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Working Party on Aid Effectiveness and Donor Practices

DRAFT GOOD PRACTICE IN PUBLIC FINANCIAL MANAGEMENT: INCREASING THE PREDICTABILITY OF AID FLOWS

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This paper is presented for DISCUSSION at the next meeting of the Joint Venture on Public Financial Management to be held on 17-18 November 2004. It was elaborated by DfID.

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GOOD PRACTICE IN PUBLIC FINANCIAL MANAGEMENT

INCREASING THE PREDICTABILITY OF AID FLOWS

I. KEY ISSUES

1. Predictable development finance is an essential component of both sound macro-economic management and stability and good public financial management, which will contribute to the effective delivery of services. Concerns over unpredictable development finance have been raised by both partner governments and donor officials. The 2003 Rome declaration highlighted that “donor’s practices do not always fit well with national development priorities and systems, including their budget, programme, and project planning cycles and public expenditure and financial management systems. We recognise that these issues require urgent, coordinated, and sustained action to improve the effectiveness on the ground”

2. Increasing the predictability of aid flows is important because:

Existing flows of aid are very unpredictable

IMF research shows that aid is far more volatile than domestic revenue. For the 33 countries in the world where aid accounts for more than 50% of total government expenditure, aid receipts are seven times more volatile than domestic revenue. In addition, regarding reliability of donor pledges, a 72 country study the IMF discovered that project aid assumptions in the budget were 15% higher than disbursement outturns and that programme disbursements were under budget figures by 30%.

Donor commitments in this area were made in Rome in 2003

Multi-year programming of aid – Donors, wherever possible should programme their aid over a multi-year time frame that is consistent with the financial planning horizon of the partner government, and are transparent about the circumstances under which aid flows may vary. The combination of longer term and more predictable finance enables partner governments to have more trust in the reliability of donor finance, this is necessary to plan increases in service delivery capacity, and facilitates macro-economic management.

Provide full information on aid flows - Donors should provide partner governments with full information on aid flows. This should be done regularly and in a timely manner. This enables governments to integrate aid into macroeconomic and budgetary management and to publish details of aid received.

Increasing predictability is closely linked to increasing accountability

3. Increased accountability by donors for the finance they provide and on partner Governments to demonstrate the impact of additional funding will be a strong driver of increased predictability. Parallel efforts by the International Federation of Accountants to develop an accounting standard in the area of development assistance will complement the good practices outlined in this note. The standards will call for increased disclosure and transparency by partner Governments which in turn will drive the provision and dissemination of information by donor agencies. Partner Governments have also noted the importance

of comprehensive and predictable accounting of aid as a means of improving accountability to their own legislature for all public resources.

It will ensure that increasing aid flows are effectively utilised

4. The relationship between good governance and better economic and social outcomes is acknowledged and within governance planning and budgeting is an essential element. Following the Monterrey consensus, indications suggest that the global volume of official development assistance will increase by at least \$16 billion from 2006. This means that many partner Governments will have to plan and budget for significant increases in the aggregate volume of aid they receive. Donors will also face increasing scrutiny by their own constituents to demonstrate that aid has been used efficiently and effectively.

Conditionality

5. The research undertaken for this paper has shown that issues related to the use of conditions are considered to have the most impact on the predictability of aid flows. It is considered that an extensive discussion on conditionality is outside the scope of this paper but it will identify how conditions can be administered in a more effective way to reduce the level of unpredictability.

Links with other Good Practice Papers

6. The imperative of improving the predictability, transparency and accountability of aid are therefore becoming increasingly important. Changes by the donor community will need to be complemented by increasing capacity and capability in PFM by partner governments. The identification of good practices in that area is the subject of a linked but separate good practice paper on capacity building.

7. While there are specific practices which relate to different aid modalities the emphasis of this paper is on all aid modalities. It therefore covers the spread of support from technical assistance provision, project support and the full range of programmatic support. Additional guidance on the PFM implications of Budget support is contained in a separate Good Practice Note.

II. PURPOSE

8. The purpose of this note is to put forward a set of good practices on how donors and partner governments can collaborate to increase the predictability of aid flows and hence strengthen public financial management, increase macro-economic management and stability and hence deliver effective services. In pursuing this goal it seeks to achieve four specific objectives.

- **Provide consistent definitions.** It is important that there is a consistent understanding by donors and partner governments of the status of donor transactions. At what stage and in what way can indicative donor commitments be used by partner governments in their own planning and financial management cycle.
- **Provide information in a consistent and usable form.** Many partner Governments have a wide range of donors providing support in a variety of different formats. The result is often that the partner Government, which often has the least capacity, is forced to manage a portfolio of support, which lacks coherence and where information is supplied in an inconsistent way. More consistent information flows will assist the ability of the partner Government to report fully to its own stakeholders about the resources it has been entrusted with.

- **Creating delivery mechanisms that will support alignment and harmonisation.** There is a tremendous amount of scope for donors to reduce the burdens they place on partner Governments. In this area there is a need to both clarify and agree on common systems of classification, notification and disbursement which will rationalise existing practices.
- **Promote transparency and accountability** Increasing predictability will both promote and be promoted by increased transparency and accountability.

