

FISCAL DECENTRALISATION IN UGANDA



THE REPUBLIC OF UGANDA

***DRAFT* STRATEGY PAPER**

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Prepared by the FISCAL DECENTRALISATION WORKING GROUP

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LIST OF ACRONYMS

BFP	Budget Framework Paper
CBG	Capacity Building Grant
CG	Conditional Grant
DDP	District Development Plan
DTB	Development Transfer Budget
DTS	Development Transfer System
EG	Equalisation Grant
FDS	Fiscal Decentralisation Strategy
FY	Financial Year
IDA	International Development Association
IGG	Inspector General of Government
IPF	Indicative Planning Framework
LCII	Local Council Two (Parish)
LCIII	Local Council Three (Subcounty/Division)
LCV	Local Council Five (District)
LDG	Local Development Grant
LG	Local Government
LGA	Local Government Act (1997)
LGBC	Local Government Budget Committee
LGBFP	Local Government Budget Framework Paper
LGDP	Local Government Development Programme
LGFR	Local Government Financial and Accountability Regulations (1998)
LGFC	Local Government Finance Commission
LGROC	Local Government Releases and Operations Committee
LM	Line Ministry
MFPED	Ministry of Finance Planning and Economic Development
MOLG	Ministry of Local Government
MOPS	Ministry of Public Service
MTEF	Medium Term Expenditure Framework
NAADS	National Agriculture Advisory Services
PAC	Public Accounts Committee
PAF	Poverty Action Fund
PDP	Parish Development Plan
PEAP	Poverty Eradication Action Plan
PMU	Programme Management Unit
RTB	Recurrent Transfer Budget
RTS	Recurrent Transfer System
UCG	Unconditional Grant
UNCDF	United Nations Capital Development Fund

1 INTRODUCTION

1.1 Background

Uganda has one of the most ambitious decentralisation programmes amongst developing countries. Decentralisation is central to Uganda's mode of governance as spelt out in the 1995 Constitution and the 1997 Local Governments Act confers.

The process of decentralisation is at the heart Poverty Eradication Action Plan (PEAP), which sets out the strategy through which the Government of Uganda (GoU) aims to eradicate absolute Poverty by 2017. The PEAP is implemented through the Medium Term Expenditure Framework (MTEF).

The GoU is a front runner in translating debt relief under the Highly Indebted Poor Country Initiative into increased financing for Poverty Reduction Programmes via the Poverty Action Fund (PAF). The combination of the PEAP/MTEF framework and the PAF resource transfer modalities have given donors sufficient confidence to provide a growing proportion of their aid as budget support.

As a result, over the past three years there has been an extraordinary rate of growth in social sector expenditure, with expenditures on PAF programmes growing from 17% to 34% of the Government of Uganda Budget. Due to Uganda's Decentralisation Policy, this has meant a rapid increase in resource flows to local governments, and a corresponding increase in primary service provision. As PAF expenditures are tied to the achievement of PEAP Goals, the majority of the increase in transfer of resources has been via an increasing number of conditional grants.

1.2 Fiscal Decentralisation Study

There has therefore been growth in the number and diversity of transfer mechanisms from central government and donors and this has been a matter of growing concern in both central and local government. Many of these mechanisms are not well adapted to the decentralised framework, with local governments given little real power over the allocation resources, and little involvement of lower level local governments in the decision making.

Problems with management and financial accountability have arisen from the profusion of different transfer systems and bank accounts. Line Ministries are faced with major problems in dealing with quarterly reporting from a growing number of conditional grants and a growing number of districts. In addition, there is concern about the different design and type of conditionalities under the Ministry of Local Government's (MoLG) Local Government Development Programme (LGDP) and the PAF conditional grant regulations, and the bureaucratic load of multiple procedures, bank accounts and lines of reporting.

It is against this background that the GoU commissioned the Fiscal Decentralisation Study to examine how to streamline and harmonise the present systems and processes of transferring resources to local governments. The Study was carried out in a consultative manner, involving central and local government institutions.

Following the completion of the Study in January 2001, the GoU convened a Working Group to examine the proposals for operationalising the recommendations in the Fiscal Decentralisation Study. The Working Group drafted this Fiscal Decentralisation Strategy Paper, which has had the input of all key stakeholders, including central government, donors and local governments

1.3 Objectives of the Fiscal Decentralisation Strategy

The objective of the Fiscal Decentralisation Strategy (FDS) is:

“To strengthen the process of decentralisation in Uganda through increasing local governments’ autonomy, widening local participation in decision making and streamlining of fiscal transfer modalities to local governments in order to increase the efficiency and effectiveness of local governments to achieve PEAP goals within an transparent and accountable framework”.

The focus of the strategy is therefore in two areas:

- ?? The promotion of local government autonomy and the widening of participation in decision making in order to enhance the efficiency in allocation of resources towards the achievement of PEAP Goals in line with local priorities.

This will be achieved by:

- Increasing the discretionary powers given to local governments in allocating resources towards both recurrent and development activities.
- Promoting increased participation of all levels of local government in the decision making process.
- Providing direct financial incentives for local governments to increase local revenue, and ensuring that local revenue contributes meaningfully to local development.
- Harmonising the central and local government planning and budgeting cycles to ensure that local needs and priorities do feed back into the national budget,

- ?? Improving the effectiveness of Local Government Programmes through strengthening the effectiveness, transparency and accountability of local government expenditures.

This will be achieved by:

- Streamlining the systems of transferring funds from the centre to local governments.
- Developing a strong framework for financial accountability and increasing the focus on book keeping.
- A simple system of reporting on financial and output information.
- Rewarding those local governments which implement programmes well, in adherence to the legal and policy framework, and sanctioning those which do not.
- A more co-ordinated, and better targeted system of monitoring and mentoring local governments by central government.

1.4 Fiscal Decentralisation Strategy Proposals

The Strategy Objectives will be achieved within the legal framework provided by the Constitution 1995, the Local Government Act 1997 and the Local Government Financial and Accounting Regulations 1998.

The Unconditional, Conditional, and Equalisation Grants will therefore remain the means by which central government fund local governments. These Grants will be channelled to local governments via two transfer systems, Recurrent Transfer System (RTS) and the Development System (DTS)¹. Within these systems the existing number of conditional grants will be reduced. The planning and budgeting for services under local governments will be more

¹ The proposals are solely concerned with Transfer Systems - how the three grant types specified in the Constitution are transferred to local governments. The FDS does not intend to change the Constitutional Requirements.

participatory, and local governments will have more flexibility in allocating resources from central government. The central and local government budget cycles will be harmonised to ensure that local government issues feed back effectively into the budget process.

