



**ADDIS ABABA UNIVERSITY**

**COLLEGE OF DEVELOPMENT STUDIES**

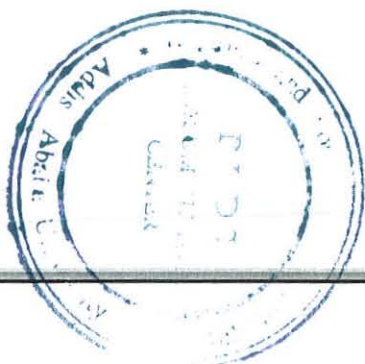
**INSTITUTE OF REGIONAL AND LOCAL DEVELOPMENT STUDIES**

**A COMPARATIVE STUDY OF PUBLIC EXPENDITURE MANAGEMENT IN  
TIGRAY REGIONAL STATE: CASES FROM BUREAU OF AGRICULTURE AND  
RURAL DEVELOPMENT AND BUREAU OF EDUCATION**

**A Thesis submitted to Addis Ababa University, in partial fulfillment for the Degree of Master  
of Arts in Regional and Local Development Studies.**

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## TABLE OF CONTENTS

	<u>Page No.</u>
Acknowledgement_____	i
Table of contents_____	ii
List of Tables _____	v
List of Figures_____	vi
Acronyms _____	vi
Abstract _____	viii
CHAPTER ONE – INTRODUCTION _____	1
1.1 Background_____	1
1.2 Statement of the Problem_____	3
1.3 Objective of the Study_____	4
1.3.1 General Objective_____	4
1.3.2 Specific Objectives_____	4
1.4 Research Questions_____	5
1.5 Research Design and Methodology_____	6
1.5.1 Research Design _____	6
1.5.2 Research Methodology_____	6
1.6 Type of Data and Collection Instrument_____	6
1.7 Significance of the Study_____	8
1.8 Scope of the Study_____	9
1.9 Limitations of the Study_____	9
1.10 Organization of the Study _____	9

CHAPTER TWO – CONCEPTUAL FRAMEWORK AND LITERATURE	10
2.1 Introduction	10
2.1.1 Requirements of Public Expenditure Management	12
2.1.2 The Role of Budget	13
2.1.3 Cash Management	16
2.1.4 Expenditure classification	17
2.1.5 Chart of Account	17
2.1.6 The Accounting and Reporting System	18
2.2 Countries' Experiences	24
2.2.1 Introduction	24
2.2.2 Malawi	24
2.2.3 Guina	27
2.3 Public Expenditure Review in Ethiopia	28
2.3.1 Resource Allocation in Tigray Regional State	31
2.3.2 Economic Contribution of Agriculture Sector Bureau in Tigray	32
2.3.3 Economic Contribution of Education Sector Bureau in Tigray	32
2.4 Linking of Sector Level Policy, Planning and Budgeting	33
CHAPTER THREE – EMPIRICAL DATA ANALYSIS AND DISCUSSION	36
3.1 Introduction	36
3.2 Characteristics of Respondents	36
3.3 Expenditure Planning, Approved Budget and Actual Utilization	37
3.3.1 Agriculture Bureau Recurrent Budget Execution	41
3.3.2 Agriculture Bureau Capital Budget Execution	44
3.3.3 Education Sector Bureau Capital Budget Execution	45
3.3.4 Education Sector Bureau Recurrent Budget Execution	47
3.4 Evaluation of Financial Utilization and Physical Performance	50
3.5 Management of Donor's Fund	51

3.6 Estimation of Revenue and Collection	54
3.7 Procurement System	55
3.8 Accounts Record and Reporting System	56
3.9 Internal and External Auditing	58
CHAPTER FOUR - CONCLUSION AND RECOMMENDATION	61
4.1 Conclusion	61
4.2 Recommendation	64
References	68
<u>Annex</u>	
Annex –A Questionnaires used for data collection	72
Annex _B Checklist of focus group discussion	77
Annex _C Checklist of Interview	78
Declaration	78

## List of Tables

	<u>Page No.</u>
1.1 Distribution and Characteristics of Respondent _____	7
1.2 Participants of Focus Group Discussion and Interview by their Position____	8
2.1 Charts of Account of Federal Government of Ethiopia_____	17
3.1 Budget Request, Allocation and Actual Spending (2003-2006) _____	41
3.2 Recurrent Budget Vs Expenditure By Expenditure Category _____	42
3.3 Capital Budget Vs Expenditure By Source Of Finance _____	45
3.4 Capital Budget Vs Expenditure by Sector (2003-2006)_____	48
3.5 Budget Vs Expenditure Funded By Donors(2003-3006) _____	52
3.6 Actual Revenue Collection Of The Bureau(2003-2006)_____	55

## List of Figures

	<u>Page No.</u>
2.1 Accounting Cycle _____	19
3.1 Agriculture Bureau Recurrent Budget and Actual (2003-2006) _____	43
3.2 Agriculture and Education Bureau Capital Budget and Actual _____	47
3.3 Education Bureau Recurrent Budget and Actual Expenditure _____	45

## List of Acronyms

ACT	Actual
ADB	Africa Development Bank
BOARND	Bureau of Agriculture and Rural Development
BI	Budgetary Intuition
BUD	Budget
BoFED	Bureau of Finance and Economic Development
COFOG	Classification of the Functions of the Government
CABRI	Collaborative Africa Budget Reform Initiative
DSA	Decentralization Support Activity
DFID	Department For International Development
EMCP	Expenditure Management and Control Program
FDRE	Federal Democratic Republic Ethiopia
GFS	Government Financial Statistics
GDP	Gross Domestic Product
IMF	International Monetary Fund
Ke/BeMa/2	Capital Budget Mastaweqya/2
Me/BeMa/2	Medebegna Budget Mastaweqya/2

MTEF	Medium Term Expenditure Framework
MDG	Millennium Development Goal
MEFF	Macro-Economic and Fiscal Framework
MoFED	Ministry of Finance and Economic Development
MoPED	Ministry of Plan and Economic Development
MoF	Ministry of Finance
NGO	None Governmental Organization
OECD	Organization for Economic Cooperation and Development
PER	Public Expenditure Review
PEM	Public Expenditure Management
PEP	Public Expenditure Program
PRSP	Poverty Reduction Strategy Paper
PASDEP	Plan for Accelerated and Sustained Development to End Poverty
SAS	Statement of Audit Standards
TARI	Tigray Agricultural Research Institute

## *Abstract*

*One of the principal objectives of the developing countries is to accelerate the pace of social and economic development. However, the over all effort to achieve this development objective has remained an elusive and difficult task. This is so partly due to lack of financial resources, problems of resource allocation and inefficient utilization of the resources in the public sector.*

*Effective and efficient public expenditure management has remained to be one of the serious problems often encountered by the sector bureaus of Tigray regional government. The core essence of the problem lies in the way the strategic and annual plans are formulated, the different components of budgets are allocated and utilized, physical and financial performances are evaluated and reported as well as inefficiencies related to systems of monitoring and control.*

*This study attempts to analyze the case by considering the performance of the Tigray Region Agriculture and Rural Development Bureau and Education Bureau based on Modified Cash Based Accounting System introduced since 2003. Accordingly, the analysis in this study covered, among others, resource allocation between recurrent and capital budget by source of finance, the pattern of expenditure in relation to the priorities expressed in the 3-5 years strategic plan of the sector spanning the period 2003-2006 as well as the effectiveness and efficiency of auditing and procurement procedures and systems in place.*

*The study revealed that the execution capacity of capital budget for both sector bureaus has been low during the period under review. Moreover, in both sector bureaus, the financial management system especially with respect to off setting budget allocated from loan and assistance and regional and federal governments lacked clear and transparent reporting system. As a result, the report on budget utilization does not reflect the actual budget utilized during a fiscal year, as it does not capture the expenditure components related to loan and assistance provided in cash or in kind or by way of technical assistance from donors.*

*Information gap on the budget approved at the federal level, lack of qualified human resource and the absence of effective internal audit function are among the factors for the constraints in the execution of capital budget and prevalence of weak financial management.*

*Strengthening the management information system, arrangement of local and foreign training for building the capacity of staff, ensuring participatory approach during the preparation of annual plans and working with higher government officials for possible arrangement on information flow with respect to approved and released budget are the major recommendations of the study.*

***Key terms: Strategic Planning, Source of Finance, Medium Term Expenditure  
Management, off Budget Fund, Cost Center***

# CHAPTER ONE

## INTRODUCTION

### 1.1. Background

There is a consensus in developing countries that economic development is an urgent priority. However, the task to bring economic development has remained an elusive and difficult one. This is so partly due to inadequate financial resources and low level of investment in these countries. The financial resources are in scarce supply to meet ever increasing social needs and population growth. The availability of financial resource is constrained by difficulty of generating the required level of saving out of low level of per capita income and economic growth. Therefore, given limited resources and increasing demands, it is paramount to improve resource allocation through proper economic policy and expenditure management (Getachew, 2005).

The Ethiopian economy is predominantly agricultural with about 85% of the population being directly dependent on it for their livelihood. The sector contributes about 50% to the GDP, generates about 90% of export earnings and supplies about 70% of the country's raw material requirement for large and medium sized agro-based industries (PASDEP, 2006). Yet, however, the sector remains to be predominantly agrarian with low productivity.

The government has taken various measures aimed at changing the structure of the economy and encouraging rapid economic development. Such measures include the adoption of poverty reduction strategy that is built on Agricultural Development Led Industrialization (ADLI), Justice System and Civil Service Reform and Capacity Building. The Civil Service Reform Program encapsulates the following five components:

- Top management systems
- Human resource management
- Service delivery
- Ethics
- Expenditure Management and Control Program(EMCP)

The main objectives of the EMCP are to bring about institutional and structural changes in public expenditure management to improve both its strategic and technical components. EMCP consists of the following components:

- a) Development and adoption of a new financial legal framework;
- b) Basing planning and budgeting on a medium term macroeconomic and fiscal framework;
- c) Reform of the budgeting system; and
- d) Improvement and capacity building in the accounting and auditing systems(FDRE, 1999).

The Government's Medium Term Expenditure Framework (MTEF) is contained in the Expenditure Management and Control Program (EMCP) component of the reform program. The sub-program is envisaged to improve the management of resources for enhancing sustainable economic growth and reduce poverty (FDRE, 2003).

The framework attempts to link expenditures with policy priorities and budget realities. It also links policy-making, planning and budgeting, reflecting government's capacity and willingness to prioritize expenditure programs thereby integrating the top-down resource envelope with the bottom-up sector programs (World Bank, 1998).

To this end, a sector development program approach has been developed to overcome numerous problems encountered in the expenditure managements of sectoral bureaus.

In line with the regional government civil service reform program component pertaining to expenditure management and control program, both Agriculture and Education sector bureaus have introduced since 2003 a new accounting system called Modified Cash Based Accounting. Various other measures also being taken aimed at improving the public expenditure management practice. However, there are still a number of constraints that need to be surmounted for enhancing public expenditure management pertaining to the activities of the bureaus.

This paper, hence, attempts to identify, assess and analyze the constraints encountered by the bureaus during the period 2003-2006 and puts forward recommendations that help for enhancing the efficiency of public expenditure management.

## **1.2. Statement of the Problem**

According to (BoFED, 2002), it is a critical problem that the public expenditure management of Tigray has no multi-year planning, which encompasses the whole government activities, sectoral development and poverty reduction programs. There are no criteria for determining inter-sectoral resource allocation. Significant part of budget is not only treated as an annual budgeting exercise, but also it lacks standardized preparation to estimate recurrent and project costs. These conditions indicate that budget is decided on the basis of inadequate information, often without sufficient knowledge of programs and performances.

Tigray Regional Government has introduced a new financial and budget reform that superseded the single entry accounting system since 2003

The reform has aimed to replace the former control function of the accounting and budgeting system by a new system that provides management information while still performing the control function. Discussion held with concerned officials and experts of pertinent bureaus revealed the absence of any study to address any problem faced during the implementation of public expenditure management at both sector bureaus.

Even though the region has been undertaking different reforms to solve the conflict between successful expenditure management systems remains a continuous problem of the region. The expenditure planning and budget reform projects are unable to deliver the systems that effectively perform policy review processes; proper budget approval; utilization of resources and reporting process.

Moreover, discussion held with concerned officials and experts of pertinent bureaus revealed the absence of any study to address any problem faced during the implementation of public expenditure management in both sector bureaus.

### **1.3. Objective of the Study**

#### **1.3.1 General Objective**

The general objective of the study is to examine the effectiveness and constraints of public expenditure management in the Bureau of Education and Bureau of Agriculture and Rural Development of the National Regional Government of Tigray.

### **1.3.2 Specific Objectives**

The specific objectives of the study are:

- To assess if the budget preparation process is participatory in the bureaus;
- To evaluate the effectiveness of capital and recurrent budget allocation and utilization;
- To analyze the effectiveness of the bureau's recording and reporting system in line with recently based on the introduced cash based accounting system;
- To evaluate the impact of the new PEM on the internal audit system in both bureaus;
- To assess if the PEM has resulted in efficiency on the procurement system; and
- To identify major drawbacks and explore possible ways for surmounting the drawbacks

### **1.4. Research Questions**

The following are the core research questions addressed in this study:

- Is the budgeting of the bureau prepared following participatory approach?
- How the allocation and execution of capital and recurrent budget are effectively performed?
- Does the procurement system in place allow for effective and efficient use of public funds?
- Is the overall auditing system is adequately described?
- Is the existing accounting system suitable for providing integrated, timely and reliable financial information to decision makers and concerned stakeholders?