III. GUIDING PRINCIPLES

9. The following principles guide the elaboration of good practices:

1. **Identified good practices cover all aid modalities.** While some of the good practices may apply more directly to some aid modalities, the express intention of this paper is to seek ways of improving the predictability of all assistance.
2. **Alignment** The impact of increased predictability needs to be measured at the country level. Are donor resources planned, budgeted and disbursed in ways consistent with the public financial management systems of the partner. Are proposals consistent with the reform strategy of the recipient? Do changes in donor practices increase or reduce the burden on recipient countries?
3. **Good financial management practices are characterised by predictability, comprehensiveness, transparency and accountability.**
4. **The Ministry of Finance (or its equivalent) has the prime responsibility for the management of public funds.** Improving this function is dependent on ensuring that all donor flows are explicitly captured or recorded within the Government's financial statements. This principle will be expanded in the forthcoming IFAC accounting standard on external assistance.
5. **Operationalising the commitments made in Rome.** A key guiding principle is taking the Rome commitments as a starting point and seeking to identify good practices which best exemplify these commitments. Of critical importance are the two commitments (see Box on page 1) made by donors to programme their aid over a multi-year time frame consistent with the financial planning horizon of partner governments and to provide full information on aid flows.
6. **Good Practices covering the complete budget cycle.** While considerable attention is focused on good practices in budget formulation the credibility of donor agencies is dependent on consistency in budget execution. The good practices therefore set out to cover practices through the budget cycle and this will encompass a range of time horizons. Information for the medium term planning horizon will feed into the MTEF process, information for the forthcoming financial year will feed into the annual budget cycle and disbursement information will be captured within the annual reporting cycle.

IV. GOOD PRACTICES

10. The first four sets of good practices are structured according to the lifecycle of an aid agreement covering pledge, dialogue/negotiation and commitment, minimising in-year variability and disbursement. A further set of good practices cover cross-cutting subjects not related to any one stage of the agreement cycle. A suggested set of indicators is also included. Supplementary material in terms of definitions, suggested disbursement templates and information on the IFAC cash accounting standards are appended.

Pledge

11. Improving predictability will be dependent on a clear and shared understanding of the nature of a pledge, an understanding of the constraints in translating pledges into commitments and the treatment of pledges within a partner Government's financial management system.

12. For most donor agencies there is a distinction between a pledge and a formal commitment. In most cases there is a need for further approval to translate the pledge into a commitment that could be included in a countries formal medium term financial framework.

13. For many donors a pledge can be described as a formal promise of future funding defined as an [overall] indicative financial amount [not necessarily categorised by type of aid]. It may be made at for e.g. a country Consultative Group meeting, or high-level consultation between donor and partner country during sector reviews etc. The pledge has political or moral force and may be heavily conditional. When pledges are communicated to partner governments it is suggested that a minimum set of information is included covering amount; proposed timeline for disbursements, conditions attached and the date by which the pledge will be confirmed. Only when the pledge has been formally confirmed (see below) should it be formally included within a partner government's PFM cycle.

Dialogue/Negotiation and firm commitments

14. Donor agencies need to signal unambiguously and in a timely fashion what may be included in a partner government's budget framework. Where a binding commitment has been entered into this should be clear. Where other pledged amounts or indications of assistance have been the subject of dialogue or negotiation this may require a distinct further action or change of status of the aid transaction. The critical issue is that partner governments have confidence that the information provided is sufficiently robust for them to incorporate in the their annual budget and medium term planning.

Box 1. An approach to budget dialogue - Mozambique

Mozambique Multi Donor Budget Support: The Mozambique MOU for MDDBS outlines the three stages of dialogue that the donors should engage in with the partner government. These three stages are:

(Note: the financial year in Mozambique runs from 1 January to 31 December).

- **Annual DBS Review:** occurring in April, this review is aligned with the Government of Mozambique's (GoM) planning, budget and monitoring cycle. This review provides the basis for the budget support donors to provide indicative commitments for year n+1. The dialogue process (mainly) uses the same documents as those submitted by the GoM to Parliament.
- **Mid-term Review:** this review occurs in September and is the time when the donors provide confirmed commitments for year n+1
- **Budget Working Groups:** these occur four times a year (February, May, August and November) and discuss the budget execution progress during the previous quarter. The working groups are also the fora at which any adjustments to the agreed budget support disbursement schedule are made.

15. In the case of Tanzania, budget support donors notify the Government of indicative amounts for the next financial year (and the three year MTEF) eight months before the start of the financial year. The amount for the next financial year is then confirmed 3 months before the start.

Box 2. Improving projections: the Tanzanian experience

Tanzania has been actively seeking to incorporate multi year commitments within its planning process for some time. The PER process currently forms the analytical basis which supports the government MTEF, MTEF and budget development process. The PER process (PER FY03 Report, World Bank June 2003) has tried to explicitly improve projections by DPs for donor assistance. In particular the External Finance Dept of MoFEP has over the last two years successfully requested DPs, to provide data on budget support, sector support and other grant and loan disbursements and projections of support to the Country. Work is still underway to ensure comprehensiveness of coverage.

This information is then validated (against known information on ongoing plans etc) before being recorded in an Aid Flow Database. This data is then used to assist MoFEP to develop the resource envelope for the MTEF, MTEF and Budget Guidelines.

16. While the examples above are drawn from a budget support context, the previous OECD-DAC Guidelines encourage donors to provide full information on all aid flows in order to enable partner governments to integrate aid into budget management and to accurately report on aid receipts. The IMF Manual on Fiscal transparency also supports the concept of budget comprehensiveness, meaning that all aid, regardless of the modality should be included within the partner government budget.

