

Linking the PRS with National Budgets A Guidance Note

**PREM Poverty Reduction Group
September 2008**



THE WORLD BANK

Linking the PRS with National Budgets

A Guidance Note

Introduction	3
1. Finding the gaps in the policy, planning and budgeting cycle.....	5
a) Typical Problems.....	5
b) Towards Stronger Links	6
c) Diagnostic & Reform Questions	8
2. Introducing a strategic phase and medium-term perspective to the budget process..	10
a) Typical Problems.....	10
b) Towards Stronger Links	11
c) Diagnostic & Reform Questions	14
3. Results Orientation in the budget process.....	16
a) Typical Problems.....	16
b) Towards Stronger Links	16
c) Diagnostic and Reform Questions.....	21
4. Alignment of PRS and budget reporting with decision making processes.....	22
a) Typical Problems.....	22
b) Towards Stronger Links	23
c) Diagnostic and Reform Questions.....	26
Key Resources	27

Acknowledgements

This guidance note was written by Tim Williamson and Vera Wilhelm and based on the report “Minding the Gaps” Integrating Poverty Reduction Strategies and Budgets for Domestic Accountability, V. Wilhelm, P. Krause (editors) World Bank 2007. The note was drafted under the guidance of Ana Revenga and Louise Cord (both PRMPR) and benefited from comments and support by James Brumby (PRMPS), Marijn Verhoeven (PRMPS), Duncan Last (IMF), Paolo de Renzio (ODI) and Kathy Hull (consultant). The production of the note benefited from financing by the Trust Fund for Environmentally and Socially Sustainable Development supported by Finland and Norway which is gratefully acknowledged.

Introduction

Links between the Poverty Reduction Strategy (PRS) and the budget, whether at the formulation, execution, or reporting stage, are integral to the successful implementation of the PRS and vital for strengthening government accountability. When the two systems are well integrated, three benefits are likely to emerge:

- PRS priorities are more likely to be implemented as planned.
- Spending agencies can be held to better account for performance.
- Parliament can have an increased role in monitoring PRS outcomes.

Yet low-income countries face significant challenges in trying to better link planning and budgeting initiatives. Fragmented institutional ownership and weak incentives have limited the ability of policymakers to link planning and budgeting processes.

The purpose of this note is to provide practical guidance to developing country practitioners and international donors. It builds on a study entitled *Minding the Gaps*¹, which was based on detailed case studies in nine low-income countries and a review of relevant experience in four higher-income countries. Specific lessons from the case studies are shown in Box 1.

Box 1: Four Lessons from Minding the Gaps

Lesson 1: Strengthen and harmonize existing processes and adopt a gradual approach to reform. The enhancement of the policymaking function of the budget in line with PRS priorities often requires a flexible approach to PRS design, building on existing processes. An increased focus on results requires not only technical capacity but also a change in organizational culture. Experience in the case study countries shows that successful budget reform processes tend to evolve gradually, through an integrated approach that links improvements in public financial management to broader civil service reform. In essence, short cuts tend not to work.

Lesson 2: Build support from within. Initiatives that may help to catalyze the improvement of core policy processes and internal accountability include:

- Introducing or reforming cabinet committee structures, to strengthen high-level political ownership and build a challenge function within the executive.
- Building policy links from the budget up, rather than from the PRS down, since most successful reform efforts have focused on turning budgets into more policy-oriented tools.
- Introducing a strategic phase in the budget process to ensure that sector managers and the cabinet review high-level policy priorities and their impact on inter-sectoral resource allocation before the preparation of detailed operational budgets.

Lesson 3: Target reporting to decision making processes. Reporting instruments best serve their purpose when they are instigated by, and remain linked to, decision making processes involving actors who are likely to demand and use the information. Priority should be given to reporting on domestic budget execution, rather than externally-driven Annual Progress Reports, while introducing outcome information alongside financial reporting whenever possible.

Lesson 4: Keep it simple. As the case studies show, comparatively simple budget reforms can significantly improve the budget's responsiveness to policies. Such reforms start with making budget execution credible and transparent. Structuring the PRS in a more budget-friendly manner, for example by sector, would facilitate the role of sector agencies in elaborating policy priorities. It could expand ownership and boost incentives for integration of key stakeholders, thereby strengthening domestic accountability.

¹ World Bank (2007)

This note provides guidance in four areas:

1. Identifying the gaps in the policy, planning and budgeting cycle.
2. Introducing a strategic phase and medium-term perspective to the budget process
3. Introducing a performance orientation to the budget.
4. Aligning PRS and budget reporting with decision making processes.

Each section sets out typical problems, emerging good practice, and a series of diagnostic and reform questions. Since successful strategies will rest on adapting ideas and tools to local circumstances, these questions are not intended as a blueprint. Rather, they are offered as guidelines to help practitioners to identify country-specific barriers to and paths for reform.

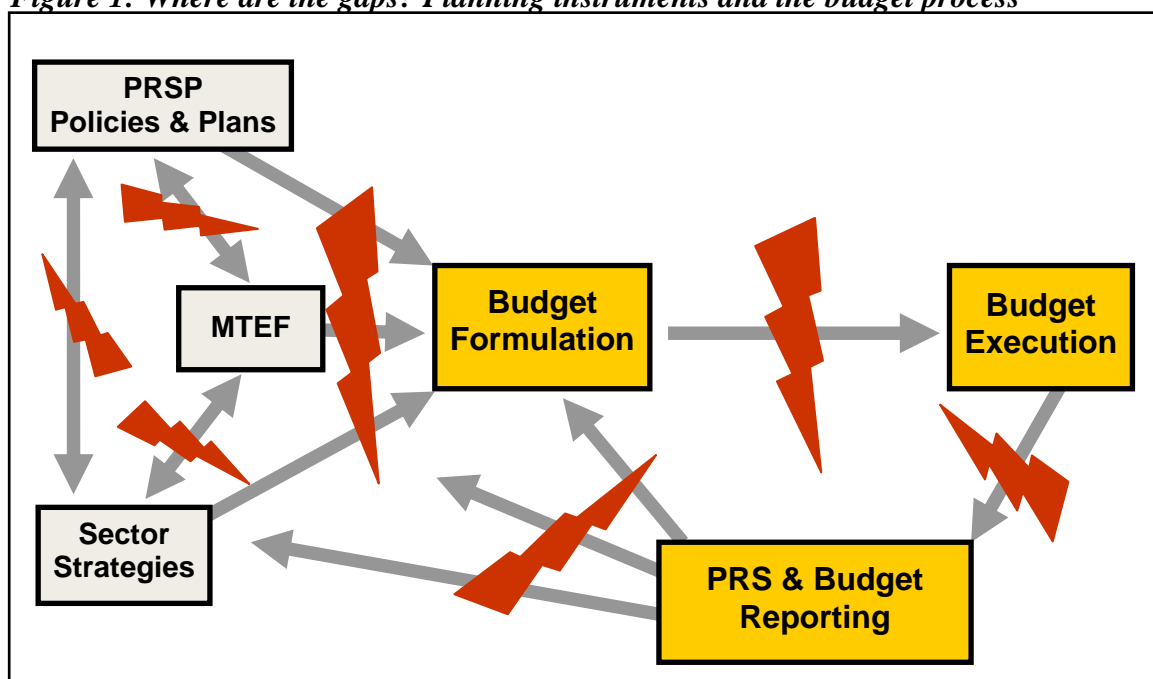
1. Finding the Gaps in the Policy, Planning and Budgeting Cycle

Fractures exist in nearly all planning and budgeting process, whether between the PRS and budget, the budget and actual spending, or the budget and reporting. To foster integration, it is important to build on existing systems and establish the basics of a credible budget.