## **1.5 Research Design and Methodology**

### **1.5.1 Research Design**

Following the endorsement of the research proposal, a set of research questions that help to probe into issues related to public expenditure management for both Bureau of Education and Bureau of Agriculture and Rural Development of Tigray Region were set out. This was followed by identification of possible data sources. Considering the limitation of resources (time and money) and possibility of access and availability of data, only two bureaus, namely Bureau of Education and the Bureau of Agriculture and Rural Development are selected.

### **1.5.2 Research Methodology**

The methodologies adopted for this research are as described below:

## **1.6 Type of Data and Collection Instrument**

Both qualitative and quantitative data were generated. Primary and secondary sources were used as input for the study. Secondary data were collected from both bureaus for the period of 2003-2006. Primary data were generated using questionnaires, focus group discussion, personal observation and interview.

### **a) Primary Data Sources**

The primary data sources were purposely-selected informants from the Bureau of Agriculture and Rural Development, Bureau of Education, Bureau of Finance and Economic Development (BOFED) and the General Audit Bureau of the Regional Government.

## Sample Size and Techniques

The next step was the determination of the number of respondents from each sector bureaus. Since they are limited numbers of qualified personnel under these sectors, a total sample size of 54 respondents was selected for the study. Fifteen each from the Agriculture and Rural Development Bureau and Education Bureau were purposely selected to fill in the questionnaire designed for relevant primary data, four for focus group discussion and two for interview from each sector bureaus. From the total respondent 16 females and 38 males was considered for the study. The distribution and status of respondents is shown in table 1.1 and 1.2.

**Table 1.1: The Distribution and Characteristics of Respondents**

Organization	Position of respondent				Level of Education			Sex	
	Expert	Team leader	Department head	Total	Diploma	BA	MA	Male	Female
BOFED	2	3	1	6	2	3	1	4	2
Agriculture	17	3	1	21	5	14	2	16	5
Education	17	3	1	21	3	15	3	14	7
General audit	4	2	-	6	-	5	1	4	2
Total	40	11	3	54	10	37	7	38	16

Source: Survey data 2008

Table 1.2 Participants of Focus Group Discussion and Interview by their position

Position in the Bureau	Education Bureau		Agriculture Bureau		Audit Bureau		BOFED	
	FGD	Interview	FGD	Interview	FGD	Interview	FGD	Interview
Account's Team Leader	1		1		–		1	
Budget expertise	2		2		–		2	
Procurement Team Leader		1	–	1	–			1
Department Head	1		1		–			1
Team Leader of internal audit		1		1	–		1	
Expert and Team Leader of General Audit Bureau	–		–		4	2	–	
<b>Total</b>	<b>4</b>	<b>2</b>	<b>4</b>	<b>2</b>	<b>4</b>	<b>2</b>	<b>4</b>	<b>2</b>

Source: Survey data 2008

## b) Secondary Data Sources

The secondary data sources mainly included financial proclamation and regulations issued by the federal and Tigray Regional Governments. More ever strategic plan of the regional government, four years (2003-2006) annual budget performance, annual reports as well as financial manuals were used.

## Data Analysis

Percentages, graphs, ratios, etc were used in the interpretation and analysis of quantitative data generated.

## 1.7 Significance of the Study

The researcher believes that this study could serve as input for concerned decision makers and executive organs for further improve the public expenditure management system in the agriculture and Education bureaus. It also provides for further research in the field area.

## **1.8 Scope of the Study**

This research examines how financial and budget management are implemented in the Tigray Regional Government Agriculture and Rural Development and Education Bureau for the period spanning from year 2003 to 2006. The assessment focused on recurrent and capital budget utilization by source of finance, management of donor's fund, efficiency of the internal control and procurement system and measures required to attain the desired effectiveness in implementation of public expenditure management.

## **1.9 Limitation of the Study**

Non-availability of series data and information from the under review bureaus have their own limitation on the findings and recommendations of the study. The analysis covered a period of only four years (2003-2006). Since the time period covered is too short, the findings could have been more conclusive had it been possible to use a time series data with more span of time.

## **1.10 Organization of the study**

This thesis is organized into four chapters. The first chapter is the introduction, which consists of background of the study, statement of the problem, objective of the study research questions, scope and limitation of the study. The second chapter discusses the conceptual and theoretical framework of the study. The third chapter presents major discussion and findings of the study. Chapter four contains the conclusion and recommendations of the study.

## CHAPTER TWO

### CONCEPTUAL FRAMEWORK AND LITERATURE REVIEW

#### 2.1 Introduction

The Expenditure Management and Control Program (EMCP) aims to improve the financial management system of the country. This will be achieved through the establishment of a new legal framework for expenditure management control; rolling-out of budgeting, accounts and procurement reforms; modernization of the cash management system; strengthening of internal and external audit; and development of a medium term planning system. Although the ground work for the EMCP sub-program has been laid by the government treasury fund and with the support of other donors under the Decentralized Support Activity (DSA) project

Public expenditure management (PEM) refers to the management of public resource expenditure encompassing fiscal and other expenditure channels. PEM is the macroeconomic management of public revenue used to acquire resources. (Rechard Alen, 2001)

According to this definition, PEM is the way by which public resources are allocated and utilized. PEM is a new approach to an old problem. The problem is the allocation of public money through collective choice. For more than a century, public money is allocated through budgeting. Budgeting is the routines and procedures devised by governments to decide the amounts spent, balance between revenue and expenditure, and the allocation of funds among public activities and entities. (Rechard Alen, 2001)

PEM includes all the components of a country's budget process both "upstream" (preparation and programming) and "downstream" (execution, accounting, control, reporting, monitoring and evaluation). In addition, it includes the legal

and organizational framework and arrangement for forecasting revenues and expenditure, formulating medium term expenditure frameworks, linking the budget to policymaking, preparing the budget, managing cash and monitoring expenditures, performing internal control and managing assets (Mokoro,2000).

PEM operates through budget decisions, but differs in two important ways from conventional budgeting. First, it supplements the conventional procedural rules with substantive policy norms. That is in addition to the application of the right procedure, PEM strives to achieve the desired policy outcomes. Second, PEM covers a broad range of institutional and management arrangements, not just those traditionally associated with budgeting (World Bank, 1999). Moreover, conventional budgeting operates through accepted procedural norms, while PEM emphasizes substantive outcomes. These outcomes pertain to (a) total revenue and expenditure, (b) the allocation of resources among sectors and programs, and (c) the efficiency with which government institutions operate (Salvatore Schiavo-Compo and Daniel Tommasi, 1999).

Public expenditure management is a key instrument of government policy. Public expenditure management is instrumental in nature. There is a necessary distinction between the expenditure policy question of “what” to be done, and the expenditure management question of “how” it is to be done. The three goals of policy translate into the following three key objectives of good public expenditure management (Salvatore Schiavo-Compo and Daniel Tommasi, 1999).

1. Fiscal discipline (expenditure control)
2. Allocation of resources consistent with policy priorities (strategic allocation)
3. Good operational management

### 2.1.1 Requirements of Public Expenditure Management

Public expenditure management requires:

- A greater focus on performance
- Adequate links between policy making, planning and budgeting
- Well-functioning accounting and financial management

Since 1980s, there has been a growing interest in the quality of public sector expenditure management in developing countries (World Bank, 1997).

PEM was associated with the Medium Term Expenditure Frameworks (MTEF) approach to budgeting. These frameworks attempt to strengthen the link between planning, policy-making and budget in the budgeting cycle. Conceptually, MTEF are the ideal tool for translating Poverty Reduction Strategy (PRS) into public expenditure programs within a coherent multiyear macroeconomic and fiscal framework (World Bank, 1998).

MTEF is developed to overcome some of the weaknesses of the limited planning horizon of the traditional annual public sector budget. Long-term planning would ensure fiscal discipline and improve the link between a government's priorities, as agreed in its Poverty Reduction Strategy Paper (PRSP), and the allocation of its financial resources. It also assumed that an MTEF would ensure the adequate planning of recurrent capital spending implications. (Alison Evan and Malcolm Homs, 2003)

A key distinguishing feature of an MTEF is the integration of policy, planning and budgeting within a medium term perspective. An MTEF typically consists of a top-down resource envelope consistent with macroeconomic stability and broad policy priorities and a bottom-up estimate of the current and medium term cost of existing national programs and activities and an iterative process of decision-making that reconciles these costs with available resources. (Alison Evan and Malcolm Homs, 2003)

MTEF process is represented in the following three steps:

1. Estimate total available resources for the public sector over a multi-year period, usually within a multi-year macroeconomic and fiscal policy framework.
2. Estimate the actual cost of government policy and programs by sector in a multi-year context.
3. Reconcile the information in steps 1 and 2 to align policies with available resources, and using this information as a basis for improved policy and funding choices, and ultimately improved outcomes. (World Bank and Korea Development Institute, 2004)

### **2.1.2 The Role of Budgeting**

The term budget is used to mean a plan for financing an enterprise or government during a definite period, which is prepared and submitted by a responsible executive to a representative body whose approval and authorization are necessary before the plan may be executed (Hyde, 1992). The government budget represents a plan/forecast by the government of its expenditures and revenues for a specified period. Budgeting could be conceived as a process for systematically relating expenditure of funds to accomplish planned objectives (Schick, 1992). Budgeting is not solely a matter of finance in the narrow sense. Rather it is an important part of government's general economic policy. It is a strong instrument in implementing the long term, medium term, and annual administrative and development programs.

Budgeting involves different tasks on the expenditures and revenue sides of government finance. On the side of expenditure, it deals with the determination of the total size of the budget (i.e. total amount of money for the year), the size of outlays on different functions, and the magnitude of outlays on various activities. On the revenue side, it involves the determination of the size of the overall

revenue and foreign aid. Furthermore, budgeting also addresses the issue of the budget deficit (i.e. the excess of outlays over domestic revenues), and it is financing (Premachand, 1983).

In Premchand (1983), it has been indicated that the purposes of budget serves as a tool of accountability and management, as an instrument of economic policy and as a type of legislation and political exercise. Especially, budgeting as an instrument of economic policy has function that is more important. It indicates the direction of the national economic growth, fair distribution of income and efficient allocation and utilization of resources. Budgeting also serves to promote macro economic stability of the country through fiscal policy. This means, government use taxation, government expenditure and borrowing to achieve economic growth, full employment, price stabilization and fair income distribution. In short, modern budgeting system has three functions – allocation, stabilization and distribution function (Premachand, 1983).

#### **a) Budget Preparation**

Budget planning and preparation are the heart of good public expenditure management. In keeping with the three key objectives or PEM, the budget preparation process should aim at:

- Ensuring that the budget fits macroeconomic policies and resource constraints;
- Allocating resources in conformity with government policies; and
- Provide conditions for good operational management. (Potter and Diamond, 1999)

Annual budget preparation (as well as any expenditure program) may be organized following top-down or bottom-up approaches:

A **top-down approach** consists of defining aggregate resources available for public spending over the planned period (derived from a sound macroeconomic framework); establishing sectoral spending limits that fit government priorities and; Notifying line ministries of these spending limits, early in the budget process

A **bottom-up approach** consists of formulating and costing sectoral spending programs for the planned period within the given sectoral spending limits; and Iteration and reconciliation mechanisms for eventual overall consistency between aims and availability.

#### **b) Budget Execution**

A major challenge that has been faced by many African countries is to enhance the credibility of the budget by reducing the gap between planned and actual spending. According to the PEFA framework, a well-performing public financial management system ensures that the budget is 'implemented in an orderly and predictable manner and there are arrangements for the exercise of control and stewardship in the use of public funds. Poor budget execution can undermine fiscal policy, distort allocations and undermine operational efficiency (CABRI,2008).

Budget execution is the phase when resources used to implement policies incorporated in the budget. A well-formulated budget can poorly implement, but a badly formulated budget cannot be implementing well. Budget execution procedures must ensure compliance with the initial programming, but they are not simply mechanisms for ensuring compliance. Successful budget execution depends on numerous other factors, such as the ability to deal with changes in the macroeconomic environment, the implementation capacities of the agencies concerned, and the problems met in program implementation.(Rechard Alen, 2001).

### **c) Budget Implementation**

Budget implementation is the primary concern to ensure the fulfillment of the financial and economic aspects of the outlays (Premchand, 1983).

### **d) Adjusted Budget**

Adjusted budget means the appropriated budget adjusted for addition to and/or reductions from the appropriated budget. The adjusted budget is the benchmark for budget control, as an item of expenditure must not exceed its adjusted budget (MoFED, 2007)

## **2.1.3 Cash Management**

Cash management has two functions. First, it ensures that borrowing is well within the specified limits and, second, to ensure that interest on debt minimized. Both of the two aspects neglected because of the practices of debt management, as well as the lack of consciousness of the cost of interest in government. Cash management has the following purposes: controlling spending in the aggregate, implementing the budget efficiently, minimizing the cost of government borrowing, and maximizing return on excess operating cash balances. Control of cash is a key element in macroeconomic and budget management (Rechard Alen, 2001).

Efficient cash management is having the right amount of money in the right place and at the right time to meet the government's obligations in the most cost-effective way.

### 2.1.4 Expenditure Classification

Classifying expenditures is important in policy formulation and identification of resources allocation among sectors; for ensuring compliance with legislative authorizations for policy review and performance analysis; and for day-to-day administration of the budget. Expenditure classified in different ways for different purposes, such as; for administration of the budget and budgetary accounting; and for presentation of the budget to the parliament. (Rechard Alen, 2001). There are four major functional classification of expenditure: Administrative and General, Economic, Social, and others.

### 2.1.5 Chart of Accounts

Chart of account is an accounting terms. A chart of account is a listing of the titles of all the accounts in a ledger and their related account code numbers.