17. Donors should be encouraged to participate in an annual budget dialogue, giving firm projections for both pledged and committed resources that are expected to be made available both within the PGs forthcoming financial year and in the relevant medium term period and should record the status of the aid transaction (loan or grant) accordingly. Wherever possible, this stage should be linked to the annual performance review of the PRS and so encourage alignment to government processes. This stage would support budget comprehensiveness by including all aid modalities.

V. REDUCING IN YEAR VARIABILITY

18. A significant reason for the variability of aid flows within a financial year can be attributed to the application of conditions. While the application of conditions is likely to remain a key feature of the aid relationship between partner Governments and donors it is important to seek ways to apply conditions in a way that minimises the impact on in-year disbursements.

Box 3. Managing conditions and variability

Multi Donor Budget Support (MDBS) Memoranda of Understanding – The concept of reducing in year variability to zero, in the context of budget support disbursements, is particularly challenging. However, in many of the countries where multi donor budget support operates, the joint memoranda of understanding agreed between the donors and partner governments, do already aim to reduce in-year variability. For example:

- “Budget support donors undertake to avoid, where possible, in-year suspensions of budget support, and allow for dialogue and time for remedial actions where problems arise.” Partnership Framework for Harmonisation and Alignment of Budget Support between the Government of Rwanda and its Development Partners, Nov. 2003.
- “Budget support partners [BSP] (excluding the World Bank and Sweden) will not disrupt disbursement in-year except in the case of a breach of trust caused by the Government of Mozambique failing to fulfil underlying principles of the partnership.” Revised MOU between BSP and GOM, ver. 9. The World Bank is excluded because they decide on disbursement in year n during year n, based on performance in year n-1. Sweden is excluded in order to operate a performance tranche mechanism (70% base tranche, 30% performance tranche).
- “In year cuts will be avoided except in the most serious of circumstances.” Uganda – Operational Principles for Budget Support Development Partners, draft, 2 May 2003.

These case studies demonstrate that steps have already been taken to reduce the extent of in-year variability and the value of the principle should therefore be accepted by donors. In addition, Germany is currently implementing efforts to ensure the “suspension of aid in the current financial year only in exceptional circumstances” (BMZ Spezial, Harmonisation of donor practices in German development cooperation, Action Plan). This is in line with agreed OECD/DAC guidelines which state that “donors should suspend support within-year only in exceptional circumstances that are clearly defined” (p.23, *Harmonising donor practices for effective aid delivery*).

19. Donors seek to ensure that performance related tranches are applied in advance of the financial year to ensure that in year changes in disbursement are kept to an absolute minimum. This would mean that performance related conditions which have an impact on the year t+1 are determined early enough in year t that donors are still able to communicate their commitment for year t+1 in a way consistent with the good practices outlined in the previous section.

20. If agreed conditions have not been met, the performance related tranche would be adjusted accordingly, but in terms of the predictability of funding the partner government would know the precise amount of resources at their disposal in the forthcoming year.

21. The quality of the information supplied to partner governments could be enhanced through the introduction of a donor peer review, which could build on the experience illustrated in Tanzania (see Box 2). This would serve to increase the confidence that partner governments have in both donor pledges and annual commitments.

Disbursement

The evidence on volatility suggest that there is significantly less of a problem on predictability in relation to project aid than in the area of programmatic lending. Delays in project disbursement can be attributed to a range of factors of which weaknesses in project design are a significant feature. Box 4 indicates steps that have been taken by South Africa to improve project planning.

Box 4. Realistic Project Planning

RSA Policy Framework and Procedural Guidelines for the Management of ODA, 1st Edition (October 2003): The government of the Republic of South Africa has drawn up a detailed policy framework and procedural guidelines to assist its staff in the management of ODA. These guidelines include a list of key criteria, which should be used by government officials to check the design of projects. The checklist, which covers eight areas of project design, is a means of mitigating the risks associated with a poorly designed and planned project. The following is a summary of the eight areas of project design covered by the checklist:

- Target group: precisely defined and specified at the right level;
- Development objective: consistent with RSA's development objectives and not too ambitious;
- Principal objective: a single objective that is precise and verifiable;
- Outputs: feasible, precise and verifiable;
- Activities: realistic in time available and appropriate to the situation;
- Inputs: relate directly to the specified activities and precisely defined (quality, quantity and cost);
- External factors: linked to the correct project level, precise and verifiable;

Indicators: means of verification should be available, reliable and up-to-date.

22. In addition to addressing issues around project design, good practice suggests that increased attention needs to be paid to a more realistic assessment of project management, procurement, reporting and other administrative requirements. This also needs to be matched by realism surrounding expectations of progress and disbursement.

23. Where appropriate Donors should provide additional information on the cash disbursement pattern through the year where these deviate significantly from an even rate of disbursement. This is an extremely critical piece of information, which will have a direct bearing on the ability of a country to manage its cash resources during the year. This should be provided on a periodic basis.

Classification

24. This is a technically complex area where action is needed to align donor classification systems with those of partner governments and reduce the use and need for parallel accounting arrangements.

25. Significant progress has been made in this area. Multilaterals now seek to align to existing systems and avoid the creation of parallel or duplicate arrangements, including in the case of the World Bank the flexibility to use partner governments Chart of Accounts.

