

Chapter 7. MANAGING AND MONITORING BUDGET IMPLEMENTATION¹

A. BUDGETARY ACCOUNTING

1. Importance of budgetary accounting

Budgetary or appropriation accounting consists of tracking and registering operations concerning appropriations and their uses. It should cover appropriations, apportionment, any increase or decrease in appropriations, commitments/obligations, expenditures at the verification/delivery stage, and payments. As indicated in chapter 10, budgetary accounting is only one element of government accounting system, but it is the most crucial for both formulating policy and supervising budget implementation. In particular, weaknesses in budgetary accounting and recording make quality analysis of the performance, outputs or outcomes impossible (see chapter 15 for an elaboration).

Most developed countries keep registers for their transactions at each stage of the expenditure cycle, or at least at the obligation stage and the payment stage. This, whatever their accounting system or budget execution procedures. Many developing countries keep similar registers, either at the spending agency level or through centralized control procedures². However, in both cases, budgetary accounting presents inadequacies. On the one hand, when registers are kept by agencies, information is not systematically available at the level of the Ministry of Finance, which would need it to supervise budget implementation. In practice, in some of these countries budgetary accounting covers only payments. On the other hand, where control procedures are centralized, sometimes information on budget execution concerns administrative steps that do not correspond to the stages in the expenditure cycle described in chapter 6.³ Such "administrative" information is useless for analyzing budget implementation. In FSU countries, spending agencies keep books on an "accrual" basis (although not in conformity with generally accepted accounting principles). Such arrangements, despite their advantages, created difficulties in the timely monitoring of payments according to the budget classification. Therefore, in these countries efforts are currently focused on the implementation of a system of monitoring payments.

The benefits of monitoring either obligations or expenditures at the verification stage or the payments stage are sometimes debated. Actually, information is needed at each stage of the expenditure cycle and can be easily compiled, thanks to developments in electronic technology.

Adequate recording of appropriations, revisions in appropriations, transfers between appropriations, apportionment, etc. is a prerequisite for good management. In several developing countries, it is difficult to know exactly which budget is being implemented, because decisions concerning allocations and reallocations of appropriations are contained in various circulars and are not gathered into a single document. The budget implementation plan should be updated regularly to take into account decisions concerning appropriations.

Accounting commitments/obligations (obligational accounting⁴) is essential in keeping budget implementation under control. They provide the basis for budget revisions. Decisions to increase or decrease appropriations and the preparation of cash plans must take into account commitments already made. For internal management, spending agencies need to follow up accurately the orders and the contracts they have awarded.

Accounting for expenditures at the verification stage (sometimes called expenditure accounting) is important to program and agency management. It gives elements for assessing costs, although these elements need to be completed with information on depreciation, inventories, etc. Expenditures at the verification stage show how far program and project implementation has progressed. In chapter 11 the preparation of reports on development expenditures at the verification stage is recommended. Recording expenditures is also required for managing payables and contracts. It is a requirement of any accounting system that recognizes liabilities.

Some countries that have non-pure cash accounting system do not report payments along the budget classifications (see chapter 7). Actually, expenditures should be recorded according to the budget classification at each stage of the expenditure cycle, to identify sector or program imbalances at that stage.

A comprehensive and timely monitoring of budget transactions could be ensured with adequate information systems recording transactions at each stage of the expenditure cycle, and appropriate electronic connections between the “Ministry of Finance” and line ministries. Basic financial controls can be automated and made when registering the transactions. To some extent, differences between budget executions systems based on external ex-ante control and system based on internal controls are dimming with modern technologies. Nevertheless, implementing an information system is not a panacea. It is costly, but overall it requires appropriate budget accounting procedures that do not exist in many developing countries. Computers do not make up for poor governance and systemic lack of compliance. In such situations, they can only increase the number of non-regular transactions and off-budget procedures aiming at overcoming computerized controls.⁵ Procedures for overcoming computerized controls are discussed in chapter 7.

Box 25
The Budget Accounting System in the People's Republic of China

"Budgeting dictates accounting" is perhaps the simplest way to describe government accounting practice in China today. The budget laws enacted are elaborated in rules and regulations issued by the Ministry of Finance. The Bureau of Budget Management of the Ministry of Finance develops accounting rules and procedures that conform to the budget rules and procedures. The advantages of this system are: (i) it ensures consistency between budgeting and accounting; and (ii) it enjoys the enforcement power of the state.

