

EITI AS AN INSTRUMENT OF FISCAL TRANSPARENCY AND ACCOUNTABILITY: A CASE STUDY OF TWO FCV COUNTRIES

Prepared by Emmanuel F. Cuvillier and Sridar Padmanabhan Kannan, Governance Global Practice

Transparency and accountability in sector governance are basic and essential requirements to leverage the extractives (oil, gas, and mining) sector as an engine of economic growth in fragility, conflict, and violence (FCV) affected settings. Enabling them involves two vital steps. Transparency requires obtaining or publishing relevant and actionable data about sector governance. Accountability involves having the data to support responsible, efficient, and informed sector governance.

Although several mechanisms exist to facilitate transparent data disclosures, the Extractive Industries Transparency Initiative (EITI) is the preeminent global standard to promote the open and accountable management of oil, gas, and mineral resources. This *Governance Note* presents a case study about how data disclosed through EITI has been effectively leveraged to support more transparent and accountable fiscal governance in two FCV countries — Afghanistan and Iraq.

INTRODUCTION

EITI seeks to strengthen extractives sector governance and promote understanding of natural resource management by disclosing vital sector data. It requires periodic public disclosures of information about a country's extractive industries, including legal and regulatory information; license and contract details; data on beneficial owners of operations; production figures; and economic and social contributions of companies. Also required is the disclosure of financial data related to extractive industries, such as reconciled figures of company payments and government revenues; revenue allocations and transfers; data on sector exports; and quantitative information about the sector's contribution to the economy.

Fiscal transparency is a vital requirement for effective fiscal policy making. Budgets, including their underlying fiscal forecasts, must provide a clear statement of the government's budgetary objectives and policy intentions. Credible budgets also require comprehensive, timely, and reliable data about the evolution of public finances, which enable sound financial projections (see box 1).

Box 1. What Kinds of Data Benefit Fiscal Policy Making?

Fiscal transparency ideally involves ensuring published fiscal reports:

- Cover a wider range of public sector institutions;
- Capture a broad range of direct and contingent assets and liabilities;
- Take a rigorous approach to fiscal forecasting and risk analysis; and
- Present actual and forecast fiscal data on a consistent basis.

Fiscal accountability concerns the government and its civil servants being answerable to the country's citizens and public institutions. Accountability is ensured when actionable data disclosed through fiscal transparency measures are used effectively by public oversight institutions for either sanction- or nonsanction-based approaches. Enforcement is usually vested with a country's legislative body, such as the National Assembly of Afghanistan, Iraqi Council of Representatives, and the Parliament of the Kurdistan Region of Iraq.

Analyses of data disclosed through EITI, especially in countries dependent on extractive industries, often enable the identification and delivery of key measures to strengthen fiscal accountability.

WHY EITI?

Governed well, the extractives industries sector can be an engine of economic growth and sustainable development. When natural resource management is reinforced by appropriate systems, informed and transparent decision making, and efficient institutions, the sector can significantly boost medium-term economic growth, foreign direct investment, government revenues, and inclusive benefit sharing. This is especially true in resource-dependent economies or small-size economies with significant resource potential. The sector can also be leveraged to enable economic diversification over the long term.

When mismanaged, the sector may become a fertile

ground for rent-seeking and corruption. The adverse environmental, social, economic, and political consequences are well documented in literature describing the “resource curse” paradox. Specifically, many countries with an abundance of extractive resources often have lower economic growth, weaker public institutions, and worse development outcomes than countries not similarly endowed.

The nature of this sector has significant implications for FCV countries. It can either help boost peace-building efforts or fuel conflicts. Either way, it is of paramount importance that efficient, transparent, and accountable governance of the sector be ensured.

The Country Cases: Afghanistan and Iraq

These two FCV countries offer contrasting scenarios of the sector’s potential and role in their respective national contexts.

Afghanistan. An International Development Association country with a small-size economy, Afghanistan largely depends on external aid funding. The development of extractive industries is at a nascent stage. In 2016, the sector accounted for about 4 percent of government revenues and 5.5 percent of exports, mainly led by coal production and sales, according to the latest EITI report.¹ Significant development potential in metals, such as copper and lithium, points to a greater relevance of the sector in the context of a global low-carbon future. A large-scale copper mine, under negotiation, also can be a turning point.

The most useful contribution of the sector lies in its potential to boost government revenues in the medium-term through greenfield projects, thereby reducing reliance on foreign aid. Afghanistan continues to rely on grants to finance 75 percent of total public expenditures. A clear case exists for Afghanistan to sustainably, transparently, and accountably harness its resources for national development. The medium-term nature of the sector’s returns also lends itself to potentially contributing to peace-building strategies.

Iraq. An International Bank for Reconstruction and Development country, Iraq depends on its oil and gas sector economically. In 2016, it accounted for 99 percent of export values, 96 percent of government revenues, and almost 30 percent of gross domestic product at a time when the average oil prices were the lowest in more than a decade. These figures remain about the same over the past decade, revealing the extent to which the national economy is exposed to the volatility of the commodity price cycle and contributing to a weakening of fiscal resilience.

