

Public Finance Management Reforms in Nepal's Federal System

An Assessment of Karki
Interim Government Initiatives



**PUBLIC FINANCE
MANAGEMENT REFORMS
IN NEPAL'S FEDERAL
SYSTEM**

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Government Initiatives*

**DEMOCRACY
RESOURCE CENTER**

**Democracy Resource Center Nepal
Lalitpur**

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Table of Contents

Acknowledgments	v
Acronyms	vi
Executive Summary	1
Background of Study	7
Methodology	11
Budget Reprioritization	12
Budget Reprioritization at the Federal Level	13
Provincial Government Budget Reprioritization	16
Local Government Budget Reprioritization	19
Public Spending Aims and Realities	22
Fiscal Administrative Reforms	27
Fiscal Administrative Reforms at the Federal Level	27
Fiscal Administrative Reforms at the Subnational Level	29
Institutionalization of Reform Points	36
Embedded Systems vs. Work-in-Progress	37
Conclusion	45
Recommendations	47

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Acronyms

APF	Armed Police Force
B.S.	Bikram Sambat
C-GAS	Computerized Government Accounting System
DCC	District Coordination Committees
DPR	Detailed Project Reports
DRCN	Democracy Resource Center Nepal
EBPS	Electronic Building Permit System
EFT	Electronic Funds Transfer
EMIS	Educational Management Information System
FY	Fiscal Year
Gen-Z	Generation Z
GIOMS	Government Integrated Office Management System
IPFMS	Integrated Public Financial Management System
IT	Information Technology
LISA	Local Government Institutional Capacity Self-Assessment
MoF	Ministry of Finance
NEPSE	Nepal Stock Exchange Limited
NID	National Identity
NNRFC	National Natural Resources and Fiscal Commission
NRs.	Nepali Rupees
PAN	Permanent Account Number
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
PM	Prime Minister
QR Code	Quick Response Code
RMIS	Revenue Management Information System
SuTRA	Sub-National Treasury Regulatory Application
USAID	United States Agency for International Development

Executive Summary

This study assesses the public finance management (PFM) reforms introduced and implemented by the interim government following the Gen-Z movement, and centers on two thematic areas: budget reprioritization, and fiscal administrative reforms. The report covers the Interim Government’s period (September 2025–March 2026), and focuses on the federal level, Lumbini and Madhesh provinces, and three municipalities in each of the two provinces.

Through a budget reprioritization decision, the Government of Nepal aimed to cut various federal-level projects and unproductive expenditures in order to save approximately NRs. 120 billion for the elections, reconstruction of properties damaged during the Gen-Z movement, and other activities. Key directives sent to ministries and subnational governments include dismissing contract employees or limiting them strictly to approved positions (*darbandi*); prohibiting projects valued at over NRs. 1 million from being implemented via user committees; limiting the number of staff at ministers’ personal secretariats; conducting broad reductions in administrative expenditures; initiating procurement controls, including restricting spending on vehicles, furniture, and preparation of detailed project reports; and making digital governance and electronic payment systems mandatory.

While the federal-level budget reprioritization was reported a success, there was no uniformity in the subnational governments’ responses or

results. Lumbini provincial government cut 20 percent its budget and sought to eliminate unnecessary administrative expenses but retained National Pride projects, large-scale infrastructure, multiyear plans and Special/Conditional Grants. It was stated that contract staff members had been removed, but some personnel had been retained by reclassifying them as ‘office helpers’, despite the fact that they were skilled professionals. Madhesh provincial government took a more assertive stance on provincial autonomy over its budget, and in reducing personnel at secretariats, and has resisted implementing the federal circular.

Across the selected local governments, budget reprioritization took different forms, and were implemented at different scales, as dictated by the extent of damage suffered. These reprioritizations centered on quickly resuming services, rebuilding damaged structures, and maintaining administrative operations. Budget reprioritization varied, but in general cuts were made to infrastructure (including roads and temples construction), public awareness programs, social and distributive programs, and administrative expenses. Generally, the education, health and agriculture budgets were left untouched. However, the federal circular on contract staffing was largely bypassed. The needs of the municipalities under dire emergency conditions highlighted other imperatives, especially in the absence of the Federal Civil Service Act. Uncertainty reigned following the Supreme Court’s interim order regarding user committees. Some provincial and local bodies continue to work through user committees, while others have stopped entirely.

While the budget reprioritization and expenditure cut faced little political or legal resistance at the federal level, obstacles to public spending cuts at the subnational levels were linked to the lack of consultation and coordination, and were perceived as ‘top-down’ directives in contradiction to the spirit and the letter of the constitution.

Regarding fiscal administrative reform, this report focuses on digital governance rollout, Single-Window Systems, tax administration modernization, and performance metrics.

At the federal level, there has been major progress on these areas. The Government Integrated Office Management System (GIOMS) has been implemented. The second phase of the Single-Window System is currently under implementation at the ministerial level. And work linking Permanent Account Number (PAN) and National Identity (NID) with the Online Tax Clearance System with a ‘faceless audit’ system currently in the development phase, is ongoing.

Provincial governments have partially adopted fiscal administrative reform systems developed and implemented by the federal government. In Lumbini and Madhesh provinces, electronic payment services and online revenue systems are in place, while necessary steps are being discussed to establish GIOMS. While advances have been made in digitalizing expenditure, the same progress has not been made in terms of revenue collection.

Local levels reveal similar dynamics, with large variations in implementation. There has been negligible progress in implementing the GIOMS and the Single-Window System. Obstacles cited at the provincial and local levels to fiscal administrative reforms include: lack necessary of digital infrastructure, specifically the lack of reliable internet and electricity; shortage of Information Technology (IT) skilled staff; and lack of digital literacy among service seekers. The move toward digital financial management systems, paperless administration, and technology-enabled service delivery has exposed gaps in institutional readiness, technical skills, and supporting infrastructure.

Both the provincial and local levels lack formal frameworks or measurable indicators to evaluate performances related to digitalization systems. The absence of performance frameworks appears more systemic at the provincial level than at the local level. Lack of standardized indicators,

targets, and evaluation frameworks has resulted in fragmented monitoring practices and weak accountability mechanisms.

However, separating reforms that have been implemented and are in the process of being institutionalized from reforms that remain either at the inception phase or works-in-progress allows for a more nuanced, and perhaps more positive, picture. Those reforms that have been integrated into daily operations have become difficult to be reversed. And more specifically, the digitization of financial transactions has emerged as a key area of progress. The transition toward electronic payment systems is well advanced. Core financial management systems have also achieved significant uptakes. Systems such as Sub-National Treasury Regulatory Application (SuTRA), used for accounting and financial reporting, are fully functional at the provincial level, and are being used widely by local governments. Practical reforms aimed at reducing procedural burdens have also created progress in administrative simplification. Taken together, these reforms reflect incremental but important shifts toward a more digital, standardized, and user-oriented PFM system.

Several reform initiatives remain at an early stage of development, pilot implementation, or partial adoption, with significant variation across provinces and local governments. This unevenness is evident across digital governance systems, tax administration modernization, Single-Window Systems for businesses, and decentralized taxpayer services. While evaluating success, the short timeframe in which these fiscal administrative reforms were initiated by the Interim Government should be noted. It had a limited tenure, and it had been formed at a time of immense crisis.

The implementation of budget reprioritization and fiscal administrative reform in Lumbini and Madhesh Province is hindered by a complex web of legal, structural, and technical obstacles, and by political tension between levels of government in Nepal, mostly linked to incompleteness of political federalization. The absence of an effective inter-governmental mechanism

between the three tiers has turned reform implementation into a series of isolated, uncoordinated actions with no shared ownership of reforms.

Recommendations

- Replace unilateral circulars with a negotiated intergovernmental coordination protocol
- Prioritize passing the Federal Civil Service Act to complete the framework for administrative federalism and to provide staffing stability.
- Create a clear interim policy for contract employees management to ensure continuity of service delivery during administrative transitions or budget cuts.
- Legislate protections for health and education budgets to protect essential public services from budget cuts during times of crisis.
- Invest in IT human resources.
- Develop a national digital infrastructure investment plan for subnational governments.
- Establish performance frameworks at provincial and local levels with federal facilitation.
- Invest in multi-level digital literacy as a public good.
- Conduct a Structured Post-Crisis Review and Publish Lessons Learned.

Background of Study

Nepal's economy remains fragile despite public finance reform efforts, including the enactment of laws,¹ the implementation of the Public Expenditure and Financial Accountability (PEFA) framework since 2008,² and the digitization of financial systems.³ According to the National Statistics Office, 20.7 percent of the national population lives below the poverty line. Transparency International data shows that Nepal ranks 109th out of 182 countries on the corruption perception index. Furthermore, 61 percent of Nepal's total foreign currency earnings come from remittances. While remittances play a vital role in sustaining the economy, they have contributed little to economic growth and job creation. The country still relies heavily on foreign grants and loans to finance public capital expenditures.⁴ By the end of January 2026, the government's total public

¹ Laws including, the Public Procurement Act (2063 BS), the Customs Act (2064 BS), and annual Finance Acts, as well as essential policies, guidelines, action plans, and procedures for budget execution.

