita allocation—with the highest level in Kayin being 4.9 times the lowest level in Yangon. This, however, is a much lower variance range than previously seen for general grant transfers.

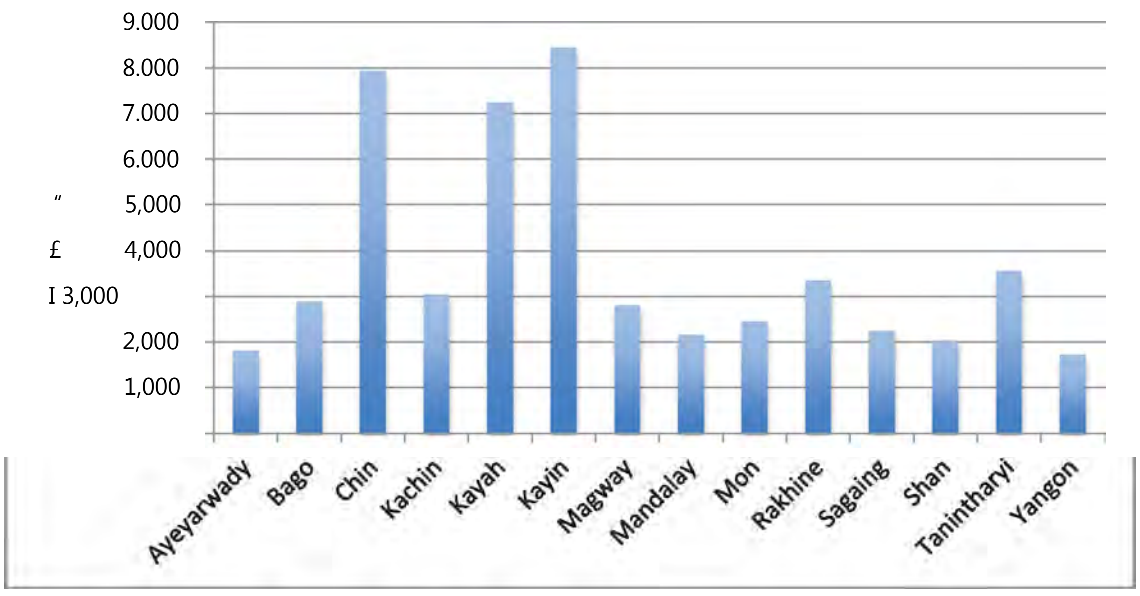
Table 18 Variance in DBE budgets per capita - FY 2016/17

State or Region	MMK per capita
Ayeyarwady	1,805
Bago	2,882
Chin	7,926
Kachin	3,038
Kayah	7,237
Kayin	8,439
Magway	2,801
Mandalay	2,163
Mon	2,455
Rakhine	3,350
Sagaing	2,249
Shan	2,030
Tanintharyi	3,555
Yangon	1,730
Average	3,690
Measures of Variance	

Minimum value	***1,730***
	Yangon, Ayeyarwady, Shan
Maximum value	***8,439***
	Kayin, Chin, Kayah
Max:Min Ratio	***4.9***

It may be that this variance does somehow reflect the relative needs or costs of basic education provision in different states and regions, although, if so, the relatively very low allocation to Shan State, for example, is surprising. It may also be that it is simply the combined result of the disparate criteria applied by the Union DBE. In this regard, it seems likely that, just as with general grant transfers, there is an implicit bias in the allocation mechanism towards states/regions with a smaller population size, such as Chin and Kayah.

Figure 15 Financing per capita for basic education investments: FY 2016/17



C. How are Subnational Expenditures Planned and Budgeted?

In the preceding sections, state/region expenditure responsibilities and their financing, as well as some implications for the quality of public financial management are examined. This section looks at how planning and budgeting for these responsibilities are undertaken. Starting with some general considerations on the topic; the section then provides an account of how these expenditures are planned and budgeted, and how priorities for inclusion in these budgets are determined; and then at the issues arising. The focus is primarily on the capital budget. This is because, apart from its relative weight (40-60% of state/region budgets), it is the part of the budget where there are much greater decision-making options, and hence, much greater scope for local prioritization and discretionary choice—whether for better or for worse. By contrast, the current budget is very largely pre-empted by the existing staffing arrangements and related operational expenses, leaving little scope for the re-arrangement of priorities on an annual basis.

C.1. Preamble: General principles and issues

C.1.1. The scope of subnational planning

Subnational government planning is usually limited to its mandated functions or responsibilities. In other words, subnational governments are not expected to plan for things for which they are not responsible. The scope of subnational planning then is largely defined by its functional responsibilities. This scope can vary a great deal from country to country.

In many countries, the scope of subnational planning has often been limited to ***investment*** planning-such as the construction of schools, roads, and health centers. This type of planning does not take into account recurrent expenditure, which is the on-going spending needed for things such as paying staff salaries. In other words, subnational planning tends to have a greater focus on ***infrastructure*** spending and less on other inputs, such as staffing.

A second dimension to subnational planning is about ***coordination.*** Subnational government departments often 'share' their responsibilities with other departments, and/or with other stakeholders—for example, with line departments such as health and education, the private sector, nongovernment organizations and, in many cases, lower or upper tier subnational governments. Thus, a subnational government may have the responsibility for building primary schools, but the Ministry of Education may be responsible for providing teachers and paying their salaries. This means that subnational planning, if it is to be coherent and efficient, often requires a good deal of coordination between subnational levels and Union agencies involved in service delivery.

A third dimension to subnational planning concerns ***timelines.*** For longer-term or multi-year planning, subnational governments may undertake ***strategic*** planning, through which they identify strategic priorities. Secondly, subnational governments often plan their priority actions or investments over a 3-5-year period, establishing a 'pipeline' of projects which is a listing of investment projects to be implemented over a period of time, if and when, funding becomes available for them.

Annual plans, on the other hand, assist the annual budgeting process. They tend to be more realistic given that they need to be drawn up within the framework of a hard annual budget constraint-meaning that there is a fixed spending limit that the budget cannot exceed. Subnational annual planning also typically requires a good deal of detailed technical work such as the appraisal, design, and costing of infrastructure projects.

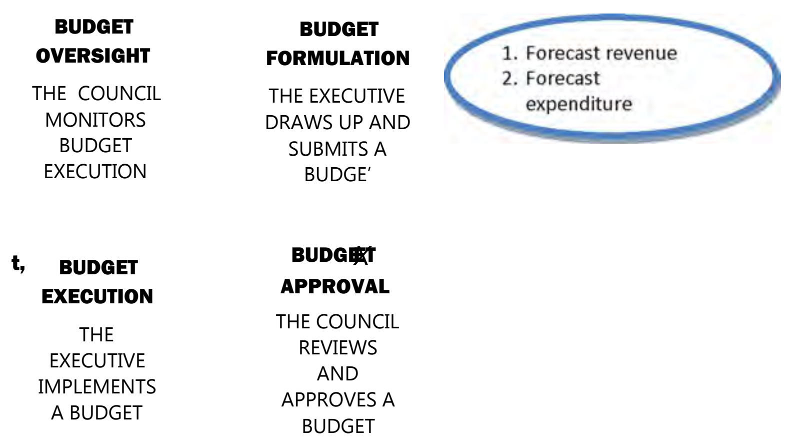
A final dimension to subnational planning is related to the method, or ***way*** in which it is done. In many countries, emphasis is placed on ***bottom-up*** or ***participatory*** planning, through which local citizens and communities become actively involved in identifying their needs and priorities. This way of planning is seen as a way of attaining the 'allocative efficiency' of decentralization, whereby subnational governments can ensure a better match between the supply of different public goods and services and local demand for them.

C.1.2. The scope of subnational government budgeting

As with other public sector budgets, a subnational government budget is a projection of all expected revenues, including transfers and grants from the central government, and of all planned expenditures for the coming year. It is important for two main reasons. First, it translates subnational government policies, political commitments, and goals into decisions on how much revenue to raise, how to raise it, and how to use these funds to meet competing needs. Second, a subnational government budget represents a type of ***compact;*** an agreement between the executive branch—a mayor or a local administrator—and the elected council that approves the budget. This compact is a legal or semi-legal commitment by the executive branch to raise certain revenues and to spend on agreed items. In principle, what is budgeted can be spent, and what is not budgeted cannot be spent. However, budgets can usually be revised, and indeed, budget revisions can be very frequent.

Generally, laws and regulations make provisions for subnational government budget formulation, and usually specify that annual budgets must be balanced so that projected expenditures do not exceed revenues, as well as specifying deadlines for the submission and approval of budgets. Subnational budget formats are also often specified through regulations. Sometimes, these regulations can be quite restrictive, thus reducing the degree to which subnational governments enjoy real budgetary autonomy.

Figure 16 The full budget cycle: Formulation, approval, execution and oversight



Formulating a subnational government budget is usually the responsibility of the executive. In some countries, this is the elected mayor or chairperson and his or her team. In other countries, it is the appointed chief executive such as a governor.

A first step in the process of formulating the subnational government budget is to forecast ***revenues*** as accurately as possible. These are the own-source revenues and the fiscal transfers discussed previously under Section B.

The second step in the budget formulation is to forecast total ***expenditures.*** In principle, this should be linked to planning, especially with respect to capital expenditure. Local planning processes should have identified priority projects to be included in the budget. These should be identified after an assessment of the relative merits of different options, in order to identify the 'best' option, since available resources will never cover all proposals emerging from the planning process. For recurrent spending, which is often dominated by payroll costs, forecasting should also be linked to an analysis of previous expenditure patterns and projections about service delivery.

Subnational governments will normally budget for expenditures that are directly related to the public goods and services that they are expected to deliver: social services, infrastructure, and administrative services. In deciding on specific expenditures, however, subnational governments may also be expected to assess their budgets in terms of the extent to which proposed spending is 'pro-poor', and thus likely to reduce poverty within the subnational government's jurisdiction, or in some cases, to analyze the likely budget impact in gender terms.

Once the annual budget has been drafted by the subnational government executive, it needs to be submitted for ***approval,*** the second stage in the budget cycle diagram. In most countries, annual budgets need to be submitted to the local council for approval, usually in a mandatory budget session. However, in some countries, most notably in francophone ones, subnational councils do not actually approve annual budgets, but 'adopt' them, pending full approval of their 'legality' by the central government (or a centrally appointed administrator) that aims, in principle, to ensure that budgets are balanced and only include permissible expenditures.

The subsequent stages of budget execution and budget oversight are critically important stages in the PFM cycle, but are not addressed in this report.

C.2. Subnational planning in Myanmar

As in most Asian countries, planning has historically been an important government function in Myanmar. Plans, plan procedures, and planning departments are seen to play a key role at all levels, and all the more so due to Myanmar's embrace over many years of a socialist development path.

C.2.1. Institutional framework for planning

The planning commissions and committees

Following a Presidential Notification of May 2016,[33] the supreme national planning body is now the National Planning Commission (NPC). This commission is chaired by the President, and comprises all Union ministers and all 14 state/region chief ministers. The membership is essentially the same as the Financial Commission established under Article 229 (a) of the 2008 Constitution, but with the addition of Union Ministers, alongside state/region chief ministers. Since early 2016, the NPC has been supported by what is now the Department of Planning and Economic Development within the Ministry of Planning and Finance (MOPF), but was formerly a full Ministry of Planning and Economic Development. [34]

At subnational level, through a follow-up notification,[35] State/Region Planning Commissions have also been established with the mandate to "analyze and approve the plans which support the socioeconomic development of respective states/regions without affecting the environment." These state/region Planning Commissions are chaired by the chief minister and comprise all state/region ministers, representatives of the private sector, and with the state/region executive secretary acting as commission secretary. It is, however, too soon to say how they are working.

[33] Presidential Notification No. 11/2016 of 5th May 2016.
[34] The Ministry of Planning and Finance was also previously merged between 1972 and 1993.
[35] Presidential Notification No. 12/2016 of 5th May 2016.

The Plan Formulation and Implementation Committees

A complementary notification re-stated the role of the pre-existing Plan Formulation and Implementation Committees (PFICs).[36] These remain in place at all subnational levels, and are apparently now intended to be subordinate to, and submit planning proposals to, the State/Region Planning Commissions, rather than to the State/Region Planning Department.

Box 11 Subnational Plan Formulation and Implementation Committees (PFICs)

State PFIC
Chair: S/R Minister of Planning and Finance
Members: MPs; selected NGOs and business persons; S/R Directors of Budget, Education, Health, Highways, Agriculture, Forestry, Fisheries, Veterinary Services, Land Records, Industry, etc.
Secretary: S/R Director of Planning. Joint Secretary: S/R Director of DRD

District PFIC (DPFIC)
Chair: District Administrator (GAD)
Members: MPs; selected NGOs and business persons; District Directors of Education, Health, Highways, Agriculture, Forestry, Fisheries, Veterinary Services, Land Records, Industry, etc.
Secretary: District Planning Officer. Joint Secretary: District Director of DRD

Township PFIC (TPFIC)
Chair: Township Administrator (GAD)
Members: MPs; selected NGO and business persons; Township Directors of Education, Health, Highways, Agriculture, Forestry, Fisheries, Veterinary Services, Land Records, Industry, etc.
Secretary: Township Planning Officer. Joint Secretary: Township Director of DRD

Note: Respondents in some states/regions gave differing accounts of PFIC membership at different levels, so there may be differing arrangements. The membership indicated above is the fullest range reported for each level.

C.2.2. Plans and plan cycles

An overarching 20-year long-term National Comprehensive Development Plan (2011-30) was prepared under the previous Presidency, which in turn gave rise to a series of Five-Year medium-term development plans, at both Union and state/region levels, and which then, in turn, were operationalized through annual development plans for the state/region government, for state/region departments, and also for each township, and which synchronize with the annual budget cycle.

In principle, the second Five-Year Plan cycle (FY 2016/17-FY 2020/21) is now underway at both Union and state/region levels. The state/region Five-Year Plans are divided into two parts or volumes: (I) the state/region's own plan which is funded by the state/region government's own budget; and (II) the Union plan for the state/region which collates the investment activities of various Union line ministries for the state/region concerned.

However, these long- and medium-term planning frameworks are now seen as outdated. They are widely viewed as having been prepared in a top-down manner, with an excessive focus on physical infrastructure and inadequate focus on social services. The general opinion expressed was that for the time being, the main focus must be on the annual development plans until a new strategic planning framework has been developed that is consistent with the political and policy priorities of the current

[36] Plan Formulation and Implementation Committees Notification No. 13/2016 of 5th May 2016.

civilian government.

Section C.3. examines the annual planning and budgeting cycle and procedures, though this may now change somewhat to reflect the role of the newly created Union and State/Region Planning Commissions.

C.3. Annual planning and budgeting cycle

C.3.1. Introduction to the Annual Plan and Budget

There is an annual cycle of steps undertaken in states/regions toward preparation of the annual state/ region plan and budget. Before examining this cycle, it is important to first clarify the distinction between the 'plan' and the 'budget', and the role of the Planning and Budget Departments.

Annual Plan

The role of the Planning Department is to manage an annual process whereby a set of discrete investments (primarily comprised of capital budget items) is formulated by each state/region department in a manner consistent with the medium-term planning goals and priorities. Very often, this simply amounts to a detailing and updating of the provisions and costings in the Five-Year Plan for that particular year. Over the past few years, much greater emphasis has been given to ensuring that this process is a bottom-up one, originating from the township level.