The sector’s ideal contribution would be toward increasing the country’s revenues, economic growth, and investment;

anchoring infrastructural development; and facilitating inclusive revenue sharing. At the same time, measures would be needed to protect the economy from external shocks associated with the sector.

Both Afghanistan and Iraq are EITI implementing countries. While providing technical assistance to them to address corrective actions for improved implementation, two important linkages were observed: (i) at times, administrative reforms were required to facilitate effective data collection, warehousing, and disclosures; and (ii) the data collected could help improve administrative and developmental outcomes.

AFGHANISTAN: DATA SYSTEMATIZATION FOR DEVELOPMENT

Efforts in Afghanistan seek to enable systematized data disclosures and simplify data collection efforts, given security concerns that often restrict movement and coordination. In this context, governance enhancements are being supported through new draft mining regulations and digitized systems.

New Draft Mining Regulations

This effort seeks to empower the use of data for improved governance and fiscal accountability.² Using an innovative approach, technical support was provided to embed and regularize data disclosures, required under the EITI standard, into the draft mining regulations — a vital step for good sector governance.

Box 2. Regularizing Data Disclosures Improves Transparency and Accountability

- Greater availability of sector data adds credibility to fiscal transparency and enables fiscal accountability.
- Access to relevant, disaggregated data enhances the quality of information for government use. Consolidation and cross-verification of data sets are also possible within and between departments.
- Data timeliness is improved significantly through mandatory time-bound data reporting, which enables more efficient and informed administrative decisions.
- Finally, systematized data collection and disclosures are facilitated through required maintenance of a publicly accessible digital mining cadaster, mineral license register, and register of beneficial owners.

Digitized Systems

The Ministry of Mines and Petroleum (MMP) uses digitized systems to increase fiscal transparency and accountability by collecting and disclosing vital data (see box 3). Its Mineral Cadaster Administration System (MCAS) and Non-Tax

¹ For more information and to access reports, see EITI’s website at <https://eiti.org/>.

² The regulations are pending Cabinet approval.

Revenue System (NTRS) capture license and nontax revenue information in a real-time, disaggregated, and automated manner. Drawing from these internal systems, an online transparency portal³ automatically discloses all federal licenses, license coordinates, dates of issue, beneficial ownership details, and disaggregated nontax revenues.

Box 3. How Digitized Systems Help Improve Fiscal Transparency and Accountability in Afghanistan

- Nontax mineral revenue administration was enhanced at the Ministry of Mines and Petroleum (MMP) through readily available and accessible information on revenue collection and mineral production.
- Monitoring of mining operations was enhanced by empowering the MMP with readily available data on license coordinates and attendant details.
- Investor and civil society organization confidence in sector governance are expected to increase following transparent data disclosures in formats that enable further end-user verification and analysis.
- Crucial mining tax laws were enabled. Addressing data gaps in the MMP's digitized systems enabled the ring-fencing of corporate income taxes on a per-mining license basis, as required by law. The move, the implementation of which commenced in 2019, is expected to increase tax revenues.

To adhere to the treatment of confidential data as required under Afghan laws, these data are further automatically aggregated above confidentiality thresholds prior to disclosure through the transparency portal. Crucial data are also manually uploaded on the MMP's website, such as data regarding mineral production and provincial licenses and contracts.

IRAQ: BASELINE DATA FOR BROADER REFORMS

Efforts are being made to facilitate reliable data disclosures in the oil and gas sector. They would enable greater stakeholder engagement and provide a baseline for analyses and sector reforms by the government and development organizations. Governance enhancements are being supported with regard to the legal framework, citizen engagement and conflict mitigation, and public financial management (PFM) systems.

Legal Framework

Greater clarity about the legal framework has been facilitated. With no unified law governing the oil and gas sector, it is subject to multiple regulations and frameworks. The most recent EITI report offers clarity to stakeholders about vital aspects of sector governance, such as data

regarding licensing, revenue sharing and allocation mechanisms, revenues collected, the roles and functions of state-owned enterprises (SOEs), and the relationship of SOEs with government ministries (see box 3). Most importantly, coordinates of oil and gas operations in Iraq have been publicly disclosed for the first time. The EITI quality assurance mechanisms add veracity to the data disclosed, now available in consolidated form for stakeholder use.

Box 4. Fiscal Transparency in State-Owned Enterprises: The Next Big Target in Iraq

- State-owned enterprises (SOEs) are vital actors in the oil and gas sector. All sales and distribution fall under their purview. They are also the major players in oil and gas extraction.
- Oil and gas SOEs retain a significant portion of their earnings, which amounts to a very large portion of government revenues. In 2016, SOEs transferred 45 percent of their net profits to the Ministry of Finance, while retaining 33 percent for themselves and the Ministry of Oil.
- Enabling fiscal transparency and accountability in SOEs is crucial for broader good governance. Ongoing linkages are being explored to enable the publication of audited financial statements using International Financial Reporting Standards.