² PEFA framework has been used to monitor and evaluate the financial management system. This framework covers revenue management, intergovernmental fiscal management, external oversight, transparency, and credibility.

³ The Government of Nepal had been integrating technology into financial systems since 1990s, however, nationwide digitization of financial systems gained momentum with the launch of Digital Nepal Framework in 2019. See: Onlinekhabar. 2018. All Government Transactions Go Digital Now. April 25, Available at: <https://english.onlinekhabar.com/all-government-transactions-go-digital-now.html>; accessed on March 8, 2026.

⁴ The High-Level Economic Reform Recommendation Commission Report (2024) provides a detailed discussion of these economic challenges facing Nepal.

debt had reached NRs. 2.806 trillion. Of this, NRs. 1.487 trillion represents external debt, while NRs. 1.319 trillion represents domestic debt.⁵ To strengthen the national economy, the Government of Nepal formed a High-Level Economic Reform Recommendation Commission on October 7, 2024, to provide recommendations on economic reforms. The commission submitted its report to the government on December 9, 2024, outlining necessary reforms in the economic sector.⁶

Following the Gen-Z protests in September 2025, which led to the resignation of the then Prime Minister (PM) KP Sharma Oli, President Ramchandra Paudel swore in Sushila Karki as the PM of the Interim Government. Following PM Karki's appointment, the House of Representatives was dissolved, and she called for elections for the House to be held on March 5, 2026. Rameshwor Khanal, chair of the above-mentioned High-Level Economic Reform Recommendation Commission, was appointed Finance Minister on September 15, 2025, and he announced a major budget restructuring exercise as soon as he was sworn in.⁷

The interim government faced large challenges given their six-month mandate. This included: holding parliamentary elections scheduled for March 5, 2026, with no previously allocated budget; reconstruction of the massive damage resulting from Gen-Z protests;⁸ and compensation

⁵ Ministry of Finance. 2025. *Public Debt Report up to the End of Poush 2082*. Kathmandu: Public Debt Management Office, Ministry of Finance, Government of Nepal.

⁶ The commission, formed under the chairmanship of former Finance Secretary of the Government of Nepal Rameshwor Prasad Khanal, included Mahesh Acharya (Secretary), Rajesh Agrawal, Kamlesh Kumar Agrawal, Chandra Prasad Dhakal, Dr. Kalpana Khanal, Dr. Bishow Gauchan, Prof. Dr. Ram Prasad Gyawali, and Dr. Prakash Kumar Shrestha as members.

⁷ NEPSE Trading. 2025. Finance Minister Khanal Prioritizes Implementation of Economic Reform Commission's Report. September 16. Available at <https://nepsetrading.com/blog/finance-minister-khanal-prioritizes-implementation-of-economic-reform-commissions-report>; accessed on February 3, 2026.

⁸ Committee Formed to Assess Damage to Public Property, Physical Infrastructure, and Private Establishments and to Prepare a Public Reconstruction Plan. 2025. *Report on the Assessment of Damage to Public Property, Physical Infrastructure, and Private Establishments and the Public Reconstruction Plan Related to the Movement of 23–24*

payments for 53 families of deceased and over 2,400 injured. The damages totaled NRs. 84.45 billion, NRs. 44.93 billion in damages in the government sector and NRs. 33.54 billion damages in the private sector. Furthermore, all of this was to be achieved without the introduction of a supplementary budget.

To hold timely elections, repair and rebuild damaged structures, resume services, and undertake compensation payments, budget reprioritization became imperative. On September 21, 2025, the Council of Ministers approved budgetary measures, and Minister Khanal sought to implement key structural reforms that emerged from the High-Level Economic Reform Recommendation Commission.

This study assesses the PFM reforms introduced and implemented by the interim government following the Gen-Z movement and centers on two thematic areas, the reprioritization of the budget and fiscal administrative reform. In terms of the latter, the focus is on four key initiatives: digital governance rollout – i.e., digital payment systems; Single-Window System; tax administration modernization, and performance metrics. The goal is to analyze public spending and institutionalization of reform points by tracking federal and subnational government decisions and reform alignment.

Bhadra 2082. Kathmandu: Committee Formed to Assess Damage to Public Property, Physical Infrastructure, and Private Establishments and to Prepare a Public Reconstruction Plan. Available at https://giwmscdntwo.gov.np/media/pdf_upload/Cheti%20Mulyankan_hpt2aje.pdf; accessed on March 2, 2026.

Methodology

The report covers the Interim Government’s period (September 2025–March 2026), focusing on the federal level, and Lumbini and Madhesh provinces. To examine the different impacts on metropolitan cities, sub-metropolitan cities, and rural municipalities, Aurahi Rural Municipality, Janakpurdham Sub-Metropolitan City, and Birgunj Metropolitan City were chosen from Madhesh Province while Narainapur Rural Municipality, Ghorahi Sub-Metropolitan City, and Butwal Sub-Metropolitan City from Lumbini Province were included.

The study employs a mixed-methods approach, combining field research, in-depth interviews, and desk-based literature and budget reviews. This includes examining government policies, laws, and institutional frameworks on public financial management, budget implementation, and fiscal reforms. Additionally, news reports, articles, reports and government decisions were reviewed to analyze policy responses and implications. Fieldwork was conducted by two-member research teams, deployed to Madhesh and Lumbini provinces. A structured interview checklist was developed in consultation with subject-matter experts and coalition members before research teams were deployed. Semi-structured interviews were conducted with 53 elected representatives and government officials at the federal, provincial, and local levels.

Officials and personnel from institutions such as the Ministry of Finance (MoF); the Ministry of Industry, Commerce, and Supplies; the

Department of Industry; Policy Research Institute; High-Level Economic Reform Recommendation Commission; and Nepal Stock Exchange Limited (NEPSE) were interviewed at the federal level. At the provincial level, interviews were conducted with officials and personnel at the Office of the Chief Minister of Lumbini Province, Ministry of Economic Affairs and Planning, Lumbini Province Planning Commission, Ministry of Physical Infrastructure Development, and the Ministry of Health. Similarly, in Madhesh Province, interviews were conducted with officials and staff from the Ministry of finance, Ministry of Physical Infrastructure Development, and the Ministry of Youth, Sports, and Social Welfare. In the local governments selected for this report, elected representatives and bureaucrats were interviewed.

Budget Reprioritization

Budget Reprioritization at the Federal Level

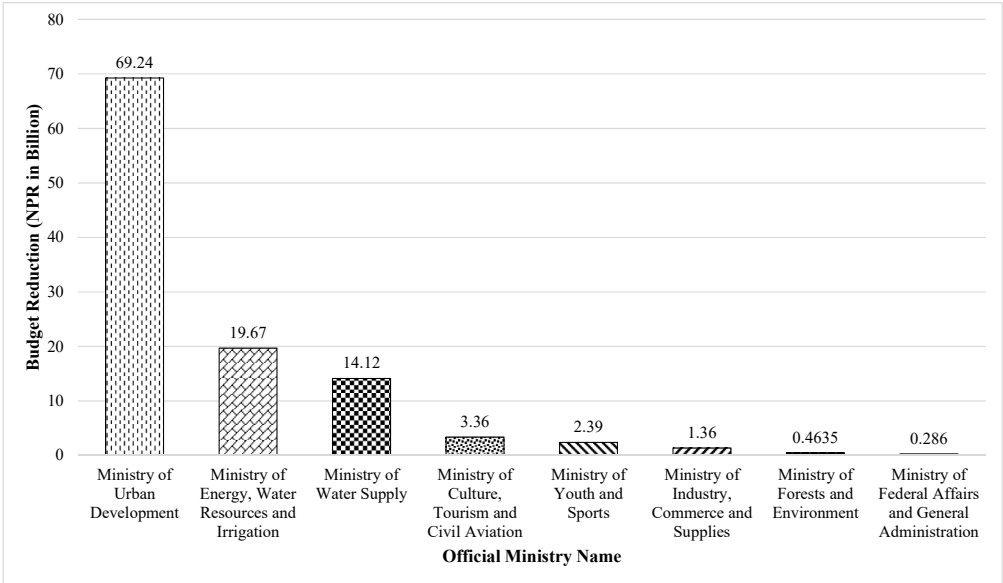
On the first day of office, Finance Minister Rameshwor Khanal announced that up to NRs. 100 billion could be raised by cutting politically-driven, unprepared, and fragmented projects from the current budget. He also formed a three-member taskforce, led by the Budget Division chief, to identify low-priority projects. The government adopted a policy of managing election expenses from internal resources and rebuilding only the most essential public infrastructures. Through the budget reprioritization decision, the Government of Nepal aimed to save approximately NRs. 120 billion by cutting various federal-level projects and unproductive expenditures.

This included around 1,300 projects that were not entered into the project bank, amounting up to approximately NRs.110 billion; around 4,000 small-scale or fragmented projects, amounting to approximately NRs. 30 million; seminar and meeting budgets amounting to around NRs. 12 billion, etc. Additional measures include halting purchase of new government vehicles, mandatory electronic payment, and stopping any major reconstruction.