**Table 2.1 Chart of Accounts of Federal Government of Ethiopia**

Major Category of Account		Account Code Range
Revenues	Domestic revenue	1000-1799
	External assistance	2000-2999
	External loan	3000-3999
Expenditures		6000-6999
Assets		4100-4999
Liabilities		5000-5599
Net Assets, Equity or Consolidate Fund		5600-5699

Source: MoFED Budget Manual, 2007

## 2.1.6 The Accounting and Reporting System

### a) Accounting System

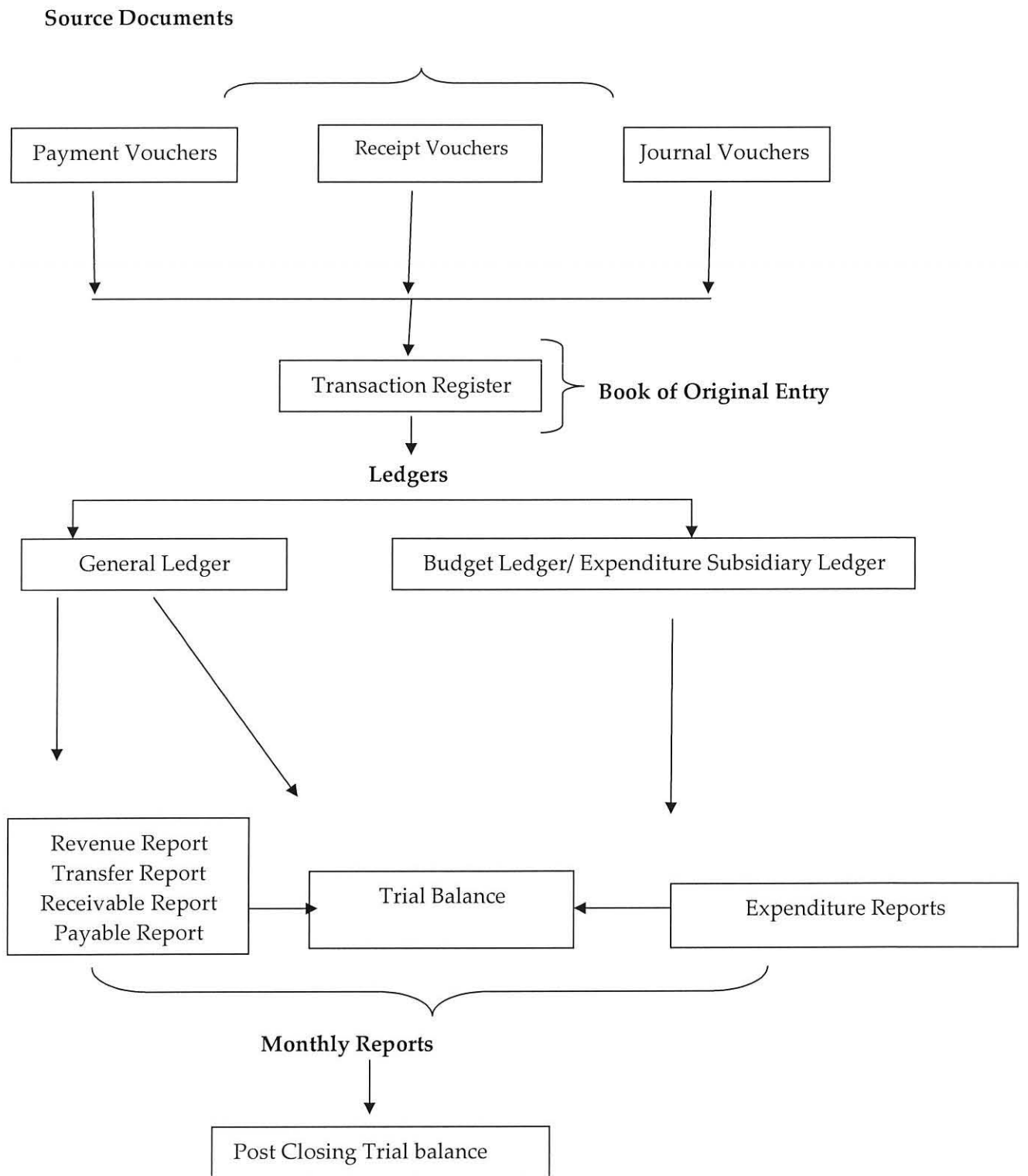
Accounting system means the series of tasks and records of an entity by which transactions are processed as a means of maintaining financial records. Such systems help to identify, assemble, analyze, calculate, classify record, summarize and report transactions and other events. The accounting system was established to mirror the budget format in order that actual spending compared to what was budgeted (SAS, 2004).

Tigray Regional Government adopted the general ledger and the modified cash base accounting system. The process that maintains budget control over expenditure is included in the description of the accounting system. Accounting for transactions must be:

- Authorized by the appropriate authorities
- Captured when they occur
- Recorded in the accounting system
- Summarized by account
- Reported to the appropriate authority
- Source of Finance:

The diagram below provides an overview of the accounting cycle used by the region

Figure 2.1 Accounting Cycle of Tigray Regional Government



Source: (MoFED, 2007)

## **b) Payment Received for Budgeted Expenditure**

Government funds are the primary source of domestic expenditures. Bureau of Finance and Economic Development (BoFED) transfers funds monthly to the executive organs such as bureaus, agencies, commissions and offices based on requests made by the government organs.

## **c) Source of Finance**

The source of finance of any expenditure is either domestic or external. There are two domestic sources of finance: Treasury and Retained Revenue. There are also two external sources of finance: Assistance and Loans. All expenditures must be linked to the source of finance (BOFED, 2002).

The bureau also receives cash for budgeted expenditure in a variety of other ways depending on the source as follows:

- Retained revenue is revenue earned and collected directly by the bureau that allowed keeping and expending for its own purposes.
- Assistance is provided by various donors using one of three channels:
  1. Channel One: some donors provide assistance through BoFED. These funds requested and distributed from BoFED to sector bureaus like government funds.
  2. Channel Two: some donors provide assistance directly to the concerned bureau. These funds requested and distributed from the donor to the bureau in a manner prescribed by the donor.
  3. Channel Three: some donors provide assistance without cash movement. The donor maintains control over these funds. When a budgeted expenditure incurred, the donor pays the invoice directly to the provided on behalf on the sector bureau.

- Loan: donors provide loan funds using channel one or two.
- Aid in Kind: any goods received by a sector bureau as assistance or loans considered as payments received by a sector bureau to meet expenditure (BOFED, 2002)...

#### d) Commitment

Commitment is a way of marking off part of the budget that has not yet spent but that is obligated for a specified expenditure. After the approved budget, the Budgetary Intuition (BI) may enter into contract of issue purchase orders. These obligations to spend money are treated as commitments; that is, before the good or service is ordered and before the payment is actually made, the amount of the purchase order is subtracted from the BI's approved budget. A commitment is a tool that prevents overspending by identifying amounts committed to pay for items that have been requested but not yet ordered and to determine the budget that is available (uncommitted) for expenditure. No further spending approval if the uncommitted balance reduced to zero or if budget is not available to meet planned expenditure, Commitments are budgetary control device (BOFED, 2002).

Each time a commitment is made, as evidence by any one of the source documents mentioned below, it is taken to the appropriate person to ensure that the commitments are recorded in the budget ledger card and to obtain confirmation that there is an available budget to meet the expenditures. The appropriate person records the commitment and signs the source document as evidence of recording the commitment in the budget ledger card and confirming the budget is available for spending (BOFED, 2002)..

Pro forma invoice, Purchase Order, A contract, a support letter or minutes of a meeting, used through Journal, suspense payment voucher, and payment voucher are important and mandatory support documents to record commitments (BOFED, 2002).

### e) Reporting System

For each bank account, an accounting unit provides to prepare a complete set of monthly report and bank reconciliation includes all of the following:

- Revenue/Assistance/Loan report The Report provides information by item of revenue of the year-to-date revenues for the Reporting Unit.
- Expenditure Report provides information on the year-to-date expenditures of each BI by source. The purpose of the Expenditure Report is to facilitate consolidation of the actual expenditures and comparison of budgeted expenditure to actual expenditure.
- A receivable is an amount owed to the bureau or to a BI by another BI, a person, or a non-government entity.
- Transfer report. The purpose of the Transfer Report is to facilitate verification and reconciliation of cash transfers between BoFED and a Reporting Unit and vice versa.
- Payable report the purpose of accounts payables are payables that result from exchange transactions by the bureau. When the bureau receives either a good or a service before paying, the amount owed is an accounts payable.
- Trial balance including the bank reconciliation for each bank account unit The Trial Balance is the summary of the net cumulative debit and credit balances contained in the General Ledger at the end of each month for each account code represented by a General Ledger Card.

- Bank Reconciliation is the process of comparing the bank statement with the books of account is known as reconciling the bank account, and the schedule that is prepared to demonstrate the results of the comparison is called bank reconciliation (MoFED, 2007).

#### **f) Internal Control and Internal Audit System**

Internal Control is an integral component of an organization's management processes which are established in order to provide reasonable assurance that the operations are carried out effectively and efficiently, financial reports and operational data is reliable, and the applicable laws and regulations are complied with so as to achieve organizational objectives.

Control is defined as any action taken by management to enhance and to achieve the established objectives and goals.

Internal control system means all the policies and procedures (internal controls) adopted by the management of an entity to assist in achieving management's objective, safeguarding of assets, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information. Statement of Auditing Standards (SAS, 2004).

Internal audit provides an independent and objective consultancy service specifically to help line management improve the organization's risk management, control and governance. The service applies the professional skills of internal audit through a systematic and disciplined evaluation of the policies, procedures and operations that management put in place to ensure the achievement of the organization's objectives, and through recommendations for improvement. Such consultancy work contributes to the opinion which internal audit provides on risk management, control and governance (Institute of Internal Auditors, 2001).

## **2.2 COUNTRIES' EXPERIENCES**

### **2.2.1 Introduction**

Public expenditure management is applied differently in different countries. However, the underlying goal has always been to improve the quality of public services and the effectiveness of allocation and administration system. However, such benefit of public expenditure management has not been fully captured by many developing countries due to the absence of effective local public expenditure management.

In Africa Region the recent study of Public Expenditure Review's (PERs), noted that the notion of a PER is somewhat fluid and the form, content, and process of preparation vary widely (Smoke, Paul 1997).

The study found:

- Little evidence of careful preparation of PERs
- Variability in involvement of donor agencies on the preparation of the PER
- Little focus on revenue generation; lack of country evidence to support recommendations
- Omitted issues of intrasectoral resource allocation
- Few details on monitoring indicators (World Bank, 1999).

### **2.2.2 Malawi**

The MTEF has been introduced in response problems facing on Malawi in the area of budget preparation and management. Some of the major weaknesses to be addressed are as follows:

- Five Year Development Plans and three year Public Sector Investment Programmes, which set out national and sectoral objectives, policies and

specific projects, were not linked to the availability of resources through a macroeconomic framework.

- The budget preparation process did not link the achievement of objectives and meeting of targets with the funds required: there was greater emphasis on control of inputs and less on improving performance of the sector through meeting its objectives and targets
- The recurrent budget was prepared on an incremental basis (adding a percentage to last year's estimates) without reviewing whether the activities being funded should be continued
- Activities continued from year to year while resources were declining, therefore some activities, which were critical, were under funded
- The classification of the budget did not show activities (e.g. provision of extension services) but only types of expenditure (e.g. fuel)
- The investment budget was prepared separately from the recurrent budget, therefore the recurrent costs arising from the investment programmes were not taken care of
- Controlling Officers did not have much autonomy to utilize funds for better performance; rather proper accounting was emphasized more (Salvatore Schiavo-Compo and Daniel Tommasi, 1999)

In 1995, the Government of Malawi decided to adopt a Medium-Term Expenditure Framework (MTEF) in response to increasing fiscal imbalances. The objectives of the Malawi MTEF are to link medium-term, or strategic, planning and the annual budget process in such a way as to restructure recurrent and development expenditures in line with clearly established priorities and available resources. Restructuring achieved through a top-down process of allocating resources between sectors based on relative priorities, and a bottom-up process of identifying the actual costs of policies and strategies in each sector (World Bank, 1998).

MTEF process was used in the preparation of the 1996/97 Budget in the four major spending sectors: Agriculture, Education, Health and Works and Supplies. The Police also requested to join the MTEF process. In year 1996/97 budget year, the process involved developing information on the actual costs of activities as a guide to allocating resources to achieve their objectives.

So far, they practiced an integrated sector approach to planning involving:

- Reviewing and defining sectoral objectives and policies;
- Identifying activities needed to implement sectoral policies.
- Identify activities that scaled back or stopped to fit within expenditure ceilings. Progress at the sector level is already evident.
  
- Linking policy objectives and costing is underway although progress has been uneven across the pilot sectors. There is a clear understanding, particularly among the four initial pilot ministries, of the objectives of the MTEF and unanimous agreement that this is the way to move forward. The most obvious improvements are in the much clearer articulation of programs and their costs and in the start on re-prioritization and removal of unnecessary duplication (World Bank, 1998).