Citizen Engagement and Conflict Mitigation

Citizen engagement has been enhanced, and conflict mitigation has been supported. Given the sector's economic importance, the role of data disclosed through EITI in enhancing citizen confidence in sector governance cannot be understated. During violent protests in April 2018 over oil revenue distribution, data disclosed through EITI served as a ready source of information for public engagement. Data from EITI reports were publicized through local radio stations. They served as proof to address popular misconceptions, especially regarding employment levels of Iraqis in the oil and gas sector. The annual Citizen's Budget of Iraq for the year 2018, which was publicly disseminated, included a chapter that presented the main findings of Iraq's most recent EITI report. A similar EITI based analysis has also been performed for this budget for the year 2019, the adoption and publication of which is currently being considered by the government of Iraq. While the citizen's budget shares details and plans on a forward-looking basis, Iraq's EITI reports provide an evidence-based look at the sector's past performance. This interlinkage between budget projections and past performance in Iraq's most vital sector will further inform citizens about governance performance.

³ For more information, see <https://afghanistan.revenue.gov.af/dashboard> and <https://momp.gov.af> (transparency tab).

PFM Systems

Ongoing enhancements to PFM systems are being supported. The Ministry of Finance is moving from paper-based financial recording to a digitized PFM system.⁴ To complement this effort, a PFM transparency subportal is being developed within the ministry to publicly display nonconfidential financial data in an automated way. Given the oil and gas sector accounts for the greatest proportion of Iraq's financial data, EITI data disclosure standards will be embedded in the transparency subportal.

CHALLENGES FACING FCV COUNTRIES

Based on activities undertaken in Afghanistan and Iraq to use EITI and data systems for improved fiscal transparency and accountability, several challenges are identified as common to the FCV context in regard to government reforms, scope of data use, automated data systems, and software compatibility.

Government Reforms

Sequencing of improved data use in relation to broader government reforms is a challenge. Legislative and regulatory reforms are often required before the creation of data systems, collection, and reporting. However, sometimes data improvements are needed to inform meaningful legislative and regulatory reforms. The sequencing of reforms depends on the level of baseline data available, which is different for each country. Identifying the right sequence is vital toward ensuring meaningful output delivery.

Scope of Data

The scope of data use is influenced by wider governance reforms. Efforts to improve data collection, reporting, and systematization are best accompanied by wider administrative and institutional reforms. Where reforms are ongoing, the leveraging of data, including through EITI, can add tremendous value. Data can be used to accelerate reforms, improve administrative efficiency, and inform governance decisions. However, in the absence of reforms, only limited improvements can be made. The value added of the systems would be limited, and data gaps would likely remain.

Automated Data Systems

Large initial investments in the short term are required for creating automated data systems. This makes sense only where there is government buy-in or ownership for sector development or when overall fiscal accountability exists. Also, institutional capacity would need to be built for operating these systems and for using the data to make better informed governance decisions. In this context, policy makers must

perceive the sector as a strategic reform priority. In the longer term, these investments will significantly reduce the costs of data reporting initiatives, such as EITI, and enable enhanced revenue collection and management.

Software Compatibility

Software compatibility is a vital factor when designing interlinked data systems. The viability of linkages created through information technology is as important as the data disclosed. Sometimes, systems cannot be interlinked due to software incompatibility and lack of interoperability. Feasibility studies will be required to compare the benefits of data integration and automation in relation to the expected costs of interlinking various data systems. As much as possible, it is also important to ensure the use of open data software to empower the host ministry to undertake necessary changes.

FUTURE FOCUS AREAS

When it comes to using EITI or data systems for improved fiscal transparency and accountability, the steps taking precedence for the future in both countries are closely linked to their respective priorities.

In Afghanistan, the priority is to boost investor confidence, increase government revenues, and counter illicit revenue flows. It will be crucial to link the internal systems of the country's tax administration, customs and export administration system, and MMP systems (MCAS and NTRS) to compare extractive production with relevant data, such as exports, tax revenues, and nontax revenues.

In Iraq, the priority is to expand the umbrella of fiscal transparency and accountability to critical sectors and other areas of government intervention, which account for significant revenue flows. It will be crucial to support financial reporting by major oil and gas SOEs using good practice standards comparable to the International Financial Reporting Standards and facilitating their audit by Iraq's Federal Board of Supreme Audit.

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For more information, contact: govglearns@worldbank.org.

⁴ For more information, see the World Bank's website at <http://documents.worldbank.org/curated/en/home> for "Iraq — Modernization of Public Financial Management Systems" (P151357) and "Strengthening Public Financial Management Oversight and Accountability Institutions in Iraq" (P170704).