Key directives sent to ministries and subnational governments include dismissing contract employees or limiting them strictly to approved positions (*darbandi*); prohibiting projects valued at over NRs. 1 million from being implemented via user committees; limiting the number of

staff at ministers’ personal secretariats; conducting broad reductions in administrative expenditures; initiating procurement controls, including restricting spending on vehicles, furniture, and preparation of detailed project reports; and making digital governance and electronic payment systems mandatory. In all, the federal government made decisions to cut projects, control unproductive expenditures and revise contingency limits. It also released funds for election expenses, and provided relief and compensation to the deceased and injured.⁹

Federal Ministry Budget Cuts: Fiscal Contraction Overview



Interviews in January 2026 revealed that the MoF had completed the project reprioritization process. Initially, a budget of NRs. 120 billion was suspended; subsequently, NRs. 35 billion of that amount was released. The

⁹ Interview with the Secretary of the Federal Ministry of Finance conducted in Kathmandu on January 22, 2026, and interviews with the Under Secretary of the Ministry of Finance and the Under Secretary of the Ministry of Industry, Commerce and Supplies conducted in Kathmandu on January 23, 2026.

released funds were specifically allocated for projects that had completed the tendering process by October 22 (Asoj 5), outstanding liability payments, and the Business Recovery Action Plan.¹⁰ Exact breakdowns were not available at the time of the interviews.¹¹

The budget reprioritization was drawn from both recurrent and capital expenditures. This included NRs. 19.21 billion for elections and NRs. 150 million allocated to the Reconstruction Fund. Under these provisions, funds were directed toward making service delivery more effective, including the procurement of vehicles and maintenance of physical assets. For instance, the Supreme Court procured vehicles through a combination of internal budgetary transfers (virement) and additional budget facilitated by the Ministry.

Regarding relief and compensation, a decision was made to provide NRs. 1.5 million each to the family of 53 deceased. For the injured, NRs. 35,000 per person was provided for treatment. In February 2026, a total of NRs. 7.1 million was disbursed as lifetime pension support to the families of those martyred during the movement.

According to the Secretary of the Federal Ministry of Finance, cuts were only implemented within the Federal Budget. Consequently, local and provincial budgets remain untouched and conditional grants have not been halted. However, the federal government issued a circular via email on September 23, 2025 to provincial and local governments on budget reprioritization. The offices of the Chief Ministers and Councils of Ministers of each province then relayed the circular to their subordinate provincial ministries and agencies. Emails were sent to local governments through the Ministry of Federal Affairs and General Administration.

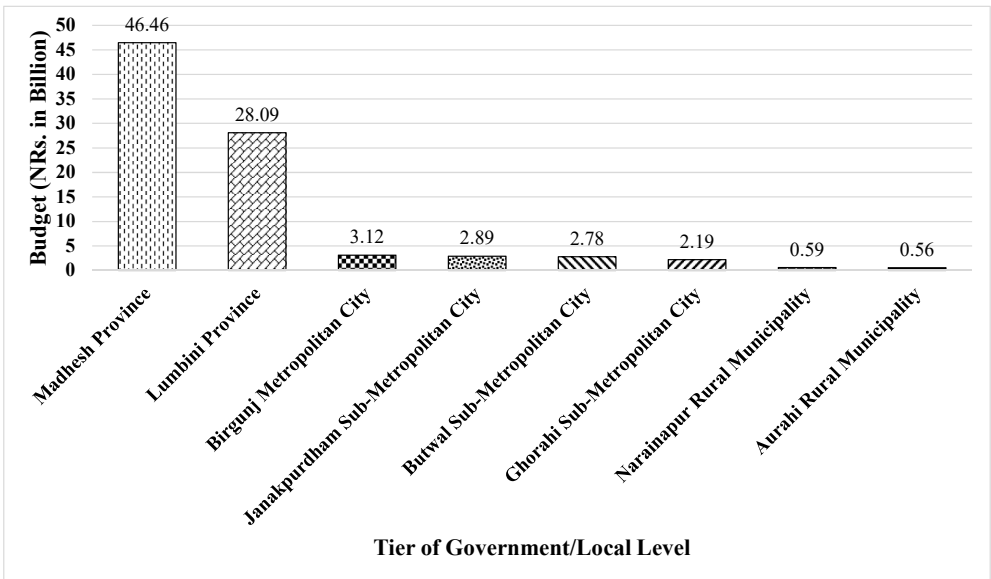
¹⁰ Interview with the Secretary of the Federal Ministry of Finance conducted in Kathmandu on January 22, 2026

¹¹ Interview with the Under Secretary of the Ministry of Finance on January 23, 2026.

Provincial Government Budget Reprioritization

There has been no uniformity in the responses of provincial governments to budget reprioritization. Lumbini Province had seen less damage compared to other areas, though Butwal and Nepalgunj were hit hard. Since provincial structures did not sustain heavy damage, reconstruction needs fiscal year (FY) 2082/083 year are being managed via the regular maintenance budget for urban development.

FY 2082/083 Budget of Madhesh and Lumbini Provinces and Six Local Levels



However, the Lumbini Provincial government cut 20 percent its budget.¹² In terms of the administrative cuts, there was an emphasis on

¹² Some viewed it through the lens of past practices where 20–25 percent of the budget typically remained unspent. They noted, ‘This budget wouldn’t have been implemented anyway; budget that would have been cut later has simply been cut in advance.’ Furthermore, there is a lingering suspicion that despite these initial cuts, the final installment of the budget might still be frozen at the end of the fiscal year, as has happened in previous years.

keeping offices running at a minimum functioning level, with unnecessary administrative overheads, ‘tea expenses’, and various allowances cut. Despite damage to cars, no new vehicles have been bought, and new construction has been pushed to next year’s budget.

While small, fragmented projects (*tukre yojana*) have been cut, decisions have been made to protect National Pride projects, large-scale infrastructure, multiyear plans and special and conditional grants. More specifically, blanket cuts to multiyear projects would not be made, with an emphasis on the continuation of the project cycle, even if only 30 to 40 percent of the funding could be provided. It has been decided to carry out a case-by-case analysis of such projects.

Secretary of the Lumbini Ministry of Finance stated that the federal circular to remove contract personnel beyond the officially sanctioned number of posts had already been implemented.¹³ However, other interviews revealed a more complicated picture. In the Ministry of Infrastructure, contract employees were said to be limited to drivers and office helpers. Furthermore, a senior official from the Health Ministry stated that in order to bypass federal restrictions on contract hiring, skilled professionals such as nurses, engineers, and IT staff are being officially reclassified as ‘office helpers’.¹⁴ This protects their jobs but creates a massive legal and safety liability, as they are performing specialized tasks without the legal status or salaries to match.

In the Madhesh provincial government, the dynamics are different. The provincial government has not yet completed any budget reprioritization. According to Ram Kumar Mahato, Secretary of the Provincial Ministry of Economic Affairs, the Ministry has requested all other ministries to submit detailed reports on damages sustained during the movement, along with the current status of projects being implemented by the respective ministries.

¹³ Interview with the Secretary on January 29, 2026.

¹⁴ Interview with the official on January 29, 2026.

Although this request was made in January 2026, the Madhesh provincial ministries have yet to submit the required information.¹⁵ The process is currently stalled in the data-collection phase, and a formal decision on reprioritization will only be planned once all data are fully compiled. At the time of research, there is no evidence of budget reprioritization or reallocation across any of the ministries under the Madhesh provincial government.

This provincial government has taken a more assertive stance on provincial autonomy, treating federal circulars as ‘optional’ rather than ‘mandatory’. Furthermore, the circular was largely read as an attempt to interfere in the province’s authority. The overall emphasis was on making decisions based on its own laws, structures, and fiscal standing. For example, according to the secretary at the Madhesh Province Finance Ministry, while the federal government may face pressures on its resources with its high liabilities, the province is currently in a surplus and thus can carry out a multiyear project using its own resources if it desires.¹⁶

However, in view of potential budget shortfalls, the Ministry of Economic Affairs informed other ministries to prepare for an approximate 20 percent budget reduction. There is also a formal proposal to reduce contingency expenses from 4.5 percent to 2.5 percent. Furthermore, the purchase of new vehicles has been suspended, citing sensitive public sentiment following the Movement. New directives for expenditure curtailment have also been issued, making prior approval from the Finance Ministry mandatory for Detailed Project Reports (DPR), procurement of vehicles, furniture, machinery, or tools, and residential building construction.

In terms of staffing, there has been resistance in the province against reducing personnel numbers. For example, while the federal circular limits

¹⁵ Interview with Mahato on January 27, 2026.

¹⁶ Interview with the Secretary on January 29, 2026.

staff in a minister's secretariat to three individuals, it was stated that at least six persons are required for smooth functioning of a ministerial office.

According to Section 11 and Schedule 2 of the Remuneration and Facilities of the Chief Minister and Ministers Act, 2075 (B.S.) of the Madhesh Province, up to eight staff members, excluding a computer operator, are allowed to be appointed. Although the Chief Minister directed the staff to follow Provincial Law, employees are waiting for a formal decision from the Council of Ministers, out of fear of their accounts going into arrears in future audits. This has resulted in salary payment for staff secretariat being halted.

Local Government Budget Reprioritization

Budget reprioritization has taken different forms and scales across the selected municipalities. The extent of damage incurred during the Gen-Z Movement largely dictated the allocation of resources, including at income-generating offices. Budget reprioritization at the local government level has centered on quickly resuming services, rebuilding damaged structures, and maintaining administrative operations.