The PFM system in Malawi has been characterized by serious flaws in a broad range of areas. Budgeting, financial control, cash management, accounting and auditing all suffer from significant weaknesses. Government of Malawi has drawn up comprehensive sets of measures required to strengthen public financial management and accountability, for example as set out in the Malawi Financial Accountability Action Plan (MFAAP), finalized in 2003 and approved in May 2004. Nevertheless, only limited progress has yet been achieved in the implementation of the large number of tasks identified within it, largely due to its complexity and lack of focus. The Government of Malawi and donor efforts in

a number of demanding fields – such as the introduction of an Integrated Financial Management Information System (IFMIS) and a Medium Term Expenditure Framework (MTEF) – have been quite disappointing and have had only limited success. This is suggestive of a lack of government commitment, or lack of broader consensus within government, to effective PFM systems. The lack of commitment is compounded by the fact that donors have encouraged the Government to adopt complicated budget management systems such as Output Based Budgeting in an environment of limited capacity. Some improvements have been made since 2004 by the new government, mostly in the exercise of fiscal discipline and fiscal control. This has enabled some of the foundations laid in the earlier period to play a more productive role. Standard operating procedures for government processes seem to have been allowed to operate with less resort to exceptional procedures or *ad hoc* interventions. Additionally, there are signs that the parliament is taking its role in PFM more seriously, with improved scrutiny of executive action. However, concerns remain over the level of compliance by Ministries with existing PFM regulations, the continuing lack of enforcement of some sanctions, and the delays in certification of accounts by the National Audit Office (Paolo de Renzio and Bill Dorotinsky, 2007).

### 2.2.3 Guinea

A 1996 public expenditure review in Guinea revealed a complete mismatch between the stated policy priorities of the government and actual priorities based on expenditure allocation. Although the government has designated primary education, public health and road maintenance as priorities, funds often end up being allocated to other areas instead. There was no system for costing out policy proposals or subjecting them to rigorous scrutiny (World Bank, 1997).

An exercise to cost out the policy mix needed to meet the government has stated priorities revealed that the share of priority programs in total spending would need to triple over the succeeding four years (1998-2001) implying drastic cuts in other expenditures in order to remain within the budget constraint.

The report also stated that actual allocations to meet the recurrent costs of investment projects fell far short of what would be required for adequate operation and maintenance. Based on the findings and recommendations of the PER, the Government of Guinea has recently launched an initiative to define affordable policies. Four line ministries are already revising their medium term policies and costing out their implementation. Government is also working on preparing an MTEF for the four ministries (initially): Ministry of Health, Ministry of Agriculture, Ministry of Education and Ministry of Transport and Public Works in the context of its economic reform program, and central ministries are preparing a macroeconomic policy document to assist cabinet in intersectoral allocation decisions. Finally, the Ministry of Plan has taken steps to improve the predictability of the macroeconomic framework (World Development Bank, 1997).

I hope that Tigray Regional Government will be learning from the experience of Malawi they taken a corrective action to overcome the challenges and problems faced to their country..

### **2.3 Public Expenditure Review in Ethiopia**

The Ethiopian experiences with respect to the budget system have not been significantly different from experiences of other developing countries. During 1950s and 1960s, the country has engaged in detailed planning exercise, which was the main instrument for resource allocation. It has undergone significant change in the area of policy and planning, revenue collection and expenditure allocation, and over all financial management.

As Ghirmai (1990) noted, for the first time government budget was published in Ethiopia in 1945. The budget format that was established during the time was used for a long period of time. The 1955 constitution specified the definition of powers of Ministries, Council of Ministers, and Legislative body with regard to budget preparation and execution. The specified powers and responsibilities for executive and legislative bodies were the starting point for effective budget allocation.

Ghirmai has further substantiated and evaluated the determinants of the growth and allocation of government expenditure in Ethiopia. By using regression model, he has identified factors responsible for the growth of government expenditure. According to him, the growth of government expenditure was greater than GNP growth rate. In other words, per capita GNP appeared to be a weak determinant of government expenditure. Government expenditure for recurrent budget, and particularly that of administrative service has been significantly increased as compared to total government expenditure for the period of 1958-1977 (EFY).

None-economic factors such as planning, allocation techniques, war, and droughts have influenced the administrative expenditure. For example, the defense expenditure of the country was extremely growing faster than other sectors due to the existence of continuous civil war. On the other hand, as the ratios of dependent variables show some growth, no increment in the ratio of education was identified. Therefore, the resources that are available for expansion of public goods such as education, health and rural water supply were significantly limited.

Public spending in Ethiopia has increased substantially, by 80 % in nominal terms since 1997/1998. This represents an increase from 24% of GDP in 1997/1998 to 35% in 2002/2003 (World Bank, 2004).

The Expenditure Management and Control Program (EMCP) strategic plan developed for Public Expenditure Management (PEM) in Ethiopia is meant to improve the management of resources by the Federal and various Regional Governments so as to enhance sustainable economic growth and reduce poverty (FDRE, 2003).

Expenditure Management and Control Program has been operating since 1997 to improve budget cycle management in Ethiopia, starting from the federal level and then working its way to the regions (World Bank, 2004).

The increase driven at first by increased military spending during the war years (1998-2000). Defense spending has since declined, but spending in other areas increased by a corresponding amount, leaving total spending at the new, substantially higher, plateau level. The increase financed by increased domestic borrowing, but since 2001, it sustained by greatly increased donor inflows. (World Bank, 2004).

Budget execution has generally been sound in Ethiopia. There is no evidence of loss of expenditure control or over-spending at the aggregate level and based on the available accounting system funds appear to be spent on their intended uses. The Country Financial and Accounting Assessment completed in 2002 confirmed the absence of major problems of leakage or diversion of funds from intended uses. With the exception of 2002/03, typically the recurrent budget has been 100% spent in any given year. There is under-spending on the capital budget, which was 77% spent on average (World Bank, 2004).

According to (World Bank, 2004), the following three factors can be identified as a reason for under-spending:

- Problems associated with physical implementation;
- Bottle necks related to donors requirement for procurement and accounting;

- Problems related to estimation and recording-the budget is based on donor projections of spending, which tend to be optimistic, while reporting is based on actual aid expenditures resulting in a large apparent mismatch between budget and actual spending.

### **2.3.1 Resource Allocation In Tigray Regional State**

Tigray National Regional State operates in accordance with the principle of decentralization of power and responsibilities for enhancing the service delivery to the community in the region. The situation inevitably calls for increased financial activities, both in revenue generation and resource utilization at each level of administration. Hence, strong financial management need to be introduced and put into practice at all levels. Financial management covers the following wide spectrum of inter-related financial activities:

The financial aspects of multi-year investment plan and its financing;

- ❖ The formation of the annual budget, incorporating the priorities of the local community with national and regional investment and service initiatives, together with the annual planned requirements against the estimated funding availability;
- ❖ The control and management of the revenue and expenditure in accordance with the approved budget;
- ❖ The accounting and recording systems;
- ❖ The financial reporting;

The policy of the Federal Democratic Republic of Ethiopia (FDRE) focuses on the development of rural areas, promotion on agricultural production and expansion and food security, the conservation of natural resources, and the rehabilitation and expansions of health and education service, roads and drinking water supply. The government has an influence on the spending patterns of donors and the NGO's (World Bank, 2001).

Both Bureau of Agriculture and Rural Development and Education Bureau prepared strategic plan of 3-5 years (2003-2007). The designed sustainable and fast regional strategic plan was based on the objective of attaining economic growth. The plan also envisaged linkages among sector bureaus on matters of planning, policy and budgeting. Since 2003, both bureaus adopted sector program approach of public expenditure management developed to overcome a number of quite specific problems in relationship between government and donor partners (BOFED, 2002)

### **2.3.2 Economic contribution of Agriculture in Tigray**

Sustainable economic growth is an essential condition for poverty reduction in Tigray. In the 1980s and early 1990s, economic performance was extremely weak, in terms of GDP growth, which recorded often less than the growth in population. Based on the data availability from Bureau of Plan and Economic Development (BOPED), in Tigray, agriculture contributes around 57% to the regional GDP, of which 36% is from crop production and about 17 and 4% is from livestock and forestry respectively (BOPED, 2004).

### **Economic contribution of Education in Tigray**

Access to and utilization of education provides households the means to improve the household status socially and economically, as well as preparing people to exercise better decision-making that will directly affect the security of the household (IDA 2007). The failure to realize social benefits, such as the extension of health facilities and educational opportunities, also frustrate the incentive among the peasant population to change from subsistence to intensive agricultural production (Glantz 1987). The regional government of Tigray has been made efforts to expand the human capabilities of rural households for the last decade. As a result, it is observed that human capabilities have substantially improved, started from extremely low levels. Starting from a low

base, Tigray's enrolment expansion at all levels of education has been impressive, regional primary gross enrolment rate in grades 1-8 increased from 68.8 percent in 1999 to 104.1 percent in 2006. Female gross enrolment rate has also increased from 64.9% in 1997 to 103.8% in 2006 (BOPED, 2004).

## **2.4 Linking of Sector Level Policy, Planning and Budgeting**

The separation of policy making, planning and budgeting at the federal government level is also replicated at the regional and sector level. The requirement, therefore, is to create enough certainty so that regional governments, line ministries, agencies and regional executive bodies can plan have the incentives to do so, and have better information on which to base strategic and operational decisions.

Defining and implementing a sectoral MTEF involves preparing estimates of overall resource availability, reviewing financing mechanisms, and preparing prioritized government spending plans.

This is clearly not a one-off process. Rather it is iterative and must take into account, on a periodic basis, changes in sectoral needs and priorities and changes in the overall resource envelop.

The government has been moving for some time towards a more systematized medium term planning process, using a locally adapted approach along the lines of the medium-term expenditure framework in use in several other countries.

The Ethiopian application of the general concept has involved a three-tier approach, consisting of the following:

- A rolling Macro-Economic and Fiscal Framework (MEFF) which would result in a three-year projection of the likely resource envelope for the

country and a breakdown by broad sectors of federal government expenditure and subsidies to the Regions;

- A three-year Public Investment Program which would derive its annual ceilings from the MEFF; and was intended to be transformed into a full Public Expenditure Program (PEP); and
- Binding budget calendar, this would ensure that the Regions in particular would receive timely information about the level of the federal subsidy, which constitutes the bulk of the revenues of regions. The budget calendar also defines the place for MEFF and PIP (World Bank, 2004)

## **Budget cycle**

Breaking down the budget process into consecutive stages makes it easier to understand the various steps of the budget cycle:

1. The cycle starts with the government's policy perspective, including an analysis of the previous fiscal year, the setting of priorities, and estimates of income.
2. It is followed by the government's budget formulation: including setting the resource framework, objectives and priorities.
3. Upon enactment through the legislature, the budget is actually executed (or implemented) during the fiscal year: Revenues are collected, funds released, personnel deployed, and the planned activities are carried out.
4. The budget cycle ends with the monitoring and evaluation of achievements: Expenditures are accounted for, the achievement of targets is measured, and the audit institutions provide their feedback to the legislature. Their information is used to analyze and formulate next year's budget.

## **Organizational Issues**

The responsibilities of the different actors involved in budget preparation and policy formulation must be clearly defined and delimited:

- The Prime Minister, Office of the federal level and the president offices at regional level coordinate policy formulation and arbitrate any conflict that may appear in budget preparation.
- The Federal Ministry of Finance and Economic Development sets the guidelines for budget preparation, scrutinizes budget requests and ensures the coordination of the budget preparation process, as well as budget the overall consistency of budget with policy and macroeconomic objectives.
- At federal level, line ministries and agencies are responsible for preparing their sector programs and budget, within the policy directions and financial envelopes decided by the government. Bureaus and other agencies carry out similar functions at regional level.

## Chapter Three

### Empirical Data Analysis and Discussion

#### 3.1 Introduction

This chapter focuses on the finding of an opinion survey made at Tigray Region Agriculture and Rural Development Bureau and Education Bureau related with resource allocation and expenditure management process. The survey employed with structured open-ended and closed-end type of questioners, focus group discussion with higher officials and interviews with some senior experts of the bureaus. The analysis also supported by secondary data collected from the respective bureaus.

The selection of the public bodies is based on the priority set by regional government budget and magnitude of spending.

Because of the adoption of new modified base accounting system and budgeting system Bureau of Finance and Economic Development plays the main role in planning, budgeting and financial related activities to each sector bureaus through tentative training. Each sector bureaus has responsibilities to prepare its strategic and annual plan, physical and financial reports for different bank accounts, to control its budget against the approved budget and perform financial activities ranging from recording transaction to preparing financial reports.

#### 3.2 Characteristics of Respondents

The effective of government expenditure management depends on the quality and skill of the staff in the bureau. As we saw on table 1.1, from Agriculture and Rural development Bureau, 67% of the total respondents are degree holders, 24% are diploma holders and the remaining 9% are masters, while on

Education Bureau 72% of the total respondents are degree holders, 14% are diploma holders and the remaining 14% are masters. The researcher understood from the focus group discussions that the staff of the bureaus has taken training on the newly adopted budget, accounting, procurement and internal audit system. From the questioners filled by the experts, team leaders were taken training respective to their job. Based on their response, ten (33%) respondents were said that the training given to them is not sufficient to discharge their responsibility on the new system and twenty (67%) of the respondent replies that the training given to them face a shortage of time.

During the focus group discussion, the officials indicates they have high staff turn over. As both department heads explained, their bureaus are not able to retain its staff due to the uncompetitive salary scale.

### **3.3 Expenditure Planning, Approved Budget and Actual utilization**

#### **Linkage of Budget to the Strategic Plan**

Since annual plans are set to concretize the objectives and targets set in the strategic plan, it becomes essential to see the linkage of annual budget to the strategic plan and the extent to which the annual budget earmarked to contribute to the attainment of the goals and objectives set in the strategic plan. In this regard, effort was made to review both the strategic and annual plans of the bureau and focus group discussion with concerned officials and experts of the bureau. A total of thirty sample stakeholders requested from the two sector bureaus to give their opinion on the linkage between the annual budget and the strategic plan. Out of this nine (30%) of the respondents indicated that budget allocated by the government and donors assistance and loan are linked to the strategic plan while fifteen (50%) respondents indicated that it is only the government portion of the budget that is linked to the strategic plan. The remaining six (20%) respondents responded that they have no any idea about

the linkage. The focus group discussion and interview have revealed that the strategic and the annual plan have strong linkage with the priority concerns spelled out in the strategic plan of their bureau.