26. There are a number of ongoing initiatives, which seek to capture data in a comprehensive and consistent form.

Box 5. Mechanisms for aid management

Aid Management Platform for the Government of Ethiopia – Ethiopia is being used as a testing ground for a new initiative (supported by the World Bank, OECD/DAC, Development Gateway and UNDP) aimed at developing an Aid Management Platform. The initiative will provide an ICT aid management solution within the context of an appropriate institutional and procedural framework. It is occurring hand-in-hand with the MoFED's ongoing efforts to improve aid management capacity, including the preparation of an aid policy and strategy document. The AMP consists of five modules with different functionalities:

- **Aid Management:** capture aid flows; capture information on aid at various stages (through inception, implementation and completion); relate use of aid to outputs (e.g. physical progress).
- **Fiscal Calendar:** to help donors to align themselves to Ethiopia's processes; enable coordination of donor missions; identify reviews and reporting requirements; facilitate timely reporting on conditions.
- **What-if Analysis:** enables scenario analysis to determine predictability of aid funding; facilitates application of discount factors determined from past disbursement trends.
- **Knowledge Base:** central store for government and donor documents relevant to harmonization efforts, aid management, SDPRP, PRSC, MTEF, annual budget, conditionality, etc.
- **Reports and Analytics:** Capability to report disbursement by donor, region, sector, beneficiaries, source (bilateral, multilateral, NGO etc); inventory of ongoing projects and forecast of external assistance for next 3 years by donor.

The implementation of the AMP is planned for spring 2005. It will start with the MoFED and donors and then progress to federal institutions and then all regions. The AMP will allow for multiple classifications of information. This means that the GoE and the donors can view data according to their own classification. By this means, the AMP can facilitate the "translating" of one chart of accounts to another.

27. The ongoing work in Ethiopia will seek to capture all aid flows regardless of their modality. It is suggested that the development of any country specific notification template should include the following list of items, covering both forward projections and actual disbursements, which will ensure that all relevant information is captured.

- Type of notification (pledge/commitment/cancellation etc.);
- Point of contact within the PG;
- Point of contact within the donor;
- Details of the relevant aid agreement;
- Modality of aid;
- Currency, amount and timing of projected disbursement in the case of pledge/commitment;
- Disbursement type (cash/in kind etc), amount and currency;

- Details of bank account and who controls it;
- Classification of payment (in accord with IMF-GFS);
- Other provisions, such as provisions relating to interest accrued; provisions relating to unspent amounts at the end of each financial year.

28. A draft aid notification template is attached at Annex2

VII. CONDITIONS

29. The use of conditions will continue to play an important role in both the development of the donor/partner government relationship and in the management of aid flows. Increasing predictability will be contingent on their use in a consistent, transparent and accountable manner. The IFAC Standard proposes that “significant restrictions on access to assistance or conditions on the use made of assistance are summarized and disclosed in notes to the financial statements”.

30. The categorisation of conditions can be extremely helpful providing they are clearly notified and communicated. It is considered helpful to distinguish between conditions which have a bearing on the overall relationship of the donor to the partner government and those which apply to a particular instrument. A suggested division of conditions in to four categories is given below.

Box 6. Categories of conditions

Procedural Conditions: procedural or contractual conditions call for the PG to comply with certain bureaucratic or administrative requirements. Some may be specific to a particular donor and others may be common across donors. This category would include, for example, following specific procurement and auditing procedures, or the stipulated use of a donor agent;

Policy Based Conditions: policy based conditions are linked to certain policy actions or reforms required of the PG. These conditions are typically linked to indicators such as actions and outputs. Good practice suggests policy based conditions should be drawn from the PG’s PRSP in order to ensure that they are owned by the PG;

Macro-economic Conditions: macro-economic stability is normally a pre-requisite of the provision of budget support. It is normally demonstrated by a country being on track with the IMF;

Political Governance Conditions: the exact terminology given to “political governance” conditions varies but they are those conditions that relate to a PG’s commitment to high level good governance, addressing issues such as human rights, democratisation, the environment, gender issues, anti-corruption measures etc.

31. The MDBS arrangement in Mozambique distinguishes between two-tiers of conditions which allows sensitive issues of political governance to be dealt with at the higher level and a different set of conditions will therefore apply to a particular aid instrument.

Box 7. Two tier agreements

MDBS in Mozambique – The MOU agreed between the MDDBS donors and the Government of Mozambique seeks to distinguish between the donors' response to under-performance against indicators and targets in the Performance Assessment Framework (PAF) and their response to serious violations of the underlying principles of the agreement (i.e. political governance concerns). Donors' responses to under-performance against indicators in the PAF are summarised in the individual, bilateral agreements, whereas the political governance principles are outlined in the joint MOU where it states that:

"The GOM is committed to respect for human rights and the rule of law, exercise of democratic governance, sustainable poverty reduction and sound economic management. The GOM is committed to sound implementation of this MoU, including openness to engaging in serious policy dialogue on the key issues within the above areas and within the implementation of its poverty reduction strategies, for which it is accountable to the Mozambican people through the Assembly of the Republic."

The assessment of whether these GOM is fulfilling these principles is undertaken on an on-going basis with decisions made bilaterally. It is only a breach of the underlying principles that should lead to an in-year suspension of aid, although the first response, prior to suspension, should be dialogue between the GOM and the donor[s].

