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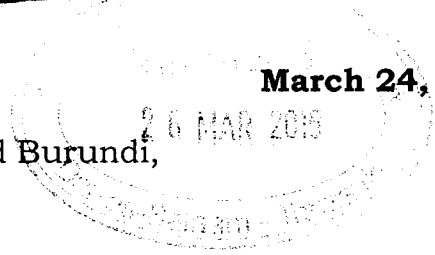
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Country Director for Tanzania, Uganda and Burundi,
World Bank Country Office,
50 Mirambo Street,
DAR ES SALAAM



LETTER OF DEVELOPMENT POLICY

1. On behalf of the Government of the United Republic of Tanzania, I hereby write to request approval of the Open Government and Public Financial Management Development Policy Credit in the amount of US\$ 100 million. This credit will assist the Government in the implementation of the Open Government Partnership commitments and in improving Public Financial Management in Tanzania which will contribute in the achievement of the objectives of the National Strategy for Growth and Poverty Reduction and the First Five Year Development Plan. In particular, this credit will enhance the governance initiatives of the Government by promoting transparency in public service delivery and expenditure and in the proper management of public financial resources.

2. Tanzania has taken major steps to improve governance in collaboration with the World Bank and other development partners. To spearhead improvements in service delivery, the Government has adopted the Big Results Now (BRN) as an overarching strategy for achieving quick results. The BRN will require efficient and effective public financial management systems to deliver funding to the front line. It will also require increased transparency to inform citizens on Government performance. We are committed to changing the way Government functions. It is in this light that we are pleased to provide the following summary of the policy areas that this operation seeks to support.

BACKGROUND AND RECENT DEVELOPMENTS

A. MACROECONOMIC PERFORMANCE

3. **Tanzania's recent economic developments have been favorable with stable growth and inflation under control.** GDP growth remains robust,

reaching 7.3 percent in fiscal year (FY) 2013/14, and is projected to remain at the same level in FY2014/15. Economic expansion has been driven by several fast-growing sectors, such as mining, communication, financial services, construction, manufacturing, and retail trade. By contrast, agriculture—the sector on which about 80 percent of households depend as their primary economic activity—has continued to post slower growth and weaker productivity gains. Inflation has steadily declined over the past two and a half years due to tight monetary policy as well as falling international energy and food prices. The inflation rate was four percent in January 2015, down from over 19 percent at the end of 2011.

4. Sustained public and private consumption and investment have been the main drivers of economic growth from the demand side. Both household consumption and private investment growth has remained high between 2007 and 2013, accounting for 57 percent and 34 percent of GDP growth respectively. Comparing two periods of 2001-2006 and 2007-2013, the share of public consumption and investments in GDP growth increased from 29 percent to 40 percent and from 11 percent to 15 percent, respectively, reflecting the Government's effort to sustain social service provision while scaling up infrastructure investments in the country.

5. However, the relatively high economic growth has not translated into growth of productive jobs that are sufficient to absorb the rapidly growing labor force in the country. So far Tanzania has not been able to stimulate job creation at a sufficiently rapid pace because productivity growth has been limited in a small set of sectors that are relatively more capital/technology intensive rather than labor intensive. Therefore, productivity growth and increased diversification of the economy will be central to enhancing the expansion of private firms and their capacity to create productive jobs. These issues are at the center of the Country Economic Memorandum (CEM) launched in September 2014 and the private sector CEM which is being prepared by the Bank.

6. Tanzania's economy has increasingly become more open, with increasing diversification toward new products and markets during the past five years, but remained low than the average for Sub-Saharan Africa. The trade-to-GDP ratio has risen from 42 percent in 2008 to 49 percent in 2013 which is significantly low compared to the Sub-Saharan Africa average of around 66 percent. Although the export structure remains largely dependent on primary commodities such as minerals (especially gold), coffee, tea, cashew, and cotton, the recent surge in manufactured exports to EAC and the Southern African Development Community (SADC) has been a notable and welcome development. During the same period, imports grew faster than exports, leading to a growing trade deficit over time.

