

**State of Public Finance in Bosnia and Herzegovina
- Report -**

September 2014

1. Introduction

This report aims to identify the state of public finance in Bosnia and Herzegovina (BiH) by analysing key indicators and aspects of public finance. Also, it provides a comparison between key indicators for Bosnia and Herzegovina and those for Serbia, Montenegro and Macedonia.

The report/analysis focuses on the following aspects and indicators:

- A brief overview of the projects and programmes that have dealt with or are dealing with fiscal sector reform, aiming at full compliance with EU requirements;
- Analysis of the institutional capacity of key institutions dealing with public finance;
- The scope and structure of public expenditure (Economic Budget Classification);
- Public expenditure according to functional budget classification, with special emphasis on expenditures for general public services;
- Budget as one of the main instruments to implement governments' economic and social priorities;
- Projections of expenditures for several years ahead as part of the budget process, which explicitly include the costs and implications of new policies and laws;
- The difference between forecasted and actual revenues in the budget;
- The difference between forecasted and actual expenditures in the budget;
- The budget as a result of consultation with institutions that are budget users, as well as with Parliament/Assembly, subject to a fixed budget calendar;
- BMIS – Budget Management Information System;
- Public-sector wage bill, and its share in the gross domestic product (GDP) and budget expenditure;
- The share of expenditures for goods and services in budget spending;
- Vertical and horizontal compression of salaries of civil servants.

2. Projects in the fiscal sector¹

Since the economic criteria for EU integration are laid down in the Stabilisation and Association Agreement with the European Union, the European Union Delegation in Bosnia and Herzegovina is, expectedly, one of the biggest donors in public administration reform, including public finance and fiscal system, through the IPA (Instrument for Pre-Accession Assistance) funds. Donor support was/is given to the following areas: development and implementation of a countrywide BiH Public Internal Financial Control Strategy (PIFC); building capacity for consolidation of public finance data in line with international, especially EU principles, standards and practices (ministries of finance at the state and entity levels and the level of Brčko District); improving the quality of fiscal policy and the links between fiscal policy makers and budgeting procedures; strengthening treasury operations in compliance with EU

¹ <http://www.usaid.gov/bosnia-herzegovina/partnership-opportunities> (Request for Proposal No.: SOL-168-14-000006 – Fiscal Sector Reform Activity in Bosnia and Herzegovina)

standards; assistance in public procurement reform; strengthening capacity for public debt management.

There are also many donors operating through the Public Administration Reform Coordinator's Office (PARCO). Projects aimed at further public finance reform are defined in the Action Plan (later modified and referred to as the Revised Action Plan – RAP 1), and are to be financed from the Public Administration Reform Fund (PAR Fund). Main contributors to the PAR Fund are international donors and foreign governments: Delegation of the European Union in BiH, Ministry of Foreign Affairs of Great Britain, Swedish International Development Cooperation Agency (SIDA), The Royal Netherlands Embassy, and Ministry of Foreign Affairs of the Kingdom of Norway. Areas of interest are²: (1) Policy dimension of the public finance system; (2) Raising efficiency and effectiveness of budget management (including introduction of BMIS – Budget Management Information System – to manage budget in line with best European practices; (3) Improving the accounting framework and the treasury system operations; (4) Introduction of Public Internal Financial Control (PIFC) in full compliance with EU requirements; (5) Improving the organisational structure and investing in capacity building; (6) Development of public-private partnership; (7) Public procurement system; (8) Effective management of public debt. Some of these areas are/were indeed financed by the PAR Fund, but other donors also get involved working in coordination with PARCO office and the Revised Action Plan (RAP1). Since the Revised Action Plan expires in December 2014, some of its parts are very likely to remain unfulfilled. Since the last available/adopted RAP1 Progress Report is from July 2013³ (biannual report for 2013), it is not known what sections of the Revised Action Plan will not be implemented.

The International Monetary Fund Mission (IMF) is a strong supporter of fiscal sector reform. The US Agency for International Development (USAID) and IMF coordinated their activities in the fiscal arena, in areas such as Unified System of Registration, Control and Collection of Contributions, and Payroll Processing System. The IMF has recently supported the adoption of the new Law on Budgets in the Federation of Bosnia and Herzegovina (FBiH) and the state-level Public Procurement Law of BiH, which was drafted with the assistance of the European Union. The new Public Procurement Law further harmonises and regulates the domestic public procurement framework with EU standards. This will have a direct impact on public expenditure. The IMF also supports the work of all four tax administrations⁴ in Bosnia and Herzegovina. The new Law on Budgets in the Federation of Bosnia and Herzegovina is very important for improving fiscal discipline.

² <http://parco.gov.ba/latn/?page=456>

³ Information that the 2013 RAPI Progress Report had been adopted by the Council of Ministers was published on the PARCO website on 10 September 2014, but as at 16 September 2014 the Report is still not available on the PARCO website.

⁴ Tax Administration of the Federation of Bosnia and Herzegovina, Tax Administration of the Republic of Srpska, Tax Administration of Brčko District, Indirect Taxation Authority of Bosnia and Herzegovina

USAID has implemented four projects in the area of fiscal sector reform (TAF, ELMO, TARA and TAMP), during a period of over ten years. Significant reforms have also been undertaken to streamline the entity-level tax administrations, as well as in the field of direct taxation, unified system of registration, control and collection of contributions, simplifying the payment of taxes and contributions, and developing fiscal analysis capacity. USAID plans to continue its activity in the fiscal sector through a new project (Fiscal Sector Reform Activity in BiH), which will be implemented in coordination with other donors, as well the Public Administration Reform Coordinator's Office, the Public Administration Reform Strategy in BiH and the Revised Action Plan, with special emphasis on public finance, information technology, and building policy-making and coordination capacities.

There is also ongoing cooperation between the governments in BiH and the GIZ project (German Technical Cooperation Agency) for technical assistance in public administration reform. GIZ provides support for introduction of electronic tools into the public procurement system of BiH.

DfID's (UK Department for International Development) project SPEM (Strengthening Public Expenditure Management in BiH) was completed three years ago⁵. The project supported introduction of medium-term budget planning in BiH (10-step budgeting process).

3. Institutional capacities

In the field of public finance, the PARCO's Revised Action Plan (RAP1) envisages, *inter alia*, implementation of capacity building activities with a special focus on the ministries of finance, and in particular their units responsible for the budget and fiscal policy. Continued training of staff is implemented at all levels (Bosnia and Herzegovina – BiH, the Federation of Bosnia and Herzegovina – FBiH, Republic of Srpska – RS, and Brčko District – BD) in the form of workshops, training events, presentations and seminars. However, the training of staff in the units responsible for the budget and fiscal policy has been implemented only partially (2013 RAP1 Biannual Progress Report). The RAP1 Progress Report places focus on strengthening capacities of the units responsible for the budget, while those that are responsible for fiscal policy are backburnered, and are not explicitly mentioned, though anticipated by the Revised Action Plan. Although USAID provided significant support to strengthening capacities and developing quantitative models of entity units dealing with fiscal policy, there is still considerable room for further strengthening entity capacities, as well as capacities at the national level and in Brčko District. Although a proposal has been circulating for many years to establish special fiscal analysis within the entity ministries of finance, this has only been done by the Ministry of Finance of RS. The Ministry of Finance of FBiH has adopted a new Regulation on Internal Organisation and Staffing, but this new regulation does not include a unit for fiscal analysis.