During Budget Implementation, there will be extra focus on financial accountability, to ensure the provisions of the Local Government Financial and Accounting Regulations are adhered to. Local governments will prepare combined reports on expenditures and outputs for all recurrent expenditures together under the RTS and all development expenditures under the DTS.

This Strategy largely deals with the nature of new Fiscal Transfer Systems. In order to ensure the benefits of the new systems are fully realised, national sector policies will be reviewed to ensure that they are more flexible and make use of the Local Government Structures. These sector reviews are crucial to the success of the Strategy.

Policies will be developed which provide incentives to Local Governments to achieve sector goals, as opposed to exercising tight ex-ante controls, as is current practice under conditional grants. Overall the criteria for allocation of funds to Local Governments will be reviewed to ensure that they are more poverty focused, that they enable the achievement of sector goals and that there is a better balance between discretionary and non-discretionary funding. Central government institutions operations with local governments will be better co-ordinated, and they will be empowered to take on their roles under fiscal decentralisation as stipulated in the law.

As their capacity improves over time, the autonomy given to Local Governments in both allocating resources and implementation will be increased within the framework of the Recurrent and Development Transfer Systems. This will involve increasing the discretionary funding available to local governments via the Unconditional and Equalisation Grant, and increasing the flexibility local governments have over planning and budgeting for conditional grants.

2 THE RECURRENT TRANSFER SYSTEM

2.1 Recurrent Transfer System : The Concept

All unconditional and conditional grant transfers for recurrent expenditure will be made via a single Recurrent Transfer System (RTS). Transfers will be made on the basis of the annual Recurrent Transfer Budget.

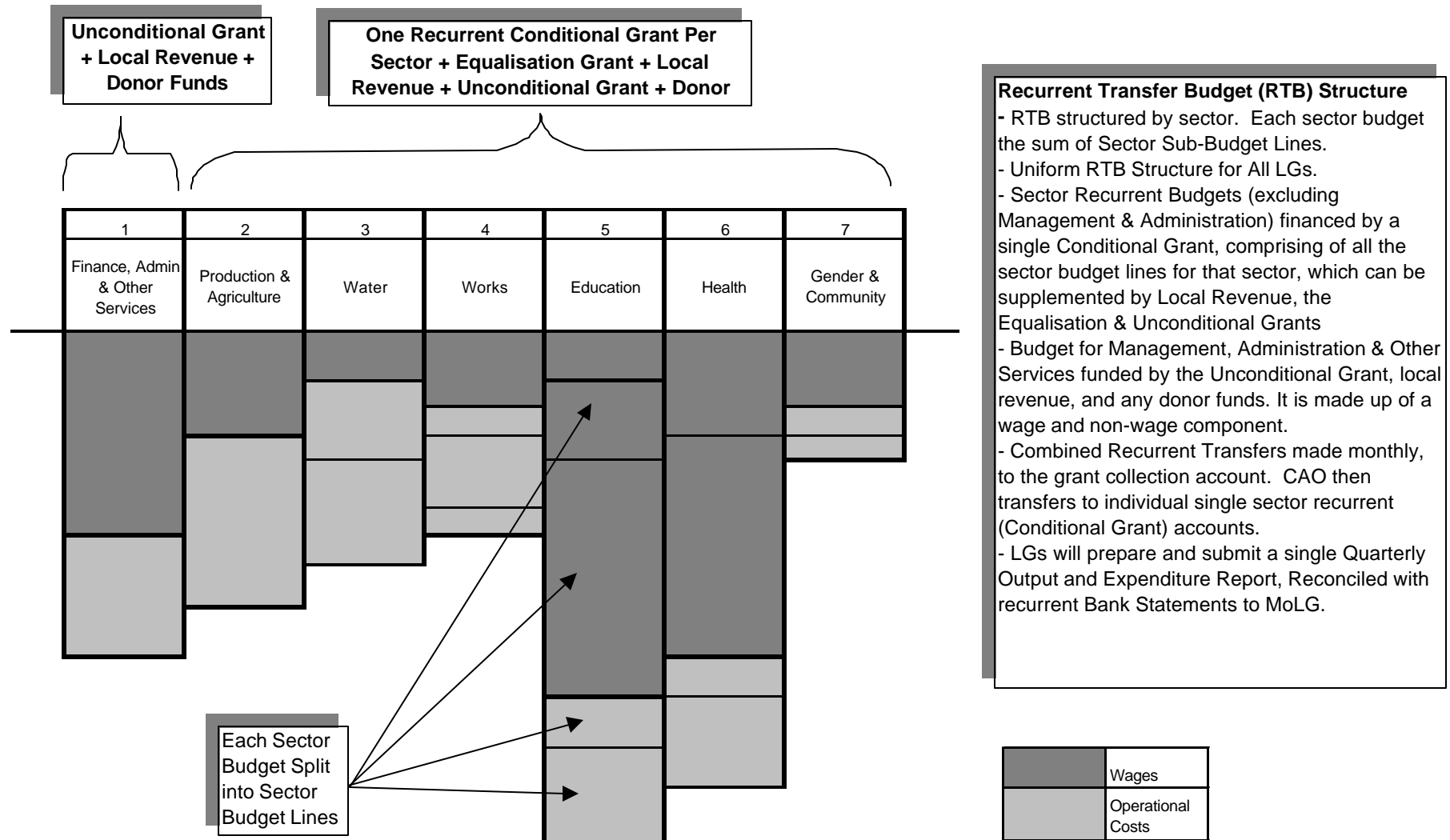
Local governments will be given some flexibility over the allocation of resources between and within sectors, within the Recurrent Transfer Budget. Flexibility will be increased over time as local governments' capacity and performance improves. This will enable local governments to ensure that allocations are made in line with local priorities, whilst ensuring the achievement of national poverty reduction goals.

2.2 The Structure of the Recurrent Transfer Budget

At the beginning of the budget cycle each District/Municipality will be presented with a draft Medium Term Recurrent Transfer Budget (RTB). This will have two important elements:

- The structure of the Local Governments Recurrent Budget
- Indicative budget ceilings for recurrent sector conditional grants from central government.

BOX 2A: LOCAL GOVERNMENT RECURRENT TRANSFER BUDGET



Local Governments will also be informed of the indicative ceilings for the Unconditional Grant and Equalisation Grant.

The RTB will be structured by Sector Budgets (e.g. health, agriculture, education etc). The Sector Budget is made up of the summation of sector budget lines. Each sector budget line will represent an expenditure area (e.g. primary teacher's salaries and primary capitation) within that sector. The recurrent sector budget lines will cover all expenditure areas in a sector in which Local Governments are mandated to deliver services, as provided for in the Local Government Act.

