Civil Society Governance Diagnostic Report on Sri Lanka
An Assessment of the Anti-Corruption Landscape of Sri Lanka
CIVIL SOCIETY GOVERNANCE DIAGNOSTIC REPORT ON SRI LANKA
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Civil Society Initiative on Anti-Corruption Reform for Economic Recovery
Civil Society Governance Diagnostic Report on Sri Lanka

ISBN:

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Review and Oversight: Civil Society Initiative on Anti-Corruption Reform for Economic Recovery
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CIVIL SOCIETY GOVERNANCE DIAGNOSTIC REPORT: An Assessment of The Anti-Corruption Landscape of Sri Lanka

This Civil Society Governance Diagnostic Report on the Anti-Corruption Landscape of Sri Lanka (Report), prepared on the basis of extensive local consultation over a two-month period with a range of community and sectoral representatives as well as experts in the key subject areas, focuses on the main governance determiners that have influenced the corruption context in Sri Lanka. It identifies crucial factors that need to be harnessed to facilitate and sustain anti-corruption measures necessary to ensure that Sri Lanka recovers successfully from its current financial crisis making the best use of the International Monetary Fund’s (IMF) Extended Fund Facility (EFF). Based on this input and a study of best practice in similar situations, including the IMF’s own governance diagnostic recommendations recently made in comparable circumstances, the Report assesses progress made, identifies key weaknesses, and provides a list of measures deemed necessary to steer immediate and future reforms.

A. INTRODUCTION

This Report was prepared on the basis of extensive consultation with a range of stakeholders from across the country, as well as guidance received from experts in the field. Over 250 participants representing key sectors, geographical locations, ethnic, religious and cultural groups, contributed to the content of the Report. This study was designed to identify and prioritize, both from a public opinion and governance perspective, the core elements of the national (anti-) corruption landscape, which should be systemically addressed in order to ensure the necessary fiscal and governance outcomes for Sri Lanka to overcome the current crisis.

The information used in preparing this report were of five types: they are (a) national studies/reports/summaries on core focus areas of the corruption landscape identified in the core group, the Key Informant interviews (KIs) and through a snowball approach which led to other studies cited in the initial ones examined, (b) relevant regional/comparative studies and analyses of similar issues and concerns, (c) the range of related legislation and documents concerned with them, (d) journalistic and more public-oriented pieces on the governance-corruption nexus, and (e) relevant IMF conceptual documents and country reports.
B. BACKGROUND TO THE STUDY

By early 2022, Sri Lanka was facing the worst economic crisis since independence. With the full depletion of its foreign reserves, the country came to a standstill, unable to import essentials such as fuel and food. In May 2022, Sri Lanka defaulted on its debts for the first time in its history. This crisis ignited an unprecedented people’s uprising whereby large numbers of Sri Lankans persevered in a continuous peaceful protest for over four months, demanding the resignation of the then president and a true ‘system change’ that would end corruption and poor governance. This demand from the citizens arose from the common understanding that the economic crisis was a result of economic mismanagement coupled with a governance crisis, embedded in deep-rooted corruption.

Therefore, fighting corruption, demanding accountability for the crisis and the recovery of stolen assets etc. became part of the public discourse in Sri Lanka.

The government, led by the new president, reached out to the IMF to facilitate the debt restructuring process and to inject essential foreign reserves that were urgently needed to keep the country moving and to begin the process of economic recovery.

Ten months later, in March 2023, the IMF Executive Board approved US$2.9 billion under a new EFF arrangement for Sri Lanka, after the government obtained financing assurances from the major creditors. This IMF programme, being the 17th one in Sri Lanka, enabled Sri Lanka to defer bilateral and private debt service payments for two years and work towards a debt treatment that achieves debt sustainability. Importantly, this IMF program includes governance and anti-corruption as a key pillar, and as such, initiated a governance diagnostic – the first of its kind in Asia.

At this decisive moment of time in Sri Lanka, which will determine if the country recovers or is limited to temporary survival, the critical importance of anti-corruption and governance reforms that address the root causes of the crisis and make pathways for real and equitable economic recovery cannot be overstated.

The civil society groups that initiated and gave leadership to this effort of developing an independent governance diagnostic for Sri Lanka – the Civil Society Initiative on Anti-Corruption Reform for Economic Recovery (the Core Group) – were of the view that the economic crisis in Sri Lanka is first a crisis of governance. This view has wide resonance with the Sri Lankan people. If the foundational governance issues in Sri Lanka are not addressed by concrete actions, then the policies and plans for debt sustainability and economic recovery are likely to be on shaky ground.

The process of writing this report followed island-wide consultation with civil society groups and subject experts, with a focus on developing solutions regarding high-level corruption and lack of democratic accountability that is afflicting the future economic prospects of the country.
C. METHODOLOGY

Key Informant Interviews (KIs) and Focus Group Discussions (FGDs), comprising over 250 representatives from across the country, formed the basis of public input and feedback, thus shaping the content of the Report, which was prepared under the guidance of the Core Group. An extensive review of the relevant economic governance literature was complemented by an examination of similar situations where IMF EFFs had generated governance diagnostic reports, including recommendations implemented as a result of these reports. The understanding is that while this civil society initiative is wholly independent and demand-driven, it also seeks to constructively engage with the parallel process undertaken by the IMF’s own governance diagnostic.

The recommendations, which have been derived from these consultations with key stakeholders and from the literature, draw on four sources: (i) Governance commitments in Sri Lanka’s current IMF programme, (ii) Governance benchmarks in IMF programmes in other countries, (iii) Governance benchmarks identified from current research and analysis in Sri Lanka, and (iv) evidence-based recommendations of Governance benchmarks strongly articulated and supported by a range of interlocutors, including experts in the field, in discussions held across the country.

The draft findings/analysis and recommendations stemming from them were shared with the Core Group and designated others (at a Validation Meeting) for their final comments and endorsement. The final report was revised based on this feedback, subject to the endorsement of the Core Group, for more official distribution to all key stakeholders, including the Government of Sri Lanka and the IMF.

Limitations

The findings of this report are limited by various constraints, including the limited knowledge that could be collected from a wide base of civil society organisations (CSOs) within a short space of time. Many organisations that provided input were articulate about Sri Lanka’s governance challenges. However, many also were not able to formulate, in the limited time, precise, actionable solutions. The ability to incorporate input was also limited by the focus of this diagnostic, which is on governance issues with macro-economic impact. Many civil society contributions stressed the pressing issues of human rights and justice, which were outside the scope of this effort, even while they remain extremely important.

However, the present Report has two distinct advantages over the similar effort by the IMF. The first is that it was able to be more deeply connected to the pulse of the people and civil society in Sri Lanka. The second is that it has not been constrained by the need to have the sign-off of the Sri Lankan government, which is at the heart of the governance crisis. Therefore, while acknowledging that the output will invariably be incomplete, we believe that it is yet productive, and should be considered a reference point for international engagement and assistance, in the midst of Sri Lanka’s governance and economic crisis.

1. In keeping with the agreement to respect full confidentiality, no names or official designations of any participants have been included, but records of all discussions have been maintained by author. The main FGDs were held in Ampara, Anuradhapura, Batticaloa, Jaffna, Kandy, Kurunegala, Matale, Nuwara Eliya and Ratnapura, while smaller groups were consulted in other areas as well. 30 KIs were held in addition to four Core Group discussions and a Validation meeting.

2. The institutional support and intellectual guidance received from TISL throughout the study is gratefully acknowledged. The Core Advisory Group steered the study by providing substantive advice, thereby shaping its focus and content. Research and analytical support received from Verité Research oriented the findings and provided the evidence-base for its recommendations on economic governance. The Report in its final form reflects the input and feedback received from the spectrum of stakeholders consulted, with no one group being privileged. The draft recommendations have been validated by several key experts.
D. OVERALL CONTEXT & LITERATURE REVIEW

A core insight of the consultations is that the emphasis of recent efforts to address the current crisis have focused excessively on the foreign debt crisis and/or addressed it as a balance of payments problem. This approach to Sri Lanka’s predicament cannot engage adequately with the larger governance crisis that caused the debt and economic emergency in Sri Lanka. Therefore, it also cannot engage in meaningful dialogue on the social cost and repercussions of the proposed economic recovery program. This discussion is long overdue already since the distribution of the social cost is manifestly unequal, even while it encroaches on all sectors, classes, and regions.

The view was strongly held that the proposed and already-implemented IMF-oriented reforms should not additionally burden the income-poor and vulnerable sectors of the population who are currently facing huge economic hardships. The perception of respondents consulted in this study is that proposed reforms in effect load costs on the poor while conferring benefits on the more affluent. Hence, governance benchmarks should be designed to address both short-term and long-term fiscal and related governance vulnerabilities. It was pointed out in the field discussions that the current growing sense of economic injustice has been exacerbated by the fact that the architects of the economic crisis do not bear any part of the burden of its proposed reform, which has been, again, firmly thrust, without any dialogue, on the victims of this very crisis.

“...There are many people who come from the South to speak with us about what they call common issues which they say we should unite on. We have got used to this form of manipulation too, and so we have a test for their sincerity and commitment to an equal partnership as the basis of this unity. That is the basic issue of power sharing. If you don’t put at least the 13th Amendment on the table, we know where you are coming from.” Key Informant Interview in the North.

Corruption is the core issue that determines the nature of the Sri Lankan polity. In fact, corruption has spread so far and wide that the country is currently facing imminent State Capture, which “prevents public institutions from fulfilling its mandate and neutralizes internal and external checks on such systems”. It has been persuasively argued that “Sri Lanka, a fragile democracy that emerged from a 26-year civil war only in 2009, is on the verge of becoming a captured state”. State Capture is said to operate in three ways, which comprise “influencing the formation of law and policy”, “influencing the implementation of policy”, and “disabling the accountability institutions”, paving the way to usher in a kleptocratic regime.

3. All of the FGDs and many of the KII consultations highlighted this point with concrete examples, such as the issues they face in fulfilling basic needs and obtaining fundamental services for their families, which make survival itself very difficult for underclass groups across the country.

4. See, for instance, Institute of Policy Studies (July 2022), Sri Lanka’s Deepening Economic Crisis: The Plight of the Poor: “The country’s worst economic crisis since independence has battered Sri Lankans from all walks of life but the fallout are impacting the poor with greater intensity.”


A useful working definition of kleptocracy is the “systemic transnational corruption involving political, business or criminal elites and their professional intermediaries for the purposes of illicit self-enrichment or furtherance of political objectives”\(^8\), which is a devastating condition that Sri Lanka may be on the brink of succumbing.\(^9\) When national corruption is on a scale and depth that it lends itself to kleptocracy, nothing short of stringent transparency and accountability combined with the end to impunity has a hope of curbing its cancerous growth.

A current study has identified that among the high probability and high-risk tactics used in Sri Lanka are the structural weakening of the country’s accountability framework, influence and interference with public officials, abuse of state-owned enterprises, manipulation of public procurement procedures, manipulation of state and private mass media, suppression of civil society, and the use of illicit financial transactions.\(^10\) It is crucial that the majority of these factors have been identified in the present study as core areas for fiscal and governance reform. In this context, a Politically Exposed Persons (PEP)\(^11\) database of the type that was maintained by Transparency International Sri Lanka (TISL) which was publicly accessible, needs to be developed “with useful, up-to-date information such as real estate and other property ownership, [and] asset declarations data.”\(^12\) The recommendations in this Report too clearly reinforce this approach to addressing large-scale and systemic corruption.

The report prepared by the Centre for Policy Alternatives on the Commission of Inquiry (CoI) and the Special Presidential Commission of Inquiry (SPCoI) on Political Victimization clearly outlines the serious consequences for the independence of the judiciary and the undermining of due process in the rule of law that take place when narrow political motives remain unchecked, creating extremely problematic precedents.\(^13\) It is telling that even the Attorney General “himself objected to his own officers being summoned to the CoI and questioned as to ongoing prosecutions. The Attorney General resisted such questioning on the basis that a fact-finding Commission of Inquiry had no powers to interfere with ongoing court cases.”

Regarding taxation, it is important to reiterate the core principles of tax policy, which appear to be observed just as much in the breach in the new reforms as in the past. These governance principles are neutrality, efficiency, certainty and simplicity, effectiveness and fairness, flexibility, and horizontal and vertical equity.\(^14\) The recommendations in this Report seek to uphold and protect these principles, while facilitating the fiscal outcomes necessary for economic recovery.

In this framework, **neutrality** “implies that the same principles of taxation should apply to all forms of business, while addressing specific features that may otherwise undermine an equal and neutral application of those principles,” while **efficiency** assures that “compliance costs to business and administration costs for governments should\(^15\) be minimized as far as possible.” **Certainty and simplicity** address the principle that “tax rules should be clear and simple to

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9. See An Overview of Kleptocratic Tactics in Sri Lanka (2023), unpublished paper by TISL, which states “In Sri Lanka, the problem of ‘kleptocracy’ is not yet sufficiently discussed in the public domain, even though the tactics are by kleptocrats quite openly” p. 104.
10. Ibid.
11. “Individuals who are or have been entrusted domestically with prominent public functions, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state-owned corporations, important political party officials.” As cited in An Overview of Kleptocratic Tactics (op. cit.)
12.Ibid., p. 100.
14. While these principles appear in many similar forms, the OECD provides a comprehensive analysis from which this list of fundamental principles has been taken. https://www.oecd-ilibrary.org/docserver/9789264218789-5-en.pdf?expires=1693809082&id=id&accname=guest&checksum=FE2B7787CA0A43ED22EC5530203BE25
understand, so that taxpayers know where they stand. A simple tax system makes it easier for individuals and businesses to understand their obligations and entitlements.” The principle of **Effectiveness and fairness** insists that “taxation should produce the right amount of tax at the right time, while avoiding both double taxation and unintentional non-taxation. In addition, the potential for evasion and avoidance should be minimised. If there is a class of taxpayers that are technically subject to a tax, but are never required to pay the tax due to inability to enforce it, then the taxpaying public may view the tax as unfair and ineffective.”

**Flexibility** posits that “taxation systems should be flexible and dynamic enough to ensure that they keep pace with technological and commercial developments.” Finally, horizontal **Equity** “suggests that taxpayers in similar circumstances should bear a similar tax burden. Vertical equity is a normative concept, whose definition can differ from one user to another. According to some, it suggests that taxpayers in better circumstances should bear a larger part of the tax burden as a proportion of their income...Equity is traditionally delivered through the design of the personal tax and transfer systems.”

