The Budget Handbook

understanding and working with Malawi's finances

Compiled by:
Phoenix Securities and Management and
The National Democratic Institute for International Affairs

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INTRODUCTION

Introduction

At the request of the Speaker of the National Assembly, the National Democratic Institute for International Affairs (NDI) has devoted much of its program activity to strengthening the existing committee system. NDI has targeted the committees that are most important to parliament and that have the greatest impact on the nation.

In May 1996, NDI invited Mr. Leon Cohen, Chair of the Guateng Provincial Legislature's Budget and Finance Committee, to speak to members of the Malawi Budget and Finance Committee about the budget process in South Africa. From this initial meeting, a recommendation was made to identify a budget expert who could assist the committee on a long-term basis. This was a tall order to fill; thus, a decision was made to try a different approach to assisting the committee members. Rather than going outside the country, NDI decided to identify local budget and economic experts who could explain the budget process and who could later be called upon by the Committee if additional answers were required to very specific questions.

In addition to the seminar, NDI and Phoenix Securities and Management developed the enclosed budget handbook which will hopefully provide those who use it with the necessary information to effectively read, evaluate and comment on the national budget.

Every attempt has been made to ensure that the information contained in this handbook is relevant and accurate. However, as with most processes which are dynamic, it is hoped that this book will continue to evolve and expand as the budget process in Malawi become more standardized.

A special thanks to those individuals who provided assistance in putting this handbook together:

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Please feel free to send us recommendations for changes and any other feedback.

Consuella Brown
Program Director
February 1997

HOW TO READ A BUDGET

WHAT IS A BUDGET ?

Budget *noun* 1. A financial statement of estimated income and expenses of a country for a period of time; also a plan for financing a government based on such a statement.

2. Loosely, the cost of operation, living, etc.; as, a minimum weekly *budget* for a family of five.

verb To put or allow for in a budget.

Webster's New Collegiate Dictionary

So we can therefore say that a budget is a forecast of how much money is likely or expected to be earned over a specific period of time *and further*, it is a working plan as to how that money should be spent.

In terms of governmental budgets, the specific period of time is usually one year, known as a fiscal or *financial year*, which is normally divided up into four *quarters* of three months each. The date upon which the financial year begins is set principally for administrative convenience, and in Malawi, the financial year for the government begins on 1st April and ends 31st of March.

Budget policy is a critical part of any government's economic policy. Shifts in proportional allocation can be looked upon as a key indicator of the government's priorities in the coming financial year.

WHAT IS IN THE MALAWI NATIONAL BUDGET ?

The Malawi National Budget generally contains first, *the financial statement*, which will be a brief explanation of what were the goals to be achieved in the previous financial year's budget and how well the aims and objectives were executed. The financial statement, in short, should tell us *where we are now*. It tells us what the financial performance of the government was in the previous year and tells us briefly which areas shall be highlighted in the next year's estimates.

Following the financial statement are *tables* which summarize estimated recurrent expenditures, estimates of revenues, the budget summaries and economic classification of recurrent expenditure.

The next section, which is the main bulk of the budget document, deals with each individual *vote*. The term "vote" in this context means the budget for the individual ministries, independent offices, departments, etc. Each vote begins with a page called the *treasury memorandum* The treasury memorandum is a brief description of what the particular organization that is the subject of that particular entry does and is intended to do. It finally states the approved and revised budget for the previous year and the budget estimate for the coming financial year.

The next part of the vote is the detailed breakdown of ;

(1) the actual expenditure for the previous financial year,

(2) the approved and revised expenditure for the current financial year, and

(3) the budget estimate for the coming financial year.

This breakdown is further split into sections A, B and C for ease of reference. Section A is a simple statement of the amount estimated amount necessary to carry out basicoperations for the financial year. Section B is a summary of the estimates per program, and section C details how the money is spent in each program.

Each vote concludes with an *appendix* which is composed of the staff breakdown indicating number of personnel at each grade.

Also included in the budget estimates is a new section called the Malawi Medium Term Expenditure Framework or MTEF. This is a pilot program intended to improve and the budget process "that will facilitate a long lasting improvement in the management of public resources." The MTEF was introduced in Financial Year 1996/97 in four ministries; Health, Agriculture, Education and Works as well as in the Malawi Police Force. Among the program aims is the goal to assist ministries and departments to decide what programs are indeed their priorities and to plan and allocate available funds accordingly. This year the program will expand to cover more ministries and departments with the eventual goal of the entire budget process, both recurrent and developmental, being formalized

The final section of the budget document is the *appendices*.

HOW IS THE MONEY COLLECTED AND HOW IS IT SPENT ?

The principal means by which the Government finds money to implement it's programs is by revenue collection through The Department of Customs and Excise and through The Department of Income Tax. Through these departments taxes on income and profits such as company tax, individual taxes (P.A.Y.E, graduated, withholding, etc.), property taxes, taxes on goods and services such as surtax and licenses (motor vehicle, business and professional), international trade taxes such as customs and import duties, as well from non-tax revenues such as treasury fund receipts, fees and departmental receipts, reimbursements and rents.

Please refer to appendix # 1 for pie charts illustrating Central Goverment Revenues

How the government spends its revenues is of course what the entire budget procedure is all about. Herein lies the fundamental questions of "why the paymentof taxes is vital and what can the citizens of Malawi expect in return?". Those

questions will be addressed below, but here we are more interested in the mechanics of "how". The major
areas of spending can be broken down into general services, social services, economic services and unallocable services.

Please refer to appendices #s 2 and 3

WHO PREPARES THE NATIONAL BUDGET AND HOW?

There are two types of budgets in Malawi. The recurrent budget and the development budget. The recurrent budget includes those expenditures estimates that can be covered by Revenue collected by the government. The development budget is comprised of funding amounts for projects that will be sustained by monies from Malawi's donor partners.

The Recurrent Budget

The process of preparing the recurrent budget is commonly referred to as "The Budget Cycle". It is not, as in some countries, a definitive process with set procedures on a precise timetable, it is rather a more flexible progression toward what is hoped to be an acceptable compromise.

Generally, it can be said to begin with the Budget Department of the Ministry of Finance. The Treasury will generally write the ministries in October instructing them to begin preparing estimates of their needs in the coming financial year. This will be done by section heads and they will in turn submit these estimates to department management who will be given the task of collating the information from all sections in the department before submitting it to the ministry of administrators. After review by the ministry administrators, the estimates for the entire ministry are submitted to the Treasury.

Meanwhile, the Treasury and Economic Planning & Development (EP&D)with the assistance from the Reserve Bank of

Malawi conduct consultations with the International Monetary Fund (IMF) and the World Bank to establish a rough idea and create a forecast of the next financial year's revenues, expected Gross Domestic Product (GDP) and likely inflation and compare this data to the intended levels of the government's spending. These consultations which are on-going through out the financial year and during the budget cycle result in the Policy Formulation Paper (PFP), a policy and objectives guideline, which contains the figures for expected GDP growth, inflation, expected revenues and an agreed upon "ceiling" to be used in the total expenditure allotments for the coming year. This agreement is then tabled before the Cabinet for their revision and approval and an instruction is then sent through the Treasury to advise the ministries of their respective ceilings.

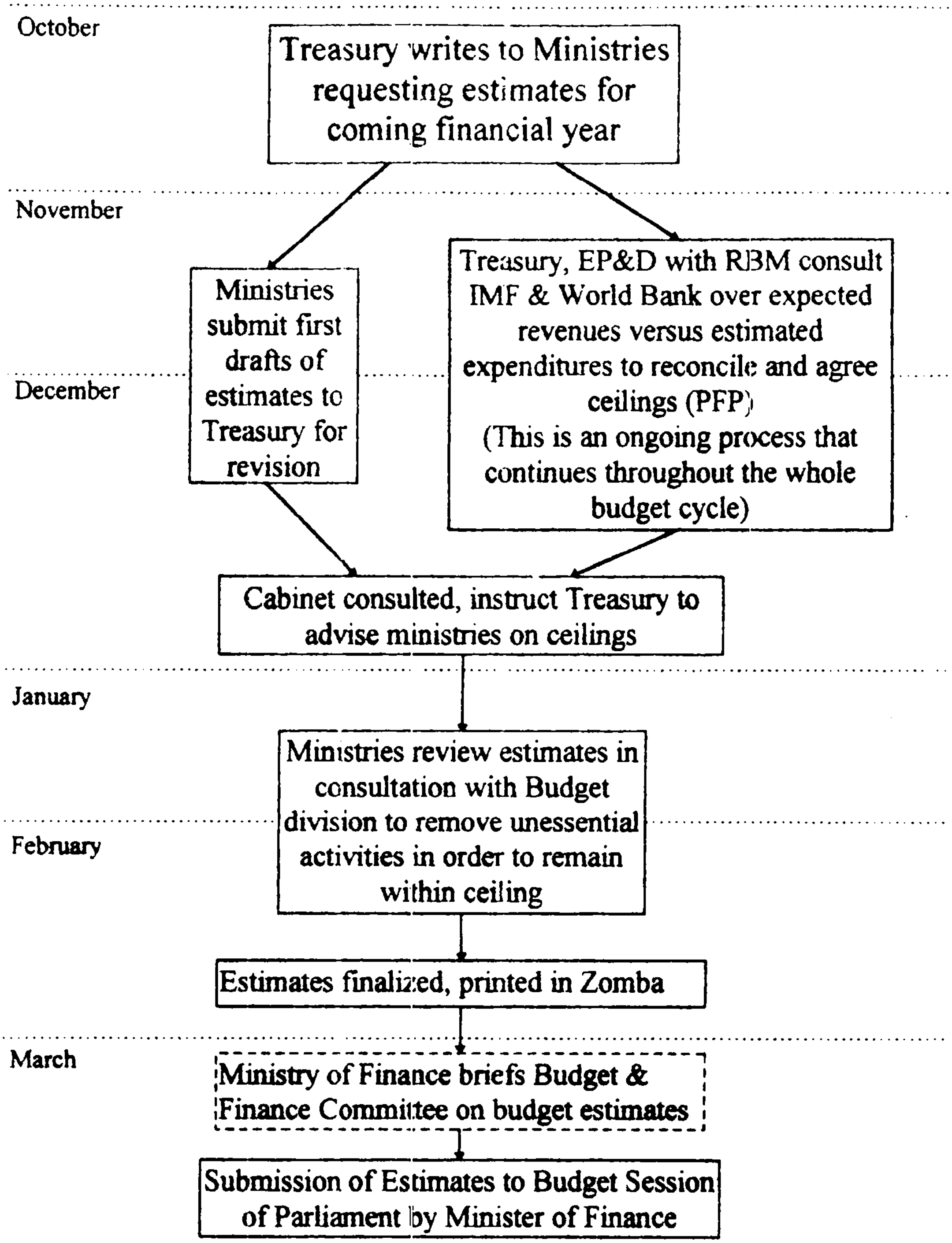
At this point in the process,the ministries have of course already prepared their first drafts of estimates; yet it is likely that these estimates will exceed the ceiling, thereby necessitating a need to review their costs and program priorities and eventually re-submit these after long, often painful discussions with the Treasury about removing "unessential activities" in order to stay within their allocated limits. This process has to be completed by middle to late February so that figures can be collated, checked and double checked before being printed in Zomba.

As the estimates of expenditure near final completion the Minister of Finance will confer with the Budget and Finance Committee of Parliament and brief them on the budget estimates for the approaching financial year.

In March the Budget Session of Parliament begins with the Minister of Finance making his/her annual speech on the government's past performance and it's economic plans for the coming financial year. This is of course followed by parliamentary debate, amendment and eventual approval of the budget, barring unforeseen complications.

Please refer to "The Budget Cycle" flow chart below

The Budget Cycle-Recurrent Expenditure



The Development Budget

The preparation of the development budget is largely done by EP&D in consultation with the particular ministries involved in the individual projects. EP&D receives project proposals from the ministries in April and May and after scrutiny of the projects submitted, begins discussions with the ministries in June.

If projects submitted are acceptable and fall within the scope of the Public Sector Investment Program (PSIP), funding is made available. For those projects not immediately funded but deemed to be worthwhile, EP&D will assist the ministry concerned to locate donor assistance.

Please refer to appendix # 4

HOW DOES THE BUDGET AFFECT THE PEOPLE IN MALAWI ?

The question of cause and effect on the people of Malawi in regards to the National Budget and it's effect can best be addressed on citizenry is posed is best answered by looking at taxation and what services and benefits the government derives from this revenue.

First of all it must be noted that in FY1996/97 projected estimates assumed that revenue from customs and excise would be more than twice the amount expected to be raised from income tax. Of a total labor force of approximately 4 million people in 1992, only 559,042 of them were in paid formal employment, of whom 79.1% were in the private sector? The remainder were working mainly in small scale agriculture and micro-business according to The Economist Intelligence Unit.

What this essentially meant was that roughly 85% of the labor force was being taxed only indirectly through surtax and other instruments so insignificant as to rarely be noticed at all. This also meant that the burden of taxation was carried by 15% of individuals and companies in Malawi that were easier for the government to track and find.

It is also assumed that those companies and individuals who import goods from abroad either do so with the intention of either reselling those goods for profit or have sufficient disposable income to spend on personal luxury goods. When these people/companies are assessed with duties on their imports they are fully aware of the rates of duty which shall be assessed against them and (though they may not be happy about it, they) plan accordingly.

In return for these obligations placed on the citizenry by the government, certain benefits are expected by those same citizens to be provided by the government in the form of services. Such basics as Defense and Justice are perhaps two of the most essential reasons for the existence of a revenue base for essential services. It is social services such as education and health and the Economic services such as transport and posts and telecommunications that different administrations give varying degrees of importance to that become the basis for real contention. For example a commercial farmer in the rural areas will be far more interested in how much of the budget is spent on building and maintaining road networks to the major markets than if a certain ministry has sufficient cleaning materials. Likewise, if one is a businessman engaged in foreign trade, the reliability of the posts and telecommunications network as well as the road conditions would be ones primary concerns. But for the vast majority of the people of Malawi, living at or below the poverty line, it is the social services such as availability of medicine, access to clean water guarantee of personal safety and free education which have the greatest impact on their daily lives and ultinately the future of their children.

How To Read The Budget

Reading a budget is an often confusing exercise that can be simplified if you take the proper steps. Very often the first problem a layman is likely to have is that he is given a mass of information, and not knowing where to begin, he will likely try to read straight through from beginning to end as if it were a novel. This is not an effective way to proceed because very few people can absorb this kind of information. The usual result is that at the end he has read almost every single word of a large document but has probably not even a vaguely useful understanding of what has passed before his eyes.

First of all you need to know what you are looking for, then you can proceed from there.

Step 1. When you first open up the budget estimates you will come to the table of contents which will tell you on which page to find the particular vote you are looking for.

Step 2. Go to the FINANCIAL STATEMENT. This will tell you the budget performance of the past financial year, which will include revenue performance and expenditure. It will also include BUDGET ESTIMATES for the next financial year and the planned recurrent expenditure.

Step 3. You are now ready to turn to the Vote which you want to know more about. For the sake of this exercise, we shall say that we are looking at Vote 039 : Ministry of Commerce and Industry.

Step 4. The vote begins with a preface page called the TREASURY MEMORANDUM which will give you a brief description of the functions of that particular Ministry. It will tell you the main departments that make up that Ministry, and you will also find the current and future priorities of the Ministry. Lastly the TREASURY MEMORANDUM will indicate the amounts that will be required to carry out the activities of the Ministry for the coming financial year.

Step 5. Now you are ready to read the VOTE. As you look at the lay out of the page, the first thing you will find below the vote number and name of the ministry will be section "A". This section, very briefly, states the estimated required amount to fulfill the ministry's function for the upcoming financial year.

Step 6. Section "B" is a summary of the estimates per program for the individual programs that the ministry shall carry out. The programs shall first be listed by their titles and estimated resources. At the end of that section you will see a row that says "total amount" and from here you can gauge the allocations over time so as to make it easier to compare percentage of allocations over time with other Ministries.

Step 7. Section "C" gives a more detailed expenditure per individual program such as the personal emoluments, goods and services and capital formation.

Step 8. As you look at the page on the Ministry programs you will notice that you have the text on the left and numbers on the right. The numbers are in a series of columns. First you will notice all the columns have been labeled as; "Actual", "Approved", "Revised" and the last column, "Estimates".

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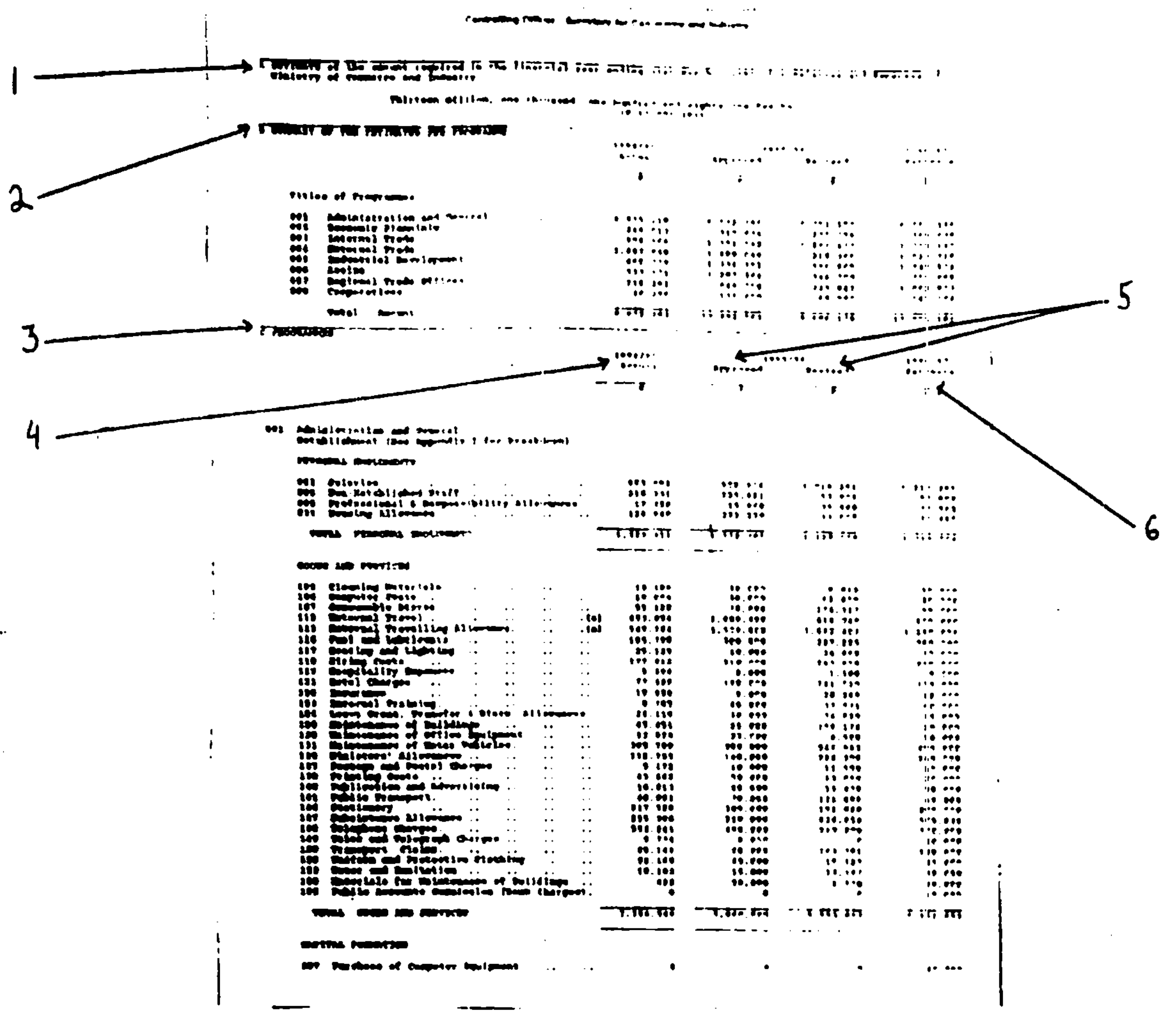
Please refer to the following page for a sample page from a "Vote"



(1) Section A : Estimates of the amounts for the Financial Year.

(2) Section B : Summary of Estimates Per Programme.

(3) Section C : Programmes; gives detailed breakdown of expenditure per individual programme.

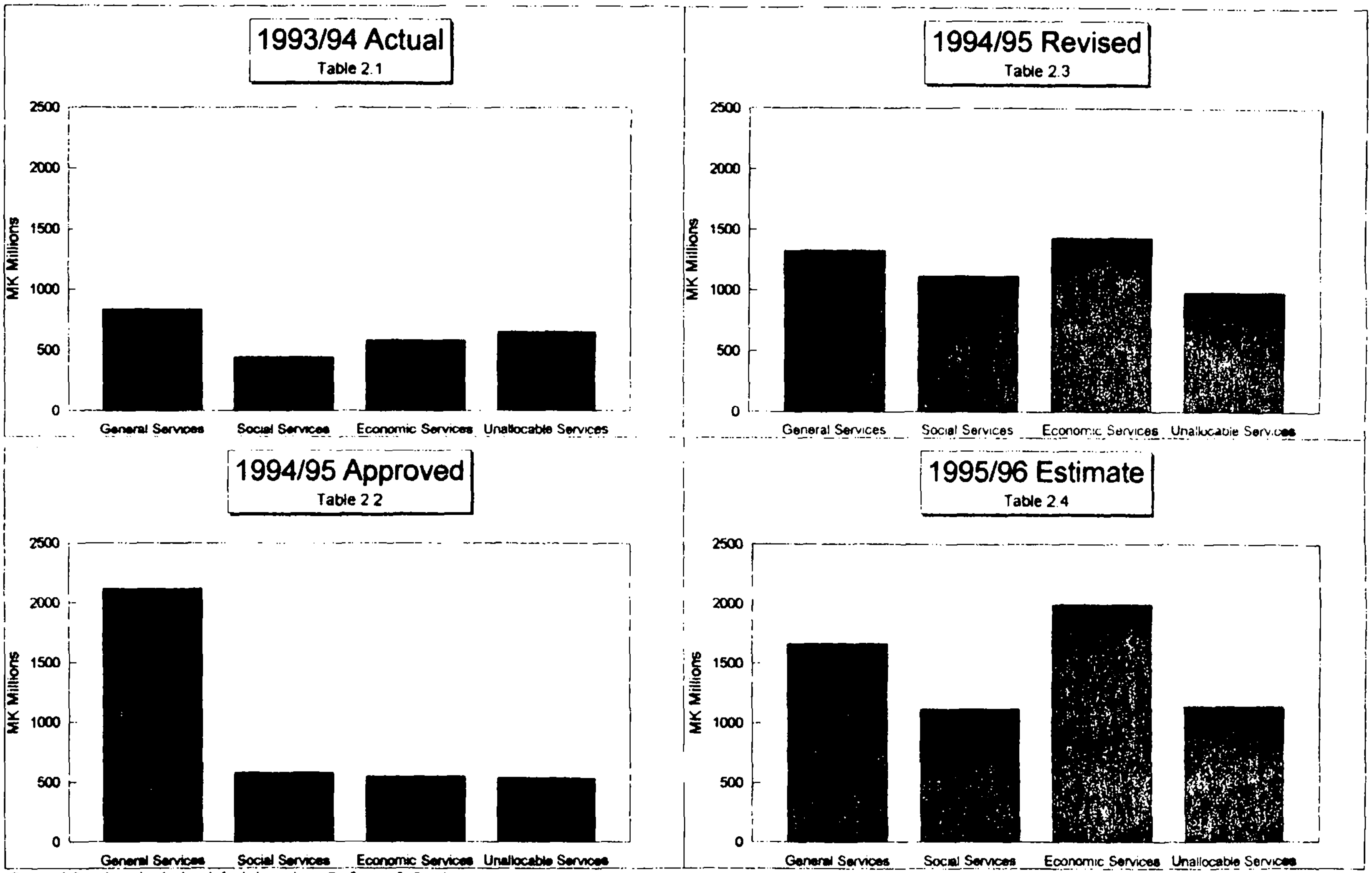
(4) The Actual column contains the expenditure for the previous year as captured by the Accountant General's office.

(5) The Approved and Revised columns are to be looked at together as they are both for the current year. The approved column will reveal the amount Parliament has authorized to be spent during the current financial year. The revised column will show you how much the ministry is likely to spend for the year at their current rate of spending.

(6) The last column is labeled Estimates and it will tell you the amount Parliament will be asked to approve as expenditure for the upcoming financial year.

BUDGET APPENDICES

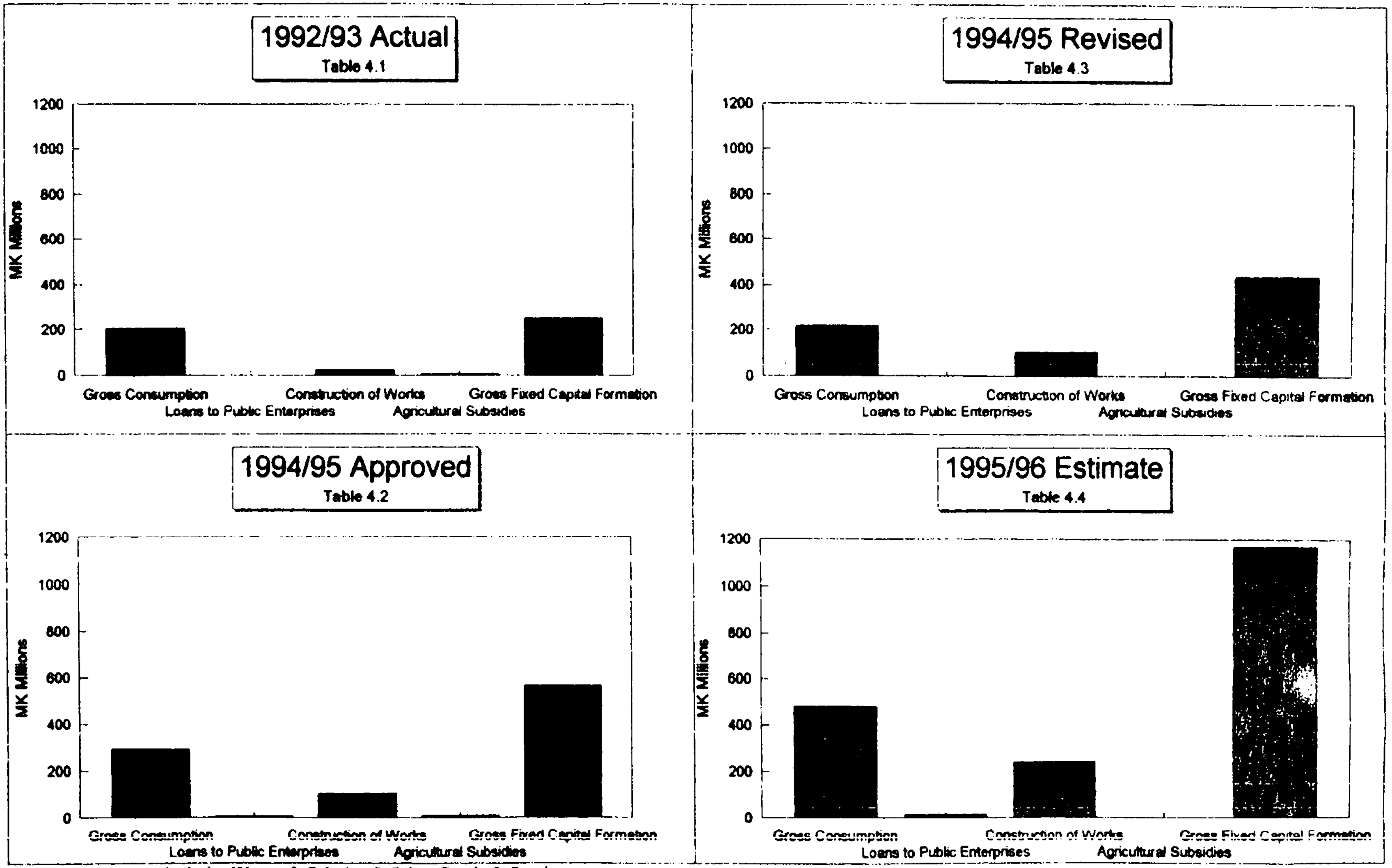
Functional Classification of Central Government Recurrent Expenditure



General Services include: Administration, Defence & Justice.
Social Services include: Education, Health & Community & Social Development.
Economic Services include: Natural Resources, Transport, Posts & Telecoms.
Unallocable Services include: Public Debt servicing, Pensions & Gratuities.

Source: Ministry of Finance/Economic Report 1995

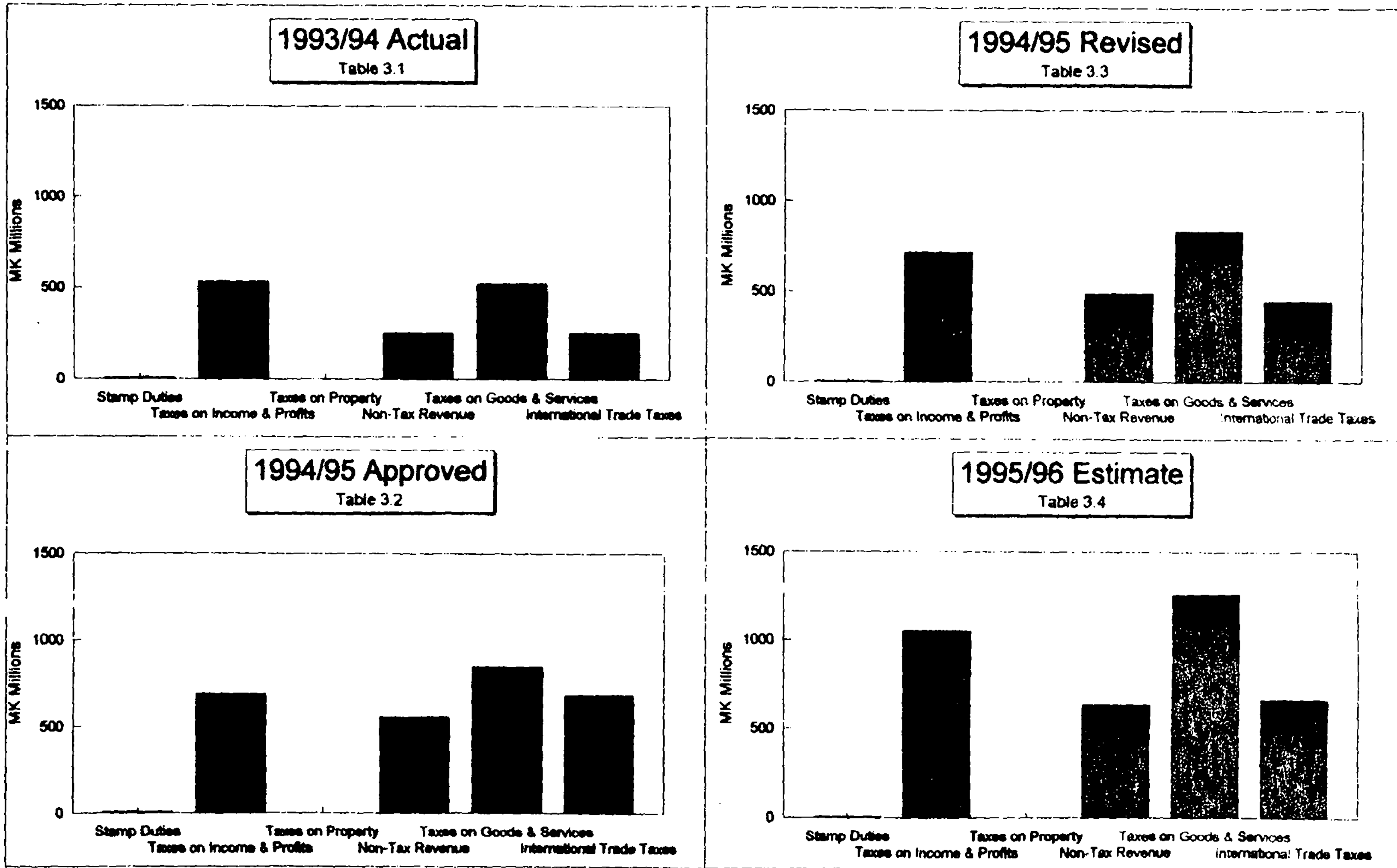
Economic Classification of Development Expenditures



Gross Consumption includes Wages & Salaries & Other Goods & Services.
Gross Fixed Capital Formation includes buildings.
Construction of Works includes Roads & Bridges, Services & Equipment.