The overall budgetary accounting systems are operated by the Ministry of Finance and the finance bureaus at each subordinate level of government. They track the execution of overall budgets—that is, receipts and payments. Reports are prepared on the tenth day of each month; in addition, monthly, quarterly, and annual statements are submitted. These statements basically report the amounts of the various sources and uses of funds. The primary objective of the accounting system is to prevent spending in excess of appropriations, and to ensure the collection of revenues.

Chinese budgetary accounting is characterized by its faithfulness to the prevailing ideology and public policy, a high degree of uniformity, and broad coverage (Shi and Jiang 1993, 10-15). Moreover, budgeting practices are highly uniform as a consequence of the central government's authority to prescribe the rules and regulations, and the existence of an elaborate administrative apparatus to enforce them. The regulations determine such details as the charts of accounts for all the administrative units and institutions at all levels of government throughout China. Until recently, the Chinese accounting system encompassed not only government but state enterprise accounting as well. As a consequence of economic reform, state enterprise accounting has been separated from budget accounting, even though standards are still set by the government through a unit of the Ministry of Finance. There is an ongoing debate as to whether institutional accounting should be dissociated from budgetary accounting (Lee, 1996).

Source: James L. Chan, ed., *Research in governmental and nonprofit accounting*, vol. 9, 1996.

2. Defining and Monitoring Commitments

Registering and monitoring commitment is required for different purposes, such as contract and program management, budget implementation supervision and cash management, and fiscal analysis (to assess the deficit on a "commitment basis").

For contract and program management, it is important to register all legal commitments (contract awarded, order passed, etc.). Program managers should register all legal commitments from an order for stationery to a multi-year contract for an investment project of a significant size.

For cash planning and funds release, it is important to know the obligations to pay that will occur over the planned period. It can be expected that an order for stationery will be completed over the planned period, but contracts for investment projects (and legal commitments) may cover several fiscal years. Therefore, for cash

planning the important is the tranche of the commitment that will generate a liability over the planned period, which is generally the legal commitment for supplies but not for multi-year investment projects.

For budget preparation, it is important to know the forward costs of multi-year investment projects and the expenditures that are “compulsory” or that will occur without adjustment measures (see discussion in chapter 4). The government has legal or moral obligations to pay personnel and entitlements. It is necessary to compile all policy commitments whatever their form, legal contract, administrative decisions, promises, etc.

For fiscal analysis, arrears must imperatively assessed. They are the difference between expenditures at the verification stage (“accrued expenditures”) and payments (issues related to the “float” are discussed in section D below). The difference between commitments and payments give an approximate estimate of arrears. However, this estimate is satisfactory only if “expenditures on a commitment basis” do not include multi-year commitment and administrative reservation of appropriations.

For the day-to-day administration of the budget, it is necessary to define precisely what is a commitment, in the “budgetary sense”. For budget management, the “commitment” could be defined as: (i) the legal commitment, when it makes sense to define the commitment on this basis (for example, contracts and orders for supplies, investment, maintenance works, etc); and (ii) expenditures at the verification stage, for other items (personnel, debt servicing, utilities bills, transfers). For orders concerning petty expenditures, the commitment and the verification stage may be confused in the budget implementation reports, however programs managers should monitor all their legal commitment, whatever their amount. The financial regulations should give a clear definition of commitment

An administrative procedure for reserving appropriations can fit some organizational arrangements (the “commitment/reservation” is in some countries, a procedure for delegating authority) or some programs (e.g. “annual commitments” of multi-year program). However, in countries that confuse this procedure of reservation of appropriation with other commitments, it is necessary to define an additional stage in the

expenditure cycle for the commitment (as in the USA, where it is distinguished “commitment/reservation” from obligations).

Whatever the name of the transaction called “commitment” in the budgetary jargon, it is necessary to monitor for multi-year projects both forward commitments (legal commitments) and expenditures at the verification stage, and to estimate the annual tranche of the commitment.

As discussed in chapter 4, the deficit on a “commitment basis” is an indicator of fiscal position, which aims at comparing the actual level of expenditures, including arrears, with revenues. Expenditures to be considered when calculating this deficit should be either “annual” commitments or expenditure at the verification stage. This indicator would be meaningless if it includes multi-year commitments and commitments that are merely reservations of appropriation. Moreover, to identify orders not yet delivered and to estimate arrears more accurately, expenditures at the verification stage must also be reported, in addition to commitments.

