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Putting Aid On Budget

A Study for the Collaborative Africa Budget Reform Initiative (CABRI)

and

the Strategic Partnership with Africa (SPA)

ETHIOPIA CASE STUDY – WORKING PAPER

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THE AID ON BUDGET STUDY

The Collaborative Africa Budget Reform Initiative (CABRI) and the Strategic Partnership with Africa (SPA) commissioned study of "putting aid on budget" has the following outputs:

- An ***Inception Report***, which defines the issues and research methodology.
- Ten ***country studies from sub-Saharan Africa***. Of the ten country studies, ***Ghana, Mali, Mozambique, Rwanda*** and ***Uganda*** were studied in depth, and separate country reports are available. The experiences of Burkina Faso, Ethiopia, Kenya, South Africa and Tanzania were also reviewed and summary information is included in the Synthesis Report annexes. Findings from all ten countries are included in the Synthesis Report.
- A ***Literature Review***, which (a) documents existing good practice guidance that is relevant to the incorporation of aid in recipient country budgets; (b) reviews the policies and guidelines of the major multilateral and bilateral agencies as these affect the incorporation of their aid into government budgets; and (c) documents relevant experiences of efforts to capture aid in government budgets, including desk reviews of some additional countries, including countries from outside Africa.
- A ***Synthesis Report*** which draws on all the other study components to develop overall findings and recommendations.
- A ***Good Practice Note*** which distils the lessons of the study and is aimed at donors as well as partner governments.

The reports can be downloaded from the CABRI website at http://www.africa-sbo.org/

The **Ethiopia case study** is a background working paper to the Aid on Budget study (not a separate country report). (The Section B matrix is used in the Aid on Budget Synthesis Report Annexes.)

Disclaimer

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This working paper was prepared by independent consultants. Responsibility for the contents and presentation of findings and recommendations rests with the study team.

The views and opinions expressed in the working paper do not necessarily correspond to the views of CABRI or SPA.

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Acronyms and Abbreviations

AfDB	African Development Bank
AG	Auditor General
AMP	Aid Management Platform
BoFED	Bureau of Finance and Economic Development
CAD	Central Accounts Department
CSRP	Civil Service Reform Programme
DAC	Development Assistance Committee
DAG	Development Assistance Group
DBS	Direct Budget Support
DSA	Decentralisation Support Activity
EC	European Cmmission
EFY	Ethiopian Financial Year
EMCP	Expenditure Management and Control Programme
EPG	Ethiopian Partners Group
ETB	Ethiopian Birr
EU	European Union
FIS	Financial Information Systems
FS	Food Security
GDP	Gross Domestic Product
GFS	Government Finance Statistics
GoE	Government of Ethiopia
IBEX	Integrated Budget and Expenditure
IDA	International Development Association
IFMIS	Integrated Financial Management Information System
INTOSAI	International Organisation of Supreme Audit Institutions
MEFF	Macro-Economic and Fiscal Framework
MDGs	Millenium Development Goals
NGOs	Non-Governmental Organisations
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
ORAG	Office of the Regional Auditor General
OFAG	Office of the Federal Auditor General
PACs	Public Accounts Committee
PASDEP	Plan for Accelerated and Sustained Development for the Elimination of Poverty
PBS	Protection of Basic Services
PDAE	Paris Declaration on Aid Effectiveness
PEs	Public Enterprises
PEFA	Public Expenditure and Financial Accountability
PEM	Public Expenditure Management
PEP	Public Expenditure Programme
PFM	Public Financial Management
PIP	Public Investment Programme
PIUs	Project Implementation Units
PRSP	Poverty Reduction Strategy Plan
PRSC	Poverty Reduction Support Credit
PSCAP	Public Sector Capacity Building Programme

PSD	Private Sector Development
PSNP	Productive Safety Net Programme
SN	Sub-National
TA	Technical Assistance
UK	United Kingdom
UN	United Nations
UNDP	United Nations Development Programme
UNICEF	United Nations International Children's Emergency Fund
US	United States
WoFED	Wereda Office of Finance and Economic Development

A. Country Context

A.1 Key Information Sources

Laws and other key documentation of country systems:

- The Constitution of the Federal Democratic Republic of Ethiopia (1994), Proclamation on the definition of power and duties of the executive organs (04/1995), Federal Government of Ethiopia Financial Administration Proclamation No. 57/1996, Council of Ministers' Financial Regulations No.17/1997, Federal Government of Ethiopia Proclamation establishing the Office of the Federal Auditor General No. 68/1997
- Proclamation on the establishment of Ethics and Anti-corruption Commission (235-2001)
- Federal Government of Ethiopia Proclamation Determining Procedures of Public Procurement and Establishing its Supervisory Agency Proclamation No. 430/2005
- Federal Public Procurement Directive, MOFED, July 2005

Diagnostics:

- Federal PEFA Review (2007)
- Regional PEFA Review (2007)
- Fiduciary Assessment (2005)
- Public Expenditure Review – The National State of Tigray [Irish Aid] (2006)
- Protecting Basic Services Instrument – Lessons to be learnt [draft] (2008)

Harmonisation:

- Paris Declaration on Aid Effectiveness (2005)
- Joint Declaration on Harmonisation, Alignment and Aid Effectiveness (DAG/Government of Ethiopia – Draft – 2007)

Aid Management Platform:

- AMP Presentation – Development Gateway Foundation (DGF), Ethiopia: A case study in managing aid by results (DGF)

A.2 Country Institutions

1. After a long history of highly centralised government, Ethiopia is now a federal democratic state that has also embraced wide-scale decentralisation below regional government level.

2. Its constitution, adopted in 1995, sets out a constitutional framework of democratic federalism, with the governance of much of the country bestowed on nine regional governments (and two municipal administrations with regional status).

3. Regional governments run by elected sub-national governments (Regional Councils) are accountable to their citizens and have wide-ranging revenue and expenditure assignments. Most of their resources come from transfers from Federal government via a block grant system. At the centre of the financial management structure in each region is the Regional Bureau of Finance and Economic Development (BoFED) responsible to the Regional Council. BoFEDs are required to prepare annual budgets and accounts of the Regional bureaux and the consolidated accounts of the Region. These have then to be audited by the Regional Auditor General and submitted to the Regional Council.

4. But below this the system is also highly decentralized, with responsibility for much primary service delivery falling to *wereda* (or district) administrations, each representing about 100,000 people with an elected council and a set of sectoral offices. There are currently around 750 *weredas*, with numbers having risen in the last year.

5. Thus there are a number of relationships that need to be taken account of when mapping the fiscal framework: relations between federal government and the regions, between each region and the districts (or *weredas*) below it, and the relationship between Weredas and village councils (or *kebeles*). Whilst the (political governance) issues around federalism and decentralisation are distinct, they contribute two important facets to the fiscal architecture. The 1995 constitution sets out the main issues for decentralisation.

6. In terms of **expenditure assignment,** Federal Government looks after issues of state and certain sector issues best handled at this level (e.g. food security, transport policy). Regional governments are responsible for the implementation of socio-economic development policy, policing of regional states, regional water resource development and standard setting for primary service delivery. *Weredas* are responsible for delivery of primary services.

7. The principal transfer mechanism between Federal Government and Regions is the General Purpose grant, or the Block Grant. The intention behind this is to move resources down to lower levels of government, whilst not compromising the abilities of these tiers to make their own spending decisions. Funds are untied. Funds are allocated according to a transfer formula, which is designed to address efficiency and equity in the allocation. Current formula methodology aims at ensuring horizontal fiscal equalisation, meaning that as a guiding principle each region should be given resources to provide average or standard public services, taking into account average levels of efficiency and average efforts to raise revenue from its own sources. Currently these formulae are being reviewed, and more transparent systems have already been piloted and will soon be introduced nationally A key driving principle behind Ethiopia's federalism is one of regional equity, viz. that any one region should not get over and above what it is due, or place itself at unfair advantage over any other region. This has prompted Federal Government to implement an offset mechanism, where any donor support to a particular region may result in a reduction of Federal Block Grant.

8. Similar mechanisms are in place to transfer resources from regions to *weredas* or districts. It is at district level where primary services are delivered, and thus where much pro-poor budget execution is performed

9. It is largely, at least *prima facie*, up to regions and *weredas* to decide over the sectoral distribution and the allocation of funds between recurrent and capital expenditure.

10. Budget planning and fiscal management therefore happens at a number of different points through the institutional framework, at federal, regional and sub-regional level. This is testimony to the fact that there is not just one budget (and one associated planning process) but rather a multiplicity of plans and budgets, at different tiers in the hierarchy of governments and administrations throughout the federal state, making the sort of analysis needed for this sort of exercise necessarily complex.

11. At the Federal level, the House of Peoples' Representatives is constitutionally mandated to "*ratify the Federal budget*" (Article 55, 11). But Cabinet is responsible for the elaboration of the budget in relation to agreed policy frameworks (in particular Ethiopia's second

generation PRSP, the Plan for Accelerated and Sustained Development for the Elimination of Poverty [PASDEP]), with the Ministry of Finance and Economic Development (MoFED) overseeing budget formulation (with input from sectoral ministries and agencies) and execution. MoFED is involved in the elaboration of the Macro Economic and Fiscal Framework (MEFF)[1] and of the Public Investment Program (PIP). It is also in charge of preparing the Annual Fiscal Plan. MoFED centralises the budget preparation process with line ministries and other Budget Institutions. And it is involved in day-to-day budget execution through treasury and internal audit/inspection activities.

12. The role of the Federal Auditor General is constitutionally defined. Reports of the Auditor General are tabled at meetings of the House of Peoples' Representatives.

13. At regional level a similar institutional pattern is followed, with regions consolidating both budgets and out-turns of weredas within each region.

A.3 Aid Context

14. Ethiopia has high levels of aid dependence. Average total ODA per annum for the period 2003-2005 has run at $1,890 million per annum[2]. Primary expenditure outturn for Ethiopian Financial Year 1997 (July 2004-July 2005) ran at around $2,702 million[3].

15. Composition of aid flows has varied considerably over recent years, with the mix of grants and loans occasionally being around 50/50, with grants beginning to take precedence.

16. A particular feature of Ethiopia's aid dependence is its propensity to need assistance to meet challenges of livelihood vulnerability for its people, and to bridge food gaps, both in terms of in-kind support and (increasingly) cash transfers to the vulnerable. In any one year at least 4 million people are in need of some food related assistance, and large portions of the population are extremely food vulnerable, and susceptible to changes in weather.