a) Typical Problems

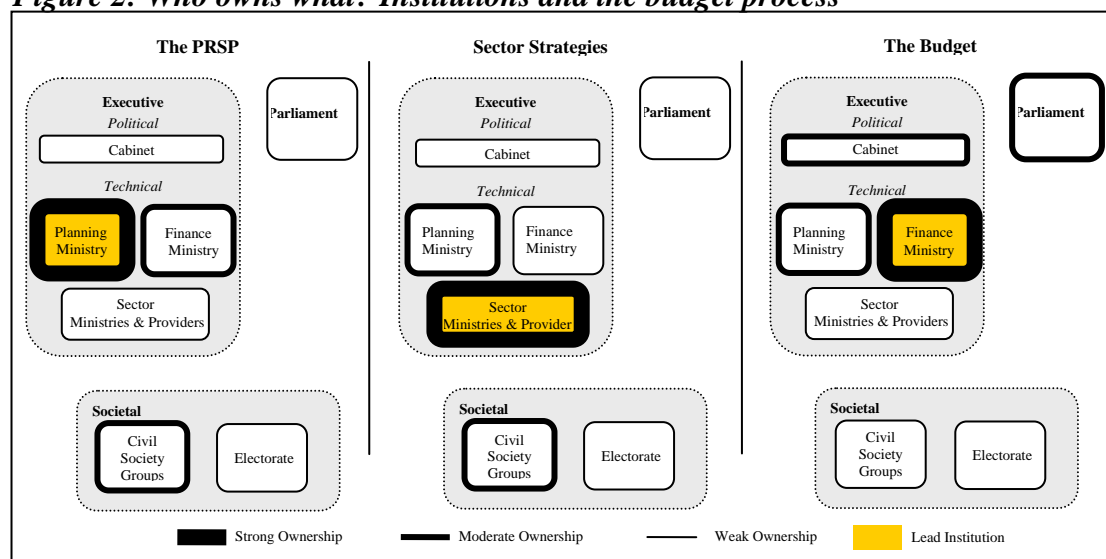
Gaps and fractures in planning and budgeting systems pose obstacles for attempts to integrate the two (Figure 1). Among the many typical problems, there may be: multiple sector plans that are not fully linked to the PRS; additional national development strategies exist alongside the PRS; and inadequate reflection of PRS and/or sector priorities in budget allocations. In addition, the budget may be unrealistic and not be implemented as planned, reporting on the budget may be limited to inputs, and PRS reporting may not be linked to the budget. Weaknesses and fractures at any point undermine the prospects of PRS policies being implemented effectively.

Figure 1: Where are the gaps? Planning instruments and the budget process



Key contributing factors to this fragmentation are the asymmetric patterns of ownership over different instruments and processes (Figure 2). For example, the Ministry of Planning may lead the PRS process, line ministries, the development of sector strategies, and the Ministry of Finance, the budget. Whilst ownership of these instruments is strong within the responsible institutions, it is moderate or weak elsewhere. Without a central driving force for linking these processes, there is often little incentive among stakeholders for integration.

Figure 2: Who owns what? Institutions and the budget process



b) Towards Stronger Links

Successful reforms have addressed the gaps by linking planning and budgeting systems whilst ensuring the basics of PFM reform are being tackled. The experience of higher-income countries (Australia, Chile, South Africa and South Korea) demonstrate three important lessons for overcoming gaps in planning and budgeting processes. First, domestic ownership of the reform agenda is crucial and often extends beyond the ministry of finance to the cabinet, and, in some cases, parliament and civil society. Second, an integrated approach to reform rests on strong institutional connections between planning and budgeting. And, third, the most effective reforms begin with getting the basics of public financial management right, before moving on to more sophisticated, performance-oriented reforms.

Emerging good practice from both higher and low-income countries demonstrates that there are often 3 steps to overcoming gaps in existing systems:

Step 1: Identify the weakest links in policy, planning, budgeting and reporting.

Often reforms to link the PRS and budget are undertaken without a comprehensive understanding of where the gaps lie. For example, there is little point trying to strengthen the link between the PRS and allocations set out in the MTEF if the MTEF does not form the basis of annual budget allocations. The first crucial step therefore rests in identifying the areas in which the most fundamental weaknesses in budgeting and planning occur.

Step 2: Address PFM basics from the outset.

A reliable budget is key to strengthened links between planning and budgeting processes, since the entire system will lack credibility if spending agencies do not receive their annual funding allocations during the budget year and spend in line with those budgets. Establishing a realistic overall fiscal ceiling and a top down resource envelope for the public sector provides the stable platform for credible resource allocations to spending institutions. The starting point is an accurate macroeconomic framework, which enables realistic expenditure allocations. Basic systems of budgeting, internal controls, accounting and reporting need to be in place to ensure that overspending does not take place and arrears are not incurred.

Box 2: Getting the basics right in Malawi

In Malawi, efforts to link to the PRS to the budget in 2002 failed as there was widespread fiscal indiscipline and informality in the budget cycle. Since 2004, the government has worked to establish credibility of the budget.:

“The change in Malawi’s political leadership [in 2004] and direction has begun to change the incentives around the budget. Fiscal discipline has been restored for the first time in about a decade. In general, sector allocations now remain within their ceilings..... actors in the public sector are aware that their spending wishes need to be included in the annual budget in order to be realised. The new salience of the budget thus creates a new incentive to integrate planning processes into the budget cycle.”

Malawi now has a basis to start addressing fragmentation in its planning and budgeting cycle.

Source: Minding The Gaps

Malawi’s experience (Box 2) is a case in point: unless basic PFM issues are tackled, more advanced reforms to link planning and budgeting systems are likely to flounder. There is, for example, little value in budgeting for results (i.e. what will be achieved with the money) if the mechanisms for budgeting for inputs (i.e. what the money will be spent on) are not credible. Similarly, there is little value in attempting to integrate PRS reporting with budget reporting if there is no established system for the latter.²

Step 3: Link policy, planning and reporting initiatives with the budget process.

Once PFM basics are established, the integration of policy, planning, budgeting and reporting processes is likely to yield greater results. High level ownership of the reform agenda is often crucial to ensure integration of disparate systems. Sections 2 to 4 all look at specific tools and systems which can help with integration.

As a general rule, successful reforms to integrate planning and budgeting rarely involve the creation of new “systems.” Rather, they tend to either build on or rationalize existing instruments. While there is therefore no single solution to integrating planning and budgeting processes, successful efforts have involved some or all of the following:

- A rationalization of different policy, planning and reporting instruments and a clarification of their respective roles (e.g. the integration of national planning instruments in Albania and South Korea described in Box 3 below).
- The consolidation of central functions into one ministry (e.g. combining the Ministries of Planning and Finance in Uganda) or the implementation of a joint decision making structure (e.g. setting up a Budget Guidelines Committee in Tanzania, jointly chaired by the Ministries of Planning and Budget).
- Strong cabinet involvement in strategic decision making around the policy, planning and budgeting cycle, often through the establishment of cabinet committees.
- A degree of delegation of both planning and resource allocation powers to spending agencies, plus emphasis on accountability at that level.

² More detailed guidance can be obtained from <http://intranet.worldbank.org/WBSITE/INTRANET/OPERATIONS/INTRANETFINANCIALMGMT/0,,contentMDK:21425372~menuPK:3965511~pagePK:210082~piPK:210098~theSitePK:275851,00.html> and <http://blog-pfm.imf.org/> on establishing the basics of PFM.

