



SIGMA

A joint initiative of the OECD and the EU, principally financed by the EU



Creating Change Together

PUBLIC ADMINISTRATION REFORM ASSESSMENT OF TURKEY

APRIL 2014

Authorised for publication by Karen Hill, Head of the SIGMA Programme

2 Rue André Pascal
75775 Paris Cedex 16
France

<mailto:sigmaweb@oecd.org>

Tel: +33 (0) 1 45 24 82 00

Fax: +33 (0) 1 45 24 13 05

www.sigmaweb.org

This assessment report has been produced with the financial assistance of the European Union. It should not be reported as representing the official views of the EU, the OECD or its member countries, or of beneficiaries participating in the SIGMA Programme. The opinions expressed and arguments employed are those of the author(s).

Assessment reports describe preliminary results or research in progress by the author(s) and are published to stimulate discussion on a broad range of issues on which the EU and the OECD work. Comments on Working Papers are welcomed, and may be sent to SIGMA-OECD, 2 rue André-Pascal, 75775 Paris Cedex 16, France.

This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.

ASSESSMENT OVERVIEW AND RATIONALE

Turkey is in the process of Stabilisation and Association Agreement negotiations with the European Union. In the period under review Turkey has made progress, as demonstrated by the commencement of the Visa Liberalisation Dialogue and the signing of the Readmission Agreement and the Memorandum of Understanding on 16 December 2013. Negotiations were also opened on 5 November 2013 on Chapter 22, Regulatory Policy and Co-ordination of Structural Instruments.

Following discussions with the European Commission (EC), SIGMA gave priority in its 2014 assessment of Turkey to areas of public administration reform (PAR) and in particular those areas where actual reform was being implemented or planned. This report covers the period from April 2013 to March 2014.

Each assessment area is presented in a separate thematic report, which includes a brief description of the state of play and recent developments. This overall assessment is followed by a more detailed analysis with conclusions.

SIGMA's 2014 assessment of Turkey focused on:

- [PUBLIC FINANCE MANAGEMENT](#) – This assessment concentrated on progress made in the implementation of key reforms in the area of [Public Expenditure Management System](#), such as embedding a system of strategic management and performance budgeting and strengthening the interrelationship between strategic planning and financial elements of the budgetary process.
- [PUBLIC PROCUREMENT](#) – This assessment focused on the regulatory framework for public-private partnerships and the concessions regime and on the regulations recently introduced on the use of offsets.

SIGMA, working in co-ordination with the EC's Directorate-General for Enlargement (DG ELARG), has developed a draft set of principles of public administration, designed to define key requirements for good public governance and to serve as basis for measuring progress over the years. Some country assessments in 2014 were used to pilot these draft principles. The assessment of Turkey has not followed this approach in all aspects, but it has used the framework as a basis for the analysis.

The principles of public administration are due to be released in November 2014.

PUBLIC FINANCE MANAGEMENT

TURKEY
APRIL 2014

1. State of play and main developments since last assessment

1.1. State of play

The most recent forecasts for Turkey show a General Government Deficit of 1.6% of GDP in 2013, 2.9% in 2014 and 2.5% in 2015, and a General Government Debt ratio of 36% of GDP in 2013, 36.7% in 2014 and 36.2% in 2015¹. However, there are downside risks to these projections² owing to the recent depreciation of the lira and also the interest rate increase in early 2014, which is expected to dampen economic activity during 2014 and into 2015.

The main elements of a good system of strategic management and performance budgeting exist, but there is still a gap between strategic planning and the financial elements of the budgetary process which weakens the implementation of Government policy³.

The Ministries of Finance and Development and the Under-secretariat of Treasury are responsible for different parts of the budget process and broader fiscal policy. For example, line ministries negotiate current expenditure allocations with the MoF and capital investment allocations with the MoD. While strong co-ordination for macroeconomic management has been established between these ministries⁴, the difference in responsibilities makes it more difficult to decide on trade-offs between current and capital allocations, as well as prioritising fiscal policies.

Expenditure from the own resources of public institutions, the “revolving funds”, has increased steadily over the years and now accounts for over 6% of General Government Expenditure. The funds present a risk to the Government’s planned fiscal targets since they are outside the budget process and the direct control of the MoF.

1.2. Main developments since last assessment⁵

Since the last assessment, the main focus of the administration has been on strengthening reforms previously introduced to establish modern budgeting procedures.

The most important development has been the implementation in January 2014 of a database that enables the MoF to monitor the transactions of revolving funds.

Four International Public Sector Accounting Standards have been transposed into national regulations, with a further two to be transposed later this year.

¹ The most recent debt forecasts are by the EU Commission in its Winter 2013 European Economic Forecast of February 2014.

² http://ec.europa.eu/economy_finance/eu/forecasts/2014_winter/cc_turkey_en.pdf.

³ See Joint EU-Turkey Gap Assessment Report at <http://stratejikyonetisim.org/en/resources/>.

⁴ The High Planning Council and the Economy Coordination Board, chaired by the Prime Minister and the Deputy Prime Minister for Economic and Financial Affairs respectively, also ensure inter-agency coordination and harmonization of the policy framework.

⁵ March 2012.

PUBLIC EXPENDITURE MANAGEMENT SYSTEM

2. Analysis

Multi-Annual Financial Framework

1: The Government approves and publishes a Medium-Term Budgetary Framework (MTBF) on a general government budget basis, which covers a minimum time horizon of three years.

The Ministry of Development (MoD) publishes the annual Medium-Term Programme (MTP) that sets out the main macroeconomic and fiscal policies and forecasts over the next three years. The MTP includes three-year expenditure and revenue forecasts for central and general government⁶.

The Ministry of Finance (MoF) produces the three-year Medium-Term Fiscal Plan (MTFP), which includes deficit and borrowing targets, total revenue and expenditure estimates, and ceilings for public administration bodies in line with the MTP. The Ministry also publishes “ceilings of appropriation proposals” for the general government administrations as an annex to the MTFP⁷. The multi-annual aggregate expenditure ceilings are politically binding insofar as they are approved by the Government, although bids from individual organisations often exceed indicated ceilings⁸.

Neither the MTP nor the MTFP include a formal fiscal sensitivity assessment. However, the Government previously has been willing to take corrective action when necessary. In September 2012, the Special Consumption Tax (SCT) was raised on several items to avoid breaching budget targets⁹.

The MTP 2014-2016 projected strong growth in real GDP over the period, which was built on strong domestic demand. These projections are higher than the most recent EU Commission and IMF forecasts for Turkey, as shown in Figure 1 below¹⁰. The lower growth profile of the EU forecasts reflects the recent depreciation of the Turkish lira and the monetary tightening which occurred after the MTP and IMF forecasts were published.

⁶ Central government is defined as those institutions set out in Charts 1 to 3 of the PFMC Law. General government includes local government, certain extra-budgetary funds and revolving funds.