Regarding the potentially negative consequences of making sudden increases in taxation without an evaluation of potential impact and consequences, it is also notable that the phenomenon known as the “brain drain” has worsened in the context of Sri Lanka's economic crisis. This can be illustrated by a significant surge in the issuance of new passports in 2022. Specifically, the number of general passports (excluding Diplomatic and Official passports) rose from 545,883 in 2019 to 910,138 in 2022. It's worth noting that the numbers in 2020 and 2021 were considerably lower, likely due to the impact of the Covid-19 pandemic.17 While there is no single reason that can account for this serious blow to Sri Lanka’s human resource asset, the new tax regime of higher marginal personal income taxes, which impacts professionals, has been cited as a reason for this exodus, which for instance is claimed to have resulted in 30–35% vacancies in university faculties, and even the closing down of certain hospital departments, according to a survey conducted.18

Any discussion of the Sri Lankan context must necessarily engage with the vexed question of the Executive Presidency, seen here in a most powerful form. The commitment to abolish the Executive Presidency has been a long-standing election promise, which continues to be reneged upon by successive incumbents once voted into power. The following statement succinctly and precisely argues the case against the present situation:

“**We advocate the complete abolition of the executive presidential system of government. Civil society has long campaigned for this, in view of the authoritarianism, maladministration, and corruption that this institution has fostered ever since its introduction... The reinstatement of parliamentary democracy will ensure the constant political accountability of the executive to the legislature, together with such other legal safeguards for constitutional rights, good government, pluralism, and devolution.**”

18. Professionals’ Trade Union Alliance (PTUA), March 2023. A Fair, Transparent And Accountable Taxation System For Sri Lanka. More specifically, in a survey of university academic staff undertaken in May 2023, 80.9% of 1464 respondents from 21 state universities identified the “very high income tax” as a key reason for “considering moving to another country.” Unpublished FUTA data.
An overpowerful Executive Presidency in Sri Lanka lends itself not merely to the systematic abuse of power, but also to gross violation of human rights and corruption on an unprecedented scale, in the face of which the usual checks and balances have no meaning.

In this context, the devolution of political and administrative powers, which can start with the full implementation of the 13th Amendment to the Constitution, is seen, especially by non-majority community respondents, as contributing to the necessary safe space and enabling environment for the broad public dialogue and ownership that is required for even the IMF agreed governance benchmarks to succeed. The United Nations High Commissioner for Human Rights (UNHCHR) has argued that “fundamental changes will be required to address the current challenges and to avoid repetition of the human rights violations of the past.” Similarly, the development trajectory and choices made by successive regimes were not seen as conducive to inclusivity or equity.

No part of the necessary public participation and ownership of the reform agenda will be possible if there is no safe space nor an enabling environment for dissent and constructive engagement by the full spectrum of stakeholders representing diverse opinions expressed in different languages through different cultures. This civic space combined with a rights-based approach is essential for the political-economic recovery to be sustainable, yet it is this very bedrock upon which macro-critical reform must be anchored that appears to be lacking today.

The documents examined in preparing this report were of five types: they are, not in any particular order, (a) national studies/reports/summaries on core focus areas of the corruption landscape identified in the core group, the KIIs and through a snowball approach which led to other studies cited in the initial ones examined, (b) relevant regional/comparative studies and analyses of similar issues and concerns, (c) the range of related legislation and documents concerned with them, (d) journalistic and more public-oriented pieces on the governance-corruption nexus, and (e) relevant IMF conceptual documents and country reports.

Hence, IMF diagnostic reports undertaken within the last decade were examined to establish the kind of “structural benchmarks” that they advocated. In this category, IMF governance diagnostic reports for Mali (2023), Zambia (2022), Mauritania (2022), Moldova (2022), DR Congo (2021), Ukraine (2020), and Mozambique (2019). These proved to be very fruitful to identify similar benchmarks that had been recommended, such as the independent prosecutor’s office in Ukraine. It was also clear that the country reports varied in quality and depth appreciably, presumably as a function of the level of engagement and commitment of national counterparts. In addition, the emerging IMF literature on its own governance diagnostic process was instructive both for what it sought to do, and what it omitted altogether. It appears that the IMF itself is struggling to better understand the role and function of this diagnostic in a conceptual and disciplinary space that is outside its core business and area of expertise.

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20. This view was articulated in the strongest terms in both the FGDs and KIIs in the North and East, and it was echoed by many majority community respondents as well. The absence of both local government and provincial representatives has clearly deepened this view in other areas of the country as well.
22. https://www.themorning.lk/articles/xm7zdSoWtWzU7TgiCu
23. Naomi Klein’s Shock Doctrine, which argues that in times of unprecedented crisis and difficulty, unpopular and unsustainable policies are enforced by the elites without much opposition from the citizenry, is instructive here. See Klein, Naomi. 2007. The Shock Doctrine: The Rise of Disaster Capitalism.
The national studies, reports and other documents were the most useful sources for this analysis. Local and international organisations engaged in the areas of both governance and anti-corruption had done key assessments and evidence-based recommendations which the public consultations completely vindicated. While some emerging areas, including responding to the multiple crises facing Sri Lanka today were generally under-served, especially by multi-disciplinary studies, the work of, in alphabetical order, The Centre for Policy Alternatives (CPA), Transparency International Sri Lanka (TISL), Verité Research stood out, and formed the basis of this report’s analysis, though the author bears responsibility for any errors and omissions. Even as the agreement was formalized, the IMF Tracker maintained by Verité Research proved to be a most useful resource in its real-time monitoring and assessment of progress in meeting agreed benchmarks.

Since governance assessments done in relation to financial corruption in the region were scarce – Sri Lanka is the first country in Asia that the IMF is undertaking a governance diagnostic – it was difficult to obtain useful comparative data. However, a longer and better resourced study would have been able to identify more nuanced regional comparisons, synergies and core differences which would have deepened the analysis undertaken here.

In many of the most important instances, current legislation and related documents have been carefully analysed by specialist organisations and collectives. Media reports and studies were generally superficial and partial, though some important contributions proved useful. In general, material in the national languages Sinhala and Tamil were less easily available and often not accessible at all, which has serious adverse effects on the level and quality of public engagement on these fundamental issues.

The detailed reliance on the literature, in each of its five categories, can be seen in the body of the text through referencing and citation.
E. ORGANISATION OF FINDINGS

The discussion and hence the Report was structured around a tripartite framework of anti-corruption measures deemed necessary for immediate (up to six months), short-term (six months to one year), and medium-term (one to two years) implementation in order to facilitate financial recovery without falling back into replicating the same root causes that drove the country into this predicament in the first place.24

Hence, even the substantive recommendations were conceptually divided into three categories, though they did not map precisely onto the implementation timeframe. These were:

A. Measures to enhance transparency and accountability of existing systems that are necessary to produce the required fiscal governance outcomes.
[18 recommendations: 4 tax and expenditure-related, 4 audit-related, 1 on domestic debt restructuring and superannuation funds, 1 on asset declaration, 3 on corruption, 1 on procurement, 2 on elections, 1 on environment impact assessment, and 1 on civic space]

B. Measures to improve macro-political-economic stability and sustainability.
[12 recommendations: 3 on amending current tax legislation, 1 on increasing powers of the National Procurement Commission, 1 on debt management, 1 auditing under-performing ministries, 1 on conflict of interest, 1 on changing parliamentary standing orders, 1 on state enterprises, 1 on demilitarization, 1 on social safety net improvement, and 1 on illicit financial flows]

C. Measures towards structural changes that are necessary to significantly reduce corruption risk and impunity.
[4 recommendations: 1 on stolen asset recovery, 1 on establishing an independent corruption prosecutor’s office, 1 on alienating land in the Malaiyaha Tamil areas, and 1 on the Constitutional Council]

The final assessment, made both in the KIIs and FGDs as well as in the analytical literature, identified key recommendations based on their fundamental importance in achieving the core fiscal outcomes and/or achieving the pre-requisite credibility within the diverse social fabric, addressing the geographical, ethnic, religious and cultural divides. Hence, while all recommendations are marked as being important for the success of the reforms, they have been disaggregated in terms of timeframes for implementation, using the IMF’s own tripartite classification: “Immediate – to be implemented in up to six months, Short Term – to be implemented in six to twelve months, [and] Medium Term – that may require up to 24 months.”25

24. This insight is based on KI interviews with leading economists, political scientists and public intellectuals with proven expertise in the field.
F. ANALYSIS

The analysis of the present governance gaps and deficiencies has been organized into three distinct but overlapping categories that relate to (a) measures that enhance transparency and accountability of existing systems, and, based on problems identified in current regulations and practices, (b) measures that can improve macro-political-economic stability. Where even such policy changes are inadequate, a third analytical category has been included (c) to recommend the structural changes that are necessary to achieve the relevant governance targets and goals. Taken together, this framework will form the basis for determining the macro-critical governance benchmarks that the reforms should meet.

A. Measures to enhance transparency and accountability of existing systems that are necessary to produce the required fiscal governance outcomes

The main benefit of transparency benchmarks is that they strengthen vertical accountability. Transparency benchmarks would tend to thwart attempts by politicians or political parties to conceal from the voting public the ways in which government might be serving vested interests over the public interest. This in turn will boost horizontal accountability, empowering institutions such as the judiciary, the anti-corruption agency, the auditor general and the Parliament, to curb irresponsible fiscal management and/or corruption.

1. Maintain a fiscal transparency platform that displays all information related to tax exemptions
   1.1. Publish a full list of all firms receiving tax exemptions through all laws and institutions empowered to offer such tax exemptions, and an estimation of revenue lost to the State
   1.2. Set stricter criteria for tax incentives and exemptions given via the Strategic Development Projects Act (Define a clear tax concession methodology) based on the investment
   1.3. Publish rationales for each project selected under the Strategic Development Projects Act
   1.4. Publish project plans and projected financials for each Strategic Development Project along with the revenue forgone
   1.5. Publicise a full list of beneficiaries of tax exemptions or rebates granted on imports, listing out the specific product categories and the value of the tax concessions received by each of the beneficiaries, with an estimation of the revenue lost
   1.6. Make available an economic analysis relevant to each exemption, evaluating the fiscal case for, and implications of, the exemption

Rationale:

Most countries show an increase in the ratio of government revenue to Gross Domestic Product (GDP) alongside GDP growth. Sri Lanka, however, has had the opposite outcome, and now records one of the lowest levels of government revenue to GDP in the world26. A significant contributor to this unusual trajectory is the high political discretion and low transparency permitted when providing tax concessions with low transparency.

Currently, many tax exemptions are granted using numerous laws, and without analysis or public justification. The Strategic Development Act No. 14 of 2008 provides various tax exemptions up to a maximum of 25 years. Currently, there are 16 identified strategic development projects that enjoy various tax exemptions under this Act. On average, each project enjoys a holiday of 14 years on corporate income tax, 9 years on CESS and 7 years on Port and Airport Development Levy (PAL), Value Added Tax (VAT) and duties specified in the Customs Ordinance.

To enhance effective policymaking, it is important for Sri Lanka to have analyses and reasons, for tax exemptions. Requiring the publication of relevant analyses, itself, could stem the excessive provision of selective tax concessions. Many of the existing concessions could also be reduced, and potentially terminated, based on the rather vague and loose conditions governing them. This would pave the way for sustained increases in tax revenue.

Such changes to the dynamics of tax concession decisions can help improve fiscal outcomes in the medium term.

2. Publish an annual report by 31st March each year, setting out the previous year’s expenditure variations against the approved budget, and explanations for the same

Rationale:
The global open budget survey has shown Sri Lanka as having an uneven and unimpressive performance in terms of budget transparency. In addition to that, an analysis published by Verité Research also shows poor budget accountability. In the words of an economist interviewed: “it is not only that the Sri Lankan government fails to say what it will do, it also fails to do what it says”. Exhibit 2 from a budget transparency presentation by Verité Research shows this for the agriculture and irrigation sector.

In 2021, 27.3% of the Sri Lanka’s employed population report themselves as being in the agriculture sector. This justifies the promises made in each budget on agriculture spending. However, Exhibit 2 shows how seriously short the actual expenditure is from what is promised in the budget. The exceptions (when budgets are met or exceeded) are the years of, or just prior to, a national level election.

Fiscal consolidation has been prioritised afresh in Sri Lanka due to the debt sustainability crisis. The most sensible path to fiscal consolidation on the expenditure side, is to reduce wasteful and less useful expenditure. However, in the absence of expenditure transparency, fiscal consolidation can happen through cutting back on critical expenditure that is important for both growth in future economic productivity as well as social safety and security in the present. The above example shows that Sri Lanka tends to achieve fiscal consolidation – when under pressure – by cutting back on critical areas such as spending on agriculture.

Comprehensive reporting on expenditure variations against the budget, at the earliest possible date after expenditure is finalized (rather than projected), as set out in this proposal, can help mitigate this negative approach to fiscal consolidation in Sri Lanka, and focus fiscal consolidation in directions that help rather than hurt future economic growth.

27. The data was shared with the author by Verité Research from publications that are yet pending.
29. For more information refer to the public finance platform of Verité Research: https://dashboards.publicfinance.lk/budget-promises/
3. Quarterly publication of a revenue report detailing changes to revenue measures that might result in annual revenue loss of 0.1% of GDP

Rationale:
Historically taxes in Sri Lanka have been subject to ad hoc changes. Major tax changes have been introduced without publishing any rationale or analysis on the potential revenue loss. For instance, personal income taxes were revised six times between 2010 and 2023.32

The absence of a requirement to publish any analysis or explanations regarding the revenue impacts of tax policy changes has led to unpredictable, sub-optimal and unstable taxation. The ad hoc reduction of taxes in 2020 are often discussed among economists as a major factor in Sri Lanka spinning into critical loss of government revenue, being downgraded by credit rating agencies, and its debts repayments becoming unsustainable.

This kind of publication requirement would foster the discipline of supporting policy decisions with analysis before they are adopted and enhance public and parliament understanding about the effects of government policies on revenue.

There is also precedence for this being placed within a set of IMF programme commitments. In Zambia and Central Africa the governance diagnostics requested quarterly publications detailing the revenue implications of taxation policies.33


4. Publish follow-up on actions taken to regularise qualified opinions of the Auditor General

Rationale:
By law, all annual reports published by the state are required to include and publish the Auditor General’s opinion or statement alongside the financial statements. Despite the Auditor General highlighting various concerns and offering recommendations in these reports or statements, these insights often go unnoticed, with no subsequent actions being taken.

For instance, the Auditor General has consistently pointed out violations of the fiscal rules established in the Fiscal Management (Responsibility) Act since 2014. However, no measures have been undertaken to address these highlighted concerns.

Therefore, an annual publication that details the follow-up actions taken in response to the concerns raised by the Auditor General would focus attention on resolving persistent financial and fiscal issues that are currently overlooked, and hold institutions accountable for doing so.

There is also precedence for this being placed within a set of IMF programme commitments. In the Democratic Republic of Congo the governance diagnostic requested a publication on “Follow up on auditors qualified opinion”.

5. Implement all the provisions of the Fiscal Management (Responsibility) Act (FMRA), revised as appropriate, and ensure that non-compliance is penalised, since the Act itself has no explicit provisions to deal with non-compliance

5.1. Amend the FMRA, to publish an annual report that sets out tax collection performance, as well as the actual and projected shortfall in tax collection, by all revenue codes up to 8 digits

5.2. Publish all Cabinet decisions, especially in relation to fiscal matters, including the decision-making principles and guidelines being followed, such as those covered in Chapter VI of the Constitution’s “Directive Principles of State Policy and Fundamental Duties”. In addition, reasons and justifications for the decisions taken as well as all documentation on which the decisions were based should be made available to the public

5.3. Amend the FMRA to mandate the timely preparation and publication of annual audited financial statements of all key 52 SOEs

General Rationale:
The non-collection of taxes in Sri Lanka has become a significant concern, particularly due to the lack of public awareness regarding this issue. Over the years, there have been instances where taxes, such as mansion taxes (a new tax introduced alongside the 2016-18 IMF programme) and the casino entrance levy, have remained uncollected, despite being passed into law.