Source: Ministry of Finance/Economic Report 1995

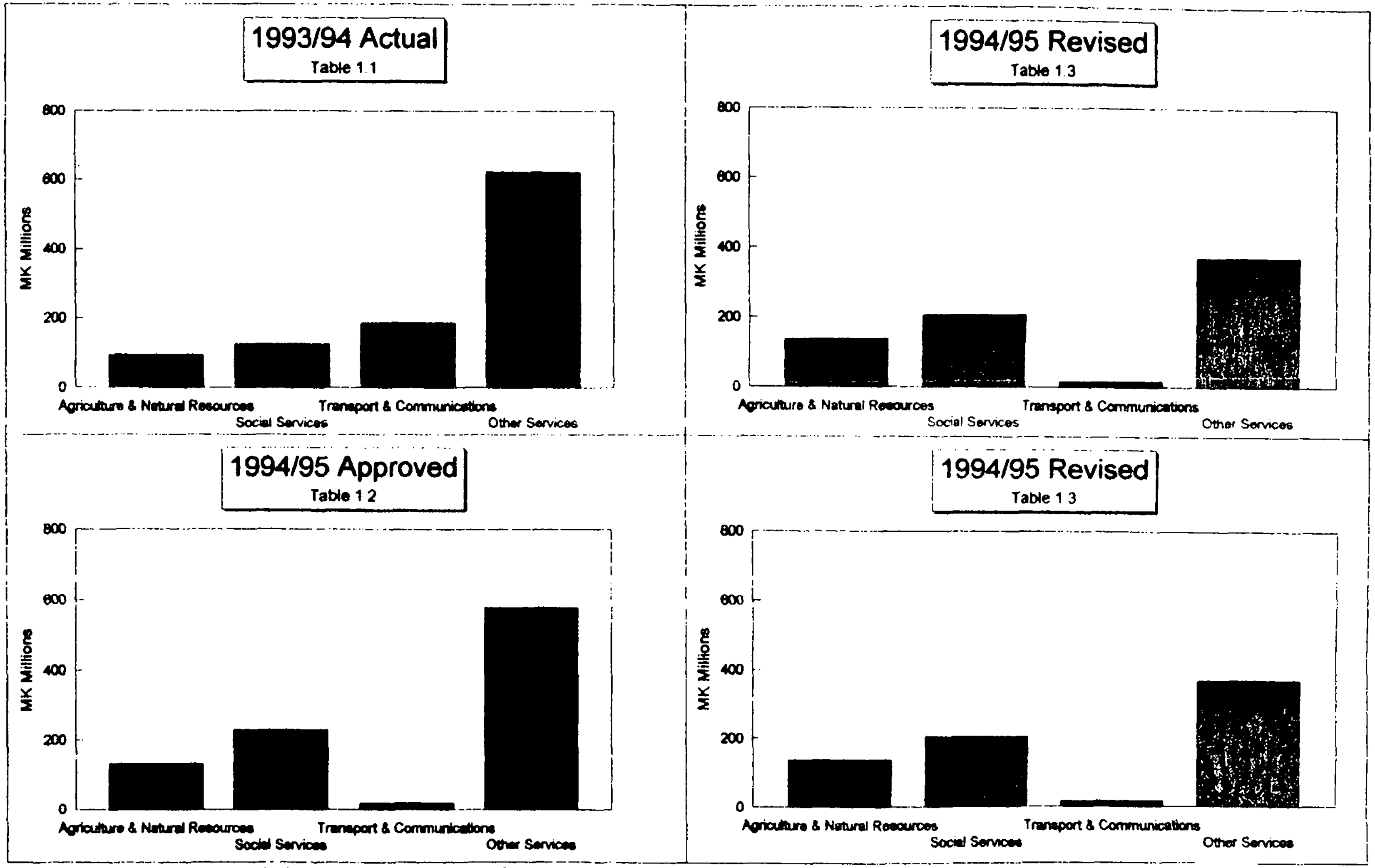
Central Government Revenue



Taxes on Income & Profits includes taxes on individuals and Companies
Taxes on Goods & Properties includes taxes on Accomodation & Refreshment, Surtax, Excise Duties & Licenses.
International Trade Taxes includes Customs & Import duties.
Non-Tax Revenue includes Treasury fund receipts, Rents, Departmental receipts, Drought Levy, Fuel Stabilization Fund & Reimbursements

Source: Ministry of Finance/Economic Report 1995

Central Government Development Expenditure by Main Heads



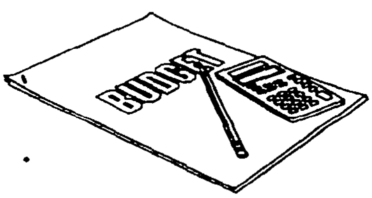
Agriculture & Natural Resources includes: Agriculture, Forestry & Game, Veterinary Service, Surveys & Lands & Fisheries
Social Services include: Education, Health & Community & Social Development.
Transport & Communications includes: Transport & Post & Telecoms.
Other Services includes:Power,Government buildings,Housing,Water & Sanitation,Finance,Commerce & Industry & Works.

Source: Ministry of Finance/Economic Report 1995

OVERSIGHT

The Importance of Budget Oversight

The function of budgetary oversight serves many democratic and governance functions . Primarily, as a balance of power between the executive and the legislature and more specifically another avenue for the people of a country to express their concerns and needs to the government. Therefore, at its base, oversight's most important function is to make sure that funds are being properly allocated as desired by the people.



By reducing the likelihood of budgetary irresponsibility the government is able to make the most of the limited resources that are available. Effective budget consultations protects from funds being wasted on projects that do not provide adequate results per expense. In all countries there is a lack of funds to address all the desired programmes. No matter how wealthy a country is, its government must make hard budgeting decisions regarding what programmes will get funded and at what levels.

There is always the potential temptation for personal gain to be made by using knowledge of budget and tax information is always a danger. The use of sensitive information to reap private wealth is universal to all budgets, public and private. The only method for stemming this danger is to introduce transparency as soon as is feasible to the budget process. While there is always a need to conduct budget prioritizing privately, the need to keep this information from public view after it has been decided serves no function other than to introduce the potential for private gain and fostering public distrust.

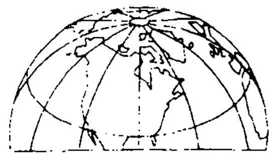
Effective budget consultations protect from waste and provide adequate results per expense

Budget Oversight by Other Countries, a Comparison

There are many approaches to budget oversight. Each method is unique to the legislative model within that particular country. For instance, in many Commonwealth countries a certain unchangeable amount of funds are made available for ministries to spend. While in some Federal style democracies a system of sequestrations is established that automatically cuts programmes once the spending limits have been breached. However, implicit in all of these systems is the mandate to achieve a certain level of accountability and transperancy at the executive level.

No budget process is completly free of problems that may in directly circumvent the process; however, please find below three models of legislative oversight from the Canada, South Africa and the United States.

CANADA



Canada's two-chamber, parliament has the main responsibility for legislation. The Prime Minister usually selects his cabinet from the seated members of the House and occasional from the un-elected, Senate.

The Minister of Finance is one of the most active members of the cabinet and he is primarily responsible for providing Parliament with broad based economic decisions. He is also a member of the Treasury Board on which several other cabinet Ministers sit. It is this board's duty to oversee the integrity of the financial, resource and management aspects of all government programmes. They are also supposed to provide all resource estimates for future programmes. The final budget manager for the executive is the Comptroller General who is entrusted to establish that all government departments are being operated responsibly.

Direct budgetary oversight for Parliament comes when it receives two budget documents. The first is as the budget itself, delivered by the Minister of Finance. The second comes from the President of the Treasury Board and contains the Main and Supplementary Budget estimates as they have been approved by the entire Board. Sometimes provided along with these documents is an assessment of the economic environment with a medium-term economic forecast. These are all delivered within two months of the start of the new fiscal year. This informative process and the ability to provide interim funding gives the Canadian Parliament a vital facet of the budget oversight process, time for consideration.

An extensive system of post-budget discussions exist to provide feedback

Once at the Parliament, these documents are examined by the sectoral committees and continue to be considered past the beginning of the new fiscal year (April 1), usually for a total of four months. The duration of this phase creates a budget crisis which is handled by Parliament granting interim spending authority for departments. This keeps the government operating.

The Main Estimates reach the floor of the Parliament usually about six weeks prior to the start of the new fiscal year. During the consideration of this document, the Canadian Parliament will usually approve of less than 30% of the recommended spending. Furthermore, the Executive can only increase the amounts to be spent after Parliamentary assent. In finalizing their budget both the House and Senate sit as a Committee of the Whole to vote on the Main Estimates. Once this has occurred, usually by the end of June, Canada has passed its budget.

This is not the conclusion of the Parliamentary oversight for their budget. An extensive system of post-budget discussions exist to provide feedback. By having an ongoing examination of the budget, its expenses and projected costs, Canada is in a perpetual budget drafting and editing cycle. One budget doesn't so much end as it does meld into the next one. This would not be possible if it weren't for the continual exchange of information between the Parliament and Cabinet.

Many changes have been made to the Canadian budget system over the past few years. The highest priority was to open the system. The Canadian Parliament believes that a greater degree of public input improves the overall system of taxes and spending. The level of secrecy involved in their budget system in the past had caused an uncomfortable feeling of mistrust from Parliament and the people. Public hearings by the House of Commons Finance Committee well before the Fiscal New Year not only includes the people in the budget system but also provides valuable information for the MPs while sparking public interest and debate. This extra layer of information allows the Parliament to better consider the budget once it's on the floor. Various Ministers also have pre- and meetings with citizen groups.

SOUTH AFRICA

Having emerged from a closed government during the past few years, South Africa has faced some unique government challenges. Among these are the revamping of its Parliamentary consideration of the national budget. Following are opinions from concerned parties on what is currently wrong with the system and how it can be made better.

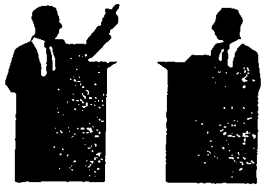
Iraj Abedian, of the School of Economics at the University of Cape Town, believes that the time constraints put on the S.A. Parliament has reduced them to nothing more than a rubber stamp of approval for the budget regardless of any changes they may want to make. Furthermore, the time frame for consideration of the Budget in South Africa is far too short for the proper examination of the document. According to South African MP, Ken Andrew, just the ability to examine the budget is not enough. Along with the ability to scrutinize should be the power to amend. But not total power of amendment; he believes there should be parameters for such action. Barbara Hogan, South African MP, also sees the necessity in the Parliament taking part in the budget process, but she does not recognize any validity in them actually being involved in the executive process of developing the budget's financial estimates. According to her, the relationship should be based on "joint problem solving" between the two bodies. In this system the Legislature is empowered to provide the public with an opportunity to be heard concerning the budget.

Further developing this concept is James McCrindell from the Canadian Treasury Board. He also feels that the South African budget systems will be improved through creating a balance of responsibilities. He recommends that South Africa should also consider the need for transparency with freedom for independent criticism. The sharing of information between the Parliament and Executive is a vital aspect of the government's responsibility of drafting and enacting a legitimate budget.

Direct accountability for the work is also a shared responsibility

The common thread between all these recommendations is the creation of an oversight system. First is the concept that oversight needs to be placed within the budgeting framework. The Parliament's being engaged in composing the budget is the most basic type of oversight. The next idea places parameters on the ability to oversee.

By establishing set areas of interaction the people involved will more easily be able to perform their roles. This leads to the next area of concern. The recommendation is made that the executive should develop the budget without Parliamentary influence makes for a separation of responsibility. Coming from this is a direct accountability for the work done while there is also a shared responsibility to complete the task. Finally, is the recommendation to open the system and to be scrutinized by external participants. This may include having open hearings, making the budget proposal public prior to its consideration in Parliament, issuing press releases, having press conferences and allowing the media to interact with all participants in the budget process. Once a budget system is open to the public, under the joint direction of the executive and Parliament there is less reason for concern; transparency brings responsive accountability.



THE UNITED STATES

In the United States a system of "Checks and Balances" traditionally describes the relationship between the Executive and Legislature. This is most evident during the annual budget process. The importance of representative budget practices is seen in the fact that over the past few years the disagreements between the two branches of government has been illustrated out during the consideration of the federal budget. This is not to say that their system is primarily dysfunctional, it is merely a symptom of the equal sharing of budget responsibilities.
The amount of time and attention that is given to the annual federal budget in the United States is the bedrock of the Congressional oversight.
Even though the President is required to send his own version of the budget to Congress, the Budget Committees write their own. This happens every year, even when the Chairman is of the same political party as the President. Having two or three different budget documents does not mean they are completely at odds, most of the spending changes from one to the other represents a minority of the total federal expenses. But it is this amount that the most political disputes arise.

Budget oversight includes a series of Committee and Sub-Committee hearings with in-depth questioning of witnesses

Before the budget is considered by either Congressional body several oversight actions are taken by each Committee. These include a series of Committee and Sub-Committee hearings with in-depth questioning of witnesses. These are the people who are responsible for drafting the budget figures as well as testimony from concerned parties who are lobbying for funds. All of the hearings are open to the public and many are televised.

Another step in the process is

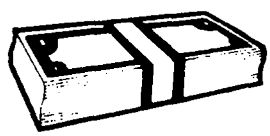
the Committee's consideration of the budget. It is at this time that Committee members offer amendments. After this consideration is complete the report on the budget, known as the "Chairman's Mark", is made public as soon as possible. This allows for each Congressional Committee to read how the programs within their jurisdiction are going to be funded.

The Congress has its own internal oversight provisions. These restrict the amount of time the budget will be considered and provide a germaneness tests within which floor amendments must be considered. The primary rule for Budgets amendments are that they cannot worsen the deficit and cannot create new legislation. Even with these constraints many budget changes are made and political battles are fought through amendments.

The root of the power held by Congress is a hold-over from the Colonial times when it was learned from the British that the Parliament should have the 'power of the purse.' The United States Constitution states in Article 1 Section 7 that "All Bills for raising Revenue shall originate in the House of Representatives; but the Senate may propose or concur with Amendments as on other bills;" later Section 8 states. "The Congress shall have Power to lay and collect Taxes, Duties, Imposts and Excises, to pay Debts and provide for the common Defense and general Welfare of the United States." This codifies primary Congressional oversight in the document that is the base on which the U.S government is founded.

The President must sign the document to make it a law. If he disagrees to the spending it will usually receive a veto. It is at this time that much of each branch of government's ability to act independently is tested. This is when both branches run the risk of shutting down the federal government. For millions of people this means vital services stop. Social security checks don't go out, farm subsidies stop, Federal parks are closed and passports and travel visas aren't issued just to name a few programs that get effected. This is much more the exception than the rule; in many years there are joint Congressional-White House meetings that are convened simply to 'hammer out a deal' for the federal budget. In many of these session the best programs and deficit reduction measures are made.

The sharing of responsibility for drafting the federal budget in the United States instills the public's trust in both branches of government. Since all sides are considered, from witnesses in hearings, to the majority and minority members of the Budget Committees, by the members amendments on House and Senate floors and with Executive participation at the start and conclusion, no voter can feel as though they were not represented or informed during the drafting, consideration and signing of the federal budget. All throughout the process the media and interest groups are there to observe and comment.



Budget in Brief

The Honourable Paul Martin, P.C., M.P.
Minister of Finance

March 6, 1996

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"Seldom, in our history, have so many experienced such anxiety. Canadians feel our very way of life is at risk.

If there is one obligation before government today, it is to do its part to address these deep concerns. It is to do what we must so that confidence can overcome anxiety, and hope can replace despair. In short, we must act now to help Canadians secure their future.

Canadians know this can't be done by government alone. It will require the concerted efforts of individual Canadians, their governments, business and others for our country to tackle these challenges effectively. What Canadians want from their government is for it to set the goals, to have a plan and then to work as hard as it can – and as long as it must – to help get the job done."

The Honourable Paul Martin, P.C., M.P.
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Securing the Future

The 1996 budget consolidates and extends the actions taken under the comprehensive strategy set out in the 1994 and 1995 budgets. The three budgets work together to help Canadians secure their future in a number of key areas:

Securing our financial future: The government's fiscal goals will be met or exceeded, year by year, through sustained reductions in government program spending.

Getting government right: Further action is being taken to define a more appropriate and effective role for the federal government in the modern economy and federation.

Securing social programs for the next century: The government is acting to restore confidence in the old age security system and provide a secure, stable and growing system of federal support for medicare, post-secondary education and social assistance.

Investing in the future: The government has reallocated money to new investments in priority initiatives to support youth, technology and international trade – areas critical to future jobs and growth.

Securing Our Financial Future

The deficit: Actions set in motion in the 1994 and 1995 budgets ensure that the deficit targets for 1995-96 and 1996-97 will be achieved. This budget secures the government's deficit target of 2 per cent of GDP in 1997-98 and takes action to ensure ongoing deficit reduction. The deficit track, year by year:

1993-94 – $42 billion (5.9 per cent of GDP)
1994-95 – $37.5 billion (5.0 per cent of GDP)
1995-96 – $32.7 billion (4.2 per cent of GDP)
1996-97 – $24.3 billion (3 per cent of GDP)
1997-98 – $17 billion (2 per cent of GDP)

Table 1
Summary statement of transactions:
Fiscal outlook with budget measures

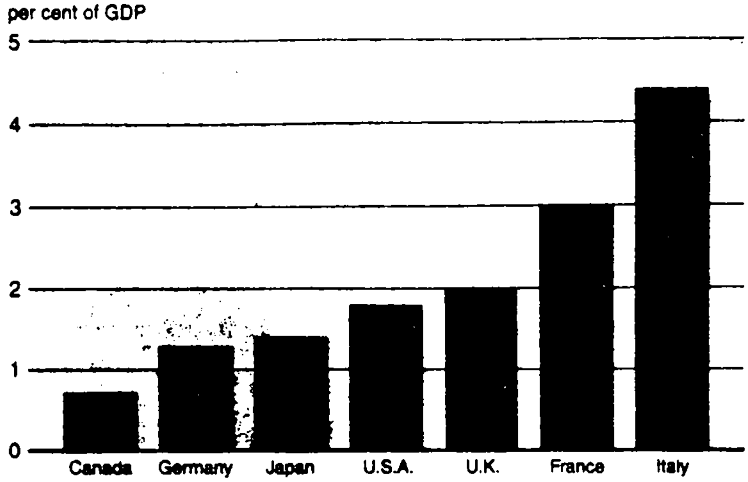
	1993-94	1994-95	1995-96	1996-97	1997-98
	(billions of dollars)				
Budgetary revenues	116.0	123.3	130.6	135.0	141.0
Program spending	-120.0	-118.7	-113.8	-109.0	-106.0
Operating balance	-4.0	4.6	16.8	26.0	35.0
Public debt charges	-38.0	-42.0	-47.0	-47.8	-49.0
Underlying deficit	-42.0	-37.5	-30.2	-21.8	-14.0
Contingency reserve			-2.5	-2.5	-3.0
Deficit	-42.0	-37.5	-32.7	-24.3	-17.0
Non-budgetary transactions	12.2	11.6	12.7	10.6	11.0
Financial requirements	-29.8	-25.8	-20.0	-13.7	-6.0
Net public debt	508.2	545.7	578.4	602.7	619.7
GDP (calendar year)	712.9	750.1	780.0	806.0	841.0
Per cent of GDP					
Revenues	16.3	16.4	16.7	16.7	16.8
Program spending	-16.8	-15.8	-14.6	-13.5	-12.6
Deficit	-5.9	-5.0	-4.2	-3.0	-2.0
Financial requirements	-4.2	-3.4	-2.6	-1.7	-0.7
Net public debt	71.3	72.8	74.2	74.8	73.7

No tax rate increases: There are no tax rate increases in this budget, not personal, not corporate, not excise. There have been no personal income tax rate increases in any of the last three budgets.

Program spending: This budget will help ensure deficit reduction beyond 1997-98 with $1.9 billion in additional spending cuts for 1998-99. There will be a substantial and sustained reduction in program spending – all budgetary spending except interest on the public debt – from $120 billion in 1993-94 to $105.5 billion in 1998-99, a decline of 12 per cent.

Chart 1

Projected 1997 central government financial requirements



Source: National budget plans.

Financial requirements – the new funds that government must borrow from financial markets each year – will be cut to $6 billion (0.7 per cent of GDP) in 1997-98, the lowest among all G-7 central governments.

Combined savings resulting from the 1994, 1995 and 1996 budgets will mean that the net debt in 1998-99 will be $91 billion lower than otherwise would have been the case. There will be almost $7 of expenditure cuts for every dollar of tax increases in the combined actions of the three budgets.

The debt-to-GDP ratio (the size of the debt in relation to Canada's economy) will finally begin to decline in 1997-98 – the economy will grow faster than the debt.

Economic assumptions: The government's fiscal projections continue to be based on economic assumptions that are deliberately more cautious than those of most private sector forecasters. In addition, substantial contingency reserves will back up the assumptions. If not needed to meet unforeseen economic changes, the reserves will go to reducing the deficit further.

Economic results: Restoring financial health paves the way for a more dynamic job-creating economy. A lower deficit means lower interest rates, growing confidence and new investment leading to more jobs and growth.

- *Inflation and interest rates:* Inflation is low and will remain low. Short-term interest rates have declined by about 3 percentage points since March 1995.
- *Cost competitiveness:* Canada's cost competitiveness is the best it has been in 45 years.
- *Trade surplus:* Our merchandise trade surplus has reached record levels and the current account deficit as a share of GDP is at its lowest level in 10 years.
- *Foreign borrowing:* Canadian dependence on new foreign loans has fallen from $29 billion in 1993 to $13 billion in 1995. That dependence will continue to decline.

Job creation is the most important statistic of all. Since the beginning of 1995, 263,000 private sector jobs have been created. These gains have been partially offset by declines in public sector employment. Further reductions in the unemployment rate will require a strengthening of private sector job creation.

The challenge is to build on our gains. Toward that goal, the budget announces a wide range of additional actions to help secure the future for Canadians.

Getting Government Right

The budget takes further actions to create a focused, more affordable government that effectively advances the key priorities of a productive, job-creating economy in a modern Canadian federation.

Program Review: The program review began in 1995 and is extended in this budget with $368 million in spending cuts for 1997-98 and more than $1.9 billion in 1998-99. The savings will help to meet the 2-per-cent deficit target in 1997-98, to guarantee continued deficit reduction beyond the fiscal planning period and to fund high-priority initiatives.

- Federal departmental spending will be 22 per cent lower in 1998-99 than 1994-95.

Table 2
Direct budget savings

	1994-95	1995-96	1996-97	1997-98	1998-99	Cumulative effect on net debt
			(billions of dollars)			
1994 budget	1.5	8.0	10.9	11.9	12.6	44.9
1995 budget		5.0	10.6	13.3	13.8	42.7
Total	1.5	13.0	21.5	25.2	26.4	87.6
1995 Employment Insurance reform[1]				0.7	0.8	1.5
1996 budget			0.0	0.2	1.7	1.9
Total	1.5	13.0	21.5	26.1	28.9	91.0
of which:						
Expenditures	0.7	10.6	18.9	23.3	25.6	79.0
Revenues	0.8	2.4	2.6	2.8	3.4	12.0

[1] Savings for 1996-97 were included in 1995 budget savings.

Note: Table shows net savings from deficits that would have otherwise occurred in the absence of direct measures in the budgets. Numbers may not add due to rounding.

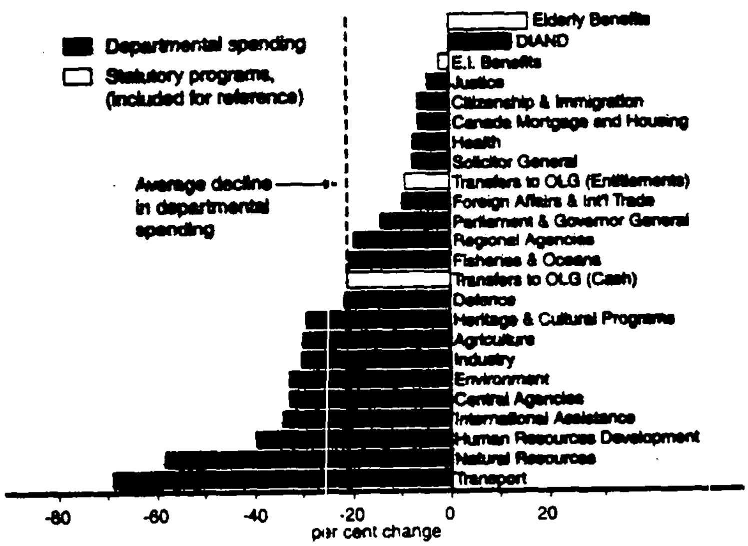
Departmental spending: Most departments will have their budgets cut by at least a further 3.5 per cent in 1998-99; some are cut much more.

- Spending on defence and international assistance will be further reduced. The growth of spending on Inuit and Indian programming will be restrained.
- The dairy subsidy will be phased out over five years and the postal subsidy program reduced. By 1998-99, grants and contributions to business, including reallocation to new initiatives to encourage technology and innovation, will be down 60 per cent from 1994-95, from $3.7 billion to $1.5 billion.
- Further savings in VIA Rail's operating subsidy will be achieved in 1998-99 through measures to improve productivity, and funding for Atomic Energy of Canada Limited will be reduced.

Chart 2

Departmental spending

1998-99 relative to 1994-95



- *Canada Mortgage and Housing Corporation* will phase out its remaining role in social housing except for housing on Indian reserves. The government is now prepared to offer provincial and territorial governments the opportunity to take over the management of existing social housing resources provided that federal subsidies on existing housing continue to be used for housing assistance for low-income households.

Privatization, commercialization: Building on the progress made in privatizing Canadian National Railways and selling a substantial part of its shares in Petro-Canada, the government will continue to pursue opportunities for privatization of Crown corporations and commercialization of other government activities. Initiatives will include the sale of Theratronics International Limited and the government's shares in National Sea Products Limited.

Alternative service delivery: Legislation will be introduced to create fewer, more effective service agencies with the emphasis on better service, greater efficiency and partnership efforts.

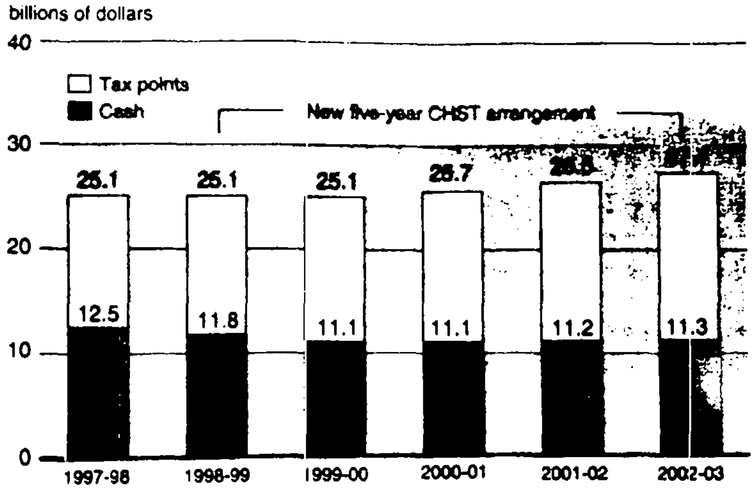
- A *Single Food Inspection Agency* will regroup food inspection and quarantine-related services currently provided by three government departments into one single agency. The new agency will facilitate the development of a new partnership with the provinces in a more effective, efficient joint food inspection system.
- *Canada Revenue Commission:* A national revenue agency to be called the Canada Revenue Commission will be created. It will facilitate less costly administration and the development of a closer partnership with the provinces in revenue collection.
- A *Parks Canada Agency* will be set up as a separate service agency to manage and preserve a system of national parks, national historic sites and canals and related protected areas for the use and enjoyment of Canadians.

Securing social programs for the future

The government is acting to ensure that social programs are affordable and will be there for Canadians in the future.

Chart 3

CHST: Security and stability



Restoring growth to transfers to provinces

Canada Health and Social Transfer (CHST): Stability and subsequent growth will be restored to transfers to the provinces with a stable, predictable and sustainable system of long-term CHST funding for health care, post-secondary education and social assistance.

Secure and growing funding: The federal government will legislate a new five-year CHST funding arrangement beginning in 1998-99. For the first two years, federal support (tax transfers plus cash) will be maintained at $25.1 billion. Over the subsequent three years, transfers will grow at an increasing pace related to the economy.

- Entitlements over the five-year period will grow from $25.1 billion to approximately $27.4 billion.
- To provide additional protection to provinces, a new cash floor will guarantee cash transfers of at least $11 billion in all years.
- Secure and growing funding will ensure the federal government's capacity to uphold the principles of the Canada Health Act and the principle that no residency requirements can be imposed on social assistance recipients who move from one province to another.