### **Requested Budget**

Sector bureaus are responsible for preparing their budget request based on the aforementioned programs and budget ceiling. The budget preparation involves an assessment of new and existing program and performance of on going projects with their work plan. They have to prepare a justification for each expenditure item by using cost build up in each project and cost center. Based on the outcome of the review and capacity of financial absorption, budget proposal is prepared and submitted to BoFED. After submitted their request, the head of public bodies and relevant department heads defend their budget request in a formal budget hearing with BoFED. After budget hearing is over, the budget request of sector bureaus be revealed, adjusted, consolidated and BoFED make some recommendations. The total recommended budget by each sector bureau has submitted for approval. Finally, the BoFED notifies budget entitlement of each sector bureaus.

The most important issue is not only how the budget process is undertaken but also the linkage between expenditure planning and budget process. One of the most important findings of this study is that the expenditure planning is not well integrated into budget process. Majority, 75 percent, of the respondents indicated that the link between macro economic policy, expenditure planning and budget process is inadequate. This is so at least for couple of reasons. 20 (67%) indicates lack of skilled manpower and 10 (33%) respondents replies low attention given by the higher officials. The survey also identified that the linkage between capital and recurrent budget is inadequate. During the focus group discussion with higher officials, participants argued that expenditure planning, particularly PIP process operates in parallel with budget process,

which caused confusion and it would be one of the most challenging aspects of the expenditure planning reforms. During review, a pertinent report by the researcher indicates on table 3.1 that both sector bureaus budget request have high disparities with the approved budget.

In addition, each sector bureaus, government policies and strategies did not formally reviewed and updated for the purpose of budget allocation.

### **Allocation of resources**

As mentioned on the theoretical part of the study, Public Expenditure Management is the way by which public resources are allocated and utilized. With out implementing the allocated budget effectively it is impossible to achieve the intended objectives.

In most developing countries, 80% of local government budget is taken by recurrent expenditure. However, capital expenditure gets the lowest share of the budget. On the other hand, the habitual approach to minimize recurrent expenditures in order to leave as much room as possible for capital projects raises the question of sustainability and efficiency of expenditure (World Bank, 1999).

In Ethiopia for the period of the year 1991 - 1998, local government budget was taken by capital and recurrent budget 70 and 30 percent respectively. This proportion indicates that the shift of resources from consumption to development areas. However, the composition of expenditure had fluctuated substantially form year to year. For instance, from 1998-2001, on average, the composition of expenditure for capital reduced from 30 to 25 percent while the recurrent expenditure increased from 70 to 75 percent. The composition of expenditure has changed substantially due to the sharp increase in defense

expenditure and interest payment. Thus, capital spending has been more vulnerable than recurrent expenditure ( MoFED, 1967-2002).

In order to carry out the activities and achieve the outputs for which they are responsible, Tigray region raise own resources and get a transfer from the federal government. Own revenues and part of the transfer cover recurrent expenditures (salaries and other recurrent costs); the rest of the transfer, plus foreign resources, covers capital expenditures.

As table 3.1 shows, that education sector bureau takes the highest share of capital and recurrent budget indicates that 88.08, 54.95, 100.64 and 91.94 million birr respectively from year 2003 to 2006.

On the other way, the allocation of capital and recurrent budget to agriculture sector bureau shows that small share 16.4, 12.37, 24.38 and 29.45 million birr respectively from year 2003 to 2006.

### **Capital and Recurrent Budget allocation and execution**

It is one of the measures used to evaluate the financial performance of the sector bureaus. It shows whether the allocated fund in the budget year is utilized fully, the degree of budget execution highly depends on the capacity of the sector bureaus to use it. However, it is not a type of measure, which can tell how efficiently, and economically the budget is used for the intended purpose.

As noted during review of pertinent document, both agriculture and Education sector bureau used to prepare preliminary sub-agency and project profile forms for recurrent budget ME/BEMA/2 and for capital budget KA/BEMA/2. There are still separate forms for recurrent and capital budgets with more detail information for the latter. Expenditure for both capital and recurrent budget are justified against cost centers and the work plans. Each cost center has one strategic plan into which all expenditures fit.

The work plan for each cost center:

- Defines the outcomes expected in the budget year;
- Defines the expected outputs;
- Sets out the objective and strategies; and
- Presents the required resources to achieve those outcomes and justifies the resources requested in terms of salaries, non-salary recurrent expenditure and capital expenditure.

**Table 3.1 Budget Request, Allocation and Actual Spending in million Birr2003\_2006**

Year	Statues	Agriculture			Education		
		Capital	Recurrent	Total	Capital	Recurrent	Total
2003	Request	32.53	16.70	49.23	125.98	52.98	178.96
	Approved	8.200	8.20	16.4	61.39	26.69	88.08
	Actual	1.39	8.19	9.58	31.23	25.87	57.1
	<b>% of Act/Approved</b>	<b>17%</b>	<b>99.9%</b>		<b>51%</b>	<b>97%</b>	
2004	Request	3.170	16.70	19.87	53.63	36.67	90.3
	Approved	2.190	10.18	12.37	29.49	25.46	54.95
	Actual	1.360	9.66	11.02	19.03	23.74	42.77
	<b>% of Act/Approved</b>	<b>62%</b>	<b>95%</b>		<b>65%</b>	<b>93%</b>	
2005	Request	8.24	15.27	23.51	89.36	89.36	178.72
	Approved	5.20	19.18	24.38	44.30	56.34	100.64
	Actual	4.92	16.03	20.95	24.43	53.96	78.39
	<b>% of Act/Approved</b>	<b>95%</b>	<b>84%</b>		<b>55%</b>	<b>96%</b>	
2006	Request	13.63	35.61	49.24	56.50	93.20	149.7
	Approved	11.94	17.51	29.45	33.63	58.31	91.94
	Actual	1.34	20.25	21.59	18.52	45.75	64.27
	<b>% of Act/Approved</b>	<b>11%</b>	<b>116%</b>		<b>55%</b>	<b>79%</b>	

Source: Agriculture and Education sector bureau various years report

### 3.3.1 Agriculture Bureau recurrent budget execution

Table 3.2 shows that execution of recurrent budget for agriculture sector bureau were 99%, 95%, 84%, and 116% during the 2003, 2004, 2005, and 2006 respectively. This indicates that the budget execution with respect to recurrent budget is at excellent. However, there is a

weak controlling mechanism of the allocated budget, which is why the recurrent budget execution of year 2006 is more than the allocated budget that exceed by 16%. As compared to capital budget, the financial report with respect to the recurrent budget shows far better result.

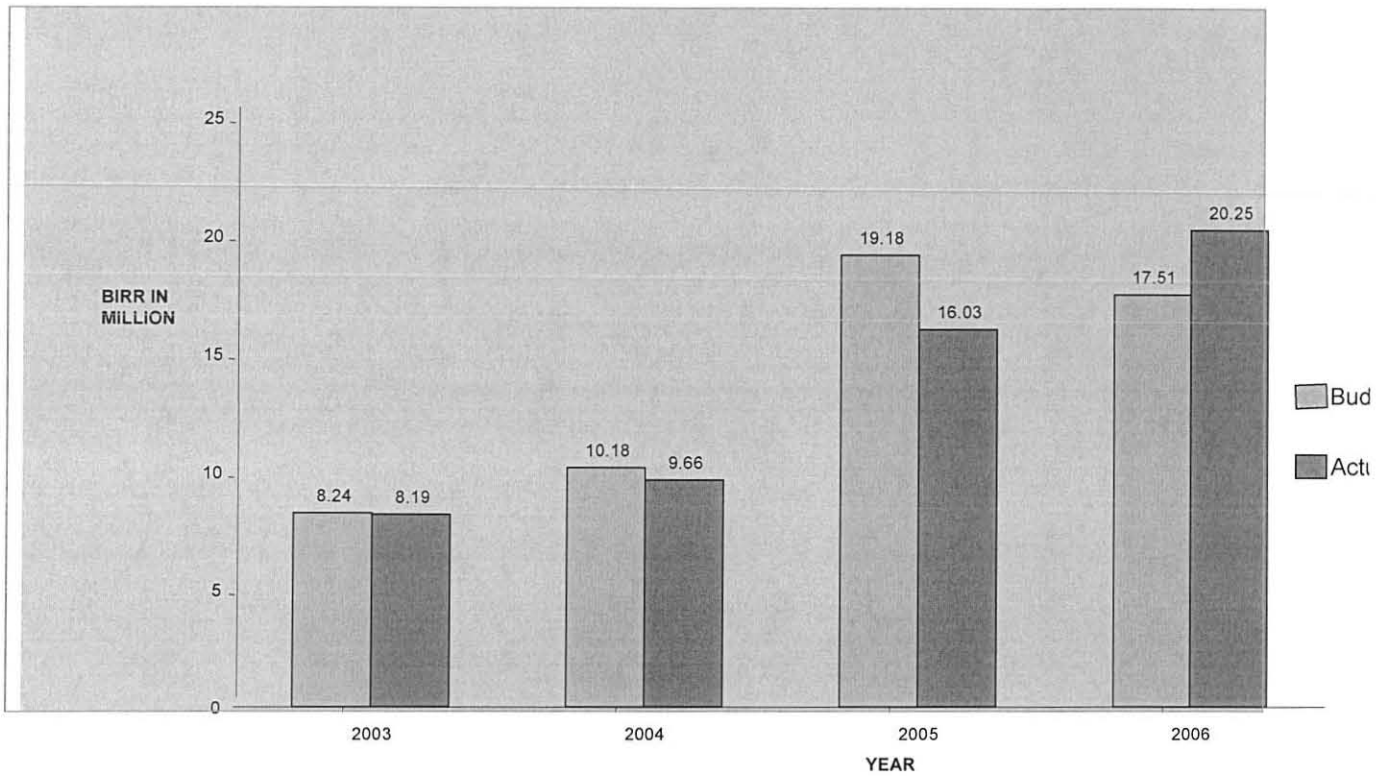
Table 3.2 Recurrent Budget Vs Expenditure by Expenditure Category in (000 Birr) 2003-2006

Organization	Year	Personal service		Goods and Services		Fixed asset and Construction		Others		Total		% of actual/Budget
		Bud.	Act.	Bud.	Act.	Bud.	Act.	Bud.	Act.	Bud.	Act.	
Agriculture	2003	4.12	4.12	4.08	4.07	-	-	-	-	8.24	8.19	99.79
	2004	4.22	4.42	5.80	5.07	0.10	0.10	0.06	0.07	10.18	9.66	95
	2005	7.13	6.94	11.87	8.91	0.17	0.17	0.01	0.01	19.18	16.03	84
	2006	9.59	8.97	7.71	9.88	0.07	1.39	0.15	0.01	17.51	20.25	116
Education	2003	9.7	9.29	16.35	16.05	0.43	0.39	0.19	0.13	26.69	25.87	97
	2004	8.12	7.44	17.08	16.17	0.02	-	0.24	0.13	25.46	23.74	93
	2005	14.09	14.03	42.11	39.79	0.12	0.12	0.02	0.02	56.34	53.96	96
	2006	18.30	16.05	38.86	28.40	1.12	1.19	0.03	0.11	58.31	45.75	79

Source: Bureau of Finance and Economic Development Report of Various Years

Figure 3.1

AGRICULTURE BUREAU  
RECURRENT BUDGET AND ACTUAL



Source: Bureau of Finance and Economic Development various years report

Table 3.2 and figure 3.1 show recurrent budget and actual expenditure of Agriculture and Rural Development Bureau during the period under review. As can be seen from the table, the performance ranged between 84% and 116% during the period.

Table 3.2 indicates that, nearly 50 percent of recurrent budget went to wages and salary expenses while the balance was used for covering operating expenses, procurement of fixed assets and construction activities.

During the focus group discussion, respondents indicate that the overspending report on 2006 was related to the actual expenditure on goods and construction that took place in the budget year while the budget was approved in 2005.

However, the researcher's observation differs from the perspective of the respondents, because budget was approved for one year and the unused budget does not transfer to the next year budget. Therefore, this implies a weak controlling mechanism of the allocated budget, that is why the recurrent budget execution for year 2006 exceeded the allocated budget by 16%.

### **3.3.2 Agriculture and Rural Development Bureau capital budget execution**

The major sources of finance for capital budget expenditure in the region are, loan and assistance. Table 3.3 below shows capital budget expenditure of the bureau by source of finance for the period under review. As can be noted from Table 3.3, during 2005, loan constituted the major share in the financing of capital budget while in 2006 the loan share of financing was replaced by assistance followed by treasury. The share of treasury in the financing of capital budget showed an increasing trend with the exception of 2005 during which the major part of the capital budget was financed by loan.

Actual expenditure of capital budget during the period under review ranged from 11% to 95% indicating the overall low performance of capital budget utilization. The highest performance (95%) was registered in 2005 and the lowest (11%) in 2006 during which the entire finance from loan and assistance and major part of finance allocated from treasury was not utilized. The major components of capital budget include personnel service, goods and services, fixed asset and construction and other.

