

## **CG Meeting Donor Budget Support Group**

Budget support helps to increase the effectiveness of aid in several ways. It strengthens local ownership and accountability by linking aid more directly to local priorities. It can lower transactions costs by encouraging donors to harmonize their procedures with those of the Government. Finally, the promise of budget support provides a powerful incentive for Governments to improve budget and financial management systems and for the public to demand accountability about how resources are used.

The Donor Budget Support Group was formed after the last Consultative Group Meeting in response to the Government's statement that its preferred aid modality is untied budget support. It does not support specific sectors although the expectation is that resources channeled through this form of assistance will be allocated to priority programs identified in the IP-ERS and the annual budget strategy paper. Budget support therefore aims to make a significant contribution to the Governments economic growth and poverty reduction objectives.

The donor group is open to all countries and development agencies who are in principle willing to consider making this form of assistance available, with a view to coordinating the preparation and disbursement of such assistance in line with the Government's budget preparation process. Membership includes the EC, World Bank, DFID, KFW, SIDA, as well as the IMF.

### **Recent positive developments**

The donors have agreed with the Government on the terms of reference for a joint technical working group to ensure that the budget support is provided to the Government of Kenya in a coordinated manner and aligned with the IP-ERS. The group has also contributed to the organization of a high level Strategic Partnership with Africa workshop on the medium-term expenditure framework (MTEF), harmonization, on budget support and sectorwide approaches, which was held in Nairobi in June 2004. This meeting helped to clarify the general conditions necessary for coordinated budget support. Such conditions include an opportunity for coordinated dialogue during the budget preparation cycle to ensure that budget is comprehensive and pro-poor (taking into account the regional and gender dimensions of poverty), a positive assessment of progress in implementing the government's IP-ERS, and establishment of appropriate fiduciary safeguards that would provide assurance that donor resources would be effectively utilized to support implementation of IP-ERS priorities (taking into account the fragility of budget resources).

Some progress has been made in fulfilling these conditions. The government has established a new budget timetable that provides an opportunity for the government to review progress in IP-ERS implementation and discuss indicative levels of donor budget support early in the budget cycle. This expanded timetable also allowed for greater transparency and consultation in the budget formulation process.

However, the preparation of the annual progress report IP-ERS was delayed and the envisaged review has not yet taken place. Government has therefore decided to exclude budget support from the MTEF framework being used to prepare the budget strategy paper. It is hoped that based on the experience gained in preparing the first annual progress report of the IP-ERS and improvement in government capacity in the area of M&E, it will be possible to adhere to the agreed timetable next fiscal year.

A second area of progress has been in the coordination of fiduciary assessments. In May 2004, the World Bank together with DFID, EC, SIDA and the IMF completed a common assessment of Kenya's public expenditure management system based on an agreed set of international benchmarks, which cover budget formulation, execution and reporting. At the time of the review, Kenya had met 3 of the 16 benchmarks. The Country Integrated Fiduciary Assessment (CIFA) prepared in early 2005 confirmed that the Government now meets 5 benchmarks out of a total of 16. The government has agreed to update its Enhanced Financial Management Action Plan with the objective of meeting all of these benchmarks before the end of its current term of office in 2007. Donors have also agreed to coordinate their technical assistance in this area in support of the revised plan. Two donors who are actively considering budget support to Kenya have also linked the provision of budget support to progress in meeting additional public expenditure management benchmarks.

Although the government and donors have not succeeded in developing a harmonized timetable for key decisions on annual commitments or harmonized tranche release procedures and appraisal coordination, there has been some progress in these areas. The Bank has invited the EC and African Development Bank, the two other donors currently envisaging providing direct support for the fiscal 2006 Kenya budget, to participate in its identification and pre-appraisal missions. Coordination between the EC and World Bank has been closer in the preparation of their respective tranche release conditions. However, donors have not yet developed a common matrix listing key benchmarks to help to monitor the implementation of the IP-ERS, which could be a basis for agreed disbursement conditionalities for budget support. Even without such a matrix, continuing dialogue between the government and its partners on the budget outcomes is essential, given that the budget reflects government's priorities more closely than any other document.

### **Key challenges which must be addressed**

The dialogue on coordinated budget support has been to a great extent overshadowed by the Anglo-leasing affair and concerns that a number of other defense and security-related procurement programs are tainted by corruption. Although the government has subsequently tightened the administrative procedures governing security procurement, the slow pace of investigation and prosecutions on these matters and widespread public innuendos that cabinet ministers have directly and personally benefited from these transactions has dented the credibility of the Government's zero tolerance policy on corruption and led to a more cautious approach to the provision of budget support. In this

regard, passage of the new procurement bill currently before parliament, which provides for greater transparency and improved oversight of procurement, is an important benchmark of progress in strengthening the anti-corruption framework. Kenya's development partners are also keenly following the progression of the pending files in the Kenya Anti-Corruption Authority to ascertain whether high profile corruption cases can be satisfactorily solved.

The donor budget support group welcomes the introduction of the new budget process which aims to improve the coordination between ministerial public expenditure policy reviews and the MTEF with a view to strengthening the linkage between the IP-ERS and the budget. A key challenge for the budget strategy paper will be to specify the priority programs that will receive funding in the next budget and will be predictably funded during the period of the MTEF. A mechanism is also needed for ensuring that such programs receive priority should additional funding become available either through additional revenue efforts or increased support from development partners (particularly direct budget support).

Another challenge will be to improve budget execution; both by ensuring that proper expenditures in next year's and the remainder of the MTEF budget are appropriately funded, and by reducing virements and improving the utilization of committed resources. This in turn will require improvements in financial management systems, discussed in the related donor group report on public financial management.

### **Indicators of success**

The key indicator of success for this subgroup will be a substantial increase in the share of donor disbursements to Kenya in the form of budget support. A second indicator of success will be the proportion of such budget support that is considered sufficiently predictable to be included in the MTEF budget estimates as a line item identified by donor. A third indicator is that total disbursements of appropriations in aid increase.

Secondary indicators related to donor harmonization include the development of a common matrix of policy actions and outcomes which constitute agreed individualities for donors to disclose funds and the extent to which this matrix constitutes a subset of the policy agenda contained in the Government's IP-ERS and its annual progress reports.