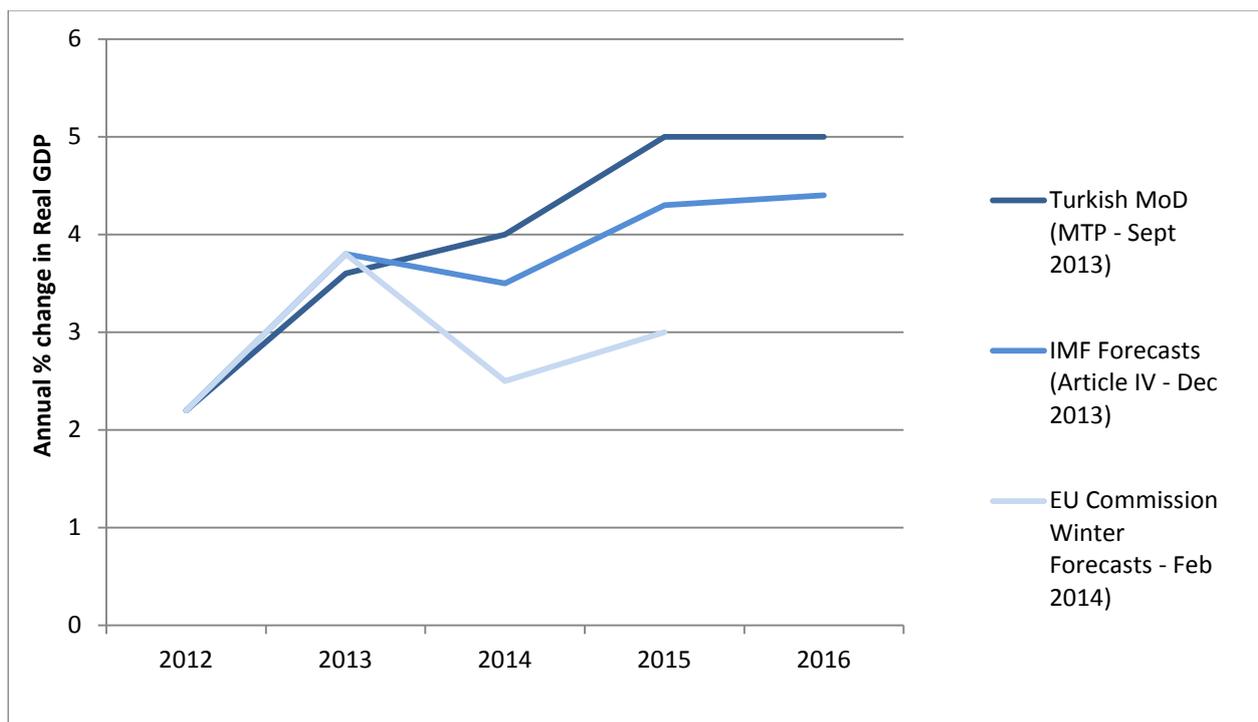
⁷ The relevant institutions are listed in Charts (I) and (II) annexed to the PFMC Law.

⁸ See page 66 of Joint EU-Turkey Gap Assessment Report at <http://stratejikyonetisim.org/en/resources/>.

⁹ <http://www.reuters.com/article/2012/10/16/turkey-budget-idUSL5E8LG63L20121016>.

¹⁰ <http://www.mod.gov.tr/Lists/RecentPublications/Attachments/30/Medium%20Term%20Programme%202014-2016.pdf>,
http://ec.europa.eu/economy_finance/publications/european_economy/2013/pdf/ee1_en.pdf,
<http://www.imf.org/external/pubs/ft/scr/2013/cr13363.pdf>.

Figure 1. Comparison of GDP growth forecasts for 2014-2016



Sources:

<http://www.mod.gov.tr/Lists/RecentPublications/Attachments/30/Medium%20Term%20Programme%202014-2016.pdf>

http://ec.europa.eu/economy_finance/publications/european_economy/2013/pdf/ee1_en.pdf

<http://www.imf.org/external/pubs/ft/scr/2013/cr13363.pdf>

A comparison of central government revenue projections in the MTP 2012-2014 against actual receipts for 2012 and 2013, and the latest forecast for 2014 shows the outturn to be 0.8% higher in 2012, 7.7% higher in 2013 and 3.3% higher in 2014. However, while the outturns include the impact of the 2012 in-year tax increases, there is no evidence to suggest that there is a significant problem with the forecasting methodology.

A similar comparison of central government expenditure forecasts in the MTP 2012-2014 shows actual expenditure exceeding target by 3.1% in 2012, 6.7% in 2013 and 6.8% in 2014 (assuming that the latest forecast will be equal to outturn for 2014). Extending this analysis to general government, deviations from target increase to 3.4% in 2012, 9.7% in 2013 and 9.1% in 2014. Given this tendency to deviate from target, it is notable that the IMF advises in its 2013 Article IV Report that a tighter fiscal stance be pursued, with expenditure being reined in and any additional revenues going to debt reduction.

The deficit and debt paths implied by these revenue and expenditure forecasts are also set out in the MTP. The Regulating Public Finance and Debt Management (RPFDM) Law provides that the Debt Risk Committee (DRC) determines the general strategies for managing public assets and liabilities. The MTP 2014-2016 states that debt management policies will continue to be based on strategic benchmarking¹¹.

Projects funded through Instruments for Pre-Accession Assistance (IPA) are co-ordinated in a separate process to the budget. This process is co-ordinated by the National Financial Assistance Directorate of the Ministry of EU Affairs and involves the Ministries of Finance and Development. The Ministry of the Economy and the Under-secretariat of Treasury are also involved in the process, with line ministries becoming involved for their own projects. The only link with the budgetary process is where a project is to be co-financed by a public institution, in which case the co-funded element is provided for within the ceiling.

¹¹ The strategic benchmarks for 2013 are set out in the *Public Debt Management Report 2013*, published by the Under-secretariat of Treasury.

There is no independent fiscal council to comment on fiscal policy and monitor actual fiscal performance.

The MTP and the MTFP clearly set out three-year projections for central and general government and the assumptions on which they are based. However, IPA funded projects are not included in the projections. Although there is no formal fiscal sensitivity assessment, the Government has a record of taking corrective action if necessary. The absence of an independent external monitoring institution leaves a gap in fiscal policy oversight.

2: The forecasts that each public sector organisation submits to the MoF for compiling the overall MTBF are linked to a strategic plan for the same medium-term timeframe.

All general government institutions are required to publish five-year strategic plans based on macro-economic and fiscal projections prepared by the MoD¹². Each year, they also produce one-year performance programmes, which present annual policies, expected results and resource allocation, as well as annual activity reports, which include information on performance and administration in addition to some financial information, though not about deviations from budget targets¹³. These reports are prepared by Strategic Development Units (SDUs) within the institutions. The SDUs are primarily responsible for strategic planning and the performance budgeting process in co-operation with the line units.

While the strategic objectives are referenced in the annual budgetary documentation, the overarching requirement for the line ministries is to adhere to the budgetary allocations. There is inconsistency between the presentation of the budget and performance objectives. Although the MoF is “authorised to define the procedures and principles on the compatibility of administration budgets with the performance indicators stated in the strategic plans”¹⁴, a 2013 Gap Assessment Report found that the introduction of these strategic management elements had yet to have a major impact on policy decision making. It also found that there was range of systemic, technical and institutional problems in relation to linkages between strategic planning/management and performance budgeting¹⁵.

There is a lack of understanding of the process at the level of the line units. The Ministries of Development and Finance, which are driving this performance budgeting initiative, have the capacity to fully implement a more strategic perspective. However, changing the traditional culture within public institutions is proving difficult. Finally, the annual performance plans are monitored by the MoF, but there is no follow-up action taken regarding institutions deviating from previously set performance targets¹⁶.