The Annual Plan (as indeed, the Five-Year Plan) is little more than a listing of projects (with technical details, location, size, etc.) and costs. The annual planning process culminates in preparation of the Annual State/Region Plan Law that summarizes the approved plan, and to which there are two Annexes: Volume 1, which is the summary of investment projects (with details of type, location, costs etc.) funded by the state/region government budget; and, Volume 2, which is the list of investment projects to be undertaken by the different line ministries in the state/region, and to be funded by the Union budget.

Annual (estimated and revised) budget

Ahead of every fiscal year, around November, the Union Budget Department issues a circular to instruct state/region governments to prepare their budget estimates (BEs) for the coming fiscal year. This circular provides instructions for a process that is generally as follows:

Table 19 Budget circular: General budget estimate approval calendar

1st stage	- All line departments will submit proposals to their State/Region Department Directors that indicate whether proposals are capital, current, or debt.
2nd stage	- State/region Department Directors will submit proposals to their State/Region Budget Department. - State/region Budget Department will assess proposals for consistency, accuracy, and compliance with laws and regulations.

3rd stage	- State/region Budget Department will combine all departmental proposals and submit to the state/region government for review and approval. - State/region government will then submit proposals to the State/Region Hluttaw for approval. - State/region government will then submit proposals to the Union Financial Commission for approval
4th stage	- After approval, the Union Financial Commission will submit all approved budgets to the Union government, to prepare the Union Budget Law - The Union Hluttaw will approve the Union Budget Law - The State/Region Hluttaw will then approve its State/Region Budget Law

The role of the state/region Budget Department is therefore to manage this process, whereby a set of annual revenues (own-source and transfers) and expenditures (current and capital) is approved, consistent with Ministry of Planning and Finance regulations and with overall government policy priorities. The BE once finalized and approved, is reflected in the annual State/Region Budget Law.

During the year, however, the budget needs adjustment, as changes in both actual revenues and actual expenditure levels become apparent. In June, every year, the Budget Department therefore issues a circular that requires state/region governments to review the budget implementation, and formulate a Revised Estimate (RE), which is then submitted for approval by Union Government and the Financial Commission.

The more detailed timetables stipulated by the Budget Department for the budget estimate and revised budget are attached in Annex 4 for the 'normal timetable' (as in FY 2015/16) and the accelerated timetable (for FY 2016/17).

The state/region expenditure budget is classified into two main columns corresponding to the current budget and the capital budget. In some cases, there is also a separate 'Contributions' column that appears to be used to record transfers of funds from the state/region government to entities or departments within the state/region. Capital expenditures are all those expenditures over MMK 1 million, which create assets whose lives will be more than one year and, hence, will not need to be replaced during the year.[37]

Table 20 State and region budget format for expenditures

State/Region Collecting Entity	Current	Capital	Contributions
Part 1 State/region government entities			
Part 2 State/region departments (GAD, Forestry, etc.)			
Part 3 State economic enterprises			
TOTAL			

Source: State/Region budgets

Relationship between annual plan and budget

State/Region level

Table 21 provides a schematic picture of the relations between the annual state/region plan

[37] As noted elsewhere, there are reasons to believe that this classification is not always followed consistently.

on the left side, and the annual state/region budget on the right side.

Table 21 Schematic relationship between the annual plan and annual budget

ANNUAL STATE/REGION PLAN (Vol 1)		ANNUAL STATE/REGION BUDGET			
PROJECTS & DETAILS	COSTS	FOR PLAN INVESTMENTS		OTHER	
		CAPITAL	CURRENT	CAPITAL	CURRENT
DEPT. A. Project 1. Project 2. Project n.					
DEPT. B. Project 1. Project 2. Project n.					
DEPT. C Project 1. Project 2. Project n					
DEPT N. Project 1. Project 2. Project n.					
TOTAL					

The annual budget comprises: (a) expenditures corresponding to plan investments, which are mainly, but not entirely, capital expenditures; and (b) other expenditures which are mainly administrative and current, which are not related to investment projects, and were not included in the state/region plan.

As noted, there is also a State/Region Plan (Vol II) for those expenditures funded under Union ministry budgets.

Township level

State/region government plans and budgets are translated into corresponding annual plans and budgets for townships, and the two Volumes are integrated into one simple document, showing both state/region and Union-funded expenditures together. Table 22 is an illustration for Hpa-An Township:

Table 22 Hpa-An Township approved plan and budget - MMK millions - FY 2016/17

Entity or Department	Budget Source		
	Kayin State	Union	Total
Part 1 - State Government Administration			
Administration	320.71	-	320.71
Hluttaw	323.74	-	323.74
Executive Committee	-	93.70	93.70
Attorney	39.20	-	39.20
Auditor General	4.20	-	4.20
PART 1 - SUB-TOTAL	687.85	93.70	781.55
Part 2 - Ministries and Departments			
Agriculture	2,738.57	2,494.81	5,233.38
Environmental Conservation	287.23	-	287.23
Commerce and Industry	305.50	-	305.50
Electricity	3,116.00	876.42	3,992.42
Labor	-	77.47	77.47
Planning and Finance	77.58	7.05	84.63
Health	290.83	948.38	1,239.21
Education	-	4,430.51	4,430.51
Courts	1,623.90	1,455.12	3,079.02
Border Affairs	1,047.00	1,716.68	2,763.68
Home Affairs	543.35	232.58	775.93
DAO	419.05	-	419.05
PART 2 - SUB-TOTAL	10,449.01	12,239.02	22,688.03
GRAND TOTAL	11,136.86	12,332.72	23,469.58

Source: Hpa-An Township Planning Office

Convergence of the annual plan and capital budget cycles: An overview

How the annual plan and capital budget cycles integrate is now examined—a process which, as outlined in the box on the annual state/region plan and budget cycle, normally begins around June FY N-1, and culminates in March FY N-1 with approval by the State/Region Hluttaw of the Budget Law and the Plan Law for the fiscal year in question.

Box 12 Annual state/region plan and budget cycle: An overview

- Generation of plan and capital budget proposals (June-October FY N-1):
  - Review of past and current plan implementation;
  - Initial circulars or instructions by line ministries and by the Union Planning Department to start the planning and budgeting process and indicate the major deadlines;
  - A 'bottom up' process of consultation (from township, to district, to state/region) to elicit local plan and budget proposals in each sector, consistent with provisions of the Five-Year Plan; and
  - 'Separating proposals for state/region budget funding from those for Union ministry funding - from which point there are two sets of parallel procedures:

- <u>either</u> Stream I: Proposals for state/region plan and budget (August-March FY N-1):
  - Aggregation by the state/region line departments of various 'bottom-up' proposals, plus proposals by MPs, etc., internal review and amendment;
  - Submission of the proposals to the state/region Planning and Budget Departments for review, dialogue with line departments, and amendment;
  - A circular by the state Budget Department to guide state/region departments in preparing their capital and current budget proposals;
  - State/region government receives indication of its grant transfer amount, and finalizes its initial budget proposal (Note in some cases this is taken as a ceiling, but in other cases it is not);
  - Submission of the budget proposals to the state/region government (cabinet) for review and amendment;
  - Submission of the budget proposals to the State/Region Hluttaw for review, amendment, and approval;
  - Submission of the budget proposals by the state/region government to the Financial Commission for review and approval;
  - Union government submits the budget proposals to the Union Hluttaw for approval of state/ region grant transfers;
  - State/region government submits the budget proposals to the state/region Hluttaw; and
  - State/region Hluttaw reviews and approves the State/Region Budget Law and Plan Law, including Volume 1 annexed to the Plan Law.

- or Stream II: Proposals for Union Ministry plan and budget (Aug-March FY N-1):
  - Aggregation by state/region line department of various 'bottom-up' proposals, plus proposals by MPs, etc., internal review and amendment;
  - In some (but not all) cases, submission of the proposals to the state/region government for review and input (but not to the Hluttaw);
  - State/region line departments submit their proposals to the Union line ministry;
  - Union line ministries review all the state/region submissions, approves individual state/ region budgets based on total sector funding, and submits the proposals to the Financial Commission for approval;
  - Union government submits the proposals to the Union Hluttaw for approval of the Union budget;
  - Union line ministries inform state/region governments and line departments of the approved state/region budget for each sector; and
  - State/region Planning Department consolidates all approved Union sector budgets into Volume 2, annexed to the State/Region Plan Law.

A few points need to be highlighted in regard to this general overview of the cycle:

- There are important differences between different departments within the same state/region, in both the timetable, the process, and the degree to which they engage in local participatory consultations. For example:

- The Department of Rural Development is much more pro-active in promoting consultations to solicit proposals at the village and village tract levels than, say, the Department of Basic Education or Department of Highways (unsurprisingly, in view of the different types of investments involved).
- DBE submits its budget proposal to the Union level in August, whereas the Department on Rural Development submits only in December.

• There is a key point in the process where, depending on whether the investment is to be funded by the state/region or Union budget, state/region departments then channel their proposals into:

  - Either Stream I: To the state/region Planning and Budget Departments, thence to the state/region government;
  - Or Stream II: to the parent Union ministry. Although in some cases (e.g. the DRD and Department of Basic Education, but not the Department of Health) input is requested from the state/region government (although not from the state/region Hluttaw) before submission to Union level.

It also needs to be noted that in the past two years, two factors have affected the process and the timeline:

• First, in the aftermath of the November 2015 elections, the previous government decided to accelerate the usual budget timetable to ensure approval of the Union and state/region government budgets by January 2016 - i.e. before the newly elected leadership took office - and thus moved up the usual March deadline. The two Time-Charts in Annex 4 illustrate in detail the FY 2016/17 budget timetable alongside the usual timetable, as followed for the FY 2015/16 budget.

• Second, and more significantly, the Medium Term Fiscal Framework (MTTF) reforms adopted by MOPF have led to two important changes in the procedures and timetable for the annual state/region budget process. Please see the ***Key Reforms Underway*** section.

C.3.2. The annual process step-by-step

Generation of annual plan and budget proposals

Plan implementation review (April-June FY N-1)
This exercise is conducted by the State/Region Planning Departments and through the township, district, and state/region Planning and Finance Implementation Committees. The aim is to make an assessment of the implementation status of the state/region Five-Year and annual plans. Implementation reports are prepared and issues identified to inform planning for FY N. Given the timing, this assessment necessarily looks at the plan implementation status as of FY N-2, which is 2 years before the fiscal year for which the plan is being developed.

Local consultation and proposal process (June-July FY N-1)
The focus on securing local input into the annual process only began under the FY 2012-2016 Five-Year Plan. There is now an effort to secure a wider range of local input into the annual planning and budgeting process although, as noted, this varies greatly by sector. These processes are initiated by the Planning Department at each subnational level, which invites line departments at the corresponding levels to submit their investment proposals, together with standard investment proposal forms and guidelines for line departments to complete. See Forms and Instructions used for FY 2016/17 in Annex 5.

The line departments at state/region, district, and township levels proceed to formulate investment proposals, employing varying degrees of local consultation but, to date, this has been circumscribed by the provisions of the Five-Year Plan. These Five-Year Plans generally have detailed provisions for investment, and are sometimes costed for each of the 5 years. As a rule, these provisions are the default for the departments concerned, with flexibility lying in the option to choose just a sub-set, and/or to update the costs or the location of the investment. Any major deviations from the Five-Year Plan apparently require clearance by the Planning Department.

Review and submission to state/region

Investment proposals formulated by local line departments are then processed as follows:

- Proposals to be submitted for state/region budget funding are submitted to the Township Plan Formulation and Implementation Committees (TPFICs) or the District Plan Formulation and Implementation Committees (DPFICs) (depending on the level at which plans are formulated) where they are reviewed, queried, possibly amended, and then in parallel:

  - The Planning Department at that level sends the proposals up to the State/Region Planning Department (for consolidation);
  - The line department at that level sends the proposals up to the state/region line department for review and approval.

- Proposals to be submitted for Union budget funding are sent directly by the line department at that level up to the state/region line department (and they are not reviewed by the TPFIC or DPFIC).

Box 13 Silos at the township level: Limited scope for integrated planning

The formulation and review of investment proposals at the township level are driven by line departments, with the Planning Department playing mainly an administrative role. The Township Plan Formulation and Implementation Committee (TPFIC) does not provide a viable platform to screen or explore inter-sectoral linkages. Further, DAO investment planning is conducted in parallel, with the Planning Department and TPFICs being simply copied on DAO proposals.

Stream I: Proposals for the state/region budget

Review, amendment, consolidation by state/region line departments (August-October)

The state/region line departments receive proposals from their local branches and then review, adjust, and aggregate them, along with their own budget proposals, and they prepare a consolidated set of line department budget proposals for the state/region:

- The capital investment budget proposal is forwarded to the State/Region Planning Department.
- The combined capital and current budget proposal is forwarded to the State/Region Budget Department.

Review and consolidation by the State/Region Planning Department (September-October)

The Planning Department collects capital investment proposals from all line departments, reviews for consistency with the Five-Year Plan, and aggregates these into a combined capital budget proposal for the state/region government. This is then sent both to the State/Region Budget Department and also copied to the Union Planning Department.

Review, analysis, and consolidation by the State/Region Budget Department (September-October)

The State/Region Budget Department combines budget proposals from all line departments, reviews for consistency with budget classification rules and norms, and checks for overlapping departmental proposals. It may amend and/or trim certain proposals if they are judged to be excessive. This may involve some negotiation and iteration with the respective state/region line departments. All finalized budget proposals are then consolidated and forwarded to the State/Region Cabinet and chief minister.

Review, cut-backs, and finalization by the state/region government (November-December)

The State/Region Cabinet and the chief minister undertake a review of the combined budget proposal in order to finalize the budget proposal based on their policy and political priorities, but also in light of the state/region revenue ceiling so that they can achieve a balanced budget. The down-sizing of the budget proposal, in light of the actual revenue ceiling, is a critically important stage in the budget process. Up to, and including FY 2015/16, state/region governments were not informed of the amount of the Union fiscal transfer until January. As a consequence, state/region governments engaged in iterative rounds of 'cut-backs'[38] on their proposals, as follows:

- First round (November): this was normally sent first to the State/Region Hluttaw for approval, and then to the Vice-President and MOPF at the Union level, which reviewed all state/region submissions, determined the size of the deficit grant to allocate to each, and then informed the state/region governments.
- Second round (December): State/region governments then engaged in a round of 'cut-backs' to the budget proposal with iterations between the State/Region Cabinet, Budget Department, and state/region line departments. The resulting reduced budget proposal (now matched to available resources) was then submitted to the Union Financial Commission for approval. However, it was suggested that in some states/regions, a third iterative round was needed as these states/regions were unable to cut-back sufficiently and/or they hoped to gain an increase in the size of the deficit transfer.

Box 14 'Cutting back' budget proposals

The iterative process for down-sizing the budget proposals used to be undertaken in a very short time, with very little opportunity for a technical/economic review of the merits of different options, or for consultation with local stakeholders to better assess preferred options, and a high likelihood of political and bureaucratic lobbying determining the priorities actually selected and excluded.

Union government approval (January-March)

The Financial Commission approves the 'balanced budget' proposals for state/region governments (January), and then the Union government drafts the Union Budget Law (to which are annexed the proposed deficit transfers to states/regions).