In the only metropolitan municipality studied, Birgunj Metropolitan City undertook a significant budget reprioritization of 37 percent of the municipality for service resumption and the suspension of 25 percent of the ward-level budget, which was later released after conditions stabilized. Administrative spending was slashed from NRs. 10 million to NRs. 4 million, made possible by eliminating duplicate budget heads. The city utilized NRs. 50 million from the Disaster Fund for immediate reconstruction of damaged buildings, and to shore up operational costs, but has since replenished the fund. The overall damages were estimated at NRs. 1.35 billion, with reconstruction of the municipality building estimated to cost NRs. 300 million. A total of NRs. 100 million has been allocated for the year.

Variations were evident across sub-metropolitan municipalities. In Ghorahi Sub-Metropolitan City, heavy losses and damages were cited, with costs amounting to approximately NRs. 70 million for equipment and for reconstruction of damaged structures. The municipal budget was reduced from NRs. 1.75 billion to NRs. 1.35 billion. Budget cuts reached 50 percent for development expenditure (reconstruction), and went up to 70 percent in other areas. Even in wards not severely affected, the budget was cut by 50 percent. In a pragmatic move, the mayor allocated NRs. 2 million specifically to the land revenue (*Malpot*) and survey (*Naapi*) offices to buy furniture and computers as 60 percent of city revenue comes from land transaction fees.

In Butwal Sub-Metropolitan City, reconstruction is estimated to cost over NRs. 100 million. However, unlike other municipalities, federal support is evident with the finance minister, among others, personally visiting the area. A major relief package was negotiated for reconstruction, including a 50 percent contribution by the Municipal Development Fund, 40 percent coming from soft loans, and 10 percent coming from Municipal Matching Fund.

In Janakpurdhama Sub-Metropolitan City reconstruction was said to require approximately NRs. 1 billion. The Sub-Metropolitan City reprioritized 10 to 20 percent of its budget. Ten percent of the internal development budget was redirected toward reconstructing the municipal building, and toward procuring essential office supplies, including computers, printers, and furniture. The budget for office supplies had to be drastically increased – from an initial allocation of NRs. 5 million to nearly NRs. 15 million. The Sub-Metropolitan City’s Financial Strategy for Reconstruction includes mobilization of an inter-contingency fund and discussions with the Town Development Fund for a NRs. 30 million project to reconstruct a building under a proposed model of 25 percent municipal contribution, 25 percent grants, and 50 percent loan.

Of the two rural municipalities covered in this report, reconstruction requirement in Narainapur Rural Municipality was said to be minimal. However, upon receiving the circular for reprioritization and the province's 20 percent budget freeze, the Municipality did not implement the budget allocated for the FY 2082/083. The delay in holding the winter session also hindered budget implementation and reprioritization. Budget originally allocated for public construction and essential maintenance – such as road repairs or physical damage – were utilized to cover reconstruction costs which amounted to between NRs. 10 and 15 million. Pressure was eased by the fact that a shift to a new municipal building was imminent.

The other rural municipality, Aurahi, sustained damages totaling NRs. 50 million and has strategically reallocated its budget to restore essential infrastructure and fund security. Funds originally earmarked for road construction, temple building, and public awareness programs were diverted to reconstruct ward office buildings, police posts, and Armed Police Force (APF) camps, as well as to procure necessary office supplies. Chairperson of the Rural Municipality stated, “We have used our own budget via fund transfers for repairs and reconstruction. We suspended programs that were not immediately critical and redirected those investments towards urgent needs.”¹⁷ The disaster budget has not been touched.

In summary, during reprioritization, cuts were made to infrastructure, including road and temple construction, public awareness programs and social and distributive programs, and administrative expenses. Essential schemes and programs for daily livelihood have not been affected. These include education (incentives/salaries, Grade 8 board exams), health (medicines, maternity services, vaccinations), agriculture (irrigation, seeds), drinking water, electricity and agriculture. There were some variations. For example, law enforcement was prioritized in Aurahi and there was a significant expansion in the health budget in Birgunj.

¹⁷ Interview with the Chairperson on January 26, 2026.

While the nature of revenue sharing among the three tiers of government remains unchanged, given past practices of Fiscal Equalization grants being reduced, and negligible resources arriving from the provinces, concern regarding availability and dependability of revenues are widespread. Internal revenue collection has been impacted. For example, Ghorahi Sub-Metropolitan City initially targeted to collect NRs. 700 million in internal revenue, but this was revised down to NRs. 450 million following the Gen-Z protests.

The federal circular on contract staffing has largely been bypassed. The needs of the municipalities under dire emergency conditions highlighted other imperatives, especially in the absence of the Federal Civil Service Act. In Narainapur, instead of cutting, they were in the process of hiring 44 contract-based employees. Birgunj Metropolitan City maintains that its own local laws allow the mayor to appoint two advisors. Furthermore, firing contract staff was argued to leave vacant essential computer operators and they have been retained. In Aurarhi, the firing of contract staff has led to legal battles, further creating administrative stability in the context of a shortage of staff.

In terms of user committees, legal uncertainty prevailed. Following the Supreme Court's interim order regarding federal directives on user committees, the federal government failed to issue clarifying circulars to the sub-national levels. This has led to a complete lack of uniformity; some provincial and local and provincial bodies continue to work through user committees, while others have stopped entirely. No inter-governmental discussion has taken place to resolve this confusion.

Public Spending Aims and Realities

Analysis of public spending reveals that there were enabling conditions for budget reprioritization. Foremost, the political crisis caused by the Gen-Z movement prompted an urgent need to restore governance, resume public services, and organize the snap elections. This gave the interim

government a solid political mandate to implement swift fiscal actions, such as reprioritizing the budget, controlling expenditures, and enforcing financial discipline. Centralized policy directive enabled quicker decision-making and coordination across ministries and government levels. The Ministry of Finance played a proactive role under then Finance Minister Rameshwar Khanal. It established a technical task force to pinpoint low-priority projects, control non-productive spending, and coordinate financial adjustments among various ministries.

The need to finance the House of Representatives elections, rebuild damaged infrastructure, and compensate victims established clear priorities that justified reallocating resources and boosting political support for budget reprioritization.

At the subnational government level, the federal government's budget reprioritization decision and the circular issued by the Ministry of Finance served as policy triggers for provincial governments to begin fiscal adjustments. Although implementation varied across the two provinces studied, the federal directive established the initial framework for provincial actions. As provinces were also affected by the Gen-Z movement, this enabled provincial governments to implement short-term administrative adjustments, such as suspending non-essential expenses and reallocating resources to priority areas. Local governments were similarly faced with extraordinary levels of crises which allowed them to reallocate funds to address urgent needs, such as rebuilding damaged infrastructure, restoring services, and maintaining administrative operations. In some municipalities, between 20 to 50 percent of development budgets were reprioritized. Local governments, closest to citizens, prioritized urgent service restoration efforts, such as rebuilding office buildings, repairing ward offices and police posts, and procuring essential office supplies. This responsiveness enabled quick adjustments to local fiscal priorities. Local governments have direct accountability to citizens, which motivates them to focus on maintaining essential services and visible rebuilding efforts, thereby aiding the practical implementation of budget reprioritization.

While the budget reprioritization and expenditure cut faced little political or legal resistance at the federal level, obstacles to public spending cuts at the subnational levels were linked to the lack of consultation and coordination. To begin with, the federal government announced these reform programs centrally, without prior consultation with provincial and local governments. Further, while federal circulars were dispatched via email, there was a noticeable lack of joint discussion or follow-up regarding their practical implementation. This led to a situation where federal directives were often perceived as ‘administrative commands’ rather than collaborative policies, frequently resulting in interpretive conflicts with provincial or local laws. For example, in terms of federal-province relations, the Secretary at Ministry of Finance of Lumbini Province stated that while the Province is autonomous, in this ‘extraordinary situation,’ the federal government made a decision, and all seven provinces chose to own and implement it.¹⁸ However, the Secretary did relay that there was dissatisfaction regarding the budget cuts, and pointed to provincial dependence on the center. As noted above, the Madhesh provincial government cited its own autonomous status to reject the federal directives.

Coordination between the provinces and local governments replicated the same hierarchy. The Secretary at Lumbini Province Finance Ministry said, ‘We cut the total budget of what we provide to local municipalities by 20 percent. How they manage their internal cuts is entirely up to them. We simply followed the federal circular and implemented it through a cabinet decision.’¹⁹ As with Lumbini, the Madhesh provincial government undertook no consultation with local bodies while deciding to freeze the budget. The District Coordination Committee (DCC), which are constitutionally mandated to facilitate coordination, were found to be completely inactive in this reform process.

¹⁸ Interview with the Secretary on January 29, 2026.

¹⁹ Interview with the Secretary on January 29, 2026.

The top-down, mandatory budget cuts had real consequences. More specifically, the decrease in federal capital spending – estimated at around 17 percent – disrupted the execution of development projects, and postponed several scheduled programs and infrastructure activities, especially at the provincial and local levels. As resources were redirected to address urgent crisis-response needs, routine development costs and sectoral programs encountered implementation challenges.