⁵ http://www.mca.org.uk/library/documents/pkf_with_department_for_international_development.pdf

The personnel of this unit would be concerned only with making models for projections of revenues and expenditures, simulating the effects of various legislative amendments, etc. through sophisticated quantitative methods, such as microsimulations and econometrics. Although such a unit does not exist in FBiH, employees of the Tax Policy and Public Revenue Sector undertake the modelling upon themselves in addition to their regular tasks, and cannot focus on such complex processes, even though they are making maximum efforts. In any case, employees in the fiscal policy units at all levels need further capacity building for (microsimulation and econometric) modelling in order to be able to make more precise projections of revenues and expenditures. USAID plans to finance, among other things, such further capacity building through a new pipelined project Reform of the Fiscal Sector in Bosnia and Herzegovina to be implemented over a period of five years. The SIGMA⁶ 2013 report also highlights the need for capacity building with a view to improving reliability of fiscal impact estimates.

4. The scope and structure of public expenditure (Economic Budget Classification)

This section focuses on the structure of public expenditure according to Economic Budget Classification,⁷ as well as the scope of individual expenditure items in total expenditure. Also, a comparison will be made with Serbia, Montenegro and Macedonia. The calculation of expenditures presented herein does not include expenditures made at the municipal level and extra-budgetary funds.

Table 1: Scope and structure of public expenditures and expenses as a share of total expenditures and expenses and GDP, 2014

Countries and Entities	Wage Bill	Goods and Services	Transfers	Capital Expenditures	Interest Payments	Reserves	Expenditure for Financial Assets	Repayment of Debts	Expenditures and expenses as a share of GDP
FBiH	10%	3%	42%	1%	4%	0%	1%	38%	N/A
FBiH (with cantons)	30%	6%	35%	5%	2%	0%	1%	20%	26%
RS	32%	5%	33%	1%	3%	0%	0%	25%	23%
BD	33%	20%	30%	16%	0%	0%	0%	1%	N/A
BiH (consolidated)	35%	8%	31%	5%	2%	0%	0%	19%	29%
Serbia	17%	6%	34%	3%	7%	0%	2%	29%	47%
Montenegro	34%	11%	13%	11%	8%	1%	0%	19%	28%
Macedonia	16%	13%	44%	16%	3%	0%	0%	8%	30%

⁶ SIGMA is a joint initiative of the EU and the OECD.

⁷ Economic Budget Classification was developed by the IMF and is known as the GFS (Government Finance Statistics).

Sources: author's calculations based on publicly available budgets found on the websites of Ministries of Finance (countries, entities and cantons); GDP – Central Bank of BiH; Agency for Statistics of BiH; Directorate for Economic Planning of BiH; Investment-Development Bank of RS; Republic Institute of Statistics (Serbia); National Bank of Serbia; Chamber of Commerce of Montenegro; Ministry of Finance of Montenegro; State Statistical Office (Macedonia); www.izvoznookno.si

The share of public expenditures and expenses (consolidated for BiH including the following levels: FBiH with the cantons, RS, BD and BiH) in GDP in BiH is about 30%, similar to Macedonia and Montenegro. The highest public expenditures and expenses as % of GDP are found in Serbia, as high as 47% (Table 1)⁸.

In terms of structure, public expenditures and expenses consist of eight categories: wage bill, goods and services, transfers, capital expenditures and grants, interest payments, reserves, financial assets, debts. Consolidated data for BiH show that wage bill makes up a major share of the expenditures and expenses (35%). The wage bill share at other administrative levels (FBiH with the cantons, RS and BD) is similar to BiH (consolidated) and ranges between 30% and 33%. Put simply, about a third of the expenditures and expenses in BiH (consolidated) goes on public sector wages (gross salaries, remunerations and contributions paid by the employer). Another third of all expenditures and expenses in BiH (consolidated) goes on various transfers (31%), and about 20% goes to debt repayment. Capital expenditures account only for 5% of total expenditures and expenses.

Compared with other countries in the region, BiH (consolidated) allocates approximately the same proportion of the budget for salaries as Montenegro, and more than Serbia (17%) and Macedonia (16%). In Serbia, the percentage of the budget that goes to debt repayment is higher than in BiH (29%), while the percentage in Montenegro (19%) is the same as in BiH, and in Macedonia (8%) much lower than in BiH. Of the countries in the region, Macedonia allocates most towards capital expenditure – 16% of the total budget.

Table 2: Scope and structure of public expenditure as a share of expenditure, 2014

Countries and Entities	Wage Bill	Goods and Services	Transfers	Capital Expenditures	Interest Payments	Reserves	Expenditure as % of GDP
FBiH	14%	5%	68%	3%	6%	0%	N/A
FBiH (with cantons)	38%	8%	44%	6%	3%	0%	21%
RS	43%	7%	44%	2%	3%	0%	17%
BD	33%	20%	31%	16%	0%	0%	N/A

⁸ The state level (BiH) is not reviewed here because it has very limited powers.

BiH (consolidated)	44%	10%	38%	6%	3%	0%	24%
Serbia	25%	9%	50%	5%	10%	0%	32%
Montenegro	42%	14%	16%	13%	10%	1%	23%
Macedonia	18%	14%	48%	17%	3%	0%	27%

Source: see source for Table 1

In Table 2, six groups are treated as total expenditure, i.e. expenditures for financial assets and repayment of debts are excluded. In this case, the total expenditure as a percentage of GDP in BiH (consolidated) is 24%, very similar to Montenegro (23%) and Macedonia (27%). However, the distribution within expenditure is different, with almost half of the budget in BiH (consolidated) going to salaries. This percentage is similar to Montenegro (42%), but is significantly lower in Serbia (25%) and Macedonia (18%). The percentage of funds allocated for the purchase of supplies and services is similar in BiH, Serbia and Montenegro, totalling about 10%, while reaching 14% in Macedonia and Montenegro. Capital expenditures are still the highest in Macedonia at 17%, whereas in BiH they amount to 6%, which is approximately the same as in Serbia (5%).

5. Expenditure on general public services (Functional Budget Classification)

Based on the Functional Budget Classification⁹, the table below (Table 3) shows the share of total expenditures and expenses that goes on general public services.

Table 3: General public services as a share of expenditure and expenses, 2014

Levels in BiH	General public services	Other general government	Common and utility services	Economic services	Other spending
FBiH (without cantons)	51%	6%	36%	7%	0%
RS	6%	15%	36%	9%	33%
BD	21%	12%	53%	5%	9%
BiH	18%	69%	3%	6%	3%
BiH (consolidated for 4 levels)	29%	21%	31%	7%	12%

Sources: author's calculations based on the Framework Budget Document for: FBiH (2015-2017), RS (2015-2017), BiH (2014-2016); Brčko District (Budget 2014)

As shown in Table 3, about 30% of the consolidated budget for BiH goes on general public services. However, there is a logical inconsistency in the percentage for the Republic of Srpska (extremely low) and for the Federation of Bosnia and Herzegovina (extremely high).

⁹ Functional Budget Classification was developed by the OECD and is known as the COFOG classification (Classification of the Functions of Government).

Specifically, general public services account for only 6% and other spending (including the debt) for 33% of the budget expenditure in RS, while in FBiH general public services account for 51% of the budget expenditure and other spending is practically nonexistent. In fact, such huge discrepancies are due to the fact that different levels of government use different statistical classifications. Classifications should be harmonised and improved in order to be comparable.

6. Budget as a reflection of policies and priorities

The Public Administration Reform Strategy¹⁰ envisages improvement of policy objectives and budget. There are two aspects to the policy-budget link: on the one hand, the budget is the main tool through which Government implements its strategic priorities and, on the other, the implementation of policy objectives is constrained by the availability of budget resources. Due to these mutually affecting aspects, the budget needs to clearly reflect policy objectives. Also, decision-makers must determine policy priorities in order to use the already limited resources as effectively as possible.