17. Aid and development assistance is disbursed using different modalities, or using different 'channels'.

18. Some support, known as support through **Channel 1** is a direct transfer from the donor to the Ministry of Finance using the national treasury. Funds are than transmitted to the final beneficiary through the government PFM architecture, and is thus usually subject to the normal government rules and regulations regarding disbursement and expenditure. It can be tied or untied. Within Channel 1 there are subtle variations, described as Channels 1a and 1b. Channel 1a is managed by the Ministry of Finance and Regional bureaux and uses government rules and priorities to allocate the funding. Channel 1b looks similar in that government systems are used to **manage** the funds (accounting, reporting and the like). However, **allocation** of funds for expenditure lies outside of the government system (i.e. it is not allocated according to block grant formulae or regional planning). These funds are often managed through separate bank accounts, and reflect on the part of donors a wish to fund

[1] With the participation of the Ministry of Revenue and the National Bank.
[2] OECD DAC Development Statistics.
[3] 22,967Billion Ethiopian Birr, at a rough exchange rate of 8.5 birr to the US dollar. This is per data supplied by MoFED for the recent PEFA review.

regional and wereda mandates. But they bypass the Federal and Sub-National Government allocation structures. There is considerable debate about the appropriateness of this.
19. Some support, known as utilising **Channel 2**, will involve direct transfers too, but will 'bypass' the Ministry of Finance, going instead through a sector Ministry (e.g. the Ministry of Health) or government entity at sub-national level (e.g. regional government, regional Bureau of Health). Whilst this support has the advantage of targeting beneficiaries, it also has distinct disadvantages. Firstly the targeting is the donor partner's and not the government's, meaning that there is a possibility that support will not be addressing national priorities or aligning with national planning mechanisms. Secondly, there are no guarantees that such support will be 'captured' within national systems; indeed, it may have donor requirements to manage, report and disclose funds in a different way, effectively setting up a parallel system.

20. 'Traditional' donor partner project support utilises Channel 3. This is not characterised by the direct transfer of funds to a recipient, but will rather involve the setting up of implementation units in parallel to existing government structures, the hiring (by the donor) of technical assistance and the direct provision of goods and services (by the donor). Whilst such projects may reflect national priorities there are no intrinsic guarantees that this is the case. Nor will much of this support be captured in budgeted outturns of governments, although it is possible (and increasingly common) that such interventions are at least captured in some way on national plans.

21. In Ethiopia the main modalities of partner support have been:

- Loans – from the multilateral agencies IDA and AfDB. There are strict regulations about these being 'on budget', both in the way of donor 'conditions' and requirements under Ethiopian law.

- Direct Budget Support – unearmarked (but often linked to fairly specific 'conditionalities') and delivered through Channel One, through the national treasury. Again this was an instrument used predominantly by the multilaterals, with some bilaterals, most notably the United Kingdom, either committing support or actively considering support. This, however, proved in 2005, to be politically too difficult in the aftermath of federal elections where violence broke out. Budget support proved too difficult an option for donors, particularly in respect of domestic accountability pressures.

- Regional Budget Support – unearmarked support delivered not into the Federal treasury, but directly into the treasuries of a region. This is subject to offset in block grant, in an attempt to preserve the Federal Government's attempts at ensuring regional equity. There are thus question marks about what additionality regional budget support might give, although there have been examples (e.g. Irish Aid's support of the Regional State of Tigray's strategic plan) where 100% offset has been negotiated down to a lower figure. But even in this case offset is applied.

- Support to the Public Sector Capacity Programme (PSCAP), a joint donor-government pool, where donors pay into an earmarked treasury pool to facilitate the implementation of a multi-sector reform programme. IDA regulations govern procurement and contracting, but in all other respects this resembles earmarked budget support.

- The Protection of Basic Services (PBS) instrument, which has effectively replaced DBS over recent years. It is an instrument designed to maintain and promote the delivery of basic (pro-poor) services by the sub-Federal Governments and administrations of Ethiopia, whilst at the same time enhancing the transparency, accountability and the culture of democracy in their delivery at local level. It is, implicitly if not explicitly, meant as a direct replacement to DBS, and some of the support under its auspices is provided as a form of highly conditional – and some would say 'sector'-specific budget support[4] through Channel 1. This is not

[4] Component 1 meets current standard definitions of sector budget support, as it is intended to. It only supports dialogue around particular aspects of SN service delivery, and within these wide parameters it is unearmarked and is subject to national systems of allocation and distribution

conditionality focused on sector allocations per se, and supports rather than bypasses national and sub-national allocation mechanisms. There is a number of 'tests' which focus on demonstrating some fiduciary principles, ongoing increases of sub-national allocations through the block grant mechanisms, fairness in the allocations across regions and ongoing commitments to enhanced financial and social accountability. In practice, and taken as a whole the instrument is actually a *melange* of support under the different Channels. There are four components of the programme:

  - The core is Component 1, essentially the financing of the delivery of services through Channel 1, and monitoring that delivery to ensure timeliness, additionality, fairness and verification of actual spending of resources on basic services.
  - Component 2 is, in essence, a 'big push' to try to ensure success in meeting the Health MDG. It is 'on budget' but not 'on procedure' inasmuch as procurement is done in accordance with IDA not Government of Ethiopia regulations, but is managed by the Ministry of Health. In-kind support is procured at Federal level, and distributed to weredas, but neither Regions nor the Federal Ministry of Finance has an input into, or data on sub-national allocation. This can be classes as Channel 2 support.
  - Component 3 will support activities endeavouring to close the gap on supply side capacity relating to financial accountability and transparency, including a 'continuous audit' process of funds flow and expenditure down to district level under the grant mechanism. The continuous audit is interesting inasmuch as it explores not just whether funds (Component 1) have been used for their correct purposes, and in accordance with the regulatory and legal framework, but also whether there have been year-on-year increases in service delivery expenditure at wereda level. Whilst verification processes stop short of establishing direct attribution of increased expenditure back to PBS Component 1 there is a very strong implication that this is what is, in essence, being established. Component 3 of PBS is managed by MoFED, but is, in a sense, projectised.
  - Component 4 aims to enhance social accountability, where citizen voice relating to local service delivery, primarily through civil society intervention, is built and plays a key part in future budgeting processes. Much of this support is to civil society organisations, and is characterised by disbursement through Channel 3. Whilst the temptation is there to look at PBS piecemeal (partly encouraged because its different components use different channels) it is supposed to be seen holistically as a sort of programmatic support.

- The Food Security Programme, which has employed a mix of food aid in kind (Channel 3) and direct transfers into both Channels 1 and 2. Aid in kind has largely been managed by a government agency, the Disaster Prevention and Preparedness Agency (so is Channel 2), although some managed by USAID is managed outside of this (through Channel 3 mechanisms). This has increasingly been superseded by -

- The Productive Safety Net Programme, effectively direct cash transfers allowing the funding of cash safety nets for the country's most vulnerable. The earliest inception of the programme saw cash flows somewhere between Channels 1 and 2, using mechanism first developed for the Food Security Programme.[5] Effectively a hybrid system, initial disbursements were made in the form of Federal Specific Purpose Grants, disbursed from the federal level (from donor funds) directly to the implementing agency at regional level. Over a two year period this has been brought into line with something more akin to earmarked Channel 1 support. These donor funded interventions run in parallel to Federal Government's own Food Security Programmes, using a domestically financed purpose-specific grant mechanism.

- Sector Support Programmes, which have again been a melange of different channels of support and modalities. There are Education and Health Sector Development Programmes, with some support coming in the form of 'earmarked' support through Channel 1, some as transfers to the lead ministries of the sector (Channel 2) and some in the form of in-kind support or technical assistance (Channel 3).[6]

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[5] It is interesting to ask why modalities have been developed in this way by donors. One interpretation is that, certainly in the past, donors have been a little wary of surrendering their funding entirely to Government of Ethiopia systems. Such hybrid design has often been characterised by Channel 2 disbursement directly to the beneficiary (by-passing the Ministry of Finance and Economic Development), perhaps as a means of helping to ensure that funds are received by the recipient and used for purposes intended, but some sort of capture of expenditure into core government systems.

[6] One conclusion one might draw from this is that, faced with the same challenge (posed by the sector development plans and priorities) different donors have come up with different solutions, effectively

And there are sector development programmes for the roads sector and water; the former is supported by sector-specific budget support (Channel 1) provided by the EC.

- Traditional project support, through either Channel 2 or Channel 3.

- Aid in kind, particularly food aid delivered outside of the Food Security programme. Any aid in kind has to be reported by the recipient Ministry or agency to the Ministry of Finance and Economic Development, but there have been some problems with this. Aid in kind is difficult to predict (so often is either not on plan or is inaccurate) and can vary according to external factors (e.g. famine).

22. One interesting feature in regard to the management of some of these modalities is that the World Bank has a role in leading on PBS, the Productive Safety Net and PSCAP programmes.

23. The overall trends of donor support see a move towards Channel 1 support. Channel 2 and 3 instruments have become increasingly less significant, although it seems that some donors are still not able to embrace using modalities which involve direct cash transfers into the government treasury, to be managed by government accounting systems.

24. One issue of great concern to government is the predictability of aid flows. Figures furnished by Government for the Federal PEFA review showed that bilateral donors often pledged much more than was eventually disbursed. This compounds a problem that already exists with regard to the time horizons against which firm commitments are made, which are already too short to be useful for medium-term planning, but rather has the potential to impact at a later stage in the budget cycle, in terms of the availability of in-year ceilings. In a governance structure where there is already a multiplicity of budget and budget processes (at Federal and SN level) this can theoretically have a very detrimental impact at all levels of government, although figures seem to show that if there is a 'hit' to be take, it will be absorbed where possible at Federal level, reflecting a desire to protect grass-roots service delivery as far as possible.

A.4 Institutions for Aid Management

Structures managing aid

25. At Federal Level, aid management is under the overall control of the Ministry of Finance and Economic Development (MoFED).

26. It has dedicated departments, the Bilateral and the Multilateral departments, each charged with negotiation, agreement, resource mobilisation, recording and accounting, tracking and reporting. A number of these duties are performed via the Aid Management Platform (see below).

27. Both the Bilateral and Multilateral departments will liaise with the Budget Consolidation Department and the Planning Department for planning purposes, the Central Accounts Department for reporting and accounting and the Treasury Department in respect of disbursement.

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demonstrating the fact that some donors are more wiling to trust their funding to core government systems than others.

28. Where support is earmarked to a particular sector, or is a specific Ministry Project, the Ministry of Finance's two resource mobilisation departments still have to lead negotiations, and be the main signatory.
29. Sub-national governments do not have the power to enter into agreements with donor agencies independently of MoFED. In some cases, where such support may be contributions to sub-national treasuries an offset will be applied. Government is resistant to any attempt of donor agencies setting up strong bilateral relations with any one region, and has expressed its displeasure when bilateral and multilateral agencies (as distinct from international NGOs) have tried to set up regional offices to deal with SN governments directly (the case of UNICEF and its desire to set up regional offices has been cited). There is no resistance to such arrangements when MoFED is still the focal point of agreements around disbursements, however (e.g. Irish Aid and its offices in National State of Tigray).

30. Where a public body, such as the Ethiopian Roads Authority, the Ethiopian Telecommunications Corporation or the energy sector, is in receipt of donor funding this too will be handled by MoFED's resource mobilisation departments, with different liaison points for accounting functions, but with disbursement through the national treasury. However, as the PEFA Performance Report of 2007 has noted, both public enterprises and a number of funds of government (including the Road Fund, Pensions Fund and Disaster Preparedness funds) are not on-budget. Scrutiny of public enterprises by Federal Government is apparent, but the funds are much more autonomous, and can represent anything between 12% and 15% of federal government expenditure. Nevertheless, information about these funds is disclosed as part of the budget information that goes to parliament (effectively a note to the accounts) and is subject to external audit which reports to parliament.