3. Managing Payables and Arrears Issues

Sound management of payables, namely, arrears and outstanding invoices and bills, is required. Payables are often distributed among various offices, such as the program manager office, the departmental office, the financial adviser/controller’s office, and the Treasury office. The invoice cycle generally needs to be simplified, for good accounting and transparency.

Computerization could help in tracking the invoices, but only to a certain extent, since invoices can be accumulated upstream and downstream to the computerized cycle. For example, in a Treasury Information System, if checks are made by the Treasury, invoices could be accumulated at: (i) the level of the spending agency manager, who does not send in the invoices when he knows that the Treasury does not have cash; and (ii) the Treasury level.

Therefore, whatever the mode of management (manual or computerized), some principles must be adopted:

- Expenditures must be verified as soon as the goods or the services have been acquired;
- Expenditures that are verified must be entered immediately into the accounts;
- Payments must be recorded as soon as they are made.

As discussed in chapter 6, procedures for carrying over are needed to take into account expenditures incurred during a fiscal year that are not paid in the same fiscal year.

Each contract, or at least those contracts concerning civil works and projects of a significant size, needs to be monitored accurately. Payments that will be made over the fiscal year must be planned to prepare cash plan. In the day-to-day management of payables, it is necessary to take into account the date at which the payments are due. To avoid penalties for late payments, invoices should be paid on the due date, but to reduce borrowing needs they should not be paid in advance (cash management issues are discussed in chapter 8).

In some countries, expenditures monitored at a "payment voucher stage" , corresponds neither to the verification stage nor to the payment stage. The registration of expenditures at the verification stage must be made as soon as deliveries are verified.

4. Arrears Issues

A number of transition economies and developing countries face arrears problems. Arrears pose problems to suppliers and have disruptive effects on public expenditure management. When the government accumulates arrears to private suppliers, private suppliers, at first, face financial difficulties. Then, they develop an appropriate billing strategy, such as requesting to be paid before they delivering, overbilling invoices, and bribing line ministries and/or Treasury officials responsible for the management of the waiting list of arrears.

Arrears have many causes, such as insufficient commitment control or the perverse effects of a cash rationing system that do not take into account commitments already made. Improved commitment monitoring is generally required.

However, in many cases, the decision or the event that generates an obligation to pay, is upstream to the commitment in the budgetary sense. Arrears in utilities services consumption are frequent. Generally, state-owned utilities (and even private companies) do not stop providing services to government agencies even when they are not paid. Limiting arrears generation in this sector requires both realistic estimates of annual consumption and internal management measures (such as installing meters, regulating phone calls). The measures must be imperatively identified at the budget preparation stage.

Limiting arrears generation needs a combination of measures such as realistic budget estimates, internal management measures, control of personnel staff, control/monitoring of commitments and especially of forward commitments, and decisions related to entitlements.

The estimation of generation of arrears is an important issue in some countries. Arrears are sometimes distinguished from float, which corresponds to the usual processing period to outstanding invoices. A stricter definition is to say that any invoice due on one date and not paid on that date must be included in the stock of arrears. An appropriate budgetary accounting as suggested above is necessary for establishing a permanent system for monitoring arrears.

When a country faces arrears problems, it should prioritize of payments on the basis of the date on which invoices are due and on their order of precedence. In some developing countries, programs to reduce the stock of arrears led to questionable practices, such as the generation of new invoices which were given the privileged status of arrears, the payment of expenditures despite their noncompliance with to procurement regulations, choices based on patronage. Strict control of the judicial regularity of arrears payments is required. The audit offices should scrutinize such operations.

B. IMPLEMENTATION OF POLICIES

1. Reviews

Budget implementation should be reviewed periodically to ensure that programs are implemented effectively and to identify any financial or policy slip-ups.

The review of budget execution should cover financial, physical and other performance indicators (see chapter 15). Cost increases due to inflation, unexpected difficulties, insufficient initial study of projects, and budget overruns must be identified so that adequate countermeasures can be prepared. A comprehensive midterm review of the implementation of the budget is needed, while the financial implementation of the budget should be reviewed monthly.

Development budgets are often beset by implementation problems because of insufficient implementation capacities and other factors such as delays in mobilizing external financing, overoptimistic implementation schedules, climatic hazards, or difficulties in importing supplies. Mechanisms for reviewing the most significant or problematic projects are needed. These could consist of a regular monthly or quarterly review of projects within line ministries and a midyear review involving line ministries and central agencies.