Any new investment proposal of more than TRY 5 million requires a feasibility study to be undertaken. While this study should include cost benefit analysis and other relevant types of assessment, the quality of these studies is mixed and SIGMA interviews indicated that at line ministry level, there is some inconsistency between institutions as to whether the SDU or the line unit proposing the project takes the lead in conducting the review. The MoD review investment projects regarding both the financial and economic aspects of the project.

The public finance management and control (PFMC) Law provides for a linkage between strategic planning, operational performance and annual resource allocation and much work has been done to develop this. However, at this relatively early stage, the linkages are weak. The divide between the initial setting of strategic plans and the annual monitoring of performance is an impediment to an effective process. As in many other countries, implementing the necessary cultural changes that give effect to this process is proving difficult. The appraisal process for large scale investment projects is not robust.

¹² Article 7(b) of the PFMC Law.

¹³ Article 41 of the PFMC Law.

¹⁴ Article 9 of the PFMC Law.

¹⁵ This Gap Assessment Report is available at: <http://stratejikyonetisim.org/en/resources/>.

¹⁶ This issue was highlighted during SIGMA interviews and is also mentioned in the Gap Assessment Report.

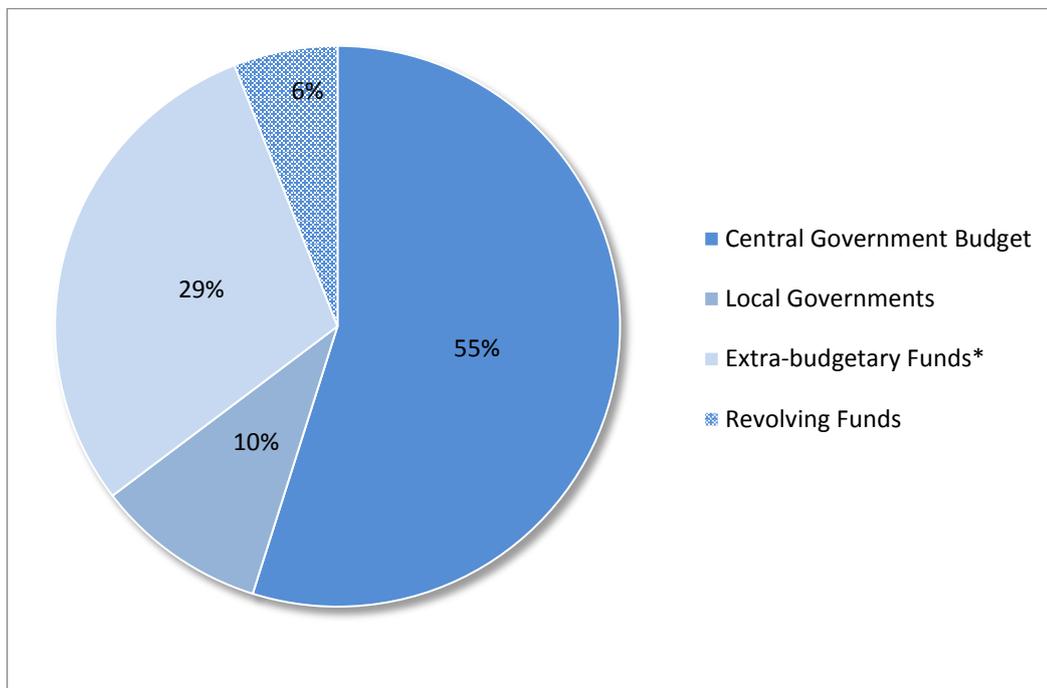
Annual Budget Process

3: The Budget process is based on transparent legal provisions established in the Constitution, an organic budget law and/or related laws.

The legal provisions for the annual budget are set out in the Constitution¹⁷ and the PFMC Law, which defines the main general government administrations, defines public expenditure and revenue, provides for the principle of unity of treasury, establishes the roles of the MoF, MoD and Under-secretariat of Treasury, and sets out the basis for the central government Budget Law and the annual budget process.

Figure 2 shows that in 2013 central government accounted for 54% of general government spending, extra-budgetary funds¹⁸ accounted for 30%, local government for 10% and revolving funds for 6%.

Figure 2. Breakdown of general government expenditure 2013

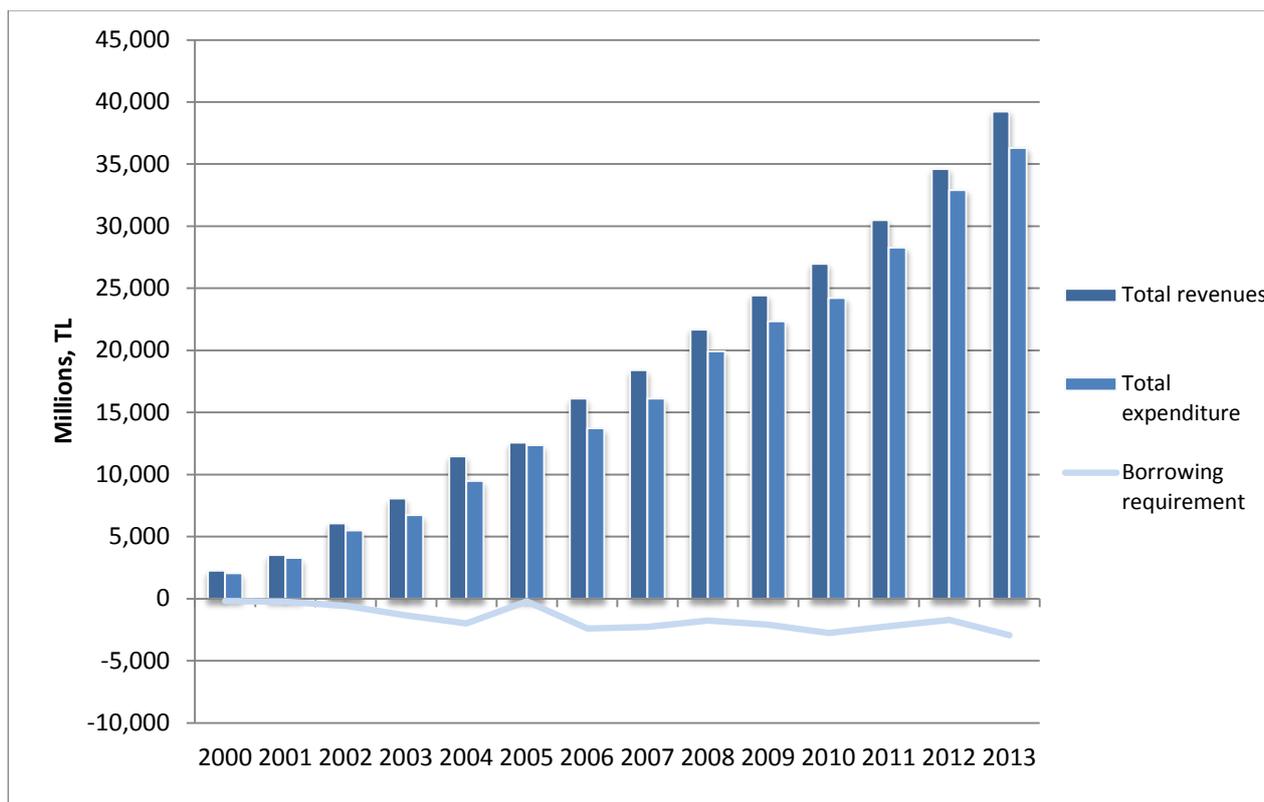


Source: <http://www.mod.gov.tr/Pages/GeneralGovernmentStatistics.aspx>

The moneys available to ministries through revolving funds are considered by the MoF when setting expenditure ceilings, but are outside the scope of the Central Budget even though these funds are defined as part of central government. A variety of fund types are grouped under the term “revolving funds” and the sector with the largest level of expenditure from this source is the Ministry of Health. Expenditure from these funds has grown increasingly large in recent years, and as they are not subject to control by the MoF or the Parliament, they present a risk to the fiscal stance set out in the latest MTP. Figure 3 shows the evolution of revolving funds from 2000 to 2013.