32. The setting of conditions should include early warning systems which will clearly highlight problem areas. This in itself would improve predictability by allowing earlier dialogue and potential resolution before there is a financial consequence.

33. While there are understandable concerns that increased harmonisation between donors could increase overall volatility, the principle of seeking engagement and dialogue with partner governments at an early stage and avoiding in year adjustments where possible will lead to significant improvements in predictability.

Information Flows

34. The breadth of reporting requirements both in terms of timing and coverage together with the capacity constraints within many Ministries of Finance provide a range of challenges, which need to be progressively addressed.

35. Donor information flows should be both consistent with partner government reporting formats and provided on a regular basis with a periodicity that is appropriate.

36. Given that many partner governments still have major capacity constraints it is recommended that multi-contact communication is good practice. It should reflect the different functions of the Ministry of Finance and be undertaken in a way that is supportive and not undermining of existing structures. It should be complemented by initiatives to build capacity in internal communication.

37. As a minimum notifications are therefore copied to the following constituent parts of the Ministry of Finance with additional copies copied to the Planning Ministry, the relevant sector ministries and the Supreme Audit Institution.

38. Key parts of Finance Macro modelling/Planning secretariat

- External relations
- Budget division including relevant sectoral offices
- Accountant General/Treasury function
- Debt management (where appropriate)

39. There would also be major advantages in donors collating this information and sending a joint return into Government, which captures all the relevant information across the donor group.

40. Wider publication of donor commitments and actual disbursements would be an additional way of promoting wider in-country accountability which in itself create n incentive to improve predictability.

41. It is clearly recognised that managing information flows is the prime responsibility of the recipient. However in a transition phase, while capacity is being developed the implementation of the above practices by donor partners would assist partner governments in their management of information.

Indicators of Good Practice in Aid predictability

Good Practices	Success Criteria	Source of Information
Donors make formal medium term commitments which can be included within a partner governments medium term plan.	Partner Government Medium term frameworks incorporate information from all donor partners	Medium term expenditure framework and supporting documentation.
Annual donor commitments captured in the annual budget	Partner Government budget incorporate information from all donor partners	Annual budget and supporting documentation
Donor disbursement of aid consistent with annual commitments	Minimal variation between funds committed and actual disbursements	Actual donor disbursements compared to budget.
Proportion of donor support disbursed in advance of the final quarter of the year	Up to 75% of donor funds received by the end of the third quarter.	Ministry of Finance in collaboration with Central Bank
Proportion of total donor flows captured on budget	Increased proportion of donor flows reflected in the budget	Ministry of Finance in collaboration with Central Bank

ANNEX 1

LIST OF DEFINITIONS

TERM	Definition
Accountability	That decision makers be held responsible for the exercise of authority vested in them. Budget officials and line ministry officials answer for the use of funds and face the consequences of misuse of funds. In the context of this good practice paper improved accountability applies to both donor and recipient government but particularly of the recipient government through enhanced budget comprehensiveness and transparency allowing allocation of resources to meet political imperatives and public and parliamentary scrutiny.
Additionality	The assumption that resources provided by a donor are additional to the planned resources of a government. It is argued by some that, given budget dialogue, donor funds are not or should not be seen as additional to that which the government intended and the term should be avoided. However, donors need to look towards their home public. In that context additionality is useful to demonstrate benefit. Further, in the context of fungibility, donors wish to see spending in priority social and pro-poor areas maintained or enhanced rather than, as a result of aid resources being brought to the sector, the government resources being switched to other purposes.
Alignment	<p>This word is being attributed three meanings (applicable to programme and project aid), of bringing into agreement:</p> <ol style="list-style-type: none"> 1. donors (this good practice paper however, uses the alternative terms coordination or harmonisation in this context); 2. donor support, to be consistent with the development priorities of the country as defined in poverty reduction plans, sector plans etc.; and, 3. linked to the principle of predictability, to place in relation to each other in terms of timing: <ul style="list-style-type: none"> ▪ commitment with the partner government planning and budgeting cycle/process; and, ▪ disbursement with recipient budgeted income. <p>In the context of this good practice paper it is the latter definition that is most relevant, i.e. that a donor notifies a receiving government of its commitments and disbursements for the recipients' planning, budget and accounting periods (rather than its own).</p> <p>In future this alignment may be enhanced by the alignment of the PSRP annual progress report with the budget cycle.</p>
Appropriation	The budget as approved by the legislature for line item of spending. The budget law gives the executive branch the authority to incur obligations, which become due during the budget year up to a specified amount for specified purposes within a financial year.
Budget Support	General programme assistance without specific allocation, e.g. to a sector, programme or project: the financial transfers contributing to closing a budget deficit. Not hypothecated (earmarked) to any type or purpose of expenditure, the modality would normally include budget dialogue and agreed prioritisation, in the context of sector priorities and poverty reduction plans. The (local currency equivalent) funds are transferred into the consolidated fund or general revenue balance of the treasury, or otherwise consolidated, and will be expended using the recipient's allocation, procurement and accounting systems. A medium term budget framework (MTBF) may set out what the government wants to achieve

