

Mokoro Ltd

Putting Aid on Budget

**A Study for
the Collaborative Africa Budget Reform Initiative (CABRI)
and
the Strategic Partnership with Africa (SPA)**

LITERATURE REVIEW

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Aid on Budget Literature Review

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Acronyms and Abbreviations

AAP	Assessment and Action Plan (HIPC)
AfDB	African Development Bank
AIMS	Aid Information Management System
AOB	Aid On Budget
AsDB	Asian Development Bank
CABRI	Collaborative Africa Budget Reform Initiative
CFAA	Country Financial Accountability Assessment
CPAR	Country Procurement Assessment Review
CPIA	Country Policy and Institutional Assessment
DAC	Development Assistance Committee (of OECD)
DFID	Department for International Development (UK)
EC	European Commission
ED	Exposure Draft (IPSAS)
H&A	Harmonisation and Alignment
HIPC	Heavily Indebted Poor Countries
IDB	Inter-American Development Bank
IFAC	International Federation of Accountants
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
IPSASB	International Public Sector Accounting Standards Board
JICA	Japan International Cooperation Agency
MCC	Millennium Challenge Corporation
MDGs	Millennium Development Goals
MOPAN	Multilateral Organisation Performance Assessment Network
NGO	Non-Governmental Organisation
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PBA	Programme-based Approaches
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
SECO	Swiss State Secretariat for Economic Affairs
Sida	Swedish International Development Cooperation Agency
SPA	Strategic Partnership with Africa
TOR	Terms of Reference
UNDG	United Nations Development Group
UNDP	United Nations Development Programme

INTRODUCTION

Terms of Reference

1. Mokoro Limited has been commissioned by DFID on behalf of CABRI (the Collaborative Africa Budget Reform Initiative) and SPA (the Strategic Partnership with Africa) to undertake a consultancy on “Putting Aid on Budget”. The aim of the consultancy is “to produce outputs which will better equip governments in Sub-Saharan Africa to lead country-level processes to ensure external development assistance (aid) flows are properly reflected in national budget documents, ex ante (budget presented to legislature) and ex post (out-turn accounts)”. (Aid on Budget Study Inception Report, Mokoro Ltd, 2007)
2. The TOR for the consultancy require a literature review of existing good practice, a study of country practices in at least ten African countries, a more in-depth investigation of what works and what does not in some of the case study countries, and the preparation of a Synthesis Report and a Good Practice Note based on the research results.
3. The Japan International Cooperation Agency (JICA) has funded an expanded Literature Review to strengthen the evidence base for the study, which will cover existing good practice documents and existing aid agency policies in more depth, and scan additional countries for evidence of lessons learned about putting aid on budget. Box 1 provides the detail from the Terms of Reference (TOR).

Box 1: TOR for the Aid on Budget Literature Review

- (a) Document existing good practice guidance that is relevant to the incorporation of aid in recipient country budgets (e.g. any direct or indirect references in OECD DAC guidelines, IMF recommendations, treatment in the PEFA analytical framework, guidelines under development by the International Federation of Accountants (IFAC) etc.).
- (b) Review the applicable policies and guidelines of the major multilateral and bilateral agencies as these affect the incorporation of their aid into government budgets.
- (c) Seek and document relevant experiences of efforts to capture aid in government budgets. This will focus mainly on countries that are not case-studies for the main Aid on Budget consultancy, including countries from outside Africa. It is expected that relevant material will mainly be found in the documentation of harmonisation and aid coordination efforts at country level.

Literature Review Structure

4. The main body of the literature review is organised as follows:
 - Section A* looks at the international good practice guidance for putting aid on budget and documents the literature on: sound budgeting and financial management and the implications for aid management; the aid effectiveness consensus and the good practice principles for putting aid on budget; and, how aid on budget is monitored.
 - Section B* provides illustration of different donor¹ approaches to putting aid on budget. The bilateral agencies covered are: Canada, Denmark, France, Ireland, Japan, the Netherlands, Norway, Sweden, the United Kingdom and the United States and the multilateral organisations. The multilateral organisations covered are: the African Development Bank, the Asian Development Bank and the Inter-American Development Bank, the World Bank, the International Monetary Fund, the European Commission and the UN.
 - Section C* covers a selection of countries’ relevant experiences of efforts to capture aid in government budgets. The countries covered are: Bangladesh, Bolivia, Botswana, Nicaragua, Senegal and Vietnam. These are additional countries to the case study countries covered in the main Aid on Budget study (Burkina Faso, Ethiopia, Ghana, Kenya, Mali, Mozambique, Rwanda, South Africa, Tanzania and Uganda).

¹ For readability, “donors” will be used to refer to bilateral donors and international organisations providing development financing, concessional and non-concessional.

5. The full bibliography of the review is provided.
6. The annexes provide detailed information on:
 - Annex A Paris Declaration 2006 Monitoring Survey
 - Annex B Public Expenditure and Financial Accountability assessments
 - Annex C Aid on budget profiles of the donors covered in this review
 - Annex D Aid on budget profiles of the countries covered in this review.

Definition of “on budget”

7. The Aid on Budget study Inception Report notes that the definition of ‘on budget’ is ambiguous, and that there are also a number of related terms with often a lack of clarity over definitions and usage. These terms are linked to the capture of aid at different phases of the budget cycle. Box 2 shows the terms and definitions of them used in this study. (Mokoro Ltd, 2007: 4)

Box 2: Dimensions of aid ‘on budget’

Term	Definition
On plan	Programme and project aid spending integrated into spending agencies' strategic planning and supporting documentation for policy intentions behind the budget submissions.
On budget ²	External financing, including programme and project financing, and its intended use reported in the budget documentation.
On parliament (or "through budget")	External financing included in the revenue and appropriations approved by parliament.
On treasury	External financing disbursed into the main revenue funds of government and managed through government's systems.
On accounting	External financing recorded and accounted for in government's accounting system, in line with government's classification system.
On audit	External financing audited by government's auditing system.
On report	External financing included in ex post reports by government.

Source: Mokoro Ltd, 2007.

² It should be clear from the context if "on budget" is meant in a more general sense than this precise definition.

SECTION A: GOOD PRACTICE GUIDANCE RELEVANT TO “AID ON BUDGET”

Consensus on sound budgeting and financial management systems

Existing good practice principles

8. Putting aid on budget was identified as an element of good practice in public financial management (PFM) in the 1990s in seminal texts such as Allen Schick’s *A Contemporary Approach to Public Expenditure Management* (Schick, 1998),³ the World Bank’s *Public Expenditure Management Handbook* (World Bank, 1998) and the International Monetary Fund (IMF) *Code of Good Practices on Fiscal Transparency* (International Monetary Fund, 1998). Almost a decade later the analysis and conclusions presented in these publications are accepted as conventional wisdom. These are accepted as good practice principles for budgeting and financial management systems for all countries and not just developing ones.

Comprehensiveness

9. The view that budgets need to be comprehensive for the government to be in a position to follow good macroeconomic management and promote allocative efficiency is of central importance. That is, the budget should include *all* revenue and expenditure:

“The basis for sound government finances is generally a single central fund into which revenues are received and out of which public activities for citizens are paid. For good macroeconomic management, controls need to be exercised over all revenues and expenditures. Activities placed outside the official “budget” are not subject to the discipline of the resource allocation process. A comprehensive budget process promotes allocative efficiency because it forces trade-offs between the different ways a government uses financial resources.” (World Bank, 1998: 98)

Transparency

10. Another key principle of sound budgeting and financial management is the importance of transparency, which requires that decision makers have all relevant issues and information before them when they make decisions. The financial crises of the late 1990s led to a discussion of the role of inadequate or inaccessible budget information in contributing to vulnerability. There was agreement that improving fiscal transparency would be a driving force for improving fiscal management. (IMF, 2003: 4)

11. In April 1998, the International Monetary Fund adopted the *Code of Good Practices on Fiscal Transparency*, the foundation document commonly used to assess the extent to which a government has open and transparent financial management and accountability.⁴ It is based on four general principles: clarity of roles and responsibilities; public availability of information; open budget processes; and assurances of integrity. The supporting *Manual of Good Practices on Fiscal Transparency* provides guidance on the Code’s implementation, setting out in more detail the principles and practices. (International Monetary Fund, 1998) All countries are encouraged to follow the good practices proposed in the Code; implementation is on a voluntary basis.

Accountability

12. Transparency is also important to ensure accountability:

“Transparency and accountability require that decisions, together with their basis and the results and the costs, be accessible, clear and communicated to the wider community. ... Decision makers must be held responsible for the exercise of the authority provided to them.” (World Bank, 1998: 2)

³ This was the main text for the World Bank Economic Development Institute course on *Budgeting Processes and the Analysis and Management of Public Expenditures*.

⁴ Kopits and Craig (1998) provides a discussion of basic concepts and definition of fiscal transparency that was a basis for development of the fiscal transparency code.

Implications for aid management

13. These general principles of sound budgeting and financial management have important implications for the management of external assistance by developing countries. As summarised in the OECD 2006 Guidelines on *Harmonising Donor Practices for Effective Aid Delivery, Volume 2*, donors have both a developmental and a fiduciary interest in the quality of partner countries' public finance management (PFM). For many developing countries aid is a substantial share of public resources, especially for the poorest countries, thus how aid is managed is an important determinant of overall PFM (OECD, 2006c: 19).

14. The IMF *Manual on Fiscal Transparency* highlighted that the relationship between the domestic budget and externally financed expenditure raises issues in many developing countries, as separate, non-transparent processes for determining the size and allocation of external and other budgetary receipts are often the source of financial control problems (International Monetary Fund, 1998: 17), and adversely impact on the comprehensiveness, transparency and accountability of the recipient country's budgeting and PFM system.

15. The World Bank *Public Expenditure Management Handbook* set out that poor aid management means a poor PFM system due to two main factors:

- Different priorities (not only between a donor and a country, but between donors).
- Poor coverage of aid funding in the budget. One of the coordination problems identified is keeping track of how much donors have spent and what the funds have been spent on. (World Bank 1998: 5, 106)

16. In countries with large external aid inflows many externally financed transactions were found not to be captured by the government accounting system. Sometimes this has been a direct consequence of donor financing arrangements:

“For example, expenditure may be debited directly from donor agency or trust accounts, and special accounting arrangements may be set up to ensure accountability to the donors, usually at the expense of transparency and accountability in the recipient country.” (International Monetary Fund, 1998: 58)

17. In particular, the treatment of non-cash aid⁵ in the budgeting and accounting systems was found to be particularly non-satisfactory:

- It is rarely fully recorded.
- Assets created or acquired are not being recorded in a way to help identify long-term operations, capital depreciation, and maintenance needed.
- There are problems with the timely recording and valuation of such assistance. (*ibid.*: 59)

18. Following from the identification of these main issues, the recommendations for effective budgeting and financial management include putting aid on budget at each of the different stages of the budgeting cycle.