This lack of transparency and consistency in tax collection has allowed vested interests, politicians and government officials to collude in behaviour that systematically reduces government revenue and increases the primary deficit. Comprehensive and timely reporting on tax collection shortfalls as set out in the above proposal can help mitigate this negative impact on government revenue.

Ever since the law was promulgated as a result of pressure from the IMF at the time, key clauses of the Fiscal Management (Responsibility) Act No. 3 of 2003, have been systematically observed in the breach, but since the Act has no mechanism for imposing penalties for non-compliance, systematic non-compliance has gone unaddressed.37,38 Passing an improved Act, potentially in the form of the Public Finance Management Act, and complying with it can be a combined commitment to improved governance that de-risks Sri Lanka’s public finance outcomes.

**Rationale (5.3):**
The timely publication of audited financial statements has been emphasized in IMF programmes in Zambia, Democratic Republic of the Congo, and Mozambique. This action aims to strengthen transparency and efficiency in fiscal governance, addressing deficiencies in financial information quality and disclosure practices within SOEs. In Mozambique, the emphasis extends to publishing annual financial statements with the opinion of the external auditors for the main SOEs.39

Sri Lanka’s 2023 IMF programme includes a commitment to publish audited financial statements for 2021 by 19 major SOEs (the other 33 had already published for 2021) and publish audited financial statements for 2022 by the of June 2023.40 This commitment aims to strengthen the governance of SOEs and enhance their financial transparency.

> “The Cabinet operates without any transparency or accountability, and though this has been going on for a long time, it is in this crisis situation this lack of any openness is most badly felt. No one knows what decisions they take and even how and why. This must change if we are to get out of this mess.” *Key informant interview*

However, as of June 30th, 2023, only 11 out of the 52 Key State-Owned Enterprises identified by the Ministry of Finance had released their audited financial reports for the year 2022.41 This progress falls short of Sri Lanka’s commitment to the IMF, which entails publishing financial reports for all 52 key SOEs by the end of June 2023. Consequently, this IMF condition has not been fulfilled, despite the critical role that the publication of financial information plays in enhancing transparency and accountability within State-Owned Enterprises.

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38. For instance, clause 3(a) states that one of the key objectives is the “reduction of government debt to prudent levels, by ensuring that the budget deficit at the end of the year 2006, shall not exceed five per centum of the estimated gross domestic product and to ensure that such levels be maintained thereafter.”
To rectify this shortfall, amending the Fiscal Management (Responsibility) Act (FMRA), No. 3 of 2003, to mandate the timely preparation and publication of annual audited financial statements for all 52 key State-Owned Enterprises (SOEs) is imperative. This step is vital in aligning with Sri Lanka’s commitment to the IMF programme and ensuring transparency and efficiency in fiscal governance within the SOE sector.

The next recommendation concerns the **superannuation funds**, including the largest of its kind, the Employees’ Provident Fund (EPF), where, as described below, there is a clear conflict of interest in relation to the Domestic Debt Reconstruction legislation, euphemistically termed Domestic Debt Optimization, which was approved by Parliament on 01 July 2023.

### 6. Limit budget allocations under the development activities of the Department of National Budget (discretionary spending) to 3% of total expenditure

**Rationale:**
Section 6(1) of the Appropriation Act No.30 of 2021 allows for funds placed under the development activities of the Department of the National Budget (NBD) to be transferred to any other head in the schedule subject to the order of the Secretary to the Treasury, Deputy Secretary to the Treasury or the Director General of the NBD.42 Parliamentary approval for such transfers is not required and Parliament will only be notified via the submission of a report within two months of such a transfer. Thereby the law allows funds under the development activities of the NBD to be expended in a discretionary manner by the government, leading to the terming this allocation as a “discretionary budget” or a “slush fund”.43 The allocations made for this budget head were significant during the period 2015 to 2018 as is evident in the exhibit.

**Figure 2: Discretionary Budget Balance as a percentage of total expenditure over the years**

<table>
<thead>
<tr>
<th>Year</th>
<th>Budget Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>20.0%</td>
</tr>
<tr>
<td>2016</td>
<td>28.7%</td>
</tr>
<tr>
<td>2017</td>
<td>18.0%</td>
</tr>
<tr>
<td>2018</td>
<td>11.8%</td>
</tr>
<tr>
<td>2019</td>
<td>5.3%</td>
</tr>
<tr>
<td>2020</td>
<td>4.7%</td>
</tr>
<tr>
<td>2021</td>
<td>1.5%</td>
</tr>
<tr>
<td>2022</td>
<td>5.8%</td>
</tr>
</tbody>
</table>

Note: Total expenditure for 2022 and 2023 are the revised budget and estimates respectively
Source: data and analysis provided by Verité Research, Sri Lanka

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The problem of increased allocation for the discretionary budget was taken note of in the 2018 and 2019 reports of the Committee on Public Finance (COPF). It noted that this loophole of discretion had been abused to manipulate the budget process and use funds for purposes other than what was anticipated in the budget. To contain this abuse the report of the COPF at that time requested that this aspect of the budget should restricted to a low percentage of total expenditure. Therefore, this recommendation is also consistent with that request of the COPF.

7. Reduce corruption and waste in relation to the benefits provided to political leaders and senior bureaucrats through enforcing systems of transparency and accountability

7.1. Annual publication of a vehicle registry owned by each ministry by vehicle type

Rationale:
The 2018 reports from the Committee on Public Finance (CoPF) underscore a persistent issue with regard to budget allocations for vehicle acquisitions. The 2018 budget had a twelve-fold increase in the funds allocated for vehicles. The Ministry of Finance (MOF) explained the increase as being due to a plan to procure a substantial number of utility vehicles.

The CoPF asked the MOF at that time have “higher disclosure standards” to avert misleading budget allocations, particularly regarding the notable escalation in military vehicle acquisitions. This recommendation came after the CoPF secured from the MOF a database of vehicles, which had not been available in previous years. Despite the request of the parliament committee, this database is currently not being proactively disclosed – leaving much space for mismanagement of high-cost movable assets.

Mandating the publication of this database of all state-owned vehicles can enhance visibility, improve management of the assets and reduce wasteful expenditure – leading to better public finance outcomes.

There is also precedence for this being placed within a set of IMF programme commitments. In Zambia, Moldova and Mozambique, the governance diagnostics requested the publication of all government owned assets (including real estate assets).

8. Address the politicization of the public service:

8.1. Establish transparent selection, assessment and promotion criteria for ministry secretaries and other senior public servants through an open public dialogue, and implement these criteria uniformly within six months

Rationale:
As has been pointed out ad nauseam “The progression of Sri Lanka’s economy is dependent significantly on the performance of the public sector. A more efficient and productive public sector is an absolute need in driving forward Sri Lanka’s economic recovery.” The Steering

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Committee on Public Sector Reforms of the Ceylon Chamber of Commerce has identified that the “appointment, evaluation and removal” of the most senior public servants – ministry secretaries – needs to be free of political influence or pressure if basic professionalism is to be maintained, which is currently at the discretion of the President.

“There is no light at the end of the tunnel. You can’t do your job at this level without getting the ‘rub’ from the man in charge.” KII

Ministers, and even the Prime Minister or President, should not be permitted to hand pick their key officials because this leads to bias and partisanship on the one-hand and a feudal servility and personal dependence on the other. It is only through a merit-based system that the integrity of the public service can be re-established, and in turn it is only through such a renewed public service that the present culture of cronyism and the seeking and delivering of special favours can be defeated. Once a patron-client relationship has been developed between a politician and a public officer, it is virtually impossible to restore impartiality because “Once a politician has obliged [in] this way the officer is obliged to reciprocate and couldn’t refuse demanded political favours.”

9. Publish data related to all secondary market transactions of the Employees’ Provident Fund (EPF), with adequate detail to assess off-market rates of sale and purchase (as analysed by the forensic audits of the EPF published in 2019)

9.1. Ensure a clear separation between the Central Bank’s (a) management of the EPF and other superannuation funds and (b) the management of the debt auction, in order to prevent a manifest conflict of interest

9.2. Place in the public domain the relevant data and analysis that justifies the unorthodox local currency domestic debt restructuring conducted in Sri Lanka

9.3. Amend the laws relating to the issuing of local Treasury Bills and Bonds in Sri Lanka to embed the pari passu principle and rebuild confidence in local currency debt

Rationale (9.1):
The EPF is Sri Lanka’s single largest fund and is managed by the Central Bank of Sri Lanka. The majority of private sector salaried employees are mandated to place a portion of their income as retirement savings in the fund. Due to the high inflow of deposits, the EPF is the largest single holder of government treasury bonds, holding 36%.

The Central Bank of Sri Lanka is both the administrator of the EPF as well as the entity that has determined that only the EPF should be subject to restructuring of its local currency sovereign bonds. This action, loaded with a conflict of interest, has made it clear that there needs to be a more independent and transparent governance structure for the EPF.

48. Ibid.
49. KII observations of experts in the field.
The flawed management of the EPF and resultant injustice is clear from the fact that the decision to cap interest earned by deposits in the main superannuation funds, including the EPF, at 9% per annum has been made while the Central Bank’s own EPF scheme continues to earn an annual interest which is significantly higher.54

The infamous, politically charged scandal which took place during a treasury bond auction in 2015, colloquially referred to as ‘the bond scam’, involved secondary market transactions of the EPF where government debt was sold at high yields (lower prices) to private secondary market dealers, who then immediately resold it at lower yields (higher prices) to the EPF. The forensic audits of the Central Bank completed in 2019 exposed this as a systematic practice. This renders debt auctions suboptimal because the expected benefit to the government in reducing the cost of debt through the EPF’s participation in the primary auctions is channeled to benefit secondary market players instead. The result is that the cost of debt to the government increases and the returns to the EPF reduce. The consequences on the cost of debt can be significant, as the EPF is a fund of LKR 3.38 trillion at present, which is 25.6% of the entire LKR debt of the government (as of end 2022).55

Timely publication of data related to all secondary market transactions of the EPF has multiple benefits. It will help proactively identify irregularities, enable better oversight, safeguard the retirement savings of workers, and reduce the cost of government borrowing – which is a critical need for debt sustainability and economic recovery. There is presently a Bill that has been introduced to parliament setting out a format for the publication of EPF investments, in an appropriate format. This makes the implementation of this proposal feasible in the near term.

“If the Central Bank had decided to tamper with the benefits received by a private bank or other financial institution, the directors and shareholders of that bank would have raised a huge protest and made official complaints against this decision. The difference with the EPF is that the “directors” of the EPF are also the Central Bank, so there is no protest or complaint. Surely this is wrong? And, I have heard that their own provident fund is much more than what they have decided we will get. Can anyone say that this is correct?” Key Informant Interview

Rationale (9.2)
The Domestic Debt Restructuring (DDR) policy recently announced by the Government of Sri Lanka has created history by exclusively targeting contributory superannuation funds for local currency debt restructure.56 That is, instead of targeting holders of a particular class or set of bonds that were released to the market at very high yields (exceeding 30%) in 2022, the government has targeted only the holdings of those bonds in superannuation funds, excluding all other financial institutions and individuals.

The Employees Provident Fund (EPF) is the largest such fund, with 2.4 million active member accounts (with a total of 22.4 million passive and active member accounts).57 The Central Bank

54. When asked about this conflict of interest and self-contradiction, the Governor of the Central Bank stated on 09 July 2023: “We have identified this and to address this aberration the Monetary Board has decided to review this and from next year to change the policy in some way.” [emphasis added], available at: https://economynext.com/sri-lanka-central-bank-to-change-its-pension-funds-policy-125566/
of Sri Lanka is by law the Trustee of the EPF\textsuperscript{58}, and is using its legal power to submit “voluntarily” the EPF to the highly unorthodox debt restructure invitation (at the time this document is being published). However, in addition to having a conflict of interest in analyzing the merits of this unprecedented DDR action, which the Central Bank itself designed, it has also failed to make public whatever data and analysis that it utilising to justify the decision.

The proposal seeks to ensure democratic expectations of public financial accountability, on a matter that has caused huge vexation among the population at large. Providing the public with transparent and rigorous analysis to demonstrate at least the technocratic merits of the decision that has been taken can shore up some level of trust and acceptance, which is otherwise in a precipitous freefall.

Political instability occurs in situations of grave injustice that is forced upon large sections of the population, without democratic recourse to address grievances. Therefore, complying with this proposal will also mitigate three other risks: (1) growth in opposition to the current plan for economic recovery laid out in the IMF program, which current enjoys the support of at least 28% of the population\textsuperscript{59}, (2) generate a political electoral demand to reverse this action in the future, even it was justifiable based on data and analysis which is currently suppressed, and (3) galvanize larger political instability leading to larger economic instability in Sri Lanka.

If the data and analysis is not being provided because it fails the test of reasonable analytical justification, then the recommendation should be to reverse the unorthodox DDR action as soon as feasible.

\textbf{Rationale (9.3)}

The way the local currency debt restructuring was carried out in Sri Lanka targeted only the superannuation funds in a manner that is unprecedented in past domestic debt restructuring episodes in the world.

This sets up a heightened risk that the government could act in a manner that is arbitrary and ad-hoc in targeting local law debt treatment in the future as well. Therefore, it is a precedent that can increase the uncertainty and risk associated with local currency lending to government, and result in the borrowing costs of the government increasing unnecessarily, as the market recognizes and prices in the increased risk.

The \textit{pari passu} principle written into the laws governing international debt issuances gives confidence to those that invest in sovereign bonds that they will not be treated unequally and arbitrarily in the case of a debt restructuring episode.\textsuperscript{60} However, the local laws governing debt issuance in Sri Lanka do not have similar inbuilt protection.

Changing the laws relating to the issuing of local currency bonds to embed a \textit{pari passu} principle can have some salutary effect in reducing the fear of future actions that are arbitrary and ad-hoc in situations of debt stress. Failure to address this concern with regard to governance can have a knock-on effect on the price of borrowing in local currency with negative implications for debt sustainability in the future.

\textsuperscript{58} Sri Lanka: Employees’ Provident Fund Act, Section 5, available at: https://epf.lk/?page_id=246

\textsuperscript{59} The data was shared with the author by Verité Research, from a national survey conducted, the results of which will be in the public domain in mid September 2023.

\textsuperscript{60} While there is inadequate research on this area, especially as it relates to the domestic debt restructuring process, Rodrigo Olivares-Caminal (2013) “The pari passu clause in sovereign debt instruments: developments in recent litigation” provides an interesting account of the legal landscape on the application of this principle.
10. Ensure compliance with proactive disclosure requirements outlined under section 9 of the Right to Information Act No. 12 of 2016 which mandates the minister responsible for a project to disclose information relating to the project three months before commencement

Rationale:
The RTI Act grants Sri Lankan citizens the right to access information held by public authorities and empowers citizens to hold elected and public officials accountable. Proactive disclosure refers to the publication of information by public authorities without an official request. Compliance with proactive disclosure requirements is critical to combatting corruption by increasing transparency in government and facilitating greater accountability in the use of public funds.

Proactive disclosure also minimizes associated costs and administrative procedures and lessens the burden of complying with information requests under the RTI Act and. Proactive disclosure requirements of the RTI Act are outlined under sections 8, 9 and 10 and Regulation No. 20.

Proactive disclosure requirements under Section 9 of the Act are particularly relevant for public finance. It mandates the minister responsible for a project to disclose information relating to the project three months before commencement.