¹⁷ See Article 161 at http://global.tbmm.gov.tr/docs/constitution_en.pdf.

¹⁸ In this instance, the category of extra-budgetary funds includes the Unemployment Insurance Fund, Social Security Institutions and General Healthcare Insurance.

Figure 3. Expenditure and revenues of revolving funds

Source: <http://www.mod.gov.tr/Pages/GeneralGovernmentStatistics.aspx>

The annual budgetary process begins formally with the submission of the MTP to the Government for approval. Then the MTFP is sent to the High Planning Council for approval by 15 September at the latest. Each Ministry has responsibility for their individual documents and, while there is communication between the two Ministries and the Under-secretariat of Treasury prior to the finalisation of the reports, no single institution guides the overall budgetary process. The 'budget call' from the MoF is issued to the line ministries, giving them from mid-September until the end of September to prepare their submission on the basis of the expenditure ceilings set out in the MTFP.

The draft Central Government Budget Law and National Budget Estimation Report is then submitted to the Planning and Budget Committee on behalf of the Parliament of the Turkish Grand National Assembly (TGNA) on or before 17 October. Parliament approves the Budget Law that enters into force as of 1 January. Parliamentarians are not allowed to make expenditure-raising or revenue-decreasing proposals during the plenary debate¹⁹, but amendments are allowed during the Committee stage. These adjustments normally are very minor in scope (about 0.01% and 0.02% of central government expenditure for the 2013 and 2014 budgets respectively).

The PFMC Law sets out the legal basis for the delegation of spending authority²⁰. This provision defines the head of each spending unit to which an appropriation is allocated as the authorising officer. It also specifies that, where an organisation is within general government, the principles and procedures on the determination of authorising officers shall be defined by the Minister for Finance.

There is no formal fiscal rule anchored in legislation. Any supplementary appropriations / budgets must be approved in the same manner as the initial appropriation. However, a contingency appropriation (set at 0.2% of GDP in 2014) is also approved as part of the budget. This allows the MoF to increase expenditure without recourse to the Parliament for minor increases.

¹⁹ Article 162 of the Constitution.

²⁰ Article 31 of PFMC Law as amended in December 2005 (5436/1).

The budget process is based on transparent legal principles. However, Parliament is only given two months to consider the Budget whereas the OECD states that this should be three at a minimum²¹. Furthermore, the revolving funds, which are outside the control of the MoF, present a potential risk to the successful implementation of fiscal policy in line with the MTP and MTFP.

4: The Budget is based on accurate economic and revenue forecasts and includes comprehensive estimates of spending for the coming year that are consistent with the MTBF.

The PFMC Law requires that the MoF issue a 'budget call' and the MoD issue an investment circular to guide the preparation of budgetary and investment proposals by public institutions²². The budget preparation documentation circulated to line institutions clearly sets out the main macroeconomic and fiscal assumptions set out in the MTP and MTFP²³. All general government institutions prepare their budgetary submissions in line with these documents.

Following the submission of budget proposals from institutions via the e-budget system, both the Ministries of Finance and Development engage in parallel discussion with institutions on the current and investment ceilings. These processes are not formally linked and separate meetings are held. The budgetary timetable only allows two weeks for the negotiations process although the line ministries' internal budgetary preparations typically begin in June, prior to the formal Budget Call being issued²⁴. Notwithstanding the ongoing communication between the Ministries of Finance and Development during this stage, the negotiations on current and investment ceilings remain separate processes within the overall budget process.

The issue of risk is informally taken into account in some qualitative manner in setting the fiscal stance. However, there is no formal quantitative fiscal or sectoral risk assessment undertaken regarding expenditure. The main formal assessment of risk is undertaken by the Under-secretariat of Treasury in relation to debt management.

Figure 4 below shows the monthly pattern of expenditure in 2012 and 2013, and it is clear that monthly expenditure peaked in December of both years even though some limited carryover of appropriations is permitted²⁵.

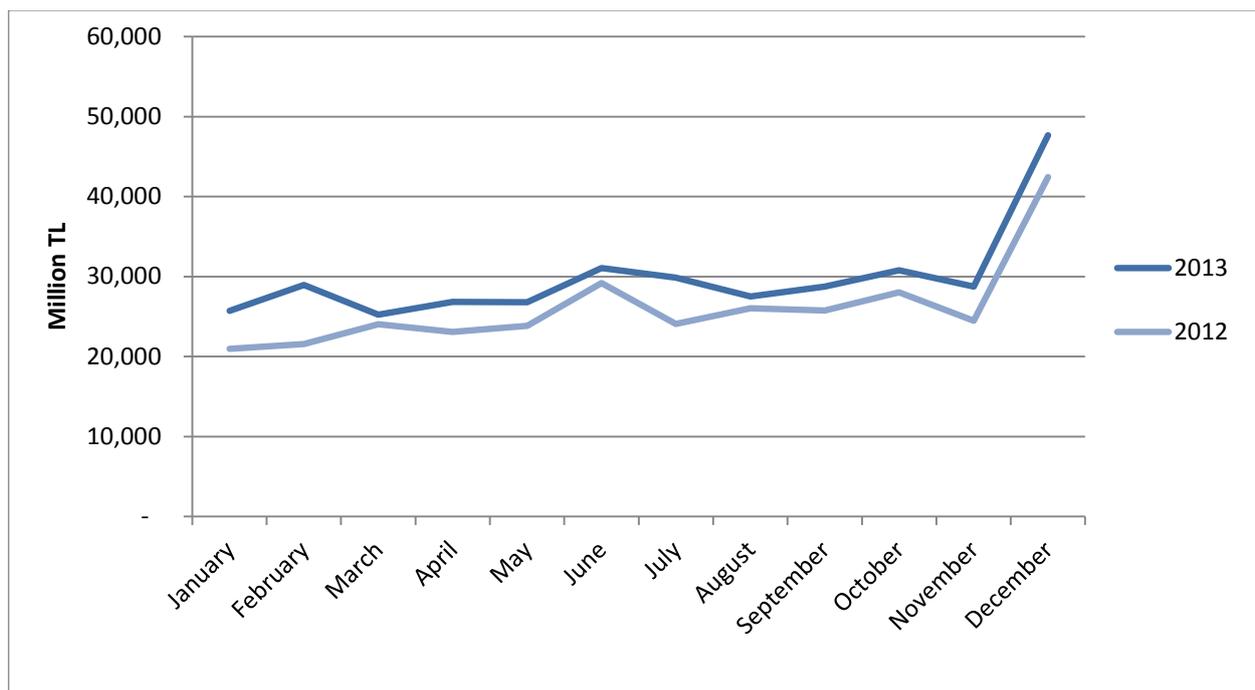
²¹ OECD Best Practices for Budget Transparency at <http://www.oecd.org/governance/budgeting/Best%20Practices%20Budget%20Transparency%20-%20complete%20with%20cover%20page.pdf>

²² Article 16 of the PFMC Law.