19. The IMF *Manual on Fiscal Transparency* sets as a minimum standard that accounting systems should cover domestic and externally financed transactions and allow for the capture and recording of information at the commitment stage and all externally financed transactions in a timely way. (International Monetary Fund, 1998: 55, 58) The *Manual* goes on to detail that as cash systems are generally unsatisfactory as a means of tracking aid in kind, a full accrual system is needed to deal with non-financial assets in a fully integrated way and all countries should maintain at least memorandum-level records of significant receipts of aid in kind. (*ibid.*: 59)

⁵ Aid in kind: Flows of goods and services with no payment in money or debt instruments in exchange. In some cases, “commodity aid” goods (such as grain) are subsequently sold and the receipts are used in the budget or, more commonly through a special fund, for public expenditure. Definition in IMF *Manual of Good Practices on Fiscal Transparency* glossary (International Monetary Fund, 2007: 125).

20. A checklist of good practice in the World Bank *Public Expenditure Management Handbook* includes the following that is directly concerned with putting aid on budget:
- “All aid is incorporated in the budget.”
 - “In the case of direct disbursement, government is involved in sanctioning expenditure. Government receives expenditure statements from aid agencies, and expenditures are then recorded in the government accounts.”
 - “Separate arrangements are not made for providing aid agencies with progress reports and statements on expenditure incurred by government. They are a by-product of the country’s own systems.” (World Bank, 1998: 107)

Recent developments on budget standards

21. In recent years there has been activity to develop further detailed standards on the treatment of external assistance in recipient countries’ budgeting systems.

22. The IMF *Code and Manual of Good Practices on Fiscal Transparency* were revised in 2001 and most recently in April 2007.⁶ A new recommendation in the 2007 Code strengthens the standard for reporting on external financing, with separate identification of aid in the budget:

“3.1.4 Receipts from all major revenue sources, including resource-related activities *and foreign assistance*, should be separately identified in the annual budget presentation.” [emphasis added] (International Monetary Fund, 2007)

23. Another recent development has been the issue in 2003 of the internationally recognized accounting standard, known as IPSAS (International Public Sector Accounting Standard) for cash-based financial reporting (IFAC Public Sector Committee, 2007). This is relevant to developing countries as the vast majority of governments do not have accrual-based systems. IPSAS are issued by the International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants (IFAC).⁷

24. There were calls for an internationally accepted accounting standard for reporting external assistance when the cash basis of financial reporting is adopted. Since 2005 IPSASB has undertaken a consultation process on exposure drafts to amend the Cash Basis IPSAS to include additional required and encouraged disclosures for recipients of external assistance.

25. IPSASB issued Exposure Draft (ED) 24 in 2005. It recognises the difficulty of recipient governments in collating information from donors on external assistance and proposes that reporting requirements for external assistance should be harmonised on the basis of the accounting principles followed by the recipient government. However commentators on the ED expressed concerns about the practicability of some of the proposals. As summarised by IFAC: “in at least some jurisdictions the data necessary for compliance was not readily available and the costs of compliance would outweigh its benefits.” (IFAC website)

26. The IPSASB developed ED 32 following consultation with the Eastern and South African Association of Accountants General, the OECD DAC Joint Venture on Public Financial Management, IPSASB consultative group and a wide range of constituents. ED 32 recognises that:

“... the ability of individual recipients to comply with the proposed requirements of ED 24 may differ because of the availability of the information and/or capacity of the current accounting system to capture and process the information as proposed.” (International Public Sector Accounting Standards Board, 2006)

⁶ Following an evaluation by the IMF and the World Bank of the Standards and Codes Initiative (International Monetary Fund and World Bank, 2005).

⁷ A useful overview of IFAC and the internationally recognized accounting standards, along with other international public sector standards, is provided by the 2003 PEFA-commissioned study *Overview of International Public Sector Standards in Accounting, Auditing and Internal Control* (PEFA Secretariat, 2003).

27. ED32 proposes a split into mandatory and recommended disclosures under the cash basis of accounting, as detailed in Box 3. Two brief comments on ED32 are:
- i. The definition of external assistance used in ED32 does not include assistance provided by NGOs. Most commentators agree that while there is little theoretical justification to exclude unofficial assistance such as that from NGOs, there is an argument for its exclusion on cost-benefit basis, given the likely practical difficulties governments will face in compiling the information.
 - ii. The purposes for which aid was received is an optional ('encouraged') disclosure only.

Box 3: IPSAS ED 32 mandatory and optional disclosures

Mandatory disclosures	
1.9.6	show separately total external assistance received in cash
1.9.7	show [aid in kind] i.e. payments made on government's behalf by a third party
1.9.8	break down by different providers
1.9.9	show grants and loans separately
1.9.16	show separately the undrawn balance of (a) loans \and (b) grants
1.9.18	if reporting receipt of goods or services in kind, disclose the basis of evaluation
1.9.20	disclosure of debt rescheduled or cancelled
1.9.22	where non-compliance with conditions etc has led to cancellation of loans, grants or guarantees, explain the condition and the non-compliance
Optional ("encouraged") disclosures	
2.1.60	show purposes for which aid was received
2.1.65	for undrawn aid, provide notes as to (a) providers, (b) purposes, (c) changes in amounts
2.1.73	information concerning third party guarantees
2.1.76	[more on 1.9.22]
2.1.80	repayment terms and conditions on external debt
2.1.85	disclose separately in the notes to financial statements the value of external assistance received in the form of goods and services.

Source: International Public Sector Accounting Standards Board, 2006.

28. The ED 32 was released November 2006 for comment by end of March 2007 (later extended to the end of April 2007). Field tests of ED 32 have been completed by Ghana, Uganda and Nigeria. According to IFAC, a preliminary review of field test results indicated no major impediments to adoption of the proposed IPSAS requirements within the proposed transitional period. In July 2007 the IPSASB reviewed all responses to ED 32 and provided directions for development of a first draft IPSAS to be considered for approval at the November 2007 meeting. Members confirmed that disclosure requirements are to be incorporated in the Cash Basis IPSAS, rather than in a stand alone IPSAS. (IFAC website www.ifac.org)

29. As of September 2007, the status of adoption of IPSASs by the Aid on Budget case study countries was reported by IFAC (IFAC, 2007) as:

- *Bangladesh:* Process in place to adopt IPSASs and legislation passed.
- *East and Southern Africa:* The East and Southern African Association of Accountants General member states' aims include adoption of IPSASs. The association's member states are: Botswana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Rwanda, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe.
- *Ghana:* Has adopted the Cash Basis IPSASs, is transitioning to the accruals basis IPSASs.
- *South Africa:* Adoption of IPSASs (accruals, with South African amendments) in process.
- *Uganda:* Government has adopted IPSASs.
- *Vietnam:* Process in place to adopt IPSASs with World Bank support.

Consensus on aid effectiveness

30. The development of these international standards on sound budgeting and PFM systems has fed into the growing consensus on the good practice principles of effective aid. As summarised by the DAC Guidelines *Harmonising Donor Practices for Effective Aid Delivery, Volume 2*: “Effective public finance management is crucial to countries making progress in reducing poverty. It is fundamental both to government performance and to successful aid delivery.” (OECD, 2006c: 19)

More and better aid

31. Since the start of the new millennium the need to provide more and better aid has risen to the top of the development agenda. (OECD, 2005a: 15) The realisation that millions of people were not being helped out of poverty in spite of decades of aid led to calls that overcoming human poverty would require “a quantum leap in scale and ambition.” (United Nations, 2004) The Millennium Development Goals (MDGs) set out the aims of this scaled-up approach. However, revised assessments of aid effectiveness during the 1990s meant that the international development community recognized that **more** aid would not be enough; **more effective** aid was needed.

32. An early articulation of the good practice principles for effective aid is provided by the 1986 OECD Development Assistance Manual *DAC Principles for Aid Co-ordination*, which emphasises that aid coordination is necessary for the delivery of effective aid (OECD, 1992). The World Bank 2001 *Review of Aid Coordination in an Era of Poverty Reduction Strategies* spelt out that such aid coordination should be the responsibility of the recipient country, with donors directing their support to assist developing countries in strengthening their institutional capacity to effectively discharge that coordination responsibility (World Bank, 2001: iv).

33. Today there is broad acceptance of the maxim “donors cannot develop a country; a country can only develop itself.” (OECD, 2005a: 19) The need for country ownership was highlighted by studies carried out in the 1990s which concluded that aid works in good policy environments but necessary reforms cannot be bought through conditionality.⁸ In the place of past attempts which tried to impose external solutions through conditionality, and which often failed to take account of the cultural and political context, donors called for the alignment of donor assistance strategies with priorities articulated in country-led and -owned development strategies. There was also the perception that inappropriate aid modalities had become part of the problem. Bypassing government systems and their weaknesses was seen to have led not only to non-aligned, misdirected, inconsistent and duplicated efforts, but had also to weaker government systems by fragmenting national decision-making and raising the transaction costs of aid. (OECD, 2005a: 15; IDD and Associates, 2006: 8).

34. The draft 2007 World Bank Aid Effectiveness Review reports that the Poverty Reduction Strategy (PRS) initiative was introduced in 1999: “... to help countries improve national development strategies and their implementation and to serve as a framework for facilitating alignment with country priorities, reliance on national institutions, and use of country systems to deliver aid”. (World Bank, 2007d: 1)

35. There were also calls for debt relief and a more direct focus on poverty. The international development community’s response of the Heavily Indebted Poor Countries (HIPC) Initiative led to a focus on the adequacy of government systems to allocate HIPC resources to pro-poor environments. (IDD and Associates, 2006: 8) The Poverty Reduction Strategy Papers (PRSPs) were expected to link priorities with domestic and external resources, thus facilitating strategic budgeting and allocative efficiency. HIPC Assessments and Action Plans (AAPs) prepared jointly by the World Bank and the IMF for heavily indebted poor countries in 2001 and 2004 provided the opportunity to measure progress over time.⁹ Budget execution and the ability of countries to track poverty-reducing

⁸ The Assessing Aid study (Dollar and Pritchett, 1998) was seminal. (IDD and Associates, 2006)

⁹ HIPC AAP questionnaire and guidance is provided in World Bank and International Monetary, 2003. Annex 3 has further country level detail on the AAPs.

expenditures were found to be especially weak (International Development Association and International Monetary Fund, 2005).

