



Asian Regional Conference on Public Financial Management



***PFM Reforms: The lessons learnt -promises and
tears***

Session 3- Modernizing Budget Execution
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CHANGING CONTROL LEVELS IN BUDGET EXECUTION – PREPREREQUISITES AND PHASING

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- What is budget execution and why it is important?
- How capable are the budget execution systems in Asia, and Globally?
- What are different types of control frameworks?
- What is prompting countries to change their control frameworks?
- What are the global trends?
- What are the key concerns in transition?
- How these concerns could be addressed?
- What could be a possible approach to transition?

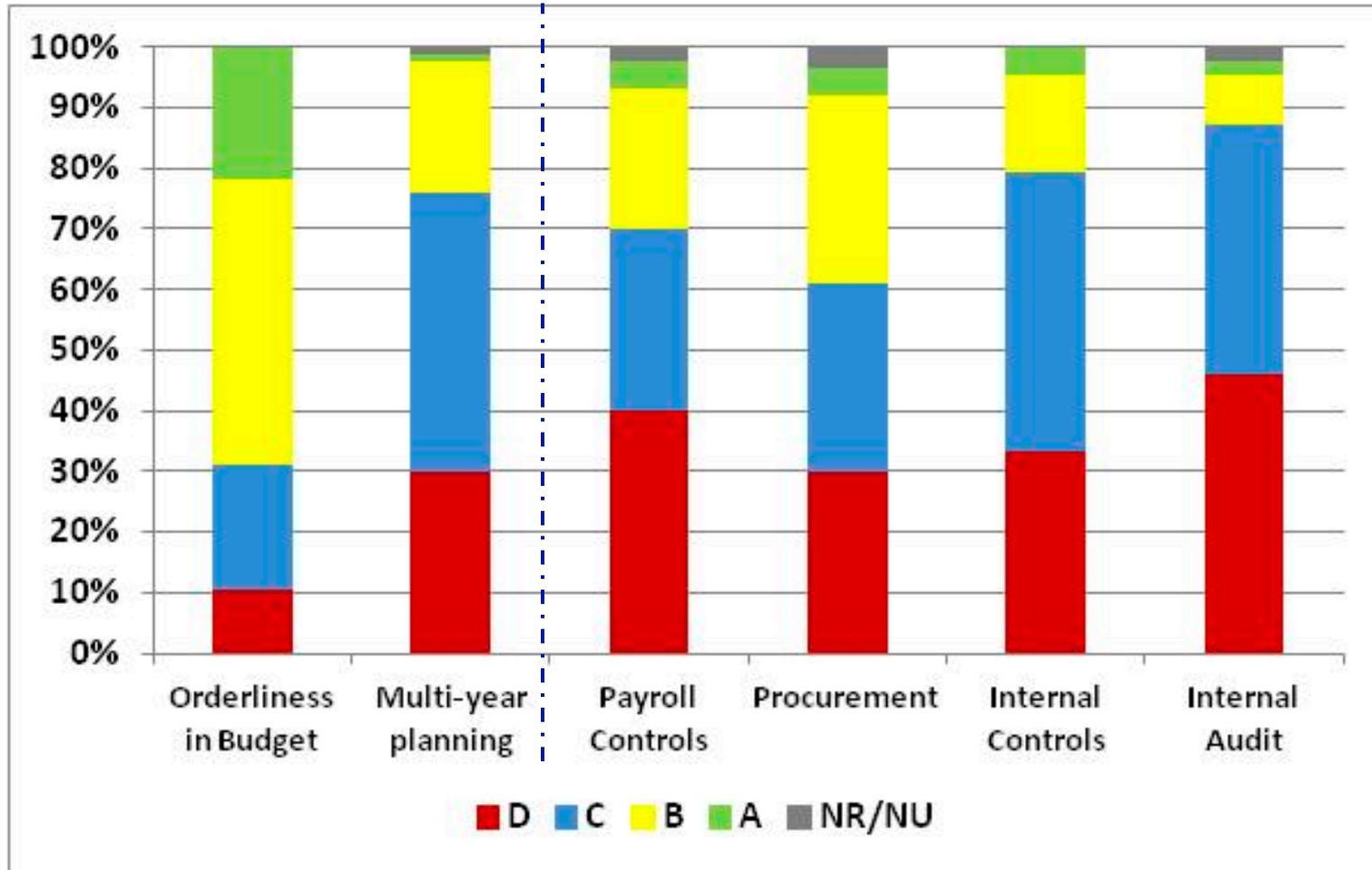
What and Why of Budget Execution

- What
 - Processes, institutions, and incentives to implement efficiently the budget [as planned].
- Why
 - Determines budget outcomes, including how efficiently outcomes are achieved
 - Impacts service delivery