This draft Law is submitted to the Union Hluttaw, which passes the proposed law on to the Joint Draft Law Committee and the Joint Public Accounts Committee, which make recommendations to the Union Hluttaw, which then approves the Union Budget Law.

State/Region approval of the Budget and Plan Laws (March-April)

After Union approval, state/region governments submit draft State/Region Budget and Plan Laws to their Hluttaw. Where there are State/Region Hluttaw Public Accounts Committees, these bodies will review the draft laws and make recommendations to the Hluttaw before approval. However, such Committees appear to be established in only a few states/regions.[39] After approval by the Hluttaw, the

[38] One state/region authority preferred to denote this step in the budget process as one of simply 'aligning the budget with financial policy' rather than of 'cutting down' - but this does not change the reality that very substantial reductions of the draft budget proposals need to be made, which in turn poses the basic question as to how expenditures are prioritized (or not) for inclusion in the final budget.

[39] Of the four states/regions under study, there is a Hluttaw PAC only in Ayeyarwady.

laws are signed by the chief minister.

Box 15 Role of the Hluttaw

It is unclear how active a role Hluttaws and their committees play in reviewing the initial budget proposals before they are sent to the Union level. In Ayeyarwady, the Hluttaw apparently does play a role at this stage where the Hluttaw Public Accounts Committee (PAC) claims to have requested cuts to Highways and GAD budget proposals. Elsewhere, the Hluttaw role at this stage is not so clear. However, even if the Hluttaw is involved, the time for its analysis and deliberation at this stage is extremely short and the time for deliberation before final approval is also very limited, to one or two days.

Stream II: Proposals for the Union budget

Review, amendment, and consolidation by state/region line departments (July-December)

State/region line departments receive proposals for the Union budget from township and district levels, and then review, adjust, and aggregate them, along with their own budget proposals, into a consolidated set of department budget proposals for their respective Union line ministry. These proposals are sometimes assigned priorities associated with various ranking criteria.

Box 16 Line departments soliciting inputs from state/region governments: Varying practice

Some state/region departments (e.g. DRD, DBE) first submit their proposed budgets to the state/ region government for comment. In Shan and Kayin, the heads of the State DBE and DRD make formal presentations to the chief minister and Cabinet on their plan and budget proposals, and to solicit their input. But some other departments such as Health simply send their proposals direct to their Union ministry. In no case are State/Region Hluttaws involved in reviewing Union line department budget proposals.

Submission to Union Line Ministries (August-December)

State/region departments submit their (often prioritized) proposals to their parent ministries for review. This step varies considerably by ministry.

For the Department of Basic Education, state/region submissions are generally made to the Union level in August. The process for review, amendment, and approval of proposals by the Union DBE requires 5-6 months (during which period the ministry is also informed of its budgetary allocation for the next year).

Box 17 Submissions to the Union level can also be a continuing process

It should be noted that these proposals are not always sent as a one-time submission to the Union. For example, Kayin State DBE first submitted a proposed list of investments for 105 schools in August 2015, but then forwarded a succession of proposals for another 250 schools between September-December. These additional proposals were reportedly sponsored by various local MPs and other authorities.

During this period, it seems there is little or no consultation between the Union DBE and the state/ region DBE on the proposed plans and budgets. The state/region departments are only informed of the approved plans and budgets around March, which inevitably entails major reductions in what had been proposed.

For the Department of Rural Development, submissions are made to the Union level much later—in November/December. In January, the Union DRD informs the state/region DRD of its budget allocation for the year. The state/region DRD will then cut back its proposal and re-submit it to the Union level, where the final approval is made, and where the state/region budget proposal may be amended.

Union government approval (January-March)

Following Union line ministry approval, the proposed sector budget is submitted to the Union government for approval and inclusion in the Union Budget Law, and follows the process outlined above.

State/region government approval of the Plan Law (March-April)

Following Union approval, the sector plan and budget for each state/region is included in Annex 2 of the State/Region Plan Law, which is approved by the State/Region Hluttaw, and signed by the chief minister.

C.3.3. Key reforms underway

Within the annual cycle outlined, the MTFF reforms have introduced a major innovation.

Up to, and including, FY 2015/16, state/region governments submitted their budget proposals to the Union Vice-President in November before they knew the amount of the fiscal transfer they would receive. This then resulted in one or more additional iterations, after they had later been informed of their grant transfer amount, whereby the state/region government would be obliged to cut back the size of the budget in one or more rounds, and then submit this to the Financial Commission for approval of the budget, based on the size of the deficit transfer to be provided.

The major innovation in FY 2016/17 was that the grant transfers were computed earlier, by formula, and formally announced to state/region governments in mid-November before they submitted their budget proposals to the Financial Commission.

The contrast between the arrangements in place until FY 2015/16, and those just introduced in FY 2016/17 are depicted in figure 17 overpage (note that the 'new' arrangements assume compliance with the 'normal' timetable whereby states/regions approve their Annual Plan and Budget Laws in March, rather than in January, as was the exceptional case in 2016).

However, the reform is in its early days and is interpreted unevenly across states/regions. Even though the grant transfers were announced in November, it seems that a number of states/region governments did not take this seriously as a ceiling, at least initially, and were reluctant to cut down their proposals initially, presumably because they hoped they would obtain a larger transfer. As a consequence, in these states/regions there were still a number of iterations in the budget finalization process, with trilateral negotiations between state/region chief ministers and Cabinets, line departments and the Budget Department, whereby the latter had to encourage that proposals were cut down to the ceiling. In other words, in some states/regions, the previous and very problematic practice of 'bidding' for budget resources based an assumed soft budget constraint, still persists.

The potentially profound impact of this reform on the quality of the budget prioritization process is discussed in Section D.

STATE-REGION ANNUAL PLAN & BUDGET PROCESS - UNTIL FY 2015/16

JUN | JUL | AUG | SEPT | OCT | NOV | DEC | JAN | FEB | MAR | APR

GENERATING PLAN & CAPITAL BUDGET PROPOSALS

- Review current Plan progress
- Bottom up process of consultation at Township level (varies by sector), to Identify projects consistent with 5 Yr Plan

Ln
ID

NEW FISCAL YEAR

T

FOR STATE/REGION BUDGET

- Aggregation of Township, District proposals by SR line depts, review & amendment
- Submission of proposals to SR Plan & Budget Depts for review
- SR Budget discusses with SR Line Depts, adjustment, cut-back, etc.
- SR Budget Dept submits to SR Govt
- SR Govt reviews, amends, submits to SR Hluttaw for approval
- SR Govt submits to Union Vice President & MoF, who determine amount of "deficit transfer"
- SR Govt then engages in iterative rounds of cutback to fit funding limit
SR Govt submits to Union Finance Commission for review, approval
- Union Finance Commission review, approval
- Union Govt submits to Union Hluttaw for review, approval
- SR Govt then submits to SR Hluttaw for review, approval of SR Budget & Plan laws
- SR Chief Minister signs SR Budget & Plan laws

STATE/REGION PLAN & BUDGET IMPLEMENTATION

FOR UNION BUDGET

- Aggregation of Township, District proposals by SR line depts, review & amendment
- In some (but not all) cases, submission by SR Line Depts to SR Govt (but not Hluttaw) for review & input
- SR Line Dept submits to Union Ministry (sometimes one time submission, sometimes ongoing process of referral of proposals from MPs etc)
- Union Ministry reviews all SR submissions, cuts back and approves In line with Its own budget ceiling, policy criteria & other considerations (SR depts generally not consulted)
- Union Govt submits to Finance Commission, then Union Hluttaw for approval
- Union Ministry Informs SR Govt & line depts
- SR Plan Dept consolidates Union Line dept budgets for the SR Into Volume 2 of SR Plan law
- SR Hluttaw approves SR Plan Law (Incl Vol 2)
- SR Chief Minister signs SR Plan Law

UNION PLAN & BUDGET IMPLEMENTATION

JUN | JUL | AUG | SEPT | OCT | NOV | DEC | JAN | FEB | MAR | APR

STATE-REG ION ANNUAL PLAN & BUDGET PROCESS FROM FY 2016/17

JUN	GENERATING PLAN & CAPITAL BUDGET PROPOSALS			JUN
JUL	- Review current Plan progress - Bottom up process of consultation at Township level (varies by sector), to Identify projects consistent with 5 Yr Plan			JUL
AUG		T		AUG
SEPT		FOR STATE/REGION BUDGET	FOR UNION BUDGET	SEPT
OCT		- Aggregation of Township, District proposals by SR line depts, review & amendment - Submission of proposals to SR Plan & Budget Depts for review	- Aggregation of Township, District proposals by SR line depts, review & amendment - In some (but not all) cases, submission by SR Line Depts to SR Govt (but not Hluttaw) for review & input	OCT
NOV	Since FY 2016/17 MoPF informs SR Govt of grant transfer Mid November	- SR Budget discusses with SR Line Depts, adjustment, cut-back, etc. - SR Budget Dept submits to SR Govt	- SR Line Dept submits to Union Ministry (sometimes one time submission, sometimes ongoing process of referral of proposals from MPs etc)	NOV
DEC		- SR Govt reviews, amends, aligns with funding ceiling - submits to SR Hluttaw for approval - SR Govt submits to Union Finance Commission for review, approval	- Union Ministry reviews all SR submissions, cuts back and approves in line with its own budget ceiling, policy criteria & other considerations (SR depts generally not consulted) - Union Govt submits to Finance Commission, then Union Hluttaw for approval	DEC
JAN		- Union Finance Commission review, approval - Union Govt submits to Union Hluttaw for review, approval		JAN
FEB			- Union Ministry Informs SR Govt & line depts - SR Plan Dept consolidates Union Line dept budgets for the SR Into Volume 2 of SR Plan law	FEB
MAR		- SR Govt then submits to SR Hluttaw for review, approval of SR Budget & Plan laws - SR Chief Minister signs SR Budget & Plan laws	- SR Hluttaw approves SR Plan Law (incl Vol 2) - SR Chief Minister signs SR Plan Law	MAR
APR	NEW FISCAL YEAR	STATE/REGION PLAN & BUDGET IMPLEMENTATION	UNION PLAN & BUDGET IMPLEMENTATION	APR

Figure 17 Annual state/region plan and budget cycle: Before and after MTFF reforms

C.4. Subnational planning and budgeting outcomes

The preceding sub-section outlined the procedures for formulating annual plans and budgets. Here the outcomes of these procedures are examined by looking at two questions:[40]

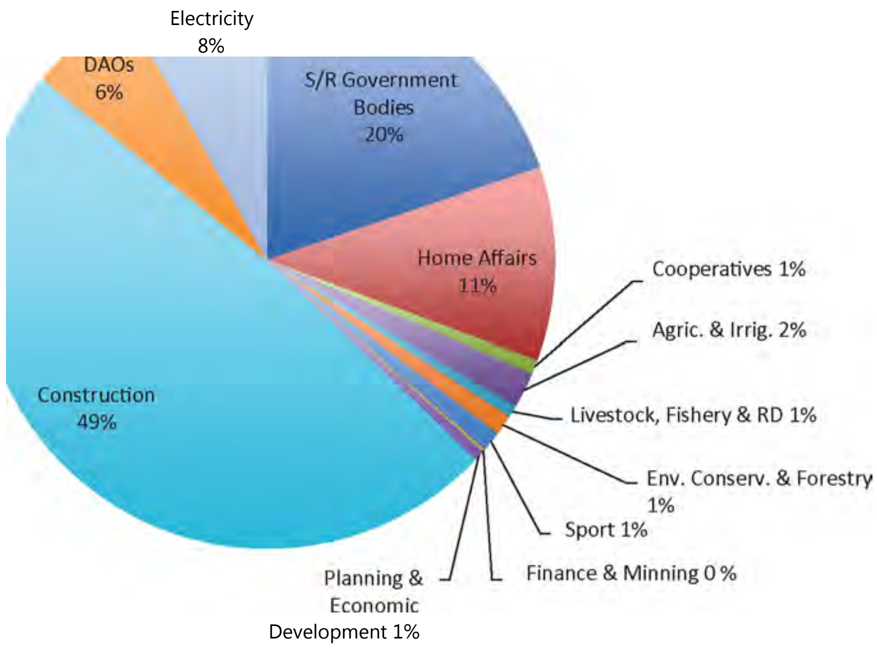
- What are the patterns of expenditure reflected in state/region budgets?
- How do specific capital budget priorities emerge from subnational planning and budgeting procedures, both within state/region budgets and also in Union sector budgets which build on subnational planning?

Expenditures are recorded by ministry and department, and as current or capital expenditure in the same Three Part format used to record revenues.

Annex 3 presents the detailed departmental expenditures—both current and investment—for Ayeyarwady, Shan, and Tanintharyi (BE FY 2016/17) and for Kayin (BE FY 2015/16), in both absolute numbers and as percentages of the totals in each case.

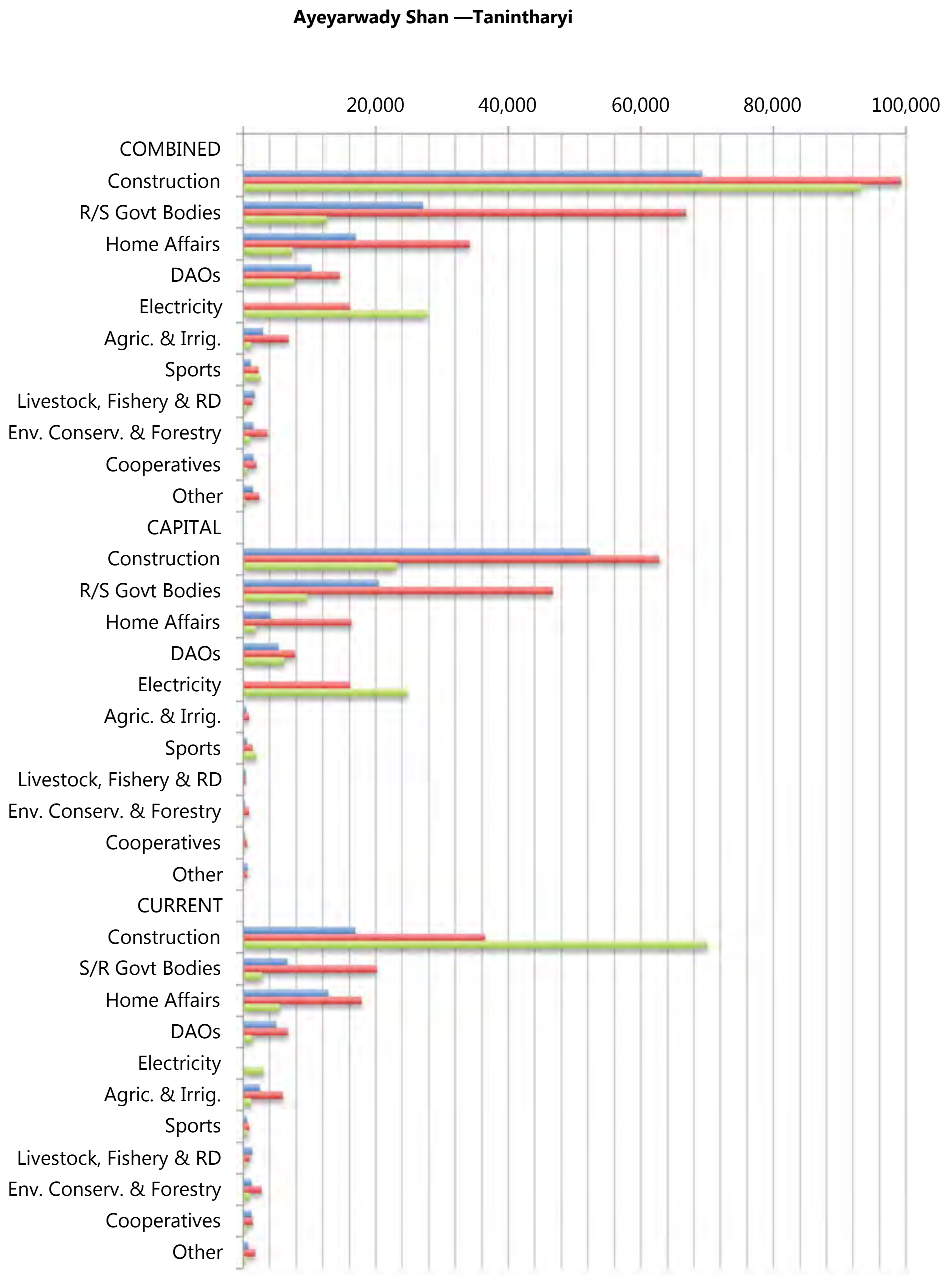
The relative breakdowns by sector are illustrated in figures 18 and 19. The overall average sector expenditure breakdown for Ayeyarwady, Shan, and Tanintharyi for capital and current budgets combined, is depicted in figure 18:

Figure 18 Average breakdown of sector expenditures across Shan, Tanintharyi and Ayeyarwady - FY 2016/17



[40] The data for this section are primarily derived from fieldwork in Shan and Kayin States, and Ayeyarwady and Tanintharyi Regions, and from the budget data provided.