Ownership, alignment, harmonisation

36. From 2000, donors and partner countries worked through various technical groups to develop good practice standards to use as a basis for harmonizing and aligning policies, procedures and practices.¹⁰ Donors and partner countries committed to implementing these good practice principles at the DAC High Level Forum held in Rome in February 2003.

37. The good practice principles adopted at Rome have at their core the concept that donor alignment with partner countries' a) strategies and b) systems is central for ensuring effective country ownership. Alignment involves putting aid on budget and the good practice principles include recommendations for both donors and governments for putting aid on budget:

“Donors should provide partner governments with full information of aid flows. This should be done regularly and in a timely manner. This enables partner governments to integrate aid into macroeconomic and budgetary management and publish details of aid received.” (OECD, 2003: 20)

“Donors should work with partner countries to rely on country owned reporting and monitoring systems. These systems should ideally provide information on financing (including aid), budget expenditure, progress in implementation, and poverty reduction outcomes/impacts.” (*ibid.*: 58)

“Donors should rely on partner country financial reporting systems when the financial reports meet the information needs of government and donors. ... Where weaknesses are identified, donors should support capacity building measures.” (*ibid.*: 70–71)

38. These commitments were further developed at the Paris High Level Forum in 2005 where over 100 donors and partner countries¹¹ endorsed the Paris Declaration. The commitments rest on five “common-sense” tenets, that aid is more likely to promote development when:

- “Developing countries exercise leadership over their development policies and plans (*ownership*).
- Donors base their support on countries’ development strategies and systems (*alignment*).
- Donors co-ordinate their activities and minimise the cost of delivering aid (*harmonisation*).
- Developing countries and donors orient their activities to achieve the desired results (*managing for results*).
- Donors and developing countries are accountable to each other for progress in managing aid better and in achieving development results (*mutual accountability*).” (OECD, 2007e: 9)

39. The Paris Declaration commitments include putting aid on budget at all points of the budget cycle. The relevant commitments are repeated in Box 4.

40. The 2006 OECD Good Practice Guidelines *Harmonising Donor Practices for Effective Aid Delivery, Volume 2* provide further elaboration of the principles of aid effectiveness and the importance of putting aid on budget (OECD, 2006c). The importance of the quality and timeliness of aid flow information and the predictability of aid, is emphasised:

“... the onus on donors to support national strategies and, whenever practical, to operate through government budgets, have highlighted the need for aid to be more predictable, and for better information exchange concerning aid flows.” (*ibid.*: 21)

“... aid predictability is an important factor in the ability of countries to manage public finances and undertake realistic planning for development”. (*ibid.*: 28)

¹⁰ The technical groups covered: donor cooperation, country analysis, financial management, procurement and environmental assessment (OECD 2005a: 16). The published Good Practice Papers are available from the DAC Guidelines and Reference Series *Harmonising Donor Practices for Effective Delivery, Volume 1* (OECD, 2003).

¹¹ Twice as many countries and new donor countries participated in the Paris Forum compared to the 2003 Rome Forum. Also, civil society representatives and parliamentarians were actively involved in the Forum for the first time (OECD DAC, 2005b).

Box 4: Paris Declaration commitments to put aid on budget**Ownership**

(14) *Partner countries commit to:*

- Exercise leadership in developing and implementing their national development strategies through broad consultative processes.
- Take the lead in co-ordinating aid at all levels in conjunction with other development resources in dialogue with donors and encouraging the participation of civil society and the private sector.

(15) *Donors commit to:*

- Respect partner country leadership and help strengthen their capacity to exercise it.

Alignment**Donors align with partners' strategies**

(16) *Donors commit to:*

- Base their overall support — country strategies, policy dialogues and development co-operation programmes — on partners' national development strategies and periodic reviews of progress in implementing these strategies (Indicator 3).

Donors use strengthened country systems

(21) *Donors commit to:*

- Use country systems and procedures to the maximum extent possible. Where use of country systems is not feasible, establish additional safeguards and measures in ways that strengthen rather than undermine country systems and procedures.
- Avoid, to the maximum extent possible, creating dedicated structures for day-to-day management and implementation of aid-financed projects and programmes.

Strengthen public financial management capacity

(25) *Partners commit to:*

- Publish timely, transparent and reliable reporting on budget execution.

(26) *Donors commit to:*

- Provide reliable indicative commitments of aid over a multi-year framework and disburse aid in a timely and predictable fashion according to agreed schedules.
- Rely to the maximum extent possible on transparent partner government budget and accounting mechanisms.

Harmonisation**Donors implement common arrangements and simplify procedures**

(32) *Donors commit to:*

- Implement, where feasible, common arrangements at country level for planning, funding (e.g. joint financial arrangements), disbursement, monitoring, evaluating and reporting to government on donor activities and aid flows. Increased use of programme-based aid modalities can contribute to this effect.

Deliver effective aid in fragile states

(39) *Donors commit to:*

- Avoid activities that undermine national institution building, such as bypassing national budget processes or setting high salaries for local staff.

Managing for Results

(44) *Partner countries commit to:*

- Strengthen the linkages between national development strategies and annual and multi-annual budget process.

Mutual Accountability

(48) *Partner countries commit to:*

- Strengthen as appropriate the parliamentary role in national development strategies and/or budgets.

(49) *Donors commit to:*

- Provide timely, transparent and comprehensive information on aid flows so as to enable partner authorities to present comprehensive budget reports to their legislatures and citizens.

Source: High Level Forum, 2005.

Aid information management systems

41. For implementation of the Paris Declaration commitments at country level, aid information management systems (AIMS) are seen as an important technical solution. The OECD DAC and UNDP issued a paper in June 2006 describing how AIMS support implementing Paris commitments and good practice in selecting and implementing such systems (OECD and UNDP, 2006).

AIMS provide an interface between national PFM systems and information in donor systems and allow for harmonised reporting of scheduled and disbursed aid, and for reporting back to donors on how the funds have been used. (*ibid.*: 2) This resulting aid flow transparency is an essential step for aid to be accurately reflected on budget. AIMS help with the reporting of aid, not the integration of aid with national systems.

42. AIMS is a technical solution: the validity of data recorded in AIMS depends directly on the quality and frequency of reporting by donors and government. According to the OECD and UNDP paper:

“The reliability of AIMS data and their value for decision-making are a function of the dialogue between government and donors and their policies and practices. ... Sustainable and reliable data flow is a precondition to AIMS implementation, as well a sustained political and financial commitment relating to good, transparent and accountable governance.” (*ibid.*: 5)

43. Box 5 provides further detail on AIMS. A UNDP 2006 discussion paper provides lessons learnt from establishing AIMS in various countries (Nadoll, 2006) and the Aid on Budget country studies looked for country-level experience of implementation of AIMS.

Box 5: Aid information management systems

OECD DAC has issued a paper summarising good practice in selecting and implementing such systems, based on several years' experience in a variety of country situations:

What are AIMS?

- AIMS are IT applications, usually databases, which record and process information about development initiatives and related aid flows in a given country.
- AIMS are not complete PFM systems. Rather AIMS provide an interface between the recipients' PFM systems and information stored in donor systems.
- A good aid AIMS will track both planned and actual commitments, disbursements and expenditures, and also the planned and actual outputs that each programme and project is intended to achieve.

What can AIMS achieve?

- Help align donor procedures and practices with government systems by providing a standard format to align to
- Consolidate the information from donor systems.
- Help reduce the administrative burden for recipients reporting back to donors on how funds are used
- Help the government to have easily accessible and timely information on planned and ongoing aid flows.

What best practices have been identified?

A number of best practices have been identified during the past few years through work carried out by the UNDP and global consultations in 2004–2006. These consultations gathered practitioners and experts from several regions and recorded their practices and experiences. Through lessons learnt and assessment of good practices it was identified that success depends on:

- ***Governments providing*** leadership; applicable policies for information disclosure and exchange; complete and verified development data; classification systems that are in line with accepted standards; and adequate staff;
- ***Donors providing*** complete, reliable and comprehensive project data, including full disclosure of financial assistance; mid-term projections of assistance delivery including disbursement schedules; validated data across reporting sources and well defined conditionalities; as well as resources and training for setting up an AIMS.

Source: OECD and UNDP, 2006.

Monitoring aid on budget

Paris Declaration indicators

44. The Paris Declaration aims to be a practical action-orientated roadmap to improve the quality of aid and its impact on development (OECD, 2006a). The Declaration is supported by a set of 12 indicators with targets for 2010, developed to track and encourage progress against the broader set of partnership commitments.

45. There are three indicators that are concerned with putting aid on budget: indicator 3 “aid flows aligned on national priorities”, indicator 5 “use of country PFM systems” and indicator 7 “predictability of aid”. Box 6 gives a summary of the targets and focus of these three indicators.

Box 6: Paris Declaration indicators and targets for putting aid on budget

<i>Indicator</i>	<i>Target</i>	<i>Monitoring</i>
Indicator 3: Aid flows are aligned on national priorities	<i>Halve the proportion of aid flows to government sector not reported on government's budget(s) (with at least 85% reported on budget)</i>	The gap between what was disbursed by donors for the government sector and what was actually recorded in the annual budget by government.
Indicator 5a: Use of country PFM systems	<i>Score 5+ - all donors use partner countries PFM systems and a two-thirds reduction in the % of aid to the public sector not using partner countries PFM systems; Score 3.5–4.5: 90% all donors, and a one third reduction¹²</i>	The volume of aid and the percentage of donors that uses a partner country PFM system as a percent of total aid provided to the government sector. Looks at the three components of a country's PFM procedures: i) national budget execution procedures ii) national financial reporting procedures iii) national auditing procedures.
Indicator 7: Aid is more predictable	<i>Halve the proportion of aid not disbursed within the fiscal year for which it was scheduled.</i>	The gap between aid scheduled and aid effectively disbursed and recorded in countries accounting systems. (Focuses specifically on in-year predictability of aid flows to the government sector.)

Source: High Level Forum, 2005; OECD, 2006b.

Paris Declaration 2006 Monitoring Survey

46. There are three planned rounds of monitoring for the Paris Declaration. The first survey was undertaken in 2006 and the Survey report published in 2007. The 2006 Survey data for aid flows of 2005 was collected from 34 self-selected countries and a comprehensive list of donor organisations covering 37% of aid programme across the world. (OECD, 2007e: 9) Annex A provides detailed information on the 2006 Survey.