	<p>and how it will be financed from both domestic and foreign sources. Sometimes a distinction is drawn between direct, general (to be nominally accounted for against certain sectors) and sector (earmarked to discrete sector[s] with conditionality related to the sector[s] and additional reporting) budget support (but see earmarked and programme aid). This form of aid should be most readily aligned to the recipient's budget cycle (given the need for budget dialogue) and most readily captured in the budget process. It should also be the most readily classified, only have broad high-level conditions, have straightforward projections (given the limited number of high value disbursements) and be readily coordinated between donors (again, given the need for budget dialogue). Not all donors are capable of budget support but it is provided by several multilaterals (e.g. WB adjustment lending¹) and bilaterals. It is moot whether DBS should include aid categorised as debt relief given the counterpart funds thus released or be considered as hypothecated programme support.</p>
Commitment	<p>Simply, the placement of a purchase order or signing of a contract or other agreement for the provision of goods, services or works. In the context of aid, a commitment is defined as (DAC extract²) "A firm written obligation by a government or official agency, backed by the appropriation or availability of...funds, to provide resources of a specified amount under specified terms and conditions and for specified purposes... Commitments are considered to be made at the date a loan or grant agreement is signed or the obligation is otherwise made known to the recipient".</p> <p>In addition, for the purposes of this good practice paper, commitment is defined as when aid that has been pledged or under negotiation becomes irrevocable (subject to conditions) through the signature of a contract, treaty, loan agreement, exchange of notes or memorandum of understanding specific to a grant, loan or project. The resources may be included confidently in a recipient's budget (if not already included). Under most donor country systems the "irrevocable" nature of the commitment requires an appropriation.</p>
Comprehensiveness	<p>Simply, the budget and accounts capturing all activities of government. In the context of this good practice paper it implies the need for donors to report on all forms of assistance and for partner governments to capture all resource transfers within financial statement, in accordance with the IMF code of fiscal transparency.</p>
Conditions	[To be developed with typology of conditions?]
Disbursement	<p>(DAC extract) A disbursement is the placement of resources at the disposal of the recipient country or agency, or in the case of internal development-related expenditures, the outlay of funds by the official sector.</p> <p>transactional transfer of funds [flow of fund ?]</p>
Earmarking	The linking of funds to a prescribed purpose where the lack of a separate bank account (or the reimbursement nature of the funding) plus fungibility makes the linking to the particular expenditure purpose notional. Cf. tracking
Fungibility	Where aid pays for something for which the government would otherwise have paid, thus releasing the government funds for some other purpose (and possibly of which the donor or their public may not approve). In helping to close a budget deficit, budgetary support most obviously is

¹ Technically, rather than direct financing to a country's budget, the WB provides external financing.

² DAC Statistical Reporting Directives, DCD/DAC(2000)10.

	supporting the overall budget, but aid directed at a sector equally closes the deficit and may allow the redirection of funds that would otherwise fund the sector. Donor funds are less fungible when linked to policy dialogue, conditionality and agreement on priorities for use of all resources (which may include continuance of government funding at agreed levels within priority sectors – see Additionality). Although presentationally projects may be easier to justify, project aid is also fungible as donor projects in a chosen sector may be offset by lower government funds to the sector. It is argued that project support is more fungible as it usually will not include access to information on sector wide performance, nor provide a forum for policy dialogue. Donor enclave projects may be regarded as not fungible if government would otherwise not have funded them (but questions would remain on ownership and sustainability).
Indicator	A measure of performance
Pledge	A formal promise of future funding defined as an [overall] indicative financial amount [not necessarily categorised by type of aid]. May be made at for e.g. a country Consultative Group meeting, or high-level consultation between donor and partner country during sector reviews etc. The pledge has political or moral force without being a commitment and may be heavily conditional
Predictability	A principle of public expenditure management and linked to the purpose of this good practice note. The extent to which the budget provides a dependable guide to public sector managers. The need to increase the predictability of all aid flows and the accuracy of partner government budgets and all financial statements. Requires alignment of the donor commitments to the budget cycle/process and making disbursements in adherence to commitments and projections.
Project Aid	<p>Development-related investment the purpose and financial allocations of which are limited to a specific period of time. Aid that is intended for a defined project Included here are:</p> <ul style="list-style-type: none"> ▪ Project Support – Funds: Financial aid for a defined project purpose. Used by multilaterals (e.g. WB investment lending) and most bi-laterals and forms the bulk of, for example, the KFW portfolio (98%). May include support to local expenditures. The recipient/implementing agency will usually procure, contract and pay invoices (subject to donor procedures and stipulations). More difficult to align given that timing tends to be dictated by the project cycle rather than budget cycle and more difficult to integrate within the budget and budget execution. The emphasis is on the spending department or implementing agency role and information on projected and actual aid flows has to come from there and is subject to the donor stipulations and release of information. ▪ Project Support –Technical Assistance/Cooperation: A form of aid in kind (expertise / services / consultancy). Similar issues to financial project aid apply but inputs are often contracted directly by the donor without full financial information necessarily being provided to the recipient. It may be mixed with financial (project) support (or indeed be an adjunct to programme aid in the form of capacity building conditionality). It may include a component supplying goods, where there is a cross-over from minor project related supplies (such as a computer or a vehicle) to more significant capital expenditure with a purpose beyond the life of the project (e.g. a computer system or a fleet of vehicles), that may have recurrent budget implications. These issues may be more intractable given the goal and purpose of this good