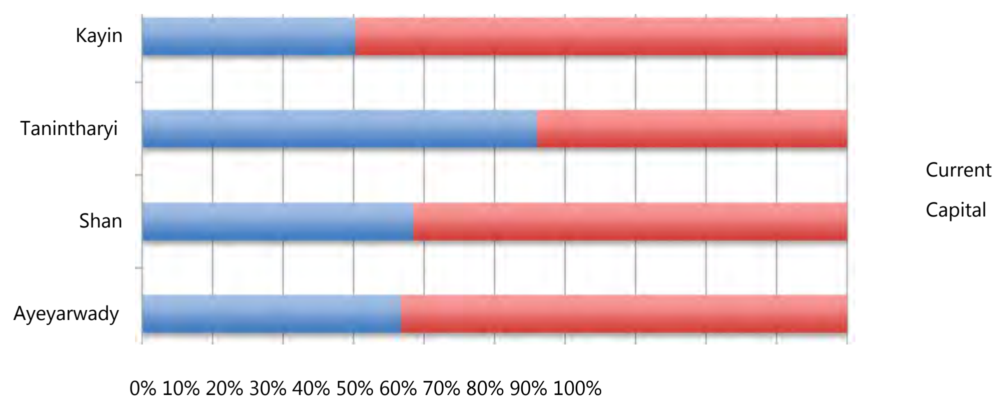
Figure 19 Budgeted expenditures by sector - MMK millions - FY 2016/17



C.4.1. Capital versus current expenditures

The overall balance between current and investment expenditure varies somewhat across the four state and region cases, with capital accounting for just over 40% of all expenditures in Tanintharyi, but up to some 70% in Kayin.

Figure 20 Balance of capital and current expenditures: FY 2015/16 and FY 2016/17



However, these average ratios vary greatly between sectors, simply by the nature of the different mixes of capital and current resources that are required. For example, provision of roads is primarily a capital-budget intensive activity, while provision of agriculture or environmental protection services is primarily current-budget intensive.

That said, there is also some ambiguity in the accounting definitions used to classify expenditures as capital versus current, which may lead to inconsistent recording. In some cases, the distinction was based on the procurement value threshold. In others, it depended on the nature of the asset being created. This might mean, for example, that certain road-related expenditures (such as the purchase of sand and gravel) are, in some cases, recorded as current expenditures, but in others, as capital expenditures. In Ayeyarwady, for example, it appears that 'by tradition',[41] expenditures on water and sanitation facilities at schools were classified as current, despite obviously being used to create fixed capital assets.

C.4.2. Sector and department expenditures

Construction appears as the dominant sector in all four state and region cases in this study (40-60% of all budget expenditures), followed variously by the state/region government (8-27%), by Home Affairs (5-19%), and by the DAOs (3-9%). In two of the four cases, Electricity is significant (6-18%), though in the other two cases, there is no Electricity expenditure at all. Looking more closely:

- Construction. As discussed above, these expenditures are almost entirely from the Highways and Bridges Departments and related to roads and bridges—mainly upgrading and repair of district- and township-level roads and bridges. However, in one state (Tanintharyi), a large share of this budget is actually for Union roads. In most state/region governments, this is primarily recorded as 'investment' (as would be expected), but in Tanintharyi, almost 70% highway expenditure is classified as 'current'. This may be either because there was indeed a predominance of road maintenance expenditure which would normally be classified as 'current' or because, as noted above, certain expenditures are sometimes classified inconsistently.
- State/region governments. This refers to the administrative and investment expenditures incurred by the subnational government and related entities (Hluttaws, Courts, etc.), the bulk of which are for investments presumably in administrative infrastructure, equipment, and vehicles.

[41] Interview with the Regional Auditor General and staff in Ayeyarwady.

- Ministry of Home Affairs. This refers mainly to varying mixes of current and capital expenditure incurred by the GAD at the state/region, district, township, and ward/village tract levels, though this may also include some local expenditures for Fire or Police Departments, which are also under the same ministry.

- DAO. This refers to various urban infrastructure (roads, drainage) and service expenditures (waste management, water supply), and to the administration costs incurred by the DAOs, and financed by their own revenues.
- Electricity. This refers primarily to investments in local power supply and distribution networks that are off the national grid.

By contrast, the virtual absence of the following expenditures in subnational government budgets is striking:

- Education and Health. These are conspicuous by their complete absence from the budgets. This, as discussed under section B.2, of course reflects the total control that Union ministries retain over these sectors.
- Departments delivering other local public goods and services in rural areas such as Agriculture and Irrigation; Livestock, Fisheries, and Rural Development; or Environmental Conservation and Forestry, all together account for no more than 2-5% of total state/region government expenditures. Yet these are, in principle, all functions in which state/region governments appear to be allowed to play a role, at least according to Schedule 2 of the 2008 Constitution.

Also, as discussed earlier, these are all sectors where there are many types of expenditure that are much more appropriately undertaken at the subnational level, and (as in many countries) even at lower levels of government than Myanmar's state/region level.

C.5. How subnational capital budget priorities are actually made

This section examines how the investment priorities actually selected for inclusion in the state/region and Union budgets emerge from the planning and budgeting processes outlined above.

C.5.1. A general necessary condition: Inclusion in the Five-Year Plan

In all sectors, and whether funded by the state/region government or by the Union budget, a primary factor in determining the priorities to be selected lies in the Five-Year State/Region or Union Plan for that sector, which contains lengthy lists of investments, with an indicative yearly implementation schedule for each of the five years. This sets the main parameters for investment selection, and largely indicates the universe within which almost all investment proposals must be selected, or at least fine-tuned and detailed, since any investments not in the Five-Year Plan require special approvals.

In other words, for a proposal to be included in the annual investment budget, it is almost always a necessary condition that it has already been included in the Five-Year Plan. However, this is clearly not a sufficient condition, and whether these plan proposals are then included or not, depends on further determining factors.

C.5.2. Priorities in state/region capital budgets: Roads and bridges

The dominant expenditure category in state/region budgets is roads and bridges, which is mainly upgrading and maintenance of the secondary network of classified state/region roads and bridges. Although, as seen previously, state/region expenditures on the Union network can also be significant.

Determining factors for investment budget priorities

- The bottom-up planning process. This annual process generates lists of road/bridge investment proposals, largely consistent with the Five-Year Plan, which are channeled up to, and aggregated at the State/Region Construction Department level, with no weeding out at the township or district levels.

- Ranking and priorities. In the course of this planning process, there is often an attempt to assign some relative priority to proposals, and two criteria are used for this:

  - Average Daily Traffic (ADT) is a measure which is allegedly used to give relative priority to road proposals. It was not clear though whether the data used for this purpose are recent or reliable, nor how the ADT measures are used. As a ranking measure, it is useful, but only if also related to the relative costs of different road projects. But in one state, it seemed to be less used as a ranking criterion, and more as a guide to determine the upgrading standard.

  - The status of the proponent. In two state/region governments visited for this study, the Department of Construction claimed to weight proposals according to who was the proponent—with the highest weight given to important Union-level officials, then to state/region ministers, then to MPs, then to township administrators, and so on. This may be a sign of practical political realities, but such an approach is clearly not the best way to ensure selection of investments that are the most likely to promote local socio-economic development or be the most efficient or equitable.

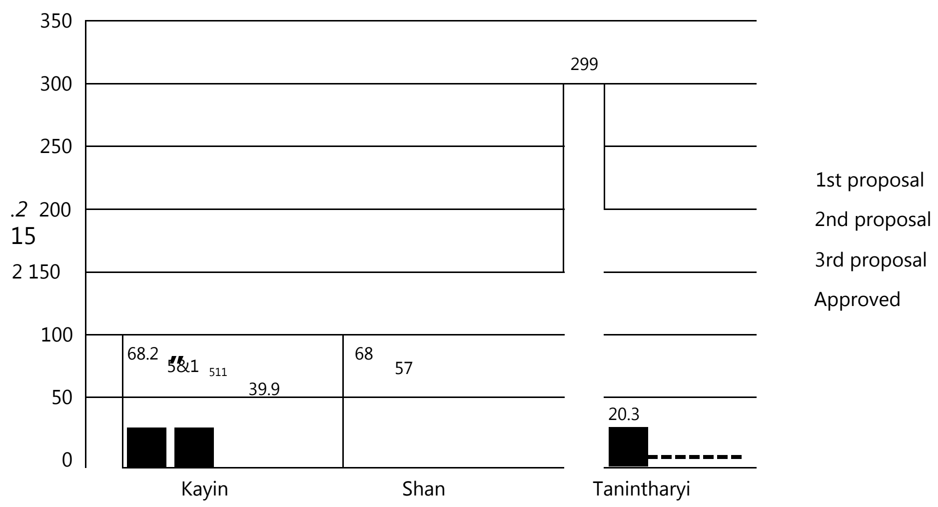
  - No economic appraisals, ranking tools, or proxy measures are used by the Department of Highways, or recommended by the Planning Department, to try to assess the relative economic merit, or the cost/benefit ratio of alternative road investments. Nor does state/region governments appear to apply any geographic criteria to favor road investments in areas of economic potential or areas of neglect.

- Hurried negotiation. As seen previously, the number of proposals submitted by the Department of Construction (DOC) to the state/region government invariably greatly exceeds the funds available. These proposals have to be cut down very quickly to the level which is affordable, and is often done in several iterations. This occurs, however, with no obvious use of transparent, technical or socio-economic criteria.

The priorities that emerge

Figure 21 depicts the proposal-cutting process, which in Tanintharyi Region was especially drastic. In Kayin, three rounds of submission and negotiation led to the funding of only about half of the original list of capital investments, and two thirds of the original current budget proposal. In Tanintharyi, only 10% of the original proposal was approved.

Figure 21 Roads budgets: From proposals to final approval in 3 states/regions - MMK billions - FY 2016/17



Source: State/Region Departments of Construction

Given the budget timetable discussed further above, the cutting process has to be undertaken very quickly in a matter of days, through a series of negotiations between the Department of Construction and the Budget Department, but where ultimately, it is the state/region Cabinet and chief minister who make the final decisions. In this rushed process, it is hard to see how technical/socio-economic criteria, even if such existed, could be properly applied to guide this decision-making over such a wide range of proposals.

The typical outcome of this process is a list of road and bridge investments which:

- Are generally a sub-set of the wider set of investments indicated in the Five-Year Plan.
- Are spread evenly across all townships in the states/regions, rather than focused in specific areas (of need or potential).
- As a consequence, typically result in fragmenting investment expenditures across small sections (2-3 km per township) of all or most state/region roads, rather than focused on a few specific roads.

In the case of roads and bridges, a factor that probably reinforces this spread of investment is that implementation is universally undertaken on a 'force account' basis by the local Construction Department or Road and Bridge Construction Units, rather than by sub-contracting to the private sector. Such a 'mode of production' allows expenditures to be more easily spread out than would be the case with sub-contracting. But more importantly, it also probably means that the planning and budgeting process faces a strong bias to ensuring adequate work for all departmental implementation staff across the entire state/region—a factor which may discourage focusing the investments in specific townships, and excluding others.

C.5.3. Priorities in line ministry budgets

Basic education

Determining factors for basic education investment budget priorities

- The bottom-up planning process. This annual process generates lists of investment proposals, largely consistent with the Five-Year Plan. These are channeled up to, and aggregated, at the State/ Region Department of Basic Education, with no weeding out of any proposals at the township or district levels. However, as Table 15 indicates, a very high percentage (up to 50%) of approved DBE investments appears to be proposed by other sponsors, and so these proposals may not emerge from this bottom-up process at all.

- Ranking and priorities. The DBE generally applies a set of three technical criteria to rank school investment proposals, whereby proposals are rated with regard to whether:

    - The current state of school facilities poses any danger to pupils (e.g. in danger of collapse) such that investment is needed to reduce this danger.
    - Investment would increase the number of pupils who can attend, and/or whether the school being targeted for investment already has a large number of pupils.[42]
    - Investment would improve the local 'image' of the school.[43]

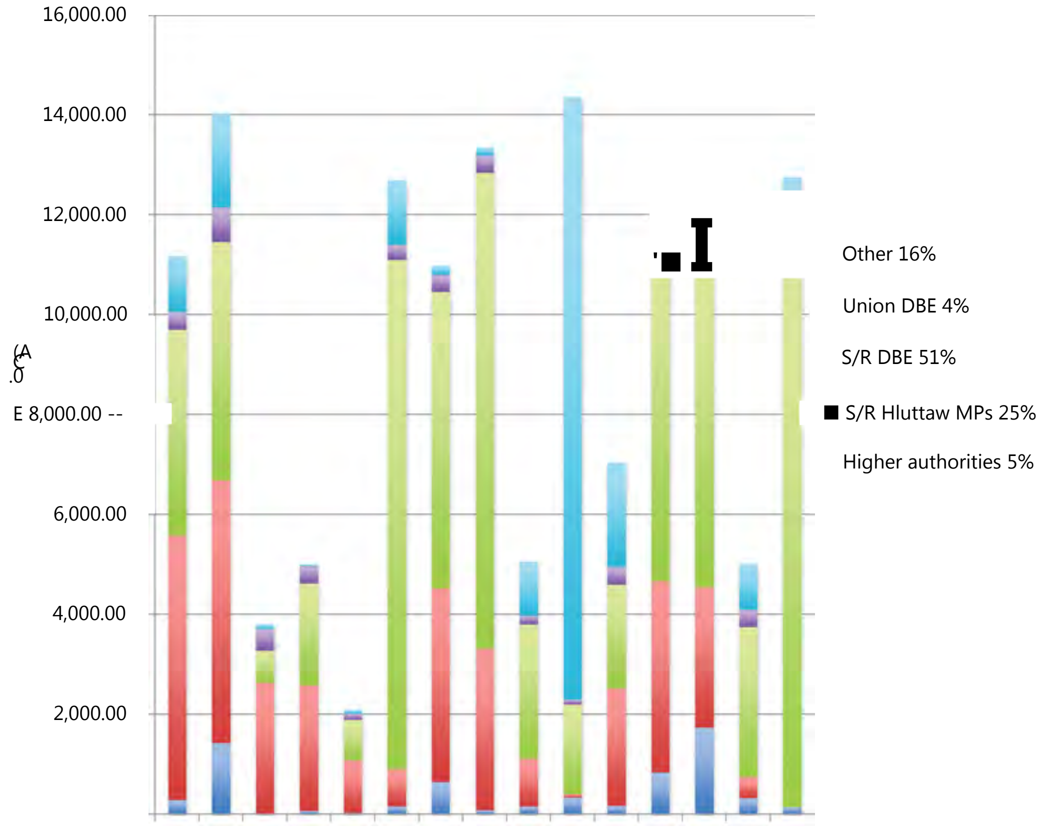
    However, it was not possible in this study to ascertain exactly how these criteria are applied in practice, and it seemed that each state/region may have used them differently.