The Public Administration Reform Strategy envisages the following:

- Approaching strategic priority-setting with complete awareness of the financial impacts of each set priority and the resources available for success within immediate and mid-term budgeting periods;
- Improving communication within institutions, between the policy-defining stakeholders and the finance units; and
- Strengthening communication between institutions, ministries of finance, and government, to ensure incorporation of policy objectives within the budget.

The Revised Action Plan (RAP1)¹¹ of the Public Administration Reform Coordinator's Office provides (in its section related to public finance) for activities aimed at increasing efficiency and effectiveness of budget management. The section dealing with the budget as a reflection of government policies and priorities pays particular attention to strengthening communication between institutions' management and finance units. This means more intensive inclusion of the management in the process of budget preparation and consultation between the Budget Departments of MoFs and budget users. The end result of this process should be improved decision-making, identification and ranking of policy priorities, objectives and financial needs. Also, the plan is to improve monitoring of set goals, impact assessments and internal and external reporting.

Simply put, the ultimate goal of reform should be to ensure that budgets reflect government targets in line with the projected macroeconomic indicators, social conditions and fiscal

¹⁰ <http://parco.gov.ba/latn/?page=110> (Public Administration Reform Strategy)

¹¹ <http://parco.gov.ba/latn/?page=453> (Revised Action Plan)

framework. It is important to note that all legislative amendments that have financial consequences for the budget should be accompanied with projected financial consequences with adequate explanations thereof. Budget is not planned for one year only, but for the next three years, and everything should be in accordance with the communication between the ministries of finance and budget users.

6.1. Budget Framework Paper

All laws governing budgets¹² at all four administrative levels provide for the preparation of a Budget Framework Paper (BFP), which serves as a basis for drawing up the budget. BFP includes the following:

- Macroeconomic projections (economic development forecast, social sector development forecast, forecast of macroeconomic indicators, fiscal framework)
- Projections of budget funds and expenditures for the next three years.

So, for example, BFP is adopted for the period 2015-2017 in 2014, and serves as a basis for drafting the budget for 2015.

The laws governing the budgets also provide that all proposed laws or any other legal acts that result in financial or fiscal impacts must contain, as a background document, projections of fiscal impact on the budget, and the explanation thereof, as well as how lost revenue will be compensated from other sources. The projections should be made for the current year and the next two years (three years in total). This is stipulated in particular detail in the Law on Budgets in the Federation of Bosnia and Herzegovina and the Law on Budget System of the Republic of Srpska.

The Budget Law of the Brčko District BiH requires that any regulations that might have financial consequences for the budget should be substantiated by an accompanying cost-benefit analysis, but it does not provide any specific guidelines.

The Law on the Financing of Institutions of Bosnia and Herzegovina has no provisions governing the financial effects of new or amended regulations. However, the provision on balancing the budget only mentions that the Ministry of Finance may balance the budget by finding new revenues or reducing projected expenditures.

Review of the FBiH and RS BFPs for 2015-2017 indicates that the documents are in compliance with the relevant legislative provisions and the prescribed timeframe. In both entities BFPs are publicly available and can be accessed on the websites of the entity ministries of finance.

¹² Law on the Financing of Institutions of Bosnia and Herzegovina, Law on the Budgets in the Federation of Bosnia and Herzegovina, Law on the Budget System of the Republic of Srpska, Budget Law of Brčko District of Bosnia and Herzegovina

Although the law provides for the adoption of a BFP at the level of BiH, it has not yet been adopted or, at least, is not made publicly available, even though the deadline for its posting on the website of the Ministry of Finance and Treasury of BiH was 15 July 2014. This begs the question – if BFP has not been adopted, why has it not been adopted yet, because this constitutes a violation of the budget process; or, if it has been adopted, why is it not available on the website of the Ministry of Finance and Treasury of BiH, because this makes BFP non-transparent and is also a violation of the budget process.

Similarly, in Brčko District the last available BFP is the one for 2012-2014, which makes this document non-transparent.

6.2. Budget calendar

BFP is part of the budget process, and is made in accordance with the budget calendar. The budget calendar is shown in the table below (Table 4).

Table 4: Budget calendar

	FBiH	RS	BD	BiH
Instruction 1; MF – Users	15/02/	15/02/	31/01/	31/01/
Users’ proposals	15/04/	30/04/	15/04/	15/04/
MF preliminary draft of BFP				28/04/
MF – Government	15/06/		15/06/	15/06/
Adoption of BFP	30/06/	30/06/	30/06/	30/06/
MF – BFP – municipalities, cities, funds		01/07/		
Web MF	15/07/		15/07/	15/07/
Submitting BFP to the Assembly (Memorandum)			15/07/	
Instruction 2 – Budget constraints	15/07/	01/07/	01/07/	01/07/
Users’ budget requests	15/08/	01/09/	01/08/	01/08/
Consultation between MF and users	15/09/			01/10/
MF – Government Budget draft	15/10/	15/10/	15/09/	01/10/
Council of Minister – Presidency Budget draft				15/10/
Government draws up budget draft	01/11/	05/11/	01/10/	
PM/Presidency/Mayor – Parliament Budget Draft	05/11/		01/10/	01/11/
Assembly’s opinion		15/11/		
Final budget proposal Government – Assembly		01/12/		
Budget	31/12/	15/12/	01/12/	31/12/

Sources: Law on the Financing of Institutions of Bosnia and Herzegovina, Law on the Budgets in the Federation of Bosnia and Herzegovina, Law on the Budget System of the Republic of Srpska, Budget Law of Brčko District of Bosnia and Herzegovina

The budget process at all four administrative levels takes place in a similar way, with several different steps.

The first step is to Instruction No. 1 on the manner and elements of BFP, which the MoFs sends to budget users, containing basic economic assumptions and guidelines for the preparation of BFP, overview of budget users' priorities, as well as the timeframe and deadlines for the preparation of BFP. Deadlines for sending the Instruction to budget users range from 31 January to 15 February, depending on the administrative level.

The next step is budget users' proposals for the preparation of BFP, which should be submitted not later than 15 April, except in RS, where the deadline for submission is 30 April.

At the BiH level, the Ministry of Finance and Treasury of BiH is required to draw up, by 28 April, draft sections of BFP containing macroeconomic and fiscal projections for the current year and the next three years.

After submission of budget users' priority proposals for the preparation of BFP, MoFs prepare their respective BFPs and submit them to the governments by 15 June, except in RS, where the deadline is not specified.

Governments adopt BFP by no later than 30 June, whereupon in RS it is submitted to cities, municipalities and funds, and in BD and FBiH to parliaments as a Memorandum. Posting BFP online should be completed by everyone by no later than 15 July, except in RS where BFP is posted on the relevant website even though there is no explicit legal obligation in place.

The next step is submission of Instruction No. 2 to budget users by MoFs. Instruction No. 2 contains budgetary constraints, methods and deadlines for the preparation of the budget, which in FBiH is submitted by 15 July, and at other levels by 1 July.

Budget users submit their budget requests to MoFs within the time period ranging between 1 August and 1 September. Consultation between MoFs and budget users is required under the budget laws in FBiH and BiH, and the deadline for the consultation is 15 September in FBiH and 1 October at the level of BiH. Consultation is not provided for under the budget law in BD, while the budget law in RS provides that consultation shall take place only when necessary, i.e. it is not a required part of the budget calendar but is left to the discretion of the Ministry of Finance. Such a vague legislative provision does not improve communication between the Ministry of Finance and budget users.

The Ministry of Finance submits to the Government the draft budget for the next fiscal year by 15 September in BD, 1 October in BiH, and 15 October in RS and FBiH.

The next steps will be disaggregated by administrative levels, for reasons of clarity.