	practice paper.
Programme Aid	<p>DAC defines programme aid as:</p> <ul style="list-style-type: none"> ▪ General programme assistance – assistance made available to a developing country without specific sector allocation for general development purposes, i.e. balance of payments, budget support and commodity assistance; ▪ Sector programme assistance (hypothecated) – assistance directed to a specific economic or social sector, such as agriculture, education, community development and transportation (includes SWAp). In this category are included both: <ul style="list-style-type: none"> ▪ earmarked funds that, in terms of the mechanics of disbursement, may be indistinguishable from budget support but are earmarked to a sector programme and may or may not have different conditionality to budget support or additional sector specific conditionality and/or monitoring; ▪ trackable funds that through special accounts (basket or otherwise) can be tracked to the sector or purpose within a sector. <p>May be accompanied by capacity building technical assistance.</p>
Sector Wide Approach (SWAp)	<p>An approach or working method, not an instrument. All significant funding for the sector supports a single sector policy and expenditure programme, under Government leadership, adopting common approaches across the sector, and [progressing towards] relying on government procedures to disburse and account for all funds. Most examples are in a transition process where a hybrid of approaches may be contained within a sector, including existing projects. For this reason donor agencies with a technical assistance function (e.g. JICA and GTZ) may be signatories to an MOU, as well as donors with programme funds to disburse (whether or not within the pooled fund arrangements). The definition therefore, encompasses a direction of change: a process of moving over time towards broadening support from all sources of funding, making the coverage of the sector more comprehensive, bringing ongoing projects into line with the SWAp, and developing common procedures and increased reliance on government.</p>
Tracking	<p>The ability to track funds through bank accounts and account movements including currency conversions. “Tracking” implies the ability to track funds via separate accounts through to the achievement of their purpose. The bank accounts give physical separation of funds, not merely crediting separate accounts for separate sources (which could all share a single bank account).</p>
Transparency	<p>(OECD Best Practices for Budget Transparency). Openness about policy intentions, formulation and implementation. Budget transparency is the full disclosure of all relevant fiscal information in a timely and systematic manner. The Best Practices are in three parts:</p> <ul style="list-style-type: none"> ▪ principal budget reports and their general content; ▪ specific disclosures to be contained in the reports; ▪ practices for ensuring the quality and integrity of reports. <p>The IMF Code of Good Practices on Fiscal Transparency stresses its contribution to good governance and importance for macroeconomic stability and growth. The code is based around:</p> <ul style="list-style-type: none"> ▪ roles and responsibilities in government being clear (with a clear legal and administrative framework); ▪ public availability of information (including timely publication); ▪ open budget preparation, execution and reporting; ▪ assurances of integrity.

DRAFT AID NOTIFICATION TEMPLATE

Instructions for Completion

The Aid Notification is prepared by a donor agency for each aid pledge, commitment, budget advice, disbursement transaction, and cancellation. Copies are sent to all officers in the receiving country who have responsibilities with regard to aid, such as the planning agency, external relations agency, budget agency, accounting and treasury, and debt management.

The date of the notification is relevant to countries keeping their accounts on a cash basis: payments made by a donor on behalf of a recipient are counted as cash receipts according to the date of this formal advice.

It is used for all modalities of aid.

Its purpose is to provide the recipient with all the information that originates with the donor agency (HQ or country office) and that is needed by the recipient for comprehensive accountable management. It is consistent with the good practices identified in the Framework for Donor Cooperation (Rome Declaration, February 2003).

Line 1: This informs the recipient whether the notification is about a pledge, budget advice, commitment, actual disbursement or a cancellation of an earlier commitment. A pledge is an indication of future funding, typically made at a Country Consultative Group meeting, which is not regarded as a legal commitment. A budget advice is notice of the resource available for budgetary purposes, whether pledge (but shortly expected to be committed), a new commitment or confirmation of previous commitment, sent at the start of the recipient's budget cycle to assist in macrofiscal planning. A commitment is a firm written obligation, typically made in a grant or loan agreement. A disbursement is a payment by the donor that is counted toward its commitment. A cancellation is a formal withdrawal from a commitment, for stated reasons. Tick one of the five boxes.

This line also informs whether the notification is about development assistance or humanitarian assistance (tick one box).

Line 2: The donor agency enters its name and contact details in case any queries arise.

Line 3 identifies the agreement partner (government or NGO), and the implementing agency.

Line 4 specifies the Agreement under which the aid is given. Serial numbers may be given to a series of transactions under a single Agreement, so that the recipient can ensure that all notifications are received and processed. The aid may be by way of loan or grant (tick the appropriate box) and it may be intended for use on current expenditure (such as operating and maintenance) or on capital expenditures (tick the appropriate box). These classifications conform to IMF-GFS classification of loans and grants received.

Line 5 applies to multi-year pledges and commitments. Fill in the recipient's financial year and the amount pledged or committed for disbursement in each year. The currency is the currency used by the donor agency. [It is not considered practical for the donor to make conversions to the recipient's currency].

Line 6 identifies the modality of aid. General budget support is aid that is not allocated (earmarked, hypothecated) to any particular sector, programme or project. Sector/programme support is allocated to

particular economic sectors or programmes. Investment project support is allocated to particular projects and is usually (but not necessarily) trackable by having its own bank account. Technical assistance (technical cooperation) is project support that is allocated to human resource capacity building. Tick one box.

