Establishing a PBO: The experience of African countries

Analytical Capabilities: Budget Formulation
Legislative Debate
Budget Preparation
Resource management
Accountability
Strategic Budgeting
Enactment
Reporting & accounting
Internal Control & Audit
External audit
Legislative Debate
Internal Control & Audit
Resource management
Reporting & accounting
External audit
Accountability
Budget Process
Budget formulation process allows for...

- A single allocation process that limits the possibility of “secret budget deals” being struck
- The reprioritisation of resources in order to accommodate new priorities or the scaling-up of an existing spending programme
- The allocation of additional revenue in accordance with the strategic priorities, which in most cases will require that trade-offs be made, often between equally high-priority programmes
- More inclusive budget decisions that considered both technical inputs and political imperatives
Why a budget process

PRIORITIES:
The perennial problem...

- Election promises
- SOEs
- Exom bills
- Public sector wage bill
- Budget deficit
- Social grants
- Service delivery backlog

How are we supposed to fit that into THIS?

Unaffordable flagship projects
Unforeseen disasters
Standard budget items

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... because there is a budget constraint

\[ G_t + r t B_{t-1} = T_t + B_t + A_t + O_t \]

- \( G_t \) is government non-interest expenditure in time \( t \);
- \( r t B_t \) is non-discretionary debt interest payments;
- \( T_t \) is taxes, fees, and other government revenues, including those arising from seigniorage (inflationary finance);
- \( B_t \) is total government borrowing (domestic and foreign net of use of deposits); and
- \( A_t \) is grants; and \( O_t \) is other sources of funds, such as sale of assets.
Budget process (2)

Executive

- Decide and agree strategic budget priorities
- Consider spending plans and make trade-offs
- Approve new budget proposal

Ministry of Finance/Budget

- Estimate of revenue available for new budget
- Budget Hearings
- Consolidation and finalization of proposed new budget

Ministries, departments & agencies

- Preparation and submission of spending plans
- Presentation of spending proposals at Budget Hearings
- Revise spending plans in accordance with the Executive Budget Proposal

Timeframe of between 3 and 9 months

Tabling of Budget for Legislative Approval
## Budget formulation checklist

<table>
<thead>
<tr>
<th>Topic</th>
<th>Action taken / to be taken</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Political considerations</strong></td>
<td>Can spending plans be aligned to the medium- to long-term strategy</td>
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<tr>
<td><strong>Broad consultation</strong></td>
<td>Are role-players routinely consulted, including the finance ministry, in the policy design phase</td>
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<tr>
<td><strong>Financial considerations</strong></td>
<td>Has a credible costing method been used to determine medium-term spending estimates</td>
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<td></td>
<td>Have different financial options been considered, such as public-private partnerships, user-charges, etc.</td>
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<td></td>
<td>If an MTEF is in place, can funding be deferred to a later year</td>
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<tr>
<td><strong>Implementation capacity</strong></td>
<td>Is there absorptive capacity, and can this be demonstrated from past performance</td>
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Financing the budget
## Financing the budget

<table>
<thead>
<tr>
<th>Sources</th>
<th>Application</th>
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<tbody>
<tr>
<td><strong>Taxes</strong></td>
<td><strong>Value Added Tax</strong></td>
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<tr>
<td></td>
<td>Tax:GDP</td>
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<tr>
<td></td>
<td>• Forecast</td>
</tr>
<tr>
<td></td>
<td>• Policy</td>
</tr>
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<td></td>
<td>• Administration</td>
</tr>
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<td></td>
<td>• Compliance</td>
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<tr>
<td><strong>Personal Income Tax</strong></td>
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<td><strong>Customs</strong></td>
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<tr>
<td><strong>Excise Duties</strong></td>
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<tr>
<td><strong>Grants</strong></td>
<td><strong>Budget Support</strong></td>
</tr>
<tr>
<td></td>
<td>• Integration</td>
</tr>
<tr>
<td></td>
<td>• Predictability</td>
</tr>
<tr>
<td></td>
<td>• Transparency</td>
</tr>
<tr>
<td><strong>Program</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Project</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Debt financing</strong></td>
<td><strong>Concessional (MDB)</strong></td>
</tr>
<tr>
<td></td>
<td>• Proportion between domestic and foreign</td>
</tr>
<tr>
<td></td>
<td>• Risks</td>
</tr>
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<td></td>
<td>• Sustainability</td>
</tr>
<tr>
<td></td>
<td>• Contingent Liabilities</td>
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<tr>
<td><strong>Domestic</strong></td>
<td></td>
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<tr>
<td><strong>Foreign</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Other</strong></td>
<td><strong>Privitization</strong></td>
</tr>
<tr>
<td></td>
<td>• Who pays: taxpayer or user</td>
</tr>
<tr>
<td></td>
<td>• Capabilities needed</td>
</tr>
<tr>
<td></td>
<td>• Understanding the market incentives</td>
</tr>
<tr>
<td><strong>Market participation</strong></td>
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</tbody>
</table>