- The budget proposes to phase in over the five-year period a new way of allocating CHST transfers among provinces. It would reduce by half the current per capita disparities in funding among provinces. The government will review with the provinces refinements to allocation that might be appropriate after the five-year period.

Health Services Research Fund: Federal funds will also be provided to help establish a Health Services Research Fund in partnership with provincial governments, health institutions and the private sector. The purpose of the research will be to determine what works in Canada's health care system and what does not.

Restoring confidence in the public pension system

The budget takes action to ensure that Canada's Old Age Security system will be there in the future for Canadians when they retire.

For future seniors, benefits will be better targeted by providing more assistance to low-income Canadians and reducing or eliminating assistance to those with higher incomes. For today's seniors and near seniors – and their spouses, no matter what age – pensions will be protected. They will be guaranteed no less than current pension payments.

A New Seniors Benefit will replace the existing Old Age Security and Guaranteed Income Supplement (OAS/GIS) benefits beginning in 2001.

- *Tax free:* The new benefit will be completely tax free and will incorporate the age and pension income tax credits.
- *Paid monthly:* Benefits will be delivered in a single monthly payment. Payments to spouses will be made in separate and equal cheques to each spouse.
- *More for low-income seniors:* GIS recipients will receive an additional $120 per year.
- *Spouse's Allowance:* The Spouse's Allowance program will remain in place and payments will be increased by $120 per year.
- *Combined income:* For couples, the amount of the payment will be determined on the basis of the combined income of the spouses, as is, and always has been, the case with the GIS.

- *Fully indexed:* Both the benefit levels and the thresholds at which benefits begin to be reduced will be fully indexed to inflation. This will be an important improvement for seniors who worry about eroding benefits.
- *One application:* Seniors will only have to apply once for the benefit when they turn 65. The level of benefits will be automatically recalculated each year, based on the previous year's tax return.

Most will be as well or better off: The vast majority of all seniors will be as well or better off, including:

- three-quarters of all elderly individuals and couples;
- nine out of 10 single elderly women;
- generally, all singles and couples with incomes up to approximately $40,000.

Benefit phase-out for higher incomes: For future seniors under the new system, those with higher incomes will continue to receive benefits, but at a lower level the more income they have from other sources, and those with the highest incomes will no longer receive government assistance.

Protecting today's seniors: The government's commitment to protect OAS-GIS payments for today's seniors will be met and surpassed.

Those 60 and older as of December 31, 1995 will have a choice between moving to the new system or maintaining their current monthly OAS/GIS payments, as currently structured – whichever is more advantageous to them. However, the vast majority will be better off under the new system.

More affordable and sustainable: The new Seniors Benefit will help make the public pension system more affordable and sustainable. Targeting help to those who need it most will slow the rate of growth of public pensions, making them more affordable for future generations. This will ensure that the pension system is sustainable in the future.

The new Seniors Benefit is more fully described in a separate budget document entitled Securing the Future: The Seniors Benefit.

Eligibility of immigrants for OAS/GIS pensions will be better linked to their length of residence in Canada, as it is for other Canadians. The changes will apply immediately to newcomers arriving in Canada after budget day. For all other newcomers who have already landed in Canada as of budget day, the existing rules will apply until December 31, 2000, thereby giving a period of notice. Those already receiving benefits will not be affected.

The Canada Pension Plan continues as a separate contributory pension plan. The government is working with the provinces and territories to make changes to the CPP so it can be sustained for future generations. The governments of Canada, the provinces and the territories have released an information paper on the CPP. It will form the basis of public consultations on the CPP to be held across Canada, beginning this month.

Increased assistance to those in need

Child Support: The government is announcing new child support measures to ensure that adequate levels of support are paid regularly and on time to the custodial parent. The package includes changes to the tax treatment of child support, new guidelines and enhanced enforcement. The measures are based on the philosophy that child support is not discretionary – it is the first obligation of parents, and child support payments are there to provide support for children, not income for parents.

- *New tax treatment:* The budget proposes that child support not be included in the income of the recipient for tax purposes nor be deductible to the payer if it is paid pursuant to an agreement or court order made on or after May 1, 1997. Parents with existing agreements will be able to file a joint election with Revenue Canada to apply the new tax treatment.

Further details are contained in the document, The New Child Support Package.

The Working Income Supplement under the Child Tax benefit will be doubled in two stages from $500 to $750 in July 1997 and to $1,000 in July 1998. This will provide an additional $250 million annually to an estimated 700,000 low-income working families, one-third of which are single-parent families.

Child care expense deduction age limit: The age limit for the child care expense deduction will be raised to 16 from 14 to help parents who must work at night.

Credit for infirm dependants: The value of the tax credit for infirm dependants will be increased from $270 to $400, and the dependant's income threshold for the phase-out of benefits will rise from $2,690 to $4,103.

Charitable donations: Tax assistance for charitable donations will be increased by raising the annual limit on donations from 20 per cent of net income to 50 per cent; and to 100 per cent in the event of death. Gifts of appreciated capital property will benefit from higher limits of up to 100 per cent of net income. Ways of further encouraging charitable giving and of ensuring that support for charities is effectively translated into beneficial activities will be examined.

Investing in the Future

The budget announces actions, funded by reallocation in government spending, to increase Canada's investment in areas critical to the country's economic future and to future jobs and growth – youth, technology and international trade.

Youth: Education and skills development for young Canadians will be further encouraged with an additional $165 million over three years funded from reallocation within the tax system.

- *Education tax credit:* To recognize the non-tuition costs of schooling, the amount on which the credit is based will be increased from $80 to $100 a month.
- *Transfer of tuition and education credits:* To support parents or spouses who help underwrite the education of students, the limit on transfer of tuition and education credits will also be increased from $680 to $850. This represents an increase from $4,000 to $5,000 in the tuition fee and education amounts which may be transferred.
- *Registered Education Savings Plans (RESPs):* To assist those who save for their children's education, the annual limit on contributions to RESPs will be increased from $1,500 to $2,000. The lifetime contribution limit per beneficiary will be increased from $31,500 to $42,000.

- *Child care expense deduction:* For single parents who are full-time students, the child care expense deduction will be allowed against any income. This measure will also apply to two-parent families when both parents are full-time students. Parents who are completing high school will be allowed this deduction for the first time.

Student loans: More flexible repayment terms will also be made available for loans under the Canada Student Loans Act.

New employment opportunities will be created for youth by reallocating $315 million of budget savings over three years.

- *Student summer employment:* Funds for 1996-97 student summer employment placements will be doubled to $120 million.
- *Youth employment:* Support will also be increased to help young people who have left school to find employment opportunities. The government seeks a new partnership between the public and private sectors to create entry-level jobs for the young.

Technology and innovation: The budget increases investment in technology and innovation through a number of actions over the next three years, funded by reallocations of $270 million from budget savings.

- *Technology Partnerships Canada* will be established to encourage partnership and risk sharing with the private sector and to leverage investment in the development and commercialization of high technology products and processes. The fund will grow from about $150 million in 1996-97 to about $250 million by 1998-99.
- *Business Development Bank:* New equity capital of $50 million will be injected into the Business Development Bank to increase its lending efforts in strategic growth sectors, such as new technology. This will permit up to an additional $350 million in loans to knowledge-based, export and growth businesses.
- *The SchoolNet program* will be expanded. It will ensure that every school and library in the country is connected to the information highway by 1998. By the same year, 1,000 rural communities will also be connected through the Community Access component of SchoolNet. With the help of 2,000 computer students, 50,000 small businesses will be connected to the Internet. Students will both install those systems and advise their owners on how best to use them.

- *Information highway:* To help increase the contribution of the information highway to jobs and growth, the Ministers of Industry and Canadian Heritage will be introducing policies and reforms to facilitate greater reliance on the marketplace while respecting the commitment to affordable access and to a Canadian presence on the information highway.

International trade: New steps will be taken to realize Canada's trade potential.

- *The Export Development Corporation* will receive $50 million in new equity capital for further innovative types of export financing.
- *Export financing:* A major increase in financing available to exporters will be achieved by reallocating resources from concessional loans to foreign borrowers to finance higher volumes of non-concessional financing under an improved system of risk management.

Business tax review: A comprehensive review of business taxation will be carried out by a technical committee with three key goals in mind: promoting jobs and growth; simplifying the system and enhancing fairness.

Revenues

The budget proposes further actions to ensure that the tax system raises revenues fairly and effectively, and is supportive of jobs and growth. Revenues raised will be reallocated to priority economic and social initiatives such as improved tax assistance for students, charitable donations and care of the infirm.

Table 3
Summary of tax measures

	1996-97	1997-98	1998-99
		(millions of dollars)	
Revenue-enhancing measures			
Personal income tax			
Changes to RRSPs			
Restrict tax assistance/ non-deductibility of fees		45	180
Tax world-wide income of non-res. pensioners	10	10	10
LSVC: Restrict tax assistance	15	60	70
Measures to combat underground economy	25	60	100
Total	50	175	360
Business income tax			
Resource sector			
Repeal JEC rules	–	–	–
Tighten flow-through shares	15	20	20
Temporary tax on banks	25	40	
Overseas employment credit	10	10	10
Total	50	70	30
Total	100	245	390
Reallocation to high-priority areas			
Personal income tax			
Charitable donations	-5	-20	-20
Learning package	-5	-80	-80
Infirm credit	-5	-35	-40
Child support/ Working Income Supplement	-10	-105	-180
Total	-25	-240	-320
Business income tax			
CCA for new mines, oil sands	-5	-5	-5
Extension of 60-day flow-through share rule	–	–	–
Broaden investor base for renewable energy[1]		-5	-10
Expand flow-through shares to renewable sector	–	–	–
Total	-30	-250	-335
Net impact of revenue actions	70	-5	55

[1] The budget proposes to relax the "specified energy property" rules.

– Less than $5 million.

Fairer, more affordable tax assistance for retirement savings

A number of changes are proposed to better target tax assistance for retirement savings to modest and middle income Canadians and to limit the cost to taxpayers.

- *Lifetime carry forward:* The seven-year limit on carrying forward unused RRSP contribution room will be eliminated to provide greater flexibility in making up for years when full contributions are not made. This action recognizes that many younger Canadians have difficulty finding the money to make full RRSP contributions early in their working lives and through their child-raising years.
- ***RRSP contribution limit:*** Tax assistance will be limited to helping build pensions based on earnings up to twice the average wage. To achieve this, annual RRSP and money purchase pension plan contribution limits will be frozen at $13,500 through 2003 before rising to $15,500 by 2005. The pension limit for defined benefit pension plans will also be frozen through to 2004.
- ***RRSP age limit:*** The age limit for RRSP contributions will be reduced from 71 to 69. This means individuals must begin drawing on their private pension savings by the end of the year in which they turn 69. This will bring the limit more into line with the age at which Canadians are retiring and will limit unnecessary tax deferral.
- ***Self-directed RRSP administration fees:*** Administration fees for self-directed RRSPs will no longer be tax-deductible if paid for outside the plan – the same rule as for other RRSP expenses.
- ***Non-resident pension recipients:*** The pensions of non-resident pension recipients will be taxed on the basis of world-wide income to eliminate a tax benefit that is unavailable to Canadian residents. The government is working with foreign tax authorities to ensure fair taxation of all pension recipients.

Several other measures are proposed to tighten and clarify the tax system and raise revenues for reallocation to priority initiatives.

- ***Underground economy:*** Revenue Canada will step up its actions to combat the underground economy by devoting more resources to its audit program for unincorporated businesses and self-employed individuals in order to increase the audit coverage rate for these groups. It is expected additional revenues will be about three times the cost involved.

- *Labour Sponsored Venture Capital Corporations (LSVCCs):* Special incentives to encourage investment in LSVCCs will be reduced. The tax credit for investment in LSVCCs will be reduced from 20 per cent to a maximum of 15 per cent for shares acquired after March 5, 1996. The maximum share purchase eligible for the federal tax credit will be reduced from $5,000 to $3,500, effective immediately. These measures reflect the fact that LSVCCs now have a large pool of capital to be invested in small businesses as a result of the incentives. The minimum holding period normally applied to federally registered LSVCC shares will be increased from five to eight years.
- *Resource taxation:* The rules related to the resource allowance will be tightened and clarified to ensure a more consistent and stable tax structure. Changes will be made to the accelerated cost allowance rules for new mines, including oil sands mines. Eligibility will be broadened so that other types of oil sands mines are treated more consistently.
- *Renewable and non-renewable energy investments:* To encourage renewable energy investments, the tax rules will be changed to create an essentially level playing field. Proposed changes will improve tax rules for the financing of some renewable energy and conservation projects, including the extension of flow-through share provisions.

Large deposit-taking institutions: The temporary 12-per-cent surcharge on banks and other large deposit-taking institutions will be extended for another year.

Sales tax

The government is continuing its effort to replace the federal sales tax. The objective is a system that is fairer for Canadians, simpler and less costly for businesses to comply with, and more efficient to administer. Toward that goal, the government is working with a number of provinces. If successful in getting provincial agreement, the government will take the necessary steps to implement harmonization.

Conclusion

"This budget is about consolidating the gains we have made. It is about addressing problems before they arise. It is about managing ahead, continuing to put in place new building blocks for security and prosperity ...

Our challenge today is to make Canada a place of great expectations, a country once again where our children believe they have the opportunity to do better than their parents, a place where they can dream large dreams once more.

Let us follow in the footsteps of those who came before, who saw challenge as a rallying cry to move forward, never as an excuse to give up.

And let it be said by those who come after us, that we set the goals, that we met them together, that we propelled Canada forward into a new millennium – still and always among the front ranks of nations."

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The slow revolution

The government is determined to push ahead with an ambitious programme of Budget reform. But change will not take place overnight, write **Madeleine Wackernagel** and **Lynda Loxton**

THE country's financing process is undergoing nothing short of a revolution, Director General of Finance Maria Ramos said this week.

Briefing the parliamentary finance committee, Ramos agreed that the programme of Budget reform was ambitious but it "was a very necessary transformation that needs to take place. It is not something that will happen in one day.

"We should not lose sight of the point that what we are talking about is almost a revolution in the government in the way we budget and manage financial resources."

But so far, there has been little evidence of radical change. A White Paper was scheduled for public comment in October, but has now been postponed until later this year. As one observer close to the process said: "Ramos did not say anything new. But at least she reiterated the government's commitment to doing something."

Director General of State Expenditure Hannes Smit was quick to defend the government's record: "The process took eight years to implement fully in Australia and New Zealand. People are expecting too much in too short a time. A lot of things have happened in the last three years.

"I am not just talking about restructuring. I am talking about priority shifts, changes in management styles, the government getting their ducks in a row ... somebody should just go and take stock instead of just wanting to move forward all the time and getting frustrated on timing."

Ken Andrew of the Democratic Party said: "I don't believe they are just mouthing platitudes; there is a serious intention to improve the budgetary process. Indeed, the work done to date has already helped the government to hold down expenditure, as we saw in last week's Budget.

"But there is still room for more progress and it is difficult to say if the changes envisaged will work in practice."

Ramos admitted that brief presentations to the committee did not allow enough time to go into the detail of work that had already been undertaken.

When work first started on the medium-term expenditure framework (MTEF), the data for the initial costing exercises were very scrappy and out of date and a great deal of time had to be spent updating information, she said.

"We are bringing more information into the exercise so that we are in a better position to provide an instrument that is useful. It is also very easy to take short cuts in this process because the devil is always in the detail.

"We now have the go-ahead from Cabinet to proceed with the MTEF and start implementing it, which we will do this fiscal year, particularly at the level of national government."

"Cabinet had also approved the establishment of the Budget Office and staff are now being recruited."

The new approach called for a "significant change in the culture of budgeting and financial management within government" at all levels. This would not be possible without extensive training of staff, Ramos said.

The aim is to shift from the present system of year-on-year Budgets to three-year rolling Budgets to create a better alignment between policy and resource allocation.

"This will allow us to quantify and to say that while government has all these plans ... for them to materialise, we need resources. The MTEF will allow for a closer alignment between policy and resources."

Questions about capacity and implementation remain, however, particularly in terms of the provinces.

Says Murphy Morobe of the Financial and Fiscal Commission: "What we need is a frank and brutal assessment of capabilities — now. Otherwise, at crunch-time, it will be too late. There is little sense that training is central to the whole process.

"It cannot be seen as an incidental, otherwise, just when we think it's all under control, it won't happen."

Committee members also voiced their concerns about whether many departments had the ability and skills to plan new projects, to which Smit replied that training was an important part of the new direction.

A pilot project on three-year Budgets would be launched in the Department of Land Affairs, which would provide practical experience for other departments.

"It is going to take capacity building, new thinking, not only from the officials but definitely more from the politicians because the politicians will now also be measured for delivery," he said.

Ramos said that no matter how good financial controls were, the government would not be able to meet its objectives if it did not have a clear idea of the choices it had to make to achieve certain results.

Thus, the MTEF would allow for greater stability and certainty in planning and over time would reduce the need for rollovers and front-loading.

"It will allow us to identify policy and programme trade-offs such as, for example, how to balance spending on primary healthcare and hospital rehabilitation.

"Importantly, it allows for reprioritisation and rationalisation. It allows you to make choices," she said.

On the revenue side, the Department of Finance was also working on a medium-term revenue framework, which would identify revenue sources and how they tied in with the overall direction of taxation policy, borrowing strategies and spending limits.

Ramos said this approach was important because if the government adopted a popular, expansionary route and "simply set out to fulfil the expenditure wish-lists without consideration for the kinds of resources we have available, we would be faced with an environment where expenditures far exceed the resources we have available as a government ... Thus, we need to prioritise."

Maria Ramos: Budget reform is 'not something that will take place in one day' PHOTO CREDIT: T.M.

Provinces must 'bake their own cakes'

The Finance and Fiscal Commission believes it is time the provinces raise their own revenue. Murphy Morobe spoke to **Aspasia Karras** about the commission's proposals

Murphy Morobe: 'First prize is a comprehensive government response to the proposals' PHOTOGRAPH: RUTH MOTAU

PROVINCES must start playing a much stronger role in developing their own fiscus if they are to survive as executive entities. That is the message the Financial and Fiscal Commission (FFC) is trying to hammer home with increasing urgency in its reports to Parliament's standing committee on finance.

Last week, the commission added more flesh to its proposals that provinces raise their own revenue. In the context of the administrative crises in two of the nine provinces, the Free State and the Eastern Cape, the commission may be fighting a much more complex case than just one for revenue expansion.

Murphy Morobe, chairman of the commission, argues: "The issues being raised are critical. We have to ask ourselves what form the state will and can take. As the political actors proceed with giving meaning to the provisions of the new Constitution, so will the form and content of the state unravel. We as the commission have to be aware of these developments in order to remain relevant."

The commission, an innovation of the interim Constitution, was appointed by the president. It advises and recommends approaches and solutions to the fiscal and financial requirements of the national, provincial and local governments through the relevant legislative authorities.

The commission, says Morobe, has deliberately taken a low profile during the past two years in order closely to monitor and evaluate the terrain and the role it should play. In this time it has developed its "currency" — its consistent quality of work and legitimacy.

There are precedents in other countries such as Australia and India, but their role, says Morobe, can vary from being "indispensable to the system to being about as useful as a toy telephone".

The commission's principal task is to work out a way to split the pool of money between the provinces in a given year. First, the money is divided vertically, between ministeries and national functions; then allocated to the provinces in a horizontal split. The Constitution does not explicitly state that the FFC cannot play a role in the vertical split, but it has tended to tread carefully, as the issue is a political minefield, and is now driven by a new institution — the Budget Council.

"Should we want to get more involved in the vertical split, we would have to play the role in such a way that we did not usurp the powers of the executive. After all, they have the first call in terms of determining the national interest. We cannot, however, be impassive to decisions made at that level: co-operative government impacts at all levels," says Morobe.

Trying to balance the needs of provinces against the constitutional requirements for equity in the context of a decentralised unitary state is indeed difficult, he says.

The new proposals are an attempt to address the problems of nine dependent provinces — significant imbalances in revenue-raising capacities and expenditure responsibilities, as well as growing deficits.

It is, however, the commission's role to point out that its proposals encompass the fiscal relationship envisaged by the Constitution. Only a systematic approach to these issues will prevent complete chaos.

In fact, it is talking about that most critical of concepts of co-operative governance, which Edward Kitchken from Ashoka, a non-governmental organisation dedicated to supporting innovation in social development, explains as: "The process through which power and authority are exercised between and within the state and civil society around the allocation of resources. How antagonistic forces with material interests in the state and civil society forge alliances and enter into conflicts so as to access more resources to reinforce their power."

The commission has concluded that a decentralised system can improve the allocation of resources, provided that sub-national governments are accountable to their electorates. Thus each province is given specific allocations determined at national level for education and health care, and is allowed to determine how it will spend the rest of its portion. The FFC has allowed for a five-year phasing-in process.

But Morobe elaborates: "This is not just about numbers. It is not only an expenditure issue, but more importantly a revenue issue. If we continue to make significant transfers from the centre, in some years it will become difficult to justify the existence of provinces with an executive."

An essential element of accountability is the responsibility of raising your own revenue. The issue is then not entirely about which way the cake will be split, but more importantly how provinces can be empowered to bake their own cakes. At present, the average province raises 4% of its expenditure.

The FFC, in its most recent presentation, has added some critical elements to the formula. The most controversial one is the proposal to allow provinces to raise their own revenues by imposing surcharges on personal income tax.

This does not mean that individual income tax rise, but rather that central government reduces its individual income tax rates by a few percentage points, in a phased process.

In other words, within the 25% capping on personal income tax, the provinces are given a few percentage points' leeway to levy as they choose. This would then count as own revenue. Morobe argues that in this way richer provinces, which might otherwise feel done in by the redistributive elements of the formula, can compensate for the horizontal split.

While the provinces have not been formally accorded taxing powers, the commission argues for a proxy for own revenue (a transitionally assigned surcharge) to equal the tax room given to each province in the first year.

The second element is the tax-capacity equalisation grant which seeks to compensate provinces for their different tax capacities.

"The grant will partially compensate for the different tax capacities and disparities in the various provinces," says Morobe.

Finally, the FFC has begun a major programme to develop similar recommendations for local government.

Morobe concludes: "First prize is a comprehensive government response to the proposals. But there has to be a strategy, which in the present period must also take into account the establishment of the National Council of Provinces and its role in the system.

"We are many interrelated wholes, everybody has to be alive to chapter three of the Constitution, on co-operative government and the cross-functional issues."

Debating the shape of the budget

PARLIAMENT finally passed the national budget after months of haggling and debate. **PATRICK BULGER** takes you through the process.

THE national budget is the centrepiece of Parliament's annual activity and concerns the citizenry directly because it tells you, the citizen and taxpayer, just how your hard-earned tax rand is being used. Or misused.

The interminable debates in the chambers, which start in late summer and endure throughout the winter months and which drive some MPs to distraction, are all intended to concentrate the political mind on the R173,7-billion that then finance minister Chris Liebenberg told Parliament the government would spend to implement its objectives.

Theoretically, Parliament and its plethora of committees are meant to take a close and critical look at the budget, in particular the separate votes to the different government departments.

And Parliament can then reject the budget, but this is unlikely because it would amount to a vote of no confidence in the majority party and its executive and would trigger an election.

So, unlike the situation in the United States where Congress can reject the president's budget and the president can then refuse to sign Congress's amended budget -- leading to a "shut-down" in government -- the approval of South Africa's Parliament for the budget is taken as a given.

Of course, the minority parties are free to oppose the budget or any of the separate votes to government departments. In doing so they register the strongest possible protest against the majority party's spending inclinations.

True to political form, Parliament last week finally passed the budget. In doing so it gave the nod to the executive to borrow money which it is unable to gather in taxes and other impositions on individuals and businesses. This year the government is raising loans of R28,8-billion, all of which have to be paid back, not by current generations but by our children and our grandchildren.

In other words, the government is still spending way beyond its means and, though there is now a solid commitment to spending less and gathering in more revenue, there has been a noticeable absence of calls for a "balanced budget" before borrowing which is a major political issue in the US. So where does your money go? Not surprisingly, for every R1 that the government spends, the second biggest item of expenditure goes towards servicing the loans government has had to take to bring its revenue in line with its expenditure. This year, 18,7c of every R1 goes towards debt redemption.

This is topped only by education which receives R21,2c of every R1. The remainder is spent as follows: "economic services" gets 11,4c, health gets 9,9c, welfare 9,6c, defence 7,5c, police 6,3c and housing 1,9c, and "other" gets 13,6c.

And how is the money raised? For every R1 that the government gets in, a whopping 33,4c comes from you, the individual taxpayer.

Nor does the burden on individuals end there: they still contribute part of the 21,3c that comes from value added tax, part of the 6c that comes from the fuel levy and, indirectly, part of the 12,3c from companies and 5,1c from customs and excise. In addition the government raises 16,6c by taking out loans and 5,4c comes from "other" like the sale of strategic fuel stocks and the like.

This is the scenario Parliament is presented with in March and it spends nearly six months approving the breakdown.

In an indication of how the crime wave has concentrated political minds, dissenting voices were raised against the allocations made to the crime-fighting arms of government. Both the Democratic Party and the Freedom Front voted against the correctional services allocation which they said was insufficient, the NP voted against the finance vote in protest against the tax on the life assurance industry, the NP, the FF and the DP opposed the health allocation because of the Sarafina 2 debâcle in the year, the DP and FF both opposed the justice vote, the FF opposed the land affairs vote, the DP and FF voted against the public enterprises allocation, the FF came out against the public service and administration vote, the FF, the DP and the NP opposed the safety and security allocation, and the FF opposed the South African Revenue Services vote.

Perhaps the most sobering assessment of future budgets came from the ANC's Rob Davies who warned that the Government's *new macro-economic strategy required further* cuts in the deficit; that is, the difference between revenue and expenditure.

Davies warned that the reduction would require "stiff expenditure cuts" and he went on: "There are two possibilities that can be created by the deficit reduction target.

"First of all, it can become a spur to sharpen and make more effective reprioritisation. Secondly, if that does not happen, it will mean cuts across the board, including cuts in the areas that are priorities in terms of social delivery and redistribution."

He pointed out that the government remained as susceptible to interest rate increases as ordinary consumers. In fact, a mere one percent rise in interest rates pushes up the government's debt servicing obligations by R1-billion.

The FF's Willie Botha questioned the government's commitment to fighting crime and warned that investors would stay away from South Africa. The DP's Ken Andrew warned that economic prosperity was threatened by crime and the rand's value on world currency markets and urged the government to move quickly to remove exchange controls.

With the budget now behind it, Parliament has been freed to concentrate on its other main activity: legislation.

❑ *Patrick Bulger is the political correspondent of The Star*

The Cape Times

May 1996

Business Day, 13 August 1996

Provinces given budget powers

Tim Cohen

CAPE TOWN — Government would allow provinces more power in determining their own budgets, taking its biggest step to date towards a new process of deciding expenditure, state expenditure director-general Hannes Smit said yesterday.

Budget committee meetings between government departments and the finance department on determining next year's Budget began last week and would continue this week, he said.

Discussions focused on anticipated expenditure by national departments. In previous years central government developed an estimate of expenditure for every department. This included a detailed breakdown of provincial and national portions of the Budget.

The first step of the process was implemented in this year's Budget when provincial governments' allocations were listed as a global amount in the finance department's budget. Central and provincial governments would determine an overall split between national government and provincial governments, and then each provincial

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Provinces

Continued from Page 1

government would have to decide how its portion would be divided among its departments. This would, for the first time, be done without an expenditure estimate from central government, with the provinces moving "a step closer to full autonomy", Smit said. The split between national and provincial government was determined partly by using the Financial and Fiscal Commission's draft formula and partly by extrapolating from existing expenditure, he said.

As central government intended to cut the deficit from 5,1% to 4% of GDP, there would be a real decline in the budgets of national and provincial governments. However, the average decrease in provincial government budgets would be less than the drop in the central government budget.

The budgeted expenditure of certain provinces would be greater than those of other provinces.

No changes were likely this year in the timetable for the presentation of the Budget, despite discussion last year about presenting the Budget earlier in order to allow Parliament time to recommend adjustments.

Smit expected a three-year expenditure plan to be presented to Parliament for discussion early next year.

Cape Times
March 1996

Reform budget to include participation

WARREN KRAFCHIK

THE government is sending out important signals that it is serious about reforming the budget process. The Department of State Expenditure is to hold a conference on budget reform in Pretoria on April 1-2 and, in the budget speech, it was announced that the budget will in future be tabled earlier to allow the legislature more time to consider it.

It is commonly acknowledged that the budget process is in need of a thorough overhaul. Budget reform is a broad topic that includes civil service reform, monitoring and reporting procedures, medium term planning and the like. However, there are two aspects of the problem need to be raised because they affect the ability of citizens and their representatives to be involved in the budget process.

The role of parliament in the budget process is as "the keeper of the purse" and so parliamentary review is supposed to facilitate the legislature's monitoring of departmental budgeting. Although the Constitution does not exclude the possibility of the legislature introducing amendments to the budget, this procedure was written out of the rules of parliament when the tri-cameral constitution was adopted. This implies that at present parliament continues to be little more than a rubber stamp for the budget. The budget is still essentially drafted by departments (with State Expenditure retaining a central role) and ratified by the Executive.

A related issue is that there is also no formal space within the budget process for broader civil society to make an input. At the very least, the budget process is a perfect opportunity for citizens to learn to appreciate the critical economic trade-offs facing South Africa. But civil society has already shown that it can make a further contribution. Through a variety of structured and ad hoc arrangements with portfolio committees, civil society has played an important role, over the last two years, in helping parliament to build its capacity to engage with the budget.

If no formal opportunity is created for civil society in the budget process, it is likely that only the more organised and well-resourced organs of civil society will be heard and parliament will lose an important information channel.

In order to facilitate this it is essential that we demystify the budget process. The ordinary citizen is more capable of participating in a process he or she understands.

The Minister of Finance's budget speech to parliament on March 13 is the culmination of an 18-month drafting process. It now takes a further six months for parliament to pass the budget. There are four stages to this review process.

1 The first stage consists of the Finance Minister's budget speech which serves to introduce the budget. It does not constitute the first reading in parliament.

2 The second stage begins with the parliamentary Joint Standing Committee on Finance (JSCOF) hearings. This finishes today.

Parliament then debates the budget for three days during which time the first reading of the budget takes place. The parliamentary debates are scheduled to take place this year from March 26-28.

3 The third stage begins with each portfolio committee having the opportunity to consider their departmental budgetary vote. These discussions are scheduled for the April 15-19, but the schedule is normally rather flexible. At the conclusion of each portfolio committee hearing, the committee may decide to write a report to the national assembly.

Following the portfolio committee hearings, the national assembly divides into appropriation committees that will further discuss the schedule of expenditures for each vote. The house divides into two in order to facilitate simultaneous debate on two portfolios.