²³ <http://www.bumko.gov.tr/TR,4576/2014-2016-donemi-butce-cagrisi-ve-butce-hazirlama-rehbe-.html>

²⁴ This was highlighted in SIGMA interviews.

²⁵ Articles 27 and 28 of the PFMC Law.

Figure 4: Monthly non-interest central government expenditure in 2012 and 2013

Source: Budget realisations reports published by the MoF

The Budget is based on prudent macroeconomic and revenue assumptions and includes comprehensive expenditure estimates that are consistent with these assumptions. However, the fragmentation of the budgetary negotiation process between the Ministries of Finance and Development (notwithstanding the co-ordination between the two ministries) and the extremely short two-week negotiation period with line ministries are not in compliance with international standards.

5: All public sector organisations which form part of the general government balance calculations provide the MoF with comprehensive and accurate estimates for the forthcoming year.

In general, line institutions' SDUs take the lead in budgetary negotiations between the Ministries of Finance and Development. The degree to which operational managers are involved varies between institutions. For instance, the Ministry of Health was re-organised in 2011 and three new units were established: the Public Hospitals Agency of Turkey, the Public Health Institute of Turkey and the Pharmaceuticals and Medical Devices Agency of Turkey²⁶. These bodies have their own SDUs and conduct their own budget negotiations with the Ministries of Finance and Development. The new e-budget electronic system facilitates the transmission and sharing of budgetary data between the MoF and spending administrations.

The deadlines are respected although there is weak linkage between strategy and budgetary allocations. Also there is no requirement to formally identify fiscal risks in the institutional responses to the 'budget call'. However, the budget negotiation process involves the discussion of risks²⁷.

Although the general government organisations engage with the Ministries of Finance and Development and the estimates for the upcoming year are comprehensive, the involvement of the actual spending units is inconsistent, and the links between strategy and performance and budget programmes are weak. Furthermore, risk management at both a fiscal and sectoral level is undertaken as part of the budget negotiations in an informal way.

²⁶ SIGMA interviews explored the interaction of units within the Ministry of Health, in the light of the re-organisation which was established by Decree with the force of Law N° 663 2011.

²⁷ This information is from SIGMA interviews.

Cash and Debt Management

6: The MoF, or authorised central treasury authority, has timely and accurate information on cash flows during the year so that disbursement of funds from the Treasury Single Account is centrally controlled and cash liquidity is ensured.

The PFMC Law requires the administration of revenues, expenditures, collections, payments, cash planning and debt management of public administrations within the scope of central government be managed so as to ensure unity of treasury, and that all revenues of public administrations within the scope of the general budget are deposited at the Treasury cash offices²⁸. The main treasury account is held by the Central Bank of Turkey (CBRT)²⁹. This account is the responsibility of the Under-secretariat of Treasury, with the CBRT acting as its fiscal agent.

In practice, revenues are lodged directly to treasury accounts in Ziraatbank, a state-owned bank before being collected into sub accounts of the main treasury account. These accounts can only be opened or closed by the Under-secretariat of Treasury. As the competent accrediting officer and national authorising officer for IPA funds, the Minister responsible for the Under-secretariat of Treasury bears the overall responsibility for the financial management of the funds in Turkey.

On the expenditure side, the internet based Cash Request Information System (NTAS) gathers cash requests data from about 200 public institutions, including central, regional and special budget offices, on a weekly and monthly basis. It also allows the Under-secretariat of Treasury to send information to these institutions in relation to the forthcoming cash transfers.

From the beginning of the year, the Under-secretariat of Treasury prepares daily cash forecasts over a rolling three-month period. The revenue forecasts are based on trend analysis, changes in regulations and economic analysis. The expenditure forecasts, which are divided into personal (pay) and other, are based mainly on past outturns, the monthly Detailed Expenditure Programme inputs prepared by the MoF with input from line institutions, and monthly meetings with relevant stakeholders.

Cash requirements are managed on a daily basis through an electronic system, the Public Electronic Payment System (PEPS)³⁰, which allows for transferring funds from the Treasury's account to those institutions' payment accounts to cover their following day's payments. While it also allows for sweeping unused cash balances in the general government institutions' bank accounts into the Treasury's account, this is not legally required. It is possible for some agencies to retain unused balances although unused balances generally must be transferred back to the Treasury at end-year. This system means that the Under-secretariat of Treasury can monitor the majority of receipts and expenditures of the general government institutions on a daily basis. Payments may still also be made manually by cheque in the event of a technical malfunction in the system.

The monthly meeting with institutions enables the Under-secretariat of Treasury to informally monitor future commitments. If commitments are not compliant with an institution's cash plan, the payments may be delayed. Expenditures must be made in accordance with budget allocations and cash plans³¹.

The Under-secretariat of Treasury controls disbursement of funds and ensures cash liquidity. It has timely and accurate in-year information on cash flows. Although the monitoring of commitments is informal, all expenditures are made in accordance with budget appropriations and cash plans.

²⁸ Article 6 of PFMC Law.

²⁹ Other accounts held are 411 (debt transactions accounts), 416 (foreign debt servicing account and a risk account).

³⁰ http://www.tcmb.gov.tr/yeni/announce/2012/Basci_KEOS.pdf.

³¹ Article 20(a) of PFMC Law.

7: There is a clear debt management policy and a monitoring mechanism to ensure that the country's overall debt target, as set out in the annual budget, is not exceeded.

The Law on Regulating Public Finance and Debt Management (RPFDM) defines the Under-secretariat of Treasury as the sole borrowing authority on behalf of the Government, provides for the structure of debt management in the Treasury, and determines the main principles and procedures for debt and receivables management and guarantee issuance, including a Debt and Risk Management Committee (DRC). The DRC is responsible for determining strategies for the management of public assets and liabilities, taking into account the risk and cost targets.

The public borrowing policy is based on strategic benchmarking. This policy is summarised in the MTP and set out in more detail in the annual Public Debt Management Report of the Under-secretariat of Treasury with detailed debt figures on a domestic and a general government (EU definition) basis³². Borrowing plans are designed with a three-year time horizon and financing programs are performed in accordance with specific benchmarks. For the 2013–2015 period, the strategic benchmarks are interest rate risk, exchange rate risk and liquidity risk. In broad terms, exchange rate and interest rate risks are managed by borrowing mainly TRY denominated and fixed interest rate instruments, while liquidity risks are managed through extending the average maturity and holding reserves. The ratio of domestic debt stock held by foreign investors was 23.2% of total debt in 2012³³.

Non-general government institutions (local administrations and state owned enterprises (SOEs)) may borrow without the approval of the Under-secretariat of Treasury from State-owned or commercial banks, but need the permission of the Under-secretariat of Treasury for foreign borrowing. Where these institutions wish to borrow using a State guarantee, they are assessed by the Under-secretariat of Treasury using an internal credit ratings system and may be refused based on previous performance. Institutions benefiting from a guarantee pay a premium into a 'risk' account held by the Treasury, with the level of payments adjusted based on the credit worthiness of the institution. Details of guaranteed borrowing are published quarterly by the Treasury³⁴. The funds in this account are used in the event of a call being made on a Treasury guarantee. The risk account has not needed to draw down additional funding from the Treasury since 2009.

There is a clear debt management policy which is published and feeds into the budget process, with one borrowing authority and clear delineation of responsibilities. Furthermore, the debt ratio is stable at about 36%. However, a significant issue is the capacity of non-general government institutions to borrow without requiring MoF or Under-secretariat of Treasury approval in all cases.