Donor structures

31. Development partners have two Addis-based structures which coordinate development relations and dialogue.

32. Donor agencies are represented by the Development Assistance Group (DAG), co-chaired by the UNDP and World Bank. The DAG has a number of technical working groups, often the focal point for sector support programmes, and working closely with national counterparts (e.g. Education). However, the picture is complicated somewhat by donor groups for particular programmes, which run in parallel, but run the risk of cutting across the DAG technical working groups.

33. Resident ambassadors of donor nations in Addis Ababa meet in the Ethiopian Partners' Group (EPG). Whilst the focus of much of their business is political, there are obvious crossovers with the DAG, particularly as the nature of contemporary development has increasingly taken on a political dimension (witnessed, for instance, during the suspensions of budget support following political events of 2005-2006).

34. The two groups (EPG and DAG) each contribute members to the High Level Forum, a meeting with senior members of Ethiopia's Federal Government, to discuss a range of issues. Some of these are directly relevant to the subject matter of the aid on budget study, for instance interruptions in budget support, predictability of support and the ability of international partners to commit to medium-term projections in aid.

35. The DAG and the Government of Ethiopia are currently working on a joint document, *Joint Declaration on Harmonization, Alignment and Aid Effectiveness.*

Aid data systems

36. Ethiopia is currently implementing an Aid Management Platform in collaboration with donor partners.

37. The Aid Management Platform is an e-government tool aimed at improving government capabilities to manage aid flows, related information and documents. It is a solution that has been developed by the Development Gateway Foundation, a non-profit organisation with World Bank backing, in cooperation with the OECD, World Bank, UNDP India Research and Training Centre and the Government of Ethiopia. Its purpose is to support the implementation of the Paris Declaration on Aid Effectiveness (PDAE). It is intended to put the recipient partner government in control of the development process. Its expressed benefits are that it:

- provides a consistent, transparent view of aid resources for better decision-making based on current data.
- streamlines aid management processes of developing country governments and their donors, in respect of data collection, processing, management and reporting.
- builds capacity, enables aid harmonisation and coordination.
- standardises terminology.
- enables timely, accurate, and comprehensive reporting and analysis of aid flows, trends and projects.

38. The idea is that both donor partners and government have access to a shared integrated system, and can both input data into that system. This can include commitments, disbursements and expenditure data. Information can be shared amongst stakeholders at any stage of the budget cycle, and is standardised in terms of both format and terminology.

39. The system comprises six modules, namely:

- The Aid Management Module – which enables all partners to manage their portfolios, provide timely information, and also management of that information;
- The Reporting Module – allowing the creation of standardised and customised reports for all stakeholders;
- The Monitoring and Evaluation Module – allowing results based impact evaluation of projectised interventions;
- The Planning Calendar – allowing the coordination of missions and key events in the aid budget calendar;
- The Document Management Module – allowing access to a centralised database of key documents; and
- The Budget Integration Module – allowing the sharing of information between the AMP and the budget system. (This is perhaps the most critical module for ensuring that aid is genuinely on budget, as it will ensure genuine interface between the data entered by stakeholders into the AMP and government's core budget system. However, this module has not been developed. The challenges are many, not least that Ethiopia will shortly begin the development of an Integrated Financial Management Information System (IFMIS) which will replace the existing architecture).

40. Roll-out of the system began in May, 2005. The first two modules of the platform were the first to be implemented, and there were notable early gains, in particular in agreement between all stakeholders about the design and format of reports.

41. But unfortunately the AMP is yet to be used to its full potential. Whilst progress has been made in terms of developing the AMP as a functional internal system, and is being used to generate reports for internal GoE use, and as the basis of externally supplied information, it is not available online. Input of data from donor agencies is limited, and accessibility to the system constrained to being able to examine inputs from that stakeholder agency only. It is not possible for donors (or indeed citizens and other interested stakeholders) to access the system in such a way as to see the aid picture in the round, with information disclosed in respect of all donor agencies. Some have reported that there is reluctance on the part of the Government of Ethiopia to open the system up and realise the full potential of the system by placing it firmly in the public domain.

42. That having been said, there have still been some notable gains secured by the implementation of the system. In December 2006 the Development Gateway Foundation performed a survey of system users within the Ministry of Finance and Economic Development. Some notable efficiency gains were noted, particularly in producing new reports (the average time for which had fallen from over 24 person hours to just 6.75 hours, with some users reporting a reduction of over 90%), on time spent on data entry (which had approximately halved), and in answering some typical queries. The ones used for the survey were *"What ongoing projects do we have in the health sector by donor?"* which can now be answered in an average of 24 minutes (down from nearly three hours), and *"What are the total commitments by donor by sector by financial instrument (e.g. grant/loan)?"* which can now be addressed in an average of a little over 45 minutes (down from nearly five and a half hours).

43. Nevertheless, further gains will be limited unless the AMP is able to operate in a more transparent way, with full interconnectivity of stakeholders. One of the reasons why an AMP might be seen as necessary is that donor behaviour does not always live up to the expectations required of the Paris Declaration. But if poor predictability, a lack of willingness to commit over the medium term, and poor reporting are not exposed by an AMP operating in the public domain (these all being issues, to a greater or lesser extent, in respect of donor behaviour in Ethiopia) then the mechanism will not be able to exercise maximum influence on stakeholders. The benefits of the provision of a transparent view of aid resources, and of the provision of timely and accurate data will continue to be compromised until this eventuality changes.

A.5 Legal and practical Framework for Budgeting

44. The Federal Democratic Republic of Ethiopia has a strong legal and regulatory Public Financial Management framework which has slowly evolved, partly as a result of ongoing reform processes.

45. The *Constitution* was adopted on December 8th, 1994. It establishes a Federal and Democratic State structure (Art. 1 and Art. 46). It sets out some important provisions regarding the Minister of Finance, defines some important parliamentary roles regarding budgetary oversight, and establishes the Office of the Auditor General.

46. Other important laws and proclamations relating to PFM include:

- Proclamation on the definition of power and duties of the executive organs (04/1995)
- Federal Government of Ethiopia Financial Administration Proclamation No. 57/1996
- Council of Ministers' Financial Regulations No.17/1997. This sets out the overall framework budget calendar which is then issued annually in a separate annual Financial Management Directive
- Federal Government of Ethiopia Proclamation establishing the Office of the Federal Auditor General No. 68/1997
- Proclamation on the establishment of Ethics and Anti-corruption Commission (235/2001)
- Federal Government of Ethiopia Proclamation Determining Procedures of Public Procurement and Establishing its Supervisory Agency Proclamation No. 430/2005
- Federal Public Procurement Directive, MOFED, July 2005

47. There has been a relatively long and successful track record of PFM reform in Ethiopia. Current reforms are encapsulated in the Expenditure Management and Control Programme (EMCP), now subsumed into the Civil Service Reform Programme (CSRP), part of a multi-sector Public Sector Capacity Building Programme (PSCAP), a US$400 million programme supported by government and a number of donors paying into a pooled fund.

48. Initially the EMCP comprised work streams relating to the Financial Legal Framework, Public Expenditure Programme (PEP), Budget Reform, Accounts Reform, Cash Management, Financial Information Systems, Internal Audit, External Audit, with later additions relating to the Auditing and Accounting Profession, Management Accounting, PEM Program Plan (integrating *PEM/PFM* reforms under one plan*)*, Financial Information Systems Strategy, Procurement Implementation Support, and Property Management.

49. Particular progress has been made in the areas of Budget, FIS and Accounts reform which have been bundled together in the Decentralisation Support Activity Project,[7] which given the nature of first Federal reform and then decentralisation, has had as its focus implementing reforms at SN level (albeit based on systems, procedures and methodologies first rolled out at Federal the level).

50. The DSA project has had a profound impact at all levels of government. A platform approach has been taken to reform. Initial measures have been taken to enhance the transaction platform through budget reforms (e.g. bringing together capital and recurrent budgets, reclassifying expenditure, drawing up new charts of accounts), planning reforms (budget calendars) accounting reforms (moving to double-entry, modified cash, single-pool systems through a series of incremental and sequenced reforms) and financial information systems reform (effectively seeing automation of these reforms once established, culminating in the development of an integrated system showing budget and dispersal information alongside accounting/budget execution information). A second series of reforms have enhanced the policy/performance platform through the creation of a Macroeconomic and Fiscal Framework, and is currently continuing at sub-national (SN) level with reforms to the block grant mechanisms. There has also been discussion about a move to more output-based budgeting (something which the IMF has explored at federal level), but there is still no Medium Term Expenditure Framework. The DSA project also looked at how a performance element might be incorporated into the block grant, but this is not something that is attractive to Government, which wishes to promote equity as the overriding principle driving disbursement and allocation decisions,

[7] A project funded by USAID, Irish Aid and the Netherlands, with Harvard University as the executing agent.

51. Very careful sequencing (both in terms of building up the respective platforms sequentially, and also in terms of region-by-region roll-out), iterative and repeated training, and drives to build sustainable internal capacity to continue training and reform effort (rather than rely on externalized technical support) have all contributed to the success of DSA, which has now completed the roll out of reforms to most parts of the country and which, given the 'interconnectedness' of decentralised/Federal Ethiopia has resulted in a number of positive outcomes, not least the significant reduction of accounting backlogs over recent years.

52. There has also been recent progress in some other areas of the EMCP not covered by DSA activities, in particular internal audit, procurement, cash management and external audit.

53. Another current development is the move towards the implementation of a fully integrated IFMIS system. The issue about whether to develop and implement an IFMIS has been discussed in the country for some time. Although not really part if its original mandate, the DSA project has automated its systems and procedures, and latest iterations of the budget and accounting reforms present an integrated budget and accounting solution, the Integrated Budget and Expenditure (IBEX) system, which incorporates the functionality of budget and disbursal systems and accounting systems. It has apparently now been decided to build on IBEX functionality and deliver a full-blown IFMIS system.

54. A robust classification system allows the satisfactory tracking of spending. The budget formulation and execution is based on economic and sub-functional classifications. The economic classification uses GFS standards. There are currently twenty (20) sub-functions, which are distributed among four (4) functions of expenditures: Administration and General, Economic, Social, and Other. The classification system also includes source of funding data, linked to the structure as set out in the AMP.

55. There is a similar regulatory structure in each region. Each region has its own constitution and proclamations, but the overall blueprint is based upon the framework that exists at federal level.

Budget Calendar

56. *Note: The Ethiopian Financial Year runs from July 8th one year to July 7th the following year. Ethiopian calendar years run from September 12th. Ethiopia's calendar is approximately seven years behind the Gregorian calendar, i.e. the year 2000 (EC) began on September 12th 2007 (Gregorian calendar). EFY 2000 had already begun, on July 8th 2007.*

57. A new indicative financial calendar was introduced in Ethiopian Financial Year 1994 (2001/02).[8] It includes a planning and a budgeting cycle. The planning cycle has three stages which are implemented in sequence:[9]

1. The elaboration of a Macro-Economic and Fiscal Framework (MEFF);
2. The multi-year programming through the preparation of a Public Investment Program (PIP);
3. The development of a Fiscal Plan.