47. The Survey sets the baselines for eight of the indicators, including the indicators relevant for putting aid on budget. In addition to the survey data, some of the indicators are assessed from other data sources: the World Bank Country Policy and Institutional Assessment (CPIA), the DAC Joint Venture on Procurement and the World Bank Aid Effectiveness Review (which builds on the 2005 Comprehensive Development Framework analysis) (World Bank, 2005). The World Bank Aid Effectiveness Review includes a set of Aid Effectiveness Profiles that document in-country action toward achieving the Paris Declaration goals. Table 1 shows the sources of information for each Paris Declaration indicator.

¹² These are World Bank Country Policy and Institutional Assessment (CPIA) scores.

Table 1: Sources of information for Paris Declaration indicators

	Indicators	Questionnaire	Desk review
1	Ownership – Operational PRS		CDF (World Bank)
2a	Quality of PFM systems		CPIA (World Bank)
2b	Quality Procurement systems		OECD-DAC (1)
3	Aid reported on budget	■	
4	Coordinated capacity development	■	
5a	Use of country PFM systems	■	
5b	Use of country procurement systems	■	
6	Parallel PIUs	■	
7	In-year predictability	■	
8	Untied aid	■	OECD-DAC (2)
9	Use of programme-based approaches	■	
10	Joint missions & country analytic work	■	
11	Sound performance assessment framework		CDF (World Bank)
12	Reviews of mutual accountability	■	

Notes: (1) The OECD-DAC Joint Venture on Procurement is currently developing a framework for measuring progress. (2) Information to be drawn from OECD DAC annual progress report on Implementing the 2001 *DAC Recommendation on Untying ODA to the Least Developed Countries*.

Source: OECD DAC, 2006b.

48. The Survey reports that strong expectations for reform have been created since the Paris Declaration. An increasing number of governments are reported to be working on guiding implementation of the Paris commitments in their countries, while most major donors have made major efforts to implement the commitments in their organisations. At the same time, the baseline results of the Survey (based on 2005 data) show that there is still a long way to go to meet the targets set, and the Survey emphasises that significant efforts are required (OECD, 2007e: 53).

49. The baselines for indicators reveal interesting behaviour at the national and donor level. Annex A provides the detailed findings by country and for donor for the indicators pertinent to putting aid on budget. In summary:

Indicator 3: “donors’ disbursements recorded in government’s budget estimates”

- The baseline reported by the Survey is high at 88% (the original target was “at least 85% reported on budget). However, as budgets are unrealistic in two opposite directions, over-reporting of aid on budget in individual cases balances out under-reporting in other cases, resulting in a higher baseline position.
- In the majority of countries and for a fair number of donors, performance is substantially below this level.
- The detailed figures reveal quite striking differences among agencies that are involved in similar numbers and types of countries. (*ibid.*)

Indicator 5a: “use of country PFM systems”

- The baseline reported by the Survey is low at 40% (average use of budget execution, financial reporting and auditing). If in the future country PFM quality remains largely in the range CPIA 3.5–4.5 then the 2010 target is 59%.
- There is considerable variation in the use of country systems across countries and the correlation between the quality of the country PFM system and the use being made of them by donors is very weak, suggesting that other factors other than the quality of systems are affecting donors’ willingness to use them.
- In the Survey donor information is used for calculating the proportion of aid that uses government systems for budget execution, financial reporting and auditing. It would be useful also to have the government data to monitor progress on this indicator. (*ibid.*)

Indicator 7: “aid disbursed on schedule”

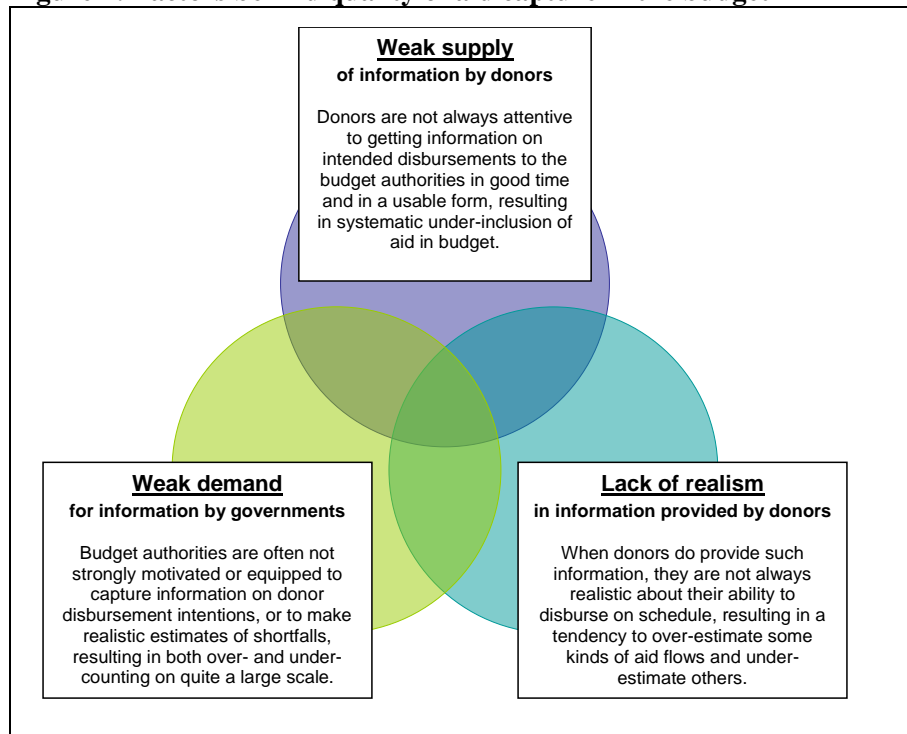
- The baseline reported by the Survey is 70%, which means that the 2010 target is at least 85%.
- The issue of over- and under-reporting of aid balancing out in the aggregate baseline described for indicator 3 also applies to indicator 7.
- For almost all countries and all larger donors, disbursements were under-recorded, sometimes very substantially
- A few of the major donors are substantial under- or over- disbursers. The Survey reports that it is unclear if there is an explanation related to the subset of surveyed countries where those agencies are involved. (*ibid.*)

50. The Survey makes six key policy recommendations. One of these recommendations focuses on donor practice of putting aid on budget:

“Donors need to support these efforts [by partner countries to deepen their ownership of the development process] by making better use of partners’ national budgets to align their programmes with country priorities. They also need to improve the transparency and predictability of aid flows by sharing timely and accurate information on intended and actual disbursements with aid authorities.” (*ibid.*: 52)

51. The Survey report stresses that the Paris Declaration commitments are *mutual* commitments, a joint undertaking of the donor community and partner countries and that the commitments, being highly interdependent, are only likely to be realised through a combination effort that acts on both sides of the problem. (*ibid.*: 15) Putting aid on budget is the joint effect of donor and government practices, and where there is poor quality of aid capture in the budget, this is the compound effect of both donor and government shortcomings. The Survey¹³ summarises the causes of poor aid capture that were reported in the Survey returns. These are depicted in Figure 1.

Figure 1: Factors behind quality of aid capture in the budget



Source: Author, based on OECD, 2007e.

¹³ The scope of the Paris Declaration Survey is to look at how implementation of commitments by partners and donors is progressing. It is not designed to reveal why the changes are or are not happening (OECD, 2007b). However, as part of the process the survey returns included the insights and opinions of some of the main stakeholders in the process (OECD, 2007e).

Challenges for monitoring

52. One of the main challenges for the 2006 Survey was the lack of consensus on practical definitions. The Survey guidance allowed for a flexible interpretation of definitions with the result that few country groups were able to reach a consensus on locally adjusted definitions. (OECD, 2007e: 46) Consequently the lowest common denominator was often applied. A number of national coordinators have the perception that donors “used the permitted leeway on definitions to place their performance closer to the targets than would otherwise have been the case”. (OECD, 2007b) The Survey highlights this concern on interpretation of definitions for indicator 5a: “For several countries it is not clear that all of the programmes included as using country budget execution systems are accurately described as “subject to normal country budgetary execution procedures, namely procedures for authorisation, approval and payment”. There are also some grey areas affecting the interpretation of the indicator. ... Together, these factors may mean that the numbers overstate somewhat the effective use of country systems.” (OECD, 2007e: 24)

53. As a result of this lack of consensus on practical definitions there is a concern that the 2005 baseline may systematically overstate the progress achieved on the 2010 targets. The Survey report cautions against “a naïve utilisation of the baseline data” and advises that firmer steps are needed to ensure the standardisation of measures for the next survey round.¹⁴ (*ibid.*)

Strengthened approach to PFM assessment and reform

54. Aid on budget is also monitored through PFM assessments.

55. In the last decade donors have focused on undertaking PFM systems diagnostics and analyses, to understand the capabilities and weaknesses of country systems in order to implement effective reforms. This has resulted in an important body of knowledge and information on the state of public financial management systems in partner countries. Box 7, reproduced from the DAC Guidelines on *Harmonising Donor Practices for Effective Aid Delivery, Volume 1* (OECD, 2003), provides a summary of the key PFM assessment instruments.

56. This growth in diagnostics and reviews and the lack of co-ordination in how they are applied led to duplication of donor efforts and high transaction costs on partner governments. In addition this made it difficult to agree a shared agenda among government and the donor community on how to improve financial management (OECD, 2003: 45). There was a perceived lack of progress on reform implementation as the numerous individual reform programmes¹⁵ were seen to have an adverse impact on country-ownership, transaction costs for countries and donor harmonisation and alignment. Therefore there was a clear need for the creation of a platform for a common point of dialogue. (Public Expenditure Working Group, 2005)

57. In response, in December 2001 the Public Expenditure and Financial Accountability (PEFA) programme was set up¹⁶ and a strengthened approach to public financial management reform developed. PEFA commissioned a study to review the various instruments and approaches used to assess and reform public expenditure, financial management and procurement systems. The study recommends a new, strengthened, approach to PFM reform which is country-led, multi-donor, medium-term in orientation, focused on better management of the budget, and supplemented by donor aid funds, as a key mechanism to reduce poverty and attain other policy goals (Allen et al, 2004). The Paris commitments support this approach, with partners and donors jointly committed to

¹⁴ There are other factors reported in the Survey report and by other observers for why the baseline data should be treated with caution. These are summarised in Annex A.

¹⁵ A recent article by the IMF estimated that there are more than 50 assistance providers that work in the PFM area and, in any one country, the average number of providers is around 7. (Allen and Last, 2007)

¹⁶ The PEFA programme has been jointly financed by the World Bank, the European Commission (EC), the UK's Department for International Development (DFID), the Swiss State Secretariat for Economic Affairs (SECO), the Royal Norwegian Ministry of Foreign Affairs and the French Ministry of Foreign Affairs. The IMF and the SPA are also partners. (PEFA website www.pefa.org)

implementing harmonised diagnostic reviews and performance assessment frameworks in PFM (High Level Forum, 2005: ¶27).