Financial Reporting

8: The MoF receives a regular and timely financial report in a common reporting format for each public sector organisation and total government financial reports are published at least monthly.

The accounting and monitoring systems operated by the Under-secretariat of Treasury ensure that it has detailed daily, weekly and monthly information on general government institutions. An electronic system operated by the MoF (SAY2000) collects financial data from central government institutions. This data is broken into key components including payroll expenditures. Financial data on revolving funds is monitored separately by the MoF through a financial management database system integrated with the SAY2000 system. This separate database became operational in January 2014. The two central institutions share information to ensure that their data are consistent. Every three months, the Under-secretariat of Treasury receives financial information for local administrations and the social security institutions through the KBS electronic system, and this can be merged with the data on central

³² <http://www.treasury.gov.tr/default.aspx?nsw=BKsmUPQeFbnBXCDahrXm1A==SqKWD+pQltw=&mid=739&cid=22&nm=712#>

³³ See Public Debt Management Report 2013.

³⁴ <http://www.treasury.gov.tr/default.aspx?nsw=EilDPQez15w==SqKWD+pQltw=&mid=702&cid=12&nm=768#>

government. While local administration data is broken down on a monthly basis, social security information is only available in quarterly terms.

The PFMC Law provides that all general government institutions shall comply with the accounting and reporting standards established by the Turkish Public Accounting Standards Board, and that the form and periodicity of the reports they must prepare shall be determined by the MoF³⁵.

The Treasury publishes a Monthly Debt Management Report³⁶. This detailed report includes: the Treasury cash balance, the domestic and foreign debt positions, borrowings of local administrations, and details of the principal budgetary receipts and expenditures from the Treasury account. The MoF publishes a Monthly Budget Review³⁷, which provides details of revenue including main taxes and details of expenditure including salaries, other current spending and capital. Expenditure by local administrations is also included. Details of future commitments are not published, although it is planned to adopt in 2014 IPSAS 32 on Service Concession Arrangements, so that future liabilities arising from these arrangements will be reported. Both monthly reports are published within four weeks of month-end. All comparisons are presented year-on-year rather than against a monthly profile.

State owned enterprises are not included in the general government sector, but report to the Under-secretariat of Treasury for cash management purposes. The Monthly Debt Management Report includes details of guaranteed and non-guaranteed borrowings by these enterprises.

At organisational level, neither the three-monthly cash profiles produced by the Under-secretariat of Treasury nor the Detailed Expenditure Programme produced by the MoF are published.

General government institutions are required to report monthly or quarterly to the MoF or the Treasury in a consistent standard established by law. Reports on transactions and debt are published monthly. However, profiles of the main fiscal aggregates though available are not published and comparisons in the monthly reports are year-on-year. This means that analysts and citizens cannot see how the execution of the budget compares to the planned budget and variations are not explained. Future commitments are not reported currently.

9: The MoF publishes an annual financial report, the presentation format of which mirrors the presentation format of the Budget.

In accordance with the PFMC Law, the MoF presents the Parliament with the annual Final Account in a format consistent with that of the Central Government Budget, within six months of end-year³⁸. The Final Account is submitted along with the following:

- 1) A general trial balance;
- 2) A budget revenues final account schedule and explanation thereof;
- 3) A budget expenditure final account schedule and explanation thereof;
- 4) A budget revenues and expenditure distribution in terms of provinces and administrations;
- 5) A schedule of State debts and Treasury warranties;
- 6) A schedule of public receivables written-off during the same year;
- 7) An asset management account summary chart.

The Ministry publishes details of budget balance, revenue and expenditure for general government on a quarterly basis. The expenditure data are published at an institutional level³⁹.

The Turkish Court of Accounts (TCA) presents to Parliament the General Conformity Statement, which reconciles the adopted budget with the final account, taking account of individual institutional audits and

³⁵ Article 49 of the PFMC Law.

³⁶ <http://www.treasury.gov.tr/default.aspx?nsw=BKsmUPQeFbnBXCDahrXm1A==SgKWD+pQltw=&mid=739&cid=22&nm=712>.

³⁷ <http://www.maliye.gov.tr/Sayfalar/Eng/HaberDetay.aspx?rid=141&lst=HaberlerListesi&csn=/>.

³⁸ Article 42 of the PFMC Law.

³⁹ https://portal.muhasebat.gov.tr/mqportal/faces/khbDetail?birimDizini=General+Government&_afLoop=10107219698577874&_afWindowMode=0&_adf.ctrl-state=11fab1are4_4.

activity reports⁴⁰. The institutional audits are conducted by the TCA, which is required to give an “opinion on the reliability and accuracy of financial reports and statements of public administrations”⁴¹ However, the 149 reports submitted for 2012 in September 2013 included a TCA disclaimer about the quality of the institutional accounts because it required financial accounts at individual institutional level and these were not available. The TCA believes that it can only audit the consolidated final report if individual reports are available. A joint MoF and TCA working group has been established to resolve this issue and increase the quality of reports to the satisfaction of TCA. It is hoped that this will be achieved by 2015⁴².

The Constitution provides that the Parliamentary Planning and Budget Committee examines the final account in conjunction with the draft Budget for the upcoming year and then presents both to the plenary for debate. Through the Parliamentary Budget Department, the Committee has a support staff of 27 (14 legislative and 13 administrative) to analyse and brief members on reports and draft legislation being considered by the Committee. However, the capacity of the Committee to fully analyse the final account and draft Budget is limited by the fact that about two thirds of draft laws are assessed first by the Committee. The Committee also prioritises the draft Budget as its own internal procedures do not allow sufficient time for detailed analysis of both the final account and draft Budget.

An accrual-based return in accordance with ESA95 general government standards is completed separately and reported to the EU every three months by the Turkish Statistics Institute. Fiscal data to the IMF is completed by the MoF, while the provision of financial data is the responsibility of the CBRT.

An annual report consistent with the detailed format of the Budget is published within six months of year-end It shows revenue and expenditure in gross terms and expenditure by institutional level. However, the MoF currently does not produce individual accounts in the format required by the TCA to meet its auditing obligations.

⁴⁰ Article 43 of the PFMC Law.

⁴¹ Article 36(2b) TCA Law No. 6085 approved by Parliament on 19 December 2010.

⁴² This information is from SIGMA interviews.

PUBLIC PROCUREMENT

TURKEY
APRIL 2014

1. State of play and main developments since last assessment

1.1. State of play

This assessment provides an overview of (i) the current regulations on large construction contracts not covered by the Public Procurement Law (PPL); that is, those regulating public-private partnerships (PPP) and concessions, and (ii) the recent introduction of offset requirements in public procurement in Turkey.

The PPP/concessions field is characterised by a large number of sector-specific regulations and institutions. There is no single authority in charge of PPPs/concessions and none which has a consolidated view of the actual situation in the field. The approaches are not harmonised among the different laws and with the requirements of the PPL. In addition, current regulations and practices focus narrowly on the project management aspects of PPP operations, and their project financing and fiscal aspects are given little attention. However, following the requirement for improvement of the PPP system set out in the Tenth Development Plan 2014-2018 adopted by Parliament 1 July 2013, the Ministry of Development has now started work on reforming the system.

The PPL still contains a long list of exemptions. Some of them reflect the fact that the basic scope of the PPL covers items which are not regulated by the EU Directives.