[8] Budget Reform Design Manual (2000), Part II, Chapter 5, pages 95–113.
[9] *Idem* page 95.

58. The budget cycle involves the preparation, review, approval, appropriation, and implementation of the annual budget and has four (4) parts (each part having one or several steps):[10]

1. The executive preparation;
2. The legislative adoption;
3. The executive implementation;
4. Audit and evaluation.

59. The calendar is roughly thus:

Financial Calendar

CYCLE	CALENDAR
Planning Cycle	
1. Macro-Economic and Fiscal Framework	July 8 - November 10
1.1 Preparation of MEFF	Not later than October 26
1.2 Approval of MEFF	October 27- November 10
2. Public Investment Program Preparation	November 11 - February 8
2.1 Public Investment Program call letter	November 25
2.2 Submission of Public Investment	Not later than December 25
2.3 Review and Finalize PIP	Dec. 26 – Feb 8.
3. Notification of a 3-year subsidy estimates	November 25
4. Prepare and finalize Annual fiscal plan	January 24
Budget Cycle	
A. Executive Preparation and Recommendation of budget	
1. Budget preparation	Not later than Feb 8
2. Notification of annual subsidy budget	Feb. 8
3. *Issue* budget call	Feb. 8
4. *Submit* budget Request	Not later than March 22
5. Preparation of the Recommended budget	March 23 - May 22
6. Budget Recommendation	May 23- June 2
B. Legislative Approval	
7. Approval and appropriation of the budget	June 8 - July 7
C. Executive Implementation	
8. Notification of the approved budget	July 8-15
9. Submission of Budget allocation and action plan	July 16-Aug. 16
10. Implementation of the approved budget	July 8- July 7

60. At SN level there is a manual for the budget cycle and budgetary entities with a calendar at both wereda and region levels which is adhered to. It is similar to that which is in place at Federal level.

[10] *Idem* page 104.

61. The recent PEFA review noted that comprehensive and clear budget directives, which reflect ceilings approved by the regional parliaments and wereda councils, are issued to wereda and regional level bodies by Federal Government on time. A potential problem is that finalisation of particular budget ceilings may be delayed (sometimes until the financial year had actually begun). Final ceilings did not materially differ from the indicative ceilings issued at the beginning of the budget process. The system thus appears relatively free of shocks at sub-national level. For EFY 1999/2000 (after the PEFA review) these problems were compounded by the length of time it took Federal Government to agree the public sector pay deal. Regional governments declared large amounts in their budgets under 'miscellaneous', in effect holding a contingency which could be allocated against any subsequent agreement.

Problems in budgeting and PFM

62. The challenges that Ethiopia faces in terms of budgeting and PFM are invariably linked to the broader challenges of federalism and extensive fiscal decentralisation. These two initiatives, linked although separate, result in a multiplicity of budgets and PFM systems under the federal umbrella. Within this complex governance structure service delivery has been devolved to administrations at very local level (weredas or districts); whilst this has enormous political advantages, particularly vis-à-vis the potential for accountability or response, there are huge challenges regarding capacity. It is widely perceived that low capacity is the biggest impediment to improving PFM nationwide.

63. The PFM system produces a Federal budget which is broadly realistic and is more or less implemented as intended. However, budget and fiscal risk oversight are not comprehensive and fiscal and budget information accessible by the public is limited. There are, nevertheless, efforts at the Federal level to ensure that the budget is prepared with due regard to government policy. Overall, these various elements support aggregate fiscal discipline, the strategic allocation of resources and an efficient service delivery in a satisfactory fashion. A move towards medium term budgeting, linked to strategic plans, and greater clarity at SN level, in particular wereda level, will enhance strategic allocation further. More robust institutional linkages between plans and budgets will also enhance strategic allocation, particularly in the context of scaling up resources for primary service delivery, an issue that has driven donor support for the Protecting Basic Services modality. But an issue here is that there are some fundamental disconnects between strategic plans and the fiscal framework. Plans tend to be ambitious and needs-based, whereas the fiscal framework is prudent, and what becomes clear is a significant funding 'gap'.

64. The capacity issue has been most apparent in the past in Ethiopia's relatively poor performance regarding in-year and end-of-year reporting. Because of the interconnectivity of the various jurisdictions at SN level, delay in end-of-year reporting in the regions has a knock-on effect for federal government. In-year reporting has been poor, and end-of-year reporting severely delayed, resulting in quite considerable backlogs of audited accounts presented to the House of Peoples' Representatives. But recently reform initiatives have really begun to take effect, and these backlogs are soon to be eliminated altogether.

65. As has already been noted, current reforms, encapsulated in the Expenditure Management and Control Programme (EMCP), which is now part of the multi-sector US$400 Million Public Sector Capacity Building Programme (PSCAP), have a fairly successful track record of reform. Reform builds on a strong culture of public service and now driven by colossal commitments of government empowerment through decentralisation. Leadership is

high, and well-articulated support modalities exist through PSCAP (although bottlenecks, some on the donor side, need to be removed so that funding can be properly mobilized).

66. Whilst the implementation of EMCP across its various sub-themes has historically been uneven, much recent success has been achieved in the roll-out of budgeting, accounting and FIS reforms country-wide via the Decentralization Support Activity (DSA) project. This is soon to come to an end and a challenge will be how to manage the transition and maintain reform effort. Government leadership in this area is high, but the capacity to take forward a coordinated reform program across a number of areas is one which may well need ongoing partner support for some while.

67. Nevertheless, outside of DSA, Ethiopia has also made recent progress in implementing reforms relating to procurement, cash management and internal audit, and is now planning to embark on the implementation of an Integrated Financial Management Information System (IFMIS).

68. Taken together, this well-articulated, government owned and government led reform programme can help deliver the reforms needed to improve on aspects reported on in this report, given time, resources and partner support.

69. However, arrangements for parliamentary scrutiny of public finances and follow up by the executive are not as strong as they could be, and were subject to some somewhat adverse comment in the PEFA review. The review also noted that external audit coverage of wereda level expenditure is not as extensive as it first appears.

70. Subsequent to the PEFA review being published there are growing concerns - on the part of donors in particular – that resources are not being utilised in the most effective manner. It might well be that this has come to a particular head because the instruments now being deployed by donors – PSNP and PBS in particular – include large elements which are managed at wereda level. Much of this is ‘anecdotal’ but it has been picked up by opposition MPs (who are nevertheless often politically motivated to pay lip service to such allegations). Some donors are frustrated by slow progress in the amelioration of reporting and audit coverage.

71. Much of the above is reflected in two Public Expenditure and Financial Accountability reviews undertaken in Ethiopia in 2007, one at federal level and one looking at seven regional jurisdictions. Annex 1 reproduces excerpts from relevant sections of each report.

B. Evidence and Assessment of Aid Capture

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B1	On plan	Ethiopia's second-generation PRSP, the Plan for Accelerated and Sustained Development for the Elimination of Poverty (PASDEP) has now been costed for all sectors and aligned with Ethiopia's Macroeconomic and Fiscal Framework (MEFF) – a three year rolling federal framework - for the life of the PASDEP (2005/6 – 2009/10). It is finalised in draft before January of each year, and is used as a basis of the annual budget, which is finally tabled by Federal Government to the House of Peoples' Representatives in May. This costing includes resources that have to be raised externally. As a second stage of the planning cycle, a Public Investment Programme is also prepared, covering capital expenditure over a three year period. In general, at the federal level, planning processes take good account of external support, and across some sectors (e.g. Education) there are joint sectoral reviews. But there is no Medium Term Expenditure Framework, linking planning processes to expenditure forecasts and budgeting systems. The MEFF only goes some way to providing the necessary linkages. Given the disconnects, the propensity to have included items at the planning phase that are not then captured in budgets, or vice versa, is heightened. In general, the links between strategic planning process and budget allocation are poor, a fact that was subject to comment in Ethiopia's PEFA	There are real issues about timeliness of information flows, and the extent to which donors feel able to make predictable commitments to aid flows in such a way that these can then be used in a meaningful way for the planning process. Tangible commitments are actually only really made on a year-on-year basis for most of the bilateral donors (the UK being a notable exception). This is one of the drivers behind GoE's move to cost the PASDEP using scenarios, where different levels of plan intervention are predicated by varying degrees of donor commitment and support. The MEFF is often based on figures of donor support that are estimates rather than firm. Donors do not, under current arrangements, usually supply indicative figures of support until January (i.e. six months before the start of the financial year), but even under this arrangement many donors are late in providing information. The Government has attempted to change this, inter alia by seeking agreement at the Development Assistance Group (the DAG) that information should be supplied in September preceding the start of the financial year in July, and by raising the issue at the High Level Forum (the forum where high-level dialogue takes place between DAG members and government). However, DAG members feel that the proposed change is not one that can be accepted, as it is too early in the budget calendars of many donors to give firm commitments this early.[11] Given the complexity of Ethiopia's planning and budgeting systems, where SN budgets are dependent on federal subsidy, these uncertainties have the potential for serious 'knock on' effects, although in practice evidence suggests that there is good predictability of federal commitments used for SN budget ceilings, even when budget support has been suspended There have also been issues around the reconciliation between costed plans for the PASDEP and disclosed receipts of aid. There have been huge discrepancies between what the Government has disclosed as the figure needed to operationalise the PASDEP, and the amounts donors say have been disbursed to government, with donor records apparently showing more funds disbursed than are disclosed in government records.	Some of the reluctance around long-term commitments from donor partners is probably due to the perceived volatility of the domestic political situation in Ethiopia. Direct budget support arrangements were severely disrupted and then 'repackaged' after the 2005 elections, and donors do not seem willing to commit beyond relatively small time horizons. It has also resulted in the design of aid modalities which, whilst using Channel 1, are relatively inflexible, having pro-poor service delivery expenditure at decentralised level as their target focus At SN level the planning process has little meaning because resource envelopes are so constrained. In reality discretion is very limited, and SN entities have to take on unfunded mandates, particularly at wereda level.

