Decentralization Support Activity Project

The DSA project is implemented by Harvard University and funded by Development Cooperation Ireland (DCI), The Royal Netherlands Embassy and the United States Agency for International Development (USAID).
The DSA Project is providing technical assistance to the Government of Ethiopia’s Civil Service Reform in budgets, accounts and budget planning. The DSA Project is implemented by Harvard University and funded by Development Cooperation Ireland (DCI), the Netherlands Minister for Development Cooperation, and the United States Agency for International Development (USAID). The Project is currently in its fourth phase which runs from July 1, 2004 to November 30, 2006.

This brief is structured as follows:

(a) what are the objectives of the reform and what are the problems it addresses

(b) what is the project’s strategy of reform

(c) what is the scope of the reform

(d) what are its main technical achievements to date

(e) what are its deliverables to date

(f) what are its scheduled deliverables by the end of phase 4

What are the objectives of the reform and what are the problems it addresses

• The three objectives of the Budget, Accounts and Expenditure Planning reforms are:
  
  ▪ to strengthen the capacity of the public finance management system to manage public sector financial transactions;

  ▪ to improve the capacity of public sector managers to use information about financial transactions to permit better control;

  ▪ to develop, on the ‘platform’ of better accounting and financial management and control systems, better planning of the public sector so that budget allocations are driven by policy.

• The reasons that such a reform was required is as follows:

  ▪ the structure of the existing government accounting and budgeting systems does not provide an adequate technical base on which to improve the allocation of public resources;
conditionalities of creditors (IMF, World Bank) require new features of financial management (e.g. consolidation of federal and regional budgets, details of pro-poor expenditure);

requirements of new aid modalities such as budget support require budget planning that presents changes in sector allocations as well as prompt financial reporting;

modernization of public sector financial systems is a major requirement for countries that wish to improve their credit ratings and attract foreign investment;

the devolution of public sector finances imposes significant new pressures on public sector financial management that the existing system could not cope with. If devolved units of government are to have more discretion over their spending decisions, the financial management systems must be able to provide an enhanced reporting and control platform that permits better planning of public resources within a strong information and control framework.

What is the project’s strategy of reform

Proper sequencing of the financial reform is absolutely critical to success. Figure 1 presents the project’s strategy of financial management reform in terms of sequence and content. The first task is to get the financial transaction platform (budget, accounting, disbursement systems and their supporting computer systems) operating smoothly to ensure efficient financial control. An efficient transaction platform also provides the timely budget and accounts data for the policy/performance platform. The policy/performance platform has three objectives: (1) to shape budgetary allocations by policy, (2) to introduce accountability for financial resources and results, and (3) to promote efficiency.

The DSA strategy of financial reform accords with international best practice of sequencing budget reform.1 The first sequence is to ensure efficient control which has been achieved by improving the transaction platform. Once effective control is established the second sequence is to introduce management which is efficiency and performance of allocation and this is being developed with the policy/performance platform as well as the legislative platform. At this stage in Ethiopia’s financial reform it is not appropriate to introduce the third sequence of financial reform—planning which involves sophisticated program budgeting and full accrual accounting.2

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The first step in the project’s strategy of financial reform was to improve the transaction platform specifically, to bring inputs of an activity together across the capital and recurrent budgets by cost center through a new budget classification and chart of accounts. Once the inputs of an activity are aggregated it is then possible to take the next step of specifying outputs and performance criteria annually and over the medium-term. In accounts, the project assisted the government in clearing a six year backlog to less than one year and reducing monthly expenditure reporting in regions to two months. The introduction of the modified-cash double-entry bookkeeping system combined with widespread training and automation has achieved these objectives.

The project’s approach to reform in Ethiopia has been to pilot a reform first and only roll it out to other jurisdictions once the pilot has been well-tested and improved upon through experience. A second principle has been to develop reforms that can be used across jurisdictions to promote coherence and integration. A third principle has been to empower government staff to do the reform and not substitute them with technical assistance staff. These are fundamental reforms and if they are to be sustained they must be managed by government staff. The reforms have been piloted in the SNNP region and then ‘cascaded’ to other regions. The SNNP pilot demonstrates that regional finance staff can manage these demanding reforms. Still, the scarcity of qualified finance
staff who can be made available consistently over time to manage these reforms is a significant challenge. The experience of the reform has demonstrated the wisdom of these project principles. While this approach may take longer in the ‘front-end’ pilot stage, wide-scale extension of the reforms (the ‘back-end’ stage) can be rapid and relatively smooth. With ‘second stage’ financial devolution to weredas which have limited capacity in financial management, a pilot approach has been critical to ensure that these systems are appropriate at this level of administration.

What is the scope of the reform

- The reform is designed to integrate all elements of public sector financial management and planning into a coherent framework, sequenced in a way that is compatible with the implementation capacity of the different levels of government.

- The reform is designed to work at all levels of government: federal, regional, and sub-regional.