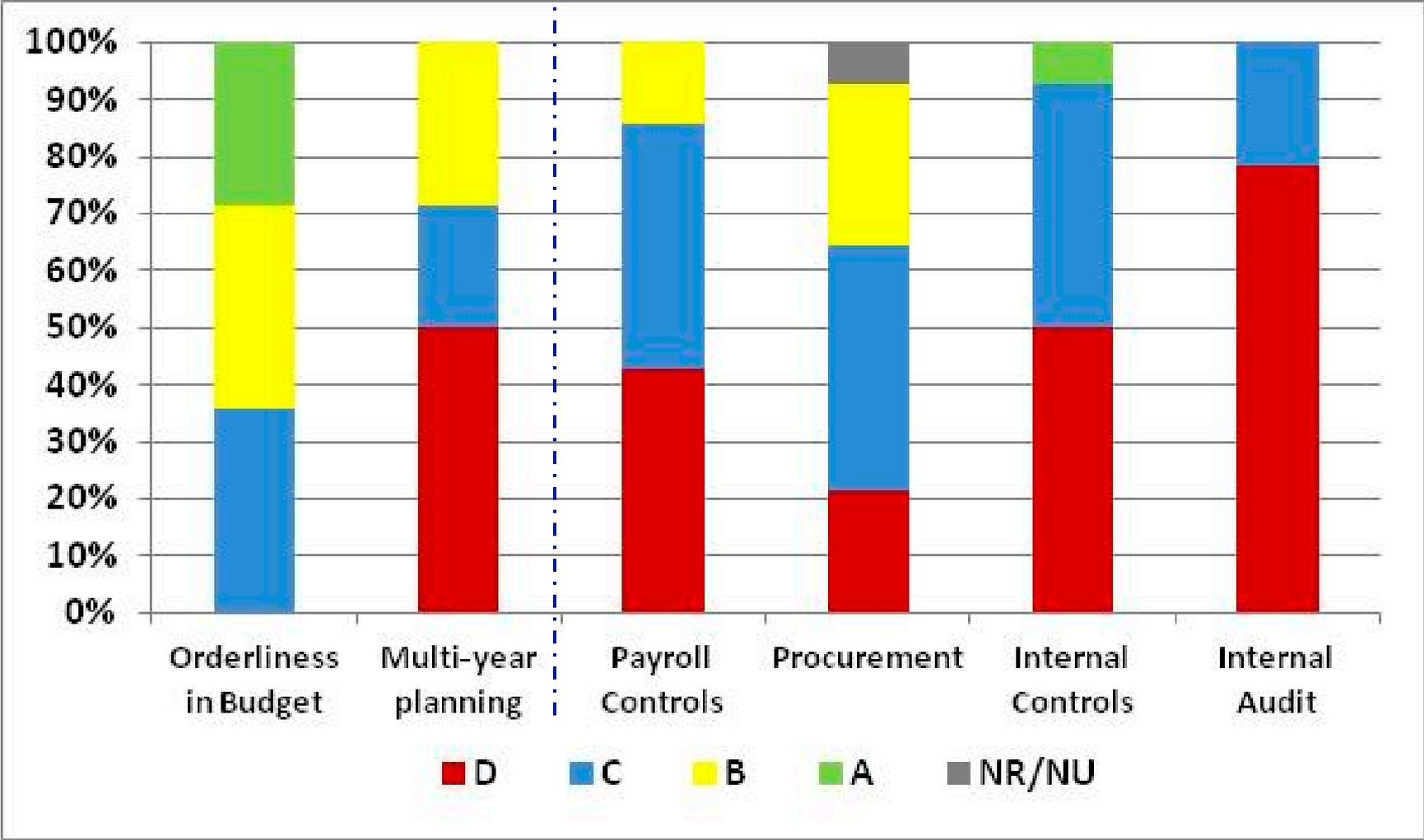
Elements of Strong Budget Execution

- Ability to execute the budget as planned
- Ability to adapt to changing macroeconomic environment
- Ability to respond to unexpected developments
- Ability to deliver services efficiently and effectively
 - Timely availability of funds
 - Efficient operations
- ***A framework – set of rules, procedures, institutions, tools, etc. - that facilitates all the above***

PEFA Scores: Global (87 Countries) 2006-2013



PEFA Scores: Asia (14 Countries) 2006-2013



Control Frameworks

	Externally Imposed (By Central Agencies)	Internally Controlled	Internally Managed
Discretion in resource deployment	No-Low	Low-Medium	High
Control focus	Inputs	Inputs	Outputs/Outcomes
Control mechanism	Pre-audit	Post-audit	Strong internal controls; performance goals setting
Nature of control	Transaction orientation; Compliance with rules	Some elements of systems orientation; Compliance with rules	Systems orientation; risk management
Accountability	Conformity with budget; use of inputs	Conformity with budget; use of inputs	Results
Center's role	Direct control over resources	In-direct control over resources	Policy guidance
Budget structure	Detailed line-item budgets	Detailed line-item budgets / Block budgets	Aggregate budgets with fewer budget-lines; Program/performance-based budgets

Why Change control Levels?