[11] Letter of DAG to State Minister of Finance and Economic Development dated 14 May 2007

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B2	On budget	The extent to which aid can be said to be on budget varies across aid modalities. The OECD/DAC Paris Declaration Baseline Survey results put aid reflected on budget at 74%. Funding through the large strategic instruments (PSCAP, PSNP, and PBS) is fully on budget. Loans are also shown. According to MoFED data, most bilateral support is through Channel 1 or Channel 2, and is captured. One possible item that is not included is any 'freestanding' technical assistance, provided not as part of donor projects (which do get captured) but as separate, self-contained interventions. One anomaly of the federal system and an issue that has arisen from time-to-time is support to sectors at sub-regional level. It is possible for such support to be on budget and on treasury for a region, yet for the activity to remain off budget or not reported at federal level. Certain donors set up their own reporting requirements, and whilst to all intents and purposes Channel 1 might be used at SN level, it is not then reported at federal level. In theory this is not permitted (as agreements have to be ratified by federal government), but in practice it has happened, and is exacerbated by the modus operandi of particular donors (e.g. UNICEF). Support of SN entities by NGOs has been subject to the same problems – again in principle, GoE should know all about aid from any given NGO since each NGO has to get regional government approval for its operations, but in practice there have been instances where operations remain 'off budget'. There are also some anomalies of funds being on-budget at regional level but not at federal level too (e.g. PSNP) which has implications for the achievement of PFM objectives in respect of sub-national expenditure. Budgets at SN level take into account aid flows (e.g. Irish budget support in Tigray, Swedish support in Amhara, etc).	Unreported aid at SN level is becoming less of an issue. MoFED reports improvements in donor behaviour. Increasingly donors are moving 'towards' Channel 1, meaning that more and more aid flows are captured, and that flows that are not are the exception rather than the rule. What is clear is that the Government of Ethiopia is itself doing much to capture as much aid on budget as possible. This can be evidence by the attempts to close out SN agreements that bypass MoFED, and by attempts (documented in 'on plan', above) to get donors to commit to timely information regarding aid commitment and disbursement. Information is credible in that it is information generated in partnership – using information passed on by donors. Increasingly, the hope is that the Aid Management Platform can be used as a vehicle for this – with donors plugging intended support figures directly into the system. There are some issues about accuracy of data for aid in kind. It is not always possible to properly predict such aid especially if it is linked to unforeseen events such as emergencies (e.g. flooding in Dire Dawa in 2006). Central Accounts department are ultimately responsible for disclosing all aid in kind that has actually been disbursed, but this is difficult to capture at budget stage.	More timely information from donors would help the completeness of budget information. A move towards single treasury systems in SN jurisdictions and an improvement in what government has termed 'UN behaviour' is helping to reduce the chances of 'undisclosed' aid at SN level. However, there are incentives for SN jurisdictions to leave such support off budget, account and report if they avoid the apparent penalisation of offsets in block grant. However, Federal government is adamant that offset mechanisms are needed, both to preserve equity amongst regions and to create disincentives for donors to upset the fine balance of the decentralised fiscal framework.

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B3	On parliament	Information about aid flows is included in the budget information pack which is presented to parliament as part of the overall budget approval process. An Appropriation Bill is approved, and this becomes the current year's Appropriation Proclamation. By implication external aid flows are noted (as otherwise, given Ethiopia's aid dependency, the budgetary expenditure approved could not be financed). One school of thought states that aid is not 'approved' by parliament as such, as parliament is informed rather than actively considers aid agreements. MoFED contested this view at the time of the review, stating that aid agreements, inclusion in the budget and the disbursement of funds are submitted for parliamentary approval.	There are real issues about the extent to which parliament engages in this process. The regulatory framework allows for parliamentary bodies at Federal and SN level to scrutinise the budget, and also budgetary out-turn, but in practice little time is given to this activity – especially at SN level. There are also issues about capacity of parliamentarians, and in particular whether there is an understanding of the role of parliamentarians, something which also impacts on the effectiveness of the external audit function.	One issue is that parliamentarians do not understand their role, or the institutional framework in which they operate. There have been similar gaps of understanding regarding the issue of external audit. As things stand, the extent to which parliament is engaged in anything more than rubber stamping is a moot point.

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B4	On treasury	Many aid modalities are 'on treasury'. What is particularly notable is that there has been a move away from Channel 2 and Channel 3 support from most donors, towards Channel 1, meaning that increasingly support is going through Government of Ethiopia Treasury systems. For example: o PBS uses Channel 1in Component 1, but Component 2 uses IDA procurement procedures and Component 4 is Channel 3. o PSNP is coming on to Channel 1 – issues had been around reporting rather than disbursement, but all funds go through treasury systems at federal level and is earmarked. At SN level it is not reported o PSCAP support is also on treasury, too (although IDA procedures are used in procurement, once more) o Sector support uses a variety of modalities, some of which use treasury mechanisms (but some of which are Channels 2 and 3) Only Channel 3 projects seem now to be totally off treasury, but these interventions are reducing in number and importance. Data provided for the PEFA review shows a move to direct budget support by donors in the FYs 2003–2004, a trend that was only interrupted by difficulties associated with the election. However, some major donors (e.g. the US) still channel a lot of support though Channel 3. If amounts are budgeted the use of bank accounts needs treasury approval. Bank account use very strictly controlled But some bank accounts – e.g. for support to government funds (road fund, etc) are not strictly speaking under the direct control of government, even though the fund itself can be seen as a n agency of government, with appropriations authorised by parliament, etc.	In some instances, there are incentives for SN jurisdictions not to disclose particular elements of support (particularly support going to sector bureaux) as, if such support remains off-budget and off-account, issues around offset of block grant might be avoided. However, this is becoming increasingly difficult because reform processes are gradually implementing single treasury systems country-wide. This plus rigorous control over bank accounts means that usually any support going to sub-national sectors is now being captured through treasury systems.	There are still incentives to maintain more traditional 'stove-pipe' grants to sectors, particularly at SN level. But a technical reform is making this 'loophole' more difficult to access. It seems that individual donor behaviour as much as anything else is a factor here. There are a number of incentives for wanting to avoid using Government of Ethiopia treasury systems, e.g. • Political issues – this became particular prominent, after the 2005 elections and relates to donor reluctance to being associated with what thy see as a poor human rights record on the part of the Government; • Offset issues – a belief that any direct support to government sectors, or sub-national government structures will be offset by compensating reductions in federal government disbursement to these areas. Offset of block grant is explicitly made in respect of donor support given to regions (e.g. regional budget support). This demonstrates the Government's own commitment to the principle of 'equity' between regions, and their belief that this is compromised by using distribution channels outside of their own. But this has had an impact on 'on budget' and 'on treasury' issues in that donors have in the past sought to give support to entities or programmes at SN level whilst 'avoiding' core government disbursement and reporting systems • Additonality issues – the need to show that donor support has resulted

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
				in greater resources at SN level has heavily influenced the design of the PBS modality. But in the past donors appear to have been reluctant to 'trust' government systems in this regard. • Systemic issues – where donors have significant doubts about the efficiency of government systems in relation to delivering support to where it is needed, or – critically – fiduciary issues – where the fear is that monies will not be used for the purposes intended before, or may even 'leak' from the system. Recent progress in PFM reform has made this position less tenable than it was.

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B5	On account	All Channel 1 funds use country's accounting system. Channel 3 support will not use government accounting systems, but nevertheless there are regulations to ensure that reporting of such activities follows government formats, to allow such activities to be put 'on report'. Support to the off-budget funds, such as the fuel fund, the Ethiopian Roads Authority, etc. is also strictly speaking off account, as these entities have their own accounting systems. However, the initial disbursements will be 'on treasury' and also 'on parliament' and fund information is reproduced as a form of note to the accounts. There has been a tendency in the past to create hybrid funding channels, where money is directed in a manner similar to Channel 1, but where separate reporting requirements are made. But the trend is now to increasingly use government accounting systems.	Accounting system allows for expenditure to be classified by source. Chart of Accounts follows GFS model. Coding allows expenditure to be identified both in terms of source of financing and detailed expenditure data (including all expenditure through SN jurisdictions). The IBEX (government accounting) system at both federal and SN levels appears to provide very concise information about sources of funds, and their use. There have, in the past, been issues around the timeliness of financial information, both regarding in-year reporting and the closing of accounts. At one stage backlogs existed for a four-year period. This was a particular issue for the consolidated accounts showing federal and regional information. In a very real sense the timeliness of such reporting was constrained by the capacity at the weakest weredas. However, these issues have also been resolved, mainly due to successful reform processes.	Steady progress in PFM reform is perhaps one critical reason why there has been a move towards Channel 1 support. The Decentralisation Support Activity Project, part of the Government's Expenditure Management and Control Programme, has addressed a number of issues, including: o New Chart of Account and coding structures; o A move to double-entry bookkeeping; o A move to single treasury accounting; o The integration of budget and accounting systems As a result accounting systems are more credible, and produce more timely information. This has, for many donors, removed the impediment to considering Channel 1 funding modalities,

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B6	On audit	The audits of the Federal Auditor General will, as a matter of course, pick up all Channel 1 support. Audit of activities under PBS modality doubly supported by the 'continuous audit' process, where accounting firms appointed by the Auditor General will audit the use of PBS monies to ensure additionality, and that they were used for SN service delivery activities (rather than for things other than those related to direct service delivery, e.g. defence expenditure). This is a particular change in focus on traditional audit, which usually looks only at the appropriateness of expenditure (and supporting systems of recording, etc), plus, at best, some consideration of efficiency and effectiveness. All IDA funds (loans and grants) are subject to audit scrutiny through a process overseen by the Auditor General (although he may appoint an executing agent for this). UN processes, such as National Execution Projects are also subject to external audit by the AG. There have been instances, both in audit fieldwork and in comments in audit reports, of the Federal Auditor General picking up anomalies about disclosure of aid (where, for instance, there appeared to be discrepancies between food aid budgets and eventual outturn).	There are a number of issues which cast some doubt on the quality of external audit processes in Ethiopia. Firstly, there are issues about audit coverage, and the respective mandates of the Federal Auditor General and Regional Auditors General. In practice SN coverage of front-line expenditure, much of which will have been funded by loan or grant is patchy (hence the need for 'continuous audit' of PBS – in a sense an attempt to bypass standard external auditing systems). Whilst disbursement of block grant to regions (which will contain elements of foreign assistance) is audited by the Federal Auditor General, the use of such monies falls under the control of Regional Auditors General, but external audit can be very limited indeed (sometimes, according to the regional PEFA, less than 30%), due to insufficient resources of the offices of Regional Auditors General. And the capacity development that has been undertaken by the Office of the Federal Auditor General is not mirrored by many of the offices in the regions (although the regional offices of Tigray and Oromiya came out of the regional PEFA assessment well, and Amhara, a region not covered by the assessment, has also a reputation for a strong office). Not only is methodology lacking; institutional frameworks are weak, with poor understanding of the role of an Auditor General widespread amongst the major stakeholders, resulting, inter alia, in poor parliamentary review and follow-up. Secondly, there has been an ongoing issue about the timeliness of audit reports. Backlogs have been severe, and observers have noted that the impact of audit reports, however good the reports themselves might be, has suffered because of the historical nature of the information examined and the issues raised. Accounting reforms have now largely overtaken this issue, and backlogs are about to be eliminated, but this issue has nevertheless had an impact.	Audits have been delayed because of accounting backlogs rather than delays in the auditing function itself. This is gradually being remedied through the ongoing PFM reforms, and, given current trajectories, backlogs will soon be eliminated. One area where Ethiopia's otherwise steadily impressive reform process has had no impact (and very little progress) is strengthening the institutional frameworks in which the Auditor General can operate (at both Federal and SN level). Parliamentarians at both Federal and Regional levels, in particular, do not seem to fully understand audit processes, and are partially responsible for regional audit offices being in the main hugely under-resourced.