Box 7: PFM diagnostic reviews¹⁷

Country Financial Accountability Assessment (World Bank)
CFAAs are a diagnostic tool designed to enhance knowledge of public financial management and accountability arrangements in client countries.
Public Expenditure Review (World Bank)
PERs analyse the recipient country's fiscal position, its expenditure policies – in particular the extent to which they are pro-poor – and its public expenditure management systems
Country Procurement Assessment Review (World Bank)
CPARs examine public procurement institutions and practices in borrower countries.
HIPC Expenditure Tracking Assessment (World Bank and IMF)
These assess the ability of the public financial management systems in highly indebted poor countries (HIPCs) to track poverty-reducing expenditures, using fifteen public financial management benchmarks.
Fiscal Transparency Review (IMF)
This is a module of the Reports on Observance of Standards and Codes (ROSC) which uses the Code of Good Practices on Fiscal Transparency adopted by the IMF in 1998
Diagnostic Study of Accounting and Auditing (Asian Development Bank)
These examine financial management and governance practices in the public and private sectors of borrower countries.
Ex ante assessment of country financial management (European Commission)
Traditionally, the EC has carried out audits of its “targeted” budgetary support with a view to determining expenditures “eligible” or “ineligible”. For future budget support, however, it is developing a new approach using <i>ex ante</i> PFM assessments based on a mix of diagnostic work completed by other donors/governments and a “compliance test” to provide an empirical evidence of performance of the PFM systems.
Country Assessment in Accountability and Transparency (UNDP)
CONTACT is a toolkit to assist governments and consultants in conducting missions to assess public financial accountability systems.

Note: Annex D looks at country experiences with putting aid on budget and provides further detail on a number of these diagnostic tools.

Source: OECD DAC, 2003.

Public Expenditure and Financial Accountability assessments

58. To enable harmonized performance assessments, the PFM Performance Measurement Framework was launched in June 2005.¹⁸ The framework includes a set of high level indicators (28 partner performance indicators and 3 donor performance indicators) which draw on the HIPC expenditure tracking benchmarks, the IMF Fiscal Transparency Code and other international standards.¹⁹ It measures the operational performance of the PFM systems, processes and institutions against the core dimensions of PFM performance.²⁰

59. The framework reflects the importance of good information on external development assistance for the effectiveness of governments PFM systems and for aid effectiveness. It recognises the needs

¹⁷ Since the publication of the DAC Guidelines, DFID has developed a new approach to assessing fiduciary risk based on a methodology similar to that of the HIPC AAPs (Allen et al, 2004).

¹⁸ The Framework was developed between 2003 and 2005 through extensive consultations, including with the DAC Joint Venture on PFM, a group of African PFM experts, and government representatives from Eastern Europe and Central Asia. Comments were also received from practitioners within the World Bank, IMF, other PEFA partners, government agencies and professional organizations. (PEFA Secretariat, 2006a: iii)

¹⁹ The PEFA note *Common Approach to PEFA value added and links to other indicators* provides a useful summary of the links between PEFA indicators and other international PFM indicators (PEFA Secretariat, 2007a).

²⁰ PEFA identify six core dimensions: credibility; comprehensive and transparent; policy-based budgeting; predictability and control in budget execution; accounting, recording and reporting; and, external scrutiny and audit (PEFA Secretariat, 2006a).

both for government to report on donor funds and for donors to provide sufficient information on their forward commitments, disbursements and the utilisation of funds. Various PEFA indicators are directly relevant to the extent that they provide information about the degree to which aid is captured in the budget system; indicators may also be indirectly relevant for the light they shed on aspects of the underlying PFM system that affect the scope for bringing aid on budget, or the quality of its capture in the budget system. In the framework five of the indicators are especially relevant for putting aid on budget:

- In the partner performance section, indicator PI-6 looks at the comprehensive of information included in the budget documentation, and Indicator PI-7 measures the capture of income and expenditure information for donor funded projects, even if they are not technically on budget or are managed outside of government's budget management and accounting system.
- The final section of the performance framework assesses donor practices, looking at the predictability of budget support and the degree to which donors provide financial information for budgeting and reporting on project and programme aid (Indicators D-1 and D-2). The framework also has a separate indicator for the proportion of aid funds that are managed by the use of national procedures (Indicator D-3). (PEFA Secretariat, 2006a)

60. Several of the other PEFA indicators also influence the potential benefits of putting aid on budget and donors' willingness to put aid on budget. (For example, PI-12 – multi-year perspective in fiscal planning, expenditure policy and budgeting – is highly relevant to the "on plan" dimension.) Moreover, the score for most indicators draws on several different sub-components. In some cases it may be worth highlighting specific sub-indicators (for example, component (i) of indicator PI 7 does not relate to aid, but component (ii) focuses explicitly on the capture of aid in fiscal reports).

61. The PEFA indicators are also closely linked to the Paris Declaration indicators:

- Paris Declaration Indicator 2(a), which deals with PFM system, is closely linked to the PEFA framework.
- Paris Declaration Indicator 5 is closely aligned to the PEFA Performance Indicator D-3
- Paris Declaration Indicator 7 is closely linked to the PEFA D-1, D-2 and the second (ii) dimension of PI-7. (PEFA Secretariat, 2007a)

62. The PEFA framework has been internationally well accepted and is now good practice for the integration and coordination of PFM assessments amongst donors (PEFA Secretariat, 2006b). For example, the HIPC-AAP expenditure tracking indicators and the DFID Fiduciary Risk Assessment indicators were focused on assessing PFM performance at the same level as the PEFA framework and both these sets are being replaced by the PEFA performance indicators.

63. At August 2007, 45 assessments had been completed, 20 completed to full draft, 15 commenced and 30 planned (PEFA Secretariat, 2007b). Annex B provides the scores of PEFA assessments for the Aid on Budget case study countries. While some of the PEFA assessments are made publicly available, the institutions undertaking the PEFA Framework are ultimately responsible for dissemination of the reports. Therefore not all reports are publicly available.²¹

64. In Annex B the scores for the indicators of interest to the putting aid on budget study have been collated from the PEFA assessments that are available. The distribution of scores for these indicators issued in the PEFA Secretariat 2006 *Report on Early Experience from Application of the Framework*

²¹ The institutions undertaking the PEFA Assessments are ultimately responsible for dissemination of the reports, including making them publicly available. During the initial period of introducing the PEFA Framework publicising the reports was not sufficiently focused on and as at December 2007 only 18 reports are available through the PEFA website. However, the assessment leading institutions have taken action to ensure publication of future reports, as well as resolving any issues that may have constrained the completed assessments from being publicized.

(PEFA Secretariat, 2006b) is also included in the annex. The findings show that there is a wide variation of scores in countries on the indicators relevant to putting aid on budget.

65. It is important to note that cross-country comparison of PEFA indicators was never an objective of the Framework. The PEFA *Report on Early Experience from Application of the Framework* explains why such a comparison is difficult:

- “Comparison between two countries only makes sense on indicators for which the compliance with scoring methodology is high in order to ensure consistency and adequate documentation for differences; on the current stock of reports that limits the countries for which such a comparison can be meaningfully taken.
- Comparison of a country’s performance against relevant global and regional averages requires that assessments have taken place in a significant number of countries with comparable characteristics, which is not yet the case.” (*ibid.*: 21)

SECTION B: DONOR APPROACHES TO PUTTING AID ON BUDGET

66. This section reviews the applicable policies and guidelines of the major multilateral and bilateral agencies as these affect the incorporation of their aid into government budgets. The bilateral agencies covered are: Canada, Denmark, France, Germany, Ireland, Japan, the Netherlands, Norway, Sweden, the United Kingdom and the United States. The multilateral organisations covered are: the African Development Bank (AfDB), the Asian Development Bank (AsDB) and the Inter-American Development Bank (IDB), the World Bank, the IMF, the European Commission (EC) and the United Nations (UN).²²

67. Donor by donor information is systematically presented in Annex C. The donor profiles in Annex C are based on a review of the available documents and, in many of the cases, responses to enquiries from the Aid on Budget team. The following paragraphs highlight overall findings from this review of donor approaches.

Paris Declaration action plans

68. Signatories of the Paris Declaration committed to “implement the action plans that [donors] have developed as part of the follow-up to the Rome High-Level Forum” (High Level Forum, 2005: ¶32).

69. The DAC reported in February 2007 that an overwhelming majority of DAC members (16 out of 24) and multilateral organisations (4 out of 5) have taken “immediate steps” to translate the Paris Declaration commitments into an operational Action Plan, and donors that do not have action plans implemented either have action plans in development or have firmly embedded the principles of harmonisation, alignment and results in their aid strategies and policies.²³

Table 2: Paris Declaration action plans

Embedded in strategies and policies	Planned	Implemented
DAC Members:		
3	4	16
Australia, US, New Zealand	Canada, Italy, Luxembourg, Portugal	Austria, Belgium, Denmark, EC, Finland*, France, Germany, Greece, Ireland, Japan, Netherlands*, Norway, Spain, Sweden, Switzerland, UK*
Multilaterals:		
1		4
World Bank		AfDB, AsDB, IDB, UNDG/UNDP

Notes:

- * Donors that are members of the Nordic+ group that also have their own agency Paris Declaration action plan
- The IMF was not included in summary statistics in the DAC Compendium as it is not a donor. The IMF supports the Paris Declaration and works within its mandate to promote implementation.

Source: Working Party on Aid Effectiveness and Donor Practices, 2007.

70. It is too early to judge the success of the implementation of these action plans, and beyond the scope of this literature review. However, it is possible to pick out key characteristics of the approaches to putting aid on budget by the donors covered in this review, and provide some illustrative examples.

²² The bilateral agencies were selected as the top ten bilateral donors by volume of ODA in 2006 (OECD, 2007a). From this group, Italy and Spain are not profiled as information was not supplied. Denmark, Ireland and Norway are added to the group profiled, in the interest of learning from the experience of donors that are actively trying to put aid on budget.

²³ In July 2007 the DAC published a compendium of donor reports on their actions to disseminate the Paris Declaration (Working Party on Aid Effectiveness and Donor Practices, 2007). This summary is also reported in the World Bank 2007 *Global Monitoring Report* (World Bank, 2007c).