7. The balance of payment remained stable in 2013/14 despite the weak performance of exports and increased imports bill. Decline in

commodity prices in 2013 adversely affected Tanzania's export basket, which is still driven by several commodities. The overall fall in unit prices of both traditional and non-traditional exports, especially gold, together with declining manufactured exports resulted in a weaker export performance with the value of exports of goods and services having increased only by 6.6 percent in 2013/14 in real terms, while the value of imports of goods and services increased by 7.2 percent. Despite the widened current account deficit, a high volume of FDI has helped the economy maintain its overall stability in balance of payments. Gross official reserves amounted to US\$4,633 million as at the end of June 2014, sufficient to cover 4.0 months of (current year) imports of goods and services for the following year. The current account balance is anticipated to improve significantly in 2014/15 as a result of reduced import bill due fall in oil import value.

8. The Central Bank has continued to follow a conservative monetary policy, which resulted in falling inflation during the last two years. Annual growth of average reserve money declined to 13.7 percent in 2013/14, down from 19.3 percent three years ago. As a result, together with falling domestic food prices, inflation reached 4 percent in January 2015—a significant decline compared to 19 percent in December 2011. However, the recent significant rise of liquidity papers for financing the budget needs to be monitored.

9. In 2013/14 the GoT implemented a tight fiscal policy that brought the fiscal deficit down to 3.3 percent of GDP from 4.3 percent of GDP in 2012/13. At 13.7 percent of GDP, the actual domestic revenue collection in 2013/14 turned out to be more than two percentage points lower than the initial target. This forced the Government to undertake significant expenditure cuts (about 2.5 percent of GDP) as well as significant accumulation of expenditure payment arrears (about two percent of GDP). As a result, overall public expenditure in FY2013/14 was 18.7 percent of GDP, which is about five percent lower than the target. The significant expenditure cuts affected implementation of the priority infrastructure investment projects and social services under the BRN and the national development plan (MKUKUTA) which had to be postponed. However, slightly higher than half of the discretionary public spending was spent on the six MKUKUTA priority sectors (education, health, water, agriculture, energy, and roads) in FY2013/14.

10. Despite improving the overall deficit in 2013/14, the Government has accumulated significant level of arrears in the range of six percent of GDP. The central government has accumulated arrears of around 1.8 percent of GDP with suppliers (mainly in road construction), to which arrears with the pension system need to be added – in the range of two percent of GDP. These figures do not include the arrears accumulated by public agencies and parastatals (e.g., TANESCO and DAWASCO), which in turn are estimated to be around 2-3 percent of GDP. While the central Government is not directly responsible for those arrears, the contingent fiscal risk is considerable.

11. Further fiscal consolidation is anticipated in FY2014/15 with an overall fiscal deficit target of 3.7 percent of GDP. This will be achieved by controlling public expenditures and increasing domestic revenues. Domestic revenue collection target for FY2014/15 is set at 13.9 percent of GDP, about 0.2 percent higher than the actual revenue collections in 2013/14, driven largely by tax policy and administration reforms introduced by the FY 2014/15 Budget Speech. The FY2014/15 public expenditure is anticipated to be around 20.4 percent of GDP, about two percent higher than in FY2013/14. A significant share of the public spending will be directed towards priority projects and programs identified under the BRN and National Strategic Investment Projects in line with the Five Year Development Plan (FYDP) and the MKUKUTA. However, implementation of the FY2014/15 budget will depend largely on the performance of the domestic revenue collection and budget execution, especially the development budget. Preliminary data shows that actual revenue collection during the first semester of the FY2014/15 has still short of the target by around 15 percent while disbursement of budget support grants of about 1.2 percent of GDP has been delayed due to IPTL scandal.