Despite these legal mandates for better governance, research conducted by Verité reveals that government compliance with proactive disclosure requirements remains low. In 2022, Verité conducted an assessment of 55 public authorities to evaluate their compliance with online proactive disclosure requirements and subsequent regulations outlined in the RTI Act.

Verité’s project-wise assessment of information disclosure under section 9 found that only 18% of information was disclosed in 2022, with a minimal increase to 25% in the subsequent 2023 assessment. The assessments also found that when information was disclosed by government agencies, the limited information disclosed was primarily provided in English, depriving access to information for non-English speakers who account for 69 per cent of the population.

An annual report by the auditor general, measuring compliance on proactive disclosure requirements under section 9 of the act can contribute to greater focus on improving the feasibility, planning and timely implementation of high-cost projects. This is likely to have positive consequences on public finance and debt management.

63. Ibid.
11. Quarterly publication of a complete set of updated information on public debt

Rationale:
A significant factor, which contributed to the government of Sri Lanka avoiding democratic pressure to improve fiscal discipline on debt, was that it was able to conceal the full extent of the debt. It did this through incomplete reporting. It was thereby able to mislead the public about the true extent of its debt.

The standard reporting on debt is focused on central government debt and debt service, rather than providing a complete view of public debt. A case study by Verité Research showed that prior to 2015 the government was able to report lower debt (at the central government level), by shifting the debt, arbitrarily, to the books of state-owned enterprises (SOEs).66

The government also used SOEs as vehicles to borrow, and accumulated large amounts of debt in them, which then substituted for funds and payments due from the government. This past practice heightened the debt crisis. According to the Central Bank Annual Report (2022), “From December 2022 onwards, several outstanding project loans, which were previously classified under entities such as the Ceylon Electricity Board, Airport and Aviation Services Ltd., and Sri Lanka Ports Authority, were absorbed into central government debt.” These loans, after being transferred onto the central government’s books, amounted to a value of USD 3,826.1 million or LKR 1,389 billion at the time of transfer.67

Under the current IMF program, Sri Lanka has committed to publishing a quarterly debt bulletins68. These bulletins provide information on public debt, including a breakdown of external debt by creditor name.69 This level of detail is not usually published in Sri Lanka outside of an ongoing IMF programme.

The recommendation is that Sri Lanka amend its financial reporting laws to include an obligation to publish quarterly, a complete set of updated information on public debt. The recommendation is also that the content of the report should include the following five elements (drawn from recommendations by Verité Research, partly based on recent improvements made by Ghana to its laws on reporting of public debt):70 (1) information on foreign debt disbursements and repayments; (2) information on domestic debt issuances and repayments; (3) information on movements in debt to GDP ratio; (4) weighted average yields by debt instrument type and creditor type; (5) the transfer of debt between the state and state-owned enterprises (SOEs).

Additionally, the Central Bank of Sri Lanka should be adopting the practice of releasing its Annual Public Debt Management Report, not more than 3 months after the end of each year. Presently, in September 2023, the report for 2022 is yet to be published.

The thirteenth recommendation addresses the crucial area of procurement, including unsolicited proposals that are Cabinet-approved on a case-by-case basis on the pretext of urgency.

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12. Maintain an online platform that publishes all significant public procurement contracts when cumulatively above LKR 100 million to any set of connected suppliers

**Rationale:**

High value procurements through unsolicited proposals, poor governance processes, tied contractors, and weak application of due process (especially in the power sector, roads and highways, and other major infrastructure), have been a significant source of fiscal leakage in the past. Many of these have also been debt financed. Reducing these leakages will reduce the space for fiscal profligacy, improve the primary deficit and reduce vulnerabilities that resulted in bringing about the debt crisis in Sri Lanka. Sri Lanka’s current IMF programme contains a more generally worded version of this action.

At present, https://promise.lk/ serves as a portal that contains tender announcements, and allows supplier registration. However, it does not contain the necessary information for any public accountability about the suppliers who submitted bids, suppliers to whom tenders are awarded, the value of the award, or the status of implementation of the relevant work. As it stands, therefore, it remains an inadequate platform to curb corruption through public and regulatory oversight.

However, it should be cautioned that the existence of a platform will not of itself ensure that the crucial factor of compliance and/or due diligence will be forthcoming. Sri Lanka’s current experience in this regard is one of deliberate disregard for such regulations and related requirements accompanied by impunity. For instance, even though the current proactive disclosure provisions under the Right to Information (RTI) legislation mandate reporting on large-scale infrastructure projects, actual compliance is 11% for present contracts. Furthermore, even though there is provision for blacklisting contractors, and given clear evidence of various types of defaulting and malpractice, only 02 entities have been blacklisted since 2006.

Hence, the issue that needs to be addressed is not only the mechanisms for public reporting but the creation of an enabling environment and the attitude change required to ensure that these mechanisms will be used effectively and impartially.

The next set of recommendations focus on Asset Declaration, to ensure that the existing deeply flawed practices are transformed to become meaningful and enforceable.

> “I'm not sure how declaring their assets will make politicians honest or non-corrupt. They will surely find a way of cheating this system too. What about family assets or fake companies? Is there not a way that Asset Declarations are verified or audited, and penalties imposed for false information? Also, if they have made their money already, how does this help? Can we not check their assets over the last, say, 25 years?” — Key Informant Interview

73. See also https://www.open-contracting.org/resources/quickstart-guide/, https://docs.google.com/document/d/1Ys1QqLdRdnvUbPB-AiQ3NbhP50oJmxkCQ/edit?pli=1, and https://www.open-contracting.org/resources/open-contracting-legislative-guide/
13. Ensure impartial implementation of the legal framework in the Anti-Corruption Act (ACA) for public access to asset declarations of persons specified therein, and promulgate regulations for its enforcement.

Rationale:
Civil Society Organisations (CSOs) in Sri Lanka have been underscoring the need for a public database on assets held by politicians and advocated for public access to be granted.75

The ability of high-level decision makers to accrue wealth privately without public detection increases their capacity to compromise fiscal revenue for the benefit of vested interests. Revelations such as the Pandora Papers exposé in 2021 demonstrate how adequate transparency and accountability on assets and liabilities and of beneficial ownership of entities by public officials could assist in proving or disproving conflicts of interest and amassing of wealth by public officials through bribery and corruption 76 With the new Anti-Corruption Act No. 9 of 2023 coming into operation effective from August 11, 2023, this change has taken effect, and it is mandatory for public officials, including members of parliament, election candidates, and the president to declare their assets.77

The Act requires the Minister to make regulations regarding the effective and timely implementation of the centralized electronic system, the form in which asset declarations are to be submitted to the system, the verification process, and details of what constitutes assets and liabilities, etc., which should be done within a 6-month period. Adequate resources must be immediately allocated to the Commission in order to build and set up the centralized electronic system, along with the required human resources and training.

14. Hold national elections in accordance with the constitutionally mandated timeframe:
14.1. Hold postponed Local Government Authorities (LGA) and Provincial Council (PC) elections within the next 3 months
14.2. Increase the financial independence of the Election Commission

General Rationale:
Ensuring national elections are held within the constitutionally mandated timeframe is a critical part of a democracy. Elections provide people with a voice and can bring about political stability by fostering policies that are more just and equitable. The absence of a publicly elected head of state adds to the crisis of legitimacy which needs an election to silence critics and obtain an unequivocal mandate and acceptance of how the economic costs and benefits are shared/distributed within the Sri Lankan society.

“Without elections nothing makes sense. I will only support other changes if you write in your report that the elections must come first. Otherwise, all this is a conspiracy of the political class.” View expressed at three FGDs

Not to have timely elections will also impact Sri Lanka’s international reputation, cause concern among potential investors, increase the risk premium on accessing debt, undermine governance, and have other knock-on implications on fiscal and macroeconomic stability of the country. The absence of any level of local and/or regional governance representation at this time in the country is a game changer in terms of public acceptance and ownership of the proposed reforms. In terms of elected representatives, there is neither a devolved provincial administration nor a decentralized local government representation, and this is unsatisfactory by any standard of governance.

Rationale (14.1)
The LGA and PC elections have been pending for a prolonged period and these elections are aimed for reconciliation and power devolution. The delimitation issued which could block the election proceedings could be resolved with amendment to the existing election law.

Rationale (14.2)
This recommendation is necessary to ensure the implementation of a fixed election calendar. It also prevents the Election Commission from being held to ransom by Parliament, thwarting the overwhelming public demand for the new reforms to be subjected to seeking and obtaining a clear mandate.

15. Ensure enforcement of election campaign expenditure monitoring offences by setting up an electronic system.

Rationale
Regulation of election campaign financing is necessary, to bring more transparency and accountability to the issue of money in politics, thereby reducing chances of concerns such as undue influence, excessive expenditure, abuse of public resources, and vote-buying. Regulation is also needed, to ensure that underrepresented groups are not further kept out of political life due to the lack of access to finances.78

The Regulation of Election Expenditure Act No. 03 of 202379 contains provisions that require candidates, political parties, and independent groups to make a disclosure of their income and expenditure to the Election Commission within 21 days of the declaration of an election result, and mandates that the Commission should make such information available for public scrutiny upon the payment of a fee, within 10 days thereof. The law imposes a limit on election expenses, but imposes no limit on campaign contributions, but only bans contributions from certain sources.80

While there are several weaknesses in the law, the major flaw remains that there is a heavy dependence on citizens and watchdogs to scrutinize the information filed by the obligated entities. Offences have been stipulated, but no mechanisms or system is required to be set up, to ensure that violations are detected.80 To do so, the Election Commission should set up an electronic system that can centralize the data, and can be used to systematically detect red flags for violation of the law.81 The current law does not require the setting up of such a system, but there is no legal barrier to the Election Commission setting up such a system.

80. Newsfirst Sri Lanka (28 March 2023), available at: https://www.youtube.com/watch?v=_zj_BmMCZi8
The next set of recommendations focus on enhancing the accountability and performance of legal actions against corruption and the abuse of power.

16. **Ensure that the Commission to Investigate Allegations of Bribery Or Corruption's (CIABOC) readiness to investigate and apply the law effectively and equally, is indicated through the exercise of its new powers:**

16.1. Adequately resource the CIABOC, including capacity assistance from development partners

16.2. Annually report on the number of inquiries, investigations or cases commenced exercising ex mero motu powers of CIABOC

16.3. Annually report the number of cases filed using new powers of CIABOC

1. Instances where assistance of any public authority or experts were obtained.

2. Number of examinations of laws, practices, procedures conducted of a public authority to discover conduciveness to corruption.

3. Number of joint investigations conducted, and number of instances teams were established for joint investigations in and outside of Sri Lanka.

4. Number of warrants issued by the Director General and arrests without warrants made.

5. Number of investigations and cases commenced on non-conviction-based forfeiture, including the number of convictions secured.

6. Number of instances and nature of codes of conduct introduced by CIABOC, to be adhered to by the private and public sector.

7. Number of instances where government departments or public authorities were advised of practices or procedures, and monitoring of the implementation of such measures.

8. Number of referrals received from a public authority or a law enforcement authority, where an offence under ACA may have or is suspected to have been committed.

9. List of rules made by CIABOC.

10. Number and nature of officers, officials and employees, of local government service, local authority, public service, public corporation and state audit service appointed to assist efficient discharge of CIABOC’s functions.

16.4. Commence prosecutions on at least 5 high-profile cases of grand corruption involving substantial state resources within 12 months of operationalisation of the ACA.

**General Rationale:**

The lack of action on corruption incentivizes corruption and the consequent fiscal impact. Transparency International’s Corruption Perceptions Index has demonstrated that Sri Lanka has been mired in corruption-related scandals for many years, with little positive change discernible.

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80. Newsfirst Sri Lanka (28 March 2023), available at: https://www.youtube.com/watch?v=_zj_BmCZ18
Rationale (16.1)
As part of Sri Lanka’s commitments in the current IMF programme, Sri Lanka’s main anti-corruption laws were revamped. The new Anti-Corruption Act No. 9 of 2023 which will come into effect from 15th September 2023 incorporates many best practices of the UNCAC.

The ACA is a key element in any viable anti-corruption strategy and corrects many of the problems in the 1954 Bribery Act, but “it requires both an additional Act to cover the ‘proceeds of crime’ to draft which a committee has been appointed, and a separate body to prepare regulations, terms of reference, operational guidelines, recruitment processes to ensure that CIABOC functions smoothly.”

Iraq’s 2016 Extended Fund Facility programme of the IMF required the government to sign agreements with UNDP to provide staff that supported the investigation of significant cases of corruption, and assisted in capacity building of the Integrity Commission.

One often-cited example of UN collaboration in building an effective corruption-busting institution is the example of the International Commission against Impunity in Guatemala (CICIG). This resulted from the Guatemalan government requesting the United Nations (UN) to establish an initiative that would assist local institutions in investigating, prosecuting, and dismantling powerful post-conflict criminal networks.

The CICIG, which is a potential model for Sri Lanka, had an impressive track record. It assisted in filing more than 120 cases in the Guatemalan justice system, implicating more than 1,540 people. Its relevance is that it demonstrates the power of external assistance to overcome the problem of local institutions being low in capacity and highly vulnerable to political influence – as they are in Sri Lanka.

Rationale (16.2)
CIABOC’s willingness and ability to apply the law equally to all without fear or favour, can enhance degraded public faith, increase accountability and afford an opportunity to prove its commitment to its renewed mandate. While, the weaknesses including delays in the judicial process, prevailing culture of impunity and fear, inadequate powers may have contributed to low investigation and conviction rates, the institution has also failed to show its readiness and willingness to fully utilize available powers. For example, under the previous CIABOC law, the number of instances in which it exercised its ex mero motu powers from 2015 when the power was given, up to 2017, is zero.

Rationale (16.3)
Marked progress in investigations, prosecutions and convictions displays the impact of laws and their effective enforcement. Prosecutorial and investigative success can be measured in an objective manner by setting up measurable proxy indicators. With the renewed mandate and new wide powers granted to the CIABOC, the institution now has enhanced capacity to conduct investigations and prosecutions in a more effective and efficient manner. Setting up investigative and prosecutorial targets based on the exercise of new powers can be a modest assessment of the institution utilizing its new powers and means to enhance capacity, the lack of which had been claimed to hinder investigations, prosecution, and its ability to secure successful convictions.

84. Key Informant Interview.
Rationale (16.4)

CIABOC’s track record has been less than impressive. It has been pointed out in Parliament that “the Bribery Commission had filed 69 cases in 2021 but had withdrawn 42. In 2022, it filed 71 cases but withdrew 43.”There is no publicly available information of such withdrawn cases being refilled. Efficient and accountable implementation of the law to prevent and reduce the number of cases, especially against those who are influential public figures, from being dismissed or withdrawn due to mere technicalities and lack of evidence, can assist the key anti-corruption agency to restore the dampened public trust.

The corruption–related governance concerns on the environment have proved to be very costly, even catastrophic, in the recent past. Hence, the need for transparency and open public access to Environment Impact Assessments (EIAs).

17. Publish all documents related to Environmental Impact Assessments (EIAs) for all large-scale infrastructure projects in an online portal to ensure transparency

Rationale:

Presently, there is limited access to information on EIAs, which impedes public engagement and sound decision-making. An online portal will encourage proactive disclosure of key EIA documents, including scoping reports, public comments, and technical evaluation committee reports. This will significantly improve the status quo and also contribute to furthering a global priority through better environment-related governance in Sri Lanka.