Behind the consensus

71. As described earlier in this review, there is a broad consensus on the good practice principles of sound budgetary and financial management systems and effective aid management. These principles include putting aid on budget. However, behind this consensus, different approaches by donors to implementing their commitment to put aid on budget are identifiable. Very different experiences of putting aid on budget, both by donor and by country, can also be found, as shown by the Paris Declaration 2006 Monitoring Survey and by the country PEFA assessments. An important factor of these different approaches is the complexity of the concept 'on budget'. Added to this is the fact that there is currently no generally agreed definition for the term 'on budget'.

'On budget' and budget support

72. There is often confusion between aid on budget and budget support.

73. Although it is a fallacy to equate aid on budget and budget support, there is a correlation between the provision of budget support and use of government systems. Donors that consistently provide technical assistance and work through NGOs are less likely to integrate aid with national budgetary systems. Equally, efforts to increase the use of programme-based approaches (PBAs) should entail putting more aid on budget. Within programmatic approaches, the provision of general budget support to the partner government's finance ministry is de facto provision of 'on budget' aid.

74. Furthermore, there are a number of donors that view the greater use of budget support as *the* key instruments for advancing the aid effectiveness agenda and improving aid delivery. The EC, for example, has set out its position clearly in support for the use of budget support:

“Budget support, general or sectoral, should be used for implementation wherever possible: this is the golden rule if aid is to be made more effective, and it should be reinforced.”
(European Commission, 2006d: 8)

75. At the same time, putting aid on budget does not equate to the idea that all aid should be provided as budget support. The Paris Declaration commitment to put aid on budget covers all aid that is disbursed for the government sector, however the aid is executed. The OECD provided the following definition of “disbursements for the government sector” that are monitored for the aid on budget targets for the 2006 Survey:

“The disbursement of ODA in the context of an agreement with the government sector²⁴ including works, goods or services delegated or subcontracted by government to other entities (e.g. NGOs, private companies)” (OECD, 2006b: Definitions and Guidance, 2)

Lack of common agreement on definitions

76. In practice stakeholders (both donors and partner countries) do not always share a common understanding of what type of aid should be on budget and what type of aid should be off budget. For example, there are different views on whether NGO funds should be included in recipient country budgets with some governments reluctant to put aid on budget if they feel that they have no real discretion over that aid.

77. The experience of the Paris Declaration Monitoring Survey revealed the extent of the lack of common agreement on practical definitions. The Survey process allowed country-level interpretation of the Survey definitions and as a result some country groups found it difficult to reach a consensus on some definitions. As different definitions were applied in different countries and it is not transparent which definitions were used where, cross-country comparison of the Survey findings is problematic. The Survey report recommends that tighter guidance is given on all 12 indicators for the next round of monitoring in 2008. Box 8 provides further detail on this.

²⁴ The government sector is defined as: administrations – ministries, departments, agencies or municipalities – authorised to receive revenue or undertake expenditures on behalf of central government. (*ibid.*)

Box 8: Interpretation of Paris Declaration Survey definitions

The Paris Declaration 2006 Monitoring Survey reports that one of the lessons learned is the need for firmer and clearer guidance on the definition and local application of indicators. The Survey reports a particular concern that the 2005 baseline may systematically overstate the progress already achieved in relation to the 2010 targets, as there is a perception that the permitted leeway on definitions allowed donors to place their performance closer to the targets. This leeway in interpretation also means that cross-country comparison of country findings is problematic.

The Survey report detailed the following concerns on the interpretation of definitions:

Indicator 5a: Use of Country Systems

- “For several countries it is not clear that all of the programmes included as using country budget execution systems are accurately described as “subject to normal country budgetary execution procedures, namely procedures for authorisation, approval and payment” (as specified in the Survey’s Definitions and Guidance paper).
- There are also some grey areas affecting the interpretation of the indicator. For example, authorisation procedures that are formally those laid down in the country’s laws and public-sector financial regulations can be subject to a large degree of de jure or de facto delegation, meaning that the “use of country systems” is somewhat nominal. Together, these factors may mean that the numbers overstate somewhat the effective use of country systems.”

Indicator 9: Aid Provided as PBAs

- “It is clear from the survey returns that donors in many countries had some difficulty in accepting the suggested definition of a PBA, and usually National Co-ordinators did not feel empowered to impose a ruling. In a number of countries, a looser set of criteria was adopted on the basis of some degree of consensus, while in some others individual donors were permitted to follow their own definition of a “programme”. In these cases, at least, the true baseline numbers for use of common procedures are lower than those presented in the tables [in the report]”.

One of the twelve recommendations made in the Survey report for the next round of the monitoring Survey, to take place in 2008, is: “Tightening the guidance on all 12 indicators.”

Source: OECD, 2007e.

No common definition of ‘on budget’

78. There is no common understanding on the definition of ‘on budget’. It is an ambiguous term that is often not clearly defined and also is often used interchangeably with other terms such as: ‘reflected on budget’, ‘written into the budget’, ‘captured in the budget’, ‘included in the budget’ and ‘integrated in the budget’.

79. As a result, the precise meaning of donors’ terminology for this area is not always clear and the variety of terms can make it difficult to understand donors’ intentions. For example, donors use a variety of terms in their Paris Declaration action plans when setting out their targets for aid on budget:

Germany – “financial cooperation is **fully reported**.” (Federal Ministry for Economic Cooperation and Development, 2005)

Sweden – “funds should always be **integrated with, and reflected in**, the planning and budgeting process of the partner country.” (Sida, 2006: 7)

United Nations Development Group (UNDG) – “100% **information made available to** national counterparts.” (United Nations Development Group, 2005b)

80. Understanding the use of these terms is important because ‘on budget’ is a complex concept. It refers to the capture of aid at different points of the budget cycle (see the dimension of aid on budget in Box 2, Introduction). Therefore the simple term of aid on budget covers a wide spectrum of experience, with various possible patterns of aid capture.

81. Work by Danida on distinguishing between aid ‘integrated in’ and ‘reflected in’ the budget is very useful to unpacking the concept of ‘on budget’. As elaborated by Danida, the use in the Paris

Declaration of the expression ‘reported on the budget’ (for indicator 3 in High Level Forum, 2005: 9) covers two distinct ways that aid may be captured in the budget:

- a. **integrated in the budget:** aid is integrated with domestic resources and its allocation is by Parliament’s decision-making
- b. **reflected in the budget:** aid appears in the budget for information purposes adding to the overview of the total resource envelope, but Parliament does not have the power to allocate it. (Danida, 2005: 4–5)

Box 9 provides a summary of the Danida definitions.

Box 9: Danida definition of ‘integrated’ and ‘reflected’ aid on budget

First, aid to the public sector may be integrated into the budget together with the partner country’s domestic resources by being part of the general treasury account (whose name varies among countries; in Commonwealth countries it is called the “Consolidated Fund”). In principle, the general treasury account includes all resources that Parliament can allocate in accordance with political priorities, laws, existing agreements, etc. The resources in the general treasury account are in all respects handled within the framework of the budget process [...].

Second, aid may be reflected in the budget. This is the case when the aid funds do not enter the general treasury account and are therefore not available for the decision-making of Parliament over the allocation of resources. This kind of aid can appear in the budget for information purposes only (but will still contribute to giving Parliament an overview of the total available resource envelope). Aid, which does not become part of the general treasury account may be termed “parallel aid” and cannot be disbursed through the ordinary government channels through which the Ministry of Finance finances the spending units.

Contrary to what is true of the integration of [aid] in the government budget, the reflection of parallel aid in the budget tells us very little about the degree to which the aid management is aligned with the partner country systems and procedures. A number of more specific features must be stated in order to clarify this.

Source: Danida, 2005: 4–5.

Reporters and integrators

82. Among the donors the differences in approaches to putting aid on budget can be plotted along a spectrum. At the one end there are donors that advocate supplying information on aid flows to the partner country so that it is ‘reported on’ budget. At the other end there are donors that advocate ensuring aid is ‘integrated on’ budget, with country systems used at each stage of the budget cycle.

83. An example of the first approach is set out by the Millennium Challenge Corporation (MCC). The MCC guidelines for fiscal transparency lay out requirements for reflection without requiring the use of country systems:

“MCC will require that, wherever possible, MCC Program activities are reflected in budget documents of the recipient country. This is to assure that the budget comprehensively provides information on all resources being utilized to achieve public purposes. Reflecting the activity in budget documents does not necessarily mean that MCC resources are managed by existing public expenditure systems.” (Millennium Challenge Corporation, 2006: 5)

84. The MCC guidelines detail that this reflection is made possible by an accounting classification system that is capable of being ‘cross-walked’ to the classification system of the national budget system of the recipient country. (*ibid.*: 7)

85. An example at the other end of the spectrum is Sida. Sida’s interpretation of the Paris Declaration commitment to put aid on budget is:

“In line with the Paris Declaration, Sida shall align to the maximum extent possible with national systems.” (Sida, 2007b: 27)

“As a minimum Sida funds shall always be integrated with, and be reflected in, the planning and budgeting processes of the partner country. In order to achieve this Sida should provide timely, transparent and comprehensive information on resource flows.” (Sida, 2006: 7)

How alignment is measured

86. Danida makes the important point that the reflection of ‘parallel aid’ in the budget does not tell us very much about the degree of alignment of that aid with partner country systems and procedures. Therefore it is necessary for donors to look at each stage of the budget cycle to see how well aid is captured in order to see how aligned that aid is.

87. Donor approaches are varied by the level of detail to which they unpack the concept of aid on budget and how they measure the degree of their alignment with country systems. The Netherlands Ministry of Foreign Affairs has developed a systematic approach to this. The central-level procedural guide or *Track Record* complements the ministry’s high degree of decentralization and is the key assessment tool in selecting the most appropriate choice of aid modalities in partner countries. It unpacks putting aid on budget to three levels of alignment (DEK, 2007). A summary of the Netherlands’ approach is provided in Box 10.

Box 10: Determining an aid modality’s degree of alignment

The Netherlands has a long standing commitment to partner country led approaches to poverty reduction going back to the mid 1990s. This translates operationally into “on-budget where possible, off budget where necessary”. ‘Alignment’ means coordination and integration with the policy and budget process(es) of the partner country. Alignment can be achieved at several levels. The aid modality can be ‘on plan’, ‘on budget’ and ‘on treasury’. Fully aligned modalities are always fully on plan, on budget and on treasury Partially aligned aid modalities are on plan and to the largest extent possible also on budget. However, they are not on treasury. Non-aligned aid modalities are to the extent possible on plan and, if possible, also to a limited extent on budget.

Table 1 is designed to help determine an aid modality’s degree of alignment.