Each Priority Sector/Sub sector in the draft RTB will be funded by a single conditional grant, which can be supplemented by other sources of revenue. There will be no more than one conditional grant per sector. This conditional grant will fund all budget lines in a priority sector, or all priority sub-sectors within that sector. This means that the multiple recurrent conditional grants operating within a sector at present will be replaced by a single recurrent conditional grant for each sector, funding the budget lines. The number of budget lines will be kept to a minimum, and will be fewer than the current number of conditional grants

Finance, Administration and Non-Priority sectors/sub-sectors will not receive conditional grant funding, but will be funded from the Unconditional Grant (UCG), Local Revenue and any available donor resources. The UCG allocation provided by central government will be adjusted so it is, at least, sufficient to cater for all the Finance and Administration functions, but local governments will be free to spend it on any area.

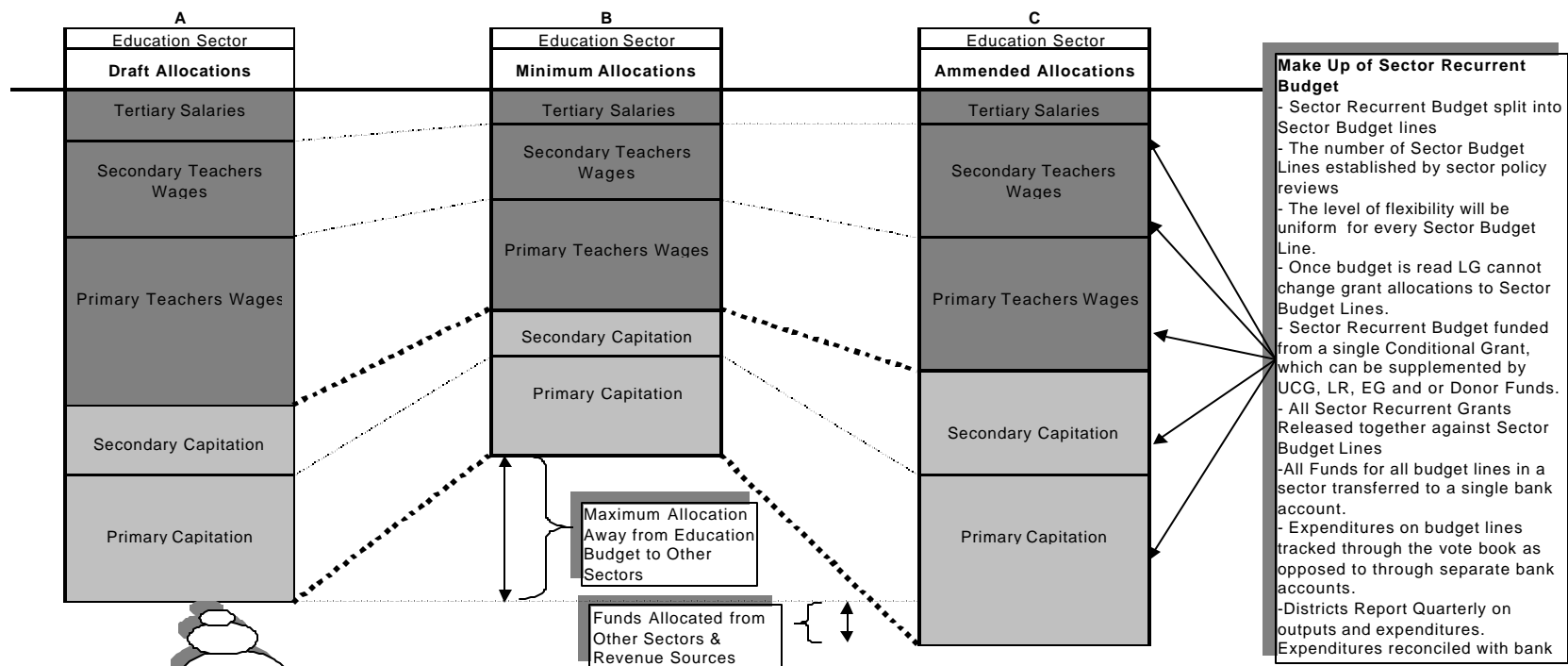
The Draft RTB will contain information about Conditional Grant allocations only. During the Budget Process, the local government will also allocate the equalisation grant, local revenue and/or the unconditional grant towards different sector budget lines as appropriate to supplement the conditional allocations from central government in the draft RTB.

The RTB format should also have a provision within it for the handling of emergency situations.

Implications :

- ?? Line ministries will need to review their policies for the recurrent aspects of local government service delivery to make them more in line with the provisions of the Local Government Act and the structure of local government. Policies should focus less on the fulfilment of ex-ante conditions and more on the provision of incentives to achieve national sector goals.
- ?? Sectors will need to identify all the recurrent activities involved in a local government delivering services in the sector, excluding those which are directly related to specific investments (investment servicing costs). All these activities, excluding the finance and administration function should be catered for in the Sector Recurrent Budget. This will include activities funded by the current conditional grants, and any recurrent activities being funded under any development activities.
- ?? Sectors will need to review the number of recurrent conditional grants currently operating with a view to establishing the minimum number of sector budget lines, which give an optimal level of flexibility to local governments when allocating funds, whilst promoting the achievement of sector goals.

BOX 2B: SECTOR BUDGETS WITHIN THE RECURRENT TRANSFER BUDGET



Revision of Sector Allocation Formulae - As part of the sector policy review process allocations need to be revised to reflect the following factors to ensure equitable distribution of resources:

- Funding of all priority sector recurrent activities
- Achievement of national service delivery standards
- Cost of Delivering of Services in different areas

Flexibility in Sector Recurrent Sector Budget Allocations

A. Draft RTB Allocations are prepared by central government at the beginning of the budget cycle and distributed to LGs; allocations to sectors and sector budget lines based on recommended levels of service delivery given overall resource availability.

B. Minimum Allocations permissible for a sector grant by the LG are set by central government at the beginning of the budget cycle and will be a fixed percentage of the Recommended allocations. LGs, if they went through a consultative budget process in the previous year, are free to allocate from one sector budget line to another within a sector, and/or away from one sector recurrent budget to another (excluding Management & Admin.) provided the minimum allocations are met for each sector budget & sector budget line, and the total recurrent transfer budget (the sum of all sector budgets) remains unchanged.

C. Amended Allocations to sector grants are prepared by the local government as part of their LGBFPS during their budget process. These include additional allocations to sector (budget lines) from other revenue sources. If the allocations are below the minimum permissible the amended allocations will be rejected and the Draft Allocations recommended by central government will prevail.