Making EIAs public is crucial for several reasons. Firstly, public access to EIAs promotes decision-making that better safeguards the environment and positively impacts communities and stakeholders. This fosters better investment decisions, lowers the costs of mitigating harm, and improves the medium- and long-term outcomes for the economy. It also has knock-on benefits in the global commons. EIAs being public and the government taking greater care to minimize the impacts on the community also help reduce public resistance to projects. As this helps avert any potential social and political instability, it can also contribute towards medium-term economic stability in Sri Lanka.

18. Protect and uphold civic space for citizen participation in all appropriate aspects of governance, including in democratic dissent and protest, where they exercise their fundamental rights as enshrined in the Constitution

Rationale

It has long been accepted as a truism that both an enabling environment and a safe space are basic requirements for meaningful citizen participation and real ownership of economic reform and recovery processes. In turn, the absence of such pre-conditions will inevitably lead to the non-sustainability, even failure, of the reform agenda. Especially in the current context

where there is a crisis of legitimacy of the current government and where the memory of the crackdown on Aragalaya (‘public uprising’ in the Sinhala language) protestors is still fresh in the public memory, this recommendation becomes macro-critical and helps set up the foundation for the other more specific recommendations.

In addition, as described above, a number of questionable and repressive draft laws, such as the NGO Bill, the Broadcasting Bill and the Anti-Terrorism Bill have been mooted, while other draconian or selectively-enforced legislation, such as the PTA and the ICCPR Act have already drastically diminished the civic space for the exercise of fundamental rights, including the freedom of expression and association, ensuring the rights of citizens to question or dissent, and to hold the decision-makers accountable is critical for the legitimacy of the reform agenda.

Hence, while this recommendation remains necessarily overarching and general, it is in many ways a pre-condition for the more specific recommendations that follow and should be seen as foundational.

The next category contains twelve governance benchmarks, the first three of which are directly related to the current taxation and revenue collection regime.

At the outset it needs to be recorded that the FGDs and KIIs foregrounded a general dissatisfaction among professionals against the post-IMF tax reforms, which have become one of the key reasons for significant brain drain, accounting for the imminent collapse of the entire higher education system in Sri Lanka. For instance, of a total approved academic cadre of 12,992 in the 17 state universities, only 6,548 are currently employed, resulting in an unfilled vacancy rate of 49.6% and counting. In 2023 alone, nearly 1000 resignations of academics have been recorded. Similarly, the exodus of medical doctors has crippled the national health system.

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91. Maneesha Dullewe (10 June 2023), “Broadcasting Authority Bill: Self or co-regulation the way forward?”, available at: https://www.themorning.lk/articles/2CjPwOnx9RLLOpAj4AR
93. Ibid.
94. Centre for Policy Alternatives, “Submission by the Centre for Policy Alternatives”, available at: https://tbinternet.ohchr.org/_layouts/15/TreatyBodyExternal/DownloadDraft.aspx?key=TmEf2qU3ZBl8xXcekZ2lWE06e45vNuJsoAXyVB+sGLLm/qjFq4mPdz7xKvByqOzTFqcszlIPDzVzZJw9IzA==
95. Based on The Morning (24 August 2023), “UGC notes need to recruit 1,000 academic dons”, available at: https://www.themorning.lk/articles/kUlWCcJ5sJHuJiCGrQ and Federation of University Teachers’ Associations (FUTA) data.
B. Measures to improve macro-political-economic stability and sustainability

Where current legislation is manifestly inadequate to address financial mismanagement and potential corruption, this second category of recommendations identifies policy changes that are required, either to plug existing gaps and/or to target new concerns. This category of recommendations stems from the fact that the present legal and administrative regime is unable to address the key macro-critical economic governance demands needed for the reform agenda.

19. Amend all tax-related legislation to remove the excessive use of discretion for taxation changes without approved schemes

Rationale:
Certain taxes in Sri Lanka, such as the Special Commodity Levy (SCL), violates the principle of parliamentary control over public finances set out in the constitution. This is recognised in a Supreme Court judgement in relation to another law with an identical level of discretion, which was challenged prior to enactment. Nevertheless, the SCL persists in its current form because Sri Lanka does not allow for post-enactment review of laws (passed quickly without challenge).

For example, the SCL Act grants the minister full discretion to announce tax changes, for immediate implementation, through a gazette notification. This enables benefits to be channelled to vested interests, creating opportunities for corruption. Parliament subsequently disallowing the tax change does not impact the tax reduction provided up to the parliamentary vote. A controversial reduction of tax on sugar in October 2020, colloquially referred to as the ‘sugar scam’, brought this abuse of discretion into public focus. Research estimates by Verité Research show that the huge revenue loss to the government (LKR 59 billion by end-2022) mostly accrued as surplus to the suppliers, rather than to the consumers.

Other legislation that is vulnerable to tax changes without the approval of Parliament includes the Colombo Port City Commission Act and the Value Added Tax Act. Presently, there are bills that have been introduced to parliament to remove the undue discretion granted in setting SCL and VAT, which makes it possible to implement these actions in the near term.

20. Fully implement the price and tax measures anticipated in the Framework Convention on Tobacco Control (Article 6), to which Sri Lanka is a signatory

Rationale:
Excise taxes on cigarettes and tobacco in Sri Lanka are a large source of revenue — accounting for over LKR 100 billion. However, successive governments have failed to properly index the tax to inflation and have allowed leakages by not implementing regulations against forestalling. The appropriate actions on tobacco taxation are already laid out in the guidance on implementing Article 6 of the Framework Convention on Tobacco Control (FCTC), to which Sri Lanka has been a signatory for over 20 years.
Failing to institute an indexation scheme on cigarette taxation has prevented the expected revenue generation from cigarette taxes. This was a proposal made as part of the 2019 budget to keep cigarette affordability on par with nominal GDP. The relevant minister used his discretion to not implement the indexation policy. This resulted in a foregone revenue of LKR 85 billion from 2020-2022 and will result in a further revenue erosion of tens of billion in 2023.100

The failure in implementing indexation and regulatory measures on tobacco taxation has led to ad hoc policies on taxation and forestalling by suppliers to undermine government revenue. For example, the 2023 budget anticipates LKR 137-140 billion in revenue from excise taxes on cigarettes. However, analysis published by Verité Research shows that the government has set out a tax increase that will only collect approximately LKR 99 billion. Therefore, the budgeted revenue targets will be missed by about LKR 40 billion on this single excise tax alone.

21. Achieve an annual reduction of 10% in the five-year average of tax exemptions (by number and/or value) in recommendations 1.1 and 1.2

Rationale:
Sri Lanka’s economic recovery and debt sustainability depend on increasing government revenue. Tax exemptions have been identified in proposal 1 as a reason for reduced revenue as they can override public interest and even IMF commitments.

In October 2022, after signing the IMF staff level agreement, the government instituted sharp increases in income taxes and public utilities’ tariffs. Nevertheless, it also proceeded to grant 12-year tax concessions to a corporate that was already well established in Sri Lanka.101 No rationale or analysis was provided for these concessions in parliament. Therefore, transparency measures alone may not curb the power of vested interests to erode fiscal performance through tax concessions.

Setting a performance target as proposed allows the government to gradually retire the existing tax concessions. It also formally limits the new tax concessions that can be provided. Failure to do so will transfer the burden of reduced government revenue to Sri Lanka’s creditors, who can then be forced to restructure debt.

22. Set up a Public Debt Management office external to the Central Bank

Rationale:
The infamous “bond-scam” exposed huge corruption in Sri Lanka, which hitherto had not focused on the punishment of the perpetrators. The circumstances were made possible by the compromised way the public debt department was found to be working in the Central Bank.102

The aim of a specialised Public Debt Management Agency (PDMA) would be to eliminate potential corruption by enhancing transparency, competence and efficiency of overall public liability and debt management in Sri Lanka. The PDMA should possess significant operational autonomy and be free of political and private sector influence.

100. Verité Research (2023), “Will the Increase in Cigarette Taxes Meet Budgeted Revenue?”, available at https://publicfinance.lk/en/topics/will-the-increase-in-cigarette-taxes-meet-budgeted-revenue-1872923079#:~:text=However%2C%20our%20calculations%20show%20that,excise%20taxes%20will%20be%20required
A PMDA, external to the Central Bank, offers several advantages. This separation clarifies that debt management is not synonymous with monetary management, ensuring clear roles for the central bank and the PMDA.\textsuperscript{103} It allows for professional debt management with the goal of minimizing the cost of debt. It should be tasked with formulating medium-term debt strategies, annual borrowing plans, and decision-making on auction cut-offs. Additionally, the PDMA should oversee both domestic and international financing decisions.

This proposal should be incorporated easily as the government has already committed to establishing a PMDA by December 2023, in alignment with international best practices, with full implementation expected by December 2024, as per Sri Lanka’s 2023 IMF programme.\textsuperscript{104} In fact, the establishment of a public debt management office has been a recurring budget promise, particularly in 2017 when the establishment of an Independent Debt Office at the General Treasury received approval from the Cabinet of Ministers.\textsuperscript{105} A proposal to establish a National Debt Management Agency was most recently put forward in the “Interim Budget” of 2022.\textsuperscript{106}

23. Strengthen the National Procurement Commission for better oversight on public procurement and pass the Procurement Guidelines of 2019 with public consultation

Rationale:
Competitive bidding is considered the best practice in most countries for public sector procurement process. However, Sri Lanka has repeatedly deviated from competitive bidding in favour of unsolicited proposals (USPs) in government procurement, often also connected to tied loans.

Currently, the approval of USPs relies on the discretion of the cabinet of ministers.\textsuperscript{107} This discretion has been exploited for malpractice. From 2015–19, Sri Lanka entered into 13 USPs for a total of over USD 3.504 million.\textsuperscript{108}

An oversight mechanism on procurement can curtail USPs and reduce the negative economic, debt, and fiscal impact to Sri Lanka, which has been studied and documented.

\textsuperscript{103} Lars Kalderen (1997), “Debt Management Functions and Their Location”, available at: https://www.elibrary.imf.org/display/book/9781557755551/ch003.xml


\textsuperscript{105} Ministry of Finance, “Budget Speech 2017”, Pg. 69, available at: https://www.treasury.gov.lk/api/file/52172dco-cfle-457c-b1a2-9b1272097742

\textsuperscript{106} Ministry of Finance, “Interim Budget Speech 2022”, Pg. 10, available at: https://www.treasury.gov.lk/api/file/89d90eaf-Seda-4947-9b43-9cb1f97ceef0


Other weaknesses in Sri Lanka’s current procurement framework includes:

- the absence of a clear procedure, as the laws and regulations governing procurement is contained in multiple documents applicable to different procurement entities, with varying degrees of legal authority, subject to ad hoc changes,
- the lack of access to information that is legally mandated to be made proactively publicly available, in general, and specifically, information that is centralized,
- the lack of coordinated oversight over public procurement (current set up provides for multiple entities including the Ministry of Finance, National Audit Office, National Procurement Commission, Parliamentary Committees, etc.)
- the continued Cabinet discretion to entertain unsolicited proposals

All of these weaknesses combined, provides fertile ground for the abuse of public resources, and corruption in the interests of the few at the cost of the many.

Related to this is the consequence of crony capitalism which creates the climate for corruption and rent-seeking on the basis of financial and other support provided to certain politicians during election campaigns and other key occasions. While a Regulation of Election Expenditure Act was passed in January 2023, its provisions remain weak on the issues of limiting election financing contributions, monitoring and enforcement. In this context, local business tends not to be truly competitive but instead relies continued on state patronage. This makes them less competitive in international markets or even in relation to internationals entering the local market. Hence, World Bank and IMF-led trade liberalization does not produce the anticipated benefits. In fact, recent studies demonstrate that trade facilitation is actually more beneficial than trade liberalization: “this research shows that the effects of trade facilitation are far superior to and more practical than the effects of trade liberalization though eliminating or lowering of import tariffs.” Whereas trade liberalization in Sri Lanka still involves politicization and huge discretion entrusted to bureaucrats, facilitation can aim at automation/digitalization, simplification and streamlining of import/export processes. In this respect Sri Lanka can follow the example of Vietnam, but the removal of political and bureaucratic discretion is not popular.

Addressing this bottleneck will go a long way in reducing the conditions that led to unsolicited proposals and other corrupt practices and the resultant lack of transparency/accountability.

These improvements can be facilitated by strengthening the National Procurement Commission (NPC) that was re-introduced by the 21st Amendment to the Constitution — granting it a mandate beyond the mere conduct of investigations, to act as a strong and independent regulatory body on procurement.

Starting in 2017, two new procurement guidelines were created with the technical assistance of the Asian Development Bank and others. However, these guidelines, though published, were never brought into effect. There still remains a need to review such guidelines with public consultation, and to formalize them.

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111. Newsfirst Sri Lanka (28 March 2023), available at: https://www.youtube.com/watch?v=_zj_BmMCZi8
113. Article 156B of the Constitution of Sri Lanka
24. Conduct special audits on the ten state ministries/agencies with the lowest proportion (in value) of competitive bidding, and over LKR 10 billion in procurement

**Rationale:**
Conducting special audits of past accounts can help to reduce malpractice in state agencies with total procurement exceeding LKR 10 billion per year. This approach would focus on big ticket procurement, which has the largest consequence. By focusing on the ten state ministries/agencies with the lowest proportion of procurement through competitive tender (by value), the audit process becomes manageable. Crucially, this recommendation seeks to minimize State Capture, because in such situations the internal checks and balances have no effect, and it is only wide public exposure that can act as a deterrent. It also sets up incentives for agencies to raise the bar on the proportion of competitive bidding in procurement.

25. Establish a publicly accessible, online conflict-of-interest register:

25.1. Mandate disclosure of conflicts by categories of persons liable to furnish asset declarations as set out in the ACA, at the commencement and end of their tenure, and periodically during office

25.2. Require disclosure of work history, board memberships, shareholding, directorships, representation roles, donors, and interests that may constitute a conflict of interest in the exercise of public office

25.3. Set up an effective monitoring body for oversight

**Rationale:**
A conflict of interest occurs “when a public official has private-capacity interests which could improperly influence the performance of their official duties and responsibilities.” Conflicts of interest carry significant and far-reaching implications, encompassing the potential for misallocated resources, diminished transparency, and erosion of public trust.

The issue of conflict of interest in Sri Lanka is addressed in several sections of the Establishments Code, which sets out the rules for recruitment, appointment, remuneration, promotion, and the general duties of public officials. However, the code lacks comprehensive guidelines and procedures for handling conflicts of interest, as noted in the review of the country’s implementation of the United Nations Convention against Corruption. Moreover, the review noted a significant lack of information concerning the practical implementation of these provisions, especially concerning the actions taken when conflicts of interest were identified. The report highlights a need for clearer rules defining conflicts of interest and outlining penalties for non-compliance. It also calls for the establishment of a monitoring mechanism and the provision of training for public officials to enhance conflict of interest prevention and detection measures in Sri Lanka.

The Anti-Corruption Act, No. 9 of 2023 takes steps to address these deficiencies by incorporating vital provisions related to conflicts of interest. This includes requirements for public officials to disclose any interests that they or their associates have in entities with which the public authority they are affiliated intends to engage, restrictions on participation in decisions with personal interests, and the imposition of penalties for non-compliance. Additionally, the Act empowers

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117. Ibid.
the Commission to establish rules governing the management of conflicts of interest among public officials, ensuring effective implementation and enforcement.