1.2. Main developments since last assessment⁴³

A major development in the public procurement field since the last assessment is the adoption of a set of amendments to the PPL⁴⁴. It introduces a number of changes to the rules and procedures regarding offset requirements, abnormally low tenders, joint procurement, complaint fees, recruitment of new staff, domestic tenderers, past performance of tenderers and tender security. However, several of the amendments to the PPL will require the preparation of corresponding secondary legislation before they can be applied, in particular those concerning offset requirements and domestic preference.

⁴³ April 2012.

⁴⁴ Articles 45-55 of Law No. 6518 of 6 February 2014.

2. Analysis

PPPs and concessions

1: There is a focal point at ministerial level with designated responsibility for public procurement policy making and co-ordination, internally and externally, with a clear mandate and the authority and resources necessary for the task.

2: The regulatory framework is aligned with the *acquis*, includes areas covered by the fundamental Treaty principles and EU case law, and also regulates areas of national interest, such as value for money in public procurement.

3: Central institutional and administrative capacity is in place to support and co-ordinate the continuous development, implementation and monitoring of public procurement regulations and practices.

PPP-related institutions

There is no single state authority responsible for governing PPP operations, and there is no one institution in charge of any systematic compilation of data on past, current or planned operations.

The Council of State was and still is the main body supervising concessions granted under the 1910 Concessions Law, in addition to the operational responsibilities of the line ministries. Other PPP operations are normally initiated and prepared by the respective line ministries, e.g. those in charge of education, health care and transport, or by the larger operational entities under their control.

A PPP unit of 9 people in the Ministry of Development is in charge of early stage technical and legal review of some PPP projects (namely, BOT projects regulated by the BOT law 3996, and healthcare facilities) along with the Treasury and the Ministry of Finance. The PPL does not cover BOT/PPP tenders. The PPA provides technical support and advice but only upon request from the Ministry of Development. A PPP department in the Treasury reviews the project file before the conclusion of the contract, but only if an explicit state guarantee is required.

The Ministry of Finance becomes involved in the financing stage because state budget funds have to be engaged up front, according to the usual budget procedures. A number of health care and educational institutions have revolving funds fed by revenues from sources other than the state budget, and these allow them to initiate PPP operations without intervention by the Ministry of Finance⁴⁵.

The line ministries are also in charge of implementation management, both during the construction and operation of facilities, with little or no information shared with other authorities.

There is no single authority in charge of co-ordinating, supervising or monitoring PPP operations at large and no clear delineation of roles and responsibilities among the plethora of authorities involved. Consequently, there is also no comprehensive overview of the projects in the PPP/concessions field, the amount of funding engaged and the practices followed.

The PPP regulatory framework

The first introduction of a private law contract option for the delegation of public services was the Law on Granting Authorisation to Institutions Other than the Turkish Electricity Authority for the Generation, Transmission, Distribution and Trade of Electricity⁴⁶, the first Build-Operate-Transfer (BOT) practice, allowing limited private sector involvement in electricity sector projects. The second BOT law, the Law on Granting Authorisation to Institutions other than the General Directorate of Highways for the

⁴⁵ Information from SIGMA interviews with the Ministry of Development.

⁴⁶ Law No. 3096, 4 December 1984.

Construction, Maintenance and Operation of Highways⁴⁷ in the highway sector, removed the monopoly of the General Directorate of State Highways for highway construction, maintenance and operation.

More recently, other sector-specific PPP laws for airports and healthcare were also introduced. The Law Amending Certain Laws and Decrees Having Force of Law [Regarding Airport Operations]⁴⁸, among others, regarding the transfer of operational rights over airports and passenger terminals from the State Airport Authority (2005) authorised the State Airport Authority to transfer its airports, in whole or in part, to the private sector through long-term lease or Transfer of Operating Rights (TOR) methods.

In a similar way, the Supplemental Clause No. 7 (added through Law No. 5396, 2005) of the Law on Health Care Services⁴⁹ extended the practice to the health services. This clause authorised the Ministry of Health to contract with the private sector for long durations (up to 49 years) for the construction of health units and the provision of non-clinical support services in return for yearly rentals paid to the private sector. It was complemented by a "Regulation on the Building of Health Facilities in Exchange for Leasing and Renewal of the Areas and Services Outside the Areas for Medical Services in the Facilities in Exchange for Leasing". It was recently superseded by a new Law on Building and Renewal of Facilities and Procurement of Services through Public Private Partnership Model⁵⁰, which also amended the general BOT law, among others, by introducing stipulations on how tenders should be conducted, with a choice between the open, the restricted and the negotiated procedure.

The nature of the solutions developed at the time, a diverse mixture of "privatisation" and public procurement approaches, indicates that the primary objective was to secure the provision of public services while generating savings for the state budget, whether on the revenue or the expenditure side. The BOT model required the private partner to finance, construct and operate the project and return the property back to the administration at the end of the designated period, whereas in the TOR model, the administration transfers its assets to the private sector in consideration of payment for a designated period. Finally, the Build-Rent-Transfer (BRT) model required the private partner to finance, construct, and rent out the property to the administration for a designated period, returning it to the administration at the end of the rental period.

The BOT contract and the TOR approach, initially understood as new forms of concessions agreements, were ad-hoc measures to allow private groups to invest for a long, fixed term without the need for complete privatisation, which was meeting strong resistance from the Constitutional Court and the Council of State. Many of the initial BOT regulations and deals were, nevertheless, challenged by the Constitutional Court and the Council of State until a constitutional change in 1999 confirmed the right of public and private parties to supply public services as equal partners under private law.

The general BOT law⁵¹, as amended, remains the major vehicle for PPP operations that in EU countries would have been considered as concessions and regulated as such. Still serving as the main legal basis of PPP operations, it was enacted for the realisation of projects in numerous infrastructure sectors, including energy, transportation, communication and municipal services. The general BOT law has some limitations, in that it stipulates that a new corporation must be founded for each project and the scope of activity of that corporation must be limited to the BOT project in question. However, following the 1999 amendments to the Constitution, changes to the BOT law introduced in 2000 brought a series of changes favourably affecting the implementation of BOT agreements with regard to arbitration, foreign elements, expropriation and employment.

The Law on Privatisation Implementation⁵² used the TOR model to regulate the "privatisation of public services" through the transfer of operating rights to infrastructure facilities for long periods of time, up

⁴⁷ Law No. 3465, 28 May 1988.

⁴⁸ Law No. 5335, 27 April 2005.

⁴⁹ Law No. 3359, 15 May 1987.

⁵⁰ Law No. 6428, 9 March 2013.

⁵¹ Law No. 3996, 13 June 1994.

⁵² Law No. 4046, 27 November 1994.

to 49 years. This law also states that the “privatisation” of public facilities is to be performed through concession contracts if these facilities have a monopoly status. It now plays only a minor role in PPP operations.

Finally, the Law on the Establishment and Operation of Electricity Plants and Energy Sales⁵³ (Law No. 4283, 19 July 1997) introduced new ad-hoc measures and incentives for the private sector in the form of Build-Operate-Own (BOO) contracts, which allocate the ownership of assets to the original investor when the contract ends. However, this law regulates the BOO model only for electricity generation plants.

The regulatory framework for PPPs and concessions is composed of a large number of laws and regulations, adopted at different times and for different, specific purposes, with no single regulation providing a set of harmonised policies and procedures.