At the state level, once the Council of Ministers draws up the draft budget, it submits it to the Presidency of BiH by 15 October. The Presidency of BiH draws up the budget proposal by 1 November, whereupon it is sent to the Parliamentary Assembly of BiH, which is required to adopt the budget for the next year by 31 December.

In FBiH, the Government prepares the draft budget by 1 November, whereupon the Prime Minister submits to Parliament the draft budget for the next fiscal year by 5 November. Parliament adopts the budget by 31 December of the current year.

In BD, the Government approves the draft budget, and the Mayor submits the budget proposal to the Assembly by no later than 1 October of the current year for the next fiscal year. Assembly approves the budget by no later than 1 December of the current year.

In RS, the Government prepares the draft budget for the next fiscal year and forwards it to the Assembly for consideration by 5 November. Assembly considers the draft budget by 15 November and submits it to the Government. This process improves the communication between the legislature and the executive and ensures inclusion of Assembly in budget preparation and drafting, which is not the case in other administrative levels in the country. The Government prepares the budget proposal for the next fiscal year and submits it to the Assembly for consideration and adoption by 1 December. The Assembly is required to adopt the budget for the next fiscal year by 15 December.

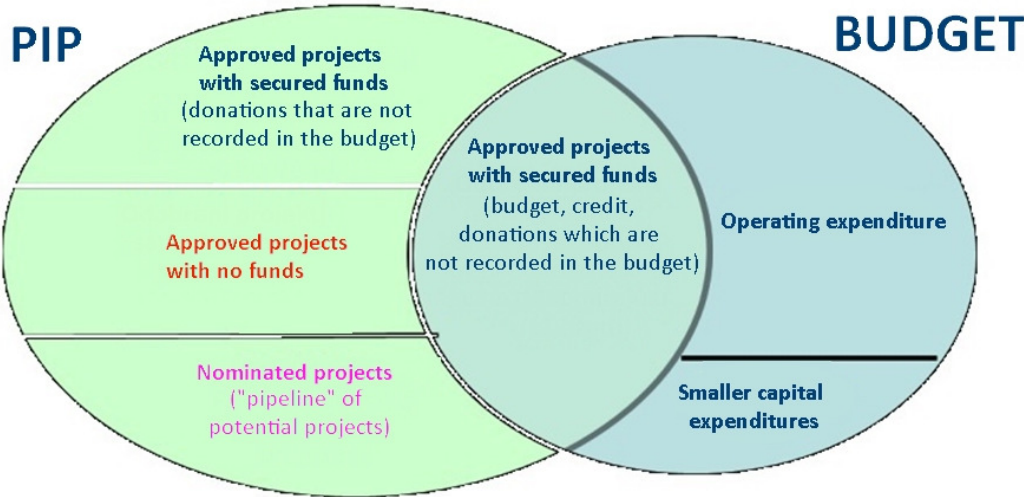
The above review of the budget calendar indicates that the legislation is fairly harmonised among all four administrative levels. It is very difficult to say whether the budget calendar deadlines established under the respective budget laws are observed in practice, as research to examine this would require much more time and a larger team of researchers. What is obvious, however, is that BD and BiH do not respect the deadlines for making BFPs publicly available on the websites of ministries of finance. Although RS is not required under the law to make its BFP publicly available on the website of the Ministry of Finance, it is nevertheless posted there. A provision making it compulsory to post BFP online should preferably be introduced in the relevant RS legislation. Budget laws in RS and BD do not provide for mandatory consultation between MoFs and budget users, which does not contribute to enhancing cooperation between them. In RS the Assembly is included in the budget consultation process, unlike other administrative levels. Therefore, continued efforts are needed in order to improve communication and involvement of budget users and parliaments in the budget preparation and drafting process. The deadlines for the adoption of budgets are

in December. All budgets for 2014 were adopted in December 2013, in compliance with the deadlines.

7. Planned budget and budget execution

This section aims to determine the accuracy of projected budget revenues and expenditures. However, during the search for data a serious lack of transparency of data was observed. Given the time of writing this report (September 2014), it is expected that all four administrative levels (FBiH, RS, BD, BiH) should already have widely available information on the execution of the 2013 budgets. However, this is not the case. It is also important to note that all capital expenditures and receipts are not included in the main budget. For example, at the BiH level, the 2014-2016 BFP contains an overview of the investments made on the basis of the document Public Investment Programme (PIP) of the BiH Institutions. It can be seen that some investments are not captured in the budget. Hence, the capital expenditures presented in the budget do not give a true picture of the investment (e.g. some investments are financed from **donations that are not captured in the budget**, Figure 1). Regarding transparency, the document Public Investment Programme of BiH Institutions is not available on the website of the Ministry of Finance and Treasury of BiH, but there is a section called Public Investment Management.

Figure 1: Link between public investment and budget



Source: 2014-2016 Budget Framework Paper of Institutions of Bosnia and Herzegovina, p. 144

7.1. Availability of data on websites

Federation of Bosnia and Herzegovina

FBiH is the only administrative level where one can transparently and without much browsing access all information pertaining to the budget (except for development programme plan).

The home page of the Ministry of Finance of FBiH (www.fmf.gov.ba) features a clearly visible link to the *Budget* section. Once opened, the section contains budget data, i.e. documents relating to the budget, sorted by years. In 2014 one can easily find all documents related to the budget for 2014, or which have been adopted in 2014.

These are the following documents:

- Report on FBiH Budget Execution for 2013
- 2015-2017 FBiH Budget Framework Paper
- General Part of the Report on FBiH Budget Execution for 2013
- Special Part of the Report on FBiH Budget Execution for 2013
- 2014-2016 Budget Framework Paper
- Deposit and transaction accounts of the FBiH Budget
- FBiH Budget for 2014
- General
- Special
- Revenues, receipts and financing
- Law on Execution of the Budget for 2014
- 2015-2017 Economic and Fiscal Policy Guidelines of FBiH,

as well as documents relating to amendments to the FBiH Budget for 2014:

- Amendments to the FBiH Budget for 2014
- Revenues, receipts and financing
- Expenses Plan, general
- Expenses Plan, special
- Article 4
- Law Amending the Law on Execution of the FBiH Budget for 2014.

So, all relevant documents are contained in one place. Of course, they can be systematised and given more specific titles (e.g. title 'General' does not say much about the content of the document), so as to facilitate access to and ensure clarity of each document. For example, the documents for 2014 can be categorised under the following headings: Budget for 2014, Budget Execution 2013, Budget Framework Papers, and Other, so as to make it even easier for users to access them.

Republic of Srpska

The website of the Ministry of Finance of the Republic of Srpska does not contain all relevant documents relating to the RS Budget. The only document available is the RS Budget and budget archive.

The budget execution report for 2013 is needed if a comparison is to be made between the actual revenues and expenditures and those planned. However, it turned out that such a report was not publicly available. Information on its adoption can only be found in the media, but its content is not publicly available.

Brčko District

The website of the Brčko District (Important Legislation – Budget of Brčko District) contains both the budget paper and budget execution document. In addition to the executed budget, the budget execution document contains the planned budget for 2013. However, the planned budget is different from the approved budget for 2013. It is not known whether there were any revisions of the 2013 budget.

Bosnia and Herzegovina

The website of the Ministry of Finance and Treasury of BiH, in the section concerning the budget and budget execution, contains a number of different documents that should be sorted by end users. Thus, for example, the budget execution section contains documents on budget execution as well as instructions for budget users which do not concern citizens, analysts, etc. For them, there should be a separate section of the website to ensure easier access.

It was also observed that the budget execution report for the entire year 2013 for the institutions of Bosnia and Herzegovina is not available on the website. It turns out that the report has not yet been adopted even though it is already September 2014.