4 The fourth stage is the second reading. In practice, once the appropriation committees have concluded their debates on each of the votes, a second reading is scheduled for parliament. This will take place after August 15.

NEXT WEEK IN PARLIAMENT

WITH the constitutional deadline fast approaching, the focus of Parliament in the next month and a half will be on the Constitutional Assembly.

On Friday next week the Constitutional Assembly will meet in a plenary session and thereafter (until May 9), CA business will dominate the lives of MPs. Monday to Thursday is therefore the last full period of committee meetings for a while.

The Constitutional Committee will be meeting on Monday to discuss the fourth edition of the final draft of the Constitution. On Tuesday, the Constitutional sub-committee will meet to consider the issues of traditional authorities, self-determination and security services.

In Parliament, interesting committee meetings look like those involving Defence, Finance, Health, Welfare and Correctional Services.

The Portfolio Committee on Defence will meet on Wednesday to consider the banning of land mines and the use of part-time forces. Last week Minister Kadar Asmal reported to the Joint Standing Committee on Defence that there was an absolute bar on the export of mines from SA.

The issue of part-time forces is also very pertinent, with white men conscripted in the apartheid era still receiving call-ups for camp duty although the state cannot enforce any one's compliance with these camp call-ups. (Wednesday, March 27, 10am in Room V119).

The Joint Standing Committee on Finance is meeting on Tuesday to discuss the issue of special pensions for people such as ex-MK soldiers. The Special Pensions Bill has not been formally tabled, but a draft document has received widespread comment.

Deputy Minister Alec Erwin has been co-ordinating a consultation process around this draft document. (March 26, 2pm, in Room 249 National Assembly Wing).

Also in the area of Welfare, the portfolio committee will be briefed by Director-General Dr Laila Patel on Tuesday. In addition to talking about the departmental budget, she will talk about the newly released white paper for social work, and the restructuring of the department.

On Wednesday the portfolio committee on Correctional Services will be briefed by Lieutenant-General Khoza on the recent escape by four right-wingers from Diepkloof prison. (2pm, Good Hope Chamber).

Source: *Budget of the United States Government, Analytical Perspectives, FY96*, pp. 311-27

25. BUDGET SYSTEM AND CONCEPTS AND GLOSSARY

The budget system of the United States Government provides the means by which the Government decides how much money to spend and what to spend it on, and how to raise the money it has decided to spend. Once these decisions are made, the budget system ensures that they are carried out. The Government uses the budget system to determine the allocation of resources among its major functions—such as ensuring the national defense, promoting commerce, and providing health care—as well as to determine the objectives and scope of individual programs, projects, and activities. While the focus of the budget system is on dollars, other resources, such as federal employment, are controlled through the budget system. The decisions made in the budget process affect the nation as a whole, state and local governments, and individual Americans. Many budget decisions have worldwide significance.

This chapter provides an overview of the budget system and explains some of the more important budget concepts. A glossary of budget terms is provided at the end of the chapter. Summary dollar amounts illustrate major concepts. These figures and more detailed amounts are discussed in more depth in other chapters of the budget document.

The budget system is governed by various laws that have been enacted to carry out requirements of the Constitution. The principal laws pertaining to the budget system are referred to by title throughout the text, and complete citations are given later in the chapter.

THE BUDGET PROCESS

The budget process has three main phases, each of which is interrelated with the others:

(1) formulation of the President's budget;

(2) congressional action on the budget; and

(3) budget execution.

Formulation of the President's Budget

The Budget of the United States Government consists of several volumes that set forth the President's financial proposal with recommended priorities for the allocation of resources by the Federal Government. The primary focus of the budget is on the budget year—the next fiscal year for which Congress needs to make appropriations. However, the budget may propose changes to funding levels already provided for the current year, and it covers the four years following the budget year in order to reflect the effect of budget decisions over the longer term. The budget includes data on the most recently completed fiscal year so that the budget estimates can be compared to actual accounting data.

The process of formulating the budget begins not later than the spring of each year, at least nine months before the budget is transmitted and at least 18 months before the fiscal year begins. (See the Budget Calendar below.) The President establishes general budget and fiscal policy guidelines. Based on these guidelines, the Office of Management and Budget (OMB) works with the federal agencies to establish specific policy directions and planning levels for the agencies, both for the budget year and for the following four years, to guide the preparation of their budget requests.

During the formulation of the budget, there is a continual exchange of information, proposals, evaluations, and policy decisions among the President, the Director of OMB, other officials in the Executive Office of the President, the Secretaries of the departments, and other heads of Government agencies. Decisions concerning the upcoming budget are influenced by the results of previously enacted budgets, including the one for the fiscal year in progress, and reactions to the last proposed budget, which is being considered by Congress. Decisions are influenced also by projections of the economic outlook that are prepared jointly by the Council of Economic Advisers, OMB, and the Treasury Department.

In the fall, agencies submit budget requests to OMB, where analysts review them and identify for OMB officials issues that need to be discussed with agencies. Many issues are resolved between OMB and the agency. Others require the involvement of the President and White House policy officials. This decision-making process is usually completed by late December. At that time, the final stage of developing detailed budget data and the preparation of the budget documents begins.

The decision-makers must consider the effects of economic and technical assumptions on the budget estimates. Interest rates, economic growth, the rate of inflation, employment levels, and the size of the beneficiary populations are some of the assumptions that must be made. Small changes in these assumptions can affect budget estimates by billions of dollars. (Chapter 1, "Economic Assumptions" in the Analytical Perspectives volume of the 1996 budget provides more information on this subject.)

Budget decisions must also take into account any statutory limitations on receipts, outlays, and the deficit (see Budget Enforcement below).

Thus, the budget formulation process involves the simultaneous consideration of the resource needs of individual programs, the allocation of resources among the functions of the Government, the total outlays and receipts that are appropriate in relation to current and prospective economic conditions, and statutory constraints.

In most years, the President transmits the budget to Congress early in each calendar year, eight to nine months before the beginning of the next fiscal year on October first. The transmittal of the President's budget to Congress is scheduled in law for the first Monday in February. For various reasons, the budget has not always been transmitted on the scheduled date. In some years, Congress has been late in passing appropriations acts for the fiscal year prior to the budget year, which delays preparation of the budget. Also, this schedule does not require an outgoing President to transmit a budget, it is not practical for an incoming President to complete a budget within a few days of taking office on January 20th.[1]

Congressional Action[2]

Congress considers the President's budget proposals and approves, modifies, or disapproves them. It can change funding levels, eliminate programs, or add programs not requested by the President. It can add or eliminate taxes and other sources of receipts, or make other changes that affect the amount of receipts collected.

Congressional review of the budget begins shortly after the President transmits the budget to Congress. Under the procedures established by the Congressional Budget Act of 1974, Congress considers budget totals before completing action on individual appropriations. The Act requires each standing committee of the House and Senate to recommend budget levels and report legislative plans concerning matters within the committee's jurisdiction to the Budget Committee in each body. The Budget Committees then initiate the concurrent resolution on the budget. The budget resolution sets appropriate levels for total receipts and for budget authority and outlays, in total and by functional category (see Functional Classification below). It also sets appropriate levels for the budget deficit (or surplus) and debt.

The explanatory statement that accompanies the budget resolution allocates amounts of budget authority and outlays within the functional category totals to the committees that have jurisdiction over the programs in the functions. The House and Senate Appropriations Committees are required, in turn, to allocate amounts of budget authority and outlays among its respective subcommittees. Other committees may make allocations among their subcommittees but are not required to. There is no allocation at the program level. However, the functional allocations are based on certain assumptions about the level of funding for major programs. These assumptions may be included in the explanatory statement, but they are not binding on the committees of jurisdiction. The budget resolution may contain "reconciliation directives," which are discussed below.

The budget resolution is scheduled to be adopted by the whole Congress by April 15 of each year, but passage is often delayed. After passage of the budget resolution, a point of order can be raised to block consideration of bills that would cause a committee's allocation to be exceeded. Like the President's budget, the budget resolution is subject to spending limitations imposed in law through 1998.

Budget resolutions are not laws and, therefore, do not require the President's approval. However, Congress considers the Administration's views, because legislation developed to meet congressional budget allocations does require the President's approval. In some years, the President and the joint leadership of Congress have formally agreed on the framework of a deficit reduction plan. These agreements were reflected in the budget resolution and legislation passed for those years.

Congress does not enact a budget as such. It provides spending authority for specified purposes in several appropriations acts each year (usually thirteen). In making appropriations, Congress does not vote on the level of outlays (spending) directly, but rather on budget authority, which is the authority to incur legally binding obligations of the Government that will result in immediate or future outlays. In a separate process, prior to making appropriations, Congress usually enacts legislation that authorizes an agency to carry out a particular program and, in some cases, includes limits on the amount that can be appropriated for the program. Some programs require annual authorizing legislation, some are authorized for a specified number of years, and others are authorized indefinitely. Congress may enact appropriations for a program even though there is no specific authorization for it.

Appropriations bills are initiated in the House. The Appropriations Committee in each body has jurisdiction over annual appropriations. Those committees are divided into subcommittees that hold hearings and review detailed budget justification materials prepared by the agencies within the subcommittee's jurisdiction. After a bill has been approved by the committee and by the whole House, usually with amendments to the original version, it is forwarded to the Senate, where a similar review follows. In case of disagreement between the two Houses of Congress, a conference committee (consisting of Members of both bodies) meets to resolve the differences. The report of the conference committee is returned to both Houses for approval. When the measure is agreed to, first in the House and then in the Senate, it is ready to be transmitted to the President as an enrolled bill, for approval or veto.

If action on one or more appropriations bills is not completed by the beginning of the fiscal year, Congress enacts a joint continuing resolution to provide authority for the affected agencies to continue financing oper-

[1] The transmittal date was changed in 1990 from the first Monday after January 3rd. Thus, President Clinton was the first President in modern times to face this problem. The 1994 Budget was transmitted in early April 1993.

[2] For a fuller discussion of the congressional budget process, see Allen Schick, Robert Keith, and Edward Davis, *Manual on the Federal Budget Process* (Congressional Research Service Report 91-902 GOV, December 24, 1991) and Davis and Keith, *Budget Process Changes Adopted in August 1993* (CRS Report 93-778 GOV, December 6, 1993).

ations up to a specified date or until their regular appropriations are enacted. In some years, a portion or all of the Government has been funded for the entire year by a continuing resolution. Continuing resolutions must be presented to the President for approval or veto.

Congress provides spending authority in permanent laws as well as appropriations acts. These are laws that do not need to be reenacted each year. In fact, while spending authority for the majority of Federal programs is provided each year in appropriations acts, most of the total spending authority available in a year is provided by permanent laws. This is because the budget authority for interest on the public debt ($297 billion in 1994) and a few programs with large amounts of obligations each year, such as social security ($321 billion in 1994), are funded by permanent law. The outlays from permanent budget authority, together with the outlays from obligations incurred with budget authority provided in previous years, account for the majority of the outlay total for any year. Therefore, most outlays in a year are not controlled through appropriations actions for that year. The types of budget authority, their control by Congress, and the relation of outlays to budget authority are discussed in more detail in later in the chapter.

Almost all taxes and most other receipts result from permanent laws. Tax bills are initiated in the House. The House Ways and Means Committee and the Senate Finance Committee have jurisdiction over tax laws.

The reconciliation directives in a budget resolution usually require changes in permanent laws. They instruct each designated committee to make changes in the laws under the committee's jurisdiction that will change the levels of receipts and spending controlled by the laws. The instructions specify the dollar amount of changes that each designated committee is expected to achieve through changes in law, but do not specify the laws to be changed or the changes to be made. However, the changes in receipt and outlay amounts are based on certain assumptions about how laws would be changed, and these assumptions may be included in the explanatory statement accompanying the budget resolution. Like other assumptions included in the explanatory statement, these are not binding on the committees of jurisdiction.

The committees that are subject to reconciliation directives are expected to prepare implementing legislation. Such legislation may, for example, change the tax code, change benefit formulas or eligibility requirements for entitlement programs, or authorize Government agencies to charge fees to cover some of their costs. In some years, Congress has enacted an omnibus budget reconciliation act (OBRA), which combines the amendments to implement reconciliation directives in a single act. These acts, together with appropriations acts for the year, often implement agreements between the President and the Congress. They may include other matters, such as laws providing the means for enforcing these agreements, as described below.

Budget Enforcement

The Balanced Budget and Emergency Deficit Control Act of 1985 (commonly known as the Gramm-Rudman-Hollings Act) constrains legislation that would increase spending or decrease receipts through 1998. It was extended and amended extensively by the Budget Enforcement Act of 1990 and extended again by the Omnibus Budget Reconciliation Act of 1993.

The Act divides spending into two types—***discretionary spending*** and ***direct spending*** (sometimes called mandatory spending). Discretionary spending is controlled through annual appropriations acts. Funding for salaries and other operating expenses of Government agencies, for example, is usually discretionary because it is usually provided by appropriations acts. Direct spending is controlled by permanent laws. Medicare and medicaid payments, unemployment insurance benefits, and farm price supports are examples of direct spending, because payments for those purposes are authorized in permanent laws. The Act specifically defines funding for the Food Stamp program as direct spending, even though funding for the program is provided in appropriations acts. The Act includes receipts under the same rules that apply to direct spending, because receipts are generally controlled by permanent laws.

The Act constrains discretionary spending differently from direct spending and receipts. Discretionary spending is constrained by dollar limits ("caps") on budget authority and outlays for each fiscal year through 1998. The caps are adjusted when the budget is transmitted each year for the difference between the inflation rates assumed when the caps were enacted and actual inflation rates. The Act requires the caps to be adjusted for certain other reasons, such as to reflect the enactment of emergency appropriations. The caps for this budget, adjusted to reflect proposed changes, are shown in the following table:

DISCRETIONARY SPENDING LIMITS

(In billions of dollars)

	1994	1995	1996	1997	1998
Budget authority	525.1	527.0	508.2	497.9	510.5
Outlays	547.6	549.8	546.8	543.8	535.5

If the amount of budget authority provided in appropriations acts for the year exceeds the discretionary cap on budget authority, or the amount of outlays estimated to result from this budget authority is estimated to exceed the discretionary cap on outlays, the Act specifies a procedure, called ***sequestration***, for reducing discretionary spending. Under a sequester, spending for most discretionary programs is reduced by a uniform percentage. Special rules apply in reducing some programs, and some programs are exempt from sequester by law.

The Violent Crime Control and Law Enforcement Act of 1994 created the Violent Crime Reduction Trust Fund and appropriated a specified amount to the Fund for each year from 1995 through 2000. Spending from the Fund is controlled by annual appropriations acts, however, it is not subject to the general purpose discretionary caps. Instead, the Act specified outlay caps, which are not adjustable, and effectively capped budget authority, as shown in the following table:

VIOLENT CRIME REDUCTION LIMITS

(In billions of dollars)

	1994	1995	1996	1997	1998
Budget authority	—	2.4	4.3	5.0	5.0
Outlays	—	0.7	2.3	3.9	4.9

The Act amended the Gramm-Rudman-Hollings Act to require a separate sequester procedure, similar to the one required for general purpose discretionary spending, if the Violent Crime Reduction caps are exceeded.

Laws that would increase direct spending or decrease receipts are constrained through *"pay-as-you-go"* (PAYGO) rules. Under these rules, the cumulative effects of legislation affecting direct spending or receipts must not increase the deficit. Legislated increases in benefit payments, for example, have to be offset by legislated reductions in other direct spending or increases in receipts. Following the end of a session of Congress, OMB estimates the net effect on the deficit of laws enacted since the Act was passed that affect direct spending and receipts. If there is an estimated net increase in the deficit for the current fiscal year and the budget year combined, the Act specifies sequester procedures for the uniform reduction of most non-exempt direct spending programs. Special rules apply in reducing some non-exempt programs. Less than 3 percent of all direct spending is sequesterable; the rest is exempt from sequester by law.

The PAYGO rules do not apply to increases in direct spending or decreases in receipts that are not the result of new laws. For example, direct spending for benefit programs, such as unemployment insurance, rises when the population of eligible beneficiaries rises and many benefit payments are automatically increased for inflation under existing laws. Tax revenues decrease when the profits of private businesses decline as the result of economic conditions. To address the problem of rising direct spending, President Clinton issued Executive Order No. 12857, which established targets for direct spending (excluding deposit insurance and interest on the public debt) for 1994 through 1997. The targets were based on estimates made in 1994 and may be adjusted for unanticipated increases in the number of beneficiaries. If there is an actual or projected overage in any year, the President must submit a message to Congress, explaining the cause. Depending on the economic circumstances at the time, the President may recommend recouping or eliminating all, some, or none of the overage. If the President recommends reducing the overage, he must specify how. The House has instituted rules to expedite its response to such a message. (Chapter 15, "Review of Direct Spending and Receipts," in the *Analytical Perspectives* volume of the 1996 budget provides more information on this subject.)

The Gramm-Rudman-Hollings Act requires OMB to make the estimates and calculations that determine whether there is to be a sequester and report them to the President and Congress. The Congressional Budget Office (CBO) is required to make the same estimates and calculations, and the Director of OMB is required to explain any differences between the OMB and CBO estimates. The estimates and calculation by OMB are the basis for sequester orders issued by the President. The President's orders may not change any of the particulars of the OMB report. The General Accounting Office is required to prepare compliance reports.

OMB and CBO are required to publish three sequestration reports—a "preview" report at the time the President submits the budget, an "update" report in August, and a "final" report at the end of a session of Congress (usually in the Fall of each year). The preview report discusses the status of discretionary and PAYGO sequestration based on current law. This report explains the adjustments that are required by law to the discretionary caps and publishes the revised caps. The preview report estimates are revised in the update and final reports to reflect the effects of laws enacted since the preview report. In addition to these reports, OMB and CBO are required to estimate the effects of appropriations acts and PAYGO laws immediately after each one is enacted. The OMB final report estimates trigger a sequester if the appropriations enacted for the current year exceed the caps or if the cumulative effect of PAYGO legislation are estimated to increase the deficit.

From the end of a session of Congress through the following June 30th, discretionary sequesters take place whenever an appropriation act for the current fiscal year causes a cap to be exceeded. Because a sequester in the last quarter of a fiscal year might be too disruptive, the Act specifies that a sequester that otherwise would be required then is to be accomplished by reducing the limit for the next fiscal year. These requirements ensure that supplemental appropriations enacted during the fiscal year are covered by the budget enforcement provisions.

Budget Execution

Government officials are generally required to spend no more and no less than has been appropriated, and they may use funds only for purposes specified in law. The Antideficiency Act prohibits government officials from spending or obligating the government to spend in advance of an appropriation, unless specific authority to do so has been provided in law. Additionally, the Act requires the President to apportion the funds available to most executive branch agencies. The President has delegated this authority to OMB. OMB usually apportions by time periods (usually by quarter of the fiscal year) and sometimes by activities. Agencies may request that an account be reapportioned during the year to accommodate changing circumstances. This system helps to ensure that funds are available to cover operations for the entire year.

If changes in laws or other factors make it necessary, Congress may enact ***supplemental appropriations***. For example, a supplemental appropriation might be required to respond to an unusually severe natural disaster.

On the other hand, changing circumstance may reduce the need for certain spending for which funds have been appropriated. However, the President may withhold amounts appropriated from obligation, only under certain limited circumstances, in order to provide for contingencies, to achieve savings made possible through changes in requirements or greater efficiency of operations, or as otherwise specifically provided in law. The Impoundment Control Act of 1974 specifies the procedures that must be followed if funds are withheld. Deferrals, which are temporary withholdings, take effect immediately unless overturned by an act of Congress. In 1994, a total of $8.6 billion in deferrals were reported to Congress and none were overturned. Rescissions, which permanently cancel budget authority, do not take effect unless Congress passes a law approving them. If such a law is not passed within 45 days of continuous session, the withheld funds must be made available for spending. In total, Congress has approved less than one-third of the amount of funds that Presidents have proposed for rescission since enactment of the Impoundment Control Act. In 1994, the President proposed rescissions totalling $3.2 billion, and Congress enacted a total of $1.3 billion.

Budget Calendar

The following timetable highlights the dates of significant budget events during the year.

Between the 1st Monday in January and the 1st Monday in February	President transmits the budget, including a sequester preview report
Six weeks later	Congressional committees report budget estimates to Budget Committees.
April 15	Action to be completed on congressional budget resolution.
May 15	House consideration of annual appropriations bills may begin.
June 15	Action to be completed on reconciliation.
June 30	Action on appropriations to be completed by House.
July 15	President transmits Mid-Session Review of the budget.
August 20	OMB updates the sequester preview.
October 1	Fiscal year begins.
15 days after the end of a session of Congress	OMB issues final sequester report, and the President issues a sequester order, if necessary.

COVERAGE OF THE BUDGET

Federal Government and Budget Totals

The budget documents provide information on all Federal agencies and programs. The total receipts and outlays of the Federal Government are composed of both on-budget receipts and outlays and receipts and outlays that, by law, are designated as off-budget. By law, the receipts and outlays of social security (the Federal Old-Age and Survivors Insurance and the Federal Disability Insurance trust funds) and the Postal Service Fund are excluded from the budget totals and from the calculation of the deficit for Gramm-Rudman-Hollings Act purposes. The off-budget transactions are separately identified in the budget. The on-budget and off-budget amounts are added together to derive totals for the Federal Government.

TOTALS FOR THE BUDGET AND THE FEDERAL GOVERNMENT

(In billions of dollars)

	1994 actual	1995 estimate	1996 estimate
On-budget:			
Budget authority	1,246	1,266	1,305
Outlays	1,182	1,247	1,307
Receipts	923	995	1,045
Deficit	−259	−252	−262
Off-budget:			
Budget authority	283	298	309
Outlays	279	292	305
Receipts	335	351	370
Surplus	56	60	66
Federal Government:			
Budget authority	1,528	1,564	1,614
Outlays	1,461	1,539	1,612
Receipts	1,258	1,346	1,415
Deficit	−203	−193	−197

Neither the on-budget nor the off-budget totals include transactions of Government-sponsored enterprises, such as the Federal National Mortgage Association (Fannie Mae) and the Student Loan Marketing Association (Sallie Mae). These enterprises were established by federal law for public policy purposes but are privately owned and operated corporations. Because of their close relationship to the Government, these enterprises are discussed in several parts of the budget, and their financial data are reported in the *Appendix to the Budget of the United States Government* and some detailed tables.

A presentation for the Board of Governors of the Federal Reserve System is included in the *Appendix* for information only. The amounts are not included in either the on-budget or off-budget totals because of the independent status of the System. However, the Federal Reserve Systems net earning are transferred annually to the Treasury, and are recorded in the budget as receipts.

Functional Classification

The functional classification arrays budget authority, outlays, and other budget data according to the major purpose served—such as agriculture, income security, and national defense. There are nineteen major functions, most of which are divided into subfunctions. For example, the ***Agriculture*** function is divided into ***Farm Income Stabilization*** and ***Agricultural and Research Services***. The functional classification is an integral part of the congressional budget process, and the functional array meets the Congressional Budget Act requirement for a presentation in the budget by national needs and agency missions and programs.

The following criteria are used in the establishment of functional categories and the assignment of activities to them:

- A function comprises activities with similar purposes addressing an important national need. The emphasis is on what the Federal Government seeks to accomplish rather than the means of accomplishment, the objects purchased, or the clientele or geographic area served.
- A function must be of continuing national importance, and the amounts attributable to it must be significant.
- Each basic unit being classified (generally the appropriation or fund account) usually is classified according to its predominant purpose and assigned to only one subfunction. However, some large accounts that serve more than one major purpose are subdivided into two or more subfunctions.
- Activities and programs are normally classified according to their primary purpose (or function) regardless of which agencies conduct the activities.

Chapter 6, "Federal Spending by Function, Subfunction, and Major Program" in the *Analytical Perspectives* volume of the 1996 budget provides information on budget authority and outlays by function and subfunction.

Agencies, Accounts, Programs, Projects, and Activities

Various summary tables in the *Analytical Perspectives* volume of the 1996 budget provide information on budget authority, outlays, and receipts arrayed by Federal agency. Chapter 26 of that volume, "Federal Programs by Agency and Account," consists of a table that lists budget authority and outlays by budget account within each agency and the totals for each agency of budget authority, outlays, and receipts that offset the agency spending totals. The *Appendix to the Budget of the United States Government* provides budgetary, financial, and descriptive information about programs, projects, and activities by account within each agency. That volume of the budget also presents the most recently enacted appropriation language for an account and any changes that are proposed to be made for the budget year.

Types of Funds

Agency activities are financed through Federal funds and trust funds.

Federal funds comprise several types of funds. The ***general fund,*** which is the greater part of the budget, is credited with receipts not earmarked by law for a specific purpose, such as almost all income tax receipts, and is also credited with the proceeds of general borrowing. General fund appropriation accounts record general fund expenditures. General fund appropriations are drawn from general fund receipts collectively and, therefore, are not specifically linked to receipt accounts. ***Special funds*** consist of receipt accounts for Federal fund receipts that are earmarked by law for specific purposes and associated appropriation accounts for the expenditure of the earmarked receipts. ***Public enterprise (revolving) funds*** are used for programs authorized by law to conduct a cycle of business-type operations, primarily with the public, in which outlays generate collections. The collections and the outlays of the fund are recorded in the same account. ***Intragovernmental funds*** are revolving funds that conduct business-type operations primarily within and between Government agencies.

Trust funds are established to account for the receipt and expenditure of monies by the Government for carrying out specific purposes and programs in accordance with the terms of a statute that designates the fund as a trust fund (such as the Highway Trust Fund) or for carrying out the stipulations of a trust agreement (such as any of several trust funds for gifts and donations for specific purposes). ***Trust revolving funds*** are trust funds credited with collections earmarked by law to carry out a cycle of business-type operations.

The Federal budget meaning of the term "trust" differs significantly from its private sector usage. In the private sector, the beneficiary of a trust usually owns the trust's assets, which are managed by a trustee who must follow the stipulations of the trust. In contrast, the Federal Government owns the assets of most Federal trust funds, and it can raise or lower future trust fund collections and payments, or change the purposes for which the collections are used, by changing existing laws. There is no substantive difference between a trust fund and a special fund or between a trust revolving fund and a public enterprise revolving fund. (Chapter 18, "Trust Funds and Federal Funds," in the *Analytical Perspectives* volume of the 1996 budget provides more information on this subject.)

Current Operating Expenses and Capital Investment

The budget includes all types of spending, including both current operating expenses and capital investment. Capital investment includes direct purchases of land, structures, and equipment. It also includes subsidies for capital investment provided by direct loans and loan guarantees; the purchase of other financial assets; grants to state and local governments for the purchase of physical assets; and the conduct of research, development, education, and training. (Chapter 7, "Federal investment outlays and capital budgets," in the *Analytical Perspectives* volume of the 1996 budget provides more information on capital investment.)

COLLECTIONS

In General

Money collected by the Government is classified into ... ...

- ***Governmental receipts***, whic' ~re compared in total to outlays (net of offsetting collections) in calculating the surplus or deficit.
- ***Offsetting collections***, which are deducted from gross outlays to produce net outlay figures.

Governmental Receipts

These are collections from the public that result primarily from the exercise of the Government's sovereign or governmental powers. Governmental receipts consist mostly of individual and corporate income taxes and social insurance taxes, but also include excise taxes, compulsory user charges, customs duties, court fines, certain license fees, and deposits of earnings by the Federal Reserve System. Gifts and donations are also counted as governmental receipts. Total receipts for the Federal Government include both on-budget and off-budget receipts (see the table, "Totals for the Budget and Federal Government," which appears earlier in this chapter.)

Offsetting Collections

These are amounts received from the public as a result of business-like or market-oriented activities (for example, proceeds from the sale of postage stamps or electricity, fees for admittance to recreation areas, or the proceeds from the sale of Government-owned land) and amounts collected from other Government accounts. Offsetting collections from the public are deducted from gross budget authority and outlays, rather than combined with governmental receipts. The purpose of this treatment is to produce budget totals for receipts, budget authority, and outlays that represent governmental rather than market activity. Intragovernmental offsetting collections are deducted from gross budget authority and outlays so that the budget totals measure the transactions of the Government with the public.

Offsetting collections are classified into two major categories: ***offsetting collections credited to appropriation or fund accounts***, and ***offsetting receipts***, which are deposited in receipt accounts. The offset is applied differently for each type.

Offsetting Collections Credited to Expenditure Accounts

For all revolving funds and many appropriation accounts, laws authorize collections to be credited directly to expenditure accounts and, usually, to be spent for the purpose of the account without further action by Congress. These collections may be from either the public or other expenditure accounts. For example, a permanent law authorizes the Postal Service to use collections from the sale of stamps to finance its operations without a requirement for annual appropriations. The offsetting collections that are authorized to be spent are recorded as budget authority. Sometimes this is not the full amount of the offsetting collections, because appropriations acts may contain limitations on the obligations that can be financed by such budget authority. In those cases, the recorded budget authority is adjusted to reflect the amount available to incur obligations. The budget authority and outlays of the appropriation or fund account are shown both gross (that is, before deducting offsetting collections) and net (that is, after deducting offsetting collections). Totals for the agency, subfunction, and budget are net of offsetting collections.

While most offsetting collections credited to expenditure accounts result from business-like activity or are collected from other Government accounts, some are governmental in nature but are required by law to be treated as offsetting. These are labeled as "offsetting governmental collections."

Offsetting Receipts

Offsetting collections that are not authorized to be credited to expenditure accounts are credited to general fund, special fund, or trust fund receipt accounts and are called offsetting receipts. Offsetting receipts are deducted from budget authority and outlays in arriving at total budget authority and outlays. In most cases, such deductions are made at the subfunction and agency levels. Unlike offsetting collections credited to expenditure accounts, offsetting receipts do not offset budget authority and outlays at the account level. Offsetting receipts are subdivided into three categories, as follows:

- *Proprietary receipts from the public.*—These are collections from the public, deposited in receipt accounts, that arise out of the business-type or market-oriented activities of the Government. Most proprietary receipts are deducted from the budget authority and outlay totals of the agency that conducts the activity generating the receipt and of the subfunction to which the activity is assigned. For example, fees for using National Parks are deducted from the totals for the Department of Interior, which has responsibility for the parks, and the Recreational Resources subfunction. A limited number of proprietary receipts, however, are not offset against any specific agency or function and are classified as undistributed offsetting receipts. They are deducted from the Government-wide totals for budget authority and outlays. For example, the collections of rent and royalties from Outer Continental Shelf lands are undistributed because the amounts are large and for the most part are not related to the spending of the agency and subfunction that administers the transactions.
- *Intragovernmental transactions.*—These are collections from appropriation or fund accounts that are deposited into receipt accounts. Most intragovernmental transactions are deducted from the budget authority and outlays of the agency that conducts the activity generating the receipts and of the subfunction to which the activity is assigned. In two cases, however, intragovernmental transactions appear as special deductions in computing total budget authority and outlays for the Government rather than as offsets at the agency level—agencies' payments as employers into employee retirement trust funds and interest received by trust funds. The special treatment for these receipts is necessary because the amounts are large and would distort the agency totals if attributed to the agencies.
- *Offsetting governmental receipts.*—These are collections that are governmental in nature but are required by law to be treated as offsetting.