Furthermore, the decision to cut back on equalization grants, which fall under the National Natural Resources and Fiscal Commission (NNRFC)’s jurisdiction, led to institutional tensions between the Ministry of Finance and the Commission. The move also heightened jurisdictional disputes among federal, provincial, and local governments. Local government associations – including the Rural Municipalities Association and the Municipal Association – publicly challenged the decision, stating that the cuts undermined constitutionally protected fiscal transfers. These institutional disagreements made it more difficult to implement budget reprioritization measures and weakened coordination across different levels of government. Budget reprioritization and expenditure cuts have also created uncertainty about future fiscal planning and resource allocation. According to the Resource Monitoring Committee of the National Planning Commission, the budget ceiling for the upcoming FY 2083/084 may be lowered. This expected reduction in fiscal space poses risks for long-term development planning and investment continuity.

Local governments, which are directly accountable to citizens, face increasing pressure when previously approved development projects cannot be carried out due to budget cuts. As noted by the Ward Chairperson of Ghorahi Sub-Metropolitan City - 13, residents questioned the delay of a previously approved road construction project after budget reductions affected ward allocations.²⁰ Such situations have led to public dissatisfaction and criticism of federal decisions to reduce the equalization grant.

²⁰ Interview with Acting Ward Chair on December 7, 2025.

Fiscal Administrative Reforms

Fiscal Administrative Reforms at the Federal Level

The Finance Minister Rameshwar Khanal had introduced ten key fiscal administrative reforms. These include tax administration modernization; paperless and faceless administration such as the GIOMS; business registration simplification; direct public engagement systems with a complaint email-box system; integration and coordination reforms; transparency and accountability mechanisms; digitization of financial transactions; revenue leakage control; ease of doing business initiatives; and legal and regulatory streamlining.

This report focuses on: digital governance rollout; Single-Window Systems; tax administration modernization, and performance metrics.

The GIOMS was launched at the federal level in 2022, but it was implemented at the ministerial level for the first time and made mandatory in the Ministry of Finance during this interim period. The GIOMS has been implemented in two ministries at the federal level: the Ministry of Information and Communications Technology and Ministry of Finance. Furthermore, the second phase of the Single-Window System is currently under implementation. Work is ongoing to link PAN with NID and the Online Tax Clearance System, while a ‘faceless audit’ system is currently in the development phase. Approximately 40 Taxpayer Service Offices have been abolished and 60,725 individuals and 221,169 businesses have

obtained online tax clearance certificates. These systems are at various stages of implementation and development. However, performance indicators to measure their effectiveness have not yet been established. Similarly, clear targets and timelines for achieving results through these systems have not been defined.

According to interviewees, the extent to which instructions to reduce risks by cutting unproductive and unnecessary expenditures have been adhered to would be measured only during the mid-term evaluation in the month of Magh, or mid-January to mid-Feb, on a sectoral, ministry-wise basis. The same applies for the directive to reduce personal secretariats for heads of offices, calculating which will be possible after administrative expenses are compared at the end of the fiscal year.

Within the Ministry of Finance, attempts are being made to make services as IT-based as possible. It was claimed that, while not entirely ‘paperless,’ the Ministry was operating in a fully ‘reduced-paper’ digital environment. Under the Digital Nepal Framework, staff capacity is being built to move everything to the digital domain. If legal hurdles are absent and IT human resources are available, there are considerations to replace computer operators with officer-level roles to shift toward an office-oriented system. However, an Under Secretary at the Ministry of Industry, Commerce, and Supplies stated that there is a shortage of skilled workers, as individuals skilled in information technology are often unwilling to work on a government salary.²¹

Apart from lack of human resources, the lack of reliable internet and electricity, and the need to ensure data integration and operational uniformity, remain the main challenges at the federal level to digital governance.

²¹ Interview with the Under Secretary on January 23, 2026.

Fiscal Administrative Reforms at the Subnational Level

Provincial status

Provincial governments have partially adopted systems developed and implemented by the federal government for fiscal administrative reform. Electronic payment services and online revenue systems are in place in Lumbini and Madhesh provinces. However, other systems have not yet been adopted, and formal discussions on establishing performance indicators have not yet occurred.

The Lumbini province government is working to operationalize a Digital Governance Framework. Key systems currently in use include SuTRA for accounting and financial reporting; Electronic Building Permit System (EBPS) for real estate and map approvals; and GIOMS and other systems. Although SuTRA was reported to be fully operational, GIOMS²² was found to have been implemented only within the health sector. Registrations, internal memos, and administrative notes have not moved online yet.

Cash payments have dropped nearly to zero. Everything from contractor payments to elderly allowances is sent directly to bank accounts via the District Treasury Controller Office. Lumbini is currently following the Federal Digital Governance Framework. Financial administration – billing, payments, attendance, inventory, and bidding – are all online. Technology and infrastructure were seen as obstacles for the provincial government. However, there was said to be no appetite for investment in this sector as

²² During an interview conducted on January 29, 2026, the Chief of the Medical and Monitoring Division, who also serves as the spokesperson and acting secretary of the Ministry of Health of Lumbini Province, stated that GIOMS had been implemented in the health sector. However, the report Lumbini Province Capacity Needs Assessment, Partnership Mapping Findings, Best Practice Options and Potential TA Deployments, published in June 2025, suggests that provincial digital governance systems, including GIOMS, were still being rolled out and had not yet achieved full integration and utilization across government institutions.

the public demand is for physical infrastructure, with budgets prioritized accordingly.

Digital governance in Madhesh Province is currently in a state of partial transition. Almost all payments are made via Electronic Funds Transfer (EFT). The cheque system has almost disappeared in the province unless there is an extreme emergency or a fear that the system might reject payment at the last minute. The Provincial Government utilizes Computerized Government Accounting System (C-GAS) for all financial transactions and the GIOMS has yet to be implemented. While digitalization is the priority, the system maintains a dual-track approach for reliability. The Single-Window System has also not been implemented.

Unlike expenditure, revenue collection has not been fully digitized across all levels. Birgunj claimed to be fully online with complete digital integration of tax and fee collection, and also in the process of developing a system for QR Code-based payments and home-based tax assessment. Janakpurdham had a hybrid system with some modules remaining manual. Aurahi maintained a manual process, with online revenue collection yet to be initiated.

While the foundational infrastructure for electronic payments is active, comprehensive systems for office management and business services remain largely unimplemented.

At the provincial level, the absence of performance frameworks appears more systemic than at the local level. Provincial governments lack centralized mechanisms for defining indicators, setting targets, and conducting standardized evaluations across sectors.

In Lumbini Province, Ministry of Finance officials confirmed there is no formal mechanism for evaluating performance related to systems or digitalization – any evaluation is left to individual ministries, producing fragmented and inconsistent practices. While provincial planning processes include broader policy goals such as growth projections and sectoral priorities, these are not linked to measurable indicators or monitoring

frameworks, creating disconnect between planning, budgeting, and evaluation. Weak alignment between political leadership and administrative structures compounds the problem, leaving performance evaluation informal, non-standardized, and secondary to immediate priorities.

This gap is not limited to Lumbini. Evidence from Madhesh Province points to the same absence of formal performance matrices, suggesting a systemic issue across Nepal's provincial governments.

In summary, provincial governments exhibit a more entrenched absence of performance matrices compared to local levels. The lack of standardized indicators, targets, and evaluation frameworks results in fragmented monitoring practices and weak accountability mechanisms. This limits the capacity of provincial governments to assess progress, ensure effective implementation, and link policy objectives with measurable outcomes. The provincial governments appear to be in a phase of incremental reform. However, they do not yet seem to have adopted the reform initiatives of the interim government. Furthermore, the federal government has also failed to advance its reform efforts in coordination with and support of the provinces. Consequently, no significant achievements are visible at the provincial level following the formation of the interim government. Instead, they appear to be continuously maintaining the same systems they had been practicing previously.

Local government status

At the local level, some systems are in place, but have not been uniformly implemented. In Lumbini, local bodies had independently adopted systems such as e-bidding, e-payment, e-filing, income software, and payroll systems. Efforts were made to merge these into integrated central systems like, Integrated Public Financial Management System (IPFM) to replace the local payroll system, and Revenue Management Information

System (RMIS) to replace income software. But data transition issues have emerged.²³

The Single-Window System has not yet been implemented. Officials have stated that the system is not currently viable because, ‘There are not many educated entrepreneurs,’ and because the market is dominated by small-scale businesses with very few large-scale enterprises. GIOMS has also yet to be implemented.

Some local levels have initiated online tax systems, but synchronizing tax administration in alignment with the federal structure remains an unfulfilled task. Missing links were evident in some municipalities where taxpayer details are online but there is no system for paying taxes online.

Local governments in Madhesh province have successfully transitioned to electronic payment systems, with SuTRA fully functioning. However, revenue collection has not been fully digitalized across all levels. Neither the GIOMS nor Single-Window System had been initiated in any of the local levels in the Madhesh studied for this report, with continued reliance on manual and paper-based flows, and fragmentation in business registration.