2.3 Sector Conditional Grant Allocations

The allocation of funds conditional grant funds to priority sector budget lines within the sector budget in the draft RTB will be based, as far as possible, on the actual cost of delivering recommended national levels of services for each sector agreed between central and local government, given the resources available.

Implications:

- ?? Sectors will need to establish the costs for local governments to deliver different levels of services. If sector grant allocations are to be made on the basis of the cost of delivering uniform levels of services countrywide, the allocation formulae will need to take into account the varying costs of delivering services in different areas of the country.
- ?? Sectors, in collaboration with the other members of the Local Government Budgets Committee (LGBC – see section 4) will need to establish national standards for service delivery, if they have not already done so. This exercise, which is currently being coordinated by MoLG should be expedited.

2.4 Flexibility Within the Draft RTB

As recurrent expenditure needs are mainly determined by national sector policies, there is limited scope or demand from Districts/Municipalities to change allocations at present. However it is important that they be given the opportunity to amend their draft RTB allocations in the light of local priorities.

Therefore, a Local Government will be allowed some flexibility to alter the levels of conditional grant funding to different sector budget lines in line with agreed parameters, and reallocate the difference within sector or between sector grant allocations in the RTB, so long as the overall allocation to that Local Government for all conditional grants in the RTB is not exceeded.

At the time the draft RTB is disseminated, Local Governments will be informed of recommended and minimum conditional grant allocations to sector budgets and sector budget lines. The minimum allocations will define the amounts by which local governments can change the recommended sector grant allocations provided to them. Local Governments will be free to supplement the sector grant allocations with the equalisation grant, the UCG, local revenue and/or donor funds.

The minimum allocations will be a pre-agreed fixed percentage of the recommended allocation, uniform across all sectors and sector budget lines. Before the beginning of each budget process the LGFC and MFPED, under the umbrella of the LGBC, will agree the percentage flexibility with local governments and/or their Associations.

2.5 Local Government Amendments to draft RTBs

Local Governments will then conduct their consultative Budget Process, where local needs and priorities are discussed in the context of the resources available under the RTB. Fora like the Budget Conference, Sectoral Committee Meetings, and Executive meetings should be used. The exercise of preparing Local Government Budget Framework Papers will be important in helping local government allocate resources according to these needs and priorities.

On the basis of the consultations the Local Government will then propose amendments to the sector grant allocations in the RTB, and the distribution of the Equalisation Grant, Unconditional

Grant and Local Revenue. The Sector Grant amendments should be highlighted in the LGBFP, which should first be passed by the Council Executive before being submitted to Central Government.

Central Government will accept the amendments to the sector conditional grant allocations in the RTB if:

?? The Total of **all** Sector Grant Allocations in the RTB has not been exceeded.

?? No allocation to a sector/sector budget line is below the minimum limit.

Otherwise the allocations in the draft RTB will prevail. The Sector Budget Lines within the RTBs from all local governments will then all be summed and re-integrated into the MTEF. These allocations will be submitted to Cabinet as part of the national Budget Framework Paper.

As part of the national performance assessment of Local Governments (see section 5.3), the budget process undertaken of each district/municipality will be assessed to ensure the legal requirements have been met. If they are not met, a district/municipality will not be able to make amendments to the recommended grant allocations in the RTB in the following financial year. In addition, those local governments that perform well in terms of both budget preparation and implementation will have the amount of flexibility available to them increased over time.

In theory, the freedom of Districts/Municipalities to propose inter-sector variations threatens to disturb the pre-agreed sectoral allocations for the budget within the MTEF. However, the net size of such changes (across all Districts/Municipalities) is likely to be small, and would probably be accommodated within the rounding-off of the national estimates. If net District/Municipality proposals clearly imply that the national sectoral allocations required amendment, the LGBC will be in a position to pursue this further, using the national BFP as an entry point.

For example, there is currently concern within Districts that the operational budgets available to agricultural extension workers are too small to enable the newly recruited staff to be effective. If most Districts were to propose reallocation into the agricultural operational costs sub-budget, this would be a sure sign to the centre that the national sectoral allocations required amendment.

Implications:

?? The Local and Central Budget Processes must be harmonised to ensure that local governments produce their amended RTBs in time to be integrated into the MTEF before the national BFP is presented to Cabinet in early March. (See Section 5).

?? Sectors and those donors providing sector support must be prepared to accept the amendments which Districts/Municipalities make if they have substantial macro implications to the sector allocations.

2.6 Transfer of Funds

Transfers would be made monthly, via the grant collection account to the District/Municipality Recurrent Sectoral accounts, against sector budget lines. Local Governments will provide quarterly expenditure reports, reconciled with the RT bank account statement/sectoral bank account statements, together with simple output monitoring reports to the Ministry of Local Government. This is dealt with in more detail in Section 6.

2.7 Increasing Local Government Autonomy over time in the RTB

It is important that those Local Governments, which make progress in strengthening their own capacity, should be subject to fewer central government controls. The Recurrent Transfer System provides a framework for increasing the autonomy local governments have over allocating resources and in implementation, as local governments' capacity increases over time.

There are two main ways this can be done within the context of the RTB and RTS:

- ?? Firstly, an increasing proportion of local governments RTB can be provided as discretionary funding in the form of the unconditional and equalisation grant.
- ?? Increased autonomy in budgeting for Sector (Conditional) Grant Funds within the RTB. The minimum sector budget and budget line allocations can be withdrawn. Local governments would be provided with a Total Recurrent Sector Grant Budget, and Local Governments would propose allocations to Sector Budget Lines during the budget process.

A gradual reduction of central government control will be linked to improvements in capacity and performance of individual local governments. This will allow an incremental movement towards a future budgetary planning system whereby Districts/Municipalities propose their recurrent transfer requirements at an earlier stage in the budgetary process, with the national budget and sectoral allocations built-up more from local government proposals.

2.8 Benefits of the Recurrent Transfer System

The introduction of a single system for recurrent transfers will strengthen local governance, accountability, transparency and service delivery as follows:-

- a. International practice : The RTS (and DTS) is in line with international practice, whereby transfers are budgeted and released together, rather than as separate sub-sectoral items
- b. Flexibility within sectors: LGs will have more flexibility within national policy to allocate money within sub-sector budgets according to local priorities. Over time, as management capacities and other systems develop, the number of sector sub-budgets can be progressively reduced, to the point where there is a single conditional recurrent transfer budget line per sector. Later, as confidence in the management of local government develops, it will be possible to remove sectoral divisions, and the recurrent transfer will increasingly become an unconditional (or much less conditional) grant.
- c. Flexibility between sectors: LGs gain the important freedom to amend allocations in the light of local priorities, before the recurrent transfer budget is finalised, increasing Local Governments autonomy over the allocation of resources.