There are several categories of intragovernmental transactions. *Intrabudgetary transactions* include all payments from on-budget expenditure accounts to on-budget receipt accounts. These are subdivided into three categories: (1) *interfund transactions*, where the payment is from an expenditure account in one fund group (either Federal funds or trust funds) to a receipt account in the other fund group; (2) *Federal intrafund transactions*, where the payment and receipt both occur within the Federal fund group; and (3) *trust intrafund transactions*, where the payment and receipt both occur within the trust fund group. In addition, there are intragovernmental transactions that are not intrabudgetary—payments from on-budget expenditure accounts to off-budget receipt accounts, and from off-budget expenditure accounts to on-budget receipt accounts.

BUDGET AUTHORITY AND OTHER BUDGETARY RESOURCES, OBLIGATIONS, AND OUTLAYS

Budget Authority and Other Budgetary Resources

Government agencies are permitted to enter into obligations requiring either immediate or future outlays only when they have been granted authority to do so by law. This authority is recorded as budget authority in the year that it first becomes available. Unobligated balances of budget authority may remain available from previous years, but they are not recorded as budget authority again in subsequent years. They do, however, constitute a budgetary resource that is available for obligation. The use of budgetary resources otherwise available may be constrained by the imposition of legally binding limitations on obligations (for example, obligations for administrative expenses of benefit programs). Such limitations substitute for budget authority, for some purposes, and are treated as a budgetary resource.

In deciding the amount of budget authority to request for a program, project, or activity, Government officials estimate the total amount of obligations that will need to be incurred to achieve desired goals and subtract the amounts of unobligated balances available for these purposes. The amount of budget authority requested is influenced by the nature of the programs, projects, or activities being financed. For current operating expenses, the amount requested usually is the amount estimated to be needed for the year. For major procurement programs and construction projects, a full funding policy generally applies. Under this policy, an amount that is estimated to be adequate to complete the procurement or project must be requested to be appropriated in the first year, even though it may be obligated over several years. This policy is intended to avoid piecemeal funding of programs and projects that cannot be used until they have been completed.

Budget authority takes several forms:

- *appropriations*, which permit obligations to be incurred and payments to be made;
- *borrowing authority*, which permits obligations to be incurred but requires that funds be borrowed, generally from the general fund of the Treasury, to make payment; and
- *contract authority*, which permits obligations in advance of a separate appropriation of the cash

for payment or in anticipation of the collection of receipts that can be used for payment.

The form of budget authority is usually determined u the authorizing statute for a program. The authorizing statute may authorize a particular type of budget authority to be provided in annual appropriations acts,) it may actually provide the budget authority in one): its forms. Most programs are funded by appropriations. An appropriation may make funds available from the general fund, special funds, trust funds, or authorize the spending of offsetting collections credited to expenditure accounts, including revolving funds. Borrowing authority is usually authorized for business-like ac- ti ties where the activity being financed is expected to produce income over time with which to repay the borrowing with interest. Contract authority is a traditional form of budget authority for certain programs,)ı ticularly transportation programs.

ecause offsetting collections (offsetting receipts and offsetting collections credited to expenditure accounts) are deducted from gross budget authority, they are re- e [illegible] negative budget authority for some purpose, [illegible] as Congressional Budget Act provisions that pertain to budget authority.

Budget authority that is provided in an annual appro-)r tions act is available for obligation only during the iscal year to which the appropriations act applies, un- ess the appropriation language providing the budget ιι 1ority specifies that it is to remain available for ι nger period. Typically, budget authority for current perations is made available for obligation in only one ear. Some budget authority is made available for a p :ified number of years. Other budget authority, in- lı ing most provided for construction, some for re- earch, and many appropriations of trust fund receipts, s made available for obligation until the amount appro-)r ted has been expended or until the program objec- i[illegible] have been attained.

Congress usually makes budget authority available n he first day of the fiscal year for which the appro-)r tions act is passed. Occasionally, the appropriations anguage specifies a different timing. The language may rovide an ***advance appropriation***—budget authority h does not become available until one year or more e nd the fiscal year for which the appropriations act s passed. ***Forward funding*** refers to budget authority hat is made available for obligation beginning in the a: quarter of the fiscal year (beginning on July 1st))ı he financing of ongoing grant programs during the ext fiscal year. This kind of funding is used mostly)r education programs, so that obligations for grants a be made prior to the beginning of the next school e[illegible]. For certain benefit programs funded by annual ppropriations, the appropriation provides for ***advance*** u. ***ling***—budget authority that is to be charged to he appropriation in the succeeding year but which au- horizes obligations to be incurred in the last quarter f the fiscal year if necessary to meet benefit payments n xcess of the specific amount appropriated for the e: .

When budget authority is made available by law for a specific period of time, any part that is not obligated during that period expires and cannot be used later. Provisions of law that extend the availability of unobligated amounts that have expired or would otherwise expire are called ***reappropriations***. Reappropriations are counted as new budget authority in the fiscal year in which the balances become newly available. For example, if a 1995 appropriations act extends the availability of unobligated budget authority that otherwise would expire at the end of 1994, new budget authority would be recorded for 1995.

Budget authority is classified in the budget as ***current*** or ***permanent***. Generally, budget authority is current if it is provided by annual appropriations acts and permanent if it becomes available pursuant to standing authorizing legislation. Advance appropriations of budget authority are classified as permanent, even though they are provided in annual appropriations acts, because they become available a year or more following the [illegible] to whi[illegible] spend offsetting collections credited to appropriation and revolving fund accounts usually is provided by authorizing legislation and, therefore, is usually a form of permanent budget authority.

Obligations and outlays resulting from permanent budget authority, including the authority to spend offsetting collections credited to expenditure accounts, account for more than half of the budget totals. Put another way, less than half of the obligations and outlays in the budget result from annual appropriations acts. Most permanent budget authority, other than the authority to spend offsetting collections, arises from the authority to spend trust fund receipts and the authority to pay interest on the public debt. Most authority to spend offsetting collections applies to public enterprise revolving funds.

Budget authority also is classified in the budget as ***definite*** or ***indefinite***. Budget authority is definite if the legislation that provides it specifies a definite dollar amount (including an amount not to be exceeded). Budget authority is indefinite if, instead of specifying an amount, the legislation providing it permits the amount to be determined by subsequent circumstances. For example, indefinite budget authority is provided for interest on the public debt, payment of claims and judgments awarded by the courts against the U.S., and many entitlement programs. Many of the laws that authorize collections to be credited to revolving, special, and trust funds make all of the collections available for expenditure for the authorized purposes of the fund. Such authority is considered to be indefinite budget authority. In some such cases, only some of these amounts are counted as budget authority, because they are precluded from obligation in a fiscal year by a provision of law, such as a limitation on obligations or a benefit formula that determines the amounts to be paid (for example, the formula for unemployment insurance benefits).

Obligations Incurred

Following the enactment of budget authority and the completion of required apportionment action, Government agencies incur obligations. Such obligations include: the current liabilities for salaries, wages, and interest; contracts for the purchase of supplies and equipment, construction, and the acquisition of office space, buildings, and land; and other arrangements requiring the payment of money. For Federal credit programs, obligations are recorded in an amount equal to the estimated subsidy cost of direct loans and loan guarantees (see FEDERAL CREDIT below).

Outlays

Outlays are recorded when obligations are paid, in the amount paid. Obligations are usually paid in the form of cash (currency, checks, or electronic fund transfers). However, obligations also may be paid and outlays recorded even though no cash is disbursed. For example, outlays are recorded for the full amount of Federal employees' salaries, even though the cash disbursed to the employee is net of Federal and state income taxes, retirement contributions, life and health insurance premiums, and other deductions. (Receipts are also recorded for the deductions that represent payments to the Government.) Outlays are recorded when debt instruments (bonds, debentures, notes, or monetary credits) are used to pay obligations. (An increase in debt is also recorded when such instruments are used.) For example, the acquisition of physical assets through certain types of lease-purchase arrangements is treated as though an outlay were made for an outright purchase. Because no cash is paid up front to the nominal owner of the asset, a debt is recorded. The actual cash payments, nominally lease payments, in such cases are recorded as repayments of principal and interest.

The treatment of interest varies. Outlays for the interest on the public issues of Treasury debt securities are recorded as the interest accrues, not when the cash is paid. Interest on special issues of the debt securities held by trust funds and other Government accounts is normally stated on a cash basis. When a Government account invests in Federal debt securities, the purchase price is usually close or identical to the par (face) value of the security. The budget records the investment at par value and adjusts the interest paid by Treasury and collected by the account by the difference between purchase price and par, if any. However, in the case of two trust funds in the Department of Defense, the Military Retirement Trust Fund and the Education Benefits Trust Fund, the differences between purchase price and par are routinely relatively large. For these funds, the budget records the holdings of debt at par but records the differences between purchase price and par as adjustments to the assets of the funds that are amortized over the life of the security. Interest is recorded as the amortization occurs. The special issues of zero-coupon bonds held by the Pension Benefit Guaranty Corporation are recorded at market value and the interest is accrued.

For Federal credit programs, outlays are equal to the subsidy cost of direct loans and loan guarantees and are recorded as the underlying loans are disbursed (see FEDERAL CREDIT below).

Refunds of receipts (such as income taxes in excess of tax liabilities) are recorded as reductions of receipts, rather than as outlays.

Outlays during a fiscal year may be for the payment of obligations incurred in the same year or in prior years. Obligations, in turn, may be incurred under budget authority provided in the same or in prior years. Outlays, therefore, flow in part from unexpended balances of prior year budget authority and in part from budget authority provided for the year in which the money is spent. The ratio of the outlays resulting from budget authority enacted in any year to the amount of that budget authority is referred to as the ***spendout rate*** for that year.

Outlays for an account are stated both gross and net of offsetting collections, but function, agency, and Government-wide outlay totals are only stated net. Total outlays for the Federal Government include both on-budget and off-budget outlays. (See the table, "Totals for the Budget and Federal Government," which appears earlier in this chapter.)

Balances of Budget Authority

Not all budget authority enacted for a fiscal year results in obligations and outlays in the same year. In the case of budget authority that is available for more than one year, the ***unobligated balance*** of budget authority that is still available at the end of a year may be carried forward for obligation in the following year. The ***obligated balance*** is that portion of the budget authority that has been obligated but not paid. For example, in the case of salaries and wages, 1 to 3 weeks elapse between the time of obligation and the time of payment. In the case of major procurement and construction, payments may occur over several years. Obligated balances of budget authority are carried forward until the obligations are paid.[3]

A change in the amount of obligations incurred from one year to the next is not necessarily accompanied by an equal change in either the budget authority or the outlays of that same year. Conversely, a change in budget authority in any one year may cause changes in the level of obligations and outlays for several years.

[3] Additional information is provided in a separate report, "Balances of Budget Authority," which is available from the National Technical Information Service, Department of Commerce, shortly after the budget is transmitted.

FEDERAL CREDIT

Government programs may be carried out through federally supported credit in the form of ***direct loans*** or ***loan guarantees***. A direct loan is a disbursement of funds by the Government to a non-Federal borrower under a contract that requires the repayment of such funds with or without interest. A loan guarantee is any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender. The Federal Credit Reform Act prescribes the budget treatment for Federal credit programs. This treatment is designed to measure the subsidy cost of direct loans and guaranteed loans in the budget, rather than the cash flows, so they can be compared to each other and to other methods of delivering benefits, such as grants, on an equivalent basis.

Under credit reform, the estimated long-term cost to the Government arising from the direct loans and loan guarantees of a credit program must be estimated and recorded in the budget in a ***credit program account***. The cost is estimated as the present value of expected disbursements over the term of the loan less the present value of expected collections.[4] For most programs, direct loan obligations and loan guarantee commitments cannot be made unless Congress has appropriated funds for the costs in advance in annual appropriations acts. In addition, the appropriation language for most credit programs includes annual limitations on the amount of obligations for direct loans and commitments for loan guarantees.

When a direct or guaranteed loan is disbursed, the program account makes a payment equal to the cost, which is recorded as an outlay, to a non-budgetary ***credit financing account***. For a few programs, the computed cost is negative for a portion or all of the direct loans and loan guarantees. In such cases, the financing account makes a payment to a special fund receipt account established for the program, where it is recorded as an offsetting receipt.

The cost of the outstanding direct and guaranteed loans is reestimated each year. If the cost is estimated to have increased, an additional outlay is made from the program account to the financing account, and, if the cost is estimated to have decreased, a payment is made from the financing account to the program's special fund receipt account, where it is recorded as an offsetting receipt. A permanent appropriation is available to pay the increased costs resulting from reestimates.

If the terms of an outstanding direct loan or loan guarantee are modified in a way that increases the cost, an outlay in the amount of the increased cost is made from the program account to the financing account. The additional cost is recorded as an obligation against the budget authority provided for the costs of the program for that year. The requirement to record the costs of modification applies to pre-credit reform, as well as post-credit reform, direct loans and loan guarantees.

Credit financing accounts record all cash flows to and from the Government arising from direct loan obligations and loan guarantee commitments. These cash flows consist mainly of direct loan disbursements and repayments and loan guarantee default payments. The cash flows of direct loans and of loan guarantees are recorded in separate financing accounts for programs that do both. The transactions of the financing accounts are displayed in the budget documents for information and analytical purposes, together with the related program accounts, but are excluded from the budget totals because they are not a cost to the Government. Financing account transactions are a means of financing a budget surplus or deficit (see **Credit Financing Accounts** below).

The transactions associated with direct loan obligations and loan guarantee commitments made prior to 1992 continue to be accounted for on a cash flow basis and are recorded in ***liquidating accounts***. In most cases, the liquidating account is the account that was used for the program prior to the enactment of credit reform in 1990.

BUDGET DEFICIT OR SURPLUS AND MEANS OF FINANCING

A budget deficit is the amount by which outlays exceed receipts. Deficits are financed by borrowing and, to a limited extent, the other items discussed under this heading. The debt (debt held by the public) is the cumulative amount of borrowing to finance deficits, less repayments. When receipts exceed outlays, the difference is a budget surplus. Surpluses are used to reduce debt and, to a limited extent, may be absorbed by the other items.

Borrowing and Repayment

Borrowing is not defined as receipts, and debt repayment is not defined as outlays. If they were, the budget would virtually be balanced by definition. This rule applies both to borrowing in the form of Treasury securities and to specialized borrowing in the form of agency securities (including the issuance of debt securities to liquidate an obligation and the sale of certificates representing participation in a pool of loans). In addition

[4] Present value is a standard financial concept that allows for the time value of money, that is, for the fact that a given sum of money is worth more at present than in the future because interest can be earned on it.

to issuing debt to the public, the Government issues debt to Government accounts, primarily trust funds that are required by law to invest in Treasury securities. This debt is not a means of financing deficits, because it does not raise any additional cash. In 1994, the Government borrowed $185 billion from the public to finance the deficit of $203 billion in that year (the rest was financed by various other means). At the end of 1994, the debt held by the public was $3,432 billion. (See Chapter 13, "Federal Borrowing and Debt," in the *Analytical Perspectives* volume of the 1996 budget for a fuller discussion of this topic.)

Exercise of Monetary Power

Seigniorage is the profit from coining money. It is the difference between the value of coins as money and their cost of production. Seigniorage on coins arises from the exercise of the Government's monetary powers but differs from receipts coming from the public, since there is no corresponding payment by another party. Therefore, seigniorage is excluded from receipts and treated as a means of financing the deficit other than borrowing from the public. The profit resulting from the sale of gold as a monetary asset also is treated as a means of financing, since the value of gold is determined by its value as a monetary asset rather than as a commodity.

Credit Financing Accounts

The net cash flows of credit programs are recorded in credit financing accounts, which are excluded from the budget totals and are called ***net financing disbursements.*** (See FEDERAL CREDIT above.) Net financing disbursements are defined in the same way as the outlays of a budgetary account and may be either positive or negative. If positive, they must be paid in cash and increase the requirement for Treasury borrowing in the same way as an increase in budget outlays and the budget deficit; if negative, they provide cash to the Treasury that can be used to finance the payment of the Government's obligations. The net financing disbursements are therefore a means of financing the deficit other than borrowing from the public.

Deposit Fund Account Balances

Certain accounts outside the budget, known as deposit funds, are established to record amounts held temporarily until ownership is determined (for example, earnest money paid by bidders for mineral leases) or held by the Government as agent for others (for example, State and local income taxes withheld from Federal employees' salaries and payroll deductions for the purchase of savings bonds by employees of the Government). Deposit fund balances may be held in the form of either invested or uninvested balances. Changes in deposit fund balances affect Treasury's cash balances, even though the transactions are not a part of the budget. To the extent that deposit fund balances are not invested, changes in the balances are reflected as a means of financing the deficit other than borrowing from the public. To the extent that the balances are invested in Federal debt, changes in the balances are reflected as borrowing from the public or as a means of financing the deficit other than borrowing from the public, depending on whether the deposit fund investments are classified as held by the public or the Government.

Exchange of Cash

The Government's deposits with the International Monetary Fund (IMF) are considered to be monetary assets. Therefore, the movement of money between the IMF and the Treasury is not considered in itself a receipt or an outlay, borrowing, or lending. However, interest paid by the IMF on U.S. deposits is an offsetting collection. In a similar manner, the holdings of foreign currency by the Exchange Stabilization Fund are considered to be cash assets. Changes in these holdings are outlays only to the extent there is a realized loss of dollars on the exchange and are offsetting collections only to the extent there is a realized dollar profit

FEDERAL EMPLOYMENT

The budget includes information on civilian and military employment and personnel compensation and benefits. It also makes comparisons between the Federal workforce, State and local government workforces, and the United States population. Two different measures of employment levels are provided—actual positions filled and full-time equivalents (FTE). One FTE is equal to one work year or 2,080 hours. For most purposes, the FTE measure is more meaningful, because it takes into account part-time employment, temporary employment, and vacancies during the year. (Chapter 12, "Federal Employment," in the *Analytical Perspectives* volume of the 1996 budget provides more information on this subject.)

TOTAL FEDERAL EMPLOYMENT

	1994 actual	1995 estimated	1996 estimated	Percent change 1994-1996
Total FTE's	4,600,057	4,484,177	4,304,585	–4.5
Federal Executive Branch civilian employees per 1000 U.S. population	11.2	10.9	10.7	–4.5

BASIS FOR BUDGET FIGURES

Data for the Past Year

The past year column (1994) generally presents the actual transactions and balances as recorded in agency accounts and as summarized in the central financial reports prepared by the Treasury Department for the most recently completed fiscal year. Occasionally the budget reports corrections to data reported erroneously to Treasury but not discovered in time to be reflected in Treasury's published data. The budget usually notes the sources of such differences.

Data for the Current Year

The current year column (1995) includes estimates of transactions and balances based on the amounts of budgetary resources that were available when the budget was transmitted, including amounts appropriated for the year. This column also reflects any supplemental appropriations or rescissions that are proposed in the budget.

Data for the Budget Year

The budget year column (1996) includes estimates of transactions and balances based on the amounts of budgetary resources that are estimated to be available, including amounts proposed to be appropriated. The budget generally includes the appropriations language for the amounts proposed to be appropriated. Where the estimates represent amounts that will be requested under proposed legislation, the appropriation language usually is not included; it is transmitted later, usually after the legislation is enacted. In a few cases, proposed language for appropriations to be requested under existing legislation is transmitted later because the exact requirements are not known when the budget is transmitted. In certain tables of the budget, the items for later transmittal and the related outlays are identified separately. Estimates of the total requirements for the budget year include both the amounts requested with the transmittal of the budget and the amounts planned for later transmittal.

Data for the Outyears

The budget presents estimates for each of the four years beyond the budget year (1997 through 2000) in order to reflect the effect of budget decisions on longer term objectives and plans.

Allowances

Lump-sum allowances may be included in the budget to cover certain transactions that are expected to increase or decrease budget authority, outlays, or receipts but that are not for various reasons reflected in the program details. Budget authority and outlays are never appropriated as such, rather they indicate the estimated budget authority and outlays that will be requested for specific programs.

Baseline

The budget baseline is an estimate of the receipts, outlays, and deficits that will result from laws already enacted. For receipts and direct spending, which generally are authorized on a permanent basis, it assumes th · continue in the future as required by current law. For discretionary programs, which generally are funded annually, the baseline commonly assumes future funding will be equal to the most recently enacted appropriation, adjusted for inflation. Because most receipts and mandatory programs adjust automatically for inflation, the baseline represents the amount of real resources that will be used by the Government over the period covered by the budget. (Chapter 17, "Current services estimates," in the *Analytical Perspectives* volume of the 1996 budget provides more information on the baseline.)

The baseline is useful for several reasons. It warns of future problems, either for Government fiscal policy as a whole or for individual tax and spending programs. It provides a starting point for formulating the President's budget. It is a "policy-neutral" benchmark against which the President's budget and alternative proposals can be compared to see the magnitude of proposed changes. And it is used, under the Budget Enforcement Act, to determine how much will be sequestered from each account and what level of funding will be available after sequestration.

PRINCIPAL BUDGET LAWS

The following are the basic laws pertaining to the Federal budget process:

- ***Article 1, section 9, clause 7 of the Constitution***, which requires appropriations in law before money may be spent from the Treasury.
- ***Chapter 11 of Title 31, United States Code***, which prescribes procedures for submission of the President's budget and information to be contained in it.
- ***Congressional Budget and Impoundment Control Act of 1974*** (Public Law 93–344), as amended. This Act comprises the·
  - —Congressional Budget Act of 1974, as amended, which prescribes the congressional budget process; and
  - —Impoundment Control Act of 1974, which controls certain aspects of budget execution.
- ***Balanced Budget and Emergency Deficit Control Act of 1985*** (Public Law 99–177), as amend-

ed, which prescribes rules and procedures (including "sequestration") designed to eliminate excess deficits. This Act is commonly known as the Gramm-Rudman-Hollings Act.

- ***Budget Enforcement Act of 1990*** (Title XIII, Public Law 101-508), which significantly amended the laws pertaining to the budget process, including the Congressional Budget Act and the Balanced Budget and Emergency Deficit Control Act. The provisions of this act, which would have expired after 1995, were extended through 1998 by the Omnibus Budget Reconciliation Act of 1993 (Public Law 103-66).
- ***Federal Credit Reform Act of 1990***, a part of the Budget Enforcement Act of 1990, which amended the Congressional Budget Act to prescribe the budget treatment for Federal credit programs.
- ***Antideficiency Act*** (codified in Chapters 13 and 15 of Title 31, United States Code), which prescribes rules and procedures for budget execution.

GLOSSARY OF BUDGET TERMS

Balances of budget authority—These are amounts of budget authority provided in previous years that have not been outlayed.

Obligated balances—These are amounts that have been obligated but not yet outlayed. Unobligated balances are amounts that have not been obligated and that remain available for obligation under law.

Baseline—A policy neutral set of estimates designed to show the effect on continuing current law through the period covered by the budget.

Breach—A breach is the amount by which new budget authority or outlays within a category of discretionary appropriations for a fiscal year is above the cap on new budget authority or outlays for that category for that year.

Budget—The Budget of the United States Government sets forth the President's comprehensive financial plan for allocating resources and indicates the President's priorities for the Federal Government.

Budget authority (BA)—Budget authority is the authority provided by Federal law to incur financial obligations that will result in outlays. Specific forms of budget authority include:

- provisions of law that make funds available for obligation and expenditure (other than borrowing authority), including the authority to obligate and expend offsetting receipts and collections;
- borrowing authority, which is authority granted to a Federal entity to borrow (e.g., through the issuance of promissory notes or monetary credits) and to obligate and expend the borrowed funds;
- contract authority, which is the making of funds available for obligation but not for expenditure; and
- offsetting receipts and collections as negative budget authority.

Budgetary resources—Budgetary resources comprise new budget authority, unobligated balances of budget authority, direct spending authority, and obligation limitations.

Budget totals—The budget includes totals for budget authority, outlays, and receipts. Some presentations in the budget distinguish on-budget totals from off-budget totals. On-budget totals reflect the transactions of all Federal Government entities except those excluded from the budget totals by law. Off-budget totals reflect the transactions of Government entities that are excluded from the on-budget totals by law. Currently excluded are the social security trust funds (Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds) and the Postal Service Fund. The on- and off-budget totals are combined to derive a total for Federal activity.

Cap—This is the term commonly used to refer to legal limits on the budget authority and outlays for each fiscal year provided in by discretionary appropriations. A sequester is required if an appropriation for a category causes a breach in the cap.

Credit program account—A credit program account receives an appropriation for the subsidy cost of a direct loan or loan guarantee program, disburses such cost to a financing account for the program.

Deficit—A deficit is the amount by which outlays exceed receipts.

Direct loan—A direct loan is a disbursement of funds by the Government to a non-Federal borrower under a contract that requires the repayment of such funds with or without interest. The term includes the purchase of, or participation in, a loan made by another lender. The term does not include the acquisition of a federally guaranteed loan in satisfaction of default claims or the price support loans of the Commodity Credit Corporation. (Cf. *loan guarantee.*)

Direct spending—Direct spending, sometimes called mandatory spending, is a category of outlays from budget authority provided in law other than appropriations acts, entitlement authority, and the budget authority for the food stamp program. (Cf. *discretionary appropriations.*)

Discretionary appropriations—Discretionary appropriations is a category of budget authority that comprises budgetary resources (except those provided to fund direct-spending programs) provided in appropriations acts. (Cf. *direct spending.*)

Emergency spending—Emergency spending is spending that the President and the Congress have designated as an emergency requirement. Such spending is not subject to the limits on discretionary spending, if it is discretionary spending, or the pay-as-you-go rules, if it is direct spending.

Entitlement authority—A provision of law that legally obligates the Federal government to make specified payments to any person or government that meets the eligibility requirements established by that law. Section 250(18) of the Balanced Budget and Emergency Deficit Control Act of 1985 specifies that the term includes, for the purposes of defining direct spending under the Act, a list of so-called mandatory appropriations in the joint explanatory statement of managers accompanying the Omnibus Reconciliation Act of 1990.

Federal funds—Federal funds are the moneys collected and spent by the Government other than those designated as trust funds. Federal funds include general, special, public enterprise, and intragovernmental funds. (Cf. *trust funds.*)

Financing account—A financing account receives the cost payments from a credit program account and includes other cash flows to and from the Government resulting from direct loan obligations or loan guarantee commitments made on or after October 1, 1991. At least one financing account is associated with each credit program account. For programs with direct and guaranteed loans, there are separate financing accounts for direct loans and guaranteed loans. The transactions of the financing accounts are not included in the budget totals. (Cf. *liquidating account.*)

Fiscal year—The fiscal year is the Government's accounting period. It begins on October 1st and ends on September 30th, and is designated by the calendar year in which it ends. Before 1976, the fiscal year began on July 1 and ended on June 30.

General fund—The general fund consists of accounts for receipts not earmarked by law for a specific purpose, the proceeds of general borrowing, and the expenditure of these [illegible]

Governmental receipts—These are collections from the public that result primarily from the exercise of the Government's sovereign or governmental powers. Governmental receipts consist mostly of individual and corporate income taxes and social insurance taxes, but also include excise taxes, compulsory user charges, customs duties, court fines, certain license fees, and deposits of earnings by the Federal Reserve System. Gifts and donations are also counted as governmental receipts. They are compared to outlays in calculating a surplus or deficit. (Cf. *offsetting collections.*)

Liquidating account—A liquidating account includes all cash flows to and from the Government resulting from direct loan obligations and loan guarantee commitments prior to October 1, 1991. (Cf. *financing account.*)

Loan guarantee—A loan guarantee is any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender. The term does not include the insurance of deposits, shares, or other withdrawable accounts in financial institutions. (Cf. *direct loan.*)

Mandatory spending—See *direct spending.*

Intragovernmental funds—Intragovernmental funds are accounts for business-type or market-oriented activities conducted primarily within and between Government agencies and financed by offsetting collections that are credited directly to the fund.

Obligations—Obligations are binding agreements that will result in outlays, immediately or in the future. Budgetary resources must be available before obligations can be incurred legally.

Off-budget—See *budget totals.*

Offsetting collections—Offsetting collections are collections from the public that result from business-type or market-oriented activities and collections from other Government accounts. These collections are deducted from gross disbursements in calculating outlays, rather than counted in Governmental receipt totals. Some offsetting collections are credited directly to appropriation or fund accounts; others, called offsetting receipts, are credited to receipt accounts. The authority to spend offsetting collections is a form of budget authority. (Cf. *governmental receipts.*)

Offsetting receipts—See *offsetting collections.*

On-budget—See *budget totals.*

Outlays—Outlays are the measure of Government spending. They are payments to liquidate obligations (other than the repayment of debt), net of refunds and offsetting collections. Outlays generally are recorded on a cash basis, but also include cash-equivalent transactions, the subsidy cost of direct loans [illegible] antees, and interest accrued on public issues of Treasury debt.

Pay-as-you-go (PAYGO)—This term refers to requirements in law that result in a sequester if the estimated combined result of legislation affecting direct spending or receipts is an increase in the deficit for a fiscal year.

Public enterprise funds—Public enterprise funds are revolving accounts for business or market-oriented activities conducted primarily with the public and financed by offsetting collections that are credited directly to the fund.

Receipts—See *governmental receipts and offsetting collections.*

Sequester—A sequester is the cancellation of budgetary resources provided by discretionary appropriations or direct spending legislation, following various procedures prescribed in law. A sequester may occur in response to a discretionary appropriation that causes a breach or in response to increases in the deficit resulting from the combined result of legislation affecting direct spending or receipts (referred to as a "pay-as-you-go" sequester).

Special funds—Special funds are Federal fund accounts for receipts earmarked for specific purposes and the associated expenditure of those receipts. (Cf. *trust funds.*)

Subsidy—This term means the same as cost when it is used in connection with Federal credit programs.

Surplus—A surplus is the amount by which receipts exceed outlays.

Supplemental appropriation—A supplemental appropriation is one enacted subsequent to a regular a nual appropriations act when the need for funds is too urgent to be postponed until the next regular annual appropriations act.