<i>Table 1 – Characteristics of alignment</i>			
<i>Modality is:</i>	<i>Fully aligned</i>	<i>Partially aligned</i>	<i>Not aligned</i>
A. On plan	Yes	Yes	Yes/No
Is the aid modality aligned with PRS(P) or any equivalent governmental programme?	Yes	Yes	Yes/No
B. On budget	Yes	Yes	No
Is the aid modality included in the preparation of the budget by the government?	Yes	Yes	Yes/No
Is the aid modality included in the adoption of the budget by parliament?	Yes	Yes/No	No
Is the aid modality included in the implementation of the budget by the government?	Yes	Yes/No	No
Is the aid modality part of the budgetary control by parliament?	Yes	Yes/No	No
C. On treasury	Yes	No	No
Does the aid modality go through the Ministry of Finance (treasury)?	Yes	No	No
Are existing budget reports used (i.e. no external reports/extra control)?	Yes	No	No

Source: DEK, 2007: 47.

Using country systems

88. Donors vary in their approaches to using national budgetary and financial management systems. Through their endorsement of the Paris Declaration all donors are committed to implementing the good practice principle of aligning with and using country systems. Indeed the OECD has emphasised that putting aid on budget in the fullest sense, that is, including the use of country systems, contains the key drivers of the aid effectiveness commitments and that one of the best ways for donors to improve the effectiveness of their aid is to rely on countries’ own systems:

“The use of country systems involves most of the drivers of aid effectiveness: ownership, capacity development, mutual accountability, alignment, harmonisation and results.”
(OECD, 2005a: 36)

89. The endorsement of the Declaration by over 100 different stakeholders is no mean achievement and as a political statement it shows convincingly the development community's commitment to move the aid effectiveness agenda forward (OECD, 2005b). At the same time and perhaps as a result of the many stakeholders, the text of the Declaration allows for flexibility in interpretation. Blunt and Samneang (2005) have published interesting analysis that shows the room for individual (donor) choice and judgement in relation to the targets that have been set. The following paragraphs draw on this analysis.

90. The Declaration allows for flexibility in interpreting the commitment to put aid on budget in two ways. Firstly, the targets are not supposed to act as a straitjacket, and if individual donors and countries want to set their own (higher) targets, then the Declaration allows for this:

“(The targets) are not intended to prejudge or substitute for any targets that individual partner countries may wish to set.” (High Level Forum, 2005: ¶9)

91. An example of the possible flexibility in interpretation is shown by the US, which endorsed the Paris Declaration and all the commitments and the 12 indicators of progress, but not the procurement and financial management targets. According to the DAC Peer Review of USAID undertaken in 2006:

“The global approach of the Paris Declaration, which focuses on collective donor engagement in meeting the targets, allows the US to be flexible about how much it can contribute, depending on the target.” (OECD DAC, 2006c: 63–64)²⁵

92. Secondly, the Paris Declaration allows for the commitments to be “interpreted in the light of the specific situation of each partner country” (High Level Forum, 2005: 3, ¶13) and includes explicit reference to this in the commitment to the use of country systems:

“Implement, **where feasible**, common arrangements.” (*ibid.*: 4, ¶21)

“Using a country's own institutions and systems, **where these provide assurance that aid will be used for agreed purposes.**” (*ibid.*: 4, ¶17)
[bold added]

93. All donors are concerned with the level of fiduciary risk involved in using country systems. As summarised by one donor, there needs to be assurance that:

“... [donor] funds do not disappear, that the funds become revenue for the partner country that the funds are used for the right purpose, contribute to the desired results and are clearly accounted for.” (Sida, 2005a: 11–12)

94. While some donors hold the view that using the country systems are the best way to strengthen them, others stress that establishing a reliable PFM system in the framework of technical cooperation is a pre-requisite. USAID sets out clearly this latter approach:

“Our ability to rely on country systems will depend directly on the pace at which their systems meet acceptable standards and are reliable. USAID is ready to progressively use ‘strengthened’ financial management systems.”

95. In their approach to implementing Paris Declaration commitment to use country PFM systems (indicator 5a), some donors are working on setting internal targets for the percentage of aid flows that are using country PFM systems (for example, Germany, UNDG). Other donors put the emphasis on continuing to expand efforts to support PFM reform and capacity building in such areas as financial management, auditing, monitoring and reporting. For example, Japan in its *Action Plan for Implementing the Paris Declaration* sets out that:

25 USAID reports on this that: “We support most of the Paris targets subsequently negotiated, except for those relating to country public financial management and procurement systems. The US has important issues with the methodology for defining and assessing quality procurements systems (Targets 5b.i and .ii) and financial systems being reformed (target for 5a.ii). For the same reasons we have a reservation on targets relating to indicator 2. We are working with the DAC to resolve these issues. Broadly speaking, we support the progressive improvement of country systems.” (USAID, 2006b)

“Sound PFM is essential for partner countries to achieve effective resource allocation (including ODA) under their national development strategies/ poverty reduction strategies. However, it is not always easy for most partner countries to establish sound PFM due to their capacity constraints. Therefore, Japan will employ various resources to support those countries which are undertaking PFM reforms.” (Government of Japan, 2005)

Incentives and challenges for donors

96. In exploring donors’ approaches and experience in implementing their aid effectiveness commitments, an important body of work focuses on the incentives and challenges faced by donors.

97. Reviews of progress made on harmonisation and alignment commitments have picked up on a certain ‘disconnect’ between donor HQ policy and donor country practice. A study on the incentives for harmonisation and alignment in aid agencies (de Renzio et al, 2006) picks out this disconnect on three levels: political, institutional and individual. See Box 11 for an excerpt of the main findings of this report as provided in the OECD 2005 *Progress Report on Aid Effectiveness*.

Box 11: Incentives for harmonisation and alignment

A September 2004 study examined how internal incentive systems in both bilateral and multilateral aid agencies influence harmonisation and alignment efforts. At the political level, the efforts and commitment of senior managers in aid agencies to “spread the harmonisation gospel” have sometimes been undermined by such external political factors as donor country politicians concerned with visibility, NGOs and private sector lobbies, and lack of commitment and leadership on the part of partner governments. At the institutional level, decentralisation to country offices has not been matched by a strong coordination and policy support role by headquarters; cumbersome and rigid procedures have made harmonisation as well as alignment more difficult on the ground; and insufficient human and financial resources have been devoted to the harmonisation cause. At the individual level, although agencies are providing increasing levels of training as well as informal incentives (mainly peer recognition), harmonisation and alignment criteria hardly ever feature in recruitment policies, staff performance assessments, and promotion systems. Therefore, the overall picture shows a certain degree of disconnect between high-level declarations and the challenges of providing adequate additional incentives to bring individual behaviour in line with harmonisation and alignment objectives. Staff members often face conflicting signals that can undermine harmonisation and alignment efforts. Some of the common challenges aid agencies face in turning around their incentive systems:

- Enhancing positive incentives and removing negative incentives at all three levels—political, institutional, and individual. An example would be building harmonisation into criteria for promotion or recruitment.
- Strengthening the link between headquarters and field offices so that the organisation as a whole can effectively use the wealth of country-level experience on harmonisation.
- Strengthening existing international mechanisms to make them more effective in the adoption and monitoring of common approaches for harmonisation.
- Ensuring that the high short-run costs of harmonisation and alignment are fully funded.

Source: Reproduced from OECD 2005: Box 17. Incentives for Harmonisation and Alignment.

98. The Paris Declaration includes the commitment for all donors (and partner governments) to: “Reform procedures and strengthen incentives—including for recruitment, appraisal and training—for management and staff to work towards harmonisation, alignment and results” (High Level Forum, 2005: ¶68).

Monitoring and evaluating donor approaches

99. There are a number of initiatives to monitor, evaluate and communicate donors’ performance on implementing the aid management good practice principles. These initiatives, summarised in

Box 12, are important sources of information on individual donor approaches to putting aid on budget. Other useful resources are provided in the Annex C donor profile reference lists.

Box 12: Monitoring, evaluation and dissemination of donor approaches

Monitoring

- Following the Paris Declaration, donors were assessed against the progress indicators and targets at country level, and the Survey report (OECD, 2007e) provides findings on donors' baseline performances.

Evaluation

- The Paris Declaration highlights the importance of an independent cross-country evaluation process. As part of this, under the direction of the DAC Evaluation Network a number of donor evaluations are to be undertaken, looking at the experience of implementing the Paris Declaration in a number of self-selected donor organisations.²⁶ Issues for evaluation include the relationships and links between headquarters and country offices and between bilaterals and multilaterals.

Review

- The Paris Declaration includes the commitment to use existing peer review mechanisms and regional reviews to support progress in this agenda. (High Level Forum, 2005: ¶11) The DAC Peer Reviews are used for reporting on Rome and now Paris commitments. Five Peer Reviews are conducted each year and each DAC member is reviewed approximately every four years. Since 2004 specific questions on the implementation of H&A principles have been introduced and reviewed countries are asked to address this issue. (OECD, 2005: 81) One report called for the Reviews to include a more stringent assessment of compliance with international harmonisation initiatives. (de Renzio et al, 2005)
- The World Bank, the IMF and other multilateral organizations (including the multilateral development banks and the UN agencies) are not included in the DAC peer review. The Multilateral Organisation Performance Assessment Network²⁷ (MOPAN) conducts (since 2003) three annual surveys on selected multilateral organisations to gain better understanding and dialogue and improve overall performance of multilateral organisations at country level. It is not an evaluation; rather it is based on perceptions of MOPAN member embassies or country offices.

Dissemination

- Dissemination of donor aid effectiveness performance is part of the OECD DAC Working Party on Aid Effectiveness communication strategy, which aims "to support and accelerate outreach towards the broad range of development practitioners who are in charge of Paris Declaration implementation". (Working Party on Aid Effectiveness and Donor Practices: 4) Publication of the *Compendium of Donor Reports on Disseminating the Paris Declaration* which provides a summary of trends and individual donor reports. (*ibid.*)
- The annual DAC Development Co-operation Report includes a qualitative summary for individual donor policies and efforts, and in the 2006 Report (published 2007) aid effectiveness, including progress on alignment with country systems, is one of the three agendas covered. The other two were donors' policies and efforts on their commitment to the MDGs and donor policy coherence (OECD, 2007a)
- In addition the World Bank Global Monitoring Report provides an update on the implementation of the harmonisation and alignment actions at the global and country level, and for bilaterals and multilaterals. (World Bank, 2007c)

²⁶ The donors to be evaluated are: Australia, Denmark, Finland, France, Germany, Luxembourg, Netherlands, New Zealand, United Kingdom and UNDP (OECD, 2007b).

²⁷ The network is formed by nine donor countries: Austria, Canada, Denmark, Finland, the Netherlands, Norway, Sweden, Switzerland and the United Kingdom. Further information on MOPAN and the annual surveys is available from the CIDA-hosted MOPAN website: <http://www.acdi-cida.gc.ca>.