3 THE DEVELOPMENT TRANSFER SYSTEM

3.1 Development Transfer System– The Concept

The concept of the Development Transfer System (DTS) is similar in many ways to that of the proposed Recurrent Transfer System. All development transfers to local governments will be made within a single DTS based on the annual Development Transfer Budget (DTB).

Emphasis will be placed on establishing a system of integrated, bottom up planning for all local development activities whether funded by Sectoral Grants or Discretionary Grants. The systems being implemented under the Local Government Development Programme will also be mainstreamed within the DTS.

3.2 The Development Transfer Budget Structure

At the beginning of the Budget Cycle, Local Governments will be provided with a draft DTB. The DTB will be divided as follows:

- ?? The Local Development Grant Budget, providing discretionary development financing to lower local governments using LGDP modalities.
- ?? Sector Development Grant Budgets, providing funds for specific sectoral investments, whose guidelines are reviewed to make them more in line with LGDP modalities.

This structure will be agreed with Local Governments early before the beginning of the budget cycles. The Draft DTB will provide indicative ceilings for the medium term. Different Levels of Local Government will be given the responsibility for planning for a specific proportion of the sector grant allocation (which will vary from sector to sector), and this will be indicated in the DTB structure.

The discretionary LDG should provide adequate flexibility for the local governments to ensure that, overall, investments are made in line with local priorities, provided that the correct balance of allocation of funds between sector development grants and the LDG in the DTB is found.

3.3 The Local Development Grant

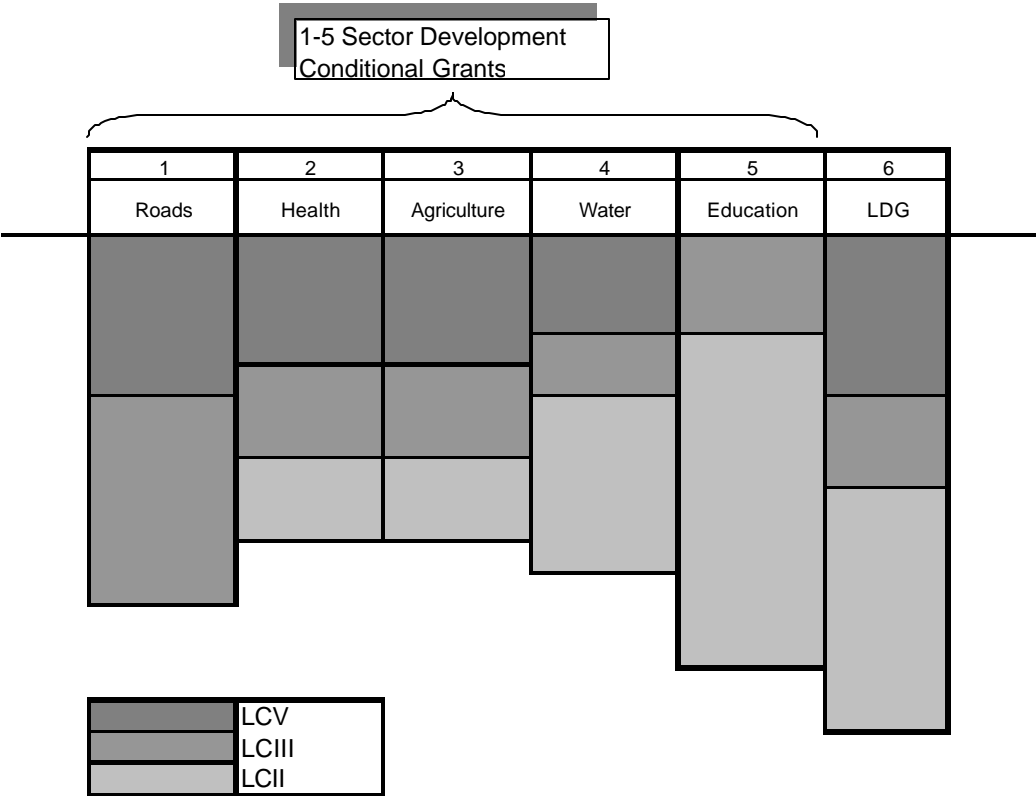
3.3.1 The LGDP Modalities

In 1995, GoU reached agreement with IDA and UNCDF to pilot devolution of discretionary development budget support to 5 Districts through the District Development Project (DDP). This was designed to test the anticipated Local Governments Act and create a “policy experiment” for developing procedures for decentralised planning, financing and service delivery. The experience of the DDP formed the basis for design of the Local Government Development Programme (LGDP) which is devolving development funds through the Local Development Grant (LDG) and Capacity Building Grant (CBG) to 31 districts and 13 municipalities.

3.3.2 Overview of LDG Modalities

The LGDP approach combines building good local governance with the implementation of development investments. LGDP provides a non-sector specific development grant, the LDG to LGs according to transparent formulae. As part of the national DTS, the LDG will be the source of discretionary financing to local governments, and the sector development grant modalities will be revised to be more consistent with the LGDP approach.

BOX 3A: LOCAL GOVERNMENT DEVELOPMENT TRANSFER BUDGET



Development Transfer Budget (RTB) Structure

- DTB made up of sector budgets, and then the discretionary Local Development Grant. (LGDP)
- Each sector budget composed of a proportion allocated to LCV, LCIII & LCII for planning purposes, which varies from sector to sector.
- The LDG, which is discretionary can be used to top up sector grant activities or fund other activities, depending on community preferences. The share of the Equalisation Grant Allocated towards development expenditure will supplement the LDG Budget.
- Sector Development Budgets financed by a single Conditional Grant whose allocation is fixed, and any additional resources allocated from the LDG.
- Combined Development Transfers made monthly, to the grant collection account. CAO then transfers to individual single sector development (Conditional Grant) Accounts.
- LGs Will Provide Integrated Quarterly Expenditure Reports, Reconciled with Bank Statements, and output reports to MoFPED.
- Reporting on sector outputs financed by LDG integrated with those financed by sector grants.

LGs qualify to access the LDG once they have achieved specified minimum access criteria. These criteria are derived directly from the requirements set out in the Local Governments Act 1997 (LGA) and the Local Government Finance and Accounting Regulations 1998 (LGFAR). LGs are required to co-finance the development funds received with 10% contribution in cash, in addition to schemespecific local contributions from communities.

Central to the LGDP design are the annual assessments of districts/municipalities, sub-counties/divisions and town councils against the pre-set governance criteria (the so-called 'minimum access conditions') and performance criteria. The '*minimum conditions*' determine whether a District/Municipality or a sub-county is eligible to access the Local Development Grant. The *performance criteria*, assessed in retrospect, determine whether a local government is eligible for a reward or penalty (i.e. whether the amount of the Development Fund is to be increased or decreased for the next financial year).