**Table 3.3 Capital Budget Vs Expenditure by Source of Finance (2003-2006) in Million Birr**

Organization	Year	Treasury		Internal revenue		Loan		Assistance		Total	
		Bud.	Act.	Bud.	Act	Bud.	Act.	Bud.	Act	Bud.	Act.
Agriculture	2003	2.02	0.11	6.18	1.29	-	-	-	-	8.2	1.4
	2004	2.19	1.36	-	-	-	-	-	-	2.19	1.36
	2005	1.00	0.72	-	-	4.2	4.2	-	-	5.2	4.92
	2006	4.07	1.34	-	-	1.49	-	6.38	-	11.94	1.34
Education	2003	27.72	21.83	1.85	1.85	31.82	7.55	-	-	61.39	31.23
	2004	17.45	12.86	-	-	12.05	6.17	-	-	29.49	19.03
	2005	20.77	20.98	-	-	4.4	1.78	19.13	1.67	44.30	24.42
	2006	7.59	11.51	-	-	-	5.29	26.05	1.72	33.63	18.52

Source: Bureau of Finance and Economic Development various years report

### **3.3.3 Education Sector Bureau Capital budget execution**

Table 3.3 below shows capital budget expenditure of the bureau by source of finance during the period under review. Education sector bureau has a higher budget share than agriculture sector bureau. As can be noted from table 3.3 on year 2003 loan constituted the major share in the financing of capital budget and followed by treasury while in 2004 the vice versa of year 2003, but on year 2005, treasury has a major share and followed by assistance. On year 2006 in contrast of year, 2005 assistance had a major share, followed by treasury. The total financing of capital budget from different source of finance showed a decrease trend.

Actual expenditure of capital budget during the period under review was the lowest utilization between 51% and 65% indicating almost 50 percent of the capital budget is under utilization. Based on review of related report of 2003 and 2004 the majority budget derived from loan did not utilize. In addition, on

2005 and 2006, budget year the most unutilized budget was that of assistance. On the other way on year, 2006 there is over utilization of approved budget from treasury and loan.

From the data indicated in figure 3.3 in both sector bureaus, the execution of capital budget was low. The researcher understands that there is a problem in capital budget execution. This means, because of lack of capacity to follow up and monitor, development projects not completed within the budget year. There is a risk of creating a more high turn over of personals and professionals. In addition to the lack of skilled and technical workers, high turn over of civil servants has led to a poor quality investment decision and inadequate utilization of the financial resources.

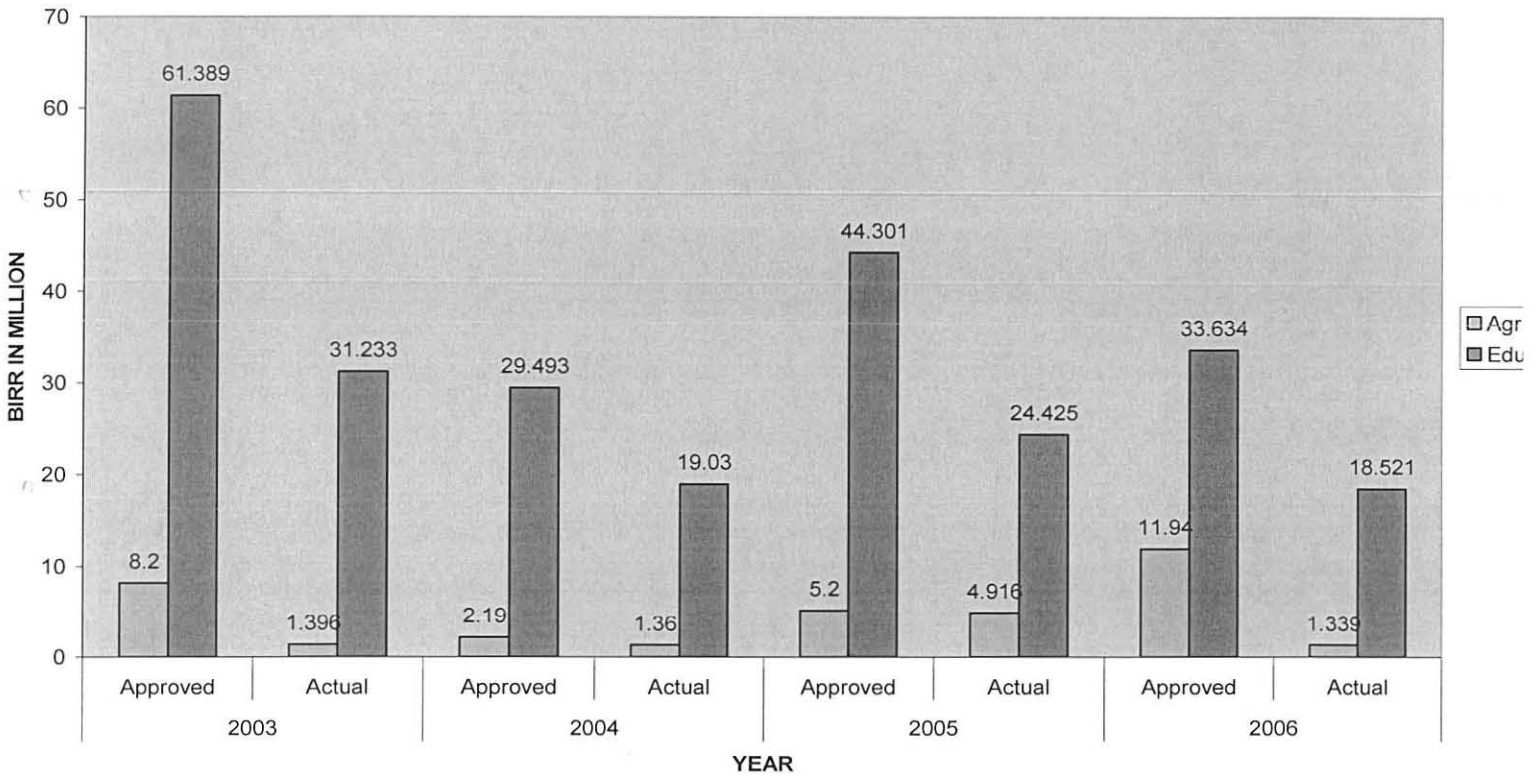
Information obtained through interviews and discussion with the concerned officials about the unutilized budget in both sector bureaus revealed the existence of information gap between concerned stakeholders during budget formulation. For instance, the parallel flow of funds did not assist in the development of an integrated plan/budget reflecting the overall needs of the bureau.

The officials indicated that the annual report produced did not capture the plan and actual expenditure related to offset budget allocated on loan and assistance. This was so because the Federal Ministry of Finance and Economic Development and the regional government allocated the budget from loan and assistance without the knowledge of the sector bureau in which case the latter could not have any information to capture the budget from these sources.

However, as the researcher understood from the focus group discussion and interview with key informants, there is an apparent need to create mechanism by which funds from other different sources are to merge with the government funds to form an integrated budget and financial reporting process.

**Figure 3.2**

**AGRICULTURE AND EDUCATION SECTOR BUREAUS  
CAPITAL BUDGET**

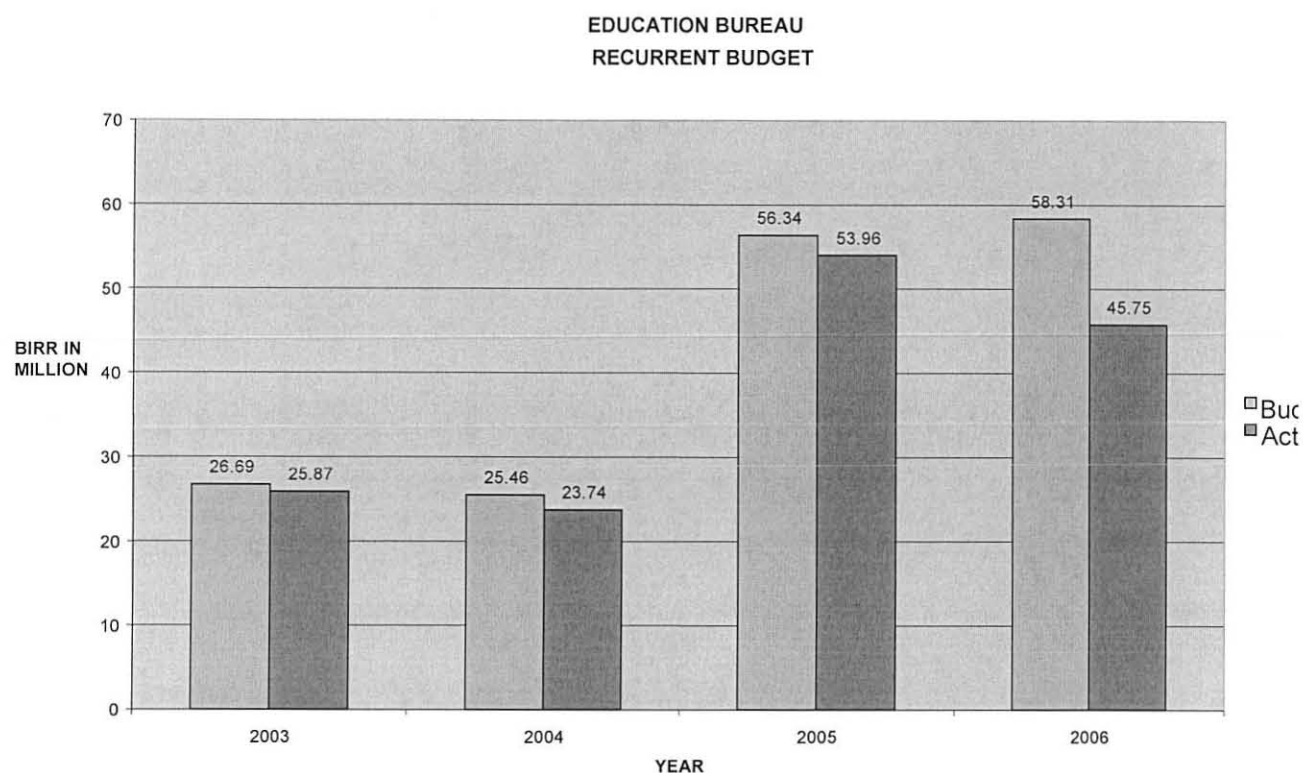


Source: Bureau of Finance and Economic Development various years report

**3.3.4 Education Bureau recurrent budget execution**

Recurrent expenditure of education sector bureau shows budget execution of 97%, 93%, 96%, and 79% from the year 2003 to 2006 respectively. This indicates that the budget execution with respect to recurrent budget is at good.

Figure 3.3



Source: Bureau of Finance and Economic Development various years report

Table 3.4 Capital Budget allocations Expenditure by Sector (2003-20006) in Million Birr

Sector	2003		2004		2005		2006	
	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Actual
Agriculture	8.20	1.39	2.19	1.36	5.20	4.92	11.94	1.4
Education	61.39	31.23	29.49	19.03	44.30	24.42	35.23	18.52
Water Resource	9.07	6.44	8.87	6.11	11.69	5.16	43.99	28.51
Rural road	29.11	28.17	1.18	1.07	1.17	1.04	1.13	0.99
Health	24.80	23.22	7.87	5.02	23.57	9.26	23.22	22.29
Others	26.57	21.22	41.53	30.82	19.90	15.30	38.48	14.94
<b>Total</b>	<b>159.14</b>	<b>112.22</b>	<b>91.14</b>	<b>63.41</b>	<b>105.84</b>	<b>60.10</b>	<b>154.00</b>	<b>86.59</b>

Source: BOFED various years report

As can be seen from Table 3.4 the performance of agriculture, compared with other sectors not only the lowest share from the government budget but also the lowest performance in terms of capital budget utilization.

### **Budget Transfer in Both Sector Bureaus**

Since future condition is not predictable, bureaus may face unexpected situation that requires transferring the budget from one type of expenditure to another. Normally, limited amount of transfers are recommended to use the budget effectively and to accommodate the negative consequences of the unexpected situation. However, if it is practiced excessively, it can be an indication of unplanned utilization of resources. Unplanned spending of the budget can affect the annual plan, which emanates from the strategic plan.

The researcher tries to observe the budget transfer from both sector bureaus financial reports. For example, on year, 2003 agriculture sector bureau for recurrent approved budget was 7.8 million but the adjusted budget was 8.2 million and for capital-approved budget it was 8.4 million and the adjusted budget was 8.2. The total budget amounted 4 hundred thousand for recurrent and two hundred thousand for capital budget for the year.

On the other hand, for the same budget year Education bureau, approved recurrent budget was 34.6 million but the adjusted budget was 26.69 million for 2003. For the same period, the capital-approved budget was 68.5 million and the adjusted budget was 61.4. This means budget transfer was made 7.91 million for recurrent and 7.1 million for capital budget.

On Education bureau, the researcher observed from its recurrent budget reports there was irregular spending patterns such as on year 2003 payments on contracting professional service, on fuel and lubricants on staff salary .

In addition from its capital budget report; payment to podium. This is an indication of either unplanned activities or unplanned and uneconomical utilization of resources.

During the focus group discussion, some participants indicate the reason for uneconomical use of the budget before the budget year lapse to protect the surplus budget from return back to the treasury of the Bureau of Finance and Economic Development. In addition, other participants admitted the uneconomical use of the budget did it purposely because they believed that the low level of budget execution would negatively affect their next year budget allocation. There for they try to utilize the budget fully but not economically before it laps by transferring from one account to another.

From the discussion, the researcher tries to observe the problem occurs that activities had not been done according to the plan. This indicates that even though both sector bureaus have annual plans which shows clearly which task has to be done when, the bureaus prefer to do activities with out following the plan. This is well known that unplanned activities are the causes of unplanned spending.

### **3.4 Evaluation of Financial Utilization and Physical Performance**

All sector bureaus' can achieve several important benefits if they regularly (such as quarterly or monthly) track the performance of their programs. Program managers and other public officials need information on both the outputs (the physical products they produce) and the outcomes of their work. This is needed to help managers and other public officials identify problem areas, identify needed improvements, and later assess the results of the actions taken.