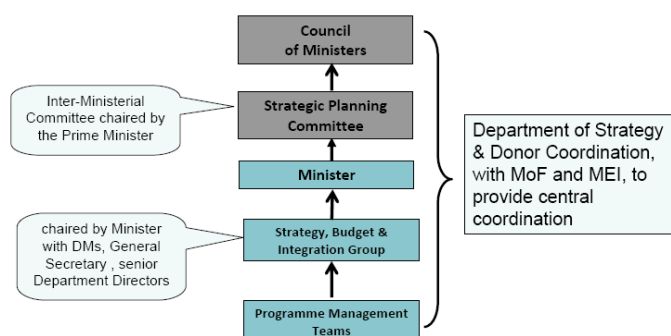
Box 3: Integrating Planning and Budgeting in Albania and South Korea

The Integrated Planning System In Albania

In Albania, numerous planning frameworks – including the National Strategy for Social and Economic Development, the EU Stabilization and Accession Agreement and the government’s Medium-term Budget Program – were implemented as separate exercises, each with its own set of priorities, procedures, and reporting requirements. Not surprisingly, this produced multiple priorities, overlapping processes, an excessive reporting burden in ministries, and public confusion.

An Integrated Planning System (IPS) – the result of a 10-month collaborative process between the Government and donors – was designed to serve as a unifying framework for existing systems. It involves:

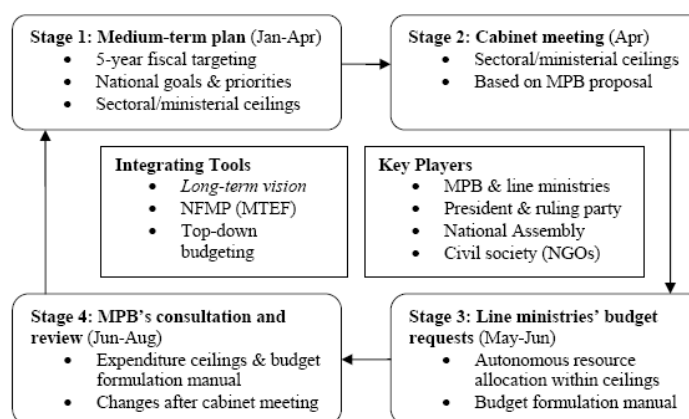
- The integration of all the principal policy and planning processes of Government.
- Creation of a Strategic Planning Committee, chaired by the Prime Minister, to oversee the IPS, and guide overall policy and fiscal directions.
- Transfer of the strategic planning function from the Ministry of Finance to a new Department of Strategy and Donor Coordination in the Office of the Council of Ministers.
- The creation of explicit links between strategy and budget, with the Medium Term Budget Program as the exclusive process through which all cross-cutting and sector strategies compete for funding and are translated into concrete plans, budgets, and expected results.



Integrating Planning and Budgeting in South Korea

After the Asian financial crisis in 1997, Korea formulated a medium-term fiscal plan focusing on recovering fiscal stability. Beginning in 2003, a new administration sought to strengthen links between planning and budgeting by introducing a Five-Year National Fiscal Management Plan and an MTEF, along with top-down budgeting.

Some of the main factors in the success of the South Korean reform program include: (i) strong political leadership; (ii) the introduction of a special cabinet meeting chaired by the President, where consensus is built on medium-term fiscal strategies and resource allocation among line ministries; (iii) a legislative framework that institutionalizes the integration of planning and budgeting mechanisms; and (iv) the concentration of the main functions in a single agency.



c) Diagnostic & Reform Questions

Diagnostic Questions: What are the gaps in the budgeting, policy, planning and reporting cycle? Are the institutions underlying planning and budgeting instruments linked?

- *Quality of public financial management.* Is the budget a reliable guide to actual revenues and expenditures? Are basic PFM systems (including a cash budget, internal control, accounting, and

auditing systems) in place? Are procedures for recurrent and development spending linked? Is there an MTEF in place?³

- *Links between PRS and other planning documents.* Is there one overarching policy or planning document? Do other national plans and policy documents exist in addition to the PRS? Do these policies and plans have distinct roles, or is there overlap?
- *Links between PRS and sector strategies.* Are sector strategies in place? Are they comprehensive and consistent with one another and what mechanisms are used to coordinate their preparation? Does the PRS reflect the content of sector level policies and strategies and vice versa? Does the PRS take past sectoral performance into account? Are both sector strategies and the PRS prioritised and costed?
- *Links between planning and budgeting.* Do the institutional links between Strategic Planning, the MTEF and annual budget need to be strengthened and better coordinated? Do MTEF documents and allocations reflect PRS and sector policies and priorities? Do budget allocations reflect the first year of the MTEF?
- *Ownership of the institutions of budgeting and planning.* Which stakeholders are involved in budgeting, planning and reporting? Is there unified ownership amongst different stakeholders (e.g. cabinet, central ministries, sector ministries, civil society, parliament)?

Reform Qs: Have adequate efforts been made to improve public financial management before addressing the linkages between the budgeting and planning cycles? Which of the gaps most significantly undermines the likelihood of PRS implementation and should be addressed first? How can institutions and processes underlying the PRS, planning and budgeting cycles be integrated or better linked?

³ N.B.: a recent PEFA PFM Performance assessment would facilitate answering these questions

2. Introducing a Strategic Phase and Medium-Term Perspective to the Budget Process

Introducing a strategic phase and medium-term perspective into the budget process can help to foster a strong link between planning and budgeting. It can facilitate the prioritization of development objectives and help to reconcile costs with available resources. It also enables better scrutiny of budget proposals by the ministry of finance, cabinet and parliament.

a) Typical Problems

The budget processes which currently prevail in many low income countries are not conducive to reconciling expenditure allocations with policy and PRS priorities. Typically, spending agencies submit separate proposals for recurrent and development spending to the ministries of finance and planning, respectively. These often take the form of unrealistic budget bids. The ministries then shrink agencies budgets to fit within the resource envelope and a consolidated budget proposal, which is compiled by the Ministry of finance, and forwarded to cabinet and parliament for approval. The oversight roles of cabinet and parliament tend to be highly circumscribed. For example, in Mozambique the draft budget is only presented to cabinet roughly two weeks before its submission to parliament, providing little scope for effective supervision. And parliamentarians rarely have political incentives to scrutinise budget proposals thoroughly.

As a result of this process, each spending agency tends to receive a standard increment on their recurrent budget and a separate development budget allocation which is made up of a list of projects. The development budget is often dominated by donor funded projects, with scarce domestic revenues dedicated to counterpart funding requirements. In sum, with the ability to make only incremental changes to the recurrent budget and limited control over investment choices, it is very difficult for governments to link resource allocations to specific policies, let alone a comprehensive PRS.

One response to these problems has been to identify priority poverty reducing expenditures, which usually relate to parts of the recurrent budget. This has been effective in expanding recurrent budgets in key areas of health and education (for example, in Uganda and Tanzania). But it cannot ensure that the overall budget is responsive to the PRS and new policy priorities.

Many countries have also introduced MTEFs with a view to linking policy comprehensively to the budget. But incentives to use the MTEF as a as a rolling budget framework are often weak. Particular for the outer years of the normal three-year timeframe, MTEFs are only tenuously linked to the budget. In some countries, this is even the case for the budget year itself. And costed sector strategies that are needed for a meaningful debate around inter-sectoral priorities and trade-offs are often absent, or inconsistent with the PRSP.

In this section we look at how the addition of a strategic phase to the budget process, combined with a medium-term perspective, can enable closer links between planning and budgeting.

