IMPROVING BUDGET IMPLEMENTATION

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Why Implementation is Important

• Much time spent by developing country governments (often with World Bank, IMF assistance or encouragement) preparing elaborate poverty reduction focused budgets
• But often these are not or cannot be implemented
• Much wasted effort – “it ends in tears”
• Greater recognition now that good budget implementation just doesn’t happen automatically
• Rather a sound budget implementation system is needed
• So we need to focus more on budget implementation issues
But there is a strong link with budget preparation

- Problems in budget implementation may reflect a poorly formulated budget – for example lack of credibility/realism
- Formulation and implementation processes and reforms are interdependent – two sides of the same coin
- for example both require reliable information on actual revenues and expenditure
- And lack of a comprehensive budget may complicate implementation – for example separate timetable and rules for capital budget, extra-budgetary funds
- And have spending ministries been fully involved in their budget formulation so that they understand and own their budget
- And how much budgetary devolution is there to spending ministries?
- That is what is level of detail of appropriations
- And what ex ante approvals are required for expenditure
Link with budget preparation

- And basis of accounting should follow the budget (cash, accrual etc)
- To properly diagnose and reform implementation requires some understanding of formulation
- Can’t effectively implement a poorly formulated budget
- The whole budget process from preparation through implementation and review should ideally be seamless
- But in practice fragmented institutional arrangements prevent this – different institutions may prepare the budget, release funds, monitor implementation and prepare budget execution reports – perhaps using different classification and reporting systems
Remember PFM Objectives

• Aggregate fiscal discipline and in year control
• Good strategic allocation of resources – pro-growth and pro-poor
• Operational efficiency – minimizing waste
• Budgets are thus not just macroeconomic instruments
• They are also the expression and intended implementation of government policies and priorities
• They are also the framework for service delivery
• i.e. Money not spent is not (necessarily) money well spent
• Also consider transparency as a separate objective
• And possibly also minimizing opportunities for corruption
Basic Budgetary Principles

(Australian Financial Management Improvement Program (FMIP))

• Managers at all levels know the level of resources they will receive and what they are to be used for
• Their budget has been determined through robust and open dialogue with MOF
• They know the expected results of this expenditure
• They have the flexibility and tools to achieve these results
• They have reliable financial and other information to enable them to manage
• As such they are accountable for financial and results management – they own their budgets
• As opposed to an MOF approach of budgeting by edict with limited engagement of spending ministries
• “Make the managers manage and let the managers manage”
Components of Budget Implementation System

- Release of funds
- Control and monitoring of expenditure – MOF and ministries
- Control and monitoring of revenues – MOF and ministries
- Cash and debt management
- Internal controls, including over payroll and procurement
- In year modifications of the budget
- In-year financial reporting
- Reporting externally on budget implementation
- External audit of budget implementation
- I will not further discuss revenue issues, debt management, internal controls or external reporting and auditing
Some issues

• Problems in budget implementation systems may reflect lack of incentives for good budget implementation, rather than lack of capacity
• What are the incentives for compliance or non-compliance – institutional issues are important, not just “technical” fixes
• To what extent are donors and their requirements part of the problem
  - project ‘ring fencing” requirements and non use of country systems
  - lack of predictability of donor funding, both project funding and budget support
• 3 PEFA indicators on use of country systems and predictability of support
• To what extent can we improve budget implementation (and PFM generally) in isolation from overall public sector reform?
• Greater complexity with unified budgets covering all level levels of government – provinces districts etc.
• Lack of information by centre on fiscal activities of sub-national government (China, Lao PDR, Cambodia, Thailand).
Cash Rationing – A caricature of budget implementation

• The budget is unrealistic – over estimated revenues and/or under-provision for expenditures
• Usually there is no system of commitment control
• During the year cash runs out
• Payments are frozen (are commitments also frozen?)
• Freeze may be across the board or on certain expenditure items
• Payments are authorized by MOF or a central committee in a non transparent way
• Expenditure arrears occur
• The freeze is disruptive to programs and suppliers
• High corruption potential – need transparent ex ante rules to determine payment priorities
• Budget priorities are likely undermined
• Revenue agencies are criticised for failing to generate sufficient revenues
• IMF previously saw cash rationing as good macro fiscal management
• Now it is regarded as a last resort to liquidity management and as inhibiting implementation of policies and priorities and good service delivery
PFM Diagnostics

- Now the accepted international benchmark for measuring PFM performance and improvement over time
- Supposedly collaborative between the country and all donors – leading to country owned and donor supported PFM reform program
- IMF plans to continue these under its “surveillance” role
- World Bank Public Expenditure Reviews and Integrated Fiduciary Assessments (previously also Country Financial Accountability Assessments - CFAAs) – Vietnam, Lao PDR, Cambodia, Philippines
- Some separate PFM assessments by ADB and European Commission
- OECD Budgeting Reviews – Thailand, Philippines, Australia
- In 2009 Lao PDR had 3 separate PFM assessments – PEFA, ADB and EC
- PEFA is now undertaking a further review of these different instruments to reduce duplication
- Consistent with donor undertakings at Paris HLF 2005 and Accra HLF 2009
Key Issues in Budget Implementation