2. In-year budget revision

It is difficult to make accurate forecasts for the implementation of certain programs or for developments in economic parameters such as inflation, interest rate or exchange rates. Some immediate needs that were not foreseen during budget execution may appear during budget execution. To limit the effects of these problems, rules for transfers must be flexible; appropriations for debt service cannot be a spending limit and should be revised according to developments in interest rates or the exchange rate. Contingency reserves may be included in the budget. However, their amount must account for only 1-3 percent of the total budget; otherwise, budget execution will involve bargaining the uses of reserves and the budget will become an allocation of reserves.

Therefore, for changes that alter the composition of the budget or when an overall increase in expenditures is unavoidable, the budget may have to be revised. Mechanisms for revisions depend on the countries, and should be clearly stated in the budget organic law. Some broad principles are desirable. Since the budget has been passed by the legislature, revisions should be made by law. Generally, changes in appropriation above a certain percentage of the initial appropriation or changes that affect the total amount of expenditures must be submitted for to the legislature for approval. To allow the government to address problems with dispatch, procedures authorizing exceptional expenditures before the Parliament approves them can be considered. However, the authority should be regulated and limited, and the executive must be required to present a revised budget to the Parliament at short notice.

Supplementary estimates should be approved only at a fixed time and the number of in-year revisions should be strictly limited (to preferably only one in-year budget revision). Some countries present supplementary estimates to Parliament on a case-to-case basis, each time the Cabinet approves a request from a line ministry be, as a result, an excessive number of supplementary estimates are prepared every year (e.g., up to 40 in Sri Lanka). Such procedures should be avoided. Budget execution is difficult to control when budget is continually being revised. Moreover, supplementary estimates granted to one sector may, all too soon, seem better allocated to a higher-priority sector. Preferably, only one budget revision should be made during the fiscal year and requests from line ministries should be reviewed together, not singly.

C. PERSONNEL BUDGETARY MANAGEMENT

Issues of personnel management cover different areas. On the one hand, fiscal stress and the changing role of the government are focusing attention on procedures for controlling personnel expenditures. The growing size of the public service is a major concern in most countries. This is mainly a policy issue, but it also requires appropriate tools for budgeting personnel. On the other hand, systems for personnel management should aim at fostering efficiency in delivering public services. This covers a wide set of issues such as compensation and measures for increasing mobility. Personnel budgeting methods need to take into account performance issues, but the balance

between fiscal discipline objectives and efficiency-performance concerns strictly depends on the context of each country.

1. Approaches

a. *Relevance of recent reforms in some OECD countries*

As mentioned above, in a few countries (e.g. Australia and New Zealand), personnel expenditure is grouped together with goods and services expenditures in appropriations. This is seen to contribute to increased efficiency in delivering services. The possibility of using savings on personnel costs for other expenditures gives an incentive to agencies to make these savings.

Before considering the adoption of such approaches in developing countries and even in certain industrialized countries, it should be noted that flexible methods for personnel budgeting, where they have been introduced, are only some of the elements of personnel management reforms. There is a broader set of measures to make personnel management flexible and reduce the scope of the government, and these measures cannot be defined and implemented alone. These reforms include, for instance, flexible personnel management, covering both compensation system and the recruitment policy, and increased pressure on agencies to downsize their activities, through market-testing systems or efficiency dividends. Increasing personnel performance is a global approach; beginning with budgetary issues is not necessarily the most effective approach of getting results.

Moreover, some measures to improve performance, such as the hiring of consultants for policy advice and the contracting out or transfer of activities to autonomous agencies and local governments, do not necessarily address the immediate fiscal problems met in developing countries.

Even if civil service reform is undertaken, a budgeting approach consisting of mixing personnel expenditures with other expenditures could have undesirable outcomes. In several developing countries, taking into account social pressures on the management of agencies, patronage, or simply the low level of wages and block

appropriations could generate an uncontrolled increase in personnel expenditures. In other countries, bureaucratic resistance may not be easily overcome, and every spending unit may try to demonstrate that its current composition of inputs is the optimal variant. Line-item budgeting has been resistant to the PPBS reforms in most countries.

It is doubtful that block appropriations can be a tool for reducing manpower levels in countries that face arrears on personnel (as is the case in several FSU countries). These countries are currently confronted with the choice of incurring arrears or firing personnel. Both politicians and civil servants show a preference for accumulating arrears. Block appropriations implemented in this context would transfer arrears generation from wage expenditure items to nonwage expenditure items.