Provincial and local levels cited the lack of digital infrastructure necessary, specifically reliable internet and electricity as impediments to fiscal administrative reform. In Ghorahi, the internet was said to be so unreliable that staff often went home to finish tasks on their private connections. According to the Information Officer at Narainapur Rural Municipality, during the rainy season, the collapse of a single electricity pole can disrupt electricity supply for months, directly affecting digital service delivery.²⁴

²³ During this transition, data from local systems was not successfully transferred; some data was reported lost. USAID’s exit was stated to be particularly detrimental as it was supposed to assist in digital revenue and data migration. The result has been the need to manually re-enter records at a time of severe human resources crunch.

²⁴ Interview with the Information Officer on January 26, 2026.

Another obstacle was the lack of IT-skilled staff at the local level to manage complex software. In Narainapur, volunteers were being utilized to input critical and sensitive data. In Janakpurdham, the IT department was said to be weak, since the permanent staff refused to be updated on new technology.

A lack of digital literacy among service seekers was also cited. For example, in Ghorahi Sub-Metropolitan City, Mayor Narulal Chaudhary highlighted the challenge of limited digital literacy, noting that although electricity bills can be paid online, many customers continue to stand in long queues at the office to complete payments in person.²⁵ In another example, teachers are required to use the Education Management Information System (EMIS) to request their salaries, but many do not know how to use it to receive their pay, and require assistance.²⁶

Field findings reveal that most local governments operate without formalized performance frameworks. Defined indicators, measurable targets, and structured monitoring systems are largely absent, leaving performance evaluation ad hoc and office-dependent rather than institutionalized.

Local authorities acknowledge this openly. In Narainapur Rural Municipality, the Chief Administrative Officer confirmed there is, ‘No target and no measurement system in place.’²⁷ In Ghorahi Sub-Metropolitan City, the Mayor Chaudhary reported that no specific goals have been set for key initiatives such as digitalization.²⁸ In Butwal Sub-Metropolitan City, officials confirmed that neither indicators nor time-bound targets have been developed. Together, these accounts show that core elements of a performance matrix – indicators, benchmarks, and timelines – are missing

²⁵ Interview with Chaudhary on January 28, 2026.

²⁶ Interview with Bhawani Giri, Education Officer, Ghorahi Sub-Metropolitan City, conducted on January 28, 2026.

²⁷ Interview with the Chief Administrative Officer on January 26, 2026.

²⁸ Interview with Chaudhary on January 28, 2026

at the local level, a gap that sectoral officials, particularly in education, link directly to weak and inconsistent evaluation.

Isolated exceptions exist. Aurahi Rural Municipality uses the Local Government Institutional Capacity Self-Assessment (LISA) system, through which all branches submit progress reports – a more institutionalized practice, though one that functions primarily as a reporting mechanism rather than a comprehensive performance matrix, lacking sector-specific indicators and outcome-based measurement. In Ghorahi, IT personnel conduct system-based monitoring to track operational effectiveness. But this remains technical in nature and is not embedded within a broader evaluation framework.

Overall, local governments show a pattern of weak performance measurement institutionalization. Partial mechanisms like LISA-based reporting offer some progress tracking, but the absence of formal matrices limits accountability, consistency, and the ability to assess development outcomes.

Decentralizing Taxpayer Services to Local Governments – Kerabari Rural Municipality

As part of fiscal administrative reform, the Government of Nepal began restructuring taxpayer service delivery by closing several Taxpayer Service Offices and transferring selected services, such as issuing PAN certificates, to local governments. The reform aimed to make tax-related services more accessible to citizens, especially in remote areas, and to bring administrative services closer to taxpayers.

Kerabari Rural Municipality in Morang district was chosen as the pilot local government for this initiative. The Taxpayer Service Program was launched in the municipality on December 24, 2025, with federal minister and officials from the Ministry of Finance and other senior government representatives present. During the launch,

services previously managed by the now-defunct Taxpayer Service Office in Birat Chowk were partially transitioned to the municipality.

Under the program, Kerabari Rural Municipality offers services related to Personal and Commercial PAN registration. According to the rural municipality Information Officer, the local office helps with issuing new PAN, replacing lost PAN cards, and correcting taxpayer information²⁹. However, tax payments are still made through the Inland Revenue system connected to the Inland Revenue Office in Biratnagar, using the taxpayer's personal login credentials.

According to Bharati Dhital, the officer overseeing the program at the rural municipality, two staff members from the former Birat Chowk Taxpayer Service Office provided a brief orientation on the day of the inauguration.³⁰ The training was mainly limited to technical aspects, such as entering signatures and thumbprints into the system and accessing the PAN registration portal. Since then, municipal officials report that no formal follow-up, monitoring, or technical support has been provided by the federal government.

As a result, municipal personnel have mostly relied on self-learning and informal assistance, including consulting online resources and contacting former tax office employees for guidance when technical issues occur. Ms. Dhital also noted that the municipality did not receive any additional infrastructure, equipment, or staff to support the new responsibility, except for printing materials needed for PAN cards. Within two months of implementation, the municipality had served between 50 to 60 service seekers.

The reform also faced initial resistance from some stakeholders, mainly due to concerns about closing existing taxpayer service offices and shifting responsibilities to local governments without sufficient

²⁹ Interview with the Information Officer on January 26, 2026.

³⁰ Interview with Dhital on January 26, 2026.

preparation. Despite these worries, the government kept expanding the initiative. By January 2026, taxpayer services had been extended to 22 local governments nationwide. The Finance Minister Rameshore Prasad Khanal announced via social media that residents of remote municipalities such as Chumnuhari and Khumbu Pasang Lhamu Rural Municipalities can now complete their tax obligations from their own local areas, emphasizing the government's goal to improve service access in geographically remote regions.

While the experience of Kerabari Rural Municipality shows the potential benefits of bringing taxpayer services closer to citizens, especially in remote areas, it also highlights the operational challenges of decentralizing fiscal administrative services without sufficient training, infrastructure, and institutional support. At the same time, the initiative is an important step toward strengthening federalism in Nepal by devolving administrative functions and expanding the role of local governments in public service delivery.

Institutionalization of Reform Points

The fiscal administrative reforms initiated by the Interim Government was enabled by already existing frameworks and processes for public financial management, including the Public Procurement Act, Finance Acts, and PEFA-based monitoring practices. These frameworks provided a foundation that enabled the government to implement budget reprioritization without requiring new systems. Existing digital systems like electronic payment platforms, online PAN registration, digital tax clearance services, and GIOMS supported fiscal transparency, payment monitoring, and administrative continuity during the reform process.

The fact that The High-Level Economic Reform Recommendation Commission (2024) had already suggested reforms related to tax modernization, digital governance, and administrative simplification further enabled the reforms. These earlier recommendations offered

technical guidance and legitimacy for implementing digital and fiscal reforms.

At the subnational levels, the federal government's budget reprioritization decision and the circular issued by the Ministry of Finance served as policy triggers for provincial governments to begin fiscal adjustments. Although implementation varied across provinces, the federal directive established the initial framework for provincial actions. The extraordinary circumstances following the Gen-Z movement further enabled provincial governments to implement short-term administrative adjustments, such as suspending non-essential expenses and reallocating resources to priority areas. At the local level, authority over their own budgets enabled local governments to reallocate funds, adjust development budgets, or utilize internal resources to address post-crisis needs. Several municipalities, such as Birgunj, Butwal, and Ghorahi, have fully adopted digital revenue systems, while others have only partially implemented them. These systems are promoting greater transparency and efficiency in local financial management.

Embedded Systems vs. Work-in-Progress

Based on the findings from the interim period (September 2025–March 2026), PFM efforts can be analytically divided into two categories: implemented and institutionalized reforms, and those that remain at inception phase or are work-in-progress reforms. At the same time, it is important to distinguish these from temporary fiscal measures, such as budget reprioritization, which – while significant – do not constitute structural reforms in themselves.

Implemented and Institutionalized Reforms

This category includes reforms that have moved beyond pilot stages and are now embedded in routine administrative and financial practices across

different tiers of government. Their integration into daily operations provides a degree of permanence, making them difficult to reverse.

A key area of progress is the digitization of financial transactions. The transition toward electronic payment systems is now well advanced, with EFT largely replacing cheque-based transactions across federal ministries and in provinces such as Lumbini and Madhesh. This shift has strengthened transparency, reduced delays, and improved traceability in public financial operations.

In parallel, core financial management systems have achieved significant uptake. Already established systems such as SuTRA, used for accounting and financial reporting, are fully functional at the provincial level and widely used by local governments, creating a more standardized and consistent framework for fiscal management across the federal structure.

There has also been progress in administrative simplification, with practical reforms aimed at reducing procedural burdens. The removal of postal stamp requirements for many government transactions, for example, represents a small but meaningful step toward streamlining administrative processes and improving service delivery for citizens and businesses.

Taken together, these reforms reflect incremental but important shifts toward a more digital, standardized, and user-oriented PFM system.

Reforms at Inception Stage and Works-in-Progress

In contrast, several reform initiatives remain at an early stage of development, pilot implementation, or partial adoption, with significant variation across provinces and local governments.

Digital governance systems illustrate this unevenness. While platforms such as the GIOMS have been made mandatory in select federal ministries and departments, its adoption has not yet extended meaningfully to subnational levels. As a result, integration across systems remains incomplete. However, provincial governments are beginning to move in

this direction. In Madhesh Province, discussions establishing GIOMS are currently underway, indicating growing recognition of its importance. In contrast, Lumbini Province has taken a more advanced step by already incorporating GIOMS in its plans and budget.