The website of the Ministry of Finance and Treasury of BiH, in the section concerning the budget, requires an access password for the Official Gazette of BiH in order to access the budgets for individual years, which makes the budget non-transparent.

7.2. Accuracy of projections

When the adopted budgets of FBiH and Brčko District are compared with their execution (Table 5, Table 6), i.e. with actual revenues and expenditures, it is evident that the actual revenues and expenditures differ significantly from the projected budget with regard to specific budget items. On the expenditure side substantial savings were made, but on the revenue side the planned levels have not been achieved. This may be accounted for by the general economic conditions in the country, as well as weak inspection of the black economy and the customarily unrealistic budget planning, where higher revenues (and, by extension, expenditures) are consciously planned for reasons of political opportunism. What is also very important to note is that the projection models for both revenues and expenditures are

imprecise and require further improvements, as already discussed in the section concerning the institutional capacity of key institutions dealing with public finance.

Table 5: Adopted budget and budget execution for 2013, FBiH and RS

	FBiH			RS		
	Budget	Execution	Variance ¹³	Budget	Execution	Variance
REVENUES						
Tax Revenues	1,344,781,036	1,262,367,000	-6%	1,404,235,000		
Non-tax Revenues	451,224,186	274,442,000	-39%	126,891,000		
REVENUES	1,796,005,222	1,536,809,000	-14%	1,531,126,000		
Receipts (financing)	418,174,900	399,042,000	-5%	413,874,000		
REVENUES AND RECEIPTS	2,214,180,122	1,935,851,000	-13%	1,945,000,000		
Surplus of Revenue over Expenditure		-65,265,179				
	FBiH			RS		
	Budget	Execution	Variance	Budget	Execution	Variance
EXPENDITURES AND EXPENSES						
Wage Bill	237,811,048	224,887,429	-5%	642,087,900		
Goods and Services	91,632,465	73,931,832	-20%	104,632,100		
Transfers	978,245,583	960,370,286	-2%	670,169,100		
Capital Expenditures and Transfers	93,304,112	44,492,823	-52%	19,164,400		
Interests	94,669,700	68,485,675	-28%	43,473,100		
Reserves	6,310,000	0	-100%	1,920,500		
Financial Assets	15,458,214	12,555,356	-20%	150,000		
Debt Repayment	696,749,000	616,392,778	-11%	463,402,900		
EXPENDITURES AND EXPENSES	2,214,180,122	2,001,116,179	-10%	1,945,000,000		
Expenditures¹⁴ without transfers	523,727,325	411,797,759	-21%	811,278,000		

¹³ Difference between actual performance and forecast

¹⁴ Excluding Financial Assets and Debts.

Expenditures 15	1,501,972,908	1,372,168,045	-9%	1,481,447,100		
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Sources: FBiH Budget for 2013, Execution of FBiH Budget for 2013, RS Budget for 2013

Table 6: Adopted budget and budget execution for 2013, BD and BiH

	BD			BiH		
	Budget	Execution	Variance	Budget	Execution	Variance
REVENUES						
Tax Revenues	173,110,000	169,089,573	-2%	750,000,000		
Non-tax Revenues	30,190,594	26,780,348	-11%	140,026,000		
Grants	2,195,993	2,087,206	-5%	7,216,000		
REVENUES	205,496,587	197,957,127	-4%	897,242,000		
Receipts (financing)	29,688,942	33,447,557	13%	52,758,000		
REVENUES AND RECEIPTS	235,185,529	231,404,684	-2%	950,000,000		
Surplus of Revenue over Expenditure		32,806,553				
Revenues for Servicing BiH's External Debt:				788,476,010		
FBiH				509,400,847		
RS				273,467,804		
BD				861,606		
BiH				4,745,753		
				1,738,476,010		
	BD			BiH		
	Budget	Execution	Variance	Budget	Execution	Variance
EXPENDITURES AND EXPENSES						
Wage Bill	80,712,501	74,855,063	-8%	636,215,000		
Goods and Services	46,705,270	44,993,785	-4%	190,477,000		
Transfers	67,573,297	70,613,961	-5%	36,911,000		
Capital Expenditures and Transfers	38,615,482	7,727,148	-80%	76,995,000		
Interests	493,574	411,174	-17%	450,000		
Reserves				8,952,000		

¹⁵ Excluding Financial Assets and Debts, but including Transfers.

Financial Assets						
Debt Repayment	1,075,403	1,101,790	2%	788,476,010		
TOTAL EXPENDITURES AND EXPENSES	235,185,527	199,699,921	-15%	1,738,476,010		
Expenditures without transfers¹⁶	166,536,827	127,984,170	-23%	913,089,000		
Expenditures¹⁷	234,110,124	198,598,131	-15%	950,000,000		

Sources: BD Budget for 2013, Execution of BD Budget for 2013, BiH Budget for 2013

8. Treasury System and Budget Management Information System (BMIS)

In the Federation of Bosnia and Herzegovina, the treasury system was introduced at the entity and cantonal levels. However, the vast majority of municipalities in the Federation of Bosnia and Herzegovina continue to operate outside the treasury system although the deadline for its introduction has been repeatedly extended under the Law on Budgets in the Federation of Bosnia and Herzegovina (old law). Apart from municipalities, there are other institutions at the FBiH level, as well as the majority of extra-budgetary funds and some state-level institutions that remain outside the treasury system. They continue to enter all their transactions manually, by filling in paper forms. This is a completely non-transparent process of reporting and is also susceptible to errors. For proper management of public funds, it is essential that all budget institutions are incorporated in the treasury system.

In the Republic of Srpska all entity institutions and municipalities have introduced the treasury system, with the sole exception of the health sector¹⁸. Integration of RS's health sector transactions into the treasury system would improve management of healthcare funds.

With the help of IPA funds and the Public Administration Reform Fund, BMIS has been introduced to all four levels of government (state, entity and Brčko District). What remains a problem, however, is the fact that cantons and municipalities in FBiH remain outside the system because RS did not give its consent to their incorporation. It is necessary to continue efforts aimed at deploying BMIS at the lower levels of FBiH administration, at least the cantonal level.

¹⁶ Excluding Financial Assets and Debts.

¹⁷ Excluding Financial Assets and Debts, but including Transfers.

¹⁸ <http://www.usaid.gov/bosnia-herzegovina/partnership-opportunities> (Request for Proposal No.: SOL-168-14-000006 – Fiscal Sector Reform Activity in Bosnia and Herzegovina)

The deployment of BMIS introduces a technical basis for improving budget management. The aim of this project is to ensure that all budget institutions access the budget preparation through a centralised online database located in the ministries of finance. Before the introduction of BMIS, budget users' requests were entered manually into Excel spreadsheets. The introduction of BMIS will reduce the likelihood of errors, increase the transparency of money management, and improve reporting and fiscal discipline.

BMIS system has been upgraded to include a component for Gender-Responsive Budgeting.

The introduction of Treasury System and BMIS at all levels will further improve the flow, accuracy and transparency of data/information as well as fiscal discipline.

Also, the introduction of BMIS provides a technical basis for improving coordination between the ministries of finance at all levels of government and budget users. The budget for 2014 was planned in BMIS system.

Given that one of the objectives of the Revised Action Plan (RAP1) is timely inclusion of Parliament/Assembly in the budget approval process and expanded reporting towards Parliament/Assembly and the public, the introduction of BMIS will provide a technical basis for clearer and more transparent monitoring of impact indicators and cost justification of the programmes and activities of budget users. That should be the end result and the expected outcome of the introduction of BMIS, which should be monitored over time to ensure that the implementation of this objective is proceeding well.