SECTION C: COUNTRY EXPERIENCES OF PUTTING AID ON BUDGET

100. The main Aid on Budget study looks at 10 African countries. Five countries are researched to the level of a factual review: Burkina Faso, Ethiopia, Kenya, South Africa and Tanzania. The other five countries are full case studies and free-standing reports: Ghana, Mali, Mozambique, Rwanda and Uganda. The literature review supplements this by profiling six other countries: *African Region*: Botswana, Senegal, *Asian Region*: Bangladesh, Vietnam and *Latin American Region*: Bolivia, Nicaragua. This group of countries was chosen to add to the main Aid on Budget countries, and in particular to add experiences from other world regions. Botswana was chosen for its long record of aid management leadership.

101. The country profiles are presented in Annex D. They have been compiled through desk research of literature and data sources. Relevant material has been found mainly in the documentation of harmonisation and aid coordination efforts at country level. In addition the Paris Declaration Survey provides country-level data for the progress indicators, which includes information on the quality of aid capture, the use of country systems and the predictability of aid for countries. The profiles are part of the platform for the Synthesis Report along with the other country studies. The following paragraphs highlight overall findings from this review of country experiences of aid on budget.

Tightened definitions and standards for assessing aid on budget

102. Standards for assessing the quality of aid on budget have tightened. Assessments over time have different methodologies, indicators and criteria, and the trend has been for the assessment of aid on budget to become more precisely defined and reported back on in disaggregated detail.

103. Past assessments, such as the HIPC AAP for tracking public expenditures, used broad grades (A = all, B = incomplete, C = none) to report back on the assessment of the quality of aid that is on budget and provided a broad definition spanning aid on budget at all of the different dimensions of the budget cycle. As a result, HIPC AAP reports for the quality of aid on budget are general (eg, Bolivia – assessment A: all activities financed by donors are disclosed on the budget; Senegal – assessment B: donor financing is shown in the government budget).

104. The Paris Declaration Survey – the next generation of assessment – has a more specified definition for assessing the quality aid on budget at the different dimensions of the budget cycle. As a result, the Survey findings are more precise (eg, Bolivia – 71% aid is recorded in government budgets, 26% aid flows use country PFM systems and 63% aid is recorded as disbursed on schedule; Senegal – 89% aid is recorded in government budgets, 23% aid flows use country PFM systems and 69% aid is recorded as disbursed on schedule)

Ownership (leadership) of harmonisation and alignment agenda

105. Across the countries, the government ownership (and leadership) of the harmonisation and alignment (H&A) agenda appears to be varied.

106. Some of the countries have translated the Paris Declaration commitments for the country context and are implementing national H&A action plans (Bangladesh, Nicaragua, Vietnam) while others are at the stage of developing such plans (Bolivia, Senegal).

107. In some of the countries there are developed aid coordination mechanisms, based on sector working groups. Government leadership of these fora is variable across countries and within the individual countries across the different sectors.

108. Botswana is considered to be a “compelling and relevant” case study for the ongoing debate on the effectiveness of partnership and coordination mechanisms. Box 13 sets out key elements behind Botswana’s experience of keeping aid predominantly on budget throughout the 1980s and 1990s, a striking exception to the general trend.

Box 13: Keeping Aid on Budget in Botswana

During the 1980s and 1990s many donors moved their aid off budget and the use of parallel systems became common practice. This was largely a reaction to a loss of confidence in the efficiency and the fiduciary standards of partner country public finance management.

However, Botswana was a striking exception to the general trend, and kept aid predominantly on budget throughout the 1980s and 1990s. The elements of Botswana's planning and budgeting system were put in place during the 1970s and have been remarkably durable. Key elements were:

- Successive Finance and Audit Acts made it a requirement that all aid should be paid into a Development Fund (alongside the Consolidated Fund). The Botswana government's own investment funds were also appropriated to the Development Fund.
- Although separate Development and Recurrent budgets were prepared, there were strong links between them. Forward plans were geared to sustainable recurrent cost projections. Ministries had to plan within recurrent cost ceilings, and all projects had to include recurrent cost projections. The planning and budget process was overseen by a strong, unified Ministry of Finance and Development Planning.
- The links between recurrent and development budgets had legislative backing, since the Finance and Audit Act made it mandatory that any project in the development budget had to appear in the National Development Plan. There was a second volume of the NDP that included summaries (including phased expenditures) for all the projects in the Plan. Through the annual budget process it was possible to add to or amend the project list, but the project expenditure ceilings in the Plan could not be ignored.
- The budget classification system, allied to computerised accounts, kept track of sources of funding (including donors) as well as lines of expenditure.
- Although donor funds were routinely earmarked to particular expenditures, the medium term perspective on planning, and the use of sector ceilings (inclusive of aid) ensured that government still had discretion over these funds – because domestic funds could be purposefully allocated to cover what was not covered by donors.
- Moreover, annual expenditures could adjust to the vagaries of donor/project expenditure patterns, because what Ministries could spend on an individual project was related to the multi-year (NDP) ceiling on that project's expenditure. Ministries had to keep to an annual aggregate ceiling on their expenditures, but within that could vary project expenditures above/below the annual estimate.

Thus Botswana had thoroughly integrated aid into all aspects of its public finance management. During Botswana's period of greatest aid dependency, most aid was on plan, on budget, on parliament, on treasury, on accounting and on audit.

Source: Government of Botswana, Planning Officers Manual, Ministry of Finance and Development Planning, June 1986.

Findings of the Paris Declaration 2006 Monitoring Survey

109. All the countries in the literature review set are reported by the Paris Declaration Survey to have baselines in the area of alignment of either Low (Bolivia and Nicaragua) or Low-Moderate (Botswana, Senegal, Bangladesh, Vietnam). (Botswana was not covered in the Survey.)

110. For all the countries covered, the country overall figures obscure the fact that there are significant variations in individual donor performance (for all three indicators).

111. The Survey reports on 2005 data. Therefore effects of reforms since 2005 are not reflected in the Survey findings.

Aid flows reported in government budget estimates

112. All the countries have reasonably high percentages of aid flows reported in government budget estimates: all are above 81% with the exception of Bolivia (71%) and Nicaragua (73%). However, the countries' high overall figures for the percentage of aid recorded in government budget estimates are a factor of over-reporting of some aid flows cancelling out under-reporting of other flows.

113. The Survey reported a number of factors for why aid was not reported accurately on the budget. These are summarised in Box 14.

Box 14: Why aid is not on budget accurately

Donors do not always provided timely information on planned disbursements.	Senegal, Vietnam, Nicaragua
Some donors do not use the same financial year as the government.	Vietnam
The budget may reflect inaccuracies or lack of realism in the estimation of the rate of programme execution and hence spending.	Senegal, Bolivia, Bangladesh
It is a challenge for governments to keep track of expenditures arising from externally resourced projects and programmes.	Senegal
Some aid recorded by donors is channelled through non-government systems. There is a lack of sharing financial information by donors or tracking of this information by government for projects donors finance themselves.	Senegal, Vietnam
Shortage of comprehensive reporting of aid flows within the government (e.g., executing agencies channelling funds directly to lower tiers of government or other public bodies failed to inform authorities about planned expenditures and neglected the established reporting procedures).	Vietnam, Bolivia, Bangladesh

Source: OECD, 2007e – Country Chapters.

Using country financial management systems

114. While the review countries have a range of CPIA ratings for the quality of their financial and budgetary systems, for all the countries the percentage of aid flows that use the national public financial management systems is low.

115. In addition there appears to be little correlation between the CPIA rating and the proportion of aid put through national systems. For example, Bangladesh has the lowest CPIA rating (3.0) in the group and the highest percentage of aid using national financial systems (53%) in the group.

116. Most of the countries (Bangladesh, Nicaragua, Senegal, Vietnam) report that budget support accounts for the majority of the aid flows that use national systems.

117. There is the expectation that the use of country systems will increase as:

- PFM reforms inspire confidence in national systems (Bangladesh).
- An objective of recent work on developing SWAs (Bolivia, Nicaragua).
- The proportion of aid given in the form of budget support is expected to increase (Bolivia, Nicaragua, Senegal).

118. Vietnam specifies that donors and governments need to explore how to expand the use of the national PFM system for non-budget support aid. Nicaragua reports that the low baseline is partly due to the backlog of uncompleted projects that were never designed to be aligned and are governed by donor rules requiring the use of their own systems

Predictability of aid flows

119. All the countries report a predictability gap from two angles: 1) a gap between what donors schedule and what donors report is disbursed, and 2) a gap between what donors' schedule and what governments report is disbursed.

120. For the first, the discrepancy between what donors scheduled and what donors reported to be disbursed was found to vary considerably among donors within countries and was mainly due to late disbursements carried over to 2005 and to delays in implementing programmes (Bangladesh, Nicaragua, Senegal). For the second, the gap between donor scheduled aid and government reports of disbursements was reported to be either because the government was not appropriately notified by donors or because the aid flows were inaccurately recorded by government (Bangladesh, Bolivia, Nicaragua, Senegal).

121. Other factors highlighted included donors not respecting disbursement agreements (Senegal), government not meeting conditionalities for aid mobilisation (Senegal) and weak coordination between donors and government in preparing realistic disbursement plans (Vietnam).

122. The Survey reports stress that closing the predictability gap will require donors and government to work increasingly together on various fronts at the same time, and three main areas for improvement are highlighted:

- The realism of predictions on volume and timing of expected disbursements;
- The way donors notify their disbursements to government;
- The comprehensiveness of government's records of disbursements made by donors.

Trend in PFM assessments (and reform)

123. PEFA assessments are planned (Botswana, Vietnam), are underway (Senegal) or have been completed (Bangladesh, Nicaragua) for all the countries reviewed (apart from Bolivia). Thus there has been a trend in nearly all the countries to using the PEFA framework for the integration and coordination of PFM assessments amongst donors.

124. The scope of this literature review does not reveal the effects of this trend on the design of PFM reform initiatives, whether they are becoming more harmonised as a result of harmonised assessment. This area is being explored by a monitoring impact report on the implementation of the PEFA framework that is currently under way (the draft report is due end 2007). This impact assessment will explore the use of PEFA assessments for dialogue on the need for and content of PFM reforms and related action plans. Given the time-lag of reform implementation and the long-term nature of most PFM reform, it will also take time before the impact of such reform can be measured. As previously noted, PFM reform that has started having an effect 2005 onwards is not covered by the Paris Declaration Monitoring Survey (which uses 2005 data).

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