PPP operations and practices

As can be seen from the nature of the various regulations currently governing PPP operations, their main focus remains that of the engineer: that is, to ensure quality of construction and fitness for purpose in technical terms. The quality of project preparation, as reflected in the project files submitted⁵⁴, is often low. In particular, the needs analysis and the evaluation of costs and benefits are typically deficient and the fiscal and financial risks are not addressed.

A major reason for these deficiencies is that there is no common approach to project preparation and appraisal, with no general guidelines and established practices, nor any body of knowledge that practitioners could easily access and make use of.

In EU countries, the key defining aspect of a PPP project is the emphasis on the financial set-up and on attracting the best financial conditions possible, in addition to securing future revenues. As a corollary, the many related legal issues are also addressed in great detail at an early stage. In Turkey⁵⁵, this side of PPP projects is less present, together with the international aspect: the need for and the advantage of tapping foreign financial markets, using the most favourable technical solutions available in the world and attracting the best foreign contractors as partners, are rarely acknowledged.

Banks and contractors in Turkey are aware of their limited capacity to cater for but a few of the projects now in process in some of the major line ministries⁵⁶. It is understood that the Ministry of Health intends to launch PPP operations for the provision of some 60 major hospitals, while road projects envisaged for the next ten years are said to amount to approximately USD 400 billion, with the local supply of financing and contractors barely able to cover more than a few percent of these projects⁵⁷. Nonetheless, in the absence of any consolidated database of current and planned PPP operations, the supply limitations are difficult to appreciate and address, and the individual line ministries continue adding to their stock of prospective PPP projects.

In today's PPP operations, there are risks to the state budget which have not been clearly identified. Given the focus on technical project management, many recent PPP operations have been successfully completed in that facilities have been built and are working. However, operation and maintenance have a tendency to become more risky and costly over time, and the revenue streams are even more unpredictable and variable. At the same time⁵⁸, BOT contracts governing many of the current PPP operations have *force majeure* clauses which imply that in case of any unforeseen problems (with corresponding cost overruns), the contractor/operator can discharge himself of responsibility, with the

⁵³ Law No. 4283, 19 July 1997.

⁵⁴ SIGMA interviews with the authorities in charge of the review of PPP (as applicable, the Ministry of Development, the Ministry of Finance and the Treasury).

⁵⁵ As evidenced by SIGMA interviews with authorities and banks involved.

⁵⁶ This was expressed by banks and construction experts during SIGMA interviews.

⁵⁷ As indicated in SIGMA interviews with banks involved.

⁵⁸ As pointed out in several SIGMA interviews, notably with the Ministry of Development.

client (i.e. the public authority concerned) responsible for the costs incurred, with the state budget as backing.

This is also the case when there is no explicit state guarantee and when, consequently, the Treasury has not had an opportunity to review the draft contract, and is therefore unaware of the contingent liability of the Government.

The current approaches do not ensure efficient, cost-effective and financially sustainable PPP operations, and not all fiscal risks are recognised and mitigated.

Offset requirements

4: There is a focal point at ministerial level with designated responsibility for public procurement policy making and co-ordination, internally and externally, with a clear mandate and the authority and resources necessary for the task.

5: The regulatory framework is aligned with the *acquis*, includes areas covered by the fundamental Treaty principles and EU case law, and also regulates areas of national interest, such as value for money in public procurement.

A recent amendment⁵⁹ to the PPL not only introduces the notion of offset requirements in public procurement practice, but at the same time immediately exempts them from the scope of the PPL, without any further effort to regulate this practice within the PPL itself. This is achieved by covering offset requirements in a new, additional item in the long list of exemptions in article 3 of the PPL:

“(u) Procurement of goods and services involving industry contribution /off-set implementation with a view to ensuring innovation, domestic production and technology transfer.”

Offsets are ‘compensatory’ deals required from foreign suppliers when goods, works or services are procured from abroad. In some cases, offsets concern the subject-matter of the contract directly, for example, industrial participation of local companies in the production of equipment procured. In other cases, they are indirect but limited to the field concerned, for example, contracts for related goods or services that have to be awarded by the supplier to local companies. They can also be indirect, when foreign suppliers have to enter a commitment to mobilise foreign investment in other sectors of the buying country’s economy or to purchase other products in that country.

A recent example from Turkey is the requirement that the successful tenderer for the supply of rolling stock for the Ankara metro source at least 51 % of the value of the contract from Turkish enterprises.⁶⁰

Such offset requirements are restrictive measures which go against the basic principles of the Treaty, because they discriminate against economic operators, goods and services from other Member States and impede the free movement of goods and services. Since they violate basic rules and principles of primary EU law, the EU Directives cannot allow, tolerate or regulate them.

The use of offset requirements in public procurement is thus incompatible with the EU *acquis*⁶¹. This applies to all kind of works, supplies, services and investments, whether they are military, security-related or civil in nature or purpose, and irrespective of whether they are directly or indirectly related to the subject-matter of the procurement contract in question. Furthermore, tenderers, candidates and successful tenderers may not be required to mobilise other undertakings, be they related to them or not, to make such purchases, subcontracting or investments.

⁵⁹ Article 45 of Law No. 6518.

⁶⁰ See e.g. <http://www.hurriyetdailynews.com/chinese-and-turkish-firms-to-build-wagon-making-plant-in-ankara.aspx?pageID=238&nID=44727&NewsCatID=345>

⁶¹ See the undated Guidance Note from the EU Commission at http://ec.europa.eu/internal_market/publicprocurement/docs/defence/guide-offsets_en.pdf

In any case, the possibility to promote “innovation, domestic production and technology transfer” has already been available within the framework of the earlier EU directives on public procurement and has become even more so in the new directives that were published on 28 March 2014⁶², e.g. through the new innovation partnership mechanism and the increased possibility to take social and environmental considerations into account. Innovation, domestic production and technology transfer would be possible to support also by making use of the enhanced provisions in the new directives for encouraging small and medium enterprise (SME) participation, by for example splitting into lots and limiting restrictive qualification requirements. However, under the EU directives, the acceptable means for promotion of domestic production would not include any form of domestic preference.

In addition, specific provisions in public procurement policies and procedures would not be the only or the major means for the development of innovation, domestic production and technology transfer, which would normally derive greater benefits from other, more targeted measures.

Consequently, to the extent that public procurement would be retained at all as a supplementary support for innovation, domestic production and technology transfer, the *acquis* requires that corresponding measures are taken within the public procurement system, rather than by exempting this whole field from its disciplines, as is now the situation in Turkey.

An additional article⁶³ in the recent amendments to the PPL states that “The procedures and principles regarding section (u) of article 3 of this Law shall be determined by the Ministry of Science, Industry and Technology in consultation with the [Public Procurement] Authority and the relevant agencies.” However, being a public procurement policy issue, the regulation of the matters covered in the new section (u) of the PPL would normally fall under the remit of the authorities in charge of policy making and co-ordination in the field of public procurement.

The allocation of regulatory authority for public procurement to the Ministry of Science, Industry and Technology for cases covered by the new offset regulation does not acknowledge the official role of the central public procurement policy and co-ordination unit established in the Ministry of Finance⁶⁴. The new offset regulation creates additional exemptions from the PPL and additional provisions for domestic preference, which both are incompatible with the EU acquis.

⁶³ Article 54 of Law No. 6518.

⁶⁴ As required by the first opening benchmark: “[A]n organisation for procurement guarantees a coherent policy in all areas related to public procurement”.