*And improved fiscal space*
Fiscal space is commonly defined as the budgetary room that allows a government to provide resources for public purposes without undermining fiscal sustainability.

1. Conducive macroeconomic conditions
2. Re-prioritization within the budget
3. Foreign aid
4. Greater efficiency of existing government outlays
5. Market engagement

Ajay Tandon, WB
Better and more credible budgets
Budget credibility is undermined by...

• Unrealistic and escapist budgeting
  o authorizes more spending than governments can mobilize

• Hidden budgeting
  o real priorities are known to a small and narrow clique within government

• Deferred budgeting
  o real spending patterns are obscured by the generation of arrears

• Fiscal dumping
  o poor planning and absorptive capacity
Reforms to produce better budgets...

• Formalized budget preparation processes
  - Structure and formality to budget preparation process
  - Budget calendars
  - What decisions are taken and when

• Fiscal rules
  - Limits to spending or debt and deficits
  - Form of:
    - Balanced budget laws
    - Administrative ceilings to constrain budget proposals
Reforms to produce better budgets (cont...)

• Medium-term budgeting
  • Reconcile aggregate fiscal discipline and public spending plans
  • Aims to create better linkages between policies and plans and revenue and expenditure estimates

• Program-based budgeting
  • Shift from controlling inputs to emphasizing outputs and outcomes
  • Changes to resource allocation, responsibility and accountability

• Budget classification systems
  • Classifying according to economic, administrative or functional nature of budget items
1. Single allocation process
2. Policy informs budgets
3. Do not promise more than can be afforded
   - The needs are always more than can be afforded
4. Trade-offs are necessary
   - Trade-offs are between equally important plans
5. Value 4 Money starts with the budget process
6. Decisions need to be informed by a wide-array of evidence
7. Absorptive capacity must be considered
Thank you
Additional Slides
Conducive macroeconomic conditions

- Sustained economic growth = improved revenue generation = lower fiscal deficits and debt
- Economic growth in Africa still a commodities story
- Room for counter-cyclical fiscal policy has narrowed

- No escaping the need for diversification and skills development
Reprioritisation

- Making a case for a reallocation of resources from elsewhere (elsewhere could be funded differently – market)
- Space for reallocation in discretionary and non-discretionary expenditure

![Bar chart showing % of GDP in various countries.](chart.png)
Earmarked taxes

• Ensures the ring-fencing of revenue source, which makes it more political than economic
• Earmarking is often viewed as an imposition of an unnecessary constraint on fiscal policy-making - reduces flexibility and allocative efficiency

Ghana National Health Insurance

<table>
<thead>
<tr>
<th>2.5% levy on goods and services</th>
<th>75% of financing</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.5% wage related premium</td>
<td></td>
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<tr>
<td>(formal sector)</td>
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<tr>
<td>General tax funded budgetary transfers</td>
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Engaging the Market

- Investors – debt will be covered by revenue
- Lenders require assurance that debt will be repaid
- Fiscus needs certainty that costs will not overrun

- Risks and uncertainty contribute to raising the cost of finance
- Strong fiscus can lower the costs of finance – debt or revenue guarantees
- Guarantees can be provided by multilateral financial institutions (MIGA)

- Several advantages, such as combined oversight and risks sharing
  - Role for DFIs to bring funders together
  - But should be shared-funding of overall project

- Specialist transaction advisors appointed
- Contract management capability developed – public sector not very good at this

Andrew Donaldson, NT