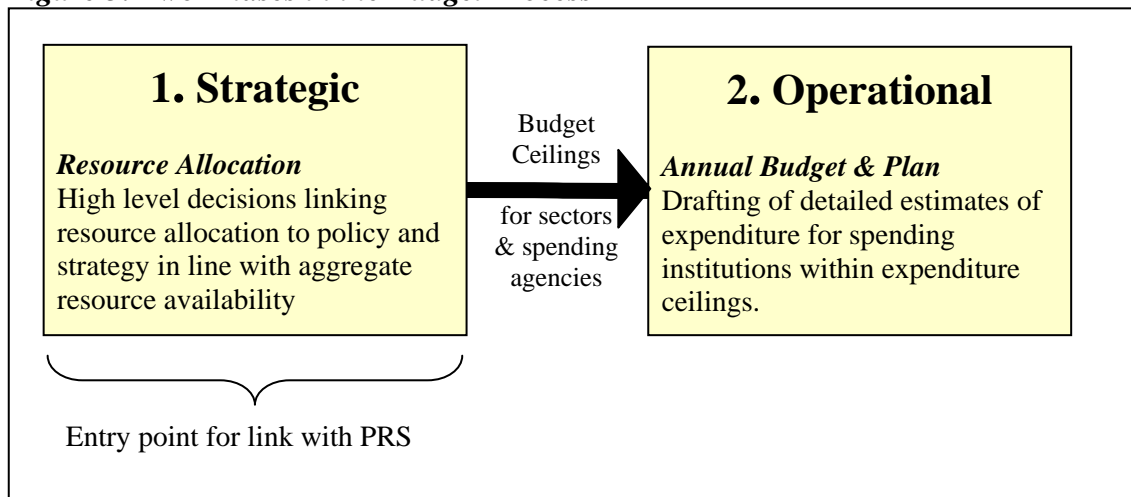
b) Towards Stronger Links

Introducing a strategic phase and medium-term perspective

The experiences of successful reformers (such as Albania, Tanzania and Uganda) demonstrate that the introduction of a strategic phase up front in the budget process can help to strengthen the links between policy, planning and budgeting.

As shown in Figure 3, the strategic phase should occur early on in the budget cycle, prior to the preparation of detailed budgets by spending agencies. During the strategic phase, the cabinet (or its equivalent) review overall allocations to spending agencies and sectors and agree upon budget ceilings for the fiscal year. As a result, there will be less motivation for spending agencies to engage in bidding games during the operational phase of the budget and a greater incentive to allocate resources effectively towards the achievement of policy objectives. For example, in South Korea it has been observed that line ministries have changed from “irresponsible budget requesters into self-disciplined budget compilation partners” since the introduction of a strategic phase in the budget process⁴.

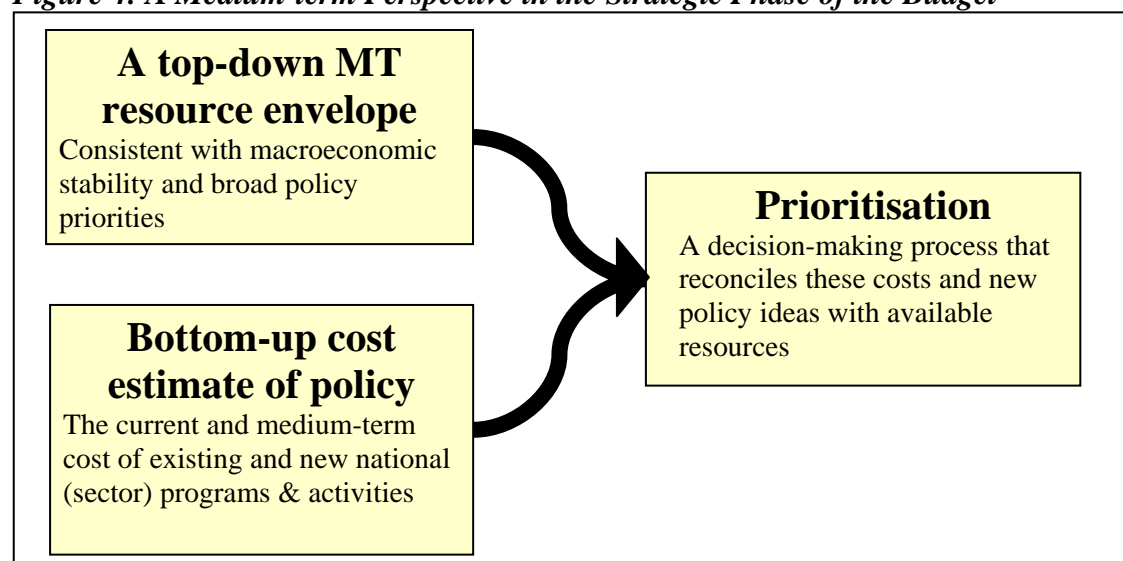
Figure 3: Two Phases in the Budget Process



While MTEFs tend to have little traction in countries without a strategic phase in the budget, they become integral once such a phase is in place. The use of medium-term perspective can help to translate longer-term policy objectives into shorter-term allocation decisions. As indicated in Figure 4, the MTEF will usually involve three steps: a top-down process of estimating available resources over the medium-term; a bottom-up process of estimating the cost of achieving policy objectives; and a final reconciliation of costs with available resources.

⁴ Minding the Gaps (2007), page. 154/55.

Figure 4: A Medium-term Perspective in the Strategic Phase of the Budget



Step 1: Estimating top-down budget ceilings

The ministry of finance will be responsible for estimating of an overall public expenditure envelope for the medium-term that is consistent with fiscal policies and macroeconomic projections. This then needs to be broken down further into an initial set of multi-year budget ceilings for sector ministries and spending agencies, based on a forecast of spending under current policies and levels of services. As an MTEF involves rolling baselines, projections in the previous year’s MTEF can form the basis of these initial budget ceilings.

Step 2: Sector strategies and bottom-up costing

Although PRSs, almost by definition, require central agreement of policy and objectives and priorities, sector level processes are crucial for fostering ownership and accountability. Key elements include the development of sector strategies, which link recurrent and development spending to outputs and outcomes, and the costing of these strategies. Rather than being “wish lists,” which do not take the availability of resources into account, bottom-up costing exercises should consider the constraints imposed by limited human and financial resources.

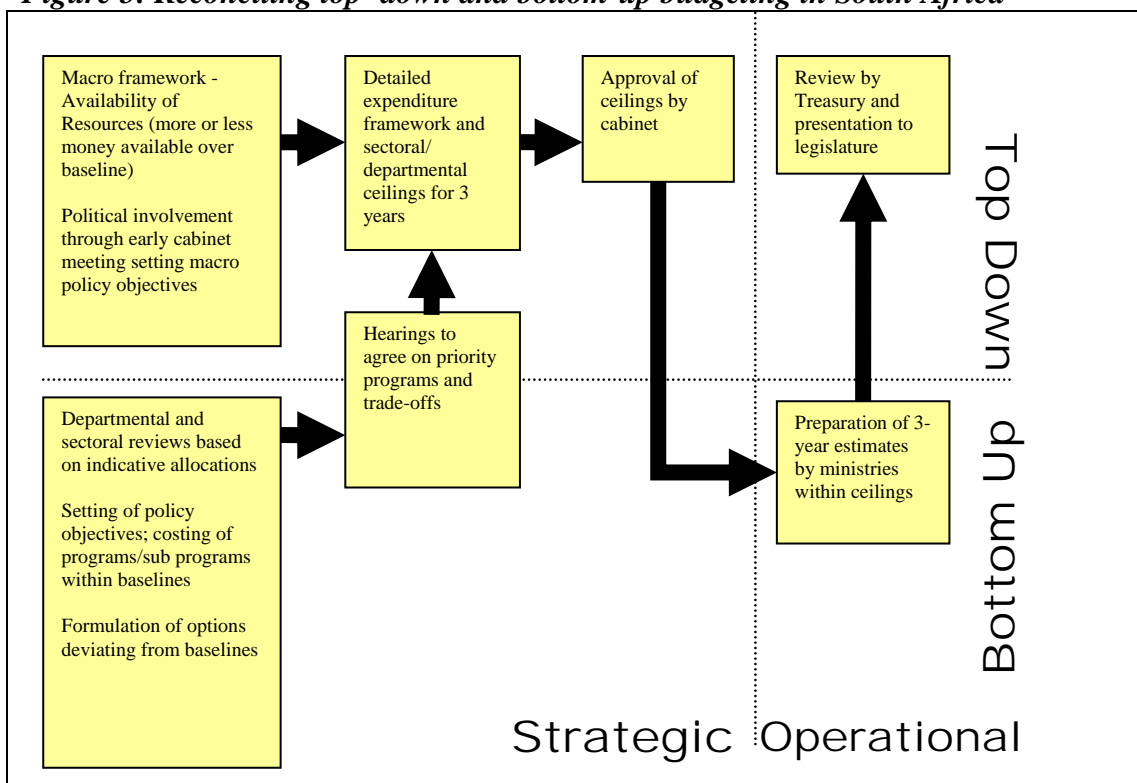
Whilst thorough costing is an important input into the budget process and medium-term planning, it can be burdensome in terms of analytical capacity and resources. Some countries have introduced halfway steps, which have fostered strategic thinking at the sectoral level, prior to the introduction of costing. For example, in Uganda and Tanzania, all spending agencies were required to prepare medium-term spending plans at a time when very few sectors had established sector strategies, let alone costed one. Such halfway steps can help to generate internal demand for bottom-up costing.