Similarly, tax administration modernization is still in progress. Key components – including the integration of PAN with the National ID system, and the development of ‘faceless audit’ mechanisms – are under development. Although online tax clearance services have expanded, many municipalities still lack the infrastructure to support fully digital tax payment and administration processes.

The Single-Window System for business services also remains largely unimplemented at the provincial and local levels. In many cases, local officials perceive it as misaligned with the realities of predominantly small-scale and informal economic environments, suggesting the need for more context-sensitive design and phased implementation.

Efforts to decentralize taxpayer services further highlight both potential and constraints. Pilot initiatives – such as those implemented in select rural municipalities – have improved access to services like PAN registration. However, these initiatives continue to face limitations related to staffing, infrastructure, and the absence of sustained technical support, raising questions about their scalability.

Eliminating Postal Stamp Requirements

To simplify administrative procedures and eliminate outdated bureaucratic practices, the Government of Nepal decided to stop using postal stamps in government transactions unless required by law. The decision was made during the 41st meeting of the Council of Ministers on December 15, 2025, and was broadly welcomed as a practical reform to make routine interactions between citizens and government offices easier. For many years, postal stamps had been routinely needed for

various government applications and official documents, even when their legal necessity was unclear. This practice often added extra steps for citizens seeking public services and created small but cumulative costs for service users.

The decision followed recommendations from the High-Level Economic Reform Commission, which was tasked with identifying structural and procedural barriers that impact economic activity, public service delivery, and administrative efficiency. In examining administrative practices, the commission found that the continued use of postal stamps in many government processes was an outdated requirement that no longer served a clear administrative or fiscal purpose. Although postal stamps historically provided some government revenue, their fiscal contribution remained small because the stamps used in administrative procedures have low monetary value. Removing this requirement therefore had minimal fiscal impact while offering the potential to simplify administrative procedures.

The requirement to attach stamps to official documents comes from the Stamp Duty Act of 1963, which mandates using stamps on certain documents to ensure their legal validity. However, experts have long argued that this requirement is outdated and creates unnecessary bureaucratic hurdles, especially as government systems increasingly shift toward digital service delivery and electronic documentation. The persistence of these procedural requirements has also been linked to broader challenges in Nepal's administrative environment. According to the World Bank's Ease of Doing Business 2020 report – which has since been discontinued – it took 22.5 days to register a business in Nepal. The report noted that procedural requirements such as attaching stamps to registration forms contribute to delays and administrative burdens in the business registration process.

In this context, the cabinet's decision to stop requiring postal stamps aligns with the Ministry of Finance's broader efforts to modernize

government systems, promote digital administration, and make it easier to start and run businesses. By removing a small but burdensome administrative requirement, the reform helps lower transaction costs for citizens and businesses and supports the government's ongoing efforts to improve the business environment.

Acting on the Commission's recommendation, the cabinet instructed government offices to stop requiring postal stamps in administrative procedures unless their use is explicitly mandated by law. The decision was widely appreciated by citizens, businesses, and administrative observers because it removes a minor but persistent procedural obstacle that had long complicated routine government transactions. This case shows how knowledge gained through policy analysis, international benchmarking, and reform commissions can help make policy decisions and administrative reforms smoother. By systematically identifying procedural inefficiencies and suggesting clear corrective measures, the High-Level Economic Reform Commission provided the analytical foundation that enabled policymakers to adopt the reform with relatively little resistance. The decision thus demonstrates how evidence-based policymaking can support small but meaningful reforms that improve administrative efficiency, lessen bureaucratic burdens, and promote a more business-friendly and citizen-centered governance system.

A deeper analysis of the institutionalization of reform points – reforms that have been successfully implemented, and are therefore harder for an incumbent government to reverse, and those that remain at the inception or work-in-progress stage – is challenging for two main reasons. This includes the short timeframe in which these fiscal administrative reforms were initiated in its limited tenure by the Interim Government. Certainly, this timeframe was one of immense crisis – many of the municipality offices included in this study had been severely damaged, and officials were

forced to work with shortages of office space, personnel, access to basic office equipment like tables, chairs, and computers, and even electricity. Making strides in fiscal administrative reforms naturally appeared far from the priority at the local level, while at the provincial level, as noted above in relation with Madhesh Province, issues arose where provincial authority superseded federal directives.

Secondly, no mechanisms were put in place to monitor implementation. None of the three tiers of government has established a separate or dedicated mechanism to track the progress of budget reprioritization or fiscal administrative reforms. Tracking is currently reliant on existing reporting lines. Data on budget expenditures, project status, and program implementation are collected through regular line ministries across the three levels of government. Because the reprioritized budget has either not yet been fully mobilized or is still in its preliminary stages, there has been a noticeable lack of focus on assessing the actual status of implementation.

The research has revealed that the federal government has relatively stronger technical capacity, more established administrative structures, and better-developed digital infrastructure, which enables it to initiate and implement reform measures more quickly and systematically. This allowed the federal government to design and launch reforms more rapidly. Provincial governments had already partially adopted federal digital systems, implementing electronic payment and online revenue collection systems that promote greater transparency and efficiency in fiscal management. Municipalities such as Birgunj, Butwal, and Ghorahi, have fully adopted digital revenue systems, while others have only partially implemented them.

However, the move toward digital financial management systems, paperless administration, and technology-enabled service delivery has exposed gaps in institutional readiness, technical skills, and supporting infrastructure. One of the main obstacles to federal fiscal administrative reform is the limited development and uneven availability of digital

infrastructure needed to support technology-based systems. Successful digital governance relies on essential resources, including digital devices, reliable internet access, stable electricity, accessible systems, and user-friendly digital platforms. Gaps in these core components continue to hinder the execution of digital administrative reforms. In several rural municipalities – such as Aurahi and Narainapur rural municipalities – the digital infrastructure needed for fiscal administrative reforms has not yet been fully set up. Even in larger municipalities like Ghorahi, Birgunj, and Butwal, rural parts within their jurisdictions face weak internet connectivity and system instability, which impacts the reliability of digital service delivery.

The shortage of well-trained technical personnel is another significant obstacle to implementing reform at all levels. Even federal agencies struggle to recruit and retain skilled information technology professionals. According to an Under Secretary at the federal Ministry of Industry, Commerce, and Supplies, individuals with advanced digital and technical skills often refuse to work within the Government of Nepal’s salary scale, leading to frequent turnover.³¹ Consequently, government agencies face difficulties in maintaining the technical capacity needed to support and grow digital governance systems.

Another challenge which hampers accessibility and slows down the use of digital administrative services comes from language barriers on digital platforms, which are mostly in English. Both Nepali-speaking and non-Nepali-speaking communities struggle to navigate these systems, especially in provinces with diverse languages.³²

Although the policy framework for fiscal administrative reform is consistent across the federal system, implementation capacity varies greatly across regions and institutions. When the federal government

³¹ Interview with the Under Secretary on January 23, 2026.

³² During DRCN researchers’ field visits to Lumbini and Madhesh provinces in January–February 2026, representatives of both provincial and local governments identified language barriers as a key challenge.

mandates digital reporting or online administrative procedures, some provincial and local governments cannot meet the required deadlines due to infrastructure and capacity limitations. In some cases, efforts to uphold fiscal discipline through digital systems may also delay service delivery. Limited infrastructure and technical capacity at the provincial and local levels have sometimes increased reliance on federal support mechanisms rather than strengthening administrative independence.

Overall, the barriers to implementing fiscal administrative reforms reveal structural disparities in institutional capacity across Nepal's federal governance system. While the federal government has launched several digital and administrative reforms, their successful implementation remains limited by gaps in digital infrastructure, shortages of skilled technical personnel, uneven institutional readiness, and coordination issues across government levels. These factors have led to inconsistent reform adoption and varying capacities for implementation across federal, provincial, and local governments.

Conclusion

The implementation of budget Reprioritization and fiscal administrative reform in Lumbini and Madhesh provinces is hindered by a complex web of legal, structural, and technical obstacles. The destruction of physical infrastructure like buildings, IT hardware, vehicles, etc., during the Gen-Z movement remains the most immediate hurdle to resuming standard operations and reform actions. Continued delay in passing the Federal Civil Service Act has left administrative federalism incomplete, causing persistent confusion in staff management. Significant conflict exists between federal circulars and provincial and local laws, leading to administrative deadlocks. Additionally, a critical shortage of skilled technical personnel is stalling the transition to effective digital governance.

Political tension between the levels of government in Nepal, mostly linked to incomplete status of political federalization, is central to this tussle. While federal circulars and directives provided a clear policy direction, they also fostered a perception at the provincial and local levels of increased centralized control. The lack of sufficient prior consultation and a concrete implementation roadmap led to confusion, along with varying degrees of resistance within sub-national governments. The absence of an effective inter-governmental mechanism between the three tiers has turned reform implementation into a series of isolated, uncoordinated actions rather than a unified national effort. In short, there are no robust institutional mechanisms to ensure shared ownership of reforms.