Trust funds—Trust funds are accounts, designated by law as trust funds, for receipts earmarked for specific purposes and the associated expenditure of those receipts. (Cf. *special funds.*)

CIVIL SOCIETY AND THE BUDGET PROCESS

THE OVERSIGHT FUNCTION OF CIVIL SOCIETY ON THE BUDGET

1. WHY OVERSIGHT?

The budget process is important to all people in Malawi by virtue of the simple fact that it is the only way that citizens can identify how government proposes to spend money collected from them. Observing the budget process ensures that people get their money's worth in the form of good roads, hospitals, schools, employment, housing, food, etc.

2. WHO OVERSEES?

It would therefore be negligent of society to take absolutely no interest in how their funds are used. However, not all citizens have the same comprehension of the process. In most cases, interest groups (such as NGOs involved in advocacy) take the lead in overseeing the process. These groups are in a good position to do so because:

a) They have a detailed understanding of the process;
b) They are composed of individuals whose main purpose is to protect the interest of the community;
c) They have access to relevant information;
d) They are in contact both with the decision makers and the rest of society;
e) They are capable of informing and influencing society to take actions that will keep decision makers in check; and
f) They are recognized by decision makers as "watchdogs."

3. HOW TO OVERSEE

Civil Society can ensure that the national budget process is transparent and that the executive is held accountable to the electorate by:

I) Raising an individual awareness of the content of the budget.
ii) Lobbying for change at specific points in the process.
iii) Facilitating dialogue between elected leaders and the electorate on the budget.

4. DECISION MAKERS' ATTITUDE

There is need for civil society to ensure that decision makers are aware that their final responsibility is to their constituents. Therefore they should not view queries on the budget with suspicion but should welcome these queries. Decision makers in fact need to obtain as much input from constituents as possible so that:

I) the budget reflects the real needs of the people; and
ii) transparency and accountability are maintained.

Who Answers to Whom?
Public Accountability on the Budget Process

by Mr. James Cairns

I. Look at the Budget as a Moral Document

- Move away from numbers and think about people
- Tries to quantify the values, priorities and needs of the government
- Allocating resources in a way that hopefully reflects the needs of the people (Public interest - who defines it? Is the system closed, creating isolated decision making?)

II. Accountability in Managing Resources

- A concept that is not new - present in any social/political system
- Democracy approaches the issue in a particular way - the relationship between citizens and leaders, elected representatives, etc. But in many different forms
- Historical context in Malawi works against these ideas - first the British and then under Dr. Banda, accountability was to the executive, not the people. So Parliament was under the executive and answered to it, not to the people.
- Not much experience either on the part of leaders or people of what it means to have a government that answers to the people. It will take time before the people can really demand it, puts bigger challenge on MPs/Government to consciously seek accountable practices
- As members here, you are accountable in several different ways, which might conflict with each other:

a. As members of this Committee to the Assembly as a whole

b. As MP to citizens in your constituency

c. As a member of a party to that of the party interests

d. As Parliament to the duties given to it by the Constitution

(Now, we can see how these might conflict at different times.)

- Which one of these should take priority? As elected representative of the people you and your fellow MPs should strive to represent their interests first.
- This is necessary if the system laid out in the Malawi Constitution is to succeed. Parliament is the peoples' assembly - it is where, through their representatives, their voice/needs/interests can be heard.
- In a country like Malawi, however, where the people have a difficult time/making their needs known, the temptation is to be more accountable to one's party than to constituents. This is not to say that parties are not important.
- Budgets are complicated things, so the people rely on your as MPs to analyze, question and interpret the budget on their behalf. (Although the budget itself is complicated, people can see for themselves whether the government actually does what it says it will do in its budget.)

III. Role of Public/Civil Society in Budget Process

- The people, through the organization - NGOs, clubs, religious institutions, etc. - need to become part of the conversation about how government will spend their money. This means government - both executive and legislative need to make an effort to communicate with people -

this means the process will take more time, and that there needs to be more openness in the process

- What do the people what or need in order to be involved?

a. Respect

b. Information

c. Transparency

d. Consultation/access

- Government should not see civil society as an adversary to any branch, but should realize that it has its own interests. Its role in democracy is to both cooperate with government to fulfill its duties and to challenge/remind government what those duties are when they are not being fulfilled.

- The Budget and Finance Committee, as the one primarily responsible for matters of revenue and expenses, needs to take the lead in making sure the voice of the public is heard and taken into account during the budget process.

a. Not just meetings in constituencies, but carefully reading of newspapers, consulting with people other than economists, etc.

b. As your terms of reference indicate, you have the mandate to encourage public awareness and debate on the budget and economic policies of government.

- What do you require to fulfill this mandate?

a. Information

b. Expertise

c. Resources

d. Commitment

- During the financial year, it is perhaps equally important for the Budget and Finance Committee (and others) to actively review how the budget is agreed to by the government. Does the money actually get spent on what it was intended for?

IV. Conclusion

- Come back to the issue of "trickle-down" as it is raised as part of the budget process to realize that budgets are not about numbers, but about the impact that they have on the people. In their conclusion they affect reality.

- Government is entrusted with power and resources to perform certain tasks for the benefit of the people.

SETTING PRIORITIES

SETTING PRIORITIES

The National Budget
Vol. I No. I
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CAREFUL PLANNING IS THE KEY TO SUCCESS

Determining What Is Important

Implicit in any fiscal exercise is not only the determination of how much money is available to spend but also the decision about what criteria will be used to determine who gets what portion of the total pot. In some instances, the criteria is already established by virtue of the need to resolve a crisis situation. In other instances, the criteria may be established by an external /internal force which has imposed funding limits (i.e. money cannot be used to pay salaries or cannot be used to cover entertainment expenses but can be used to buy supplies and equipment in order to support certain program activities). What ever the case, it is crucial that some serious thought and discussion be given to why it makes sense to allocate funds to certain expenses/projects/line items.

With careful planning and a clear set of priorities a more prudent use of scarce funds can be obtained which may also contribute to a more effective implementation of the program.

Hard Choices

There are two main components in a budget; the financial segment and the program segment; and it is not always clear which segment drives the other segment. Below is a very simple example of how a legitimate need can be directly or indirectly determined by other factors within the budget process.

A group of concerned citizens in a rural community decide that they want a hospital in their area because the nearest health care facility is 150 kilometres away. There is very little transport in the area and many people have died because they could not find basic medicines.

The group decides that the government must do something to address this very serious problem. Hence, they channel their request for assistance through the appropriate people and are eventually notified that the Ministry of Health has agreed that the request for the hospital is reasonable and should be funded.

The Ministry has reached its decision to build this hospital based on two assumptions: (1) they see that there is a genuine need for this particular community and (2) one of the ministry's long-term objectives is to provide adequate medical facilities to all citizens by the year 2004.

However, there is a problem. The revenue from customs and excise taxes and personal income taxes have been steadily declining; and the revenue forecast for the next year is not very promising. Apparently, foreign businesses are leaving the country at an alarming rate because of the great difficulties they are finding in transporting their goods. The government has decided that it must do something to stop this mass exodus and if possible entice some of the old investors back to the country. Therefore, one of the government's proposals is to build a new road that would run through this village but it would mean no hospital for at least two years.

Thus, while the community does not necessarily get what it wants there is a comprise in that the government is able to find away to secure revenue necessary to maintain many programs of national interest and the community members may be able to open businesses to service the drivers of the trucks who will now be passing through their community and they also may find that the increase in traffic will make it easier for them to travel to the nearest health care facility and to have more medicine sent directly to them.

CONTENTS

Five Key Ways to Spend Smartly

1. Identify long - short term goals.
2. Organize planning meetings.
3. Determine what activities would benefit the greater number of people.
4. Remember that scarce resources should be used wisely.
5. Treat the money of others as if it were your own.

BUDGET AND FINANCE COMMITTEE

Who is the Budget and Finance Committee and what do they do.

The current membership of the Budget & Finance Committee is:

Mr. G.E. Zulu (Chairman, Aford)
Mr. A.K.M. Pillane (UDF, Minister of Works and Supplies)
Mr. H.R. Kamwana (UDF)
Mr. A.A. Mbaya (UDF)
Mr. Mauwa (UDF)
Mr. T.J.M. Mnesa (UDF)
Mr. R.J. Makuwila. (UDF, Minister of Education)
Mr. L.J. Chimango (MCP)
Miss C.T. Kainja (MCP)
Mr. P. Chibwana (MCP)
Mr. M.N. Ndhlovu (Aford)
Mr. E.W. Musyani (Aford)

These individuals are chose by the leadership of their respective parties and the Committee chair is usually a member of one of the opposition parties within Parliament.

The Terms of reference for the Budget and Finance Committee of the Malawi National Assembly provides for several mandates:

I. to familiarise itself with the budget, published reports and economic issues, statistical information, international agreements, financial reports and reports on economic and policy statements;
II. to sharpen public awareness on the budget and Government financial and economic policies and therefore encourage informed debate on the budget;
III. to advise Parliament on Government's local and international borrowing policies;
IV. to study Government taxation policies and advise accordingly;
V. to examine estimates of expenditure;
VI. to seek advise from the Minister of Finance and officials on finance and other matters; and
VII. to report its findings to the National Assembly.

The committee is also empowered to examine the expense estimates and seek the advice from the Minister of Finance and others on these and other matters. They are then to make reports of their findings to the National Assembly.

Budget and Finance Committee, just like many other Parliamentary Committees, have not been meeting as regularly as expected due to financial limitations. I believe that Members of this Committee are in a better position to understand this state of affairs than any other Committees since you are, no doubt, aware of the economic plight the country has been going through during the past three years.

10. As a result, the Committee has not been able to offer its advice to the Minister of Finance on economic and financial issues on a regular basis. The only exception being last year when Members met the Minister just before the Budget to brief him on what they felt were priority areas to be considered in the budget. I am advised that most of the concerns were indeed taken into account by the Minister.

11. An equally important issue is the fact that Members of this Committee have not been taking a leading role during the budget debate. One would have thought that Members of this Committee should be in the forefront in explaining the budget document to other Members so that they too can contribute significantly to the debate.

12. Perhaps this is probably because Members of this Committee require a lot of information and training in order for them to understand economic issues better. This is the reason why seminars of this type are very crucial if Members are to perform their tasks more effectively.

(E) Some issues to be covered by this seminar

13. Honourable Members, Resource Persons, I am advised that the Seminar will cover the following areas:-

    (a) Economic trends, past, current and future;

    (b) The mid-term expenditure framework;

    (c) An overview of the Budget process;

    (d) An overview of how to read the Budget; and

    (e) Methodology for setting priorities.

14. I am pleased that this seminar has drawn Resources Persons from a wide range of organizations which play a vital role in our economy. I am sure Members will benefit enormously from the knowledge of very experienced and renowned individuals in our society. It is my hope that issues about the economy and government finances (which are little understood) will be demystified by our resource persons during the two days of our deliberations. As legislators, we are supposed to be as knowledgeable as possible so that we are able to make informed decisions and to pass appropriate laws in the National Assembly.

BUDGET WORKSHOP INTRODUCTION AND SPEECHES

WORKSHOP ON THE GOVERNMENT BUDGET
FOR THE BUDGET AND FINANCE COMMITTEE

A. The budget and Finance Committee Workshop was sponsored by the National Democratic Institute (NDI). It was held at Capital Hotel from Friday, 28February, 1997 to Saturday, 1 March, 1997. The Speaker of the National Assembly gave opening remarks. In his remarks, the Speaker noted that the financial initiative still remains with the Government under our Constitution and a Committee like the Budget and Finance Committee with the expertise made available to it at the seminar, may assist the House in understanding the government Budget and wether the budget has set the necessary priorities for the nation.

B. Presentations were made on the following subjects:

1. Economics of the Government Budget by Mr. Bruce Bolnick, Malawi Economic Management and Reform Project;

2. Cash shortfalls and Government reactions by Bruce Bolnick;

3. An Overview of the Budget Process by Mr. Chikhosi, Director of Budget, Ministry of Finance and Professor Max Thondolo, Economics Department, Chancellor College;

4. Economic trends, past, current and future by Mr. Matthews Chikaonda, Governor, Reserve Bank of Malawi;

5. Presentation of the Budget Handbook Draft by Mr. Bradley Austin;

6. Numbers: An overview of how to read the Budget by Mr. Waki Mushani, Deloitte and Touche;

7. Medium Term Expenditure Framework by Ms. Elizabeth Muggeridge, Ministry of Finance / World Bank and Mr. Felix Kaluma;

8. Who Answers to Whom by Mr. James Cairns, PAC

SPEECH FOR THE CHAIRMAN OF THE BUDGET AND FINANCE COMMITTEE

Honourable Speaker; The Representative of NDI; The governor of the Reserve Bank of Malawi; Ms Margaret Mudgridge from the World Bank; Mr Gerard Grant from SHARED Project, Mr Brice Bolnick from the Malawi Economic Management and Reform Project; Mr James Cairns from Public Affairs Committee; The Secretary for Commerce and Industry; The Director of the Budget in the Ministry of Finance; The Clerk of Parliament; Honourable Members of Parliament; Ladies and Gentlemen, there is a saying in English which goes: "The darkest hour is at dawn".

I, as Chairman of this Committee had been looking forward to an opportunity during which Members of my Committee and I would meet the Governor of the Reserve Bank of Malawi, representatives of the donor community and government officials in order to enhance our knowledge about economic and financial matters. I do recall, for example, that during our last meeting at Lilongwe Hotel in November, last year, I had requested the clerk of Parliament to arrange briefings for the Committee by the Reserve Bank, the donor community and other major players in our economy.

As time went by, I began to lose hope. Little did I know that something in that direction was already in the offing.

I am therefore unable to find the right words with which to thank the National Democratic Institute for taking the initiative in organizing such an important workshop for the Committee.

Mr Speaker, Sir, distinguished persons, Honourable Members, I wish to point out at the outset that economic and financial affairs are not well understood by people outside those fields. Concepts such as inflation, interest rates and the exchange rates quite often make very little sense to a lot of us. The upshot of this is that discussions on such topics are the preserve of the few who are thought to be knowledgeable.

Unsurprisingly, the budget debate in Parliament has not been spared this situation. Indeed, there have been very few Members who have analyzed the budget document in terms of the effects of various government policies in the economy. More often than not, the budget debate has turned into a forum whereby Members try to draw government's attention to problems in their constituencies. I believe Mr Speaker, Sir, resource persons, that is a very short sighted view of the budget. We as Members need to look at the budget from a wider perspective, a national perspective, if we are to assist government to arrive at proper decisions and thereby contribute towards the improvement of our economy.

I am therefore, delighted that NDI has decided to sponsor this very important workshop for the Committee. I am very hopeful that members will benefit enormously from the presentations and discussions during the workshop.

May I urge Members to participate actively in the debates. I also wish to remind my colleagues that the first step in the learning process is the need for one to accept that one does not know everything. Then you will be surprised at the amount of knowledge that you will acquire.

Education is an enemy of people who pretend to know everything.

May I end my very short speech by thanking NDI for sponsoring the workshop, the Speaker of the National Assembly for accepting to open it, and to all resource persons for sparing your time to come and share your knowledge with us.

I hope that this is only the beginning of training opportunities for Members of the Budget and Finance Committee.

Thank you, very much.

THE SPEAKER'S OPENING SPEECH

The Chairman of the Budget and Finance Committee; The Representative of NDI; The Governor of the Reserve Bank of Malawi; Ms. Margaret Mudgridge, from the World Bank; Mr Gerard Grant from SHARED Project; Mr Bruce Bolnick from the Malawi Economic Management and Reform Project; Mr James Cairns from Public Affairs Committee; The Director of the Budget in the Ministry of Finance; The Secretary for Commerce and Industry; Clerk of Parliament; Honourable Members of Parliament; Ladies and Gentlemen.

(A) Introduction

1. It gives me great pleasure, to be here this morning to say a few words to the Budget and Finance Committee before it starts seminar.

2. Parliament work as Committees of all its Members or through its appointed Committees as mini legislatures. The only difference is that Committee work largely excludes partisanship where it is frequently far more subdued; instead cooperation and common purpose between political adversaries is by no means unusual when working together in a Committee.

3. As Crick has stated: *"Any complex matter put before any large association of men is commonly dealt with in four ways: by appointing a small committee; by giving that committee as precise a definition of its functions as possible; by giving the committee as much time as possible; and by including among the committee technical experts or giving it access to such experts".*

4. The financial initiative still remains with the Government under our Constitution and a Committee like the Budget and Finance Committee with the expertise made available to it at this seminar, may assist the House in understanding the government Budget and whether the budget has set the necessary priorities for the nation.

5. Honourable Members, Resources Persons and distinguished delegates, the Budget and Finance Committee is one of the most crucial Parliamentary Committees as most of you will, no doubt agree.

6. For any organization to operate effectively, it must have funds and normally organizations will seek the views of outside bodies such as accounting firms to advise them on how best to prepare budgets which reflect certain realities.

(B) Terms of Reference for the Budget and Finance Committee

7. In Malawi, besides whatever advice is sought from outside bodies such as the World Bank and the IMF, there is a Budget and Finance Committee whose mandate is to:-

(a) familiarize itself with the budget, published reports and economic issues, statistical information, international agreements, financial reports and reports on economic and policy statements;

(b) sharpen public awareness on the budget and Government financial and economic policies and therefore encourage informed debate on the budget;

(c) advise Parliament on Government's local and international borrowing policies;

(d) study Government taxation policies and advise accordingly;

(e) examine estimates of expenditure;

(f) seek advice from the Minister of Finance and officials on finance and other matters; and

(g) report its findings to the National Assembly.

(C) How the Committee Operates

In order to perform its duties effectively, the Committee is supposed to meet regularly with the Minister of Finance, officials from the Ministry of Finance, Economic Planning and Development and the Reserve Bank of Malawi, to mention just a few, with a view to familiarizing itself with the country's current economic and financial situation. Members need to know for instance, the present rate of inflation, the relationship between inflation and interest rates, micro and macro-economic variables, the meaning of a budget deficit and how it is financed, local and international borrowing and their effects on the economy, sources and uses of finance and effects of wage increases, etc. When debating the budget, Members need to anticipate the effects of various Government policies, e.g. taxation, on the overall economy and therefore advise government accordingly.

8. Members who are not familiar with these concepts cannot offer appropriate advice to Government.

(D) Some of the Difficulties the Committee has encountered so far

9. Honourable Members, Resource Persons, I regret to inform this gathering, that the

Budget and Finance Committee, just like many other Parliamentary Committees, have not been meeting as regularly as expected due to financial limitations. I believe that Members of this Committee are in a better position to understand this state of affairs than any other Committees since you are, no doubt, aware of the economic plight the country has been going through during the past three years.

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(a) Economic trends, past, current and future;

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15. As a teacher by background myself, I believe that education is a continuing process and that knowledge should trickle down to as many people as possible. This is exactly what prompted me to invite some Members of Parliament who will attend this seminar in an observer capacity so that this crucial training should not be confined to Members of the Budget and Finance Committee.

16. This gathering will probably have heard about the training for Members of Parliament which has been going on at Chancellor College since last year,which is an attempt at improving the knowledge and skills of our Members. One of the subjects being covered in that course is *the economy* and I am glad to report that two Members from this Committee namely, Honourable M.N. Ndhlovu and Honourable A.A. Mbaya are attending that course.

17. Anyway, that is a broader course. We however require special seminars for Committees such as the one being opened today.

18. I do recall that last year the NDI did bring Mr Cohen, the Chairman of a similar Committee in the Gauteng Legislature in South Africa who held discussions with our Members. Now, this is something more comprehensive as it involves the Reserve Bank, the World Bank, Government Ministries and other important organizations.

19. I am sure this is a rare opportunity for our Members to enrich their knowledge of economic and financial issues. I therefore urge Members to listen carefully to the various presentations and to ask as many pertinent questions as possible. Mind you, the Budget Debate is just around the corner and I am relying on you all to contribute significantly so that our Budget for the 1997/98 financial year should be the best ever.

(G) <u>Conclusion</u>

20. Finally, I wish to thank the National Democratic Institute (NDI) for sponsoring the workshop. May I request the NDI to supporting the Committee in various ways, including visits to neighboring countries so that Members can appreciate how similar Committees operate elsewhere.

21. May I also express my most sincere gratitude to all Resource Persons for accepting to come, despite your tight schedules.

Thank you, very much.

BUDGET WORKSHOP HANDOUTS

ECONOMICS OF A GOVERNMENT BUDGET

PRESENTATION

BY

BRUCE BOLNICK
MALAWI ECONOMIC MANAGEMENT
AND REFORM PROJECT

ECONOMICS OF THE GOVERNMENT BUDGET: SETTING PRIORITIES

1. **Government budget and the allocation of resources: To what? For whom? At whose expense?**

    a. Size of government
    b. Structure of expenditures
    c. Tax structure
    d. Financing

2. **Size of government: First-order decision on priorities**

    a. Fundamental *political* decision
    b. "Requirements" virtually unlimited
    c. But: the budget constraint
    d. Range of observed choices
    e. Case of Malawi

3. **Composition of government expenditures: Mediating competing claims**

    a. Recurrent account vs. Development account
    b. By functional classification: agriculture, education, health, roads...
    c. By economic classification

4. ***Economic* considerations in prioritizing expenditures**

    a. Opportunity cost !
    b. Consistency with national goals
    c. *Essential functions of government*
    d. Quantity/quality trade-off
    e. Public vs private interest
    f. Donor resources & matching funds
    g. Program & project appraisal criteria
        i. Cost-effectiveness
        ii. Rate of return; diminishing returns
        iii. Income distribution effects
        iv. By-product effects
    h. MTEF

5. **Estimates vs. Out-turns: the *other* problem of priorities**

6. **Conclusion**

    a. Politics versus economics
    b. The role of the National Assembly

Table 1. Comparative Fiscal Statistics, Selected Countries Early 1990s (%)

Country	CentralGvt Exp/GNP	EducExp/ TotExp	DevExp/ GNP	GvtSaving/ GNP
Indonesia	18.9	10.0	8.1	9.8
Korea	17.1	16.8	2.9	4.1
Malaysia	26.7	20.3	5.0	7.7
Pakistan	24.0	1.1	3.6	-1.8
Singapore	19.7	22.3	4.2	11.4
Thailand	16.3	21.1	3.9	6.7
Bolivia	26.6	11.0	5.6	3.0
Chile	22.6	13.4	3.4	5.0
Colombia	18.9	2.9	2.6	5.0
Peru	14.0	na	2.9	2.2
Botswana	40.2	20.4	7.4	24.4
Ghana	21.0	22.0	3.1	0.8
Kenya	28.9	18.8	6.1	-0.4
Malawi	26.7	2.5	9.6	-4.1
South Africa	32.6	na	1.6	-1.8
Zambia	21.0	2.9	7.1	-2.9
France	45.5	7.0	2.5	-1.7
Sweden	53.9	7.3	0.7	-11.8
UK	43.4	3.3	2.8	-3.4

Sources: World Bank, World Development Report, 1995 and 1996; World Bank World Tables, 1995; UNDP, Human Development Report, 1995, and Government of Malawi statistics.

ECONOMICS OF THE GOVERNMENT BUDGET: WHY "THERE'S NO MORE MONEY"

1. Living within one's means

a. What's different about GOVERNMENT ?
b. The government budget constraint:

Total Expenditure = Revenue (incl. Grants)
+ Net domestic credit + Net foreign financing

2. The adverse consequences of "excessive" government deficits

a. Borrowing from the central bank = printing money
b. Other domestic borrowing
c. Foreign financing
d. Effect on saving, investment, and growth
e. Effect on balance of payments and the exchange rate
f. Effect on poverty alleviation

3. What is "excessive"?

a. Range of experience
b. Factors determining the prudent, sustainable deficit
c. Lessons from Asia
d. The case of Malawi

4. Role of the IMF

a. Certifying effective performance
b. Monetary programming
c. If the IMF shut down tomorrow ... !

5. Conclusion

a. Prudent fiscal management is fundamental to achieving equitable, and sustainable growth and poverty alleviation
b. The advantage of a simple fiscal rule
c. Implications for the budget process

Table 2. Malawi Fiscal Statistics
1980-1996

Year	GovtExp/ GDP	DevExp/ GDP	GvtSaving/ GDP incl grants	GvtSaving/ GDP excl grants
1980	30.8	13.3	5.5	0.3
1981	33.4	13.8	3.6	-2.7
1982	26.0	9.3	3.9	0.1
1983	29.4	9.0	0.2	-3.0
1984	27.5	8.1	0.1	-2.7
1985	27.8	8.3	2.3	-0.9
1986	26.9	6.1	1.7	-2.9
1987	30.9	7.2	-1.1	-5.5
1988	20.8	5.0	7.0	2.5
1989	25.5	5.8	1.6	-0.9
1990	21.8	2.6	-0.5	-1.3
1991	25.3	6.8	1.7	-2.2
1992	23.3	3.5	-1.9	-2.6
1993	17.6	2.9	-0.5	-0.8
1994	16.2	1.7	2.2	1.0
1995	31.2	6.5	0.8	-7.1
1996	25.2	4.9	1.4	-3.2

Note: Revenue figures shown here include grants.
Source: RBM and Government tables.

Table 3. Comparative Macroeconomic Statistics, Selected Countries c. 1994

Country	Gvt Surplus or Deficit % GDP	Avg GDP growth (%) 1980-1994	Domestic Saving % GDP	Broad Money % GDP	Govt Saving % GDP
Indonesia	0.7	6.5	30.0	46.0	8.9
Korea	0.6	8.6	39.0	40.6	4.9
Malaysia	1.7	6.1	37.0	83.9	8.9
Pakistan	(7.4)	5.8	17.0	42.3	(2.1)
Singapore	12.6	6.9	51.0	83.6	13.7
Thailand	2.1	7.8	35.0	74.2	6.6
Bolivia	(2.1)	na	8.0	45.1	(2.7)
Chile	2.1	5.1	28.0	34.9	4.9
Colombia	(0.6)	3.9	15.0	19.8	2.9
Peru	(1.8)	1.0	20.0	15.3	2.2
Botswana	11.2	8.6	25.0	26.4	23.3
Ghana	(2.5)	3.4	4.0	15.8	(0.9)
Kenya	(3.8)	3.2	24.0	32.2	(0.4)
Malawi	(5.7)	1.7	(1.0)	20.5	1.0
South Africa	(4.4)	0.9	20.0	50.4	(7.7)
Zambia	(7.3)	0.5	4.0	10.8	(2.9)
France	(3.8)	1.9	20.0	61.4	(4.2)
Sweden	(12.2)	1.3	17.0	47.5	(11.7)
UK	(5.1)	2.5	14.0	97.0	(4.9)

Source: World Bank. World Development Reports. 1995 and 1996.

OVERVIEW OF THE ECONOMIC CLIMATE IN MALAWI

RECENT PERFORMANCE AND PROSPECTS

RESERVE BANK OF MALAWI

OVERVIEW OF THE ECONOMIC CLIMATE IN MALAWI:

RECENT PERFORMANCE AND PROSPECTS

I. Introduction

Since the late eighties, Malawi has been implementing a broad-based structural adjustment programme supported by the International Monetary Fund, the World Bank and other donors. The economic performance was particularly good during 1988-91. A deterioration ensued during 1992-94 on account of two major droughts and a sharp reduction in donor aid. However, the economic situation has dramatically improved since 1995. Indeed during 1995-96, real GDP growth was about 10 percent per annum. Inflation has declined from 75 percent in 1995 (December to December) to about 7 percent at end 1996. The external position has markedly improved with gross international reserves averaging over 5.7 months of import cover during 1996. The Malawi kwacha has remained stable at about 15.3 to the US dollar since late 1995. The government deficit (excluding grants) was reduced from 27.8 percent of GDP in 1994/95 to 13.6 percent in 1995/96.

The main contributing factors to these developments were the following. On the policy front, first the authorities markedly tightened fiscal and monetary policies with the introduction of a cash budget system and the intensification of open market operations. Second the agricultural sector has been significantly liberalised. As of now there is virtually no restriction in the production and marketing of any agricultural produce. Third, public enterprises have been restructured with a large number intended for privatisation. Indeed there are over 25 parastatals that the Privatisation Commission has prepared for privatisation. Fourth, the government is implementing a civil service reform aimed at increasing efficiency by having more sustainable numbers of civil servants. Finally the wide-ranging foreign exchange liberalisation has led to increased economic activity especially in the small and medium scale industries. As of now, the foreign exchange constraint is no longer a binding problem for manufacturers.

Other favourable factors have also contributed to the good economic performance. First, the rains have been good the past two years and this has led to large harvests being realised, especially for the smallholders. Second, the introduction of multi-party democracy in Malawi has led to increased donor support in many economic sectors, especially in the social sector.

II. Recent Economic Developments

- **Inflation**

One of the most remarkable successes of government economic policies has been the fight against inflation, especially in 1996. The annualised inflation rate dropped to 6.7 percent in December. This is in sharp contrast to the peak level of almost 100 percent recorded in July 1995. The annual average rate of inflation for the year 1996 dropped to 37.6 percent, markedly lower when compared to 83.3 percent for 1995.

Table 1:

Inflation as Measured by the Changs National Consumer Price Index

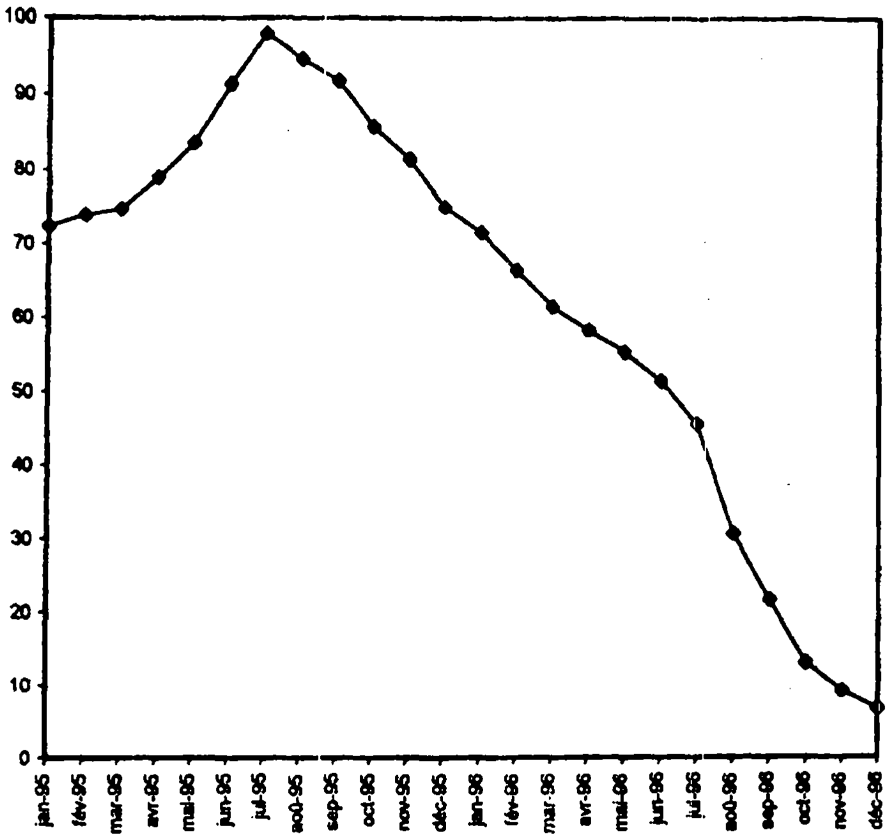
(1995-1996)

Month	1995		1996	
	Monthly Annualised	Month-on-month	Monthly Annualised	Month-on-month
January	72.4	8.0	71.4	5.8
February	73.9	5.2	66.3	2.1
March	74.7	3.8	61.2	0.6
April	79.1	3.4	58.1	1.4
May	83.7	2.8	55.1	0.8
June	91.5	2.4	51.1	-0.2
July	98.1	3.3	45.3	-0.6
August	94.7	1.5	30.5	-8.8
September	91.8	6.2	21.5	-1.1
October	85.8	7.5	13.0	0.0
November	81.4	7.5	9.2	3.9
December	74.9	5.8	6.7	3.3

Source: National Statistical Office.