	Dimension	Evidence of Capture (what is captured?)	Quality of Capture (How well? How useful?)	Explanations (Why? Why not?)
B7	On report	Information about aid flows is produced by the Multilateral and Bilateral Aid Departments in MoFED. These are not usually available in the public domain. Information about the budget – which includes most aid flows – is available in the *Federal Negarit Gazeta*, the official Government paper. However, there is no public access to the in-year budget execution reports. But the MOFED website provides quarterly information on in-year budget execution. This has been enhanced through the PBS programme. The year-end financial statements prepared by MoFED are not available in the public domain, and final accounts with audit reports from the OFAG, whilst theoretically accessible and available to the public, remain, in practice, in limited circulation. Some additional information is available to donors. Both the Education and Health Sector Development programmes produce periodic reports (which will reflect all disbursement from donors regardless of channels). Specific reporting is also available for the PSCAP programme and for the PNSP (safety net). The PBS programme also produces information on basic service spending, although this (particularly through the continuous audit process) seems to be for the benefit of donors.	There have been long-running issues about the discrepancies between government figures (produced in the Gazette, etc) and those of the international community. Quality of capture could be improved if the Aid Management Platform were able to function properly, allowing each donor is able to input commitment and disbursement data directly. This information can be used by MoFED at commitment for planning purposes, can be triangulated when funds are disbursed. But the real advantage of the system is that it is a transparent portal which effectively calls donors to account, and which can produce information in the public domain, by MoFED.	One of the issues regarding the availability of information is that, as the PEFA review has noted, there is not a developed culture in Ethiopia of sharing and disseminating information. However, as part of ongoing moves towards fuller democratisation, this is one issue that is being addressed. (The PEFA review noted, for instance, that for the first time budget information is now being pinned up in public places in weredas.) Whilst not in itself a panacea (rather a mechanism needed because of certain aspects of donor behaviour!), an Aid Management Platform working at full potential will increase accessibility of aid on budget information.

C. Reflections

72. Ethiopia has done much over recent years to reform its PFM framework. This has been a considerable challenge, particularly in the light of the nature of extensive decentralisation in an already federal state. Improvements in core systems at sub-national level have been particularly marked over the last four years or so, which has done much to allay some donor doubts about the risks that might be attributable to disbursing development aid through government systems. However, there is much still to be done; some aspects of parliamentary oversight and audit are not yet of an acceptable standard, but reform to rectify these will take some time to have a tangible impact.

73. Ethiopia has also done much to fulfil its commitments under the Paris Declaration, and seems to genuinely want aid to be disbursed through core systems and to be on budget across the dimensions. The plethora of planning and budgeting systems (as a result of federalism and decentralisation) does not make this an easy task, however. It is difficult to see what can be done on GoE's side to get more development 'on plan' given the political intricacies of the country's governance structures.

74. However, there is increasing willingness on the part of Government to have some dialogue on some of the factors that are at the core of these structures. Discussions around the subsidy formulae are a case in point. At the same time, however, the suspension of budget support has meant that a certain type of high level dialogue about governance and macroeconomic issues is no longer on the agenda, even if, when it was, it was of limited depth and quality.

75. Questions remain about some donor behaviour. Disbursements against commitment have not been particularly encouraging over the last few years, although the hiatus that followed the elections of 2005 is partially responsible for this. The Government of Ethiopia is equally frustrated by the inability of some donors to give information in a timely fashion to feed into the budget cycle, and to commit to support in a more medium-term focused framework.

76. Whilst trends seem to be moving towards support which is more 'on budget' (e.g. with $1 billion being disbursed through the PBS instrument by the end of EFY 2000) – particularly with the move to Component 1 of the Protecting Basic Services instrument, there are still some significant donors (e.g. the USA) who continue to use Channel 3 funding, and Project Implementation Units (which the Government of Ethiopia wishes to disband over the medium term). This is probably due to issues relating to politics, perceptions of fiduciary risk and perceived systemic issues. And whilst PBS is in many ways an inventive instrument (allowing countries to disburse something that looks very like sub-national budget support when domestic accountabilities often rule out DBS) it is still an instrument which is less aligned than DBS, and, in its components 2-4, uses channels other than channel 1. Some have argued that some of the initiatives central to PBS – proving additionality and demonstrating enhanced accountability – are actually all about building stronger accountability of Government to donors, and providing the information needed to 'tell the story' to political masters back home.

77. In one sense the AMP could be seem as an example of good practice. It is certainly an interesting case, but two observations need to be borne in mind. Firstly the AMP is not, as yet,

being used to its full potential, either in terms of a transparent portal or in terms of a genuine interface with core GoE systems. Secondly, the system itself is inherently a second-best solution. Reporting aid that bypasses several dimensions of the country system is not a substitute for the actual use of the country budget system. The system itself is not a necessary condition for donors to keep communications challenges open, honour commitments and use methods of disbursement which, as far as possible, put development aid on budget across the seven dimensions. Nor is it needed before Government can share information (on account and on report) about donor assistance in a transparent way.

Annexes

Annex 1

Extract from 2007 PEFA Review – Federal Government (Draft)

PI-5: Classification of the budget. A robust classification system allows the tracking of satisfactory spending.

The budget formulation and execution is based on economic and sub-functional classifications[12]. The economic classification uses GFS standards. There are currently twenty (20) sub-functions[13], which are distributed among four (4) functions of expenditures: Administration and General, Economic, Social, and Other[14].

PI-6: Budget documentation In order for the legislature to carry out its function of scrutiny and approval, the budget documentation should allow a complete overview of fiscal forecasts, budget proposals and results of past fiscal years.

The annual budget documentation[15] as submitted to Parliament (budget estimates) includes:

- Macro-economic assumptions including estimates of aggregates growth, inflation and exchange rate as prepared in the MEFF[16];
- Fiscal deficit, defined according to GFS standard[17];
- Deficit financing and composition[18];
- Current year's budget (estimated outturn) in the same format as the budget proposal[19];
- Explanation of budget implications of new policy initiatives with estimates of budgetary impact[20].

PI-7: Coverage of Government operations Fiscal information such as the budget, execution reports and financial statements should include all budgetary and extra-budgetary activities in order to allow a complete overview of revenues, expenditures and public financing.

Budgets of public enterprises (PE) activities are not included in the Federal budget[21]. In addition there are several funds, which operate in a more autonomous fashion than the PE without any scrutiny from the Federal Government. Budgets of the funds are also not included in the Federal budget either. A list of the Funds is presented in following table:

TABLE 8: EXTRA-BUDGETARY FUNDS AND YEARLY EXPENDITURE EFY 1995-1996-1997 (2002/03-2003/04-2004/05)

(In million of ETB)

FUNDS	EFY 1995 (2002/03	EFY 1996 (2003/04)	EFY 1997 (2004/05)
Road Fund	300,00	350,00	350,00

[12] Communication of the Macroeconomic Department, the Budget Consolidation Department and the Central Accounts Department The latter has provided audited data on the budget for EFY 1995, 1996 & 1997
[13] For a detailed view of sub-functions, please refer to Annex 3, Tables 1, 2 & 3 (budget data used for the calculation of PI-1 and PI-2)
[14] Budget Reform Design Manual (2000), page 20
[15] The Budget documentation has 3 Volumes, of which only Volume III is available in English.
[16] This information is included in Volume I (only available in Amharic) of the budget documentation (Communication of Budget Consolidation Department)
[17] *Idem*
[18] *Idem*
[19] *Idem*
[20] *Idem*
[21] Refer to *2.2 d*

Pension & Social Security Funds	610,00	643,00	601,00
Fuel Price Stabilization Funds	9,75	17,00	17,06
Disaster Prevention & Preparedness Fund	1196,48	1206,16	1331,00
Ethiopian Social Rehabilitation & Development Fund	216,60	330,78	310,01
Industrial Development Fund (IDF)	268,00	66,00	162,00
I. TOTAL FUNDS EXPENDITURE	2600,83	2612,94	2771,25
II. TOTAL FEDERAL GOVERNMENT EXPENDITURE	16382,00	19978,00	22967,00
III. FUNDS EXPENDITURE AS A % OF TOTAL EXPENDITURE (=I/II)	**15,87%**	**13,08%**	**12,06%**

Source: Macroeconomic Policy and Management Department of MOFED

As can be seen from above table 7, Funds expenditure as a percentage of total Federal Government expenditures went down from almost 16% to 12% in the period 2002/03-2004/05. Despite this performance, Funds expenditures remain still relatively high;

There are three (3) channels for the distribution of ODA to the Federal Democratic Republic of Ethiopia. The first (1) channel is (was) for budget support (BS), for the Protection of Basic Services (PBS), the Public Sector Capacity Building Program (PSCAP), etc. Funds for these activities go directly to the Federal budget. The reporting for these activities that are therefore reflected in the Federal budget is complete[22]. For Channel 2 distribution of ODA, there are different funding modalities to Channel 1. The funds go directly to the implementing agencies through the budget. Reporting for these funds is 80% complete. Channel 3 funds go directly to the beneficiaries. There are not reported or underreported. They are in grant form only whereas funds from Channels 1 and 2 are loans and grants[23].

Overall income/expenditure information for all loan-financed projects is included in fiscal reports[24].

Comprehensiveness & Transparency	**Scoring**	**D (i)**	**D (ii)**	**D (iii)**
5. Classification of the budget	**A**	**--**	**--**	**--**
6. Comprehensiveness of information included in budget documentation	**B**	**--**	**--**	**--**
7. Extent of unreported government operations	**D+**	D	C	--

PI-26 External Audit The use of public funds can be transparent and effective only with a high quality external audit. In the Federal Democratic Republic of Ethiopia the *Constitution* of 1994 gives power to the Federal Auditor General to audit and inspect the financial accounts of ministries and other entities at the Federal level and to report its findings and recommendations to the House of Peoples' Representatives[25]. The Office of the Federal Auditor General (OFAG) has been established by law[26]. The OFAG is a member of the International Organization of Supreme Audit Institutions (INTOSAI).

(i) Entities of the Federal Government audited annually by OFAG represent at least 50% of total expenditures (although this, to some extent, is qualified by the extent of audit of funds expended at SN level[27]). Audits performed generally adhere to INTOSAI auditing standards and focus on significant issues[28];

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[22] Communication of the Central Accounts Departments of MOFED
[23] *Idem*
[24] *Idem*
[25] Art. 101-2
[26] Proclamation No. 68/1997
[27] (Communication of OFAG) There is one issue that has recently dominated discussions relating to the scope of the Auditor General's work, however. The Auditor General will audit actual sums disbursed to SN entities through the block grant system but will not pursue the flow of monies down through the system to the point of service delivery. Some interpret the legal framework as giving the Auditor General these powers [Clause 7(2) of the *Office of the Federal Auditor General Establishment Proclamation* (Proclamation 68/1997) states that the OFAF shall "...audit or caused to be audited account involving budgetary subsidies and any special grants extended by the Federal Government to Regional Governments']. Others argue that this is the job of the Regional Auditors General. But these offices are effectively separate

(ii) OFAG's audit of the final accounts is dependent upon MOFED transmitting the appropriate documentation. The current legislation establishes that MOFED should close the final accounts and send them to OFAG within six months after the end of the EFY.[29] OFAG has four months to audit the accounts[30]. There have, in passed years, been significant backlogs. There is currently less than one-year lag in auditing the Federal Government accounts[31];

(iii) The OFAG will give an opinion on the accounts, accompanied by a report which highlights material or noteworthy issues and which makes recommendations relating to improving the standard of public financial management in budgetary institutions. The Public Accounts Committee (PAC) of the House of Peoples' Representatives reviews the audited and accompanying report in open session. Such sessions are widely reported in the media. The PAC, working through the OFAG, to a limited degree, sometimes follows up recommendations at a later date.