9. Salaries, budget and compression

This section focuses on wage bill expenditures, and their share in GDP and in budget expenditure. Additionally, it analyses the share of expenditures for goods and services in budget expenditure. The analysis includes both vertical and horizontal pay compression. All indicators are presented comparatively for BiH, Serbia, Montenegro and Macedonia. BiH data are presented for the state level, entities and Brčko District, as well as consolidated for the whole country (excluding municipalities and extra-budgetary funds).

9.1. Description of indicators

This section examines six indicators across four countries (Bosnia and Herzegovina, Serbia, Montenegro and Macedonia):

1. Wage bill expenditures over a five-year period

Wage bill expenditures include gross salaries, gross remunerations and other employee benefit plans, and other contributions paid by the employer. Therefore, this study looks at the employer's total expenses for employees. It takes a period of five years as a reasonable

medium-term period for observing changes in the expenses for employees. Sources of data used include the budget papers that are publicly available on the websites of ministries of finance and governments. BiH is analysed on several levels – state-level budget, entity budgets and BD budget. FBiH budget includes cantonal budgets for cantons where relevant data were publicly available. For the cantons where data were not available, estimates were used.

2. Wage bill expenditures as a share of GDP

Wage bill expenditures mentioned in Indicator 1 are expressed as a percentage of GDP. Wage bill expenditures for the entire country were obtained by adding up the expenditures from the state-level budget, entity budgets, BD budget and cantonal budgets. This amount was then placed in relation to the GDP of BiH. Also, the wage bill expenditures for the Republic of Srpska were looked at separately and put in relation to the portion of GDP belonging to RS. The same was done for wages in FBiH – they were placed in relation to the portion of GDP that belongs to FBiH.

3. Wage bill expenditures as a share of budget expenditure

This indicator is observed in two parts. In the first part the budget expenditure consists of wage bill expenditures, expenditures for goods and services, expenditures for interests, expenditures for reserves, and capital expenditures (excluding subsidies and transfers, expenditures for financial assets and repayment of debts). In the second part budget expenditure also includes subsidies and transfers (excluding expenditures for financial assets and repayment of debts).

4. Expenditures for goods and services as a share of budget expenditure

Indicator 4 is also observed in two parts, in the same way as Indicator 3.

5. Vertical pay compression

Vertical pay compression is defined as the ratio of highest salary to lowest salary on the civil servants' salary scale. (Mills et al., No date; Richardson & Thomas, 2013). Sources of information about salaries of civil servants used for the purposes of this report were laws on salaries of civil servants, with the exception of Macedonia, where there is no such law, but wages are regulated by the Law on Civil Servants.

6. Horizontal pay compression

Unlike vertical pay compression which looks at salaries of civil servants at different job levels, horizontal pay compression is the ratio of salaries of civil servants who are at the same or similar job level, but have different salary levels (Richardson & Thomas, 2013).

9.2. Indicators in numbers

This section will present the results of research based on the above indicators (1 through 6):

1. Wage bill expenditures over a five-year period

Table 7 below shows wage bill expenditures across countries, entities and years.

Table 7. Wage bill expenditures (in KM)

Countries and entities	2014	2013	2012	2011	2010	2014/2013 % change	2013/2012 % change	2012/2011 % change	2011/2010 % change	2014/2010 % change
BiH	643,796,000	636,215,000	635,702,000	648,144,924	671,188,000	1	0	-2	-3	-4
FBiH (with cantons)	1,363,471,991	1,308,050,726	1,277,393,140	1,246,704,641	1,196,018,618	4	2	2	4	14
FBiH	251,943,154	237,811,048	232,463,098	237,258,129	229,828,773	6	2	-2	3	10
RS	656,609,000	642,087,900	698,610,200	627,672,200	627,331,100	2	-8	11	0	5
BD	72,005,808	80,712,501	85,283,194	75,601,347	84,329,520	-11	-5	13	-10	-15
BiH (consolidated)	2,735,882,799	2,667,066,127	2,696,988,534	2,598,123,112	2,578,867,238	3	-1	4	1	6
Serbia	4,599,381,693	4,541,896,554	3,763,508,152	3,675,106,957	3,384,002,953	1	21	2	9	36
Montenegro	607,406,795	579,224,513	592,478,383	587,508,832	574,365,631	5	-2	1	2	6
Macedonia	726,932,227	710,157,053	694,354,594	713,069,902	701,854,764	2	2	-3	2	4

Source: Budget papers publicly available on web pages of ministries of finance and governments

The consolidated data for BiH in Table 7 show that there were no large fluctuations in wage bill expenditures over the observed five-year period. Comparison of FBiH and RS shows that between 2010 and 2014 the wage bill expenditures increased more in percentage terms in FBiH than in RS (FBiH – 14% (with cantons); RS – 5%). BiH (state level) and BD saw a reduction in wage bill expenditures from 2010 to 2014 (BiH – 4%; BD – 15%). If BiH (consolidated) is compared to other countries in the region, it is evident that the 6% increase in wage bill expenditures is not high. This percentage is higher than in Macedonia (4%), the same as in Montenegro (6%), but much lower than in Serbia (36%). Serbia, huge leaps in wage bill expenditures are observed in some of the years, which is not the case in BiH (consolidated), Montenegro and Macedonia.

2. Wage bill expenditures as a share of GDP

Table 8 below shows wage bill expenditures as a share of GDP across countries, entities and years.

Table 8. Wage bill expenditures as a share of GDP

Countries and entities	2014 %	2013 %	2012 %	2011 %	2010 %
FBiH (with cantons)	8	8	8	7	7
RS	7	7	8	7	7
BiH (consolidated)	10	10	10	10	10
Serbia	8	7	7	6	6
Montenegro	10	9	10	9	9
Macedonia	5	5	5	5	5

Source: author's calculations based on: GDP – Central Bank of BiH; Agency for Statistics of BiH; Directorate for Economic Planning of BiH; Investment-Development Bank of RS; Republic Institute of Statistics (Serbia); National Bank of Serbia; Chamber of Commerce of Montenegro; Ministry of Finance of Montenegro; State Statistical Office (Macedonia); www.izvoznookno.si

The share of wage bill expenditures in GDP ranges from 5% in Macedonia throughout the five-year period to 10% in Bosnia and Herzegovina (all five years) and Montenegro (in 2012 and 2014). The share of wages in GDP has remained largely constant from year to year in all countries of the region.

3. Wage bill expenditures as a share of budget expenditure

Table 9 below shows wage bill expenditures as a share of budget expenditure. Two indicators are presented – one where expenditures do not include transfers and subsidies (as well as expenditures for financial assets and repayment of debts), and the other where subsidies and transfers are included (excluding expenditures for financial assets and repayment of debts).

Table 9. Wage bill expenditures as a share of budget expenditure

Countries and entities	2014		2013		2012		2011		2010	
	% (1)*	% (2)**	% (1)*	% (2)**	% (1)*	% (2)**	% (1)*	% (2)**	% (1)*	% (2)**
FBiH	54	14	45	12	50	13	54	13	46	11
FBiH (with cantons)	68	38	67	37	67	36	66	35	62	32
RS	78	43	79	43	86	48	84	46	82	44
BD	47	33	48	34	51	39	49	37	53	41
BiH (consolidated)	70	44	69	43	71	44	72	43	67	41
Serbia	50	25	53	25	61	25	59	24	61	25
Montenegro	50	42	54	45	54	46	52	43	46	39
Macedonia	34	18	36	18	33	18	36	20	36	20

**(1) – share of expenditure excluding transfers and subsidies (as well as expenditures for financial assets and repayment of debts)*

*** (2) – share of expenditure including transfers and subsidies (excluding expenditures for financial assets and repayment of debts)*

Wage bill expenditures as a share of budget expenditure excluding transfers and subsidies (as well as expenditures for financial assets and repayment of debts) range from 34% in Macedonia (2014) to as high as 78% in RS (2014). Throughout the observed five-year period Macedonia has had the lowest percentage, remaining at 36% in 2010, 2011 and 2013 and decreasing to 34% in 2014. In Montenegro, the share increased from 46% in 2010 to 50% in 2014, whereas in Serbia it decreased from 61% in 2010 to 50% in 2014. In BiH (consolidated) the share of wage bill expenditures in budget spending has remained at about 70% over the five-year period.