Once an MTEF is in place – as in the case of Albania, Uganda, and South Africa – spending agencies will prepare medium-term budget proposals, which set out what can be achieved given medium-term resource allocations. Bottom-up costing of sector policies strategies helps answer two questions in the preparation of these proposals: First, what are spending institutions currently delivering what will it cost to maintain this level of delivery over the medium-term? And second, what is the cost of achieving new policy objectives or expanding existing services?

Step 3: Reconciling costs with available resources

The strategic phase in the budget process needs to reconcile the cost of delivering services with budget ceilings. Depicted in Figure 5, the South African budget provides a good example of the policy processes which can be employed to reconcile sectoral objectives with limited resources. Budget hearings, conducted between the finance ministry and spending agencies, help to scrutinize spending plans and promote agreement on priorities. But ultimately the decision on sectoral budget ceilings is taken by the cabinet, and approved by parliament. It is important that parliament has adequate time to scrutinise the budget proposal before the start of the new financial year and is empowered to carry out its role. This can be done through improving the presentation of the budget and establishing structures such as the Parliamentary Budget Office in Uganda, which engage parliamentarians in this task.

Figure 5: Reconciling top-down and bottom-up budgeting in South Africa



Budget strategy documents can also be a good way to ensure cabinet and parliamentary engagement. These documents tend to be based on proposals from sectors and/or spending agencies and set out past performance, future spending plans, and the links to governments policy priorities.⁵ In Uganda, the Budget Framework Paper includes explicit expenditure options. In addition to its presentation to the cabinet, it is also presented to parliament for comment. Its *Table of Contents* and an extract from a table of proposed additional budget allocations is shown in Box 4 below:

⁵ For example, the Budget Guidelines in Tanzania, The Medium-term Budget Policy Statement in South Africa and the Budget Framework Paper in Uganda.

Box 4: Extracts from the 2007/08 Budget Framework Paper in Uganda

Table of Contents

Introduction

Part I: Three-Year Macro-Economic Plan

Macroeconomic Framework
Economic Performance And Prospects For The Medium-term
Implications Of Medium-term Economic Objectives For The Budget
Competitiveness And Private Sector Development
Medium And Long Term Financing
Financial Sector Development
Employment
Resource Projections For FY 2007/08 - 2009/10

Part II: Programs For Social And Economic Development

A: Rural Development
B: Infrastructure Development
C: Trade, Industry And Tourism
D: Human Development
E: Security And Governance

Part III: Preliminary Indicative Revenue And Expenditure Framework

Revenue Outlook For The FY 2007/08
Expenditure Outlook And Options For The FY 2007/08

Extract from Table of Proposed Budget Allocations of Additional Resources FY 2007/08

Activity	Additional (UGX Bn)	Requirement	Proposed additional allocations	Funding Gap
Infrastructure				
Power Infrastructure(Energy Fund)		26	25.0	
Emergency Thermal Power		90		
Road Maintenance Backlog		87	40.0	47.0
Counter-part funds to Roads Infrastructure projects		62.53	20.0	42.5
Petroleum Exploration - Equipment and Monitoring		1	1.0	0.0
ICT - National Data Transmission Backbone		27	5.0	22.0

c) Diagnostic & Reform Questions

Diagnostic Qs: Is there a strategic phase in the budget process? How are medium-term budgets developed and how are resource allocations reconciled with costs? Is there sufficient ownership in ministries, cabinet and the parliament?

- *Strategic phase in the budget process.* Are links between policy, planning and budget allocations addressed, and, if so, at what stage in the budget process? Are spending agencies provided with budget ceilings to prepare the detailed budget estimates, or do they bid for resources? If ceilings are provided, are they derived from a strategic phase, which allocates resources according to performance and policy priorities?
- *Medium-term perspective.* Is there a rolling macroeconomic framework which projects the resources available to the public sector over the medium-term? Is the macroeconomic framework translated into indicative budget ceilings for sectors and spending institutions? Are sector strategies in place? Are sector strategies costed and are these costs realistic given the availability of resources?
- *Reconciling resources with costs.* Is there a process of consultation between line ministries and central ministries of finance on sector institutions' medium-term spending plans? Does this involve rigorous scrutiny or proposals and spending options? Is there a medium-term budget strategy document prepared by central ministries to facilitate decisions by cabinet. Does it present explicit expenditure choices, and are they linked to the achievement of policy objectives?
- *Ownership.* At what stage in the budget cycle do ministries of finance and planning, the cabinet, and parliament scrutinize budget proposals? How does the ministry of finance deal with problems in budget submissions? Are there committee structures within cabinet and parliament to facilitate

engagement in the budget process? How much time do cabinet and parliament have to scrutinize proposals?

***Reform Qs:* Does the budget process need to be adjusted to allow space for strategic resource allocation and improved medium-term perspectives? If so, how can this be done? Is there scope for strengthening sector strategies and costing at the sectoral level? What steps can be taken to ensure effective reconciliation of resources and the costs? What steps can be taken to strengthen the role of the executive and parliament at key stages in the budget process?**

3. Results Orientation in the Budget Process

The presentation of performance information alongside budget allocations can strengthen the link between resources and results, facilitate prioritisation, and highlight trade offs between expenditure choices. It also has the potential to strengthen accountability, especially if institutions' budgets are linked to the outputs they are delivering.

a) Typical Problems

While budgets and PRSs tend to concentrate on different stages of the results chain, neither focuses on public sector outputs. This creates a gap in the government's accountability to its citizens for the provision of public services.

Traditionally, budgets have been input-oriented, presenting what individual institutions intend to spend their money on. As a result, it is difficult to ascertain how much is being spent on policy priorities such as health or education, since expenditures will be spread across different institutions. In addition, an explicit link between the proposed spending and resulting government activities is often lacking.

While PRSs are results-oriented, they tend to be concerned first and foremost with development objectives (such as growth and poverty reduction). PRSs set out broad objectives which often cut across the private and public sectors. Clearly stating the development outcomes that the government wants to achieve, the PRS is usually less explicit about which institution is responsible for delivering which results. Sector strategies often present a similar challenge, even if outputs are better specified.

Largely donor-driven, initiatives to improve the performance-orientation of the PRS and budget have met with limited success. Often they result in a proliferation of indicators: in a hypothetical country with 30 spending institutions and an average of 10 departments/projects per institution, the inclusion of 10 performance targets for each department/project would result in 3000 targets for the entire government. Rather than clarifying the link between the budget and performance, this can create a sea of technocratic information which is difficult for the executive or parliament to verify.

b) Towards Stronger Links

Here we outline three stages to introducing a results orientation into budgeting, which will allow for progressive deepening of the link between budgeting and planning. The phased approaches suggested here can build on traditional administrative and line item budgets and use existing performance information. They need not entail dramatic changes to budget classification.