B. MACROECONOMIC PROJECTIONS

12. Tanzania's macroeconomic situation is expected to remain stable with the GDP growth rate anchored at 7 percent over the next two years. Scaling up of public investments (as part of the BRN initiative), if implemented successfully, should further support the drive for growth. In the medium term, the expected huge FDI inflows (potentially \$ 4-5 billion per year) toward the natural gas sector, especially for construction of LNG plant(s) that may start as early as 2017 depending on final decisions by the international gas investors, should support the growth of the economy.

13. The authorities remain committed to a prudent monetary stance and flexible exchange rate regime. Inflation is expected to stabilize at around five percent as a result of prudent monetary and exchange rate policies in addition to favorable food and global energy prices. Moreover, the Bank of Tanzania intends to gradually move to interest rates as opposed to the current reserve money targeting approach.

14. The medium-term fiscal policy framework aims at further reducing the overall fiscal deficit to around 3 percent of GDP and stabilizing the total public debt at around 34 percent of GDP in FY2014/15 These targets are consistent with the GoT's objective of maintaining fiscal sustainability, low debt distress, limiting accumulation of new arrears and expenditure cuts during budget execution, and avoiding the risk of renewed inflation pressure. This will be achieved by mobilizing additional domestic revenue. The control of recurrent spending, notably the wage bill, will be required as well as considerable improvements in the selection and management of investment projects. Close monitoring and improvement in both fiscal and debt management remains critically important.

15. The current account deficit should remain relatively high but will be offset by anticipated large FDI inflows in the natural gas sector. In the medium term, however, the current account deficit is expected to improve significantly after domestic natural gas replaces liquid fuel as the main source of thermal power generation, thereby reducing presently costly fuel imports. Construction of LNG plant(s), which is likely to be financed by multibillion dollar FDI per year, would widen the current account deficit at least temporarily due to expected growth of imported materials and equipment for the construction, but should not lead to any significant deterioration in balance of payments because of the size of potential FDI flows.

16. Tanzania's current risk of debt distress remains low provided fiscal consolidation is maintained. The last IDA-IMF Debt Sustainability Analysis (DSA) (April 2014) shows that Tanzania's risk of debt distress was low. Even though DSA indicates that public debt sustainability continues to be sensitive to fiscal consolidation and recognition of outstanding pension and other liabilities, Government is committed to pursuing a sound debt management strategy, including taking measures to urgently addressing the pension liabilities, adopting a conservative approach to non-concessional borrowing, and improving capacity to plan and execute public investments in order to ensure future debt and fiscal sustainability.

C. BACKGROUND ON THE OPEN GOVERNMENT PARTNERSHIP AND THE PUBLIC FINANCIAL MANAGEMENT REFORM PROGRAM

THE GOVERNMENT PROGRAM ON OGP

17. Tanzania joined the Open Government Partnership (OGP) in September 2011. The country's first OGP Action Plan was submitted in April 2012, focusing on enhancing transparency, citizen participation, accountability and integrity and the use of technology and innovation in service delivery sectors of health, water and education. The first OGP Action Plan was prepared following a public consultation process in which a number of key stakeholders including non-state actors, media and citizens were involved. The two year plan was self-evaluated in 2013 and independently in early 2014. Both the Self-Assessment Report and the report of the Independent Review Mechanism found that implementation was challenging and therefore limited success was recorded.

18. Tanzania's Second OGP Action Plan (2014/15-2016/17) focuses on five priority areas, selected for their cross-cutting importance. These areas are enactment of an Access to Information Act, establishing a system of open data, making budget data publicly available, making land use plans and ownership transparent, and fulfilling EITI transparency commitments. The second action plan still puts an emphasis on promoting service delivery in three key sectors of education, water and health in terms of open data, budget transparency and access to information.

THE GOVERNMENT PUBLIC FINANCIAL MANAGEMENT REFORM PROGRAM

19. **Tanzania has also prepared and is implementing a Public Financial Management Reform Program (2012/13 – 2016/17) which is currently in phase IV.** This program aims at enhancing public financial management in the areas of revenue management, planning and budgeting, budget execution, accountability and transparency; budget control and oversight; change management and program monitoring and communication. This program contributes to the MKUKUTA and Five year Development Plan objectives for achieving economic growth and poverty reduction, improving service delivery and improving transparency and accountability in government functions.