For analyzing the performance in a budget year, evaluation of financial utilization need to be carried out in relation to the physical performance. In this regard, 30 questionnaires distributed to the two sector bureaus. Out of 30 respondents, the great majority 28 respondents (93%) replied that there was no practice of evaluation of financial utilization in comparison with physical performance. While only two respondents (7%) indicated the existence of such practice. The response reveals that there was no practice of performance evaluation by comparing financial utilization with actual physical performance.

During a focus group discussion and interview with higher officials, Asked to mention the reasons for the absence of such practice, majority respondents and participants of the focus group replied lack of skilled staff is the reason for the absence of such evaluation. Whereas, some pointed out that the Bureau of Finance and Economic Development carried out performance evaluation, as it is its duty of BOFED. Still others stated that it was only the routine spending and controlling the budget was taken out as their main responsibility.

### **3.5 Management of Donors Fund**

Given the size of the resource gap and the limited capacity of the economy to mobilize domestic resources, the budget shortfall is usually covered by donor's assistance. The regional government allocates only limited amount of capital expenditure from treasury for the Education and agricultural sector bureaus. Hence, most of the programs related to agricultural development and educational program are usually financed through loan and grants obtained from multilateral s and bilateral sources.

Table 3.14 below shows budget and actual expenditures financed by donors during the period under review.

Tables 3.5 Budget Vs Expenditure Funded By Donors (2003-2006) in Million Birr

Organization	Description	2003		2004		2005		2006	
		Bud.	Act.	Bud.	Act.	Bud.	Act.	Bud.	Act.
Agriculture Bureau	Food security	33.80	31.48	171.5	123.9	118.84	79.74	202.16	193.86
	WFP	18.45	6.18	19.98	8.1	17.31	12.12	14.17	8.74
	Other fund	9.53	27.41	24.3	15.06	91.18	73.86	79.44	56.30
	<b>Total</b>	<b>81.79</b>	<b>65.07</b>	<b>215.78</b>	<b>147.06</b>	<b>227.33</b>	<b>165.72</b>	<b>295.77</b>	<b>258.90</b>
Education Bureau	WFP	2.02	1.25	2.00	1.41	2.59	2.18	1.26	1.12
	UNICEF	1.42	1.32	2.89	1.58	2.60	1.19	2.85	2.73
	Italian Cor.	3.8	0.24	3.70	2.99	2.44	1.83	14.02	1.36
	Others	0.77	0.71	0.79	0.42	1.34	0.74	0.65	0.56
	<b>Total</b>	<b>8.01</b>	<b>3.52</b>	<b>9.38</b>	<b>6.40</b>	<b>8.97</b>	<b>5.94</b>	<b>18.78</b>	<b>5.77</b>

Source: Report of Education and Agricultural and Natural Resource Bureau Various Years

During the focus group discussion and related interview, the respondent said that donor fund transfer directly to both sector bureaus poses a particular challenge. While donor procedures require reporting on utilization of fund flow in the case of channels 2 and 3 both sector bureaus a detailed breakdown of the budgets, actual spending, and actual revenues of these entities is not included in execution report submitted to Bureau of Finance and Economic Development. In addition, they put as a main reason, delays and gaps in financial reporting, due to inadequate reporting the report is by lump sum instead of by detail breakdowns, advances transfer to Woreda does not settled on time and Shortage of trained staff has been shown as a shortage on capturing the disbursement, accounting and reporting of fund utilization.

Moreover, questionnaires were distributed to concerned respondents to identify whether the sources of donor fund were considered in the formulation and execution of annual budget during the period under review. Out of 30 respondent, 25 (83%) respondents was affirmed that donor's funds were

included in the fiscal year reports of the bureau produced during the period while 5 (17%) said that it does not include in the fiscal reports . As the response from most of the sample respondents show donors fund were addressed in the fiscal and financial reports of the bureau.

In addition, the informants were requested to rate satisfaction of the donors. Out of 30 respondents 16 (53%) indicated that donors were satisfied with the report, while 14 (47%) of the respondents, replied that donors were not satisfied with the fiscal and financial reports produced by the bureau during the period under review.

In contrast, during the review of related documents, the researcher observes that there are series of categories of government expenditure that are often not subject to normal budgetary procedures and not included in budget documentation. Donor funds captured in the fiscal data is not complete. The major sources of inconsistencies relate to the relatively high amount of aid received in kind, especially on Agriculture Bureau like food aid, fertilizers and on Education Bureau like Books, computers. The failure to include all donor-financed spending can lead to inefficiencies in the composition of government spending. For example, it is difficult to know whether the government should finance the purchase of textbooks when there is uncertainty regarding whether donors have already provided for this. Macro fiscal management also made more difficult, as available information on how actual spending compares with what was budgeted was distorted.

In addition to this, all public expenditure analyses within sector bureaus need to pay special attention to the impact of various aid flows, which can be substantial but are not uniformly captured in both sector bureaus budgets. Financial data on donor and sectoral activities are not systematically collected and monitored. Capital budget of Education bureau and Agriculture and Rural Development bureau have been mainly financed by various NGO and off-budget

donor projects, with the result that the budget figures do not fully reflect the priority accorded to their program.

The researcher could not contact donors to evaluate their satisfaction with the fiscal and financial reports of the bureau produced during the period under review. However, given the problem stated earlier with respect to recording and reporting of the financing from loan and assistances, it is hardly to say that the fiscal and financial reports produced by the bureau were to the best satisfaction and expectation of donors involved in financing different programs during the period under review.

### **3.6 Estimation of Revenue and Collection**

As per the information obtained from the concerned staff of the bureau, the major sources of revenue for public expenditures included the following:

- Federal subsidy
- Donors loan and assistance
- NGO's off budget fund
- own revenue

The internal revenue refers to the revenue annually generated from different activities of the bureau. In this regard, during the discussion both bureaus indicate that there was no practice of revenue estimation.

During the period under review, the annual collection of revenue from agriculture bureau ranged from Birr 0.82 million in 2003 to Birr 1.577 million in 2006 indicating a continuous trend of growth and for Education sector bureau from 1.76 million in 2003 to 2.17 million in 2006 ( See table 3.6). The researcher can see from their reports both bureaus had no plan for revenue collection although they collected considerable amount of charge fees.

Table 3.6 Actual Revenue Collection of the Bureau (2003-2006) in Million Birr

Organization	Year	Tax Revenue		Non Tax Revenue		Total	
		Budget	Actual	Budget	Actual	Budget	Actual
Agriculture Bureau	2003	—	0.68	—	0.14	—	0.82
	2004	—	1.13	—	0.09	—	1.22
	2005	—	1.09	—	0.19	—	1.28
	2006	—	1.19	—	0.37	—	1.56
Education Bureau	2003	—	1.21	—	0.55	—	1.76
	2004	—	1.47	—	0.22	—	1.69
	2005	—	2.04	—	0.66	—	2.70
	2006	—	1.89	—	0.28	—	2.17

Source: Bureau of Finance and Economic Development Report of Various Years

### 3.7 Procurement system

According to the Ethiopian Public Procurement Proclamation no. 430/2005, Procurement means the purchasing, hiring or obtaining by any other contractual means of goods, works and services.

The aim of a procurement procedure is to acquire goods and services in the most economic, efficient and transparent manner possible. Procurement planning is also very important for the timely implementation of programs and activities. As noted during discussion with concerned stakeholders procurement is undertaken in piece or as a package. It was also indicated that the starting point in any procurement is the preparation of a bid document, which is the specification for the goods/services required. The activities to be undertaken with respect to procurement should aim at efficient and effective use of the public fund. In this regard, questionnaires were distributed to 30 sampled stakeholders. Asked if the public procurement system used to provide for efficient and effective use of public funds; out of the 30 respondents, Fifteen (50%) of the respondents feel that the procurement system provides for efficient and effective use of public fund, while 11(37%) respondents think that the system does not allow efficiency

and effectiveness in the use of public fund. The remaining respondents 4(13%) rated the procurement system as moderately efficient and effective.

During the interview with the higher officials of both sector bureaus, the respondent, reply have pointed out many problems such as weak legal framework, inadequate enforcement of existing regulations, poor planning and record keeping, weak contract management, and use of untrained staff. This is true for both government and donor financed procurement for the purchase of goods, works and services.

### **3.8 Accounts Record and Reporting System**

The financial planning policies help in designing balanced budget and reports. Both budgeting and financial reporting are the important constituents of the accounting system in a public sectors. Financial reporting refers to an effort related to assessment of financial performance of the bureau. Budgeting and financial reporting assists in decision making regarding the financial aspects of an organization, such as raising expenditure of funds for handling the financial consequences. Both of them assist government in financial management for fulfilling the rules and regulations of public finance as well as the increasing requirements for services with limited resources of revenues. Budgeting and financial reporting, both are closely related because without having correct financial statements in the financial report, true budget cannot be prepared.

As indicated, earlier the regional government introduced Cash Based Accounting System in2003, which has been adopted by both bureaus. Accordingly, both bureaus use the following practices of transaction. In the introduced modified cash base accounting has been designed to have the capability to record, analyze and report the expenditure and revenues for all types of donor funds and other special funds that are included in the

governmental budget. The system is consistent with the budgeting process and produces information useful for comparing budgeted, actual revenue and expenditure. The system requires temporary accounts as revenue, expenditure and transfers plus permanent accounts like cash and equivalent to cash, receivables, payables and net asset /equity. In addition, the system required every account to be balanced and closed every day.

In this regard, focus group discussion was made how daily balancing, recording of transactions, maintaining of ledger and bank reconciliation are being practiced in their respective bureau. The responses revealed that recording and reporting of transactions were made on regular basis following the established norms.

During discussion with the concerned staff, Agriculture and Rural Development Bureau still has 19 bank accounts while the Education bureau has 12 bank accounts with branches of the Commercial Bank of Ethiopia. Having such many bank accounts makes the activity of bank reconciliation rather difficult and time consuming

However, the researcher has observed that there is not practice of daily balancing and closing of account. They use to balance their accounts usually at the end of the month when they prepare monthly financial report. This is a difficult situation to keep correct record of financial transaction accurately. The aid in kind and technical assistance do not have any record and they do not capture as a revenue and expenditure reports.

Another problem observed is with regard to bank reconciliation. In order to check if cash balance in the bank is similar with what recorded in the account, there is a process called bank reconciliation. Unless bank reconciliation is made periodically, it is impossible to say correct record of transactions is taking place. In both sector bureaus, bank reconciliation has never been made except for one

bank account that is used for the budget fund transferred from Bureau of Finance and Economic Development (BOFED).

Moreover, there are some problems in the course of application of the accounting system in place. Some of these include the following:

- Lack of recorded information and system to know the aging of receivables;
- The use of manual recording and associated problems of inaccuracy; and
- Lack of information for reporting aids received in kind.

The above constraints need to be surmounted for proper and effective application of the new accounting system.

### **3.9 Internal and External Auditing**

#### **Effectiveness of internal audit**

The objectives of internal audit are to evaluate:

- the adequacy of the internal planning and monitoring system with regard to the operational activities of the offices;
- the effectiveness of their internal control system;
- the efficiency of work procedures; the extent of compliance with established policies, regulations and rules;
- the reliability of financial data and other information;
- the extent to which assets were accounted for and safeguarded from loss.

For both sector bureau regular and adequate feedback to management is required on the performance of the internal control systems, through an internal audit function that is appropriately structured, has adequate independence, mandate and power to report, utilizes appropriate professional standards, and reports on significant systemic issues. Specific evidence of

effective internal audit would also include assessment and monitoring of error rates, a focus on high-risk areas, reporting on correction rates, and use by the external audit of the internal audit reports, and action by management on internal audit finding.

The organizational structure of both bureaus consider of an internal audit function organized at department level. The internal audit functions independently from the finance department and report directly to the bureau head. As set out in the functional description of the department, its main activities include reviewing the reliability and integrity of information for ensuring compliance with policies and regulations, safeguarding of assets, and ensuring economical and efficient use of resources.

However as noted from focus group discussion with the concerned staff in both sector bureaus, the work of the internal audit is limited to verification of requests for payments against approved budgets and against the quarterly allocation and monthly ceilings approved by government budget. Its activities are hence limited to pre-audit works. The department does not comply with standards for the professional practice of internal auditing. Moreover, there seem to be duplication of work among the accounts department and internal audit department.

In addition, the interviews with internal audit team leaders of both sector bureaus indicate that the development of fully functioning internal audit departments is a considerable challenge. In addition, the responses of the management to internal audit reports are poor. Audited functions or departments are slow to respond to internal audit reports or fail to address issues raised in reports adequately.

In consideration of the above situations, questionnaires were distributed to concerned respondent to analyze their opinion on the internal audit control

system and adequacy of the internal audit function. The findings are provided below.

Majority of the respondents twenty-one (70%) rated that the activities of the internal control system as moderate, six (20%) as ineffective while only few three (10%) rated the efficiency as effective. All the informants affirmed that the financial activities of the bureau are audited although the response differs with respect to who undertakes the auditing work. Most informants (95%) think that auditors make adequate comment on the audit finding. As learned during discussion with the concerned staff, auditing of books of account by external auditors is usually made at interval of one to three years although the books need to audit at the end of each budget year. The latest book of account audited by the external auditor so far is that of 2005 while the book of account for fiscal year 2006 is currently under auditing. The external auditors gave the following comments:

- There is weakness of management follows up and delayed action to remedy deficiencies reported by internal Audit.
- The financial statement prepared by the bureau does not reflect the income and expenditure related to donors' fund;
- Financial reports fail to capture aids received in kind; and
- Consolidated report of the bureau contains only fund flow from the regional government disregarding the financing from off budget sources such as NGOs.