It is remarkable to note that currently the main source of inflation is related to rising food costs as a result of seasonal shortages. Due to the still tight monetary stance and ready availability of non agricultural commodities (especially imported ones), there has been relatively less pressure for prices to increase particularly from the demand side.

Chart 1: Monthly Annualised inflation rate



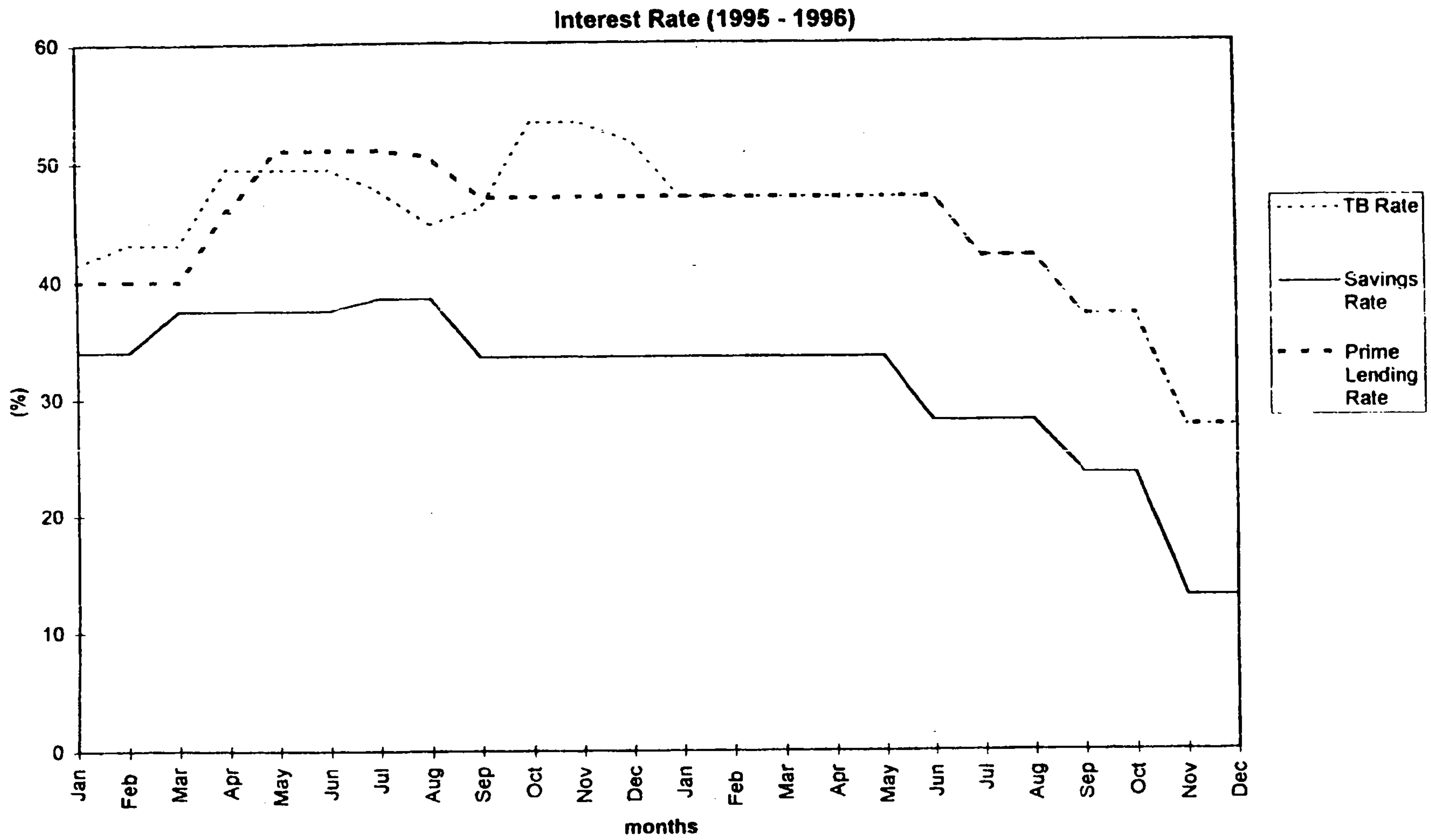
• **Interest Rates**

With the sharp drop in inflation, there has been a corresponding decline in interest rates. Within 1996, the Reserve Bank of Malawi has been able to reduce the discount rate from 50 percent in January to 27 percent in November. This move has led to significant drops in the prime lending rate of the commercial banks from 47 to 26 percent during the same period. The prime lending rate has moved further down to 23.0 percent since January , 1997 and expectations are for the rates to continue falling with inflation stabilising at a single digit level The low rates of inflation and the lending rates should improve investor confidence and growth prospects for the economy.

Table 2: Developments in Interest Rates

	1995	1996											
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Prime lending rate	47.00	47.00	47.00	47.00	47.00	47.00	47.00	42.00	42.00	37.00	37.00	27.50	27.50
Savings	33.50	33.50	33.50	33.50	33.50	33.50	28.00	28.00	28.00	23.50	23.50	13.00	13.00
TB Yield													
91 days	51.71	51.20	49.68	48.29	46.99	37.49	23.91	23.49	22.37	18.33	15.30	14.06	14.69
182 days	66.78	61.58	58.04	56.32	53.58	42.28	26.48	21.99	22.73	18.35	16.40	15.42	16.02
271 days	74.82	67.34	59.56	56.30	55.20	45.85	27.53	22.37	21.61	17.52	15.90	15.24	16.57

CHART 2



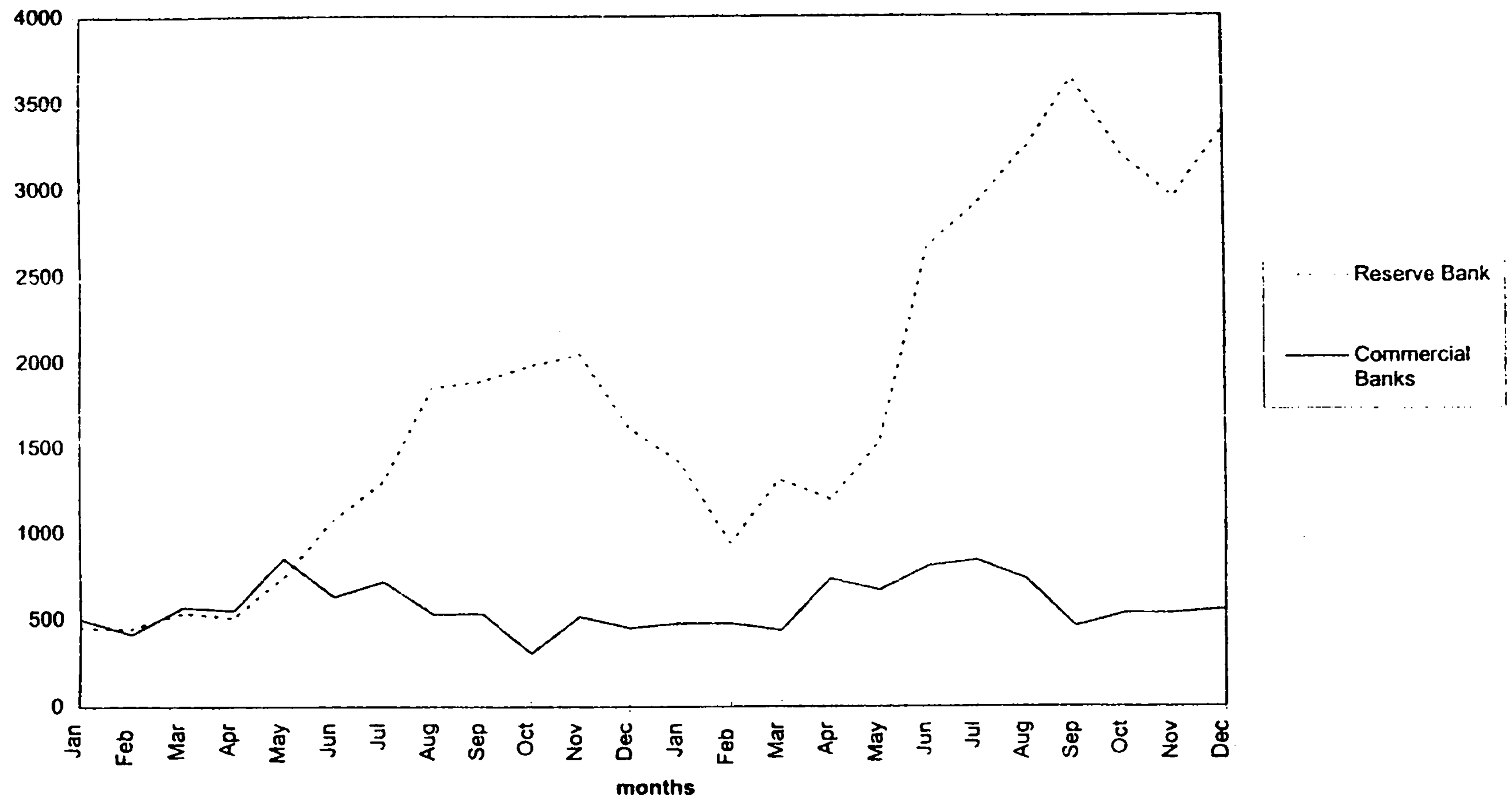
Interest Rate (1995 - 1996)
60
50
40
30
20
10
0
(%)
Jan
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec
Jan
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec
months
TB Rate
Savings Rate
Prime Lending Rate

- **Foreign Reserves Position**

The overall foreign reserves position has remained buoyant in 1996 peaking at over K3.6 billion (or close to US$240 million) in September. This happened on account of good export performance and substantial balance of payments support especially from the World Bank under the Fiscal Restructuring and Deregulation Project, and from other bilateral donors. As result, import cover averaged 5.7 months during the year, a level never attained throughout the 1980s.

CHART 3

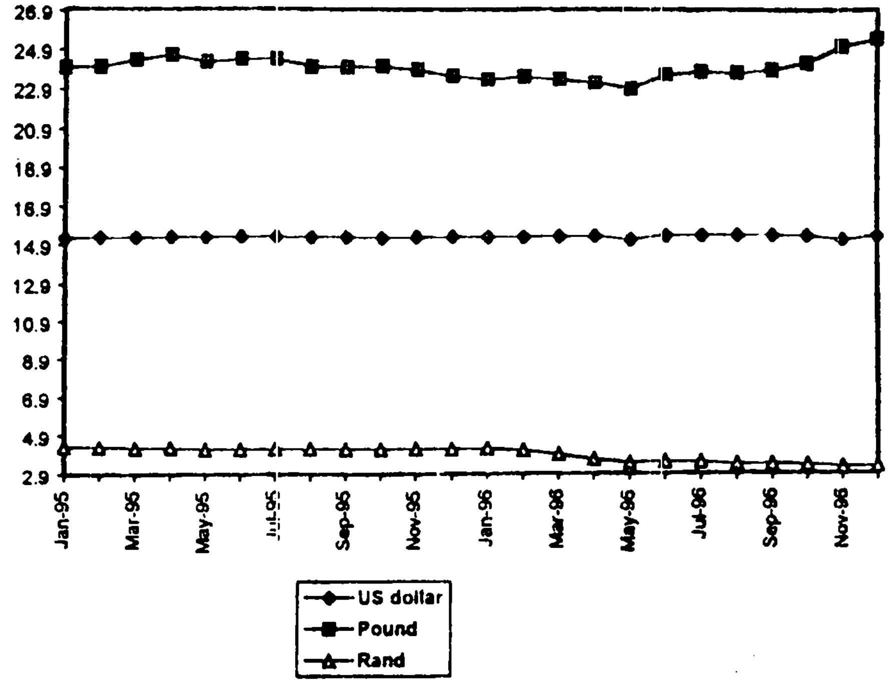
Foreign Reserves (1995 -1996)
(K Million)



•Exchange Rate Developments

The Malawi Kwacha exchange rate vis-à-vis other selected foreign currencies stabilised somewhat during the month of December and the year as a whole. Most notable was the stability of the Malawi Kwacha against the US dollar at about K15.3 per one US dollar. However, the kwacha strengthened against the South African rand, German mark and the Japanese yen. Prospects for continued stability in the kwacha exchange rate still look good because of the much improved foreign exchange position.

Chart 4: Malawi kwacha exchange rate



III. Current Economic Challenges

• Government Budget

The main reason for the good financial performance during 1996 was government's steadfast efforts to establish financial stability through the implementation of the cash budget system. Although the principle of the cash budget is incontestable --one has to live according to one's means -- its practical implementation has been quite problematic. Top on the list of problems has been budget cuts without due regard to expenditure priorities. As a result the quality of some expenditures has often left a lot to be desired, leading to a noticeable deterioration in the social sector. The Medium Term Expenditure Framework (MTEF), supported by the World Bank, should go some way in helping the government to getting expenditure priorities right by rationalising the budgeting process. It should therefore be stated that fiscal adjustment is far from complete. Some extra-budgetary expenditures continue to be made. Great challenges lay ahead especially in meeting the government's policy of poverty alleviation.

• External Debt

Although according to the World Bank, Malawi is not a debt-distressed nation, the overall level of debt is still worrisome. External debt service over the past five years has hovered at over 20 percent (the low figure of 1994 reflects some arrears) of total export earnings. More importantly, over eighty percent of Malawi's debt is not reschedulable or forgivable because it is owed to multilateral creditors.

• **New Sources of Growth**

Despite the laudable efforts in economic liberalisation and the ready availability of foreign exchange, it is noteworthy that there has been relatively slow progress in finding new sources of long term, sustainable growth. Agriculture, which is the mainstay of the economy, remains hostage to weather conditions. The government needs to intensify its efforts on the formulation of a drought management strategy which can lead to new drought resistant crops being grown. Land policy reforms will also be important in raising agricultural performance over the long run. Outside agriculture, the country needs to encourage more labour intensive, export-oriented manufacturing such as agro-processing, garments manufacturing and horticultural production including cut flowers.

• **Low Savings and Investment Ratios**

The domestic savings/GDP and investment/GDP ratios in Malawi have been extremely low especially in recent years averaging about 8 percent and 15 percent over the past 3 years. The current investment ratios are certainly insufficient even to just maintain the current stock of capital, especially in the public sector. The reduction in the Public Sector Investment Programme over the past three years partly explains this. The current unfavourable state of roads, schools, hospitals, the telephone system, etc., is a manifestation of this phenomenon. Unless more savings are mobilised, it will be very difficult to improve the investment levels, without which there can be no sustainable long term growth.

Of particular importance in this regard is the need for government to continue in a more aggressive manner, the creation of an enabling environment for private investment. Thus, government will need to address the issues on temporary employment permit , the state of the infrastructure(i.e. roads, telephones, power generation, etc.) coupled with fiscal incentives in order to encourage both domestic and foreign investment.

III. Conclusion

The economic performance over the past two years has been remarkable as highlighted above. Nevertheless, as we have just seen, the long term problems are numerous and difficult to tackle. There is therefore no room for complacency. The various achievements over the past two years, have in the main recaptured lost ground, so that to the ordinary person the situation may not seem much improved only after two years of steady growth. The main challenge for the government is to consolidate these gains so that they can translate into meaningful improvements in the lives of ordinary people. To do this the government will need to stay on course with the structural reforms. Strong political commitment will be required to make unpopular but necessary decisions which will ensure economic stability, without which there can not be any good prospects for the growth of the economy.

If the economic situation remains as stable as it is now, prospects for the medium term look good. The overall macroeconomic objectives for the next four years are (a) an average real GDP growth rate of 6.5 percent a year; (b) an annual inflation rate of 5 percent by end 1999; (c) a further reduction in external imbalances mainly by having a competitive exchange rate and keeping external indebtedness within manageable levels; (d) increasing the domestic savings/GDP ratio from about 5 in 1995 to 15 percent by 1999; and (e) the accommodation of pressing social needs like free primary education by prioritising government expenditures in the context of the MTEF.

<u>RESERVE BANK OF MALAWI</u>

26 February 1997

SOME MAJOR MACRO-ECONOMIC INDICATORS FOR MALAWI

	1990	1991	1992	1993	1994	1995	1996
1. The Real Sector							
1.1 Population growth	3.3	3.3	3.3	3.3	3.3	3.3	3.3
1.2 GDP growth	5.1	7.8	-7.9	10.8	-11.6	9.0	9.7
1.3 Per capita growth	1.8	4.5	-11.2	7.5	-14.9	5.7	6.4
1.4 Savings/GDP ratio	9.4	7.9	1.7	-3.3	8.6	6.8	7.2
1.5 Investment/GDP ratio	19.1	20.1	18.8	12.2	13.2	15.2	21.5
1.6 Public consumption/GDP ratio	15.2	14.0	18.5	17.1	22.9	20.4	15.5
1.7 Private consumption/GDP ratio	75.4	78.1	79.8	86.2	68.5	70.0	79.4
2. Rate of Price Change							
2.1 Composite consumer price	11.5	11.9	23.3	22.8	34.6	83.3	37.6
2.2 GDP deflator (market prices)	10.8	13.4	18.3	21.8	39.8	76.5	42.1
3. Public Finance 1/ *							
3.1 Deficit (including grants)/GDP	-3.3	-5.0	-9.0	-3.1	-1.2	-4.8	-4.1
3.2 Deficit (excluding grants)/GDP	-4.1	-8.7	-12.8	-4.9	-5.0	-13.7	-9.1
3.3 Revenue (including grants)/GDP	20.3	20.1	23.2	20.2	20.6	26.7	21.1
3.4 Revenue (excluding grants)/GDP	19.5	16.4	19.4	18.4	16.8	19.7	16.1
3.5 Public debt service/GDP	7.0	5.1	5.5	4.8	8.4	7.2	5.4
3.6 Domestic public debt service/GDP	2.5	2.3	1.6	1.0	3.1	3.8	3.8
3.7 External debt service/Recurrent costs	21.5	15.4	15.6	21.2	21.2	10.7	6.1
3.8 Public External Debt Stock (K' million)	4004.7	4340.9	7104.0	7479.1	29716.0	29717.8	40599.0
3.8.1 Multilateral	3182.1	3474.6	4725.5	6027.6	23902.0	24896.8	32479.2
3.8.2 Financial (London Club)	174.6	118.3	207.8	236.7	734.7	1118.0	1218.0
3.8.3 Bilateral	648.0	748.0	947.7	1214.8	5079.3	3703.0	6901.8
4. The Balance of Payments							
4.1 Trade balance (MK'million)	138.9	147.5	86.0	-46.4	1276.3	2767.9	3292.8
4.1.1 Merchandise exports(FOB) (K'million)	1123.1	1333.0	1431.6	1396.8	3253.7	6559.2	7908.6
4.1.2 Merchandise imports (FOB) (K'million)	984.2	1185.5	1345.6	1443.0	1977.4	3791.3	4615.8
4.2 Current account (K' million)	-394.7	-737.2	-988.6	-1107.0	-452.9	-834.0	-591.9
4.3 Overall balance (K'million)	47.8	11.1	-502.6	170.9	-250.8	-482.3	0.0
4.4 Current account/GDP ratio	-8.4	-11.9	-15.2	-12.1	-4.0	-3.8	-1.8
4.5 Debt service ratio /2	22.0	18.9	24.0	21.6	15.0	31.9	23.0
4.6 Shipment costs/Merchandise exports	53.7	60.8	60.9	64.9	40.5	55.8	..
4.7 Rates of devaluation	7.0	..	15&22	..	..	..	..
4.8 Terms of trade (changes)		..	..	..	..	..	..
5. Money and Credit (%)							
5.1 Rate of growth of money supply	12.5	21.6	21.8	41.8	56.4	43.7	39.9
5.2 Broad money/GDP	17.6	16.2	18.8	19.0	24.1	19.1	16.2
5.3 Currency in circulation/GDP	3.4	3.6	4.5	4.5	5.6	4.9	3.7
5.4 Narrow money/GDP	8.6	8.4	10.4	10.1	12.6	10.2	7.8
5.5 Government credit/Total credit	30.5	24.0	45.6	53.4	54.9	49.7	40.7
5.6 Private credit/Total credit	70.6	74.2	56.3	43.4	46.1	48.4	51.9
5.7 Net Foreign Assets (K' million)	-2.2	8.8	-493.8	-322.8	-287.1	195.2	1966.1

Source: Reserve Bank of Malawi and Ministry of Finance.

1/ Figures on calendar year basis(cash flow).However the actual government fiscal year begins in April and ends in March the following year.

2/ Includes private sector.

INSIGHTS ON THE EFFECTS OF GOVERNMENT BUDGETARY OUTCOMES.

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INSIGHTS ON THE EFFECTS OF GOVERNMENT BUDGETARY OUTCOMES.

PART 1

INTRODUCTION

Much of what is heard and discussed concerning the Government Budget at the beginning and end of every fiscal year usually centres on measures taken by Government to finance or avoid or reduce a perceived excess expenditure, popularly known as the Budget Deficit. There are several reasons for this. One is that since the Malawi Government has rarely experienced a surplus on its income and expenditure operations,(see appendix1) the discussion has therefore been restricted to the effects of Government budget deficits on the national economy. Whatever has been debated has therefore centred on measures Government has put in place in order to manage the effects of the more frequent Government budgetary outcome (ie. fiscal deficits) on macro-economic goals and variables namely:

(a) **Economic Growth**, ie, by how much will the production of goods and services in the whole country increase or contract as a result of running a deficit.

(b) **Price Stability**, ie., how much inflation is expected as a result of running a deficit

(c) **Full Employment**, ie., will people continue to find employment, to work gainfully, to lose jobs or fail to find work as a result of a deficit?

(d) **Productivity**, ie, will the population be able to produce significant quantities of goods and services more easily or not as a result of a deficit?

(e) **Interest Rates,** ie., will the price paid for borrowing money or the gain to money lenders be altered as a result of a deficit?

(f) **Money Supply,** ie., will the amount of money (including current account deposits) in the hands of the general public increase or decrease as a result of the deficit, and what effect will that have on prices, on production of goods and services and on interest rates?

In trying to explore the effects of a budget deficit, which is the difference between money collected and money spent by Government it may be necessary to first know sources and uses of Government money.

PART 2

GOVERNMENT BUDGETARY OPERATIONS:

2.1 Sources of Government Funds

There are several sources of funds for the government among which are the following:

(a) ***Tax Revenue***

- Income Tax both personal and company tax
- Surtax or Sales Tax
- Poll Tax

(b) ***Licences and Fees***

(c) ***Excise/Customs Duty***

(d) ***Public Debt***

- Domestic Borrowing, i.e, borrowing within the economy
- Foreign Borrowing, ie., borrowing from other countries

(e) ***Grants***

2.2 Uses of Government Funds

(a) ***Recurrent Expenditure,*** i.e., money used for the day to day running of the civil service

(b) ***Development Expenditure,*** i.e., money used for the establishment of facilities to be used for generations to come eg building roads, schools, hospitals, etc.

(c) ***Debt Servicing,*** ie, repayment of principal and interest on both domestic and foreign debt.

PART 3.

GOVERNMENT BUDGETARY OUTCOMES: THE BUDGET DEFICIT

3.1 Causes of Budget Deficit

(i) Reduction in Revenue Sources and magnitudes, eg reduced tax collection.

(ii) Lack of Government Expenditure Control

3.2 Major Effects of a Budget Deficit: Government Borrowing

When Government fails to find enough money from normal means, it resorts to borrowing from both the domestic and foreign financial markets. Domestic borrowing does not increase the amount of financial resources within the economy since the resource merely gets transferred from individuals and institutions to the Government. The means of borrowing include selling local registered stock, treasury, bills and bonds. On the other hand, borrowing from abroad increases the stock of resources in the economy. Whatever the origins of borrowed funds, the longterm effect is that of transfering repayment obligations to future generations whom Government will tax in order to secure money for debt repayment. However, of more interest to us are the immediate or short term effects of borrowing, namely, Monetary effect, Crowding-out effect, Inflationary effect, Fiscal effect and Exchange Rate effect.

3.2.1. The Monetary Effect of Public Debt

One of the early consequences of government borrowing is the raising of Interest Rates by the lending sector (due to Government determination to borrow money from anybody at any cost by sales of Treasury Bills). This has restraining effects on Private sector investment in the form of high borrowing costs. People fear getting loans for businesses because of high interest rates.

3.2.2 The Crowding-Out Effect

The Government monopolises money from banks so that others wishing to borrow money for investment and consumption can not do so. in This case, one hears about the 'Credit Squeeze' on the general public, meaning that borrowing becomes severely restricted because banks have reserved most of the money for lending to government. This has multiple effects on the economy. No investment means less production and less demand for other production inputs such as labour. Less money for consumption means less demand for consumer goods, means excess capacity in the sectors producing the consumer goods leading to less production and laying off of the workforce.

3.2.3 Inflationary Effect

(i) First If the Productive sector chooses to go ahead and borrow money for investment at the high interest rates brought about by the Monetary effect of Public Debt, the cost of acquiring or producing goods and services rises and the final price to the consumer rises even further as the producers try to cover the high interest costs.

(ii) Too much money injected in the economy chasing too few goods, because Government borrowing from the Central Bank (i.e., Government instructs the Central Bank to print money the supply of which does not correspond to the quantity of goods available at the time).

3.2.4. Fiscal Effect

(i) Government may elect to raise the level of taxes in order to reduce the deficit. Tax rises have their own effect on consumption and investment. The tax payers be they people or companies get affected. People buy fewer goods and services than would be the case if there was no tax rise. This in turn brings down sales turnover and profit in the sectors that produce the goods and services resulting in the down-sizing of production facilities with resultant loss of jobs. Companies paying increased corporation tax experience a lower return on investment which discourages them from investing further resulting in less business, less employment opportunities and loss of output to the economy.

Further effects of tax rises will depend on the type of taxes that will rise. There are two types of taxes depending on whether or not they favour the poor. Those that favour the rich at the expense of the poor are known as Regressive taxes. Those taxes that spread the burden equally between the two categories of people are known as Progressive taxes. An increase on sales tax or surtax especially on things that everyone needs every day such as food stuff and soap tends to hit the poor much more than the rich. Sales taxes are regressive because the poor who are already struggling to afford food and soap will now cut down on the consumption of these essential goods and services since they will now afford even less quantities of each.

(ii) Expenditure control through the Cash Budget system.

This works on the rule that expenditure allocation for a particular month will depend on the revenue collected in the previous month. This bring in the problem of how much to allocate to which sector with certain sectors suffering savage cuts in allocation. Unfortunately sectors like education and health can not been exempted allocation cuts resulting in shortages of teaching materials, late payment of teachers' salaries and drug shortages.

3.2.5. Exchange Rate Effect

The deficit will also affect the stability of the Kwacha relative to other currencies for two reasons:

(a) Scarcity of locally produced goods as a result of depressed private sector investment brought about by the tax rise or the rise in interest rates will force Malawians to import the scarce goods.

(b) The resultant scramble for foreign currency to facilitate importation of the scarce goods. Forex becomes a scarce commodity which then fetches a high price in Kwacha terms, meaning that one has to pay more Kwacha per unit of convertible foreign currencies. The exchange rate stops to be in the Kwacha's favour,

PART 4

MEASURES TAKEN BY GOVERNMENT TO CORRECT THE NEGATIVE SIDE EFFECTS OF THE BUDGET DEFICIT

4.1 Monetary Policy Measures.

Raising interest rates to facilitate easy sale of Treasury Bills so as to mop up excess liquidity from the economy ie, to prevent people having money in their hands. This is complemented by the fact that high interest rates encourage savings which are a withdrawal of money from the hands of the public into banks. At the same time, high interest rates discourage borrowing by the general public thus further preventing people from having money in their hands. The objective of all this is to reduce the type of inflation caused by people having too much money chasing too few goods. This may actually also deceptively end up as a deficit financing measure rather than a measure to control inflation.

4.2 Fiscal Policy Measures

Tax Cuts to stimulate consumption and investment which will in turn generate more tax revenue for the government through incremental sales tax and income tax.

4.3 Exchange Rate stabilization measures

(a) Cutting down on imports by making them expensive through imposition of high customs duty. This also serves as a way of increasing government revenue whose effect is to reduce the deficit.

(b) Rationing of foreign exchange through exchange controls

(c) Stimulate production of more exports goods eg through establishment of Export Processing Zones (EPZ) and export promotion activities such as attendance of international trade fairs.

SUMMARY

This paper has sought to explain the issues that occupy most people's minds and provoke a lot of discussion soon after presentation of the Government Budget. While it is possible for Government to balance the budget or even achieve a surplus, discussion of the effects of these has not been made because we are more concerned with the effects of budget deficits with which we have lived since independence. In seeking to familiarise oneself with causes, effects and corrective measures of budget deficits one sees the numerous dilemmas policy makers fall into. For instance, while high interest rates happen as a result of government intention to finance budget deficits, the same government uses high interest rates to reduce inflation. It takes more than common sense for one to know the exact reason of the prevailing condition of the economy such as high interest rates. It is easy for one to conclude logically that reducing inflation can also lead to a worsening investment climate.

Academically, priorities of government in economic terms should embrace items spelt out in the introduction, namely,

(a) Economic growth reflected in a year-on-year increase in Gross Domestic Product (GDP) or Gross National Product (GNP) depending on whether the country has a sizeable number of its own citizens engaged in economic activities abroad which have a direct economic benefit to Malawi;

(b) A stable price structure for all goods and services whether imported or locally produced, i.e., a bearable inflation regime.