    In Kayin State, it was suggested that, in addition to the three criteria above, proposals were also rated according to the proponent (as was noted previously in the case of roads), with preference accorded to schools with the backing of an MP or state/region minister, or other high-ranking officials.

    This appears to be supported by the fact that the Union DBE itself issued a report on school investments which were clearly categorized by proponent. Figure 22 (based on data from Table 15) clearly illustrates this. It shows that - nationally - while 51% approved school investments were directly proposed by state/region education departments, and 4% by the Union department, another 45% were proposed by MPs together with various other authorities (this pattern however varies greatly across the 14 states/regions). The underlying question is how far investment proposals from these various authorities were appraised and ranked somehow by their inherent "merit" as against the "status" of the proponent. To the extent that the latter is the case then there must be serious concern that school investments selected for funding are not always those which yield the greatest socio-economic benefit or the most equitable pattern of expenditure.

[42] Contradictory interpretations of this criterion were given in different states/regions.
[43] It was not clear what this means in practice.

Figure 22 Approved basic education investments by proponent - FY 2016/17



Source: Union Department of Basic education

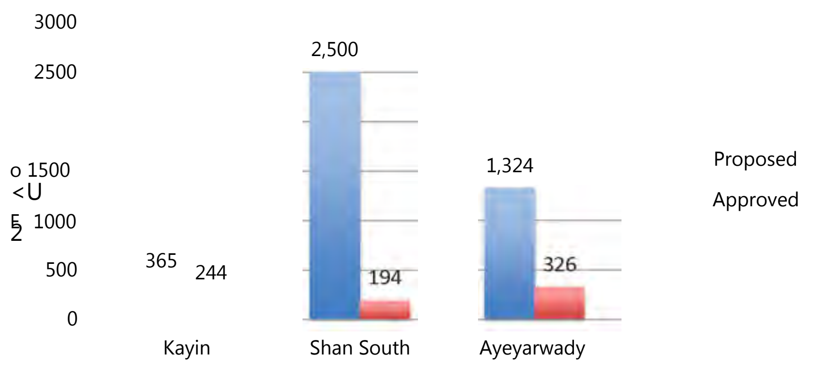
Throughout the DBE planning process, no geographic criteria appear to be used to target plan and budget resources to schools in the most deprived townships. This is despite the concerns documented in the Comprehensive Education Sector Review (CESR) which, in regard to basic education, identified continuing disparities in both enrolment rates and in education quality between states/regions, as well as between more urban and more rural, remote areas.[44]

The priorities that emerged

Figure 23 indicates the extent of the drastic 'cutting-back' process that took place in three states/ regions - with especially drastic cutting down of proposals from Shan South and Ayeyarwady.

[44] "Comprehensive Education Sector Review - Phase 1 Rapid Assessment Report" pp 27, Ministry of Education (2013).

Figure 23 Basic school investments from state/region proposal to Union approval - FY 2016/17



Source: State/Region Departments of Basic Education

It was not entirely clear whether or not the proposals by the state/region DBE include the many proposals made by other proponents: important officials, MPs, etc. (if this was not the case, then the cut-backs were relatively even more drastic).

How exactly the Union Department of Basic Education identified budget priorities within the state/ region DBE proposals was unclear. As noted, there appears to be no consultation, and State/Region Departments of Basic Education are simply presented with the results at the end of the process.

The Kayin State DBE claimed that the top priority proposals from all seven townships were respected in this selection process. Generally, given the lack of any geographic targeting of school investments, it seems that the typical outcome is indeed a list of school investments that are spread evenly across all townships in the state/region, rather than focused on specific areas of need or deprivation.

Rural development

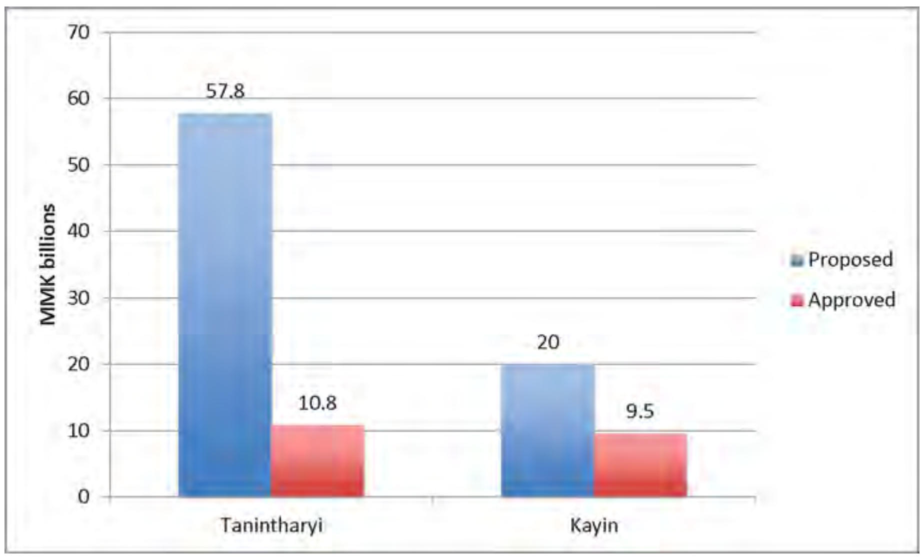
Determining factors for rural development budget priorities

- The bottom-up planning process. This process managed by the DRD is relatively developed, allowing villages and townships to generate a large volume of small, community-level investment proposals across the range of infrastructure types funded by the DRD. However, it was not clear how far these investment proposals face limits imposed by the Five-Year Plan, or whether small-scale investment proposals enjoy greater flexibility, being included within more aggregate 'block' provisions in the Plan. As with other sectors, proposals are sent up from the township to the district, and then to state/region DRD level, being simply consolidated at each level, without little screening or weeding out.
- Ranking and priorities. It was unclear if, or how, the varied range of investment proposals are ranked and prioritized by DRD. The only indication of a ranking method was in Tanintharyi and Kayin where DRD proposals are rated by the sponsor (a 'very important person', or an MP) and which may well not emerge from the bottom-up planning process, but are given higher weighting than other proposals.

The priorities that emerge

Figure 24 illustrates the extent of the cut-backs made by the Union DRD, with regard to the original submissions from Tanintharyi and Kayin.

Figure 24 DRD: From state/region proposal to Union approval - MMK billions - FY 2016/17



Source: State/Region Departments of Rural Development

In Tanintharyi, especially, there was a drastic 'cut-back' in the original proposals. These cut-backs and re-prioritization exercises apparently took place in a short space of time between December and January. No doubt, the inclusion and exclusion of proposals were at least partly determined by the fact that the DRD manages several donor-funded projects, with funding earmarked for specific types of expenditures (e.g. rural electrification). Hence, certain investment-type proposals were given implicit priority over others. Overall, it was hard to see how a very thorough review of the merits of different proposals could have been undertaken in such a short time, even if there were guidelines and criteria for doing this.

C.6. Planning and budgeting procedures: Issues arising

A wide range of issues emerge from the discussion above, indicating various factors which risk compromising the quality of subnational planning and budgeting.

C.6.1. Planning arrangements and procedures

Three problem areas undermine the quality of state/region investment planning and budgeting:

- Lack of an effective, local institutional platform to identify the planning and expenditure issues arising from 'connections' between 'layers', e.g. between rural and urban networks, or between village and township/district roads. Planning and budgeting expenditures for each of the layers was largely undertaken in separate departmental 'silos'. This could easily lead to strategic constraints or opportunities being missed, and/or to duplication.

- Lack of adequate procedures and criteria (indeed, the use of rather perverse, overtly political criteria, such as the 'status' of the sponsor, in some cases) to prepare, rank, and appraise competing investment proposals to ensure that those which were the most effective and efficient would be funded. With a move towards more bottom-up, participatory planning, such arrangements, and their transparency, will become ever more important if widespread frustration is to be avoided.

- Lack of operational criteria which could translate policy concerns about geographically inequitable access to basic services which clearly characterizes many sectors, and which could promote geographic targeting (to areas of greatest need or potential). Relatedly, there was an institutional bias toward spreading resources evenly - but inequitably - across all townships.

C.6.2. Information, time and incentives

At least until FY 2016/17, the practice whereby state/region governments submit one or more initial budget submissions to the Union level without knowing the level of fiscal transfer has had the following very perverse consequences:

- Lack of a known budget ceiling has encouraged generating an inflated volume of plan and budget proposals, with no real incentive for any serious weeding out or prioritization at township, district, or state/region levels. The recent announcement of the grant transfer amounts, starting in November 2016, will help to address this problem, but much better communications are needed to ensure that state/region authorities realize that they now face a hard budget constraint.

- Conversely, the inflated volume of proposals has reduced the capacity to properly formulate investment proposals through adequate consultation, checks, assessments, and costing.

- The FY 2016/17 budget calendar allowed only 2-3 weeks time between the announcement of the grant transfer ceiling (18th November) to the deadline for submission of the proposed budget to Union level (8th December). The very hurried, last-minute cutting-back of state/region budget proposals, mainly by the State/Region Cabinet, Budget Department, and line department heads to fit the level of fiscal transfer announced, has inevitably occurred without any thorough review of the 'pros and cons' of the competing options, or any adequate consultation with either technical staff of the departments concerned, or with stakeholders at the local level.

C.6.3 Role of the State/Region Hluttaw

The Hluttaws and their Public Accounts or Plan and Budget Committees play a fairly marginal role in the state/region plan and budget process (and none at all in the deconcentrated plan and budget processes).[45] It is not obvious how they are involved in the critical initial budget preparation stages, prior to initial submissions. Even if they are, they have very little time (given the time window noted just above) or expertise to provide effective review or input. The subsequent Hluttaw final review and approval of the budget (in March/April), takes place when there is not only little time, but also little scope to introduce much change, given that the Union has already approved the draft budget.

It was frequently argued that the role of the Hluttaw is ensured through the active involvement of individual MPs in sponsoring budget proposals in their areas. This, however, misconceives the importance of the collective, institutional role of members of the legislature in providing a check on the state/region administration and querying the merits of budget proposals, which is quite different from, and goes much beyond, the lobbying of individual members for projects in their respective constituencies.

[45] The names of these committees vary across the states and regions. At the time of this study the committees for the newly elected Hluttaws had not yet been established in at least two states/regions.

D. Conclusions and Directions for Reform

This section draws out conclusions from the issues raised in the previous sections about the quality of subnational public financial management (PFM) and service delivery, and proposes some directions for reform of subnational planning, budgeting, and financing arrangements.

D.1. Conclusions on the quality of subnational planning and budgeting

The previous sections have revealed issues which, in different ways, all undermine the quality of subnational planning and budgeting, and hence the quality of public service delivery in states/ regions. Conclusions about the impact of these issues on the quality of PFM can briefly be drawn through three key dimensions.

D.1.1. Effectiveness and efficiency

Effectiveness and efficiency are measures of the extent to which public resources are: (a) allocated according to national and local policy priorities, and (b) deployed so as to obtain the greatest impact and benefit, as well as to minimize costs. Both effectiveness and efficiency are compromised in various ways:

- Generally, the high degree of Union control over budget decisions means that, for lack of adequate information at the Union level, relative local needs and priorities may often be overlooked by, indeed simply not known to, central decision-makers when they review plans and budgets for local public goods and services. This applies, for example, to planning and budgeting decisions for small-scale investments, where local knowledge is especially important in shaping the right priorities.

- The silo-based planning, and lack of effective inter-sectoral planning platforms at subnational level, means that opportunities for linkages and synergies (e.g. between urban and rural investments) are missed.

- Various own-source revenue constraints greatly limit the overall resources available for expenditures on local priorities. This has been exacerbated by locking DAO revenues solely for use in urban areas, which reduces local resource-allocation flexibility within states/regions.

- The subnational budget preparation and prioritization process has been greatly weakened by the lack of any budget ceilings, either for township or district level, or for state/region departments. This, then leads to a greatly inflated number of proposals from each level and each department, which cannot be properly vetted, costed, appraised, or ranked within the time and staff resources available.

- Furthermore, the inadequate procedures and technical criteria for appraising and ranking alternative expenditure proposals mean that the selection of priorities for funding must often not be those which best meet national, sector, or local policy objectives, or which ensure that the benefit-to-cost ratios are maximized. The greater the move to soliciting bottom-up proposals in the planning and budgeting process, the more this problem becomes acute.

- Relatedly, the bias toward the 'equal spread' of expenditures across townships means that policies toward reducing geographic inequities within states/regions cannot be adequately implemented.

D.1.2. Equity

Equity is the measure of the extent to which budgetary resources are allocated according to relative need.
Between states and regions, there are clearly important variations in need and poverty levels. However, the major variations (a 1:12 ratio) in state/region budgetary resources per capita (resulting from large disparities in fiscal transfers per capita) do not appear to correlate at all with these variations, and pose a major geographic equity issue. This inequity will, in turn, undermine the attainment of national development policy goals, and hence the effectiveness of local PFM. It may also pose a political problem at some point.

As noted previously, within states and regions there is a tendency to ensure fairly equal spread of expenditures across districts and townships. However, given the very different population sizes and levels of poverty and deprivation across townships in many states/regions, this sort of 'equality' is actually not at all equitable.

In regard to deconcentrated line ministry resources, the only available data are for the DBE which also suggests an inequitable allocation pattern across states/regions, albeit much less so than for general revenues. Here too, the bias to equally spread DBE investment expenditures across townships in the same states/regions exacerbates intra-state/region inequities.

D.1.3. Transparency and accountability

Transparency and accountability are measures of subnational PFM quality. Here too there are problems:

- Information on state/region budgets and actual expenditures is not readily accessible, and certainly not to the general public. The procedures for selecting some budget priorities for funding and not others, and the outcomes of these procedures, are unclear, even after much probing.