PI-27 Legislative approval of the budget

(i) The draft recommended budget is the budget that MOFED prepares and submits to the Council of Ministers, who in turn reviews it and recommends it to the Federal Parliament (House of Peoples' Representatives). The recommended budget, which is reviewed by the legislature includes recurrent and capital expenditures, subsidies to regional governments and administrative councils, and an estimate of resources available to finance the budget[32];

(ii) The *Constitution* of 1994 provides the Federal Parliament with the authority to establish standing and ad-hoc committees to carry out its various reviews[33]. The *Budget and Finance Standing Committee* carries out a review. There is no evidence of existing written procedures for the review;

(iii) The recommended budget must be submitted to the House of Peoples' Representatives no later than June 7[34]. The Council of Peoples' Representatives is required to vote on the annual appropriations for the approved budget no later than July 7[35]. The legislature has about one month to review the recommended budget;

(iv) Supplementary budgets (or in-year budget amendment) can be authorized by the Council of Peoples' Representatives on the recommendation of the Council of Ministers[36]. The rules that allow such amendments are rudimentary[37].

PI-28 Legislative scrutiny of audit reports Once the budget is approved, the legislature has a key role in exercising scrutiny over it.

(i) In the Federal Democratic Republic of Ethiopia examination of the audit reports is carried out by the Public Accounts Committee (PAC)[38]. The PAC ensures accountability. It is now headed a

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institutions not under the control of Federal Auditor General. Taking this argument to its conclusion, it could be argued that the bulk of government expenditure relating to the provision of primary services thus falls to the Regional Auditors General. But the Regional PEFA review has shown that audit coverage by these institutions does not cover 50% in terms of direct external audits of *woreda* jurisdictions, meaning that overall coverage of external audit could be interpreted as being significantly lower than initial scrutiny suggests.

[28] Performance audits are carried out (Source: *Idem*)

[29] MOFED *Directive* No. 20, 2005

[30] *Idem*

[31] For EFY 1997 (2004/05), OFAG have already finalized the audits and the audited accounts have already been sent to the House of People's Representatives. The CAD of MOFED is currently finalizing the EFY 1998 (2005/06) financial statements. They will be sent to OFAG around the end of April 2007 (Communication of CAD).

[32] Revised Budget Manual, Final Draft, January 2007, page 46

[33] Art. 55-19

[34] Revised Budget Manual, Final Draft, January 2007, page 45.

[35] *Federal Government of Ethiopia Financial Administration Proclamation* No. 57/1996,Part IV, Art.16

[36] *Federal Government of Ethiopia Financial Administration Proclamation* No. 57/1996, Part IV, Art.21 & *Council of Ministers Financial Regulations* No. 17/1997, Part V, Art. 19

[37] *Idem*

[38] Communication of OFAG

member of an opposition party[39]. The PAC carries out its review within two months from receipts of the reports[40];

(ii) In-depth hearings are conducted by the legislature. They are not systematic due to limited capacity covering partially the audited entities[41];

(iii) The PAC looks at recommendations but in practice they are not acted upon by the executive.

Conclusion *An effective examination by external audit and by the legislature makes it easier for the Government to be accountable for the content and implementation of fiscal and expenditure policies.*

External Scrutiny and Audit	**Scoring**	**D (i)**	**D (ii)**	**D (iii)**	**D (iv)**
26. Scope, nature and follow-up of external audit.	**C+**	C	A	B	--
27. Legislative scrutiny of the annual budget law	**D+**	C	D	C	D
28. Legislative scrutiny of external audit report	**C+**	A	C	C	--

Audits performed by the Office of the Federal Auditor General (OFAG) represent at least 50% of total expenditures. These audits generally adhere to INTOSAI auditing standards and focus on significant issues. There is currently less than one-year lag in auditing the Federal Government accounts and this delay has been significantly reduced in the last five years. This delay is due to late submission of the financial statements to the OFAG. The OFAG forwards the audited accounts on time to the House of Peoples' Representatives and are reviewed by the Public Accounts Committee (PAC). There is follow up by the legislature (i.e. the PAC) through the OFAG but it is limited.

The *Budget and Finance Standing Committee* carries out a review of the recommended budget. There is no evidence of existing written procedures for the review. Overall the legislature has about one month to review the recommended budget. Supplementary budgets (or in-year budget amendment) can be authorized by the Council of Peoples' Representatives on the recommendation of the Council of Ministers. The rules that allow such amendments are rudimentary.

The examination of the audit reports is carried out by the Public Accounts Committee (PAC) that is now headed by a member of an opposition party. The PAC carries out its review within two months from receipt of the reports. As a result in-depth hearings are conducted by the legislature but these are not as systematic as they could be, due to limitations of both time and capacity. The PAC will look at recommendations but in practice the executive does not act them upon.

D-1 Predictability of Direct Budget Support

Donors have, over the EFYs 1996-1998, provided direct budget support both in terms of general budget support and in terms of specific instruments in support of government sectors or programmes channelled through the treasury.

As well as straightforward Direct Budget Support (DBS), donors have disbursed funds into the treasury for the Public Sector Capacity Building Programme (PSCAP), the Productive Safety Net Programme (PSNP), Food Security (FS) and Protecting Basic Services. This study only treats PBS and being, per PEFA's definition, direct budget support assistance, as other instruments, although channelled through the treasury, do not use procedures in accordance with all other government revenue, particularly in respect of procurement[42].

[39] *Idem*
[40] *Idem*
[41] *Idem*
[42] In fact some PSD funds, particularly in respect of Component 2 which is aimed at scaling up GoE's response to the Health MDGs also use different procurement rules, but it has proved too complex to identify these elements, and the review has adopted GoE's approach, that in all important respects PBS resembles DBS

A complicating factor has been that after political unrest that followed the elections of 2005 many donors suspended support, and in particular general budget support. Following on from this, donors began channelling support into the Protecting Basic Services programme, in essence an instrument devised to support the provision of services at decentralised (and in particular, wereda) level.

Table 8 below shows commitments and disbursements for direct budget support and PBS from the donors – both multilateral and bilateral - concerned.

Table 8: DBS/PBS disbursement[43]

Donor	EFY 1996 $m (unless stated)			EFY 1997 $m (unless stated)			EFY 1998 $m (unless stated)			Comments
	Commit.	Dis.	%	Commit.	Dis.	%	Commit.	Dis.	%	
World Bank (IDA PRSC III)	120	123.32	103	130	137.48	106	215	91	42	Support transferred from PRSC to PBS in '98 due to election difficulties
EU (PRBS)	95 million Euro				45 million Euro			18 million Euro		Overall, some 31.93 million euro has been cancelled due to election difficulties (and only 66% of original pledge disbursed). EU now supporting PBS
UK	34.70	34.70	100	57.90	57.90	100	63.14	63.14	100	Although the UK switched support from DBS to PBS, overall resource envelope was maintained.
Sweden				13.8	13.8	100	13.8	0	0	Support suspended
Canada				20.55	20.55	100	20.55	0	0	Support suspended – has now switched to PBS
Germany				4.89	0	0	14.38	4.89	38	

Whilst donor performance of disbursing what was committed is good in EFYs 1996 and 1997 there is a very noticeable dip in 1998. The reasons for these are due to extraordinary and exogenous shocks – the issues around the election and the inability of donors to disburse budget support, taking into account their domestic accountabilities. Nevertheless, within the scoring framework this shows an annual deviation of actual support forecast against disbursement at over 15% for one of the years under analysis. Dimension i. is therefore scored at C.

In terms of timeliness, where there were no interruptions in support (as described above) disbursement of DBS/PBS was generally according to plan (with some minor exceptions – e.g. German support, which shows disbursement made in the year following commitment). However, the disruptions of 1998 threw disbursement against commitment out of kilter, and this dimension is again scored at C (delays have not exceeded 50% in the last two of three years).

D-2 Financial Information provided by donors for budgeting and reporting on project and program aid

Donor provision of information in a timely manner to Government has proved to be a bit problematic, particularly in the case of bilateral donors and does not always accord with the Government of Ethiopia Financial Calendar.

[43] Source: MoFED figures

The Medium Term Economic Fiscal Framework (MEFF) is finalised in draft before January of each year, and is used as a basis of the annual budget, which is finally tabled by Federal Government to the House of Peoples' Representatives in May. Unfortunately this is often based on figures of donor support that are estimates rather than firm. Donors do not, under current arrangements, usually supply indicative figures of support until January (e.g. six months before the start of the financial year, but even under this arrangement many donors are late in providing information. The Government has attempted to change this, inter alia by seeking agreement at the Development Assistance Group (the DAG) that information should be supplied in September preceding the start of the financial year in July, and by raising the issue at the High Level Forum (the forum where high-level dialogue takes place between DAG members and government). However, DAG members feel that the proposed change is not one that can be accepted, as it is too early in the budget calendars of many donors to give firm commitments this early[44]. Dimension i. scored at C – at least half donors provide complete budget estimates at least three months prior to the start of the fiscal year.

Information on in-year flows from multilaterals is reported by government to be good, with information well in advance of the financial year and good quarterly information supplied.

However, information from bilaterals is often patchy, incomplete and, in some cases severely delayed, although the bigger donors reportedly provide quarterly reports or quarterly data on disbursements made for the externally financed projects and this information is available immediately at the end of the quarter.

All in all there appears to be scope for better donor-government coordination and cooperation here. One possible improvement to the current state of affairs might be the continued rollout of the Aid Management Platform, a real-time database, which will allow donors to input their commitments directly into the system, and allow consolidated information to be viewed in the public domain. However, rollout of this system is still being undertaken.

The second dimension for this indicator is scored at C – at least 50% of externally financed project estimates are received within two months of end of quarter.

D-3 Proportion of aid that is managed by use of national procedures

Much of the aid received by Ethiopia can now be said to be 'on budget'. Grant disbursement figures from bilateral donors show a total, over the three-year period (EFYs 1996-1998) of around $1,084 million[45].

A significant proportion of this is bilateral contribution to the untied, budget support type modalities (PSNP, PSCAP, etc), indicating that tradition project support, with parallel systems, are dwindling in favour of instruments which use government systems, with one important caveat. Whilst PSNP, PSCAP and other modalities use government payment and accounting systems, are subject to government audit and are reported through government reporting systems, they do not use government procurement systems, reflecting, in part, issues around procurement (see PI-19). We have not been able to disaggregate the data to allow proper scoring of this PI, but it is evident that there is room for improvement in terms of donor resources using government procedures.