Undoubtedly, in countries with a strong internal and external audit system, a long tradition of fiscal discipline, and a flexible management system for the civil service, it is better to allow spending agencies to determine the share of personnel and nonpersonnel expenditures. However, in most developing countries, special attention on personnel expenditure is required.

2. The role of ceilings

a. Personnel expenditure ceilings

Most developing countries define expenditure ceilings as budgeting personnel expenditures under a separate line item and defining rules for limiting transfers between personnel and nonpersonnel items. This definition may be insufficient. Personnel expenditure ceilings are often more of a floor than a spending limit, and rules concerning transfers are aimed at protecting personnel expenditure from overruns in spending on goods and services. In practice, the system has a certain degree of flexibility, but toward an increase in personnel expenditures. There is a need to complement it with a system that allows the government to monitor and control their legal commitments more closely, and not only cash payments and obligations.

b. Staff ceilings⁶

Several developed and developing countries make use of staff ceilings, while some industrialized countries prepare multi-year staff ceilings together with multi-year estimates⁷. These staff ceilings generally give the full time staff equivalent, and are subjected to internal or external controls or both.

When the size of the civil service must be significantly reduced, it is often necessary to prepare personnel plans to determine the specific staff sectors to be trimmed, to define an incentive policy, to estimate the amount of redundancy payments, etc. Staff ceilings would then be the annual implementation targets corresponding to these personnel plans.

In many countries, appropriations for personnel expenditures are underestimated, and ensuring compliance during budget implementation is therefore extremely difficult (for example, firing teachers during the school year could have a high indirect cost because of the disruptive effects on the education system). The inclusion of staff ceilings in the budget would allow the risks of overcommitment of personnel expenditures to be identified clearly at the budget formulation stage. Making the ceilings compulsory would avoid unnecessary commitments in the coming years such as overrecruitment.

Some countries set staff ceilings by personnel category, grade, etc., and manage budgetary posts on this basis. In the same way, a few developing countries prepare organic cadres that define the responsibilities of departments and agencies and the number of posts for each category of personnel. The preparation of these organic cadres has often been based on a needs approach that proved useless in the context of fiscal stress. Such approaches can make personnel management rigid and should be avoided. Staff ceilings should either be aggregated or broken down into a few broad categories. They serve as a tool for controlling the fiscal impact of the personnel policy of agencies and as an aid in personnel management. Line ministries should be made fully responsible for establishing staff ceilings for their subordinate agencies. Appropriations for personnel expenditures and staff ceilings should be consistent. Staff ceilings could be

announced together with expenditure ceilings at the start of budget preparation, and adequate adjustments may be made in later stages of budget preparation, if necessary.

In countries where the size of the civil service does not pose major problems and where methods for estimating personnel expenditures are satisfactory, staff ceilings are not needed. Budgeting personnel expenditures and other current expenditures under separate line-items and regulating transfers between these items could be sufficient to keep personnel expenditures under control. Information on manpower levels is required during budget preparation and should be made public (as an annex to the budget).

However, most developing countries and transition economies need to keep a tight control on their personnel expenditure and to downsize their civil service. They should prepare staff ceilings, to guide the implementation of their personnel rationalization measures.

3. Management issues

Personnel management covers a variety of issues such as those related to regulations governing the civil service or the compensation system. Some of these issues have direct budgetary consequences, notably those related to the compensation system. Personnel management must be performed by relevant line ministries or a civil service board, but any decision that affects the budget needs to be prepared in consultation with the Ministry of Finance and submitted to the same restrictions as other decisions that lead to an increase in expenditures.

4. The payroll system

A payroll system is a tool for ensuring better transparency in personnel expenditures and for monitoring staff ceilings (if any). To be cost-effective, in general, the computerization of the payroll system needs to be centralized. Arrangements can (and should be) be set to allow the line ministries to take advantage of the computerization without giving up their responsibility for personnel management. Close links must be established between the payroll management system and the personnel management system (where personnel information files are kept).

In several countries, the civil service is placed under the responsibility of a civil service board. Good coordination between this office and the Ministry of Finance must be established. If the civil service board manages personnel positions, they should be fully compatible with the staff ceilings and the appropriations for personnel expenditures.⁸ In several countries, data on the civil service are confusing and vary depending on the agency that produce it. Personnel management systems maintained independently from the payroll system are, in some countries, the source of this confusion. If a central personnel management system exists or is expected to be implemented, it must be integrated with the payroll system.