20. **The OGP Action Plan and the PFMRP define the Government program that will be supported by the proposed credit.** The Open Government and Public Financial Management development program will support the Government to implement the OGP and the PFMRP IV in the following areas: (i) enactment of the Access to Information Act; (ii) establishment of a system of Open Data; and (iii) publishing of budget data in open format in the three selected sectors of education, water and health. The program will also support the Government in implementing policy actions on (iv) cash management, (v) public investment management and (vi) procurement.

DESCRIPTION OF POLICY AREAS

ESTABLISHING THE LEGAL FRAMEWORK FOR ACCESS TO INFORMATION

21. Tanzania joined the OGP international initiative to make government business more open to its citizens in the interest of improving public service delivery, government responsiveness, combating corruption and building greater trust. Under this initiative, Government is committed to increase the availability of information to support citizens' participation in policy making and implementation, promoting high standards of professional integrity, and ensuring transparency in the management of public finances.

22. The right to be informed and to access and disseminate information is recognized in *Articles 18(1) and 18(2)* of the Constitution of the United Republic of Tanzania (1977). At present, however, there is no law that provides the means to put this constitutional right into practice. The Access to Information (ATI) Act has been extensively debated and it is long overdue. The Government has committed to prepare an ATI bill in the second OGP action plan (2014-16). Enactment of the ATI bill will provide a strong legal framework for openness in public policy making and implementation.

23. Government has completed the drafting of an ATI bill in line with international best practice legislation that includes:(i) recognition of a human

right to information, along with a broad presumption of openness of information held by public bodies, including state-owned enterprises and bodies, and private bodies undertaking public functions or operating under public funding; (ii) an obligation to publish a wide range of information on a proactive basis; (iii) robust procedures for making and processing requests which are simple, free and quick (with a clearly specified maximum response time); (iv) a limited regime of exceptions based on preventing harm to protected and security related interests, a public interest override and severability where part of a record is exempt; (v) a right of appeal; (vi) protection for good faith disclosures and sanctions for obstruction of access; and (vii) obligations to report on requests received backed up by sanctions for refusal to disclose information without reasonable cause. The ATI bill is now expected to be read in Parliament in March of 2015.

OGPFM Prior action: Cabinet approves an Access to Information (ATI) bill for submission to Parliament in line with the OGP action plan, following broad consultations with stakeholders.

ESTABLISHING AN OPEN DATA SYSTEM AND PRACTICE FOR GOVERNMENT BUDGET AND SECTOR PERFORMANCE

24. Government is committed to the open data initiative since it is a useful tool to improve functionality and effective information sharing within government and between government and citizens to enhance service delivery. This is particularly important to strengthen the links between central and local governments. Data is also a potentially important resource to strengthen government accountability in service delivery for civil society and for politicians, MPs, and local councilors. With support from the Bank, the CoT prepared an Open Data Readiness Assessment (ODRA) that was presented to key stakeholders in June 2013. The report forms the basis of the actions being taken by Government in establishing an open data environment.

25. The National Bureau of Statistics (NBS), an agency under the MOF, the Records and Archives Division and e-Government Agency both of President's Office-Public Service Management have been mandated to form the task force and to draft the guidelines and policies on open data. The guidelines on open data have been prepared and discussed at the policy making level and a letter has been issued by the Chief Secretary to all Ministries, Departments and Agencies to provide guidance on issuing open data.

OGPFM Prior Actions: Government initiates the pro-active disclosure of data by:

- (i) Issuing instructions to establish an interagency working group to set policies, advise on standards, and coordinate implementation of open data across MDAs and LGAs.

- (ii) Issuing a circular with interim guidelines for publishing data in Open Data format on the Government OD portal.