- This is an integrated reform composed of three components: Accounts and Budgeting on the one hand, and Planning on the other. These components are supported by an integrated financial information system (IFMIS) and an extensive in-service training program.

What are its main technical achievements to date

**Accounts and Budgeting**

- *design and implementation of a completely new Chart of Accounts*
  A Chart of Accounts is the foundation of any public finance system. It permits accounting (the management and recording of financial transactions) and allocation decisions (what should public money be spent on?) to be integrated and related to government priorities. This reform involved a complete overhaul of the financial system and took several years to complete. All subsequent reform activities derive from the Chart of Accounts.

- *development of a new budget classification*
  On the basis of the new Chart of Accounts the structure of budget in relation to the (changing) structure of government was fundamentally overhauled, and the process is still going on in the regional roll-outs and ‘second stage’ financial devolution to weredas. The new Budget Classification adheres to international standards (e.g. Classification of Government Functions—COFOG, Government Financial Statistics—GFS) as well as the financial data requirements of international development partners (e.g. the Joint Budget and Aid Review--JBAR, Fiduciary Assessment).
• **reduction of the backlog in accounts**
  Timeliness is a necessary characteristic of useful financial information. Information that is not timely has very limited use for decision-making. When the project began, the government accounts were six years in arrears. Financial reports for EFY 1983 were issued in EFY 1989. The project documented the existing accounting system and developed a training program for accountants at all levels of government. Currently, the backlog in accounts is less than one year and three of the four largest regions are currently able to report monthly expenditures (including all weredas) within two months.

• **development of a new accounting system**
  The new Chart of Accounts provides the framework for a new accounting system. In addition, the modernization of the accounting system involves a fundamental change to the way transactions are recorded, so that a more complete picture of expenditures can be provided. In particular, the accounts reform has introduced double-entry modified-cash accounting system in place of the previous single-entry cash accounting system (meaning that full information will be available on commitments of cash as well as actual spending of cash).

• **development of management accounting**
  The project has designed a management accounting system which is based on the requirements of the federal government, the four large regions, and development partners. Management accounting improves planning and management and meets the data requirements of development partners (e.g. JBAR, Fiduciary Assessment, Budget Support, PRSP).

• **federal disbursement system**
  The federal government has introduced a new zero balance disbursement system. The project has developed software to meet the demands of the new system and it is envisioned that this method of disbursement will eventually be introduced to regions.

• **single treasury pool**
  To improve public financial management the project developed a single pool system that redefined how the government disbursed, accounting and reported funds. The single pool accords with international best practice of a single treasury system (STS) which means that treasury funds are managed through a single bank account and all accounting and reporting is done at a single location. The system has improved the efficiency and effectiveness of reporting, the use of scarce human resources, service delivery, improved cash management and has tightened control across sectors. The introduction of the single pool has been a major factor in ensuring that weredas are able to submit monthly expenditure reports promptly (within two months).
• **nation-wide consolidated budget and accounts**

The Budget Classification system has been standardized across jurisdictions and with the automated budget and accounting systems permits the rapid nation-wide consolidation of budgets and accounts. A key conditionality by the IMF is the preparation of a nation-wide consolidated budget. A consolidated budget permits development partners who are moving to budget support to monitor sector allocations in both the budget and accounts.

• **development of new technical systems for reporting and expenditure management**

*Improved transactions management requires improved reporting:*-

- a new computerized Budget Information System (BIS) has been developed for the preparation of the budget, and is continuously being improved for use by federal, regional, and sub-regional governments. A BIS is critical in a devolved state, so that the budgets from all jurisdictions in the country can be consolidated for macro management purposes. The computer system has several features: it operates in multiple local languages, it facilitates the preparation and production of the annual budget documents, it produces the budget notifications, and it provides the baseline budget and adjusted budget for the disbursement and accounting computer system (BDA).

*Improved transactions management requires better ways of disbursing and accounting for government resources:*-

- the computerized Budget Disbursement and Accounting (BDA) system has been significantly upgraded in order to manage the disbursements of the Treasury Department and all accounting transactions and reports;

- the BDA facilitates the management of the new double-entry accounting system and also allows the consolidation of single and double-entry accounts.

- the BDA enables federal and regional treasury offices to maintain accounts and disbursements against an up-to-date adjusted budget which ensures budgetary control.

The project has developed a significant upgrade of the BIS/BDA systems with the introduction of the Integrated Budget Expenditure (IBEX) system. IBEX incorporates and extends the functionality of the BIS/BDA systems and meets the international standard of an integrated management information system (IFMIS). IBEX also significantly expands the technical platform of the current financial systems and is of international standard. IBEX has an open architecture, operates on the MS SQL Server database, uses third party security software (‘Siteminder’) and is web-enabled which allows it to operate on both local and wide-area networks. Once the
government’s WEREDANET WAN is operational, IBEX will provide the
government with the capability to manage budget and accounts on a real-time basis
at all levels of government.