D. PROCUREMENT

The main objective of the government as a purchaser is to obtain high-quality goods and services at a competitive price. Procurement procedures should provide fair opportunity to all bidders, and be designed to get the best value for money and to minimize risks of corruption and patronage. While government procurement is certainly not the only possible source of corruption, it is one of the major ones, and vigilance is always necessary to minimize corruption risks, optimize the use of financial resources, and foster the growth of competition.

1. Procurement cycle

The procurement cycle includes the following stages:

- *Identification of user needs and project preparation.* For supplies, this identification consists of establishing what users require, specifying of the goods or services to be procured, reviewing whether the needs can be met from available stores, whether they can be aggregated with any other outstanding similar requirement, etc. For construction projects, different variants are reviewed to choose the most cost-effective and the project execution plan is prepared to include the characteristics of the project. At this stage, the possibility of a public-private partnership should also be reviewed, as well as the appropriate arrangements.

- *Determination of the procurement procedure.* A key step is to determine the procurement procedure (restricted list of vendors, local competitive bidding, or international competitive bidding). For expenditures financed by external sources, procurement procedures must conform to the guidelines established by the external lender or donor. Major multinational trade arrangements like the World Trade Organization's Government Procurement Agreement also set legal obligations for national procurement systems and practices.
- *Tendering process (generally preceded by a prequalification procedure, depending on the tendering procedure).* For competitive bids, a letter of invitation is sent to tenders. This letter should specify the characteristics of the project or the goods and services to be supplied, the selection criteria, and the award arrangements. Price is an important criterion in awarding contracts, but cannot be the sole criterion. In many cases, price is less important than technical and quality criteria. Choosing systematically the lowest-priced bids could lead to buying obsolete or poor-quality goods or services. To avoid an excessive bias toward low-priced bids, it is often desirable to review the bids in two steps, first on technical grounds, and then on the basis of cost.

2. Principles of competition and transparency

The key principles in procurement are open competition and transparent process. The procurement process should be made open to public scrutiny. The results of the bidding must be made public. Competitors' names, their bid prices, and the name of the successful bidder must be disclosed.

Contract awards and the overall procurement process must be subjected to the scrutiny of the national Parliament and external audit bodies. Written (or computerized) records must be maintained and publicly accessible. These records should show which suppliers were approached, which ones were selected, the reasons for the procurement decision, details of prices, reports on the acceptance of work done or the receipt of goods ordered, and comments on the performance of the supplier.

The legal framework or the code of ethics should include standards about procurement. There should be no conflict of interest between official duties and private interests of civil servants. Appropriate levels of financial delegation and proper separation of duties must be established. Rotation of duties is generally needed to avoid risk of collision due to the development of too close and cozy relationships between the buyer and the supplier.

In some countries, the government also aims to achieve economic policy objectives through its purchasing policy, such as giving preference to local producers or promoting new standards or innovations, in terms of safety, the environment, or other areas. These criteria should be clearly stated and published. In any case, the procurement procedures should promote competition and ensure equity and integrity.

3. Procurement administration

In some countries, the purchasing function is centralized in a central procurement unit. In principle, a central purchasing unit has the advantage of allowing the government to obtain lower prices by grouping its purchases. However, the results may be disappointing because of problems such as slow and bureaucratic response to customers, excessive inventories, losses, pilferage, and slow response to market and technological changes.

It seems preferable to make line ministries fully responsible for their purchases and establish a Central Public Procurement Office to supervise and assist in the procurement activities of agencies. Under such arrangements, the Central Public Procurement Office is responsible for developing rules and regulations, creating a government-wide information and publication system, ensuring that government purchasing entities employ trained personnel, developing a training system, and maintaining general supervision of procurement systems.

E. KEY POINTS AND DIRECTIONS IN REFORMS

1. Key Points

It is possible to execute badly a well-formulated budget; it is not possible to execute well a badly formulated budget. However, budget execution is more than simply assuming compliance with the initial budget. It must also adapt to intervening changes, and promote operational efficiency. A procedure for controls is needed, but should not hamper efficiency nor lead to altering the composition of the budget. The controls must focus on what is essential while giving flexibility to spending agencies in implementing their programs.

a. Expenditure control

The budget system should assure effective expenditure control. The first step is to prepare a realistic budget and to identify measures to contain permanent commitments (such as entitlements, wages). Besides this, the budget implementation system should have the following features:

- A complete budgetary/appropriation accounting system. It is needed to track transactions at each stage of the expenditure cycle (commitment, verification, payment) and movements between appropriations or budget items (apportionment, virements, supplementary estimates).
- Effective controls at each stage of the expenditure cycle, whatever their organization.
- A system for managing multi-year contracts and forward commitments.
- Personnel management system including staff ceilings, which should be controlled and budgeted in countries that need to undertake civil service reform.