• Budget realism/credibility – is the budget implemented as intended
• Predictability and timeliness in release of funds – to allow for orderly planning and implementation by spending ministries
• Cash management and Treasury single account
• Level and type of expenditure controls
• In year budget modifications
• Quality of information from GFMIS
• Budgeting/accounting integration
Budget Realism/Credibility

- PEFA assessment contains 4 indicators
  - Aggregate expenditure out-turn compared to original approved budget
  - Composition of expenditure out-turn compared to original approved budget
  - Aggregate revenue out-turn compared to original approved budget
- Note that many countries knowingly underestimate revenues as opposed to knowingly overestimate them
- For fiscal conservatism but also as a means of undertaking discretionary expenditure during the year
- In some countries revenue overestimation reflects legislature’s powers to adjust the proposed budget and provide additional expenditures
- Stock and monitoring of expenditure payment arrears
Predictability and Timeliness in Release of funds

- See PEFA indicator 16 – covers extent of cash flow forecasting and monitoring, reliability in year information given to spending ministries and frequency and transparency of adjustments to budget allocations
- Some OECD countries have abolished the warrant system
- Credibility/realism of the budget is an important factor in enhancing predictability and timeliness
- Frequently delays in implementing/continuing capital projects
- Capital expenditures are bunched at end of year
- Excessive ex ante approval requirements may delay budget implementation
- Procurement requirements may cause delays with higher prices charged by suppliers
- A key issue is improving the rate of budget execution
- Impact of donor requirements where donor funds are involved
Cash Management and TSA

- Objective is to assure funds availability, minimize borrowing costs and avoid idle cash
- Key tools are a Treasury Single Account (TSA) or ability to “sweep” separate bank accounts to manage as a single resource
- And cash plan at beginning of year
- Funds may be fully available at beginning of year or released monthly, quarterly
- Important link between budget, ministry programs and activity, linking commitment controls with cash payments
- Used for cash flow forecasting when linked with revenue forecast
- Allows orderly planned debt issuance
- But payment arrangements can vary - central payments system, payment by ministry from TSA
- Institutional arrangements – is Treasury autonomous from Budget office or works closely with it?
Level and Type of Financial Controls

- Central control versus managerial flexibility
- Level of detail of the appropriation items
- In any case centre needs information to monitor, but information does not need to be control
- Desirable extent of ex ante expenditure controls – and exercised by who?
- Or greater reliance on ex post review
- General trend to greater budgetary devolution to spending ministries
- Control of cash payments and/or commitments – also of costs if accrual budgeting used
- Is there a parallel system of staffing controls exercised by a central personnel agency (civil service commission etc)
- Anti-corruption issues are important here – more controls may not reduce opportunities for corruption
- More “gatekeepers” may mean more opportunity for corruption
In year budget modifications

• Need to be allowed for – circumstances change
• But too much revision suggests poor budget planning
• A formal six monthly budget review and revision may be good practice – with Parliamentary approval
• All modifications must be transparent and appropriately approved
• Determine in advance where expenditure changes may be made if necessary – either reductions or increases depending on revenues
• What degree of flexibility should be allowed to individual ministries in reallocations?
• Budget contingency allowance should cover urgent and unforeseen expenditures and be transparent – not a slush find for budget formulation oversights or good new ideas
• Should be controlled by the Budget office
• Budget office must be involved in any significant budget reallocations – as they reflect changes to previously agreed priorities and service delivery
Quality of GFMIS

- Needs to meet the needs of the centre (MOF) as well as spending ministries.
- The latter may not be adequately consulted in the design.
- And if the system does not meet their needs they will develop parallel systems.
- Many poor experiences in GFMIS development – “ending in tears”.
- Inadequate involvement of users, inadequate focus on deliverables, controlled by IT professionals, changes in design.
- Failure to recognize need for seamless processes.
- In some cases emphasis on transaction processing rather than report preparation.
- May not relate to budget preparation module or commitment controls.
- May commence around development of TSA.
Budgeting and Accounting

• Budget and accounting offices should be “reading from the same page”
• Perverse effects of IFAC accounting standards developed without knowledge or consideration of budgeting
• In some countries it has taken considerable time to sort out the mess created
• Particularly where full accrual accounting has been pursued
• Monitoring of budget implementation should be the responsibility of the budget office (?)
• Accounting provides a service – accounting systems should provide timely and reliable reports on budget execution
• Not just “accountants talking to accountants”
• Budgeting and accounting should have the same base – either cash, modified accruals or (perhaps, as in New Zealand and Australia) accrual