- Externally imposed controls:
 - often lead to delays in budget execution
 - make the budget rigid
 - limit managerial flexibility to deal with changing circumstances
 - can be time consuming
 - often fail to address the real issues (overstaffing, arrears)
 - budgeting tends to focus on preserving historical funding levels, rather than responding to new needs or targeting improved efficiency
 - Program managers assume little responsibility for spending funds more efficiently – low incentive to develop capacity to manage financial resources
 - breed compliance mentality, and a tendency to evasion of rules
- Flexibility promotes:
 - optimal use of resources
 - incentives for improving efficiency
 - achievement of results vs. compliance mentality
- Program managers are better placed to take program-specific decisions
- Too much flexibility without adequate checks and balance can be harmful

What is changing?

- Size and complexity of government
- The channels of service delivery – decentralization and delegation; third party delivery
- Technological innovations
- Performance orientation

Trends in Executive Flexibility

- Relaxed central input controls
 - Greater freedom to chose and alter resource mix
 - Appropriation and central control at a more aggregate level
 - Lump sum appropriations [70% of OECD countries for operating expenditure], often with one or more sub-limits (typically for employee related provisions)
 - Limited number of line-items - a quarter of OECD countries have fewer than 300 line-items, another quarter less than 1000 lines
 - Greater flexibility in investment spending over operational expenditure
 - Relaxed virement rules
 - Almost all OECD countries allow ministries to reallocate, with restrictions
 - Carry-over of appropriations, usually with restrictions, such as limits on annual or cumulative carry-over, or on draw-downs
- Devolved personnel management
- Decentralization of common services
- Traces of recentralization in recent years

Key Concerns in Devolution

- Fiscal discipline and sustainability
 - Overspending, increased deficits, arrear creation
- Unwarranted diversion of resources
 - Undermining the legislative mandate of the budget
 - Spending on low priority items
- Opportunity for abuse of powers and misuse of funds
- Weakened efficiency of expenditure

Pre-requisites for Relaxing Controls

- Spending departments
 - Formal assignment of financial management responsibilities to line ministries
 - A distinct finance function carried out by a dedicated unit
 - Clearly defined financial powers and accountability of key players, preferably enshrined in regulations
 - Formal transparent procedures for amending approved budget
 - A control framework that guards against:
 - Overspending – availability of funds before incurring commitments
 - Irregularity – consistency of expenditures with the approved policy objectives; authorization by a competent authority; misuse of funds
 - An accounting system that can track:
 - Transactions at each stage of the expenditure cycle; and
 - movements of funds between budget –lines
 - Regular and timely reporting of expenditures (including commitments) to the MoF
 - A transparent and competitive procurement system

Pre-requisites for Relaxing Controls...2

- Finance Ministry
 - Hard budget constraints
 - Timely release of funds
 - Cash planning in conformity with appropriations and open (carried forward) commitments
 - Strong monitoring mechanism
- External oversight
 - System and performance oriented audits
 - Effective legislative scrutiny and demand for accountability for results

Possible Approaches for Developing Countries

- **Phased transition**
 - Redefined accountability of program managers
 - Formal introduction of internal control and internal audit
 - Establishment of a centralized commitments monitoring system
 - Appointment of nodal persons in each department responsible for monitoring transactions
 - Relinquishment of ex-ante controls in two phases
 - Controls aimed at ensuring regularity of payments
 - Controls aimed at ensuring that commitments are within the budget appropriations
 - Reorientation of external audit to risk-based evaluation of systemic weaknesses
 - ❖ Less risky; opportunity for adjustments, as required; long transition time
 - ❖ A possible variant could include a threshold-based delegation

Possible Approaches for Developing Countries..2

- Conditional relaxation of controls
 - Relinquishing of controls conditional on achievements of standards in seven areas:
 - Budget planning
 - Output costing
 - Procurement management
 - Budget and funds control
 - Financial and performance reporting
 - Assets management
 - Internal audit
 - Easing of controls formally linked to line departments acquiring certain competencies, embodied in a signed MoU
 - Release of controls on a department by department basis - six pioneering agencies
 - Incentivizes line-departments to improve their management; stalled reforms due to slow progress by line-ministries
 - ❖ Avoid complexity and keep the targets realistic

- In most Asian countries the budget execution needs strengthening to achieve the intended spending outcomes - Asia is not alone in this regard.
- Externally imposed controls are useful for ensuring fiscal discipline, but are often inefficient and costly.
- Internally managed systems are likely to be more efficient in service delivery, but prone to the risk of indiscipline and mismanagement.
- Strong monitoring and accountability mechanisms/frameworks are necessary to cover these risks.
- Phasing of the transition should be country and context specific, but keeping it simple is important.
- Pre-requisites will include – existence of finance offices in line ministries with capacity to collect, process and analyze financial information; basic level of controls; ability to report timely to central agencies;
- Overtime develop internal audit, strong external oversight, and legislative accountability
- Phased relaxation of controls can reduce risks at the same time allowing capacity development in line-ministries

Fiscal Affairs Department

Ambrogio Lorenzetti; The Effects of Good Government on the City Life; Fresco; Palazzo Pubblico, Siena (Italy)

Thank You!

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