Step 1: Present the budget by sector and include policy objectives up front

The grouping of the administrative budgets of institutions by sectors allows decision makers to see at a glance how much is being spent on priority areas (for example health, education, roads), something that is often not easy to do in a conventional administrative budget. Once budgets are arranged in this manner, it becomes a relatively

easy step to present policy objectives from the PRS and other strategy documents can alongside the relevant sectoral allocations.

Table 1 shows an excerpt of the sectoral grouping of administrative budgets in Uganda. Whilst most institutions will fit in one sector, some institutions may cut across sectors, and it may be necessary to split institutional budget allocations. For example, in Uganda, the budget for the Office of the Prime Minister is split across two sectors – *Economic Functions* and *Social Services and Public Administration*. Where the government does not have clear sector definitions, the higher level divisions of the standard international functional classification can be used as a starting point for defining sector groupings.⁶

Table 1: Sector Presentation of Administrative Budgets in Uganda

SECTOR/VOTE		FY 2007/08 Budget Projections					
		Non-Wage Wage Recurrent	Domestic Dev	Donor Project	Total excl. Donor Project	Total incl. Donor Project	
AGRICULTURE							
010	Agriculture, Animal Industry and Fisheries	2.41	5.53	7.08	47.05	62.07	
142	National Agricultural Research Organisation (NARO)	-	2.85	17.20	5.18	25.23	
501-850	District Agricultural Extension	3.88	3.22	-	7.10	7.10	
501-850	National Agricultural Advisory Services (Districts)	-	-	42.13	1.42	43.55	
152	NAADS Secretariat	-	4.46	5.35	9.81	9.81	
155	Uganda Cotton Development Organisations	-	3.20	-	3.20	3.20	
160	Uganda Coffee Development Authority	-	1.58	-	1.58	1.58	
SUB-TOTAL AGRICULTURE		6.29	20.84	71.75	53.65	152.53	


Step 2: Spending institutions identify their outputs as part of the budget process

Since sectoral outputs are the direct results of government activity, they are central to promoting accountability. As part of the budget process, spending institutions can be asked to identify the key outputs which they plan to achieve with their budget allocations in the coming year (or 3 years if a medium-term perspective is being used).

Table 2 below shows how performance information can be integrated into budget documentation at both the strategic and operational phases of the budget process. During the strategic phase the inclusion of major outputs and their links to development outcomes will be a priority. In the operational phase, more detailed information on performance indicators may be beneficial. As a general rule of thumb, however, output indicators should be limited to 10 per spending institution so as to distil those targets which are of highest priority and for which monitoring is feasible.

⁶ See <http://unstats.un.org/unsd/cr/registry/regcst.asp?Cl=4&Lg=1&Top=1> for a full list of the international functional classification.

Table 2: Integrating Performance Information in Budget Documentation

	Relevant information	Main target decision making processes and stakeholders	
National MTEF/ budget strategy Documents	Highlights of key policy achievements and outputs by sector in the context of past sector expenditures and future allocations	<ul style="list-style-type: none"> - Cross-sectoral monitoring and resource allocation mechanisms - President and Cabinet - Ministry of finance and planning - Parliamentary committees - Donors 	
Sector budget strategy documents	Setting out past performance in terms of outcomes, outputs, and policy actions at a sector level alongside future projections/targets in the context of past expenditures and future budget allocations	<ul style="list-style-type: none"> - Intra-sectoral monitoring and resource allocation mechanisms - Cabinet and parliamentary committees - Ministry of finance - Sector civil society organizations - Sector donors 	
Annual national budget documents	A summary of key results achieved by individual institutions alongside targets for the coming budget year including expenditure estimates and summaries of past and planned expenditures	<ul style="list-style-type: none"> - Cross-sectoral monitoring and resource allocation mechanisms - President and Cabinet - Ministry of finance and planning - Parliamentary committees - Donors - Civil society 	
Institutional operational budgets	Information on past activities, outputs and expenditures linked to implementation of operational plans and budgets (including delivery of services)	<ul style="list-style-type: none"> - Intra-institutional monitoring and resource allocation mechanisms - Managers within institutions - Cabinet and parliamentary committees - Donors providing support to the institution 	
			Operational

Source: *Minding the Gaps*

The identification of sectoral outputs should provide decision makers with two key insights. In the strategic phase, outputs should indicate what spending institutions plan to achieve with their money over the next year (or three years). During the operational phase, they should demonstrate the key services which the annual budget allocations will buy. By promoting a transparent link between public spending and services, the identification of outputs can facilitate the oversight and challenge functions of the ministry of finance, cabinet and parliament.

Step 3: Introduce a program classification and present performance information alongside it

The inclusion of simple performance information in the budget described in steps 1 and 2 above may have the effect of raising domestic demand for deeper linkages between institutions' budgets and results. The introduction of programs into the budget classification system for spending institutions can help strengthen this link, without over-complicating it.

A program classification labels the expenditures of an institution according to its core outputs, for example, "hospital services," "primary education," or "roads transport." As Box 5 demonstrates, the program classification of the budget in South Africa has facilitated the systematic inclusion of information on expenditure and inputs (including both human and capital resources), program goals and how they contribute to policy

objectives, and past and projected public sector outputs. The resulting structure can help to guide allocation decisions and foster domestic accountability. Over time, programs can become the main unit of allocation and appropriation, steering the design of domestic and donor funded projects and even the administrative structure of spending institutions.

Box 5: Programs, Inputs and Outputs in South African Budget Documentation

The South African Budget has a program structure. In the annual budget documentation, spending institution budgets are presented over the medium-term.

Overview of the Ministry of Health's Expenditures by Program and Economic Classification

Vote 15

Health

R thousand	2007/08 To be appropriated	2008/09	2009/10
MTEF allocations			
Administration	205 467	206 914	218 210
Strategic Health Programmes	3 216 723	3 461 165	3 896 242
Health Service Delivery	9 160 592	10 197 827	11 004 350
Human Resources	72 350	77 857	80 628
Total	12 655 132	13 943 763	15 199 430
Direct charges against the National Revenue Fund	–	–	–
Total expenditure estimates	12 655 132	13 943 763	15 199 430
Economic classification			
Current payments	860 193	907 778	947 422
Transfers and subsidies	11 760 745	13 010 554	14 225 288
Payments for capital assets	34 194	25 431	26 720
Total expenditure estimates	12 655 132	13 943 763	15 199 430
Executive authority	Minister of Health		
Accounting officer	Director-General of Health		

Each program includes the following: a description of the program's objectives; expenditure estimates by subprogram and economic item; a description of expenditure trends; key input information (including personnel numbers, training, capital projects, and public-private partnerships); and an overview of past and future service delivery outputs.

Outputs, Subprograms and Inputs for the Health Service Delivery Program

Subprogramme	Audited outcome			Adjusted appropriation	Medium-term expenditure estimate		
	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
R thousand							
Hospital Services	6 289 289	6 576 942	7 493 967	8 046 452	8 845 001	9 868 093	10 656 415
Health Economics	7 244	7 863	10 225	28 573	16 371	17 190	18 088
Health Information Research and Evaluation	184 028	189 836	210 833	239 844	250 507	259 513	272 551
PHC, District Health and Development	13 561	14 575	17 797	24 125	29 779	33 148	36 358
Office of Standards Compliance	16 828	9 303	11 579	19 911	18 934	19 883	20 938
Total	6 510 950	6 798 519	7 744 401	8 358 905	9 160 592	10 197 827	11 004 350
Change to 2006 Budget estimate				87 728	302 085	704 218	
Economic classification							
Current payments	66 734	54 683	54 935	95 208	105 231	117 513	125 020
Compensation of employees	51 151	29 448	31 173	47 304	49 562	52 045	54 907
Goods and services	15 583	25 235	23 564	47 904	55 669	65 468	70 113
<i>of which:</i>							
Communication	2 018	2 083	567	2 033	2 274	2 599	2 729
Consultants, contractors and special services	1 503	12 831	1 066	11 469	12 829	14 665	15 398
Operating leases	478	439	207	338	378	432	453
Travel and subsistence	4 102	9 360	9 970	14 469	16 072	18 373	19 292
Financial transactions in assets and liabilities	–	–	198	–	–	–	–
Transfers and subsidies	6 440 504	6 742 352	7 687 676	8 260 537	9 052 433	10 077 239	10 876 101
Provinces and municipalities	6 271 828	6 563 283	7 485 474	8 028 680	8 824 024	9 840 928	10 627 974
Departmental agencies and accounts	166 155	170 996	184 429	228 324	224 931	232 659	244 292
Non-profit institutions	2 521	8 073	17 680	3 313	3 478	3 652	3 835
Households	–	–	93	220	–	–	–
Payments for capital assets	3 712	1 484	1 790	3 160	2 928	3 075	3 229
Machinery and equipment	926	1 442	1 738	2 786	2 928	3 075	3 229
Software and other intangible assets	2 786	42	52	374	–	–	–
Total	6 510 950	6 798 519	7 744 401	8 358 905	9 160 592	10 197 827	11 004 350

Source: 2007/08 Budget, South Africa Treasury.