(c) A fully employed population where no workers are losing jobs (job security); everyone is finding a job (employment creation); and nobody is doing jobs that make them produce less output than would normally be the case (no under employment) .

(d) A state of affairs where machines, people, land and money are utilised to the extent that more goods are produced per machine hour; man hour; hectare cultivated or let out; or Kwacha spent than was the case in the preceding period. This is what is meant as increased productivity.

(e) Stable interest rates that are conducive to both lenders and borrowers operating gainfully.

(f) A manageable supply of money in the economy that will not trigger an insatiable demand for available goods and services.

Balancing these noble goals with the state of the national budget which history has proved to be perpetually in the negative is a wrestler's nightmare. Take the full employment goal for example. It will not tally with policies that advocate deficit financing through an increase in taxes because not only will companies grumble, so too will the ordinary citizens for the reduction in take-home pay. The ramnifications are all too obvious:

1. Reluctance by companies to invest will lead to lack of resources to train employees; update equipment and expanding operations resulting in reduced productivity and production.

2. Depressed demand for consumer products will lead to the productive sector scaling down operations including retrenching workers.

Price stability will not be achieved if customs duty is raised in the name of discouraging people from importing goods and services for the sake of reducing the demand for imports and therefore stabilising the exchange rate. Those that are determined to import will seek to have the customer absorb the duty thereby bringing 'cost-push' inflation. One could go on attacking one policy measure after another. However what is important to our legislators and policy makers is for them to know that to every prescribed medicine there is an antedote. It is therefore important for them to know both.

References

1. Reserve bank of Malawi, "Quarterly Economic Reviews"

2. International Monetary Fund "Confronting Budget Deficit" IMF, Sept 1996

Appendix 1

A HISTORY OF GOVERNMENT BUDGET DEFICITS IN MALAWI 1970-1993
(Figures in Millions of Malawi Kwacha)

	Revenue	Total Expend.	Balance
1970	38.6	73.5	-34.9
1971	45.9	71.5	-25.6
1972	52.4	83.2	-30.8
1973	59.2	88.4	-29.2
1974	65.3	90.7	-25.4
1975	76.7	117.1	-40.4
1976	81.7	126.8	-45.1
1977	100.9	136.0	-35.1
1978	136.0	202.2	-66.2
1979	156.0	252.4	-96.4
1980	198.8	309.7	-110.9
1981	214.6	370.2	-155.6
1982	230.7	324.1	-93.4
1983	272.6	422.2	-149.5
1984	311.1	469.6	-158.6
1985	383.6	540.7	-157.1
1986	457.5	590.2	-132.7
1987	549.0	808.8	-259.8
1988	689.4	710.7	-21.3
1989	855.6	1118.0	-262.4
1990	913.2	1104.9	-191.7
1991	1001.1	1547.0	-545.9
1992	1146.5	1559.9	-413.4
1993	1280.3	1577.5	-297.2

Source: Reserve Bank of Malawi Financial Economic Review, 1991 Volume XXIII - Number 2

Note: The revenue excludes grants in order to expose Government's capcity to finance commitments on its own

APPENDIX 2

SAMPLE GOVERNMENT BUDGETARY OUTCOME FOR 19XX

(Figures are in Millions of Malawi Kwacha)

INFLOWS OF FUNDS

Revenue	583,40
Grants	69.00
TOTAL INFLOWS	652.40

OUTFLOWS OF FUNDS

Recurrent Expenditure	616.50
Development Expenditure	207.40
TOTAL OUTFLOWS	823.90
DEFICIT	(171.50)

FINANCED BY

Foreign Loans	79.80
Domestic Borrowing	91.70
	(171.50)

REVENUE AND THE BUDGET: AN ANALYSIS

PRESENTATION

BY

WAKI MUSHANI
CONSULTANT

KEY ISSUES IN REVENUE ANALYSIS

- **GOVERNMENT FISCAL POLICY**

- KEY ECONOMIC VARIABLES E.G.

  - **Economic activity**
  - **Income distribution**
  - **Growth in GDP**
  - **Growth in Imports/Exports**
  - **Level of personnal and corporate incomes**

- **THE NATURE OF THE TAX BASE**

- **TAX ADMINISTRATION CAPACITY**

- **EXPENDITURE REQUIREMENTS**

MALAWI CENTRAL GOVERNMENT REVENUE

(K MILLION)

	1995/96	1996/97	% Change
A. TAX REVENUE	3,913.71	5,251.14	**34.17%**
1. Taxes on Income and Profit	1,390.00	1,845.00	**32.73%**
Companies	660.00	810.00	**22.73%**
Individuals	730.00	1,035.00	**41.78%**
Non-Resident Tax	9.00	15.00	**66.67%**
Graduated	0.00	0.00	**0.00%**
P.A.Y.E.	500.00	660.00	**32.00%**
Withholding Taxes	175.00	300.00	**71.43%**
Fringe Benefits	46.00	60.00	**30.43%**
2. Taxes on Property	0.00	0.00	**0.00%**
3. Taxes on Goods and Services	1,414.71	1,924.14	**36.01%**
Accommodation and Refreshment Tax	0.00	0.00	**0.00%**
Surtax	1,210.00	1,775.00	**46.69%**
Excise Duties	190.00	130.00	**-31.58%**
Licences	14.71	19.14	**30.12%**
Business and Professional	1.71	2.14	**25.15%**
Motor Vehicle Licences	13.00	17.00	**30.77%**
4. International Trade Taxes	1,100.00	1,472.00	**33.82%**
Custom Duties	1,100.00	1,472.00	**33.82%**
Import Duties	749.00	1,000.00	**33.51%**
Export Duties	347.00	450.00	**29.68%**
Miscellaneous Duties	4.00	22.00	**450.00%**
5. Stamp Duties	9.00	10.00	**11.11%**
B. NON-TAX REVENUE	442.13	477.03	**7.89%**
Treasury Fund Receipts	5.08	5.23	**2.95%**
Rents	40.50	90.00	**122.22%**
Departmental Receipts	382.71	323.97	**-14.04%**
Reimbursements	13.84	52.83	**281.72%**
GRAND TOTAL	4,355.84	5,728.17	**31.51%**

CENTRAL GOVERNMENT BUDGETARY OPERATIONS

(K MILLION)

	1995/96	1996/97
TOTAL REVENUE AND GRANTS	6,321.26	7,289.09
Revenue	4,355.83	5,728.17
Grants	1,965.43	1,560.92
TOTAL EXPENDITURE	7,101.93	8,877.00
Recurrent Expenditure	5,636.50	6,797.00
Development Expenditure	1,465.43	2,080.00
DEFICIT		
Excluding Grants	-2,746.10	-3,148.83
Including Grants	-780.67	-1,587.91
FINANCING	780.67	1,587.91
Foreign Loans (net)	137.81	1,657.07
Borrowing	998.73	2,361.07
Repayment	-860.92	-704.00
Domestic Borrowing (net)	-642.86	69.16

(As a percentage of GDP)

Revenue (Excluding grants)	27.04%	18.12%
Recurrent Expenditure	34.99%	21.50%
Development Expenditure	91.00%	6.58%
Deficit Excluding Grants	-17.05%	-9.96%
Deficit including Grants	-4.85%	5.02%
GDP at Current Market Prices (K mn)	16,109.70	31,620.90

FUNCTIONAL CLASSIFICATION OF THE RECURRENT EXPENDITURE			
	1995/96	1996/97	% Change
GENERAL SERVICES	1,947.47	2,028.46	4.16%
General Administration	1,438.89	1,608.46	11.78%
Defence	255.88	260.00	1.61%
Justice	252.70	160.00	-36.68%
SOCIAL SERVICES	1,270.06	1,488.14	17.17%
Education	843.99	821.03	-2.72%
Health	367.46	610.51	66.14%
Community and Social Developmen	58.61	56.60	-3.43%
ECONOMIC SERVICES	1,306.99	1,768.93	35.34%
Natural Resources	370.61	632.20	70.58%
Transport	62.11	138.18	122.48%
Post and Telecommunications	0.00	0.00	0.00%
Other Economic Services	874.27	998.55	14.22%
UNALLOCABLE SERVICES	1,928.70	2,549.20	32.17%
Public Debt Services	1,466.02	2,004.00	36.70%
Pensions and Gratuities	220.00	267.60	21.64%
Other Unallocable Services	242.68	277.60	14.39%
TOTAL	6,453.22	7,834.73	21.41%
LESS: Debt Armotization	816.72	1,037.73	27.06%
TOTAL RECURRENT EXPENDITURE	5,636.50	6,797.00	20.59%
(As a percentage of total Recurrent Expenditure)			
GENERAL SERVICES	34.55%	29.84%	
General Administration	25.53%	23.66%	
Defence	4.54%	3.83%	
Justice	4.48%	2.35%	
SOCIAL SERVICES	22.53%	21.89%	
Education	14.97%	12.08%	
Health	6.52%	8.98%	
Community and Social Developmen	1.04%	0.83%	
ECONOMIC SERVICES	23.19%	26.03%	
Natural Resources	6.58%	9.30%	
Transport	1.10%	2.03%	
Post and Telecommunications	0.00%	0.00%	
Other Economic Services	15.51%	14.69%	
UNALLOCABLE SERVICES	34.22%	37.50%	
Public Debt Services	26.01%	29.48%	
Pensions and Gratuities	3.90%	3.94%	
Other Unallocable Services	4.31%	4.08%	

MEDIUM TERM EXPENDITURE FRAMEWORK

PRESENTATION

BY

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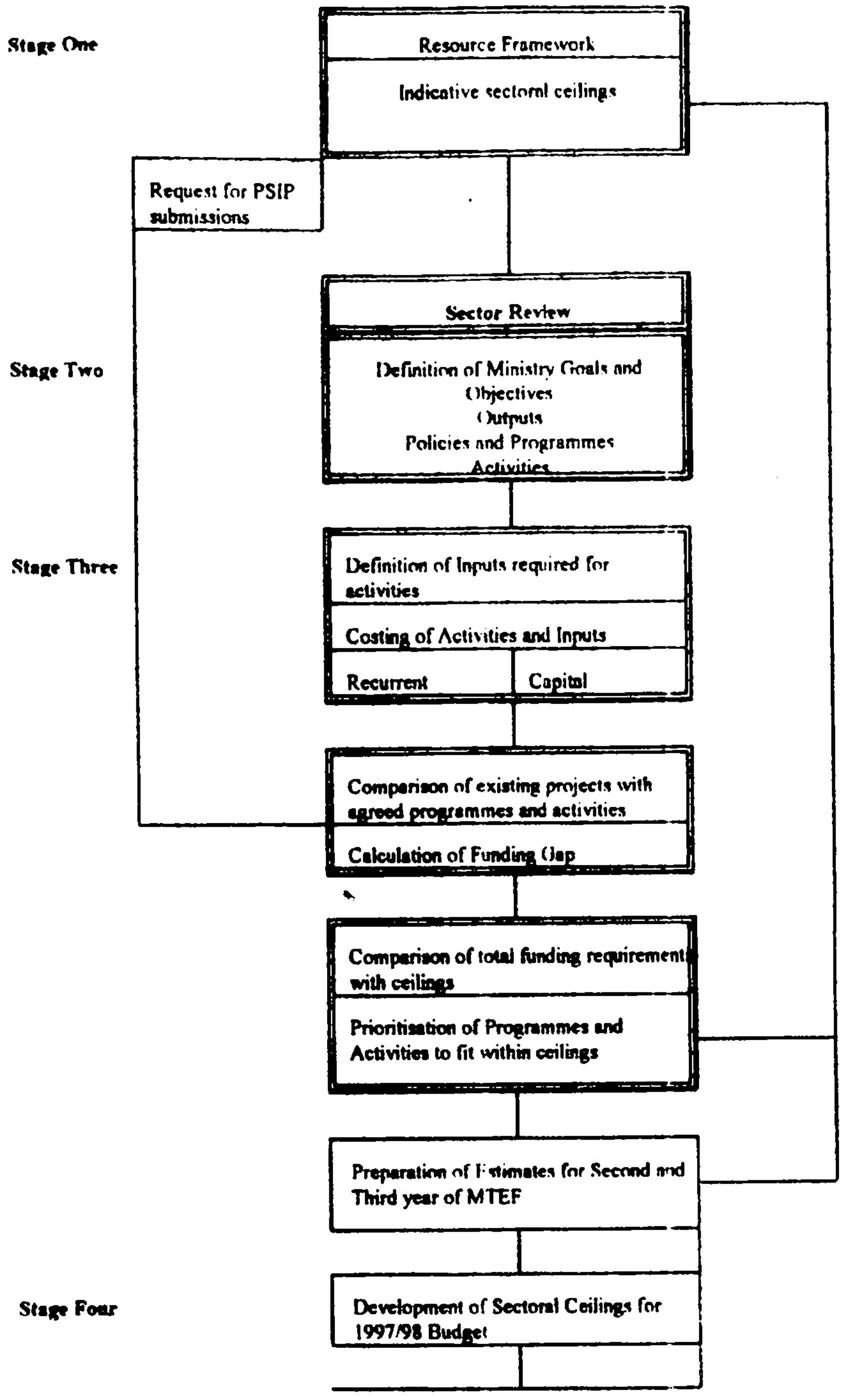
Stages in the MTEF and Annual Budget Preparation



The Medium Term Expenditure Framework

Introduction

1. The Government has initiated several measures for improving the budget process that will facilitate a long lasting improvement in the management of public resources. The most important measure taken so far is the introduction of the Medium Term Expenditure Framework (MTEF) as the basis for a more strategic approach to public expenditure planning in Malawi. The MTEF began in preparation of the 1996/97 budget in four pilot ministries, namely Education, Health, Agriculture and Works, which account for more than 40% of the recurrent expenditures. Police has also followed the MTEF approach in framing their estimates. The MTEF approach will be introduced in other sectors in the 1997/98 financial year.

2. This brief note describes the weaknesses in the existing budget system that the MTEF will address, explains the process of preparing an MTEF, and describes progress made to date.

Current Weaknesses in Budgeting

3. The current budget process has the following weaknesses:

- the **recurrent budget is prepared on an incremental basis**, i.e. simply adding a certain percentage to the previous year's estimates. The process of preparing the recurrent budget does not involve reviewing whether the particular activities are in line with Government priorities nor whether they are being implemented in the most effective manner.
- in some votes the **structure of the recurrent budget does not adequately reflect the activities** that ministries are responsible for. Instead the budget shows the types of expenditure, such as travelling expenses, under a particular cost centre, without giving any indication of the purpose of travelling;
- there is no forward planning of the recurrent budget;
- while the development budget is not prepared on an incremental basis, it tends to be driven by the availability of donor funds, rather than being based on government's own needs and priorities;
- the process of preparation and monitoring of the development and recurrent budgets are quite separate.

4. The results of these weaknesses are:

- recurrent funded programmes/activities continue from year to year, even if they are not consistent with changing priorities and circumstances. The current process also means that ministries are not reviewing whether the level of services is appropriate;

- the budget process does not involve assessing the real funding requirements of services, but is based on adding a small percentage to the previous year's allocations. The result is that essential services are underfunded;
- the efficiency and cost effectiveness of government services is not being reviewed;
- development projects proceed without assessing their recurrent cost implications and whether sufficient recurrent funds will be available to cover the recurrent costs that will arise.

The Need for Change

5. Even if government resources were expanding, the above weaknesses in the budgeting process would result in an inappropriate allocation of resources. In Malawi's situation there is an urgent need to restructure public expenditures and to introduce a more rational approach to allocation of resources.

6. The need for restructuring of public expenditures is the result of two factors:

- policies of economic reform have led the government to reconsider its role in many sectors, requiring radical changes in budget allocations between and within sectors.
- severe economic circumstances have greatly overstretched government resources, particularly the recurrent budget. This has resulted in **under-funding of priority activities**, greatly reducing the effectiveness of these services. The situation became so severe in 1995/96 that the government has introduced the cash budget as a short term crisis measure.

Objectives of the MTEF

7. The objectives of the MTEF are to improve the budget process in such a way as to:

- restructure expenditures both within and between sectors in line with **clearly established priorities**;
- identify the **actual costs** of particular activities so that government can begin to move away from incremental budgeting.
- **plan for restructuring of expenditures**, as these shifts in expenditures cannot take place from one year to the next.
- **introduce a more rational approach to resource allocation**, by identifying fewer priority activities, which would

receive adequate funding and provide greater value for money.

- integrate the preparation of the development and recurrent budgets, so as to plan for the recurrent costs arising from projects.
- **plan both budgets on the basis of government priorities** and requirements for a sector and its programmes, so that the development budget will become less project driven.

8. The aim is to indicate trade-offs between and within sectors to senior management and politicians. By estimating the real costs of providing services within sectors, government can begin to make decisions about which services it can afford to provide. The MTEF will show these trade-offs and point to changes in resource allocation that need to take place over the medium term, as well as identifying policy changes that would improve the quality of services and availability of funding.

9. A secondary objective of an MTEF, at least in developed countries, has often been to permit line agencies to take on greater responsibility for planning and executing their programmes. An MTEF enables central resource management agencies to focus on sector and programme aggregates, while allowing greater delegation to the line agencies in the matter of detail. In Malawi greater devolution of responsibility for resource allocation and management is one of the medium term objectives of the MTEF.

10. One possible misconception about the MTEF needs to be avoided from the outset: the introduction of an MTEF will not result in an increase in the availability of funds. The MTEF is simply a management tool for improving the allocation of resources and in Malawi's case, reallocating resources to fewer priority activities.

Introduction of an MTEF in Malawi

11. Malawi is learning from the experience of several other countries who are in the process of introducing a similar approach to budgeting. Rather than taking the exact procedures from these other countries, Treasury is working with four pilot sector ministries to develop methodologies appropriate to Malawi's conditions. The four pilot sectors are education, health, agriculture and works who have identified and costed programmes of activities in their sectors, focusing primarily on the recurrent budget.

12. The first round of the MTEF process has necessarily been a learning experience for both Treasury and the four pilot ministries. It is also helping to guide the process of civil service reform and restructuring by providing information on the objectives and programme priorities for the four sectors.

13. The main developments proposed for the second MTEF round are to develop a definitive timetable and procedures, by learning from the experience of preparing the first MTEF. In addition, the scope of the MTEF will be broadened in two ways - to include other sectors in the preparation process and to cover the development budget.

Stages in Preparing an MTEF

14. The stages in preparation of an MTEF are:

1. developing a consistent macroeconomic framework and from this realistic resource projections for a three year period;
2. deducting statutory payments such as pensions and debt payments;
3. breaking down the remaining aggregate expenditure figures into sectoral ceilings, based on the relative importance of each sector;
4. within each sector, determining which programmes should receive a greater or lesser share of the sector resource envelope;
5. approval of ceilings by Cabinet for the annual budget and two outer years of the three year period;
6. preparation of annual budget estimates (year 1 of the MTEF);
7. approval of the Budget by Parliament.

15. The MTEF ceilings for the outer years may either be incorporated into the government's annual budget statement, so as to emphasis its strategic perspective, or they may be shown in a separate report published in conjunction with the budget.

16. For the fourth stage in the process, sector ministries need to have sufficient information on their programmes of activities and the actual costs of these activities, before they can make realistic and rational decisions about the allocation of resources. Developing this kind of information has been the main focus of activity for the first MTEF as described below.

Progress to Date

17. Although it is usual to start an MTEF cycle with the establishment of a medium term resource framework and indicative ceilings, the approach the first time around was slightly different. The four pilot ministries, accounting for around 40% of the recurrent budget, started on their reviews in July 1995, prior to the development of the resource framework. Once the resource framework had been finalised in November, indicative ceilings were provided to the four ministries.

Sector Reviews

18. Each of the four ministries followed an **integrated sector approach** to planning which involved:

- **reviewing and defining sectoral objectives and policies.** Each of the 4 ministries had already prepared detailed policy documents.
- **identifying the programme of activities** needed to implement the sectoral policies. For some ministries this involved a fairly radical restructuring of their existing budget structures, as the current structure does not reflect the activities that the ministry is responsible for. For example, the Ministry of Health and Population has divided its hospital services programme into several programmes to indicate the type of services or activities, such as preventive and curative services.
- estimating the actual costs of providing these services;
- identifying activities that can be scaled back or stopped altogether so as to fit within the expenditure ceilings.

19. Each of the 4 ministries identified and costed their programmes through a series of workshops, coordinated by ministerial task forces and assisted by Treasury. During early November, the 4 pilot ministries and institutions undertook the most difficult task in the exercise: identifying ways in which their programme costs could be cut back so as to fit within the ceilings. The aim was to identify specific activities that would be scaled back or stopped, rather than cutting back on all activities and perpetuating the present under-funding problem.

20. Although the 4 priority sectors were the only sectors to receive an increase in the level of funding for 1996/97, many of their activities were underfunded. In order to provide sufficient funding for priority activities, funding of some activities had to be cut back for 1996/97. Programme managers in the 4 sectors were requested to explain the implications of these cuts on the provision of services and on meeting sectoral objectives. They also attempted to identify policy options for addressing the shortfall in funding.

21. The first year of implementation was a learning experience for all concerned and while progress was made in moving away from the incremental approach to preparation of the recurrent budget, there were some problems particularly in the identification and costing of programme activities. Treasury will be working with the four pilot ministries to define in detail the process that should be followed in the implementation of the MTEF for 1997/98.

Plans for the Second MTEF

22. In preparation of the 1997/98 budget, the MTEF approach will be expanded to other ministries and further improved as follows:

- including both the recurrent and development budgets;
- providing ministries indicative ceilings earlier in the year;
- Treasury will work with EP&D and DHRM&D to assist ministries in the review of their functions and activities, so as to identify those priority activities to be undertaken, and those that can be phased out, either because they are no longer compatible with government policy or they can be handed over to the private sector;
- giving more attention to the preparation of programme estimates for 1998/99 and 1999/2000 as well as to the 1997/98 annual estimates;
- improving the classification of the recurrent and development budgets so as to provide more meaningful information to managers and developing a budget and accounting coding system to reflect the improved classification system.

Requirements for the Success of the MTEF

23. The success of the MTEF in achieving its objectives will depend on the following factors:

- **political commitment and endorsement** at the highest level to make and abide by the difficult decisions involved in restructuring of expenditures. Some ministries will be need to scale back their activities so that more resources can be directed to higher priority sectors.
- **understanding of and commitment to the difficult decisions at the sector ministry level**
- **commitment at all levels to abide by the budget decisions** so that new expenditure decisions are not introduced during budget implementation that would require reallocation of resources. These new decisions mean that the priorities set when the budget is approved by Parliament are often overturned.
- **improvements in expenditure control** so that the budget decisions are not undermined by over-expenditures and reallocation of funds during budget implementation.
- **improved macroeconomic management and revenue collection** so that revenue shortfalls do not necessitate adjustments to the budget estimates, as has been the case in the 1995/96 budget.

24. The Treasury and Ministry of Economic Planning and Development are developing the conditions for successful introduction of the MTEF. These include:

- **briefings for senior management and Cabinet** on the objectives of the MTEF, as well as the preliminary findings of the first MTEF exercise;
- **extensive involvement of senior managers within line ministries** in the process of preparing the MTEF. Workshops have been held throughout the process, at which senior managers have been involved in developing the methodology and programme costs;
- **improvements in expenditure control and timeliness of expenditure reporting** through computerisation of the budget and accounting system and training of staff in improved accounting procedures;
- **training** of staff in the MTEF approach through a series of workshops to be held in 1996 and 1997.

BUDGET WORKSHOP RECOMMENDATIONS AND RESOLUTIONS

MAIN RESOLUTIONS OF THE WORKSHOP

The NDI sponsored Budget and Finance Committee workshop held at Capital Hotel from 28th February to 1st March, 1997 resolved as follows -

1. That the Committee's mandate be expanded to include consultations with the Reserve bank of Malawi, the Malawi Chamber of Commerce and Industry, MIPA and other organizations on economic and financial matters;

2. That the Committee be empowered to make proposals on natural features to be used on our currency and to submit such proposals to Parliament for its approval;

3. That the cash budget system is a necessary tool for controlling government expenditure and inflation;

4. That Members of the Budget and Finance Committee should take a leading role in the budget debate in the National Assembly;

5. That in addition to advancing the interests of their constituencies during the budget debate, members should also comment on wider issues such as the effects of increased taxation on the economy;

6. That structural adjustment policies are necessary for economic growth even though the benefits of growth take time to trickle down to the masses;

7. That the private sector is the engine for economic growth and the banks and the Government should assist in promoting it through appropriate monetary and fiscal policies;

8. That the restructuring of the civil services should focus on placing highly productive individuals in offices and that retrenchment per se may not be the ultimate solution considering the fact that our civil service is relatively small compared to some neighboring countries;

9. That the Budget and Finance Committee, being a very crucial committee, be provided with the necessary financial and technical resources to enable it carry out its functions satisfactorily.

RECOMMENDATIONS

1. NDI should consider organising more seminars of this nature to involve possibly all Committees of the House, funds permitting. The seminars should however cover a longer period of time and should include simulations.

2. NDI should consider organising a study tour for the Committee in neighboring countries so that members can appreciate how similar committees operate elsewhere.

3. That the secretariat should continue sourcing documents on financial and economic matters for distribution to Members of the Committee.

4. The Budget and Finance Committee should meet between October and December to receive a briefing by the ministry of Finance on the performance of the budget and the direction which the Treasury recommends to Ministries before Cabinet is consulted to enable Parliament/The Budget and Finance Committee to have a meaningful input in the budget process.

5. NDI should consider training the Secretariat servicing the budget and Finance Committee so that it can provide better service to the Committee.

6. NDI should consider organising a joint seminar for the Public Accounts and the Budget and Finance Committees so as to facilitate a process of consultation between Members of the two Committees.

7. NDI should consider financing the Committee to enable it meet regularly so that it can scrutinise the planning process and estimates of the national budget.

BUDGET WORKSHOP EVALUATION SUMMARY

Evaluation Summary For
Budget and Finance Committee Workshop
28 February to 1 March, 1997

NOTE: The evaluation form was distributed at the very end of the workshop and was done in an anonymous fashion as a means of soliciting more honest comments from the workshop participants. Eleven of the twelve participants returned evaluation forms. Of these eleven, the following observations were made:

Section 1

1. Venue (Poor- 0%, Fair- 0%, Good- 27%, Excellent-73%)

Comments:

-The venue was most central

2. Lodging (Poor- 0%, Fair-0%, Good-9%, Excellent-82%)

Comments:

-One participant did not require accommodation

3. Conference Room (Poor-0%, Fair-0%, Good-55%, Excellent-45%)

Comments:

-The conference room was quite good
-There was need for more microphones

4. Agenda (Poor-0%, Fair-9%, Good-64%, Excellent-27%)

Comments:

-The agenda was crammed; there was not enough room for discussion
-The agenda was well planned
-It was easy to follow

5. Resource People (Poor-0%, Fair-0%, Good-45%, Excellent-55%)

Comments:

-They knew what they were doing
- Well presented

6. Length of Workshop (Poor-9%, Fair-27%, Good-55%, Excellent-9%)

Comments:

-Please extend; the length of the workshop was very short
-There was need for more time
-People were not tired
-Not enough days; four days would do
-We needed more time for discussions
-Time too short for the contents of the workshop
-3 days would be ideal

7. Effectiveness of Workshop (Poor-0%, Fair-9%, Good-36%, Excellent-45%)

Comments:

-We probably require budget simulation
-Very effective

8. Reference Materials (Poor-0%, Fair-0%, Good-64%, Excellent-18%)

Comments:

-We need more

Section 2

9. Did you learn something you did not already know about the budget process in Malawi? (Yes-90%, No-9%)

Comments:
-I belong to the profession
-I have increased my knowledge
-It has just added on to that which I already know
-I learned more about the interpretation of the budget
-I learned about the affects of various policies on the economy

10. Do you believe that the presentations and handouts will be useful in your work as a member of the Budget and Finance Committee? (Yes-90%, No-0%)

Comments:
-It has been an eye opener
-The handouts will be useful because they will help to go through the process
-They will help me greatly
-We need another workshop as soon as possible

11. Did you find the workshop useful? (Yes-100%, No-0%)

Comments:
-The workshop was very useful
-We have learnt new ideas

12. Will you share what you learned from the workshop with other Members of Parliament? (Yes-82%, No-9%)

Comments:

-Yes, especially during parliament debates
-It is difficult in view of the various levels of appreciation
-I will teach my friends
-Yes, to those willing to learn

Section 3

13. Please list 2 or 3 things that would better enable you to perform your duties as a member of the Budget and Finance Committee more effectively?

- Interpretation of the budget;
- Involvement in the preparation of the budget from below to the top;

- Meet the initial people on the budget;
- Have handouts from those who initiate the budget;

- I have attained the skills necessary to quickly analyze the budget;
- Handouts on aspects of budget and economy;
- Policy documents from all ministries;

- More regular meetings;

- Information from Minister of Finance;

- I can now read budget figures;
- I know what happens in the Ministry of Finance:

- Reading the budget;
- Interpreting the effects of the budget on the people of Malawi;

- More statistical data and information;
- More analysis of budget after presentation;
- Consultancy service at our disposal for analysis;

- An overview of how to read the budget;
- Planning and estimates which came under MTEF;

- As a Clerk serving the committee, I will be able to explain some basic economic facts to other Members of Parliament and colleagues;
- I will also be able to source the right reference materials for members of the committee since I am in a better position to determine their needs.

Section 4

14. What kind of assistance would like NDI to provide to the Budget and Finance Committee in the future?

- Sponsoring more of these workshops;
- Offering trips to the committee to visit other committees in other countries;
- Continuous financial assistance on workshops;
- Facilitate a budget analysis seminar immediately after budget presentation by Minister of Finance;
- It would assist to have experts to analyze the budget for the committee;
- Research results on reality on the ground, e.g. situation analysis to assess whether the budget allocations really trickle down to the people or programmes/projects intended;
- Facilitate a joint seminar of the Budget and Finance Committee and the Public Accounts Committee- each should consult and inform the other;
- Let us have more workshops;
- Organize more seminars to make the committee to learn more information from several ministries;
- Upgrade secretariat servicing the committee through training the secretary;
- Make available computer services to parliament for use of remarks of the committee;
- Financing the committee to enable it to meet regularly so that it can scrutinize the planning and estimates of the national budget;
- The committee needs more workshops;
- More seminars of this nature so that we get a stronger grip on the budget formulation process;
- Study tours to other countries so that members and the clerk serving the committee can learn more about how similar committees operate elsewhere.

Section 5

15. Other Comments:

I have enjoyed the workshop and will be glad if you will organize more workshops because it is very educative to me.

We need more lectures from the Governor of the Reserve Bank on the changes in the economy.

Grateful for NDI prompt and effective response.

The workshop was very fruitful but time was too short to accommodate the material learnt so far.