The proposed recommendations go further than what is currently required under the law and align with what was incorporated in the IMF programme commitments in Zambia, which included the implementation of a comprehensive legal framework to prevent and address conflicts of interest. The actions proposed in Zambia require public officials to disclose their interests at the beginning and end of their terms and periodically during their tenure. In contrast, Sri Lanka’s existing legislation mandates disclosure for public officials when their affiliated public authority intends to engage with certain entities. Therefore, mandating disclosure for conflicts of interest among public officials can dissuade adverse compromises in financial decision-making, due to the conflict of interest.

26. Enact regulations for the transparent and accountable management of state enterprises:
The fact that state-owned enterprises (SOEs) are, in general, underperforming on a number of fronts is well-known. There are significant corruption vulnerabilities in the practice of leadership appointments, in procurement, contracting and related areas. The narrow politicisation of employment, promotions, and the handing out of perks has led to inefficiency and an ever-increasing level of non-accountability. While it is generally only the large-turnover SOEs that are in the limelight, this recommendation seeks to regularise all SOEs. Many are outdated in their very conception and systems. Others have huge gaps that led themselves to widespread corruption and waste accompanied by impunity. Foremost among these are the tax revenue agencies, which require special systems of regulation.

26.1. Reform of tax revenue agencies, including Customs, Excise, and the Inland Revenue Department to address their widespread corruption vulnerabilities that directly impact fiscal Revenue

Rationale:
Fiscal revenues are adversely impacted by the corruption vulnerabilities of the state revenue agencies. Streamlining them and making them more accountable will increase government income significantly.

27. Amend Parliamentary Standing Orders to better reflect continuity and accountability, especially to prevent disruption of the work of the Committee on Public Accounts (COPA), the Committee on Public Enterprises (COPE) and the Committee on Public Finance (COPF) each time Parliament is prorogued, under Standing Order No 114

Rationale:
When Parliament is prorogued, “In terms of Standing Orders of Parliament No. 114, the Committee of Selection has to be appointed and therefore, all the Committees for Special Purposes cease to function during the recess or the prorogation of Parliament and all of them have to be re-constituted at the commencement of each Session of Parliament except the Committee on High Posts, Sectoral Oversight Committees and Select Committees of Parliament as per provisions of Standing Order of Parliament Nos. 124(5), 111(2) and 109 respectively.”

119. Key Informant Interview insight reinforced by FGD discussions.
120. Key Informant Interview with expert in the field.
Prorogation can happen many times in a single year on the sole discretion of the President, and it has been used in the recent past to manipulate the work of Parliament as a means of dissolving ongoing committees if they appear to be toeing an independent line.122 Regular re-constitution of these three financial oversight committees and other similar committees nullifies the progress made and makes it impossible to achieve sustainable impacts or practical outcomes, thereby devaluing the governance potential of those committees. In Sri Lanka, “Parliament has been prorogued about 50 times to date since 1947 and [has had] more than 25 Sessions since 1978.”123 It is clear that prorogation is being used more frequently in recent years from the fact that the five years of the seventh Parliament had only one session, whereas the four years of the eighth Parliament had four sessions and the ninth Parliament has already had three sessions in three years.

In comparison, in India “The Rules and Procedure specifically provide that any Business pending before a Committee shall not lapse by reason only of the prorogation of the House and the Committee shall continue to function notwithstanding such prorogation.”124

28. Reduce unnecessary military expenditure by demilitarising the North and East of Sri Lanka, re-skilling of military cadre prior to release, including handing back of private and common State lands

Rationale:
As has been repeatedly pointed out, the cost of maintaining Sri Lanka’s military expenditure at approximately the same levels as it did during the height of the war, which concluded 14 years ago, has resulted in “Sri Lanka spend[ing] too much money on its defence and spend[ing] its defence budget inefficiently.”125 In this context, the defence budget comprises the military (tri-forces) and Special Task Force and State Intelligence Service expenditure. Even in the post-war period, military salaries accounted for nearly 45% of all government salaries,126 and in 2021 it accounted for 34.6% of all government salaries and wages.127 Defence spending has actually increased during the 2009–2017 post-war context in relation to the peak of the war128, and notably in 2021 defence expenditure increased by 2.2%.129 As of 2022, Sri Lanka had 255,000 active military personnel, making it the 10th largest military force in Asia.130

In addition, the clear injustice in maintaining redundant camps throughout the North and East, which has the constant potential for exacerbating ethnic tensions and retarding post-war development, are serious national concerns. The 2022 United Nations High Commissioner for Human Rights (UNHCHR) report on Sri Lanka states that “a heavily militarised environment and culture of surveillance also continues in the north and east of the country.”131 Research has shown

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122. Key Informant Interview.
123. Ibid.
124. Ibid.
commentary-archives/2022/11/27/defence-expenditure-the-elephant-in-the-budget
128. SIPRI data cited by Alphonsus.
that active troop reduction by up to 30%, facilitated by voluntary retirement and curtailment of recruitment, including other cost-cutting measures, can reduce the total military expenditure to 0.7% of GDP, which would be an annual saving of US$ 1.3 billion.¹³²

“We know from bitter experience that our problems are seen only as Northern problems and not as national problems. No one in the South will actively support us to solve our main problems like the military occupation and human rights violations. No government will listen. There is no point is talking about this over and over again without any result.” FGD participant, echoed by others.

A recent commentary analysing defence expenditure and its effect on the 2023 budget summarises the core argument succinctly, as follows.¹³³

Expenditure must be rationalized: Defence and security spending is one of the main areas in which rationalization can be improved. The Ministry of Defense has the third highest Budget allocation of all ministries.

Hence, the phased reduction of active military cadres should be an urgent priority, which needs to be accomplished through re-skilling, creation of a reserve force, and of course, freezing on hiring new recruits. In addition, using the military to compete unfairly with local farmers and entrepreneurs in the North and East should be stopped immediately.

29. Increase transparency and accountability of new social safety net cash transfers by reconceptualising multi-dimensional poverty indicators and data collection processes, while providing universal access for families with disability, illness and trauma

Rationale:
Local consultations established the fact of widespread dissatisfaction with the newest iteration of the social safety net, as there was a high degree of confusion and some lack of transparency. While the present move to multi-dimensional poverty indicators is welcome, it is necessary to recognise that coverage should be universal for non-income related needs/conditions. Open public debate of the key issues is necessary to raise awareness and garner support. It is not feasible or necessary to force such far-reaching changes without evidence-based rational discussion on the pros and cons, and hence this is at the core of the governance landscape, especially given the overall financial difficulties faced by all citizens.

“I participated initially in collecting information from families in our village and surrounding areas. Now I can’t even stay in my home because people are angry due to problems with how this information has been used to select Aswesuma recipients. Many of the young people who collected information didn’t even know or care what they were doing. An injustice has taken place. How can we solve this problem?” FGD participant

¹³² Alphonsus, ibid., pp. 5, 37. Note that report was written using data from 2017 when dollar exchange rate was much lower.
¹³³ Jayaweera, ibid.
This is then a core governance issue which has clear and strong fiscal ramifications. The IMF proposals seek to increase expenditure with improved coverage, but a recent study demonstrates that the key challenges of lack of transparency and favouritism, discrimination on the basis of ethnicity/language/gender/occupation, mismanagement and corruption, as well as communication gaps, remain inadequately addressed. Hence, the transformation from Samurdhi to Aswesuma, if it is not to be cosmetic or worse, needs to engage with many of the core issues raised by civil society groups, which include a critique of cash transfers that serve to reduce the protection of poor and vulnerable groups from neoliberal market forces. The expert members of the Validation Meeting saw this as a deliberate move to financialise human survival, moving drastically away from a system that provided subsidies, goods and services to the most disadvantaged and voiceless communities.

30. Ensure proper oversight and enforcement related to illicit financial flows (IFFs):

30.1. Establish a Politically Exposed Persons (PEP) Database that is accessible to Financial Institutions (FIs) and Designated Non-Financial Businesses (DNFBs), and the public

30.2. Introduce a publicly accessible, online Beneficial Ownership Register

General Rationale

Corrupt individuals including politicians and businessmen, criminals, and tax evaders have moved US$ 19.96 billion (Rs. 2.88 trillion) in dirty money out of Sri Lanka between 2004 to 2013. Sri Lanka has higher IFFs than countries such as Colombia. Sri Lanka has obtained a score of 72 out of 100, where 100 is the worst, in the Tax Justice Network’s Financial Secrecy Index. Scandals like the Panama Papers and the Pandora Papers, where many Sri Lankan individuals and entities were implicated, demonstrate that Sri Lanka continues to foster illicit financial flows within and across its borders.

Rationale (31.1)

A “politically exposed person” (PEP) means an individual who is entrusted with prominent public functions either domestically or by a foreign country, or in an international organisation and includes a head of a state or a government, a politician, a senior government officer, judicial officer or military officer, a senior executive of a state-owned corporation, government or autonomous body, but does not include middle rank or junior rank individuals.

Due to their official status or position held and influence, it is recognized that many PEPs are in positions that potentially can be abused for money laundering and related predicate offences, including bribery and corruption, as well as activity related to terrorism financing. The potential risks associated with PEPs justify the application of additional Anti Money Laundering and Countering the Financing of Terrorism (AML/CFT) measures to prevent, detect and manage these risks emanating from their conduct.\textsuperscript{140}

While it has promulgated laws and regulations that require FIs and DNFBs to exercise standards of due diligence when transacting with PEPs, Sri Lanka lacks a centralized PEP database. FIs and DNFBs often only have access to foreign databases, as no comprehensive official identification and classification of PEPs has been conducted in Sri Lanka by the Central Bank or the Financial Intelligence Unit that sits within it. This is required, for FIs and DNFBs to apply laws and regulations in practice, because the identification of PEPs, remains a challenge in itself,\textsuperscript{141} resulting in Sri Lanka poorly addressing the issue of IFFs.

\textbf{Rationale (31.2)}

Sri Lanka does not have a comprehensive and public mechanism to identify beneficial ownership\textsuperscript{142}, even though there has been some discussion around the need to amend the Companies Act No. 7 of 2007, to introduce increased transparency on beneficial ownership.

However, as per the Financial Transaction Reporting Act (FTRA) No. 06 of 2006\textsuperscript{143}, financial institutions (FIs) are required to identify the beneficial owners of their clients when establishing a business relationship.\textsuperscript{144} Further, there are several guidelines issued by the Financial Intelligence Unit (FIU) – the Anti Money Laundering and Countering the Financing of Terrorism (AML/CFT) regulator in the country – to help FIs and Designated Non-Financial Businesses and Professions (DNFBPs) to identify beneficial owners.\textsuperscript{145}

While these provisions are laudable, several concerns remain. The current process relies purely on FIs to collect information, leading to possible non-compliance and inaccuracies. There is no third-party verification or oversight, and enforcement for conflicts of interest, money laundering, terrorist financing or other forms of corruption and as such, enforcement will be limited to instances of suspicions being raised through suspicious activity reports by the FIs or action taken by law enforcement authorities in response to a complaint. Without public accessibility, law enforcement’s ability to detect such crimes is severely limited.\textsuperscript{146}

To combat corruption in procurement, in election campaign financing, in money laundering, and otherwise curb illicit financial flows, it is essential that there is an up-to-date, publicly accessible, online register of beneficial ownership in Sri Lanka.

\textsuperscript{141} Key Informant Interview with Transparency International Sri Lanka.
\textsuperscript{142} As per Rule 99 of the Customer Due Diligence Rules, the “beneficial owner” of the legal person or legal arrangement is a natural person who ultimately owns or controls a customer or the person on whose behalf a transaction is being conducted including the person who exercise ultimate effective control over a legal person or a legal arrangement. available at: http://fiusrilanka.gov.lk/docs/Guidelines/2018/Guideline-04-2018.pdf
C. Measures towards structural changes that are necessary to significantly reduce corruption risk and impunity

Where current legislation is manifestly inadequate to address financial mismanagement and potential corruption, this second category of recommendations identifies policy changes that are required, either to plug existing gaps and/or to target new concerns. This category of recommendations stems from the fact that the present legal and administrative regime is unable to address the key macro-critical economic governance demands needed for the reform agenda.

31. Pass legislation on asset recovery in compliance with the United Nations Convention Against Corruption (UNCAC) with wide consultation, and ensure progress on key corruption cases, including those already commenced, with technical assistance from StAR (Stolen Asset Recovery Initiative)

Rationale:
Sri Lanka’s actions in keeping with the United Nations Convention Against Corruption (UNCAC) would underscore its commitment to recovering stolen assets from safe havens.

In 2015, Sri Lanka established Presidential Task Force for the Recovery of Illegally Acquired State Assets (START) to coordinate intelligence gathering and investigations for asset identification, tracing, seizure, and repatriation.147 START also carried out a process whereby a Policy Framework148 was created for an upcoming Proceeds of Crime Act, which process was subsequently halted. Collaboration with experts from the Stolen Asset Recovery Initiative (StAR) of the World Bank and the United Nations Office on Drugs and Crime, among others and participation in fora such as the Global Forum on Asset Recovery (GFAR) strengthened Sri Lanka’s pursuit of stolen assets. At GFAR in 2017, then Attorney-General Hon. Jayantha Jayasuriya stated that they had had an opportunity to discuss 43 cases during the meetings, with requested jurisdictions (jurisdictions from whom law enforcement assistance had been sought).149 However, the progress of the taskforce and the StAR initiative appears to have stalled since the 2019 presidential election, and there is no publicly available information on any progress on these cases since 2017.150

“We are suffering now because of the highway robbery committed by one family and their friends on the people of this country. If you can’t get this money back, we will remain in this mess. Can the country develop from the money that is forcibly taken from us while the crooks continue to live in luxury? What’s the point of all this talk if the stolen money from the Central Bank, the sugar scam, can’t be taken back and the crooks punished?” Focus Group member

150. Key Informant Interview.
This recommendation has the potential to get Sri Lanka back on track, take forward a key public demand during the citizen uprisings of 2022 (which has also been a demand of the parliamentary opposition) and signal serious action to reduce corruption and recover stolen assets for the benefit of the people/victims whose assets have been pilfered away. The examples of success in countries such as Nigeria, Uzbekistan, and Kazakhstan highlight the potential and effectiveness of this recommendation.

In order to make such a crucial initiative viable and meaningful in practice, it is imperative that there is a mandated civil society role in the law-making process, as well as in the implementation of the law in keeping with international best practice, to ensure transparent, accountable asset return that ensures that repatriated assets are not re-corrupted.

Beyond the passage of the law, it is of vital importance that stalled and new cases related to important allegations and revelations, including the 43 cases in progress in 2017, be initiated or resumed, with the Executive seeking the technical assistance of StAR.

32. Establish a specialised independent corruption prosecution office with IMF technical guidance based on advising offices established in other countries

Rationale:

In Sri Lanka, the office of the Attorney General is usually tasked with appearing in court to defend the government or government officials against legal action. In cases of corruption, the same Attorney General is required to conduct the prosecution of government entities or officials. This situation is vulnerable to a conflict of interest. As described in a study undertaken in November 2020, the Centre for Policy Alternatives (CPA) has concluded that, of the “three primary functions of the Attorney General at present with regards to (a) Criminal Prosecution (b) Legislative Process and (c) Advising the government... [s]pecial emphasis [should be] placed on the proposal for introducing a Public Prosecutor’s Office, as well as, a Parliamentary Research Unit.”