- Adequate and transparent procedures for competitive procurement and systems for managing procurement and contracting out.

b. Enforcing priorities stated in the budget

- Cash rationing should be avoided (except in an extreme emergency). Budget implementation and cash plans must be prepared, but they should be based on budget estimates and take into account existing commitments.
- Supplementary estimates must be strictly regulated and their number limited.
- Virements between programs should not alter priorities stated in the budget.

c. Efficient budget implementation

- Budget funds should be released on time.
- Internal controls (within line ministries) should be generally preferred to ex-ante controls performed by central agencies, but the internal controls require a strong monitoring and auditing system. Commitments and verification controls should be internal, to avoid excessive interference by central agencies in budget management. When payment processing and accounting controls are decentralized, central control on cash is required (see chapter 6). When payment processing and accounting controls are centralized, it should be verified that payments are made on time and according to the budget and the cash plan, without additional prioritization. The use of modern technology should make it possible to reconcile the need to decentralize controls for efficiency and the need to centralize data on budget execution for expenditure control.
- Rules for virement should allow both flexibility and control over the major items.

- Carry-over appropriations should be authorized, at least for capital expenditures, but the procedure needs to be regulated.
- The contracting out of government activities should be considered, but caution is needed in contract preparation and management. Procurement for activities that are contracted out should be competitive.

2. Directions for improving budget execution

Budget execution generally needs to be improved in two respects: enhancing expenditure control and creating the conditions for increased efficiency in public spending. An adequate balance between these two different requirements must be found.

a. First step: Ensuring that the basic requirements are met

In a number of countries, the first step should be to reinforce expenditure control as well as to ensure conformity in budget execution with the policies stated in the budget. In this respect, attention needs to be paid on the following points:

- Timely release of funds;
- Cash planning in conformity with budget authorization and taking into account ongoing commitment (for a sound budget preparation is a prerequisite);
- Effective control of expenditures at each stage of the expenditure cycle (whatever their organization internal or ex-ante/external);
- Adequate budgetary monitoring, at each stage of the expenditure cycle (commitment, verification, and payment);
- Clearly defined procedures for recording transaction (notably for commitments);

- Adequate cash management (see chapter 8);
- Transparent procedures for procurement.

b. Second step: Improving the efficiency of the system

To improve efficiency in public spending, the following actions are generally needed;

- Flexible rules for virement and regulated carry-over for capital expenditures;
- Decentralized controls (in parallel with strengthened procedures for auditing and reporting).
- Market testing and contracting out.

¹ Note that management control, which is an important part of budget implementation is discussed in chapter 9 together with audit and evaluation.

² See comparison between the British System and the French System in Jack Diamond and Christian Schiller "Government arrears in fiscal adjustment programs" in "How to measure the deficit" IMF. op.cit.

³ Notably in countries that make a budgetary accounting on the basis of vouchers for payment sent to accounting offices. When these countries face arrears problems these vouchers correspond neither to accrued expenditures nor to cash payments, since arrears are accumulated upstream and downstream the stage of the expenditure cycle at which these vouchers are issued.

³ As shown by the experience of several African countries that have implemented integrated expenditure management systems in the early 80s.

⁴ Sometimes obligational accounting is confused with accrual accounting. There are two major differences. First, obligation basis is usually restricted to outlays, while accrual basis includes both receipts and outlays. Second, accrual basis recognizes liabilities at the verification stage, not at the commitment stage and (for "full accrual") covers uses of goods and services acquired (e.g., recognizes inventories, depreciation). See chapter 7.

⁵ As shown by the experience of several African countries that have implemented integrated expenditure management systems in the early 1980s.

⁶ See SIGMA-OECD, 1997.

⁷ As in the U.S., Denmark, Canada, and the Netherlands.

⁸ In Turkey, the system of cadres managed by the Personnel Presidency led besides the regular cadres, "authorized cadres" and "released cadres".