- The state/region Hluttaws appear to play a very limited role in ensuring local accountability of the budget preparation and approval process:

  - It is not clear how much the Hluttaws have a chance to review or comment on the initial budget proposals which are submitted to the Union level by state/region governments.
  - The Hluttaws appear to have had no role in the critical, iterative cutting-back negotiations through which initial state/region departmental proposals are reduced to fit the resources available.
  - The main role of the Hluttaws appears to be in reviewing and approving the state/region budget after it has been approved at the Union level, and where the chance to make major changes is very limited.
  - The Hluttaws play no role at all in reviewing budget proposals submitted to the Union ministries by state/region line departments.
  - Even where they are able to review budget proposals, the state/region Hluttaws (and their specialized Public Accounts or Budget Committees) are severely constrained: (a) they have very little time for this review given the number of budget proposals to be examined; and (b) they appear to have had little training and guidance in budget analysis.

  There seems to be a widespread view that, since individual State/Region Hluttaw representatives tend to be very actively involved in sponsoring budget proposals, the role of the Hluttaw overall is not so critical. However, this is not the case: it must be understood that the role of MPs in sponsoring their individual township interests is a very different one from the ensuring the collective role of the whole Hluttaw in holding the state/region administration to account in the budget process.

D.2. Some directions for reform

D.2.1. Greater clarity and more decentralization of expenditure responsibilities

Section A documented the very limited degree to which expenditure responsibilities are currently decentralized, as well as some of the anomalies and inconsistencies. A phased strategy of promoting greater decentralization has already been outlined elsewhere,[46] but can be restated as follows:

Short-medium term: promoting greater de-concentration

There are several types of expenditures currently managed by line ministries at the Union level, which could be deconcentrated to their respective state/region ministerial departments. Examples are the range of small-scale rural infrastructure and services funded by the DRD, investments in basic education facilities funded by the Ministry of Education, and investments in basic health facilities funded by the Ministry of Health. In each case, the respective Union ministries would need to:

- Define a list of specific expenditures over which the state/region department directors are to have planning and budgeting approval authority. These would typically be small/medium capital or maintenance expenditures whose impact and potential beneficiaries would be contained within the area of a district or a few townships, and which have no wider external effects outside the state/region in question, or fiscal consequences for the Union budget (hence, investments in new facilities requiring new staff assignments might be excluded).

- Devise a funding formula or set of norms[47] to determine the annual budget allocation to states/regions to finance these expenditures. This formula should reflect sector goals and differing levels of poverty or service coverage across states/regions, but also generate allocation outcomes per capita which are not in extreme variance.

- Devise simple budget appraisal, prioritization, and ranking procedures and guidelines to ensure that all state/region departments select proposals for funding in a consistent and transparent manner, and which ensure that those proposals included in the budget will result in greatest net socioeconomic benefit.

- Ensure that this budget ceiling is communicated to state/region departments as early as possible in the annual budget process, and that officials are trained in budget prioritization and ranking procedures.

These arrangements can usefully be piloted in selected states/regions for a budget cycle before being extended nation-wide.

The role of the Union line ministry would simply be to review, ex-post, the budget process of the state/region departments and check for compliance with the agreed procedures, but not 'second-guess' the selections made.

One issue that needs to be clarified in such deconcentrated arrangements is the role of the state/region government and Hluttaw, and how far these bodies can, or need to be, involved in the finalization of these deconcentrated sector budgets to bring their knowledge of local needs and priorities to bear on the process.

[46] See, for example, Hamish, Nixon and Cindy Joelene. *Fiscal Decentralization in Myanmar: Towards a Roadmap for Reform.* Discussion Paper 5 (Yangon: The Asia Foundation and MDRI-CESD, 2014).

[47] There is a body of international practice in the use of such sector allocation norms.

Development partners supporting these sectors would have a potentially important role to play in helping develop and monitor such reforms.

Medium-longer term: Promoting greater devolution

There is an opportunity to move towards greater devolution—that is, to assign responsibility for planning and budgeting for a clearly-defined range of local public goods and services to state/region governments. This will allow both greater potential gains from decentralization than could be obtained from simple deconcentration, and will help strengthen the legitimacy and viability of the state/region governments. A move toward greater devolution will entail:

- Identification of a few, select candidate sub-sectors, e.g. rural water supply, rural roads, basic education, basic health, etc.
- In each sub-sector, unbundling the main delivery functions under:[48] policy (setting of goals, standards, etc.), staff (hiring, payroll, supervision), assets (planning, budgeting, procurement, operations and maintenance), etc.
- Identification of those functions that can be handled by states/regions in light of key principles (subsidiarity, scale economies, externalities, and equity) and of capacity issues. The prime candidates would normally be planning, budgeting, procurement, and maintenance of small- and medium-sized investment assets (as already underlined, most policy and very many other functions are best left to the Union government).
- Estimation of likely expenditure implications for states/regions by application of average cost norms for these functions.
- Determination of the appropriate mode of financing these expenditures. Initially at least, it will be simplest to devise a conditional, formula-based grant which can only be used by states/regions for expenditures within the sub-sector.

This exercise is, however, a challenging one, both technically and politically. It means a transfer of resource control from Union line ministries to state/region governments, which may well be resisted. While the Budget Department's Intergovernmental Fiscal Relations Division (IFRD) would play a lead role, it will also require:

- At the least, a process of close consultation with, and buy-in from, the line ministries concerned, and also preferably some real-time on-the-ground piloting, monitored by the line ministry to test decentralized arrangements and reassure ministry policymakers.

- More broadly, a policy agenda to devolve more functions to states/regions will also require high-level political backing and oversight at the Union level, e.g. an inter-ministerial, inter-governmental fiscal relations working group or committee that reports to the Financial Commission, with the IFRD as the secretariat.

Resolving anomalies and inconsistencies

A number of anomalies and inconsistencies in subnational expenditure responsibilities were highlighted in Section A, and there may be many more that were not identified. These weaken the quality of subnational PFM, and will undermine sound inter-governmental fiscal relations unless they are resolved. There is both a short-term and a longer-term challenge here:

- In the short term, a review is recommended to better document these current, obvious anomalies and inconsistencies, and propose resolution, whereby: (a) there is clear definition of those expenditure responsibilities that are exclusively under state/region budget authority, and those

[48] See Section A.1.4 of this report.

under Union budget authority; and (b) any splitting of responsibilities between capital and current budgets related to the same public goods/services is minimized. This review could be undertaken by the IFRD and then submitted to the working group or committee suggested above for approval action on the recommendations.
- In the medium-longer term, as the policy agenda for greater devolution of expenditure functions proceeds, it will be necessary to ensure the ongoing review of the legal and regulatory framework in order to identify outdated, sector-related provisions that will need revision. This ongoing review would require collaboration between the Budget Department, line ministries, and the Bill Committee of the Union Hluttaw.

D.2.2. More effective and equitable financing

Rationalizing own-source revenues

A number of measures would strengthen own-source revenue mobilization, but some are easier and quicker to implement than others:

Shorter term
- Ensure that the tax and fee rates are updated from previous levels.
- Develop simple programs of guidance and training to improve tax and fee assessment, billing, collection, and administration procedures.
- In order to facilitate monitoring, change the classification of revenues in the state/region budget to more clearly separate, genuine own-source revenues from various Union transfers.

Medium-longer term
- Review the prospects for unifying state/region tax revenue collection responsibilities under one, single tax-administration unit.
- Review issues arising from laws and regulations not aligned with Schedule 5 of the 2008 Constitution and undertake reforms to clarify state/region revenue powers.

Rationalizing revenue-sharing

A review of all the current revenue-sharing arrangements between the Union and state/region governments or their departments is needed in order to assess the overall flow patterns so that the most appropriate way of sharing revenues with the states/regions can be determined. There are reasons to ensure that some of these revenues are shared on the basis of area of derivation, e.g. to allow states/regions to finance expenditures to either promote or to mitigate the impact of the activity being taxed (e.g. natural resources, tourism, etc.). However, a careful examination is needed of the equity implications of possible future natural resource revenue arrangements, and which would require compensation through the grant transfer mechanism. But other shared revenues may be better added to the general grant transfer pool.

The commercial and special goods tax-sharing initiative seems to be an example of the latter. There is no obvious reason to allocate this shared revenue on the basis of area of derivation. It would seem to be simpler and more transparent to place these total revenues into the grant transfer pool, and allocate the combined pool using the formula given in Box 19.

Further development of the grant allocation formula

In order to better ensure more equitable and more defensible per capita levels of revenues and expenditures across states/regions, it is proposed to further develop the grant allocation method and formula. If own-source revenues were at fairly similar levels across states/regions, it would be feasible to simply ignore the fiscal constraint and just use a purely needs-based formula, as many countries do.

But the fact that Yangon Region, and to a much lesser extent Mandalay Region, have much higher levels of own-revenue than other states/regions, means that the difference in fiscal constraint does need to be factored-in.

In order to avoid the incentive problems associated with inclusion of own-revenue criteria, one option is to move toward an approach that is based on both relative need, and also the own-revenue potential of different states/regions, using the Representative Tax System (RTS) approach practiced in a number of countries.

Box 18 'Representative Tax System' approach to allocating fiscal transfers

"The RTS may be defined as a hypothetical tax system that is 'representative' or 'typical' of all the taxes actually levied by subnational governments of a country. As such, it abstracts from the actual tax policy of individual subnational governments, yet it is representative of those taxing practices in the aggregate/average. The purpose of the RTS is to measure the own-revenue-raising-ability of subnational governments .... it provides information in designing intergovernmental transfers system. The RTS provides yardsticks for measuring the potential ability of each subnational government to raise revenues from their own sources."

From "Equalisation Across Sub-National Governments", S. Yilmaz, World Bank Institute.

Such an approach could proceed as follows:

Box 19 A possible alternative allocation formula and method

Short-term: Next 2 years

The RTS approach requires information about the revenue base in each of the regions/states. Given the current levels of collection from this base, it would take time to build up. Consequently, for the first year or two, a cruder approach will be needed, as follows:

Step 1. Estimate the target expenditure levels for each state/region, as follows (using FY 2016/17 data):

(a) Estimate total revenues available for subnational expenditure. The grant transfer pool + the -shared revenue pool + the sum of all state/region own revenues for the previous year. For FY 2016/17, this totals approximately MMK 2,500 billion.

(b) Agree on a simple formula for determining the relative need of states/regions. It is proposed to use the three need variables already being used, but with different weightings, such as: population (60%); poverty (20%); and land area (20%). The fiscal constraint element is addressed under Step 2.

(c) Estimate target expenditure for each state/region, applying this formula to the total pool estimated above.

For example, the target expenditure (TE) share from the total pool (transfers + shareable taxes + all own revenues) for state/region 'n' would be estimated as follows:

TE n = [(pop n /pop total) x (60% pool)] + [(pov index n x pop n) / (av pov index x pop total) x (20% x pool)] + [(land area n / land area total) x (20% x pool)]

Step 2. Estimate the grants required to meet target expenditure levels for each state/region, as follows:

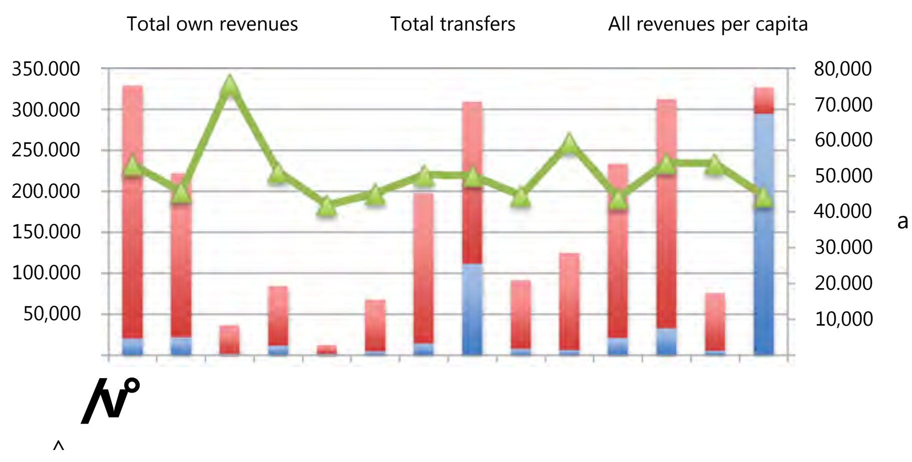
(a) From the target expenditure level for each state/region, subtract actual own revenues of that state/region for the past year (i.e. the same amount as used under Step 1.a. above).

(b) This difference is the size of the grant needed to fill the gap to meet the target in each state/ region.

Figure 25 shows the results of one possible simulation of this method, using the fiscal transfer pool for FY 2016/17 and own-revenues for FY 2015/16. The variance in outcomes of revenues per capita is much less extreme, and would seem to be much more equitable and defensible than those from the current formula.

The following figure illustrates the outcomes generated by the specific approach outlined in the Box above - total levels of revenue by source and total revenue per capita. The variance between lowest and highest total revenues per capita is about 1:2.

Figure 25 Simulation state/region revenues under a revised formula



As noted, there are many variants on such an approach whereby different combinations of weightings may be given to the need indicators, but population weighting should be kept as the principal factor.

Medium term: After 2 years

By using historic, actual state/region own-revenues, it is possible to avoid the incentive problem, but this is only feasible for 1 or 2 years. It is necessary to prepare to move to an approach based on the different own-revenue potential of states/regions, which is the Representative Tax System approach.

In the meantime, therefore, it is necessary to begin the research needed for using the RTS approach to allocating the grants. This requires an analysis of: (a) tax and non-tax revenue potential in all states/ regions—at least for the major revenue sources; and (b) the current rates of collection for these sources so that a national average collection rate can be constructed.

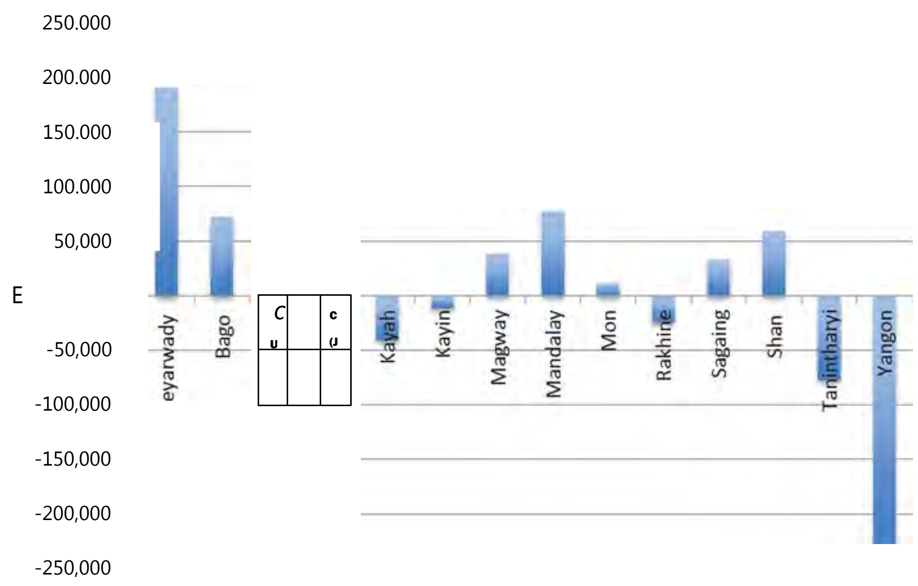
It is important to capture all own-source revenues in the variable—that is not only tax revenues but also other current revenues which are actually the main source (although this balance is likely to change if, and when, tax rates, and ultimately state/region tax powers are increased).