The minimum conditions (access criteria) include:

- ?? Development planning capacity (e.g. availability of a council-approved District Development Plan and functional planning committees.)
- ?? Financial management (e.g. proper maintenance of accounts, adherence to procurement regulations.)
- ?? Technical capability (e.g. capacity to supervise engineering works)
- ?? Programme specific conditions (e.g. 10% co-financing)

Districts/Municipalities which do not meet the minimum access criteria can still benefit from the Capacity Building Grant (a separate funding-line under LGDP) in order to assist them qualify for development funding in future.

Districts/Municipalities and sub-counties operate under incentive and penalty system linked to good governance and service delivery. Those that perform well against specified performance criteria receive an increase in their allocations in subsequent years (an additional 20%), whilst those which perform poorly have their investment funds reduced by 20%.

3.3.3 Investment menu

Under the LDG all service delivery functions within the LG Act Schedule II part 2 - with the exception of security - are eligible for funding. Local Governments can choose to fund activities outside the PEAP priorities - such as council buildings - but if expenditure on non-PEAP-priorities exceeds 20%, this leads to sanctions in the form of decrease in allocation in subsequent years. The investment menu is mainly capital items, but some recurrent expenditure is allowed as long as it is related to investment and is less than 20% of the total budget².

LGs are authorised to use the investment fund for investment planning and monitoring ('investment servicing costs') up to a maximum of 15% of the total fund. The use of LGDP funds appears unconditional in that funds are not tied to a specific sector, but LGs have to adhere to the overall planning procedures and co-funding rules. Importantly, they must meet the annual minimum criteria and performance criteria.

² The DDP-LGDP-PMU is currently working on appraisal criteria manuals to guide local councils for public investments and for activities in the agricultural sector, particularly in relation to the more difficult private-goods area. DDP-LGDP also has a 'negative list' of activities which are not eligible for funding (e.g. income generating activities for LC3 councils).

3.3.4 Allocation of Funds Between Levels of Local Governments

Box 3B: The Local Development Grant & Sensitivity PEAP Goals

Because LGDP incentives prioritise investment in PEAP priorities 3 and 4, LGDP investments are in practice, in exactly the same sectors as those funded by the sector Conditional Grants: Education, Health, Water, Roads and, to a lesser extent, agricultural production. This is clear from the following table which sets out the actual sectoral allocations, resulting from the LG and community-driven scheme selection process in the 5 DDP districts.

Use of Investment Funds by sector and main activity 1998 - 2000

Sector	Allocation	Examples
Education	43.7%	/// Class room construction /// Teachers houses /// Desks and furniture /// School library
Roads	14.8%	/// Opening of small roads /// Culverts
Health	27.7%	/// Construction of health units at parish and Sub-county level /// Mattresses, beds and furniture for Health units /// Staff housing (grass thatched huts)
Water	8.5%	/// Gravity flow schemes /// Protected springs /// Borehole rehabilitation /// Rain water harvesting for institutions /// Institutional latrines /// Water for cattle
Production	4.1 %	/// Cattle markets (Kotido) /// Improved seeds/crops for multiplication /// Improved livestock for multiplication (heifers & rabbits in Kabale)
Other	1.2%	/// Environmental protection through tree planting. /// Sub-county office blocks /// Cash Safes for Sub-counties

1) Team calculations from DDP raw data on actual outputs in five Districts and their Sub-counties. Actual allocation of LDF in FY 1999/2000. Total budget allocation was UGS 3.9 bn.

Under LGDP the LDG is simply allocated according to population. LGDP is designed to promote planning and implementation capacities at all levels of local government and to involve the whole community in scheme selection and prioritisation. 65 per cent of all LDG funds to districts is channelled through sub-counties, with allocation across the sub-counties normally following the population-and-area formula. 30 per cent of the sub-county budget allocation is provided as an indicative planning figure (IPF) for parish level planning, with the allocation based on population. Parishes are required to involve villages (LC1s) in their scheme selection process.

3.3.5 LDG Planning and budgeting procedures

Allocation of funds to local governments is based on an objective formula (adjusted for the previous years performance) and local governments budget within this financial limit. Planning at District/Municipality, sub-county and parish level therefore takes place within a clear budget limit and stakeholders at District/Municipality, sub-county and parish levels are fully informed about their budgetary entitlements.

Districts/Municipalities and sub-counties must have a 3-year rolling development plan in place, and expenditure under LDG has to be in line with council-approved annual plans. Within their budgets, sub-counties have discretion and do not require approval of plans by the District/Municipality. However, sub-counties have to adhere to required procedures to ensure

both technical quality and that recurrent cost provision is available, notably in relation to clinic and school construction.

No project-specific "LGDP planning guides" have been developed. The national guides for district development planning (issued by the Decentralisation Secretariat since 1996) and the technical guidelines from line ministries are used. However, since investment planning at sub-county level was a new concept in 1997, an *"Investment Planning guide for Sub-counties and lower Level councils"* was specially produced. This manual was issued May 1998 by the MoLG as the national planning guide for sub-counties.

The MoLG has also issued the "five little blue booklets" which explain how the LDG works and how each level of LG can access it. Another booklet explains the fund for capacity building activities and a Financial Management Guide has been produced under Regulation 4 of the LGFAR.

3.3.6 ~~Sanction/reward mechanisms for performance~~

The annual assessment exercise is the key modality in DDP-LGDP to ensure LG compliance with national regulations. The performance criteria include :-

- ?? Gradual improvements in the quality of plans;
- ?? Improvements in quality and timing of financial accounts and reports;
- ?? Improvements in technical implementation (O&M, timely completion of investments);
- ?? More participatory planning;
- ?? The poverty eradication focus of council plans;
- ?? Maintenance of databases, monitoring systems and record keeping;