This reform is both urgent and important because historically, the Attorney General’s office in Sri Lanka has failed to demonstrate significant independence from the office of the President and the Cabinet of Ministers. The president also has the discretion to appoint the Attorney General to the Supreme Court when a vacancy arises – gaining further leverage and influence over the performance of his/her functions. Over the past 2 years, numerous corruption cases have been halted or withdrawn by the Attorney General citing lack of evidence. This is despite the cases having been instituted citing adequate evidence to proceed with prosecution.

157. See for example The Morning (08 October 2021), “TISL files a complaint with CIABOC calling for an investigation into Nadesan and Rajapaks“, available at: https://www.themorning.lk/articles/166411
The United Nation’s peacebuilding initiative in Sri Lanka has identified an independent prosecution office as a critical institutional structure, necessary to foster better accountability, rule of law and human rights.\textsuperscript{160} The creation of an independent prosecution office focusing on corruption prosecution has precedent in IMF as a conditionality.\textsuperscript{161} Given the uneven history of implementation of such institutions globally due to political influence/interference, clear benchmarks need to be established to minimize co-option.

In its programme with the Ukrainian Government, the IMF insisted on Ukraine establishing, and ensuring the autonomy of, a Specialized Anticorruption Prosecutor’s Office. It also sought to establish institutions to publish quarterly data on asset declaration of high-level officials, and the number of persons indicted for corruption. In Moldova, the governance diagnostic put forth several recommendations to strengthen the powers of the existing prosecution office and enhance its independence. Among these recommendations, are the allocation of a separate budget for the office and the ability to recruit private investigators.

Moreover, as explained throughout this report, it is also clear that structural reform alone is insufficient to ensure anti-corruption outcomes because the other essential components such as strong laws to prosecute, prevent delays, eliminate political interference and evidence tampering, assure protection etc need to also be addressed.

33. Alienate land for user-owned housing in the Malaiyaha Tamil areas, and provide living minimum wage for plantation sector workers (right to housing and livelihood)

Rationale:
The mainstay of the export economy in the pre- and early post-colonial era, the plantations still provide high employment and global market leadership, but this comparative advantage has been gradually eroded due to numerous factors, including labour unrest and inadequate resource allocation. The sector is due for far-reaching change, the discussions of which are stymied due to employers and unions not being able to as yet achieve agreement on the core issues of land, housing and stable livelihoods.

“For 200 years we have made this country what it is by earning the income that helped to feed all the communities living here. But, for 200 years we have suffered without basic rights or proper incomes, and we have been discriminated against by all these same communities, all this time. We will not endure this injustice anymore.”

Key Informant Interview with Maiaiyaha Tamil activist

The 2015 World Bank Report on Sri Lanka clearly identifies that the Malaiyaha Tamil community in the plantation areas are among the most vulnerable groups in the country, as follows:

- “Despite recent improvements, poverty rates continue to be higher in the estates when compared to both urban and rural sectors, pointing to continued vulnerability.” [\#225: p. 101] The Report adds that “the poverty headcount is 10.9 percent in the estates, compared to 7.6 percent in the rural sector and 2.1 percent in the urban sector.”
- “When looking at non-monetary indicators of poverty, health and nutrition are worrisome, especially in the estates.” [\#226: p. 102]

\textsuperscript{160} Key Information Interview with Verité Research
As the data from the 2021 Annual Report of the Tea Small Holdings Development Authority indicates, there are 418,328 small holders (reflecting a 4.76% increase from 2018) comprising 74.56% of the total national tea production, demonstrating that smallholdings are an economically viable alternative to large estates. Hence, the strong demand from both the relevant FGDs as well as the KIIIs to restructure the sector on these lines presents a cogent argument from both the economic and social justice perspectives. It is the consensus view within the field that the proposed reforms are necessary to set the sector on a sound economic and rights footing.

34. Change the composition and structure of the Constitutional Council so that there is a higher ratio of non-political representatives to ensure meaningful independence in decision-making

Rationale:
There is a much larger and more important role that the Constitutional Council can play in ensuring that the key Commissions and other institutions are led by competent and independent people who remain outside the political class. This can only be achieved if the Constitutional Council (CC) has a majority of members from outside the political parties and their admirers. At present only three civil society representatives serve on the ten-member CC, which makes theirs a token presence.

If and when the CC acquires greater independence and stature, it can actively engage even in vetting senior judicial appointments to facilitate transparency and impartiality. Changes should also be made to the selection process to promote greater transparency and accountability. It is crucial that the Constitutional Council’s selection procedures are clearly defined. For example, in the Maldives, commissioners to the country’s Anti-Corruption Agency are appointed based on a weighted assessment against established criteria. Adopting a similar process in Sri Lanka could favor the appointment of technocrats with an anti-corruption background over political appointees. Publishing eligibility criteria is essential in this context while clarity in the process fosters transparency and public trust in appointment processes. Even the decision-making of the CC should be more public.
G. ASSESSMENT OF RESULTS AND ACCOUNTABILITY

“Even the good laws and regulations in place have not prevented corruption and bad governance from flourishing with impunity in this country. Impartial and efficient implementation is the single most important factor in ensuring that impunity ends that both politicians and bureaucrats are deterred from being corrupt.”
Key Informant Interview

“Without monitoring implementation, and the teeth to punish non-compliance, all these proposals are useless because they will only be used selectively against small fry or political opponents.” Key Informant Interview reinforced by FGDs.

As the legal framework and institutionalized practice that form the governance benchmarks require to address the political-economic crisis and facilitate sustainable recovery, it is necessary to understand that the planned reforms must go well beyond the life of the IMF agreement. The IMF’s own economic forecast indicate a modest improvement only set to begin in 2024, with a positive growth rate of 1.4%. This means that both the political will and implementation mechanisms should not be conceived instrumentally, mainly to circumvent IMF requirements, but must be considered holistically as integrated with other legislation and regulatory systems already in place or being drafted in parallel.

To be specific, there is clear apprehension that while on the one hand IMF-led reforms include long-overdue and generally laudable laws such as the Anti-Corruption Act, at the same time the draconian Prevention of Terrorism Act No. 48 of 1979 and the proposed Anti-Terrorism Act, the selectively and discriminatorily implemented International Covenant on Civil and Political Rights Act No. 56 of 2007 (ICCPR Act), the Broadcasting Bill and the proposed Bill seeking to regulate NGOs, all point to a systematically shrinking democratic civic space, which are in sharp contrast, even contradiction, to the IMF-catalyzed Anti-Corruption Act and the proposed Public Finance Management Act.

Given the Sri Lanka’s context of selective or non-implementation of even current legal and regulatory mechanisms166, it is imperative that monitoring and evaluation of the progress of economic reforms should involve the active and equal participation of appropriate civil society entities to ensure that targets are met, and goals remain in sight. This report has detailed instances, such as in the administration of EPF funds, where impunity has accompanied the non-compliance with even legal decisions and RTI determinations. One idea in this regard is to have a joint government-civil society committee to undertake this all-important task with

this committee reporting its findings continuously and in a publicly accessible manner. This does not, of course, preclude other kinds of independent engagement by watchdog, research and/or advocacy organisations in keeping with their mandates and expertise. Some form of multi-stakeholder monitoring and evaluation mechanism could help to ensure greater State accountability and constructive public engagement, which could then help address what is arguably the most vexed issue in the fiscal governance landscape, which is the fact that laws and regulation either remain under-implemented or subverted, and that deliberate non-compliance goes unpunished, thereby reinforcing a pervasive sense of impunity.167

167. This view was strongly held in consultations on which this report is based, where a remedy for non-implementation, selective implementation and/or subversion of existing mechanisms of corruption control was deemed to be of the highest priority. In the absence of such effective oversight with teeth to punish, participants were skeptical of the efficacy of promulgating new laws and regulations, especially in a context where even legal imperatives are regularly ignored.
# Table 1: Summary of Recommended Governance Benchmarks

<table>
<thead>
<tr>
<th>Classification of Governance Recommendation</th>
<th>Increased Transparency &amp; Accountability of existing laws to support fiscal outcomes</th>
<th>Policy changes necessary to facilitate macro political-economic stability</th>
<th>Structural changes to reduce corruption and impunity</th>
<th>Importance as recorded in FGDs and KIs &amp; Governance Commitment¹⁶⁸</th>
</tr>
</thead>
<tbody>
<tr>
<td>Timeframe</td>
<td>Immediate (0 – 6 months)</td>
<td>Short-Term (up to 12 months)</td>
<td>Medium-Term (up to 24 months)</td>
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<tr>
<td>Overarching, Foundational (01)</td>
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<tr>
<td>1 Immediate Governance Benchmark</td>
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<tr>
<td>Tax Reform, Revenue Collection and Expenditure Control: (13)</td>
<td>TAX EXEMPTIONS 1. Maintain a fiscal transparency platform that displays all information related to tax exemptions: - (6 sub-recommendations).</td>
<td>19. Amend all tax-related to remove the excessive use of discretion for taxation changes without approved schemes</td>
<td></td>
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<tr>
<td>9 Immediate and 4 Medium Term Governance Benchmarks.</td>
<td>19. Amend all tax-related to remove the excessive use of discretion for taxation changes without approved schemes</td>
<td>20. Fully implement the price and tax measures anticipated in the framework convention on tobacco control (Article 6), to which Sri Lanka is a signatory</td>
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<td></td>
<td>21. Achieve an annual reduction of 10% in the five-year average of tax exemptions in</td>
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<td></td>
<td>EXPENDITURE 2. Publish annual report setting out expenditure variations against approved budget.</td>
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<td></td>
<td>3. Quarterly publication of tax expenditure reports.</td>
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<td></td>
<td>6. Limit budget allocations under development activities of the Dept of National Budget to 3% of total expenditure</td>
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</table>

¹⁶⁸ This “Governance Commitment” is divided into 3 sub-categories as detailed in Table 2 of the Annex to the main report: (i) Governance commitments in Sri Lanka’s current IMF programme, (ii) Governance benchmarks in IMF programmes in other countries, and (iii) Governance benchmarks identified from current research and analysis in Sri Lanka. They are identified in this summary table by these 3 roman numerals.
### AUDIT, DEBT

4. Publish follow-up actions taken to regularize qualified opinions of the auditor general

5. Implement the Fiscal Management Responsibility act and ensure that non-compliance is penalized. (3 sub-recommendations)

10. Ensure compliance with Section 9 of the RTI to disclose project information

11. Publish quarterly information on public debt

22. Set up a public debt management office external to the Central Bank

4: priority among experts in field. GC (iii)

5: priority among experts in field. GC (iii)

10: priority among experts in field. GC (iii)

11: priority among experts in field. GC (iii)

22: priority among experts in field. GC (ii)

### DDR / EPF

9. Publish data related to all the secondary market transactions of the EPF, with adequate detail to assess off-market rates of sale and purchase as analysed by the forensic audits published in 2019. (03 sub-recommendations)

22: priority among experts in field. GC (ii)

9: Minimizing cost to EPF is of the highest public priority, which is non-negotiable, and has led to extensive national protests. GC (iii)

### Procurement: (03)

1 Immediate and 2 Medium Term Governance Benchmarks

12. Maintain an online platform that publishes all significant public procurement contracts. (When cumulatively above LKR 100 million to any set of connected suppliers)

23. Strengthen National Procurement Commission for oversight on unsolicited proposals and pass the procurement laws reviewed by the World Bank

24. Conduct special audits on the ten state ministries/agencies with the lowest proportion (in value) of competitive bidding, and over 10 billion in procurement.

12: priority among experts in field. GC (i)

23: very high public priority: non-negotiable. GC (iii)

24: priority among experts in field. GC (iii)

### Asset Declarations: (01)

1 Immediate Governance Benchmark

13. Ensure impartial implementation of the legal framework in the Anti-Corruption Act for public access to asset declarations

13: very high public priority: non-negotiable. GC (ii)
<table>
<thead>
<tr>
<th><strong>Deterrence against corruption, including prosecution: (10)</strong></th>
<th><strong>Environmental Protection: (01)</strong></th>
<th><strong>Democratic legitimacy and establishing mandate for reforms: (04)</strong></th>
<th><strong>Reduction of unnecessary and divisive expenditure: (01)</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>3 Immediate, 4 Medium Term and 3 Longer-Term governance benchmarks</td>
<td>1 Immediate governance benchmark</td>
<td>14. Hold national elections in accordance with the constitutionally mandated timeframe (02 sub-recommendations)</td>
<td>1 Medium Term governance benchmark</td>
</tr>
<tr>
<td>7. Reduce corruption and waste in relation to benefits to political leaders and senior bureaucrats (01 sub-recommendation).</td>
<td>17. Publish all documents related to Environment Impact Assessments for all large-scale infrastructure projects in an online portal</td>
<td>27. Amend Parliamentary Standing Orders to better reflect continuity and accountability</td>
<td>28. Reduce unnecessary military expenditure by demilitarizing North and East of Sri Lanka, re-skilling prior to release of military cadre, including handing back of private and common state land</td>
</tr>
<tr>
<td>8. Address politicization of the public service (01 sub-recommendation)</td>
<td></td>
<td>34. Change the composition and structure of the Constitutional Council so that there is a higher ratio of non-political representatives</td>
<td></td>
</tr>
<tr>
<td>16. Ensure CIABOC’s readiness to investigate and apply the law effectively (04 sub-recommendations)</td>
<td></td>
<td>14: very high public priority: non-negotiable, GC (iii)</td>
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<tr>
<td>25. Establish a publicly accessible, online conflict-of-interest register (03 sub-recommendations)</td>
<td></td>
<td>15: Priority for experts, GC (iii)</td>
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</tr>
<tr>
<td>26. Enact regulations for the transparent and accountable management of state enterprises (01 sub-recommendation)</td>
<td></td>
<td>27. Priority for experts, GC (iii)</td>
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</tr>
<tr>
<td>30. Ensure proper oversight and enforcement related to illicit financial flows (IFFs) (02 sub-recommendations)</td>
<td></td>
<td>34: Priority for experts, GC (iii)</td>
<td></td>
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<tr>
<td>31. Pass legislation on assets recovery in compliance with the UNCAC, and have Sri Lanka assessed every year by the World Bank to be making sustained progress on the STAR (Stolen Asset Recovery)</td>
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<tr>
<td>32. Establish a specialized independent corruption prosecution office</td>
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<td>7: very high public priority: non-negotiable. GC (ii)</td>
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<tr>
<td>8: very high public priority: non-negotiable. GC (ii)</td>
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<tr>
<td>16: very high public priority: non-negotiable. GC (ii)</td>
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<tr>
<td>25: priority among experts in field. Public becoming aware of this issue GC (i)</td>
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<tr>
<td>26: very high public priority: non-negotiable. GC (i)</td>
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<td></td>
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<tr>
<td>30: priority among experts in field. GC (i)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>31: very high public priority: non-negotiable. GC (ii)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>32: very high public priority: non-negotiable. GC (ii)</td>
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<tr>
<td>Social Inclusion, Social Safety Net, and protection of most vulnerable communities: (02)</td>
<td>29. Increase transparency and accountability of new social safety net cash transfers through reconceptualizing multi-dimensional poverty indicators and data collection processes, while providing universal access for families with disability, illness and trauma</td>
<td>33. Alienate land for user-owned housing in the Malaiyaha Tamil areas, and provision of living minimum wage for plantation sector workers (right to housing and livelihood)</td>
<td>29: Very high priority: non-negotiable among affected groups. GC (iii) 33: Very high priority among Malaiyaha Tamil community. Necessary for overall credibility of reforms. GC (iii)</td>
</tr>
</tbody>
</table>
### TABLE 2: DETAILS OF GOVERNANCE BENCHMARK RECOMMENDATIONS