Subprogramme	Output	Measure/Indicator	Target 2007/08
Hospital Services	Survey report on the delegation of authority to hospital CEOs	Survey report published	April 2007
	Improved capacity of hospital managers	Percentage of hospitals with managers enrolled for a formal hospital management training programme	50% of hospitals
	Effective hospital revitalisation programme	Number of new business cases accepted for the revitalisation programme	20 business cases
	Improved emergency medical services (EMS)	Number of provinces with EMS plans guided by the national EMS strategic framework	All 9 provinces
Health Information, Research and Research	Health and EMS plan for 2010 FIFA World Cup	Intersectoral plan finalised and disseminated	March 2008
	Monitoring and evaluation framework for the national strategic plan for HIV and Aids for 2007-2011	Framework finalised and disseminated	March 2008

Among the numerous insights on program budgeting emerging from international experience, the following are particularly pertinent:

- Program budgeting is an iterative process, which may build on existing classification systems; the nature of program classification will vary from country to country.
- Program classifications should only relate to one institution and should not cut across institutions.
- The classification should be comprehensive, covering all recurrent and development funding in the budget, as well as donor funding.
- The number of programs should be limited; an upper limit of 200 programs is advisable.

c) Diagnostic and Reform Questions

Diagnostic Qs: To what extent is performance information integrated into budget documentation? How does this facilitate decision making and accountability for the implementation of policies?

- *Integration of performance information in the budget.* Is the budget presented by sector? If so, are PRS and sector objectives set out alongside sector allocations? Are the outputs of spending institutions specified in budget documentation? Is the number of outputs limited or is there a proliferation of performance information? Is there a program classification in the budget? If so, is the number of programs limited?
- *Decision making and accountability* Does performance information guide the allocation of funds between sectors and sector institutions? Who (among the ministry of finance, cabinet, parliament and donors) are the main consumers of performance information in budget documentation? Is the information tailored to fit their decision making and accountability needs?

Reform Qs: What steps can be taken to introduce and/or strengthen the use of performance information in budget documentation. How can performance information be tailored to promote decision making and strengthen accountability?

4. Alignment of PRS and Budget Reporting with Decision Making Processes

Budget and PRS reporting mechanisms tend to be beset by a high degree of institutional separation and weak incentives to integrate the two systems. To foster integration, it is important to align reporting mechanisms as closely as possible with domestic policymaking processes, through a focus on public sector outputs. Incentives to integrate various systems can be strengthened by support for improvements in budget reporting and rationalization of unnecessary donor requirements.

a) Typical Problems

Institutional separation between budget and PRS reporting mechanisms prevailed in most of the low-income countries studied under *Minding the Gaps*. While budget reporting is usually limited to financial information on expenditures versus allocations, PRS reports typically focus on development outcomes without drawing a strong link between these outcomes and government spending and actions. Sector reports, which are prepared in some countries in the context of sector wide approaches (SWAs), usually focus on the implementation of strategies without explicit links to expenditures. Whilst central monitoring of poverty and sector outcomes is undoubtedly important, a key lesson from *Minding the Gaps* is that reporting on direct outputs from the public sector are crucial for fostering domestic accountability. In many countries there is a gap in the provision of information on outputs, or in the links between expenditures, outputs and outcomes.

Since different stakeholders are concerned with the production of budget and PRS (or sector) reports, incentives to integrate the two mechanisms are usually weak. While there is internal demand for the production of budget reports (all countries have statutory requirements to present financial statements to parliament), demand for the production of PRS Annual Progress Reports (APRs) tends to be driven by donors (even when preparation of the APR is highly participatory, as in Albania). In many countries the production of the APR has entailed the creation of entirely new mechanisms, often because no appropriate instruments were in place at the national level. The information reported in APRs does not tend to feed into domestic decision making processes and their production is rarely synchronized with the annual budget cycle. Incentives to share information in a prompt manner (either between ministries of finance and planning or with the cabinet and parliament) tend to be low.

Although in most countries the basic building blocks of reporting systems – such as the timely collection of administrative data – are improving, the extent to which these data will contribute to greater accountability depends on where, how, and by whom the information is demanded and used. And in this context, a key question is whether or not PRS reporting is linked to domestic policymaking processes. Thus, the challenge of integrating PRS and budget reporting is not merely a technical one but depends also on the bureaucratic and political incentives to use such information.

b) Towards Stronger Links

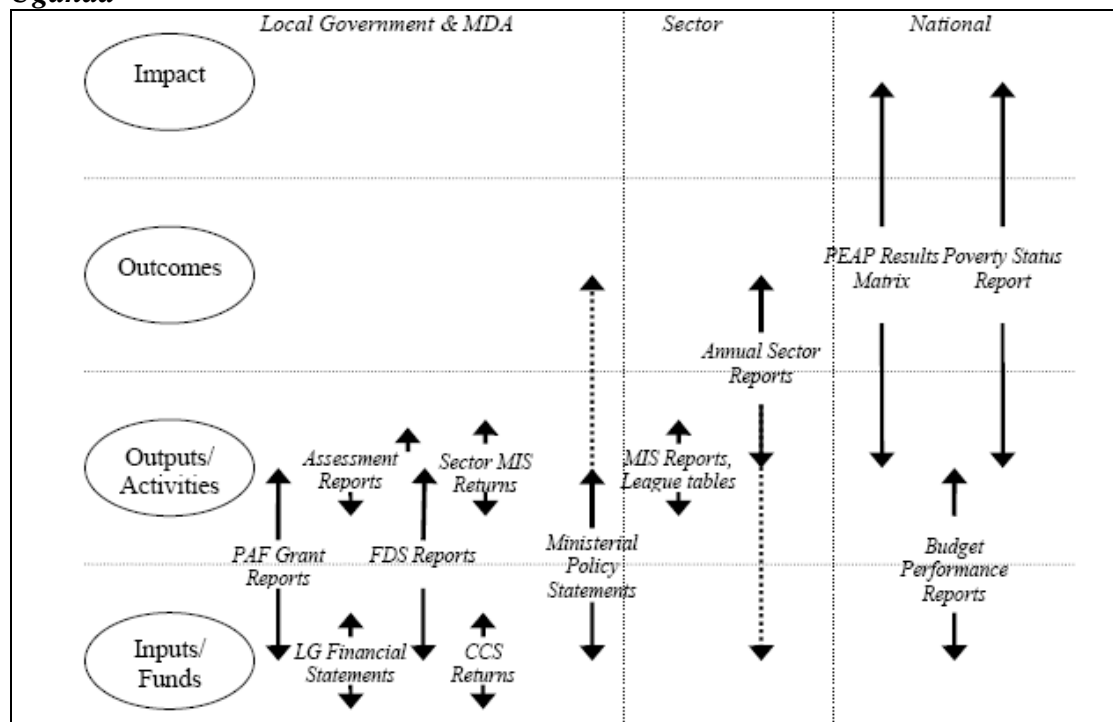
The task of building stronger links between budget and PRS reporting mechanisms begins with surveying the coverage of current systems and identifying the stakeholders vested in each mechanism. Both domestic stakeholders and international donors have an important role to play in fostering incentives for integrated reporting systems. Getting the basics of budget reporting right is probably the most fundamental step for building more integrated systems. Once these basics are in place, there will be greater scope for widening the remit of budget reporting to include performance data. Greater compatibility between the budget and PRS reporting processes can strengthen incentives to integrate the two systems entirely.