Winners and Losers

Many variations on the approach outlined are possible, but all will likely generate outcomes which are significantly different from the current ones. This means that some states/regions will enjoy higher levels of revenue/expenditure than currently, but others will enjoy reduced levels.

Figure 26 provides an illustration of the difference (+ or -) between current levels of transfers/revenue and those under the simulation based on the approach outlined above. Basically, more populated regions such as Ayeyarwady, Bago, Mandalay, and Shan will benefit, while others such as Tanintharyi, Chin, and Kachin will lose.

Figure 26 Simulation: Winners and losers from the revised formula - MMK millions



This will, of course, be politically challenging to manage. The easiest way to avoid problems is to increase the size of the grant transfer pool to a level where no state/region will receive less than it currently does (usually referred to as "holding these state/region governments harmless"), although the pattern of relative transfers from the larger pool would change greatly between states/regions.

Timely and clear communication about the grant transfer

Timely, clear, and consistent communication from the Union to state/region governments about their grant transfers is crucial:

- State/region governments must understand clearly that grants constitute a fixed 'ceiling', and that this cannot be increased through lobbying or through submitting larger budget proposals.
- Providing the budget ceiling to states/regions in November is already a major advance. If this ceiling were provided on an even earlier date, state/region governments could determine department ceilings earlier in the budget process.

D.2.3. Strengthening planning and budgeting procedures

Inter-sectoral coordination

In order to overcome the institutional silos which undermine effective local planning, the Ministry of Planning and Finance (MOPF) and the newly-formed Union and State/Region Planning Commissions need to give township and district planning bodies (Township Plan Formulation and Implementation Committees [TPFICs] and District Plan Formulation and Implementation Committees [DPFICs]) the authority and power to ensure greater information-sharing and coordination about their respective plans and budgets. For example, to avoid overlaps and maximize the potential for synergy, TPFICs/ DPFICs need to facilitate sharing among the DAOs, the DRD, and the Highways Departments.

The annual cycle

A general review of the overall state/region planning and budget cycle and timetable is important to see if:

- Communication about the grant transfers can be made even a little earlier than November to allow state/region governments to assign notional ceilings to departments, and perhaps also to townships, to discipline the investment planning and budgeting process.

- Generally, more time should be allotted to key steps in the process, e.g. the technical appraisal and prioritization of proposals before preparation of the initial budget proposal, and the review and scrutiny of this by the Hluttaw.

This review would need to be undertaken together with MOPF and state/region governments, and will focus on identifying possible redundant steps and critical path constraints which, if resolved, could allow more time for the key steps in the plan and budget preparation, review, and approval process all of which appear now to be very rushed and do not allow adequate time for these steps.

Assigning budget ceilings to state/region departments

Now that the MOPF has begun to communicate the grant transfer amounts in November, state/region governments are informed of their budget ceilings. If it were possible to assign an indicative ceiling (or range) to each of the various state/region departments before they finalize their initial budget proposals, this would introduce a major incentive for more careful and more rigorous budget prioritization by these departments. This could first be piloted with one or two selected state/region governments and departments.

Investment appraisal, ranking and selection tools

There is an urgent need to devise simple sets of procedures, guidelines, and criteria to ensure that investment priorities at the state/region level for the different departments are appraised by the Budget Department, and the state/region governments in a manner that is consistent and transparent, and where proposals are selected for budget priority based on their relative merits (i.e. potential benefits and likely costs). This is an area where there is a body of international experience and good practice from which to learn. This could first be piloted with one or two selected departments and state/region governments.

Role of the State/Region Hluttaw

In order to ensure that the State/Region Hluttaw plays a more pro-active role and performs its constitutional role, there is need to:

- Review the annual budget timetable to ensure that there is adequate time for the Hluttaw and the Public Accounts Committee (PAC) to examine state/region budget proposals at an early stage, and not just after Union approval.

- Develop guidelines and tools to assist the state/region Hluttaws and members of their specialized Public Accounts Committee or Budget Committee in playing an informed role in assessing budget proposals. Here too, there is a body of international experience and good practice to learn from that could be adapted to the Myanmar context, and piloted with one or two state/region governments.

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Annex 1

Schedule 2 of the 2008 Myanmar Constitution - State and Region Legislative List

1. Finance and Planning Sector
(a) The Region or State budget;
(b) The Region or State fund;
(c) Land revenue;
(d) Excise duty (not including narcotic drugs and psychotropic substances);
(e) Municipal taxes such as taxes on buildings and lands, water, street lightings and wheels;
f) Services of the Region or State;
(g) Sale, lease and other means of execution of property of the Region or State;
(h) Disbursement of loans in the country from the Region or State funds;
(i) Investment in the country from the Region or State funds;
(j) Local plan; and
(k) Small loans business.

2. Economic Sector
(a) Economic matters undertaken in the Region or State in accord with law enacted by the Union;
(b) Commercial matters undertaken in the Region or State in accord with law enacted by the Union; and
(c) Co-operative matters undertaken in the Region or State in accord with law enacted by the Union.

3. Agriculture and Livestock Breeding Sector
(a) Agriculture;
(b) Protection against and control of plants and crop pests and diseases;
(c) Systematic use of chemical fertilizers and systematic production and use of natural fertilizers;
(d) Agricultural loans and savings;
(e) Dams, embankments, lakes, drains and irrigation works having the right to be managed by the Region or State;
(f) Fresh water fisheries; and
(g) Livestock breeding and systematic herding in accord with the law enacted by the Union.

4. Energy, Electricity, Mining and Forestry Sector
(a) Medium and small scale electric power production and distribution that have the right to be managed by the Region or State not having any link with national power grid, except large scale electric power production and distribution having the right to be managed by the Union;
(b) Salt and salt products;
(c) Cutting and polishing of gemstones within the Region or State;
(d) Village firewood plantation; and
(e) Recreation centers, zoological garden and botanical garden.

5. Industrial Sector
(a) Industries other than those prescribed to be undertaken by the Union level; and
(b) Cottage industries.

6. Transport, Communication and Construction Sector
(a) Ports, jetties and pontoons having the right to be managed by the Region or State;
(b) Roads and bridges having the right to be managed by the Region or State; and
(c) Systematic running of private vehicles within the Region or State.

7. Social Sector

(a) Matters on traditional medicine not contrary to traditional medicine policies prescribed by the Union;

(b) Social welfare works within the Region or State;

(c) Preventive and precautionary measures against fire and natural disasters;

(d) Stevedoring;

(e) Having the right of management by the Region or State, the following:

(i) Preservation of cultural heritage;

(ii) Museums and libraries.

(f) Theatres, cinemas and video houses; and

(g) Exhibitions such as photographs, paintings and sculptures.

8. Management Sector

(a) Development matters;

(b) Town and housing development; and

(c) Honorary certificates and awards.

Annex 2

Own-source Revenues

Own-source revenues BE FY 2016/17 - MMK billions			
	Ayeyarwady	Shan	Tanintharyi
PART I - State/Region government own revenues			
Various fees, Project finance, etc. (NB. Excluded here are commercial tax share revenues, Constituency Fund & Hluttaw transfers, usually recorded under Part 1)	110.40	10,518.70	131.40
Total I - State/Region gov't own revenues	110.40	10,518.70	131.40
PART II - Revenues accruing to departments			
PART II. A. Tax revenues collected by departments			
i. Taxes collected by GAD, Forestry, Fisheries, etc.			
Excise	1,714.25	469.29	275.58
Land Revenue	93.57	221.59	55.97
Embankment Tax	7.25	28.18	0.05
Tax on Extraction of Forest Produce	266.53	133.43	748.95
Tax on Extraction of Minerals	162.72	54.95	13.47
Fishery Leases	4,268.88	6.75	96.11
Sub- Total	6,513.19	914.19	1,190.14
ii. Taxes collected by DAOs			
Property Tax	866.69	793.02	507.22
Wheel Tax	186.57	305.43	66.73
Tax Dividend	-	1,130.55	-
Sub-Total	1,053.26	2,229.00	573.95
Total II. A. Tax Revenues	7,566.45	3,143.19	1,764.09
Part II. B. Other revenues collected by departments			
Ministry of Home Affairs			
General Administration Department	12.24	18.48	9.69
Special Branch	0.05	0.10	0.04
Fire Department	13.06	3.30	0.60

Own-source revenues BE FY 2016/17 - MMK billions			
	Ayeyarwady	Shan	Tanintharyi
Sub-Total	25.35	21.88	10.33
Ministry of Co-operatives		-	
Co-operative Department	14.81	7.57	0.89
Small-scale Industry Department	1.30	2.65	1.54
Sub-Total	16.10	10.22	2.43
Ministry of Agriculture and Irrigation		-	
Agriculture Department	32.00	28.65	1.78
Sub-Total	32.00	28.65	1.78
Ministry of Livestock, Fisheries and Rural Development			
Fisheries Department	20.12	5.29	-
Livestock/Veterinary Department	3.44	8.28	1.01
Sub-Total	23.56	13.57	1.01
Ministry of Environmental Conservation and Forestry			
Forestry Department	20.42	11.26	20.14
Environmental Conservation Department	0.00	1.00	-
Sub-Total	20.42	12.26	20.14
Ministry of Sports			
Sports and Physical Education Department	21.15	92.78	4.74
Sub-Total	21.15	92.78	4.74
Ministry of Mining		-	
Mines Department (Salt Industry)	61.62	3.40	-
Sub-Total	61.62	3.40	-
Ministry of National Planning and Economic Development			
Planning Department	0.19	1.10	0.01
Sub-Total	0.19	1.10	0.01
Ministry of Construction		-	
Urban and Housing Development Department	22.48	28.01	12.77

Own-source revenues BE FY 2016/17 - MMK billions			
	Ayeyarwady	Shan	Tanintharyi
Department of Highways	203.80	139.72	19.28
Sub-Total	226.28	167.73	32.04
Development Affairs Organizations			
Development Affairs Organizations	9,299.00	12,339.64	2,524.23
Sub-Total	9,299.00	12,339.64	2,524.23
Other Departments & State Economic Enterprises			
Electricity, Freight, etc.	-	40.00	3.00
Sub-Total	-	40.00	3.00
Total II. B. Other Revenues	9,725.66	12,731.22	2,599.71
Total II. A+B Tax & Other Revenues	17,292.11	15,874.41	4,363.80
TOTAL ALL STATE/REGION OWN-SOURCE REVENUES	17,402.51	26,393.11	4,495.20

Source: State/region Budget Departments

Annex 3

State/Region (S/R) Expenditures by Sector

State and Region budget expenditures by sector - MMK millions

State/Region government entities	BE FY 2016/17									BE FY 2015/16		
	Ayeyarwady			Shan			Tanintharyi			Kayin		
	Current	Capital	TOTAL	Current	Capital	TOTAL	Current	Capital	TOTAL	Current	Capital	TOTAL
PART 1 - S/R Admin												
S/R government bodies	6,659	20,448	27,107	20,143	46,723	66,866	2,829	9,673	12,502	1,936	15,694	17,630
PART II - S/R Ministries/Depts.												
Home Affairs	12,813	4,137	16,950	17,876	16,264	34,140	5,437	1,890	7,327	4,355	3,311	7,666
Cooperatives	1,259	224	1,483	1,424	596	2,020	460	138	598	419	396	816
Agriculture & Irrigation	2,483	480	2,963	5,977	898	6,875	1,129	4	1,133	1,737	1,966	3,703
Livestock, Fisheries & Rural Development	1,366	355	1,720	925	410	1,335	416	88	504	330	999	1,329

Environmental Conservation & Forestry	1,252	259	1,511	2,806	832	3,639	828	81	909	773	9	782
Sports	529	580	1,109	898	1,420	2,318	558	1,992	2,550	152	1,800	1,952
Mining	70	148	218	28	23	51	-	-	-	-	-	-
Finance	75	265	340	177	23	199	77	8	84	65	1,800	1,865
Planning and Economic Development	638	265	903	1,625	542	2,167	263	16	279	250	17	267
Construction	16,845	52,381	69,225	36,455	62,810	99,265	70,031	23,142	93,173	10,859	23,447	34,305
DAOs	5,050	5,302	10,352	6,727	7,842	14,569	1,382	6,211	7,594	1,184	1,232	2,415
Electricity		–	–	5	16,080	16,085	3,042	24,726	27,768	–	–	–
Part - II. Total Ministry/Dept. Expenditures	42,379	64,396	106,776	74,923	107,740	182,662	83,623	58,296	141,920	20,123	34,976	55,100
PARTS 1 and II - GRAND TOTAL EXPENDITURES	**49,038**	**84,845**	**133,883**	**95,066**	**154,463**	**249,528**	**86,452**	**67,970**	**154,422**	**22,060**	**50,670**	**72,730**

Source: State/region Budget Departments

Annex 4

Planning and Budget Timetables and Procedures

Fiscal year and key MOPF-prescribed steps for state/ region (S/R) budget estimates	MOPF Calendar	NOV				DEC				JAN				FEB				MAR				APR			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
FY 2015/16 - NORMAL TIMETABLE (MARCH/APRIL DEADLINE)																									
UNION DEPT. BUDGET ISSUES THE BUDGET CIRCULAR & CALENDAR	8 NOV '14		X																						
S/R GOVERNMENT COMMUNICATES TO S/R BUDGET DEPT.	14 NOV '14		X																						
1ST S/R GOV'T SUBMITS BUDGET TO UNION DEPT. OF BUDGET	5 DEC'14					X																			
UNION GOV'T ANNOUNCES PROPOSED TRANSFERS TO S/R GOVERNMENT	30 DEC '14								X																
2ND S/R GOV'T BUDGET SUBMISSION TO UNION DEPT. OF BUDGET	5 JAN '15									X															
ANALYSIS OF BUDGET PROPOSALS BY VICE-PRESIDENT	6-13 JAN '15										X														
SUBMISSION TO UNION FINANCIAL COMMISSION & APPROVAL	14 JAN '15										X														
SUBMISSION TO UNION GOVERNMENT MEETING & APPROVAL	15 JAN '15											X													
SUBMISSION TO UNION HLUTTAW	AFTER 15 JAN '15											X													

UNION HLUTTAW REVIEW/APPROVAL OF UNION BUDGET, INCL. S/R FISCAL TRANSFERS	31 MARCH '15																				X				
COMMUNICATION TO S/R GOVERNMENTS	31 MARCH '15																				X				
BUDGET SUBMISSION TO S/R HLUTTAWS & APPROVAL	1-8 APRIL '15																					X			
APPROVAL BY S/R CHIEF MINISTER	9 APRIL '15																						X		
FY 2016/17 - ACCELERATED TIMETABLE (JANUARY DEADLINE)																									
UNION DEPT. BUDGET ISSUES THE BUDGET CIRCULAR & CALENDAR	11 NOV '15		X																						
UNION GOV'T ANNOUNCES PROPOSED TRANSFERS TO S/R GOVERNMENT	16 NOV '15			X																					
S/R GOVERNMENT COMMUNICATES TO S/R BUDGET DEPT.	18 NOV '15			X																					
1ST S/R GOV'T BUDGET SUBMISSION TO UNION DEPT. OF BUDGET	7 DEC'15					X																			
ANALYSIS OF BUDGET PROPOSALS BY VICE-PRESIDENT	11 DEC '15																								
COMMUNICATION BACK TO S/R GOVERNMENT	11 DEC '15						X																		
2ND S/R GOV'T BUDGET SUBMISSION TO UNION MINISTRY OF FINANCE & PLANNING	12 DEC' 15						X																		
SUBMISSION TO UNION FINANCIAL COMMISSION & APPROVAL	16 DEC '15							X																	