If transfers and subsidies are included in budget expenditure, the share of wage bill expenditure is reduced (compared with the results without transfers and subsidies). The lowest share is still found in Macedonia (between 18% and 20% in the five-year period), as well as in FBiH (without cantons; between 11% and 14% in the five-year period). BiH (consolidated) has a share somewhat bigger than 40%, similar to Montenegro, while Serbia's share is about 25%.

Thus, the Macedonian budget is development-oriented rather than administration-oriented. If wage bill expenditures are too high, governments have fewer funds for other expenditures, such as goods and services, maintenance, and capital expenditures. In reality, for example, this means that schools will not have the necessary equipment etc.

4. Expenditures for goods and services as a share of budget expenditure

The same methodology is used for this indicator as for Indicator 3. Table 10 below shows the share of expenditures for goods and services in the budget across countries and entities over the observed five-year period.

Table 10. Expenditures for goods and services as a share of budget expenditure

Countries and entities	2014		2013		2012		2011		2010	
	% (1)*	% (2)**	% (1)*	% (2)**	% (1)*	% (2)**	% (1)*	% (2)**	% (1)*	% (2)**
FBiH	16	5	17	6	14	4	18	6	22	7
FBiH (with cantons)	14	8	15	8	14	8	16	8	18	9
RS	12	7	13	7	12	7	14	7	13	7
BD	29	20	28	20	30	23	29	22	31	24
BiH (consolidated)	16	10	17	10	16	10	17	10	18	11
Serbia	18	9	17	8	13	5	14	6	14	5
Montenegro	16	14	17	14	21	18	24	20	27	23
Macedonia	27	14	27	14	25	14	26	15	26	15

**(1) – share of expenditure excluding transfers and subsidies (as well as expenditures for financial assets and repayment of debts)*

*** (2) – share of expenditure including transfers and subsidies (excluding expenditures for financial assets and repayment of debts)*

Table 10 shows that Macedonia has the highest share of expenditures for goods and services (budget without transfers and subsidies), varying between 25% and 27% over the observed five-year period, which is not much lower than the share of wage bill expenditures (between 33% and 36 %). Looking at other countries and taking year 2014 as an example, it is evident that there is a great difference between the share of wage bill expenditures share of expenditures for goods and services: BiH (consolidated; wage bill 70%, goods and services 16%), Serbia (wage bill 50%, goods and services 18%) and Montenegro (wage bill 50%, goods and services 16%).

5. Vertical pay compression

Table 11 below provides an overview of the ratio between highest and lowest salaries of civil servants (vertical pay compression), under applicable legislation in individual countries.

Table 11. Vertical pay compression

Countries and entities	Highest salary/lowest salary
RS	3.14
FBiH	1.76
BD	3.10
BiH	3.19
Sarajevo Canton	1.76
BiH (consolidated)	6.72 ¹⁹
Serbia	6.43
Montenegro	2.41
Macedonia	4.84

Source: author's calculations based on: salaries – laws on salaries of civil servants, with the exception of Macedonia, where salaries are regulated by the Law on Civil Servants

Table 11 shows that FBiH and Sarajevo Canton have the highest vertical pay compression ratio (1.76), while RS, BD and BiH have a compression ratio of about 3. A compression ratio of 3 means that the highest civil servant salary is three times higher than the lowest civil servant salary, e.g. if the lowest salary is KM 1,000, the highest is KM 3,000. Please note that not all cantons were taken into consideration, only the Sarajevo Canton was taken as an example. Serbia has a vertical compression ratio of 6.43; Macedonia 4.84; and Montenegro 2.42. The vertical compression ratio for BiH consolidated (all levels of government together) is 6.72. A compression ratio of 6.72 means that the highest salary a civil servant can have is about 7 times higher than the lowest civil servant salary. This means that, if the lowest civil servant salary is KM 700, the highest is KM 4.704. The reason why different administrative levels in BiH were included in the measuring of vertical pay compression is the fact that the entities, as well as the state and cantons, have broad powers. Thus, for example, ministries of justice exist at the state, entity and cantonal levels. The scope of work of civil servants at all administrative levels is similar and that is why different administrative levels were taken into account. So, there are civil servants who have similar levels of responsibility and perform similar jobs, but at the same time have different salaries.

6. Horizontal pay compression

This indicator will show examples of horizontal pay compression, i.e. differences in salaries for the same positions. In Serbia, Montenegro and Macedonia, there are no such examples as these countries have a single law that regulates the salaries of all civil servants. In BiH, each administrative level has its own law on salaries of civil servants. In RS, there are multiple laws regulating civil service salaries.

¹⁹ The highest salary is at the level of BiH, and the lowest is in RS.

Table 12 below shows two examples of horizontal pay compression in BiH, where the salary at the BiH level is shown in relation to the salaries at each sub-national level.

Table 12. Horizontal pay compression (BiH)

	RS (BiH salary/RS salary)	FBiH (BiH salary/FBiH salary)	BiH	Sarajevo Canton (BiH salary/SC ²⁰ salary)
Expert Associate	1.13	1.27	1.00	1.41
Secretary of the Prosecutor’s Office	1.82	1.59	1.00	1.76

Table 12 reads as follows: a civil servant occupying the position of an expert associate at the level of BiH has a salary 13% higher than that of a senior expert associate in RS (ratio 1.13), 27% higher than that of an expert associate in FBiH (ratio 1.27), and 41% higher than that of an expert associate in the Sarajevo Canton (ratio 1.41).

In RS there are three laws governing the salaries of civil servants: Law on Wages and Salaries of Employees in the Public Administration of the Republic of Srpska, Law on Wages and Salaries of Employees in the Judicial Institutions of the Republic of Srpska, Law on Wages and Salaries of Employees in the Ministry of Interior of the Republic of Srpska. Not all civil servants in RS are recruited through the Civil Service Agency of RS. For example, secretaries of the prosecutors’ offices in RS are considered civil servants, although they are not elected by the Civil Service Agency of RS.

10. Conclusion

This study/report aims to examine the basic aspects and quantitative indicators of the state of public finance in BiH, and compare some of them with countries such as Serbia, Montenegro and Macedonia.

Research shows that significant resources and efforts, by both European and US donors, were invested and continue to be invested in reforming the fiscal sector in BiH. Significant progress has been made in the areas of taxation, budget management, reporting, projections and other areas. Although improvements have been made in the fiscal sector, there is still room for further reforms, and also a lot of work is yet to be done for the effects of the implemented reforms to become visible.

Although considerable efforts have already been made to build capacity in key institutions dealing with public finance, a lot of work and effort is still needed to make projections of

²⁰ SC stands for Sarajevo Canton.

revenues and expenditures, as well as simulations of the effects of the new regulations, more precise. For example, lack of precision is evident in the section discussing the differences between the approved and executed budget.