Line 7 applies to donor disbursements. Disbursement may be made: (1) directly to the recipient's bank account; (2) as payment to a supplier, contractor or consultant on the recipient's specification and authorisation; (3) the donor may transfer resources in kind, such as vehicles and equipment, without attributable payment. The distinction between 2 and 3 is important, as the draft IFAC standard 'Accounting for Development and Humanitarian Assistance by Recipients' (paras. 20-21) requires a government using a cash basis of accounting to disclose only 1 and 2 as cash receipts, but not 3. Nevertheless, resources in kind can be valued at their fair values, and it is regarded as good practice for governments to disclose the full cost of their programmes irrespective of the disbursement type. Tick the appropriate box and enter below the amount and currency.

Line 8: Enter details of the receiving bank account and who controls the account. According to the draft IFAC standard, the date of receipt of cash is the date of notification that it has been credited to an account controlled by the recipient.

Line 9: Where the donor makes a payment on behalf of a recipient, though the recipient normally authorises the payment it does not know what amount has been paid or when. This notification provides the recipient with information on the details of the payment on which the expenditure can be brought to account. Note that the functional classification is the UN standard 'Common Functions of Government', which is used by all countries reporting their government finance statistics to IMF. It differs slightly from the OECD-DAC sector codes.

Line 10 is optional for a donor agency to add any relevant information or explanation.

Add the full list of parties to which the notification has been distributed.

IFAC Draft Exposure draft
Accounting for External Assistance –
Draft IFAC Standard for Recipient Governments that keep their Accounts on a Cash Basis

AID NOTIFICATION

				Date	<input type="text"/>		
				Ref.	<input type="text"/>		
1. Notification of:	Pledge	<input type="text"/>	Budget Advice	<input type="text"/>	Commitment	<input type="text"/>	
	Disbursement	<input type="text"/>	Cancellation	<input type="text"/>			
	Development Assistance	<input type="text"/>	Humanitarian Assistance	<input type="text"/>			
2. From:	Agency/fund	<input type="text"/>			Focal point name	<input type="text"/>	
	Country	<input type="text"/>	Telephone	<input type="text"/>	Email	<input type="text"/>	
3. To:	Agreement Partner	<input type="text"/>			Beneficiary Country	<input type="text"/>	
	Implementing Agency	<input type="text"/>					
4. Under Agreement:	Title	<input type="text"/>			Date	<input type="text"/>	
	Description	<input type="text"/>				Serial No.	<input type="text"/>
	Loan	<input type="text"/>	Grant	<input type="text"/>	Current	<input type="text"/>	
					Capital	<input type="text"/>	
5. Amount and Phasing: (pledge or commitment only)	Currency	Total	Fin Year	Fin Year	Fin Year	Fin Year	
	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	
6. Modality:	General Budget Support	<input type="text"/>	Sector/Programme Support	<input type="text"/>			
	Investment Project	<input type="text"/>	Technical Assistance	<input type="text"/>			
7. Disbursement Type and Value:	Cash to Recipient	<input type="text"/>	Payment on Behalf of Recipient	<input type="text"/>	Aid in kind	<input type="text"/>	
	Amount	<input type="text"/>	Amount	<input type="text"/>	Value	<input type="text"/>	
	Currency	<input type="text"/>	Currency	<input type="text"/>	Currency	<input type="text"/>	
8. Receiving Bank: (direct cash only)	<input type="text"/>						
	Controlled by Donor	<input type="text"/>	Controlled by Recipient	<input type="text"/>			
9. Classification of Payment on Behalf of Recipient or Aid in Kind	(a) Economic Classification		(b) Functional Classification				
	Compensation of employees	<input type="text"/>	General public services	<input type="text"/>			
	Purchase of goods/services	<input type="text"/>	Defence	<input type="text"/>			
	Interest	<input type="text"/>	Public order and safety	<input type="text"/>			
	Buildings and structures	<input type="text"/>	Economic affairs	<input type="text"/>			
	Machinery and equipment	<input type="text"/>	Environmental protection	<input type="text"/>			
	Other (explain)	<input type="text"/>	Housing & community amenities	<input type="text"/>			
	Recipient's Account Classification (if known)	<input type="text"/>	Health	<input type="text"/>			
			Recreation, culture & religion	<input type="text"/>			
			Education	<input type="text"/>			
			Social protection	<input type="text"/>			
10. Other Information or Explanation:	<input type="text"/>						

Signature:
Distribution:

This standard is intended to lay the basis for the future provision of historical data on all assistance to recipient countries and is therefore fundamental to all good practices in aid effectiveness. The GPP should refer to and support the standard.

The draft standard currently covers development and humanitarian assistance. The draft does not require pledges to be reported, even in the notes to the financial statements. They are regarded as not binding. While the GPP recognises the importance of pledges as a basis for further dialogue and negotiation between donors and partner governments it clearly states the need for these to be translated into formal commitments, which can be relied upon by partner governments.

The Good Practice Paper covers all forms of aid delivery, including in-kind delivery of aid. The draft standard also covers in-kind aid. Where the aid is counted as 'Payments by Third Parties' it is brought to account (based on the costs incurred by the donor) and shown in a separate column of the Statement of Receipts and Payments. All aid in kind is valued at its domestic fair value and disclosed in the Notes to the Financial Statements.

Payments by third parties are recognized when the recipient is formally advised by the donor that the payment has been made or has verified the payment in some other way. The Aid Notification template in Annex 2 provides one mechanism to capture these transactions.