CASH MANAGEMENT

26. **Government is committed to improve the predictability of funds disbursements to MDAs (including LGAs) in line with their approved budgets.** Consistent under collection of domestic revenues have undermined the Government's cash flow and its ability to provide adequate funding for budget execution. A number of factors contribute to this situation: (i) unrealistic estimates, (ii) inadequate revenue collection, (iii) slower than planned project implementation, and (iv) slow disbursement of grants. Although Government undertakes cash rationing this does not prevent MDAs from incurring unfunded expenditure arrears. In the past, the IFMIS only allowed commitments up to the level of available funds (as approved by the Ceiling Committee). This resulted in accumulation of arrears when MDAs entered into spending commitments outside IFMIS, which were not funded due to cash constraints even though they were budgeted.

27. Starting from this fiscal year, MOF has modified the IFMIS to allow all payments to be recorded in the system. Since all expenditures are reported monthly, this will allow MOF to monitor and age the arrears in a timely way to enable timely decisions on funding them or taking administrative actions against unauthorized expenditures. This will allow full disclosure and better control over the arrears by MOF. It has also confirmed the legal position by issuing instructions to spending units to commit all expenditures through the IFMIS in the 2014/15 fiscal year.

28. The Government has committed to further strengthen the use of electronic payment systems by expanding the use of the Tanzania Interbank Settlement System (TISS) and the Electronic Funds Transfer (EFT) system. Currently more than 90% of tax revenues are remitted to the Government account at BOT through TISS. The BOT has also operationalised 24 sub-treasuries at regional level connected to TISS which allows them to make direct online payment for expenses of MDAs at the regional level. This resulted from implementation of Treasury Circular no. 3 of 2010 that most of the Government payments in Ministries and Regions are to be processed by using TISS with exception of standalone MDAs. However plans are underway to connect TISS to all standalone MDAs and some councils in FY 2015/16. For councils, the Government plans to connect TISS in two phases. The first phase will cover Kinondoni Municipal Council, Temeke Municipal Council, Ilala Municipal Council, Dares salaam City Council, Arusha City Council, Morogoro City Council, Tanga City Council, Mwanza City Council and Morogoro Municipal Council. The remaining councils will be connected in the second phase. Furthermore, the Government is in the process of connecting EFT to Pension Unit at the Ministry of Finance by April, 2015 and pay all Government employees' salaries by December 2015. This will improve the

centralization payments and goes a long way to establish a single payment account.

29. The Government has initiated a program based budgeting pilot in eight MDAs (Ministries of Education, Water, Health, Transport, Finance and Community Development, Gender and Children) under the Public Financial Management Reform Program. The objective is to move from an inputs to an outputs and results based budgeting system. As part of preparation to move to PBB, the government with support from development partners has been implementing changes to the Public Finance Act, the chart of accounts and introducing templates for program based budgeting in respective institutions. For 2015/16 budget, the Government has instructed pilot ministries to prepare the budgets to include shadow budgets using the PBB template. These shadow budgets will also be tabled in parliament for discussion as part of the 2015/16 budget approval process.

OGPFM Prior Actions: To improve on cash management the following prior actions have been agreed:

- (i) MOF issues instructions to spending units to commit all expenditures through the Integrated Financial Management Information Systems.
- (ii) Appropriated Budget FY14/15 provides funding to reduce the level of expenditure arrears.
- (iii) MoF pilots payments by regional MDAs through the Tanzania Inter-bank Settlement Scheme (TISS) and Electronic Fund Transfer (EFT).
- (iv) MoF and POPC jointly issue budget guidelines for six pilot MDAs, including education, water and health to present 2015/16 estimates on programmatic classification as a supplementary budget document.