## CHAPTER FOUR

### CONCLUSION AND RECOMENDATION

#### 4.1 Conclusion

The federal government embarked on a comprehensive Civil Service Reform Program to address the weakness of public expenditure management of the country in 1986 E.C. Among others, budget reform and expenditure planning projects have been attempted to improve the quality of medium term expenditure planning and budget process. Despite of all these policy measures, the integration of medium term expenditure planning and annual budget allocation remains a continuous problem of the country. To identify the causes and extents of these problems, survey has been undertaken on Bureau of Agriculture and Rural Development and Bureau of Education on Tigray regional state related with the expenditure management and budget allocation. The survey employed structured questionnaire with close-ended types of questions, and carried out interviews with some government officials. The analysis is also supported by secondary data. The research finding and results have been identified several problems related to the implementation of annual budget, handling of donor fund, applying internal control and procurement

According to the research result both sector bureaus prepared their strategic plan to guide activities during the period under review, key stakeholders especially the staff did not participate in the formulation of the strategic plan and annual targets set by the bureau. As a result professional experts and concerned staffs of the bureau do not seem to have clear vision and mission as to what is to be achieved by utilizing the recurrent and capital budgets allocated apart from undertaking their regular routine jobs. Annual budgets prepared

during the plan period lacked strong linkage with the goals and targets set in the strategic plan.

Capital budgets in regional governments have multiple roles: as instruments of compensatory fiscal policy, as windows on the net worth of public bodies, and as vehicles for development. Governments have introduced capital budgets to serve all these objectives, singly or collectively, depending on the context. In some cases, more attention has been paid to capital budgets as a way for poverty reduction strategy.

In both sector bureaus, during the period under review periods utilization of capital budget was found generally low and can not address the development needs of each sector bureaus in that both sector bureaus did not achieve its target in the prevision of key development service. However, there is relatively better performance on recurrent budget expenditure.

The legislature's approval to collect revenue and spend it cannot be given on a weekly or monthly basis, or for an indefinite period. In almost all countries, the budget covers 12 months and both the government's revenue collecting authority and its spending authorization expire at the end of the fiscal year.

The coverage of the budget naturally depends on the scope of activities of the regional government .Whatever revenues and expenditures are included in the budget, it is important to review them and present them together. Government policy objectives can be achieved through tax policy, through public expenditure policy, or through a combination of the two. Therefore, direct comparisons are needed of the costs and benefits of alternative revenue and expenditure packages. Moreover, a sound program of public expenditure requires as a starting point a realistic estimate of revenue. This is because the choices among different expenditure proposals, choices that are at the center of the budgeting

process, cannot be made without a clear idea of how much money is likely to be available.

However, both sector bureaus undertake various activities that generate revenue. Nevertheless, it has no practice of estimating the amount of revenue that could be generated from internal source and used to collect revenues without setting targets during formulation of annual plans.

In addition, both sector bureau budget control system during the period under review was rather weak as a result of which in some of the budget years spending exceeded the adjusted budget. Moreover, owing to manual recording system there were inherent problems of inaccuracy.

Like in most developing countries, in Ethiopia too, a significant share of public expenditure is managed through special arrangements outside the normal budgetary management arrangements. These special arrangements, which are known as extra budgetary funds, are used, for example, when existing budgetary procedures are inappropriate for managing particular types of activity, when such procedures do not allow spending agencies to use revenues from cost recovery, or when certain priority expenditures need protection. Extra budgetary funds are government operations that are set up outside the annual budget appropriations process. However, they are not outside the bounds of legislative authority

How ever, on both sector bureaus accurate and timely information flow among the concerned stakeholders on issues that concern budget approval, release and execution has remained to be the major constraint for better performance of public expenditure management. Such information mainly concern fund flows from different donors and NGOs like loan and assistances received in cash, on kind or technical assistances.

From finding of this study; in both sector bureaus, there is poor regular bank reconciliation. Due to this, the cashbook is a major weakness in the overall control environment. This had also been a contributory factor to the delay in the production of the report.

On both sector bureaus there are many problems in public procurement management. The major problems include weak legal framework, inadequate enforcement of existing regulations, poor planning and record keeping, weak contract management, and use of untrained staff.

Regarding to Internal audit, in both sector bureaus, the work of the internal audit is limited to verification of requests for payments against approved budgets and against the quarterly allocation and monthly ceilings approved by government budget. Thus, activities of internal audit are hence limited to pre-audit works. The department does not comply with standards for the professional practice of internal auditing. Moreover, there seem to be duplication of work among the accounts department and internal audit department.

## **4.2 Recommendations**

To surmount constraints identified in the course of this study, the following recommendations are put forward:

1. Adopt participatory approach in the formulation of strategic plan and involve staffs at all levels during the preparation of strategic plan. On the preparation of the strategic plan broad involvement of policy makers and different stakeholders in the process expenditure planning is one of the most important factors to improve resource allocation in the public sectors.

2. Make sure that all staff of the bureau are well aware of the strategic goals and objectives set for a given plan period. For this purpose, organize a brainstorming session or workshop to obtain feedback on targets set and activities planned before submitting the plan to the higher authority. Once the strategic plan is approved, ensure that all concerned staff is well familiar with its essence and work towards attaining the set target.
3. Review critically the strategic plan in action during preparation of annual plans and ensure that all targets set in terms of physical and financial performance contribute to the attainment of the goals, objectives as well as visions and missions set out in the strategic plan.
4. Establish a system for estimating revenue to be annually generated from the revenue generating activities of the bureau. Accordingly set target for annual internal revenue, monitor and follow up collection of the revenue as per the targets set.
5. Focus on capacity building to enhance implementation capacity of capital budget. To this end, devise mechanism for arranging local and foreign training of staff. Train the staff in the application of already established computerized system of the integrated budget-expenditure system (IBEX) and bring to the attention of higher authority on ways by which technical assistance could be secured for setting up modern management information system. Organize the database and publish annual reports containing time series data on the trend of public expenditure by the bureau.
6. Financial rules and regulations are important for implementation of public expenditure management .It is easy, understandable and complete to address various possible flows in the implementation of the budget allocated from different source of finance. For instance, regarding the extent and type of budget transfers and pattern of spending, daily account balancing, monthly bank reconciliation should be addressed. In this regard Both sector bureaus required to:-

- Work on the way by which all approved budget in cash, on kind or technical assistance are to be channeled to the bureau systematically in a way that allows proper recording and reporting of funds received from different sources.
  - Establish a system for monitoring and following up fund flows from different donors and NGOs like loan and assistance received in cash or in kind or in the form of technical assistance and ensure that reports produced by the bureau meet the expectation of donor agencies.
  - Sub-optimal cash management. Both sector bureaus have large numbers of bank accounts at Commercial Bank of Ethiopia and this makes it difficult to manage overall liquidity efficiently. Studies under the EMCP have recommended Single Treasury Account system. Hence, both sector bureaus required to limit the number of their bank account to as few as possible.
  - By addressing the weaknesses in a timely manner and the procedures, relating to bank reconciliation both sector bureaus has required a priority and considerable effort to reconcile each bank account with the cashbook records.
  - Another aspect is strong accountability is needed to exercise the existing weak control system on utilization of the approved budget and high activities of budget transfer from different account codes this helps to manage proper cash flow activities.
7. To strengthen internal audit function; management body of both sector bureaus needs to review and clarify the roles and responsibilities of internal audit to retain an internal audit oversight capacity, which will provide the reliability and integrity of information for ensuring compliance with policies and regulations, safeguarding of assets, and ensuring economical and efficient use of resources guidance, and procedures.

In addition, the management body must give a direction to those audited functions or departments to respond and give valuable information for the internal audit findings as soon as possible.

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## Annex A

### Questionnaires Used for Data Collection

I am w/ro Shishay Teferi. I am a student of Regional and Local Development Studies (RLDS), AAU and doing my MA thesis on Public Expenditure Management in Tigray National Regional State the case of Agricultural and Rural Development bureau and Education Sector bureau.

In order to generate primary information, I have designed questionnaire. The information is expected to contribute for the research paper, which will be conducted for the partial fulfillment of Masters Degree. The questionnaire is designed purely for academic purpose. Thus your honest and true reply is very important for the quality of the research out put and I confidently assure you that no harm will entail in filling or writing what so ever you feel.

*Thank you for your cooperation in advance*

Pleas respond to the following questions either by putting a tick mark, circling the alternative or giving short written.

#### Personal information

1. Name of the bureau \_\_\_\_\_
2. Position of respondent \_\_\_\_\_
3. Level of education \_\_\_\_\_
4. Sex \_\_\_\_\_

### Specific Information

5. How does the strategic plan link with planning and resource allocation processes?
- A. Systematically linked
  - B. Partially linked
  - C. No systematically linkage
  - D. Others (please specify) \_\_\_\_\_  
\_\_\_\_\_
6. Do you think the budget request of your bureau adequately correspond to the programs your bureau carries out?
- A. Yes
  - B. Partially
  - C. No
7. If budget request of your bureau does not adequately correspond to the program what are the major reasons for budget fall shorts?
- A. Lack of skilled manpower
  - B. Government budget allocation choice
  - C. Lack of training
  - D. Others (please specify) \_\_\_\_\_  
\_\_\_\_\_
8. Who do participant in the process of budget preparation in your bureau?
- A. Plan and program expert of the bureau
  - B. Department/section heads
  - C. All of the above
  - D. Others (please specify)

9. Please specify what problems face your bureau during the budget preparation, execution and utilization.

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10. Dose your bureau apply performance measure during expenditure utilization?

A. Yes

B. No

11. If your answer to question number 10 is No, please why it is so.

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12. Does your bureau have periodic training scheme to upgrade the capacity of the staff?

A. Yes

B. No

13. If your answer to question number 12 is yes, how do you evaluate the training schemes?

A. Appropriate

B. Inappropriate

14. If your answer to question number 12 is Inappropriate, please list down problems you have so far observed? \_\_\_\_\_

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15. What are the benefits of the new introduced accounting system? Please describe below. \_\_\_\_\_

16. How are foreign aids and assistance included in the budget preparation of your bureau?

- A. Totally included in the bureau budget
- B. Partially included in the bureau budget
- C. Not included in the bureau budget
- D. Others (please specify) \_\_\_\_\_

17. How are priorities of capital projects set up?

- A. through government priorities and programs
- B. through priorities of donors
- C. combination of "A" and "B"
- D. Others (please specify) \_\_\_\_\_

18. Does the public procurement system used to provide effective use of public funds?

- A. Yes
- B. No
- C. to some extent
- D. Others (please specify)

19. If your answer for question number 18 is No, please list down some problems.

20. What is your opinion on the existing internal control system?

- A. Effective
- B. Moderate
- C. Ineffective

21. Who carries out the financial performance audit during the budget period?

- A. the General Auditor of the region
- B. Internal Auditor of the sector bureau
- C. Others (please specify) \_\_\_\_\_

\_\_\_\_\_

22. What was the opinion given by auditors about the performance of your bureau for the last year?

- A. Adequate
- B. Inadequate
- C. Un auditable

23. What was the time interval between the end of the fiscal year and the routine booking of transaction?

- A. One month
- B. Two months
- C. Between two months and six months
- D. Others (please specify) \_\_\_\_\_

\_\_\_\_\_

Please add any comments what you consider major challenges of expenditure management practice of your bureau. \_\_\_\_\_

\_\_\_\_\_

## Annex B

### Check list of guiding questions for the focus group discussion

1. The linkage between strategic plan and annual budgeting in the bureau
2. Weakness and strengths of the current practice of expenditure management in the bureau
3. Participation of staff and other stakeholders in planning, budget preparation and evaluation.
4. Relation with other respective bureau of the region regarding evaluation and controlling of fund flow to the bureau
5. Accountability for effective use of budget
6. Procedure and capacity to follow up, monitor and control the utilization of budget, procurement and audit functionalities
7. The level of budget execution, problems and measures to improve budget execution
8. Are all donor funds included in government budget? If not why?
9. Is there any conditionality set by donors?
10. The difference between the previous and new accounting system
11. the practices of daily balancing, bank reconciliation, annual closing and regular reporting
12. Staff situation regarding to their capacity, training and turn over composition.
13. Organization of the internal audit section, the contribution of internal audit section regard from misuse of resources
14. The quality, integrity and timely submission of financial reports and bank reconciliation for donor fund flow and approved government budget

## Annex C


Checklist of guiding questions during the interview with chief administrators of the bureau.

1. Does the draft budget of your bureau show a clear and comprehensive plan for all spending including all extra budgetary fund?
2. Do you know the entire approved budget from different source of finance allocated to your bureau?
3. Is there a mechanism to ensure that the allocation of budget for capital budget projects and work done by your bureau periodically evaluated?
4. Does your bureau face budget deficit? If so, how is it was captured?
5. Is there a systematic training and orientation program for staff in of your bureau?
6. During purchasing goods and services, does your bureau have clear planning and specification?
7. Is a register of real property asset maintained?
8. How are physical assets accounted for? How are such fixed assets valued? Are charges for depreciation made on systematic base?
9. What kind of financial analysis and reporting are made on the base of the accounting system?
10. Does mandate of internal audit clearly specified of your bureau.
11. What are the problems to carry out effective public expenditure management in your bureau?

## DECLARATION

I declare that this thesis is my original work and has not been presented for a degree in any university and all the sources of materials used for this thesis are duly acknowledge.

Name: Shishay Teferi


Signature: 

Date: January 31, 2010

Place: Addis Ababa University

I confirm that this thesis has been submitted with my approval as an academic advisor.

Issac Paul (PhD)

Signature: 

Date: January 31, 2010