Recommendations

Policy and Legal Framework

- **Replace unilateral circulars with a negotiated intergovernmental coordination protocol:** The experience of the Karki Government shows that the issue was not with provincial resistance, but with the federal government bypassing the constitutional framework of federalism. Both Madhesh's resistance and Lumbini's reluctant compliance stemmed from decisions that were centrally imposed without consultation. The newly elected government should end this practice by establishing a formal *Intergovernmental Coordination Protocol*, developed jointly with the Inter-Provincial Council and local government associations. Any measure affecting subnational budgets, staffing, or administration should require structured pre-decision consultation, with a defined window for provinces and local governments to assess legal compatibility and raise concerns. Where constitutional ambiguity exists, disputes should be referred to the Constitutional Bench rather than resolved unilaterally. This approach will strengthen trust, ensure shared ownership, and enable more durable reform implementation across all tiers.
- **Civil service reform:** The **Federal Civil Service Act** must be passed immediately to complete the framework for administrative federalism and to provide staffing stability.

- **Transitional staffing policy:** A clear, interim policy for managing **contract employees** is needed to ensure that service delivery is not paralyzed during administrative transitions or budget cuts.
- **Legislative protections for health and education budgets:** While municipalities in both provinces instinctively protected health and education spending during the 2025 crisis, this was done on an ad hoc basis with no legal underpinning. The government should enact statutory minimum spending floors for health, education, and drinking water services at all three tiers of government, ensuring these sectors cannot be reduced below a defined threshold even during formal budget reprioritization. These floors should be indexed to demographic data and reviewed frequently by the National Planning Commission in consultation with the NNRFC.

Institutional and Operational Improvements

- **Mandatory coordination:** Regular coordination meetings between the three tiers should be institutionalized to share learnings and resolve implementation bottlenecks.
- **Revise the Disaster Management Fund regulations:** The experience of municipalities such as Aurahi and Ghorahi where officials were unable to rapidly access disaster funds despite documented crises reveals a regulatory failure, not a resource shortage. The government should revise the Disaster Management Fund regulations to allow local governments to access funds within 72 hours of a formally declared emergency, with simplified accountability procedures and ex-post auditing rather than pre-approval requirements.
- **Permanent staffing:** The Public Service Commission should prioritize filling approved permanent positions to reduce overreliance on temporary contract staff.

Strategic Priorities

- **Digital human capital:** Investment must be shifted toward developing skilled IT personnel to move beyond simple electronic payments toward comprehensive digital governance, and toward educating citizens in digital literacy.
- **Reform the Project Bank to end fragmented, politically driven spending:** The interim government's reprioritization exercise identified approximately 1,300 projects that were not even entered into the Project Bank, and over 4,000 fragmented or '*tukre*' projects. These are symptoms of a project approval system that prioritizes political patronage over development effectiveness. The new government must make mandatory Project Bank registration a legal precondition for budget allocation, with no exceptions. In addition, a minimum project size threshold should be introduced for capital projects, below which funding must be channeled through block grants to local governments rather than individual federal budget lines. An independent review panel, reporting to the federal parliament, should be established to annually audit the quality of projects included in the Project Bank.
- **Mandate GIOMS implementation across all three tiers with a funded rollout plan:** The GIOMS was implemented in only two federal ministries during the interim period, and has not been adopted in any of the subnational governments studied for this report. This partial rollout is not a sign of gradual progress – it reflects an implementation model that is failing. The new government should adopt a national implementation plan with a clearly defined timeline and adequate budget allocation to ensure the effective implementation of GIOMS. Each implementation must be accompanied by dedicated hardware procurement, staff training, and a designated federal support desk. Critically, data migration from legacy systems must be properly resourced: the

loss of data during the transition from local payroll and income systems, as documented in Lumbini, must not be repeated.

- **Develop a national digital infrastructure investment plan for subnational governments:** Reliable internet and electricity are not optional amenities – they are the foundational infrastructure for fiscal administration in a digital-first government. Municipalities such as Narainapur, where a single collapsed electricity pole can disrupt digital services for months, and Ghorahi, where staff use personal home connections to complete official work, cannot meaningfully implement digital governance mandates. The government must prepare a costed National Digital Infrastructure Investment Plan to specifically target subnational governments, with particular attention to rural municipalities across all provinces. This plan should prioritize backup connectivity solutions, including satellite and off-grid power, and should be developed in coordination with the Ministry of Energy and the Ministry of Communication and Information Technology with dedicated funding streams in the annual budget.
- **Establish Single-Window Systems as a national mandate with differentiated implementation timelines:** The Single-Window System has not been implemented at any provincial or local level studied for this report. Officials at local levels dismissed the system as unsuited to their small-business environment. This view must be challenged: the Single-Window System is not only a tool for large enterprises but a means of formalizing micro and small enterprises, expanding the tax base, and reducing informal payments. The government should set a firm national mandate for Single Window implementation, but with differentiated timelines for – metropolitan cities, sub-metropolitan cities, and rural municipalities – and adapt the system’s front-end interface for low-literacy users, including through multilingual options for provinces such as Madhesh.

- **Establish performance frameworks at provincial and local levels with federal facilitation:** Provincial and local governments should institutionalize their own performance frameworks, defining measurable indicators that directly link to the Fiscal Administrative Reform agenda. At the provincial level, this should include tracking the advancement of Single-Window System rollouts to streamline inter-ministerial service delivery and to reduce administrative bottlenecks. At the local level, existing tools like the LISA system should be developed into outcome-based matrices that monitor the digitization of revenue collection and procurement processes. The federal government should facilitate this by setting minimum technical standards for interoperability, ensuring that subnational performance data remains coherent with national digital transparency goals.
- **Institutionalize the decentralization of taxpayer services with adequate support:** The pilot at Kerabari Rural Municipality demonstrates the potential of bringing taxpayer services closer to citizens, but also reveals the risks of delegating tasks without adequate funding. The municipality received PAN registration responsibilities with a single day's orientation, no additional staff, no dedicated equipment beyond printing materials, and no ongoing technical support. The new government must move this initiative from pilot to policy – but only with the resources that genuine devolution requires. Each local government receiving expanded tax service responsibilities must receive a dedicated budget line for equipment and staff, few weeks training period with structured follow-up, a named federal support officer, and clear legal protection against audit liabilities arising from system errors outside local control.
- **Conduct a national budget quality audit and publish the results:** The interim government's reprioritization exercise revealed that a significant portion of the federal budget – estimated at NRs.

120 billion – was allocated to projects with no readiness status, no project bank registration, and no clear development rationale. The newly elected government should commission an independent national budget quality audit for Fiscal Year 2082/083, covering all three tiers of government, to quantify the extent of fragmented, unprepared, and politically motivated budget allocations. The results should be published as a public document tabled in the federal parliament, and should form the evidentiary basis for a comprehensive budget reform law to be enacted within the first two years of the new government’s term.

- **Invest in multilevel digital literacy as a public good:** The digital governance agenda will stall not only because of infrastructure deficits but because both citizens and government staff lack the skills to use it. Electricity bills have been online for years in several municipalities, yet residents still queue in person to pay in cash. Teachers cannot use Educational Management Information System (EMIS) to request salaries. These are not individual failures – they are systemic ones. The government must treat digital literacy as a public service, funding structured training programs for government staff at all levels, integrating digital skills into school curricula, and deploying community-level digital facilitators in rural municipalities. Platforms and interfaces must also be redesigned with defaults in languages of Nepal, and with simplified workflows tailored to low-literacy users, particularly in linguistically diverse provinces.
- **Conduct a structured post-crisis review and publish lessons learned:** The Gen-Z movement and its aftermath constituted an unplanned stress test of Nepal’s PFM systems across all three tiers. The new government should commission a formal post-crisis review covering budget reprioritization and fiscal administrative

reform across all provinces, not just Lumbini and Madhesh. The review should assess which systems proved resilient, which failed, and why – and its findings should be published as a public document that informs the design of future emergency fiscal protocols, the next PEFA assessment, and the government’s medium-term PFM reform strategy.

About DRCN

Established in 2014, Democracy Resource Center Nepal (DRCN) is a national non-governmental organization that conducts research on social and political issues. Since its establishment, the organization has conducted field-based and fact-based research on issues such as the process of implementing federalism in Nepal's transitional politics, local level restructuring, and election observation. DRCN has been presenting the findings of its research with stakeholders, and also conducting discussions and debates. DRCN's goal is to promote effective governance under Nepal's federal structure through such research and debates.

The interim government led by Sushila Karki, formed in the wake of the Gen-Z movement, advanced various public financial management reform initiatives under limited time and extraordinary circumstances. Efforts toward budget reprioritization, expenditure control, digital financial administration, tax system modernization, and service delivery improvement gave rise to new debates and practices within the federal governance system.

This study report by Democracy Resource Center Nepal (DRCN), titled *Public Finance Management Reforms in Nepal's Federal System: An Assessment of Karki Interim Government Initiatives*, analyzes the implementation, achievements, challenges, and impact of those reform efforts at the federal level, in Lumbini and Madhesh provinces, and across six local governments. It seeks to answer whether the interim government's reform efforts remained confined to policy declarations or moved toward the institutional transformation of financial administration and budget management. It also presents important lessons and recommendations for federal governance, financial accountability, budget discipline, and public financial management reform. This report serves as a useful reference for policymakers, researchers, development partners, journalists, and civil society actors with an interest in Nepal's public financial management, fiscal federalism, and budget and financial administration reform.



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