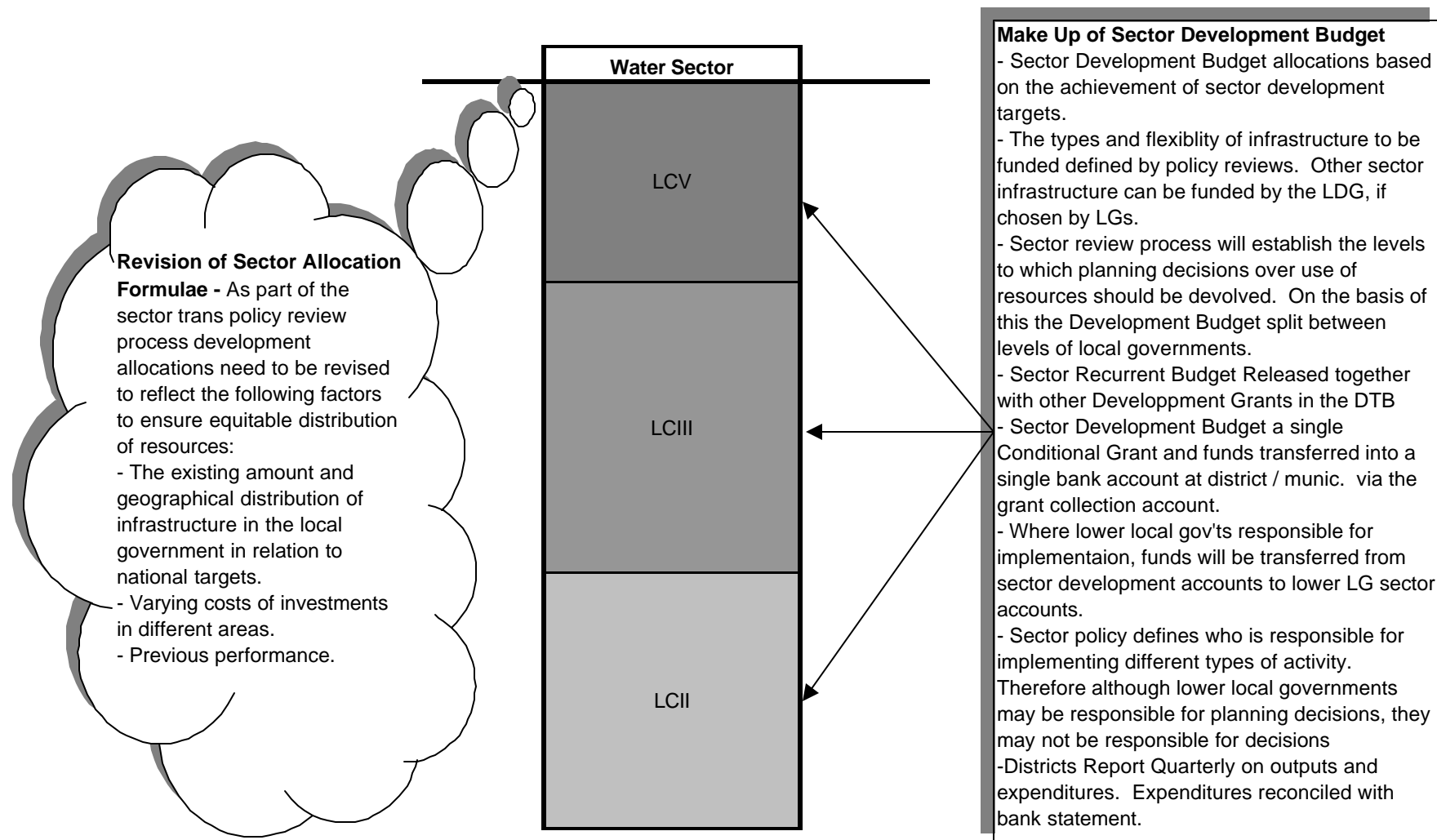
Performance is measured in terms of relative improvement over time, thus driving continuous up-grading in LG capacity. In short, the performance bar is raised each year. The annual assessment of the lower LGs is done by the District/Municipality. A MoLG-led team assesses districts and a sample of sub-counties. The assessment exercise for the FY 2000/01 (in November 2000, due to the delayed start of LGDP) included all local authorities in the country, including LGDP, DDP and bilateral-supported districts.

The precise modalities for the assessments are annually updated and specified in the assessment manual. Once they have achieved the annual minimum-conditions, LGs receive funds quarterly, and further releases depend on receipt and approval of statements of accountability for the previous-but-one quarter.

3.4 Sector Development Budgets and Integrated Planning for LG Investments

At present sector development grant modalities tend to use very different decision making mechanisms, and implementation modalities from the LDG at the local level, and these mechanisms often bypass some lower local government structures. In particular, planning for development activities locally is, at best, fragmented. Subcounties and Parishes are only given planning figures for the LDG, and the sector grants have separate planning procedures.

BOX 3C: SECTOR BUDGETS WITHIN THE DEVELOPMENT TRANSFER BUDGET



Under the DTS sector modalities will be harmonised and brought in line with the provisions of the Local Government Act, and LGDP. The planning for sector development grants and the LDG will be integrated at every level. As stated before at the District/Municipality level the DTB will bring together the allocation of the LDG with the sector grants.

As with the LDG the budget each Sector Development Grants will be divided into “shares” for LCV, LCIII and LCII for planning purposes³. On the basis of clear allocation criteria these grant shares will be divided between the individual LCIIIs and LCIIIs in the district/municipality. The lower local governments will then be provided these allocations for all grants simultaneously in the form indicative planning figures for the medium term.

Implications:

- ?? Sectors will need to review their policies for the provision of LG investments to ensure that they are in line with the Local Government Act. In doing so, elements from LGDP, such as the provision of incentives for good performance, minimum access conditions for sector grants and mandatory local contributions, will be mainstreamed into sector development policies and guidelines.
- ?? The optimal shares between different level of local government will depend on the sector and where it is best for decisions to be made. Sectors will need to establish these divisions, in consultation with local governments, the LGFC and MoLG under the LGBC.

3.5 Bottom up Planning Process

Subcounties and Parishes will therefore be provided with a budget ceiling (indicative planning figure) for each sector grant and an allocation for the LDG. The allocation for the sector grant would be the minimum a community could invest in a given sector, whilst the LDG allocation is discretionary. Parishes would first identify the investments they wish to carry out over the medium term in the sectors, and then identify activities to be funded by the LDG. If a parish thinks the allocation from a sector grant is inadequate, it will have the opportunity to undertake any supplementary activities in that sector using funds from the LDG, or identify totally new activities. The parish will also articulate priorities, which could be funded out of the subcounty shares or higher.

The Subcounty will then collect and compile all the parish plans. Taking into account the investments identified in the parish plans and it will allocate its share of the grants to activities. Similarly the district/municipality will compile all the Subcounty plans and identify further activities. The activities identified by the subcounty and District/Municipality can address important issues of “join up” in sectors such as roads and health where and investment will serve more than one parish or subcounty.

Implications:

- ?? Sectors will be required to develop planning guidelines within the framework of the DTS for lower local governments, to guide lower LGs in making sector investment decisions and to ensure those decisions are made in line with national sector policies.

³ This may be different from the funds transferred to the LG, which will depend on the level of LG responsible for implementation.