SUBMISSION TO UNION GOVERNMENT MEETING & APPROVAL	17 DEC '15							X																	
SUBMISSION TO UNION HLUTTAW	18 DEC '14								X																
UNION HLUTTAW REVIEW/APPROVAL OF UNION BUDGET, INCL. S/R FISCAL TRANSFERS	25 JAN '16											X													
COMMUNICATION TO S/R GOVERNMENTS	25 JAN '16											X													
BUDGET SUBMISSION TO S/R HLUTTAWS & APPROVAL	27-28 JAN '16												X												
APPROVAL BY S/R CHIEF MINISTER	27-28 JAN '16												X												
Fiscal year and key MOPF-prescribed steps for state/ region (S/R) budget estimates	**MOPF Calendar**	**NOV**				**DEC**				**JAN**				**FEB**				**MAR**				**APR**			
		1	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**
FY 2014/15																									
UNION DEPT. BUDGET ISSUES BUDGET CIRCULAR & CALENDAR	8 AUG '14						**X**																		
S/R GOV'T PASSES ON TO S/R DEPT. BUDGET	22 AUG '14								**X**																
S/R BUDGET DEPT. SUBMITS REVISED ESTIMATE TO UNION BUDGET DEPT.	9 SEPT '14										**X**														
REVIEW & ANALYSIS BY MOPF	16 SEPT '14											**X**													
REVIEW & ANALYSIS BY VICE PRESIDENT & FEEDBACK TO S/R	26 SEPT '14												**X**												
S/R BUDGET DEPT. RE-SUBMITS AMENDED BUDGET REVISION TO UNION BUDGET DEPT.	AFTER 30 SEPT '14													**X**											

UNION DEPT. BUDGET SUBMITS TO FINANCE COMMISSION FOR APPROVAL	2 NOV'14																	**X**							
REVIEW & APPROVAL BY UNION HLUTTAW	20 NOV '14																				**X**				
CHIEF MINISTER APPROVAL	AFTER 20 NOV '14																					**X**			
FY 2015/16																									
UNION DEPT. BUDGET ISSUES BUDGET CIRCULAR & CALENDAR	28 JULY '15				**X**																				
S/R GOV'T PASSES ON TO S/R DEPT. BUDGET	7 AUG '15					**X**																			
S/R BUDGET DEPT. SUBMITS REVISED ESTIMATE TO UNION BUDGET DEPT.	21 AUG '15								**X**																
REVIEW & ANALYSIS BY MOPF	15 OCT '15															**X**									
REVIEW & ANALYSIS BY VICE PRESIDENT & FEEDBACK TO S/R	30 OCT '15																**X**								
S/R BUDGET DEPT. RE-SUBMITS AMENDED BUDGET REVISION TO UNION BUDGET DEPT.	6 NOV'15																	**X**							
UNION DEPT. BUDGET SUBMITS TO FINANCE COMMISSION FOR APPROVAL	12 NOV '15																		**X**						
REVIEW & APPROVAL BY UNION HLUTTAW	15 DEC'15																							**X**	
CHIEF MINISTER APPROVAL	AFTER 15 DEC'15																								**X**

ANNUAL SUB-NATIONAL PLANNING & BUDGETING PROCESS
(A) Up to and until FY 2015/16 (Union grant transfer amount only announced after first budget submission)

APPROX. TIMING (VA RI ES)	I. STATE & REGION ANNUAL PLAN & BUDGET PROCESS	II. UNION LINE MINISTRY ANNUAL PLAN & BUDGET PROCESS
April-June	PFICs undertake review of Plan implementation in the previous fiscal /plan year to inform next year planning	
June	S/R Plan Depts issue instructions and timetable to launch annual plan and capital budget reparation Union Line Ministries also issue instructions to State/Region Depts to initiate annual plan and capital budget preparation for the sector	
June-July	Township & District consultations, review local needs & priorities, update 5 Yr Plan provisions, & formulate plan/budget proposals Involving Local line depts, TPFIC & DPFIC, other Township meetings, MPs, etc NB range of consultation varies considerably across sectors: much more in case of DRD, much less in case of Highways, Education or Health Proposals then flow into I. or II. below	
J uly-September	I. Proposals for State/Region Budget	II. Proposals for Union Budget
	Township/District Line Depts & PFICs prepare investment proposals & submit to State/Region Line Depts, based on consultations and the provisions of the 5 Year Plan	Township/District Line Depts & PFICs prepare investment proposals & submit to State/Region Line Depts based on the provisions of the 5 Year Plan - S/R Line Depts consolidate and adjust, - S/R Line Depts (in some cases) submit proposals to State/Region cabinet (not Hluttaw) to be reviewed & amended - State/Region Line Depts submit amended proposals to Union Line Ministries *NB 1. Some Depts (e g Health) forward direct to Union without State/Region cabinet input* *NB 2. In some State.s/Regions Education Depts also channel other proposals (e.g. from MPs) to Union level, after initial submission.*
August-October	State/Region Line Depts consolidate proposals, adjust, add own, and submit proposed: - Investment plan/budget (only) to State/Region DoP - Both investment plan/budget & current budget to DoB - S/R Plan Dept reviews coherence & consistency with % Year Plan etc, and informs S/R Det Budget. - S/R Budget Dept reviews, negotiates with S/R Line Depts to cut down amends, consolidates	Union Line Ministries: - review proposals from all States/Regions - determine budgets and specific investments for approval in each State/Region in light of relative priorities expressed by each State/Region for its proposals, sector policy, cost norms, earmarked funds or donor funding focus, etc. *NB At least for Education, even after S/R Dept Education submission to Union level, there are **ad** hoc proposals initiated by local MPs, etc., which are forwarded, through the S/R Dept, to Union level, throughout this period*
November	- DoB submits proposed initial budget to State/Region cabinet - S/R Govt reviews, amends, adds, cuts (in consultation with Budget, Plan & Line Depts) - S/R Govt submits to S/R Hluttaw foir approval - S/R Govt submits to MoF & Vice-President	Line Ministry submits budget proposal to Finance Commission
December	S/R Govt reduces & finalizes budget (in consultation with Dept Budget, Plan & Line Depts) - S/R Govt submits to Finance Commission	

January	- Finance Commission reviews & approves - Union Government submits Union Budget proposal - including State/Region grant transfers - to Union Hluttaw Union Hluttaw refers Union budget proposal to Joint Draft Law Committee 8 Joint Public Accounts Committee	- Finance Commission reviews & approves - Union Government submits Union Budget proposal - including State/Region grant transfers - to Union Hluttaw - Union Hluttaw refers Union budget proposal to Joint Draft Law Committee & Joint Public Accounts Committee
February	- Union Hluttaw Committees report back to Union Hluttaw - Union Hluttaw reviews budget proposal	- Union Hluttaw Committees report back to Union Hluttaw - Union Hluttaw reviews budget proposal
March	- Union Hluttaw queries Line Ministries where necessary - Union Hluttaw approved Union budget, incl. State/Region transfers	- Union Hluttaw queries Line Ministries where necessary - Union Hluttaw approved Union budget, incl. State/Region transfers - Union Government informs Line Ministry - Union Line Ministry informs State/Region Government
April	- S/R Govt finalizes & submits to S/R Hluttaw - Hluttaw approves Budget Law & Plan Law+ annexes: Vol 1 for S/R investments & Vol 2 for Union funded investments	- State/Region Planning Dept compiles all Union Plans into State/Region Plan Volume 2 (annexed to State/Region Plan Law).

<table>
<tr><th colspan="4">ANNUAL SUB-NATIONAL PLANNING & BUDGETING PROCESS
(A) FY 2016/17 (formula-based grants announced in November FYN-1)</th></tr>
<tr><td>APPROX. TIMING</td><td colspan="2">I. STATE & REGION ANNUAL PLAN & BUDGET PROCESS</td><td>II. UNION LINE MINISTRY ANNUAL PLAN & BUDGET PROCESS</td></tr>
<tr><td>April-June</td><td colspan="3">PFICs undertake review of Plan implementation in the previous fiscal /plan year to inform next year planning</td></tr>
<tr><td>June</td><td colspan="3">S/R Plan Depts issue instructions and timetable to launch annual plan and capital budget reparation
Union Line Ministries also issue instructions to State/Region Depts to initiate annual plan and capital budget preparation for the sector</td></tr>
<tr><td>June-July</td><td colspan="3">Township & District consultations, review local needs & priorities, update 5 Yr Plan provisions. & formulate plan/budget proposals
Involving Local line depts, TPFIC & DPFIC, other Township meetings, MPs, etc
NB range of consultation varies considerably across sectors: much more in case of DRD, much less in case of Highways, Education or Health
Proposals then flow into I. or II. below</td></tr>
<tr><td rowspan="2">July-September</td><td colspan="2">I. Proposals for State/Region Budget</td><td>II. Proposals for Union Budget</td></tr>
<tr><td colspan="2">Township/District Line Depts & PFICs prepare investment proposals & submit to State/Region Line □ epts, based on consultations and the provisions of the 5 Year Plan</td><td>- Township/District Line Depts & PFICs prepare investment proposals & submit to State/Region Line Depts based on the provisions of the 5 Year Plan
- S/R Line Depts consolidate and adjust,
- S/R Line Depts (in some cases) submit proposals to State/Region cabinet (not Hluttaw) to be reviewed & amended
- State/Region Line Depts submit amended proposals to Union Line Ministries
AIB 1. Some Depts (e.g Health) forward direct to Union without State/Region cabinet input
NB 2. In some States/Regions Education Depts also channel other proposals (e.g. from MPs) to Union level, after initial submission.</td></tr>
<tr><td>August-October</td><td colspan="2">State/Region Line Depts consolidate proposals, adjust, add own, and submit proposed:
- Investment plan/budget (only) to State/Region DoP
- Both investment plan/budget & current budget to DoB
- S/R Plan Dept reviews coherence & consistency with % Year Plan etc, and informs S/R Det Budget.
- S/R Budget Dept reviews, negotiates with S/R Line Depts to cut down amends, consolidates</td><td rowspan="3">Union Line Ministries:
- review proposals from all States/Regions
- determine budgets and specific investments for approval in each State/Region in light of relative priorities expressed by each State/Region for its proposals, sector policy, cost norms, earmarked funds or donor funding focus, etc.

NB At least for Education, even after S/R Dept Education submission to Union level, there are ad hoc proposals initiated by local</td></tr>
<tr><td rowspan="2">November</td><td colspan="2">Union Ministry Finance issues budget circular & announces Grant Transfer amount for each State/Region</td></tr>
<tr><td>Practice I.A. State/Region does not take the grant transfer seriously as the final ceiling</td><td>Practice I.B. State/Region accepts that grant transfer is the final ceiling</td></tr>
</table>

Annex 5

Form to Record Capital Investment Project Proposals by Departments - For FY 2016/17

Particular	2014-15	2015-16			2016-17				
	Provision-al Actual	Budget Estimate	Provi-sional	Total	Local Currency (MMK)	Foreign Exchange			
						Total	Free FE	Loans	Grants / Aid
1. Project Plans									
Carry Over Projects									
New Projects									
2. Projects									
Investment Projects Extended									
Investment Projects Substituted/ Replaced									
3. Machinery/Equipment, Furniture and Vehicles for Office									
Machinery/Equipment									
Furniture									
Vehicles									
Others									
TOTAL									

Annex 6

Department of Basic Education Investment Approvals

Union Department Basic Education Investment Approvals by State/Region, Proponent and Criteria

DBE budget approvals - FY 2016/17 - MMK millions						
States and Regions	A. Schools approved based on emphasis by high authorities during their field visits, included in Hluttaw public statements, and/or affected by natural disasters					
	Emphasized by high authorities during their field visits		Mentioned publicly during a Hluttaw session		Affected by a natural disaster	
	No.	Value	No.	Value	No.	Value
Ayeyarwady	5	288				
Bago (East)	I2	896	4	129		
Bago (West)	3	238	6	164		
Chin						
Kachin			3	60		
Kayah	2	31				
Kayin	I	156				
Magway	13	533	3	105		
Mandalay	I	35			I	47
Mon	3	62	2	94		
Nay Pyi Taw	2	336				
Rakhine	I	168				
Sagaing	3	468	15	360		
Shan (East)			I	119		
Shan (North)	IO	558	IO	275		
Shan (South)	15	725	2	59		
Tanintharyi			4	323		
Yangon			3	144		

Source: Union Dept. of Basic Education

	DBE Budget approvals - FY 2016/17 - MMK millions					
	B. Proposed by State/Region Hluttaw members					
	Demolished school		School with a large student population		School that badly needs repairs	
	No.	Value	No.	Value	No.	Value
Ayeyarwady	34	1,317	52	1,902	69	2,079
Bago (East)	14	722	13	433	13	550
Bago (West)	19	1,249	22	803	57	1,505
Chin			18	637	76	1,987
Kachin	9	417	53	1,884	8	222
Kayah	17	433	l	35	23	573
Kayin	3	242	9	347	3	154
Magway	27	935	27	1,186	64	1,751
Mandalay	19	659	65	2,075	l2	495
Mon	3	239	l2	567	4	140
Nay Pyi Taw	l	31			l	35
Rakhine	2	47	18	1,053	42	1,252
Sagaing	13	679	38	1,643	56	1,524
Shan (East)			2	59	l	23
Shan (North)	2	ee	8	437	5	262
Shan (South)	e	332	25	890	24	740
Tanintharyi			4	335	l	84
Yangon						

Source: Union Dept. of Basic Education

	DBE Budget Approvals - FY 2016/17 - MMK millions							
	C. Proposed by the State/Region DBE							
	Demolished school		School with a large student population		School that badly needs repairs		State/Township Offices	
	No.	Value	No.	Value	No.	Value	No.	Value
Ayeyarwady	37	1,515	47	1,398	29	1,084	1	120
Bago (East)	54	2,084	23	885	17	511	1	120
Bago (West)	11	378	7	211	17	456	1	120
Chin			2	128	14	400	1	120
Kachin	16	1,089	18	509	17	435		
Kayah	10	242	4	187	9	379		
Kayin	163	8,310	24	1,308	6	336	2	240
Magway	120	4,364	33	1,115	11	347	1	120
Mandalay	103	4,946	69	3,097	23	997	4	492
Mon	16	1,003	20	821	12	671	1	207
Nay Pyi Taw	8	554	17	878	4	363		
Rakhine	6	420	18	1,266	7	270	1	120
Sagaing	70	2,260	57	2,418	65	1,986	2	288
Shan (East)	3	227	18	605	12	312		
Shan (North)	18	636	28	968	16	519	1	120
Shan (South)	56	1,704	33	995	21	491	1	120
Tanintharyi	27	1,782	11	729	5	222	1	269
Yangon	83	6,271	55	3,902			4	480

Source: Union Dept. of Basic Education

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The Asia Foundation

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Photography by Jin Win! Yee