Planning

- development of more effective ways to plan public resource utilization in a devolved state.
The characteristics of the country’s planning systems have changed from sectoral to
spatial systems (block subsidies from the federal government to the regional
governments and now block subsidies from regional to wereda governments). This
single fact informs the need for and design of, the planning reform. The Chart of
Accounts has been designed in such a way as to provide maximum flexibility in
designing the methodologies and structures of public sector planning.

The main components of the planning reform are:-

- The development of a new Financial Calendar. The Financial Calendar defines the
  sequences of planning and the obligations of the different departments of
government within that sequence. It is the critical link between planning and
  budgeting.

- Improvement of the macroeconomic planning systems, within the Macroeconomic
  and Fiscal Framework (MEFF). The MEFF is a rolling three-year projection of fiscal
  aggregates the first year of which defines the upcoming fiscal year’s revenue,
  expenditure, and deficit target.

- Development of a wereda block grant system. ‘Second stage’ financial devolution to
  weredas required a transfer system for giving block grants to weredas which are
  now the principal level of service delivery. The project developed a needs-based
  unit-cost transfer formula which has greatly improved the equity and efficiency
  of allocations to weredas. This new transfer system has also provided the basis of
  introducing performance into wereda level allocation as well as medium-term
  expenditure planning.

- Introduction of performance budgeting. The project has introduced performance
  agreements in the SNNP weredas which require them to prepare by sector
  performance objectives and targets in advance of the receipt of their block grants.
  The performance agreements also require weredas to present a three-year plan of
  sector allocations. Other regions are adopting this methodology. The project is
  also starting to introduce performance budgeting in federal ministries.

- Development of regional competitive economic strategies. The regional Bureaus of
  Finance and Economic Development have the responsibility to coordinate
  economic strategy as well as manage public finances. The Project conducted in
  the SNNP region a pilot study on regional economic competitiveness with the
objective of promoting policy driven allocation and better coordination of region-wide economic development.

- Integrating sectoral development perspectives with integrated area planning. This should change the way Sectoral Development Programs (SDPs) are made, influence PRSP methodologies, and develop new ways of planning within weredas.

**In-Service Training Program in Financial Management**

- **development of a training strategy**
  The project has extensive experience in designing and implementing in-service training in financial management. In September 1997 the project developed a program for delivering in-service training in financial management. This program was endorsed by the Prime Minister and the cabinet and additional funding was provided to the project to implement the program. The strategy was based on building a partnership of regional (Regional Management Institutes) and federal (ECSC) training institutions to deliver the in-service training.

- **development of training materials**
  The project has developed a comprehensive set of training materials which are based on the budget and accounting procedure manuals. These materials have been translated into Amaregna, Oromiffa and Tigrigna.

- **implementation of the training strategy**
  The project has trained 41,771 government staff in financial management and an additional 22,221 are scheduled to be trained over the balance of the current phase.

**What are its deliverables to date**

The following are the achievements to date of the project in assisting the government’s reform:

- new cost-center budget system operating in the federal government, the four large regions, one small region (Beneshangul/Gumuz), and one administrative area (Addis Ababa)

- new accounts system operating in the federal government, three large regions, and one administrative area (Addis Ababa)

- automation of budget and accounts in 62 federal public bodies, at regional and zone levels in the four largest regions, at the regional level in one small region (Beneshangul/Gumuz) and at one administrative area (Addis Ababa).
upgrade of the BIS/BDA system to IBEX and introduction of IBEX in the Ministry of Finance and Economic Development and Addis Ababa

implementation of all of the budget planning components in the SNNP region and partial implementation in Amhara and Oromia regions.

What are its scheduled deliverables by the end of phase 4

By the end of Phase 4 the following activities are to be delivered:

- All federal public bodies, regions, and administrative areas operate the new cost center budgeting system.
- All federal public bodies, regions and administrative areas operate the new double-entry bookkeeping system and modified-cash basis of accounting.
- A budget planning system which promotes policy and performance based allocation of public expenditure fully operating in the federal government, one pilot region and underway in other regions.
- A financial reporting system is introduced in the federal government, regional governments, and administrative areas.
- Performance measures (objectives and targets) introduced in the budgeting system of the federal government and select regional governments.
- Management accounting operates in select regions.
- An appropriate disbursement and cash management system (including a single treasury system) operates in the four largest regions and their sub-regional governments.
- The budget and accounts systems are automated:
  - in all regional and zonal finance institutions (of the four large regions), at BOFEDs in the small regions, in the BOFEDs and sub-cities of the two administrative areas and select federal public bodies
  - at all administrative levels including weredas in the finance institutions of the four large regions using the new Information and Communications Technology (ICT) infrastructure (if it is operational in these regions).
- The disbursement system is automated in regional finance institutions.
- An additional 28,502 staff trained in the budget, accounts and budget planning reforms bringing the total number of government staff trained over the life of the project to 64,000.
- The procedures and management of these systems institutionalized in government.