PUBLIC INVESTMENT MANAGEMENT

30. The Government has prepared the Public Investment Management (PIM) manual to guide MDAs, Regional Secretariats (RSs) and Local Government Authorities (LGAs) on PIM with a focus to achieving value for money outcomes through increasing efficiency and effectiveness of public investments. Specifically, the manual is intended to serve four purposes: (a) to act as an instrument for enhancing coordination of public investments; (b) to clarify procedures for integration of projects into the national development budget; (c) to build capacity within the public sector in economic and financial analyses of public investments projects; (d) to provide guidance on integration of public

and private investments in economic development; and (e) to serve as a basis for establishing a projects database which a country now needs in order to rationalize financing of development projects by the Government.

31. The manual has been extensively discussed by stakeholders and has now been approved for use across the public sector. The MOF has included specific instructions on the use of this manual by all spending units in the preparation and selection of projects for the next fiscal year 2015/16. It is expected that the PIM manual will lead to a more objective criteria in the use of public investment resources and improved economic and social welfare of the people.

OGPFM Prior Action: MoF issues budget guidelines that require the mandatory use of the Public Investment Management (PIM) manual in preparation and screening of investment projects.

PROCUREMENT

32. Government has achieved an important milestone in improving public procurement by gazetting in December 2013 the regulations related to the Public Procurement Act of 2011. Key changes in the Act and regulations include: Providing clarity on institutional roles and mandates of the five organs involved in implementing the law: i) Ministry of Finance Procurement Policy Division (PPD) established to develop and monitor implementation of the procurement policy; ii) Public Procurement Regulatory Agency (PPRA) responsible for regulating and monitoring procurement activities in Procuring Entities (PE); iii) Public Procurement Appeals Authority (PPAA) whose mandate is to hear and determine appeals and complaints from bidders; iv) Procurement and Supplies Professional and Technician (PSPTB) responsible for regulating and monitoring conducts of procurement and supplies professionals in the country and; v) Government Procurement Services Agency (GPSA), which coordinates and manages procurement of commonly used items.

33. The accompanying regulations grant more powers to the Public Procurement Regulatory Agency (PPRA) to suspend procurement processes prior to contract award in case of non-compliance with the Act and regulations; it also extends PPRA control over procurement transactions under Public Private Partnerships (PPPs). The Act and regulations also give more autonomy to the PPAA in hearing appeals related to procurement in contrast to the past when it was a department under the MOF. Penalties for non-compliance with the Act and regulations have also been enhanced to be more stringent.

OGPFM Prior Actions: MOF publishes the regulations to implement the Public Procurement Act 2011 and a notice to all procuring entities to implement the Act and regulations.

34. Following discussions with the Bank team, we concur with the proposed triggers of the second CGPFM operation and are committed to achieving them in line with the program timeline. For the purpose of transparency, we concur that this letter of development policy and the aide Memoire of the appraisal mission can be disclosed to the public

CONTRIBUTION TO BUDGET SUPPORT AND ADHERENCE TO UNDERLYING PRINCIPLES

35. External finance continues to be an important component of the Government budget. Government continues to favor the use of budget support as the main modality for aid provision. Implementation of the Budget Support is guided by the Partnership Framework signed in May 2011. Under PFM, Government and Development Partners have agreed to implement a set of principles and commitments designed to improve the overall performance of Government, including Governance and Accountability, improved service delivery and enhanced anti-corruption efforts.

36. In the interest of transparency, I would like to assure you that the Controller and Auditor General of Tanzania, following instructions of the Prime Minister and acting on the directive of the Parliament undertook an investigation of the closure of an escrow account in the BOT that had been established to pay for disputed capacity charges to IPTL an independent power provider to TANESCO. The investigative report has been submitted to the Parliament and a decision has been made. Government is following up on implementing the decisions taken by Parliament to ensure that this issue is resolved.

CONCLUSION

37. As mentioned in my earlier letter of development policy at the end of the PRSC series, the Government welcomes the new program on Open Government and Public Financial Management. It looks forward to working with the World Bank to enhance the quality of Governance through this mechanism and to promote the development goals set out in the MKUKUTA and Five Year Development Plan.

Thank you for your continued cooperation and support.

Yours sincerely,

Dr. Servacius B. Likwelile
PERMANENT SECRETARY