Identifying gaps in reporting processes

The first step toward building stronger links between reporting processes can be made by identifying the current gaps through a relatively simple mapping exercise, which charts the coverage of various reporting systems. Typically, neither budget reports nor PRS reports tend to include comprehensive information linking government outputs and activities to poverty outcomes. Figure 6 shows a sample mapping exercise for Uganda. Most strikingly, no single reporting mechanism covers the entire range of inputs, outputs, outcomes, and impact.

However, quite atypically, Uganda has relatively good coverage of government activities and outputs in its planning reports, including sector reports. These reports also draw a link between outputs (such as investments in education) and development outcomes (such as school completion rates). *Minding the Gaps* finds that sector level monitoring processes are essential for generating demand for and supply of routine data on activities and outputs. By holding sectors responsible for deliverables, this form of reporting will also help to promote clear lines of domestic accountability.

Figure 6: Identifying the gaps in planning and budgeting and reporting processes - Uganda



Country experience has demonstrated that in practice much of the momentum for generating a culture of domestic accountability has arisen at the cabinet level. In Rwanda, for example, all ministries are required to produce annual action plans and, one year on, to report on the implementation of these plans. Reporting has taken place during a high level cabinet retreat, chaired by the President. Mozambique, Madagascar and Uganda have also instigated high level processes to promote domestic accountability – such as cabinet level committees to evaluate the performance of the budget – which are detailed in *Minding the Gaps*. These structures have ensured direct engagement of politicians (mostly ministers but in some cases also parliamentarians) at key decision points, thus ensuring political peer pressure for “sticking to the path.”

Donors also have a role to play in ensuring that their reporting requirements promote domestic accountability and reinforce rather than undermine pre-existing mechanisms. In Mozambique, an early agreement between donors and government ensured that rather than rely on a separate APR, the existing reporting mechanism to parliament would be upgraded and improved to serve both domestic and external accountability purposes.

Budget support and SWAPs can be used as a tool for encouraging improvements in the quality of budget reporting, starting with the basics of budgeting and evolving to emphasise its links to performance and development outcomes. In Mozambique, for example, the budget support performance assessment framework, PAF, has become an effective mechanism to focus both the donors and the government’s attention on limited set of indicators and efforts are currently underway in Madagascar to align donor monitoring requirements with performance matrices developed under the Madagascar Action Plan.

Strengthening the links between budget and PRS-reporting

An essential building block for strengthening the links between reporting processes is to ensure that the basic mechanisms of budget reporting are sound. As highlighted in section 1 of this note, some of the fundamental elements of sound budgeting include regular reporting on disbursements and expenditures against allocations during the financial year – both by spending institution and in the aggregate.

Beyond these essential elements, the introduction of a performance orientation in the budget (as described in section 4) can create a basis for linking reporting on expenditures to outputs and policy outcomes. A performance-orientation will widen the scope for reporting on expenditures by sectors, spending institution and programs, and linking these expenditures directly to public sector outputs.

Concurrent to improvements in the quality of budget reporting, three simple changes can be made to the PRS reporting process to enable complementarity with the budget cycle. First, and most obviously, the PRS report should be prepared in advance of the start of the annual budget cycle so that relevant findings may feed into the formulation of the budget. Second, where possible, PRS performance objectives could be linked to sectors and sector institutions so as to make them compatible with the categories employed in the budget. Third, since the budget cycle tends to focus on the lower levels of the results chain — that is, outputs and activities – PRS reporting should contain specific reference to the same outputs where possible, and draw a firm link between these and development outcomes.

With greater compatibility between the budget and PRS reporting processes established, integration of the two systems may be a feasible prospect. If complete integration is judged too an onerous task, there may still be scope to scale back on the frequency of PRS reporting on development outcomes, especially since such data tends to be generated on a 2-to-3 year, rather than annual, basis. If the two reporting systems are sufficiently aligned, then a single annual report – structured around the budget, and containing information on the allocation and expenditure of resources, the resulting activities and outputs, and development outcomes – may be sufficient to feed into domestic policy making processes *and* meet donor requirements. For their part, donors can encourage the integration of PRS annual performance reporting and budget reporting where it is feasible, and use this as the basis of routine monitoring of PRS implementation.

c) Diagnostic and Reform Questions

Diagnostic Qs: What reporting systems exist and how compatible are they with domestic policymaking processes? To what extent do donors and domestic stakeholders help or hinder the integration of budget and PRS reporting mechanisms? Have all feasible steps been taken to enable the integration of systems?

Stocktaking of current systems. What data is reported in routine administrative reports/ sectoral reports/ national surveys? Does it consist of data on inputs/ expenditures/ actions/ outputs/ outcomes? Is this information reported in budget reports/ APRs/ sector reports/ other? Is adequate attention given to the monitoring of outputs, given their importance in promoting domestic accountability?

Links between reporting systems and domestic policymaking processes. What reporting systems are used to inform decision making at the sectoral/ cabinet/ parliamentary levels? Is performance information available, which is relevant to these decision making processes, but not used?

Domestic and international stakeholders' roles in promoting accountability. Which stakeholders are most active in demanding accountability? Are cabinet ministers engaged in the reporting process? What is parliament's role in monitoring the budget and PRS reporting mechanisms? Are donors' reporting requirements based on domestic systems? Is there scope for donors to reduce parallel demands? To what degree is aid aligned with the structures of the implementing institutions?

Extent of integration and feasibility of reforms. Are the basics of budget reporting sound? Has a performance orientation been introduced into the budget and is this reflected in current reports? At what point in the budget cycle is the PRS report published? Are the development outcomes in the APR linked to outputs in the budget report? Is there any value in reporting on development outcomes annually, or should the frequency be reduced? Is there sufficient compatibility between PRS and budget reporting systems to merit integration into a single report?

Reform Qs: What action is needed to strengthen the availability of performance information, especially data on public sector outputs? How can reporting mechanisms be better targeted towards decision making processes? Can domestic stakeholders be galvanized to demand greater public sector accountability? How might donor requirements be better aligned with domestic systems? What reforms are feasible to ensure the better integration of PRS and budget reporting?

Key Resources

Overview of PFM:

<http://intranet.worldbank.org/WBSITE/INTRANET/OPERATIONS/INTRANETFINANCIALMGMT/0,,contentMDK:21425372~menuPK:3965511~pagePK:210082~piPK:210098~theSitePK:275851,00.html> and <http://blog-pfm.imf.org/>

Introducing a Strategic Phase to the Budget: ODI MTEF Guidance Note; South African Treasury Website: <http://www.treasury.gov.za/>

Introducing Performance Orientation in the Budget: Draft IMF guide to performance budgeting; South African Treasury Website: <http://www.treasury.gov.za/>

PRS Reporting and Monitoring Processes: World Bank (2006) *Beyond the Numbers: Understanding the Institutions for Monitoring Poverty Reduction Strategies* <http://go.worldbank.org/PPTOO2V1P0>

Linking PRSPs & Budgets: World Bank (2007) *Minding the Gaps: Integrating Poverty Reduction Strategies and Budgets for Domestic Accountability*; <http://go.worldbank.org/BIFFUADZD0>