<table>
<thead>
<tr>
<th>Recommended Governance Benchmark</th>
<th>Governance commitments in the current Sri Lanka IMF programme</th>
<th>Governance related actions drawn from IMF programmes in other countries</th>
<th>Governance actions drawn from research and analysis in Sri Lanka, including public consultations</th>
<th>Weightage given by experts &amp; Civil society leaders</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. Measures to enhance transparency and accountability of existing systems that are necessary to produce the required fiscal governance outcomes</strong></td>
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<tr>
<td>1 Maintain a fiscal transparency platform that displays all information related to tax exemptions</td>
<td>Comes under key state function 1 (Fiscal Governance) in the IMF’s 2018 Framework on Enhanced Fund Engagement in Governance(^{169}), covering all 3 sub-categories: revenue efficiency, expenditure efficiency and budget transparency.</td>
<td></td>
<td>Very High (among professional and middle class)</td>
<td></td>
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<tr>
<td>1.1 Publish a full list of all firms receiving tax exemptions through all laws and institutions empowered to offer such tax exemptions, and an estimation of revenue lost to the State</td>
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<tr>
<td>1.2 Set stricter criteria for tax incentives and exemptions given via the Strategic Development Projects Act (Define a clear tax concession methodology) based on the investment</td>
<td>✓</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>1.3 Publish rationales for each project selected under the Strategic Development Projects Act</td>
<td>✓</td>
<td></td>
<td>High</td>
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<tr>
<td>1.4 Publish project plans and projected financials for each Strategic Development Project along with the revenue forgone</td>
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<tr>
<td>1.5 Publicise a full list of beneficiaries of tax exemptions or rebates granted on imports, listing out the specific product categories and the value of the tax concessions received by each of the beneficiaries, with an estimation of the revenue lost</td>
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<tr>
<td>1.6 Make available an economic analysis relevant to each exemption, evaluating the fiscal case for, and implications of, the exemption</td>
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<tr>
<td>2 Publish an annual report by 31st March each year, setting out the previous year’s expenditure variations against the approved budget, and explanations for the same</td>
<td>Comes under key state functions 1 and 2 (Financial Sector Oversight) in the IMF’s 2018 Framework, covering all 3 sub-categories: expenditure efficiency, budget transparency, and governance of supervisory authority</td>
<td>✓</td>
<td>Very high among general public</td>
<td></td>
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</tbody>
</table>

\(^{169}\) See IMF (2018) Framework on Enhanced Fund Engagement in Governance, and in its “Governance Diagnostic Assessment One-Pager” circulated by the Governance Diagnostic Assessment Team to interlocutors in Sri Lanka in April 2023.
<table>
<thead>
<tr>
<th>3</th>
<th>Quarterly publication of a revenue report detailing changes to revenue measures that might result in annual revenue loss of 0.1% of GDP</th>
<th>State function 1 Fiscal Governance</th>
<th>✓</th>
<th>Very high among experts in field</th>
</tr>
</thead>
<tbody>
<tr>
<td>4</td>
<td>Publish follow-up on actions taken to regularise qualified opinions of the Auditor General</td>
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<td>5</td>
<td>Implement all the provisions of the Fiscal Management (Responsibility) Act (FMRA), revised as appropriate, and ensure that non-compliance is penalised, since the Act itself has no explicit provisions to deal with non-compliance</td>
<td>State function 2 Financial Sector Oversight</td>
<td>✓</td>
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<tr>
<td>5.1</td>
<td>Amend the FMRA to publish an annual report that sets out tax collection performance, as well as the actual and projected shortfall in tax collection, by all revenue codes up to 8 digits</td>
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<tr>
<td>5.2</td>
<td>Publish all Cabinet decisions, especially in relation to fiscal matters, including the decision-making principles and guidelines being followed, such as those covered in Chapter VI of the Constitution’s “Directive Principles of State Policy and Fundamental Duties”. In addition, reasons and justifications for the decisions taken as well as all documentation on which the decisions were based should be made available to the public</td>
<td>State function 2 Financial Sector Oversight</td>
<td>✓</td>
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<tr>
<td>5.3</td>
<td>Amend the FMRA to mandate the timely preparation and publication of annual audited financial statements of all key 52 SOEs</td>
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<td>6</td>
<td>Limit budget allocations under the development activities of the Department of National Budget (discretionary spending) to 3% of total expenditure</td>
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<td>7</td>
<td>Reduce corruption and waste in relation to the benefits provided to political leaders and senior bureaucrats through enforcing systems of transparency and accountability</td>
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<tr>
<td>7.1</td>
<td>Annual publication of a vehicle registry owned by each ministry by vehicle type</td>
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<td>8</td>
<td>Address the politicization of the public service.</td>
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<tr>
<td>8.1</td>
<td>Establish transparent selection, assessment and promotion criteria for ministry secretaries and other senior public servants through an open public dialogue, and implement these criteria uniformly within six months</td>
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<td></td>
<td>Publish data related to all secondary market transactions of the Employees’ Provident Fund (EPF), with adequate detail to assess off-market rates of sale and purchase (as analysed by the forensic audits of the EPF published in 2019)</td>
<td>State functions 2 Financial sector oversight and 3 Central Bank governance</td>
<td>Very high (non-negotiable)</td>
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<td>9.1</td>
<td>Ensure a clear separation between the Central Bank’s (a) management of the EPF and other superannuation funds and (b) the management of the debt auction, in order to prevent a manifest conflict of interest</td>
<td>✓</td>
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<tr>
<td>9.2</td>
<td>Place in the public domain the relevant data and analysis that justifies the unorthodox local currency domestic debt restructuring conducted in Sri Lanka</td>
<td>✓</td>
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<tr>
<td>9.3</td>
<td>Amend the laws relating to the issuing of local Treasury Bills and Bonds in Sri Lanka to embed the pari passu principle and rebuild confidence in local currency debt</td>
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<tr>
<td>10</td>
<td>Ensure compliance with proactive disclosure requirements outlined under section 9 of the Right to Information Act No. 12 of 2016 which mandates the minister responsible for a project to disclose information relating to the project three months before commencement</td>
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<tr>
<td>11</td>
<td>Quarterly publication of a complete set of updated information on public debt</td>
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<tr>
<td>12</td>
<td>Maintain an online platform that publishes all significant public procurement contracts. (When cumulatively above LKR 100 million to any set of connected suppliers)</td>
<td>✓</td>
<td>State function 2 Financial Sector Oversight</td>
<td></td>
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<td>13</td>
<td>Ensure impartial implementation of the legal framework in the Anti-Corruption Act (ACA) for public access to asset declarations of persons specified therein, and promulgate regulations for its enforcement.</td>
<td>State function 2 Financial Sector Oversight</td>
<td></td>
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<tr>
<td>14</td>
<td>Hold national elections in accordance with the constitutionally mandated timeframe</td>
<td>✓</td>
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<tr>
<td>14.1</td>
<td>Hold postponed Local Government Authorities (LGA) and Provincial Council (PC) elections within the next 3 months</td>
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<tr>
<td>14.2</td>
<td>Increase the financial independence of the Election Commission.</td>
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<td>15</td>
<td>Ensure enforcement of election campaign expenditure monitoring offences by setting up an electronic system.</td>
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<td>16</td>
<td>Ensure that the Commission to Investigate Allegations of Bribery Or Corruption's (CIABOC) readiness to investigate and apply the law effectively and equally, is indicated through the exercise of its new powers:</td>
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<td></td>
<td>State function 2 Financial Sector Oversight</td>
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<tr>
<td>16.1</td>
<td>Adequately resource the CIABOC, including capacity assistance from development partners</td>
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<tr>
<td>16.2</td>
<td>Annually report on number of inquiries, investigations or cases commenced exercising ex mero motu powers of CIABOC</td>
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</table>
| 16.3 | Annually report the number of cases filed using new powers of CIABOC including:  
1. Instances where assistance of any public authority or experts were obtained.  
2. Number of examinations of laws, practices, procedures conducted of a public authority to discover conduciveness to corruption.  
3. Number of joint investigations conducted, and number of instances teams were established for joint investigations in and outside of Sri Lanka.  
4. Number of warrants issued by the Director General and arrests without warrants made.  
5. Number of investigations and cases commenced on non-conviction-based forfeiture, including the number of convictions secured.  
6. Number of instances and nature of codes of conduct introduced by CIABOC, to be adhered to by the private and public sector.  
7. Number of instances where government departments or public authorities were advised of practices or procedures, and monitoring of the implementation of such measures.  
8. Number of referrals received from a public authority or a law enforcement authority, where an offence under ACA may have or is suspected to have been committed.  
9. List of rules made by CIABOC.  
10. Number and nature of officers, officials and employees, of local government service, local authority, public service, public corporation and state audit service appointed to assist efficient discharge of CIABOC's functions. |
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<tr>
<td>16.4</td>
<td>Commence prosecutions on at least 5 high-profile cases of grand corruption(^{170}) involving substantial state resources within 12 months of operationalisation of the ACA</td>
<td></td>
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<tr>
<td>17</td>
<td>Publish all documents related to Environmental Impact Assessments (EIAs) for all large-scale infrastructure projects in an online portal to ensure transparency</td>
<td>✓</td>
</tr>
<tr>
<td>18</td>
<td>Protect and uphold civic space for citizen participation in all appropriate aspects of governance, including in democratic dissent and protest, where they exercise their fundamental rights as enshrined in the Constitution</td>
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### B. Measures to improve macro-political-economic stability and sustainability

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<tr>
<td>19</td>
<td>Amend all tax-related legislation to remove the excessive use of discretion for taxation changes without approved schemes</td>
<td>State function 2 Financial Sector Oversight</td>
</tr>
<tr>
<td>20</td>
<td>Fully implement the price and tax measures anticipated in the framework convention on tobacco control (Article 6), to which Sri Lanka is a signatory</td>
<td>State function 1 Fiscal Governance</td>
</tr>
<tr>
<td>21</td>
<td>Achieve an annual reduction of 10% in the five-year average of tax exemptions in 1.1 and 1.2</td>
<td>State function 1 Fiscal Governance</td>
</tr>
<tr>
<td>22</td>
<td>Set up a Public Debt Management office external to the Central Bank</td>
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<tr>
<td>23</td>
<td>Strengthen the National Procurement Commission for oversight on unsolicited proposals and pass Procurement Guidelines of 2019 with public consultation</td>
<td>State function 2 Financial Sector Oversight</td>
</tr>
<tr>
<td>24</td>
<td>Conduct special audits on the ten state ministries/agencies with the lowest proportion (in value) of competitive bidding, and over 10 billion in procurement.</td>
<td>State function 2 Financial Sector Oversight</td>
</tr>
<tr>
<td>25</td>
<td>Establish a publicly accessible, online conflict-of-interest register:</td>
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<tr>
<td>25.1</td>
<td>Mandate disclosure of conflicts by categories of persons liable to furnish asset declarations as set out in the ACA, at the commencement and end of their tenure, and periodically during office</td>
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</tbody>
</table>

\(^{170}\) “The abuse of high-level power that benefits the few at the expense of the many, and causes serious and widespread harm to individuals and society” — found at [https://www.transparency.org/en/corruptionary/grand-corruption](https://www.transparency.org/en/corruptionary/grand-corruption). See also [https://www.unodc.org/documents/NGO/Grand_Corruption_definition_with_explanation_19_August_2016_002_1.pdf](https://www.unodc.org/documents/NGO/Grand_Corruption_definition_with_explanation_19_August_2016_002_1.pdf)
<table>
<thead>
<tr>
<th>Requirement</th>
<th>Description</th>
<th>State Function</th>
<th>Urgency</th>
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<tbody>
<tr>
<td>25.2</td>
<td>Require disclosure of work history, board memberships, shareholding, directorships, representation roles, donors, and interests that may constitute a conflict of interest in the exercise of public office</td>
<td>2 Financial Sector Oversight</td>
<td>Very high</td>
</tr>
<tr>
<td>26</td>
<td>Set up an effective monitoring body for oversight</td>
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<td>26</td>
<td>Enact regulations for the transparent and accountable management of state enterprises</td>
<td>Yes</td>
<td>State function 2 Financial Sector Oversight</td>
</tr>
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<td>26.1</td>
<td>Reform of tax revenue agencies, including Customs, Excise, and the Inland Revenue Department to address their widespread corruption vulnerabilities that directly impact fiscal revenues</td>
<td>Yes</td>
<td>State function 2 Financial Sector Oversight</td>
</tr>
<tr>
<td>27</td>
<td>Amend Parliamentary Standing Orders to better reflect continuity and accountability, especially to prevent disruption of the work of the Committee on Public Accounts (COPA), the Committee on Public Enterprises (COPE) and the Committee on Public Finance (COPF) each time Parliament is prorogued, under Standing Order No 114</td>
<td>Yes</td>
<td>High among experts in field</td>
</tr>
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<td>28</td>
<td>Reduce unnecessary military expenditure by demilitarizing North and East of Sri Lanka, re-skilling prior to release of military cadre, including handing back of private and common state lands</td>
<td></td>
<td>State function 1 Fiscal Governance</td>
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<td>29</td>
<td>Increase transparency and accountability of new social safety net cash transfers through reconceptualizing multi-dimensional poverty indicators and data collection processes, while providing universal access for families with disability, illness and trauma</td>
<td>Yes</td>
<td></td>
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<tr>
<td>30</td>
<td>Ensure proper oversight and enforcement related to illicit financial flows (IFFs)</td>
<td></td>
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<td>30.1</td>
<td>Establish a Politically Exposed Persons (PEP) database that is accessible to Financial Institutions (FIs), Designated Non-Financial Businesses (DNFBs), and the public</td>
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<tr>
<td>30.2</td>
<td>Introduce a publicly accessible, online Beneficial Ownership Register</td>
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C. Measures towards structural changes that are necessary to significantly reduce corruption risk and impunity.

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<th></th>
<th>Measures</th>
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<tr>
<td></td>
<td>Pass legislation on asset recovery in compliance with the United Nations Convention Against Corruption (UNCAC) with wide consultation, and ensure progress on key corruption cases, including those already commenced, with technical assistance from STAR (Stolen Asset Recovery Initiative).</td>
<td>✓</td>
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<td></td>
<td>Establish a specialised independent corruption prosecution office with IMF technical guidance based on advising offices established in other countries.</td>
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<td>✓</td>
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<td></td>
<td>Alienate land for user-owned housing in the Malaiyaha Tamil areas, and provision of living minimum wage for plantation sector workers (right to housing and livelihood)</td>
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<td>✓</td>
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<td></td>
<td>Change the composition and structure of the Constitutional Council so that there is a higher ratio of non-political representatives to ensure meaningful independence in decision-making.</td>
<td></td>
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<td>✓</td>
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