Donor Practices	**Scoring**	**D (i)**	**D (ii)**
D-1 **Predictability** of Direct Budget Support	**C**	C	C
D-2 **Financial** Information provided by donors for budgeting an reporting on project and program aid	**C**	C	C
D-3 Proportion of aid that is managed by use of national procedures	**Unable to score**		

[44] Letter of DAG to State Minister of Finance and Economic Development dated 14 May 2007
[45] Source: MoFED

Annex 2

Extract from 2007 PEFA Review – Seven Regions (Draft)

Indicator 5: Classification of the budget

The budget classification in the seven regions assessed is largely consistent with the Government Financial Statistics (GFS) 1986 classification and can provide information by economic, administrative and functional classifications. Revenue and expenditure data generally accord with GFS international standards. There is a limited application of functional classification at the budget preparation stage, where the focus is on economic and administrative classifications.

Budget classification in regions has improved through TA provided by the DSA project under the auspices of the Expenditure Management and Control Programme (EMCP) that has also introduced the Chart of Accounts. The classification system is used in each of the seven regions covered in this report and allows BoFEDs and WoFEDs to rationalise expenditure into a single series. Sample data from weredas visited confirmed that the classification reforms are imbedded and followed and this has in turn facilitated reporting from WoFEDs to zones and/or BoFEDs in Regions and from BoFEDs to the federal level.

Indicator	Brief Explanation	Rating
5. Classification of the budget	Budgets for all seven regions covered include administrative, economic, and functional classification of expenditures.	A

Indicator 6: Comprehensiveness of information included in the budget

The information included in budget documentation (the annual budget and budget supporting documents) has improved in recent years but does not yet provide comprehensive information on public revenues and expenditures. According to the PEFA Guidelines, the annual budget documentation should include information on 9 elements as follows where each statement applies for the seven regions as the entire sample:

1. Information regarding macroeconomic assumptions. This is not relevant for regions, although reference to regional GDP may be valid in the context of IP3.
2. Information on the fiscal deficit, defined according to GFS standard. This is provided where exceptionally the case.
3. Information on deficit financing is included. There are occasional deficits.
4. Information on debt stock is not relevant, as regions do not have a mandate for debt issuance.
5. Information on the Government's financial assets is not included for any region.
6. Information on prior year budget outturn is presented in the same format as the budget proposal for all 6 regions.
7. Information on current year is presented in the same format as the budget proposal for the coming year for all six regions
8. Summarised budget data, including revenue and expenditure data, for the main budget entities is included for the current and previous year for all regions.
9. Information on the implications of new policy initiatives is not included and there are no explanatory memoranda and analytical tables to provide additional information to the annual budget proposal.

Indicator	Brief Explanation	Rating
6. Comprehensiveness of information included in budget documentation	The FY1999 budget documentation satisfies 5 of the 7 requirements relevant for regional review listed by PEFA	A for all regions

Indicator 7: Extent of unreported government operations

The comprehensiveness of budget information at the regional level has continued to improve, in part due to donor-financed DSA project under the EMCP. In general, the regional and wereda accounts capture all government operations with the exception of donor financed budgetary transfers slated for SN level that bypass the wereda and regional budgets and miscellaneous wereda-specific transfers such as those related to health and sanitation. There is no evidence of offsets at the regional level or special means (such as fees charged or revenue collected on budget but outside the budget process).

Overall, the extent of unreported government operations is less than 1-5% but there is lack of comprehensiveness of donor funded income and expenditure data in the regional and wereda reports.

Indicator	Brief Explanation	Rating
7. Extent of unreported government operations including those funded by donors.	The comprehensiveness of fiscal information has improved in recent years for all regions although it needs to improve further in Benishengal and Gambella. The extent of unreported government operations is estimated to be in less than 5% of total expenditure. Unable to score due to lack of overall information.	Harar C, All others B

Indicator 26: Scope, nature and follow up of external audit

External audit in the regions is undertaken by Regional Auditors General and their offices (ORAGs) that are established under regional proclamations. In some cases (in particular Dire Dawa) the work of the Regional Auditor General is augmented by that of the Federal Auditor General (who has a number of regional offices). The extent to which the Federal Auditor General has the mandate to track funding flows right down to wereda level has been a point of fierce debate recently. The Federal Auditor General has argued that his constitutional powers allow funds to be tracked and monitored to the point of final expenditure, but Federal Government has contested this.

Nevertheless the relationship between the Office of the Federal Auditor General and the Regional Auditors General is close; fora exist for AGs to swap information and problem share, underpinned by mentoring support given from OFAG.

However, there are significant problems with scope. In each of the regions visited coverage of an annual audit by the ORAG is less than 50% of accounting entities and actual expenditure, both in terms of audits of sector bureaux, other agencies at regional level, and (more acutely) individual weredas, who are often not visited for three or more years. This is a reflection of the logistical and resource challenges associated with such extensive fiscal decentralisation. ORAGs are not resourced sufficiently to perform their mandate. (First dimension - D for all regions).

Annual reports of ORAGs are nevertheless submitted to the legislature within eight months of the end of the fiscal year (Second dimension – B for all regions).

There is a mixed picture relating to the follow up of recommendations contained in the reports of ORAGs. In Tigray and Oromiya (which have both introduced a Public Accounts Committee) there was clear follow up, driven by parliamentary scrutiny. There are systems in place to ensure that remedial action is taken and tracked. In other regions this was less clear, and AGs reported that sometimes action was taken, but at other times it was not, and their own powers to pursue these matters were limited (Third dimension – A for Tigray and Oromiya, and C for remaining regions).

Indicator	Brief Explanation	Rating
Indicator 26 Scope, nature and follow up of external audit	Regional audit is severely hampered by its limited scope, although annual audit reports are made and submitted to the legislatures, which are followed up to varying degrees.	All regions D+

Indicator 27: Legislative scrutiny of the annual budget law

Regional legislatures and wereda councils review annual budget laws. The extent of the review potentially covers all areas, including the fiscal frameworks at regional level, as well as the detail of the budget. There is an issue relating to the capacity of legislatures to take detailed reviews, beyond the scrutiny of income and expenditure budget lines forward, but within these parameters scrutiny is comprehensive. (First dimension A **for all regions**).

Across all regions the right of members of the legislature to review the draft budget is well respected, and is indeed a feature of the budget cycle in all regions reviewed (Dimension 2 – A for all regions).

However, the time allowed for debate of the budget was clearly insufficient (often just a day or so). Regional parliaments do not spend more than a few days reviewing the budget. At wereda level even less time is given to this activity. (Third dimension D across all regions).

With regard to in-year amendments of the budget, these are clearly regulated in sub-federal proclamations and regulations. Where amendment needs legislative approval this will be sought. Often budget revision sessions occur at the mid-point of the fiscal year. (Forth Dimension A across all regions).

Indicator	Brief Explanation	Rating
27. Legislative scrutiny of the annual budget law	Scrutiny occurs but is perhaps limited by capacity. Nevertheless, oversight and scrutiny are established in budget cycles and clear rules exist relating to budget amendments, although the amount of time elected members have to scrutinise the budget is severely limited.	D+

Indicator 28: Legislative scrutiny of external audit reports

External audit reports are scrutinised in a timely way in all regions examined except for Dire Dawa (where the ORAG actually reports to the executive). (First dimension A across all regions except Dire Dawa, which couldn't be scored). However, such scrutiny is often constrained by the Regional Councils' understanding of the nature of external audit and its own role in the process.

The extent to which there are formal hearings or parliamentary committees varies across regions. In Tigray and Oromiya hearings take place and appear to be effective, but in other regions the establishment of such mechanisms is either work-in-progress or occasional and ad hoc (Second dimension A for Tigray and Oromiya, C of all others).

The extent to which recommendations are issued and follow up also varies. In Tigray and Oromiya recommendations are both issued and robustly followed up, but in other regions it is not always clear whether councils have issued recommendations; in many cases councils do not follow up recommendations. (Dimension three – A for Tigray and Oromiya, C for all other regions.

Indicator	Brief Explanation	Rating
28. Legislative scrutiny of external audit reports.	Reports are issued in all regions, but the extent and institutionalisation of parliamentary review and follow-up is mixed.	Dire Dawa not scored (cannot score dimension 1) A (Tigray and Oromiya) C+ all other regions

Annex 3: OECD/DAC baseline survey results

The results of the 2007 OECD/DAC survey are as follows.

Areas of Harmonization	2005 Baseline[1]	Targets 2012
1. Ownership–Operational poverty reduction strategy	C	B or A
2.a. Quality of public financial systems	3.5	4.0
2.b. Quality Procurement systems	Not available	Not applicable
3. Aid reported on budget.	74%	87%
4. Coordinated capacity development	27%	50%
5.a.i. Use of country PFM systems (aid flows)	45%	63%
5.a.ii. Use of country PFM systems (donors)	88% of donors	90% of donors
5.b.i. Use of country procurement systems (aid flows)	43%	Not applicable
5.b.ii. Use of country procurement systems (donors)	82% of donors	Not applicable
6. Parallel project implementation units	103	34
7. In-year predictability	96%	98%
8. Untied aid	39%	More than 39%
9. Use of programme-based approaches	53%	66%
10.a. Coordinated missions	27%	40%
10.b. Coordinated country analytic work	50%	60%
11. Sound performance assessment framework	C	B or A
12. Reviews of mutual accountability	No	Yes
For reference: alternative measures for indicators3 and 7 (based on gap rather than ratio)		
3. Aid reported on budget	32%	16%
7. In-year predictability	31%	15%

Source: OECD/DAC Ethiopia Baseline Report, 2007.

The report contains a number of interesting observations.

Regarding ownership, it noted that some progress was still needed to ensure that there were appropriate links between 5 year plans (which are actually made right down to wereda level) and the PRSP, the PASDEP. It named Ethiopia's complex system of planning as a challenge.

But the significant progress made in PFM reform was noted.
Government Sector Aid recorded in the budget for 2005 was estimated at 74%; the report notes that is a relatively small figure given the high level of alignment of aid, and the challenge this presents was to develop modalities that strengthen the accountability of he budget process as well as meet the concerns of donors.

Coordination of technical assistance with country programmes was relatively light (at 27%), indicative of the fact that donors are not aligning well with GoE strategies when it comes to TA.

The study also notes that only 45% of aid flows through government systems, which is disappointing given the improvements in PFM systems.

Parallel implementation systems are numerous (at 103 – 62 provided by the USA) and the report notes that '… a significant proportion of aid (especially bilateral aid) to Ethiopia continues to be provided via parallel PIUs', although it also notes that some of these are well-integrated, and underpinned by agreements with government.

Discrepancies in the amount of aid disbursed per donor records to aid disbursed per Government's records were noted. Regarding predictability of aid disbursed against commitment, the picture was massively varied across donors.

What was encouraging was the finding that 50% of all aid in 2005 was delivered though programme-based approaches. However, as up to 53 of this aid was budget support, which was subsequently suspended in 2006, this picture is now almost certainly less encouraging , especially as the report also notes that the PBS instrument (which has largely replaced DBS) is less well aligned.