When the budget, which consists of eight elements (wage bill, goods and services, transfers, capital expenditures and grants, interests, reserves, financial assets, debts), is viewed in relation to GDP, the result obtained shows the share of expenditures and expenses in GDP in BiH (consolidated for 4 levels including cantons, excluding municipalities and extra-budgetary funds) is around 30%, which is not higher than in other countries in the region (Montenegro and Macedonia, with the exception of Serbia, where the share is much higher). The same is true when expenditures for financial assets and repayment of debts are excluded from total expenditures and expenses (except that in this case Serbia is much closer to other countries in the region).

What remains a problem, however, is the structure of the budget, where if total expenditures and expenses (all 8 elements) are observed, about a third of the entire budget of BiH (consolidated) goes on the wage bill. If two elements are excluded (financial assets and repayment of debts), the situation is even worse, with about half of the budget going on the wage bill. Such budgets are more administration-oriented and less development-oriented. Macedonia, on the other hand, has a budget that is more development-oriented.

In terms of functional budget classification, it is evident that around 30% of expenditures and expenses (BiH, FBiH without cantons, RS, BD) go on general public services.

The results show that there were no large fluctuations in wage bill expenditures over the observed five-year period in BiH (consolidated; 6%, 2010-2014), unlike Serbia (36%).

The share of wage bill expenditures in GDP is constant from year to year across the region, with percentages ranging between 5% in Macedonia to 10% to Montenegro and Bosnia and Herzegovina (consolidated).

The indicator that measures the share of wage bill expenditures in budget spending (excluding transfers and subsidies, as well as expenditures for financial assets and repayment of debts) points to a high share of wage bill expenditures and a low share of expenditures for goods and services. The lowest share of wage bill expenditures is found in Macedonia (34%), where at the same time expenditure for goods and services is not much lower (27%). In other countries, the percentages are as follows: BiH (wage bill 70%, goods and services 16%), Serbia (wage bill 50%, goods and services 18%) and Montenegro (wage bill 50%, goods and services 16%).

The indicator that measures vertical pay compression shows that FBiH and SC have a high compression ratio (1.76), while RS, BD and BiH have a compression ratio of about 3 (ratio

between the highest and the lowest salary in civil service). In Serbia, this ratio stands at 6.43, and in BiH (consolidated) at 6.72. The reason why different administrative levels in BiH were included in the measuring of vertical pay compression is the fact that the entities, as well as the state and cantons, have broad powers. The scope of work of civil servants at all administrative levels is similar and that is why different administrative levels were taken into account. So, there are civil servants who have similar levels of responsibility and perform similar jobs, but at the same time have different salaries.

Horizontal pay compression is not observed in civil service in Serbia, Montenegro and Macedonia, while in BiH it is found to exist between different administrative levels.

Research shows that significant progress has been made in the harmonisation of regulations relating to the preparation and drafting of the budget (budget calendar). Budget Framework Papers, whose preparation is stipulated under budget laws at all administrative levels, include: (1) macroeconomic projections (economic development forecast, social sector development forecast, forecast of macroeconomic indicators, fiscal framework), (2) projections of budget funds and expenditures for the next three years.

Also, research has shown that the budget laws in FBiH and RS explicitly specify the steps to be followed when making or amending regulations that result in financial impacts on the budget. Such a provision is also contained in the Budget Law of Brčko District, but without explicit detail. The Law on the Financing of Institutions of BiH does not contain such a provision, but only provides that the Ministry of Finance and Treasury may balance the budget by finding new revenues or reducing projected expenditures

The budget law in RS provides that consultation with budget users is left to the discretion of the Ministry of Finance. The budget law in BD does not contain such a provision. However, only the Law on Budget Systems of RS defines the consultation process between the Ministry of Finance and the Assembly.

BFPs for FBiH and RS for 2015-2017 are made available on the websites of ministries of finance, which is not the case at the BiH level (according to available information, it has not yet been adopted, which is a violation of the budget process) and BD. When it comes to transparency, the budgets for individual years at the level of BiH are not available on the website of the Ministry of Finance without the access password for the Official Gazette of BiH.

The introduction of Budget Management Information System and Treasury System provides a technical basis for increasing the transparency and control of expenditure, with better inclusion of budget users and Parliament/Assembly in budget preparation, and with better monitoring of budget execution and better reporting. Monitoring should be strengthened in the coming period to ensure that things go in the expected direction.

11. Recommendations for BiH

Although the fiscal sector in Bosnia and Herzegovina has undergone significant reform, there is still room for further improvement. Also, it is necessary to invest more effort to make the results of the reforms visible.

Analysis shows that it is necessary to further increase human resources in key institutions dealing with public finance, especially in the areas of forecasting revenues and expenditures and simulating the effects of introducing new or amending existing legislation. This is necessary in order to increase the accuracy of projections.

With regard to functional budget classification, further work is needed with a view to harmonising different statistical classifications between different administrative levels.

The Budget Law of BD and the Law on the Financing of Institutions of BiH should make specific provisions defining the steps to be followed when making or amending regulations that result in financial impacts on the budget.

In the area of transparency, efforts should be made to make all relevant documents relating to the budgets available to the public and budget users. It is necessary to allow access to budgets through websites of ministries of finance at all administrative levels, including the cantonal budgets for at least five previous years. It is necessary to increase the transparency of budget execution reports, as well as budget framework papers at some administrative levels. BiH level should adopt the budget execution report for the previous year and BFP more promptly.

In the area of reporting significant progress has been made, but further efforts are still needed to ensure consistency of reports at all levels in order to facilitate comparability of fiscal data.

It is necessary to continue to work on improving communication between ministries of finance and budget users, as well as between ministries of finance and Parliament/Assembly. This improvement should be achieved through improved legislation, as well as introduction of BMIS. Further work is needed to ensure that BMIS is deployed in cantons and municipalities. This also applies to the Treasury System, in places where it currently does not exist.

As shown by the analysis, although this has been a known fact for quite some while, BiH has very high wage bill expenditures, which include: gross salaries, gross remunerations and other employee benefit plans, and other contributions paid by the employer. These expenditures as a share of budget expenditure of BiH (consolidated) are the highest in the region. There are two reasons for this: excessive administration and high wages of certain groups of officials.

Such wages should be reduced, and complete administration should be restructured. Also, the inspectorate should increase its efforts to combat the black economy, and thus increase budget revenues and create room for more capital investment. It is important to note, although some projects are already dealing with this, that it is necessary to review and reform of social transfers.

It was also observed that BiH (consolidated) has a high difference between the highest and the lowest salary in civil service (low vertical pay compression). This difference should be neither too high nor too low. If it is too high, it creates great inequality in income. Conversely, if it is too low, people in positions of responsibility are not adequately paid. In the high-income OECD countries, the highest salaries are two to four times higher than the lowest ones (individual levels fall within this range, but not in consolidated terms, although officials have a similar scope of work) (Mills et al, no date). High salaries in the public sector make the public sector more attractive for employment than the private sector, which should not be the case. The relatively high range between the salaries of civil servants in BiH can be reduced through the introduction of more income taxation rates, which would lead to a reduction in inequality and redistribution of income from those who have more to those who have less. Progressive taxation rates can give the desired results if the salaries defined in the laws on salaries of civil servants are expressed in gross rather than net amounts. FBiH solved this through the Law on Personal Income Tax, which defines how net salary is converted into gross salary to serve as a starting basis for calculating contributions and taxes. In RS the situation is such that no matter what the rate of income tax and how many rates there are, net salary does not change. The only thing that changes is employer's costs, and there is no redistribution of income and reduction of inequalities. This should be taken into consideration when making amendments to the Law on Wages and Salaries of Employees in the Public Administration of RS.

Currently, in RS there are several laws on salaries of civil servants, regulating wages and salaries in different institutions. The possibility of integrating the existing number of laws into a single law on salaries of civil servants of RS should be considered.

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