[illegible]

- 1. Central Government Provides** Districts/Municipalities with a draft DTB which gives sectoral allocations and an allocation to the local Development Grant, and the breakdown between different levels of Local governments.
- 2. The District/Municipality Distributes** indicative planning figures to all LCIIIs for all sectors simultaneously. These include the LCIII/LCII breakdown.
- 3. The LCIII then distributes Indicative** Planning figures to the LCII
- 4.& 5. The LCII holds consultative** planning meetings to discuss the use of development funds. The LCII identifies investments to be made using sector grant funds and the LDG funds. The LDG funds are discretionary & may be allocated towards supplementing investments funded by sector grants or other activities. The LCII submits its Development Budget, and workplan to the LCIII.
- 6. The LCIII then compiles the LCII** workplans. Taking into account the decisions made by the LCII, the LCIII identifies activities for the use of the LCIII sector and LDG grant shares.
- 7. The LCIII submits its Development** Budget, and workplan to the District / Municipality. The District / Municipality compiles all the LCIII workplans and then, on the basis of the LCIII decisions made, allocates its sector and LDG grant shares. The entire DTB is submitted to council for approval before being forwarded to central government.

3.6 Local Contributions

At present the only major grant which currently requires that there be a contribution from local revenue towards investments is the Local Development Grant⁴. It is important to promote local ownership and ensure the sustainability of local government investments, that local contributions are made mandatory for all centrally funded activities.

Therefore for all local government investments a uniform contribution from local revenue will be required for all sector development grants in a local government as well as the local development grant. Investments will not be allowed to commence until the local contribution has been deposited in the relevant Bank Account. The policies for contribution in kind will also need to be reviewed and harmonised.

It is important that modalities for establishing the level of local contribution are carefully considered before they are implemented. Contribution levels must be affordable to local governments, to ensure that investments do take place, whilst sufficient to engender local ownership, and encourage local revenue raising. It may be necessary to vary the levels of contribution across local governments on the basis of an index relating to poverty/ability to pay.

Implications:

- ?? A common policy on local government contributions will need to be developed for all investments, and this will need to be integrated into the lower level planning process.
- ?? The optimal level of contribution, which should be the same across all the sector development grants (but not necessarily local governments), will need to be established. A study will need to be carried out to establish the common policy and the optimal levels of local contributions.

3.7 Recurrent Implications of Development Activities

In sectors where there are substantial recurrent budget implications for making investments (e.g. building of a new school or health centre) then simple procedures will need to be put in place for approving such investments. The relevant district/municipality department will be required to approve/rejects the proposed sector investments on the basis of the medium term RTB allocations.

3.8 Review of Development Transfer Budget Allocation Formulae

Overall the allocations formulae for grants in the DTB should both promote the achievement of sector targets, but also be poverty focused. The allocation formulae will need to be reviewed holistically to ensure this is the case.

Specifically, allocation criteria for sector grants should be clear and should promote and provide incentives for the achievement of sector targets (e.g. classroom : pupil ratio for SFG, safe water coverage, etc ...). Therefore sector allocations will need to take into account factors such as expenditure needs, the varying costs of delivering services in different areas, and the need to provide of incentives for good performance. The investments allowed under sector grants should be limited to key sector infrastructure such as classrooms or health centres.

⁴ A contribution from local revenue amounting to 10% of the Local Development Grant Allocation is required before investments can take place. The PMA and NAADs grants which are currently being piloted also require local revenue contributions.

The LDG should be able to take care of other sector priorities such as doctor's houses, headmasters' offices, latrines etc.

The LDG allocations, which is currently only based on population, should be reviewed to make them more poverty focused.

Implications:

- ?? Sectors will need to review their sector development grant allocation formulae to ensure they take into account the above factors.
- ?? Any recurrent aspects currently being funded at present through a sector development grant, bar those investment servicing costs directly associated with undertaking an investment, will need to be funded from the RTS.

3.9 Minimum Access Conditions and Performance Criteria

For the LDG the current minimum access conditions, and performance criteria will continue to be assessed during the national assessments, as will the criteria for sanctioning and rewarding LGs.

In addition, basic minimum access criteria will be developed for other development grants. There will need to be a process to define these criteria carefully, and it must be emphasised that these criteria will only be basic legal requirements that are needed for planning and accounting for funds (these probably will not be as stringent as the LDG criteria). These may include:

- ?? Updated DDP in place
- ?? Final Accounts Written and Published for previous financial year
- ?? Quarterly Internal Audit Reports
- ?? Functional Engineering Capacity

The benefits of developing and applying minimum access criteria to lower local governments (e.g. sub-counties) will need to be investigated as well.

3.10 Capacity Building Grant

It is important to note that all LGs will be able to access the Capacity Building Grant (CBG) regardless of whether they meet the minimum access criteria for sector development grants and LDG or not.

The CBG will allow LGs to address specific gaps in their own capacity identified in the national Local Government Assessments (see section 5.3). This will enable them to upgrade their capacity so they can access grants in future and/or improve implementation. Central Government, especially the Ministry of Local Government, will have an important role to play in supporting local governments address their weaknesses in capacity.

3.11 Transfer of Funds , Reporting and Accountability

Transfers would be made quarterly, via the grant collection account to the Local Development Grant bank account and sectoral development accounts. Districts/Municipalities will provide quarterly expenditure reports, reconciled with the DT bank account statement/sectoral bank account statements, together with integrated output monitoring reports. This is handled in more detail in section 7.

3.12 Evolution of the DTS – Merging Sector Development Grants into the LDG

Over time, the aim is to increase the discretionary funding available to local governments, in order to promote greater autonomy. Therefore, if it proves an efficient and effective mechanism for delivering investments at the local level nation-wide, the Local Development Grant should eventually become the unique methodology for local government development activities within a unified DTS. This would mean that all LG development expenditure funded by central government will flow via the LDG. Implementation of a DTS with a single LDG would, necessarily require the merging of the sector development conditional grants mentioned above being merged into the Development Transfer System. This could be done in one of two ways:

- ?? Increasing the proportion of funding available to local governments from the LDG relative to sector development grants over time.
- ?? For those Local Governments which demonstrate they have strong capacity, collapsing sector the grants into the LDG at one go.

3.13 Benefits of the Proposed DTS

1. Allocative efficiency : The experience of the DDP shows that LG investments are more directly attuned to local priorities and locally available resources and there is a visible and marked difference in the existence and quality of sub-county plans compared with non-DDP districts. Over time, the DTS should further reinforce this, by ensuring that all local investments use are planned for in an integrated manner from the Parish level up..
2. Political Accountability : DDP has shown that, as a result of discretionary budget support, councillors are able to engage in meaningful participatory planning and investment. The DTS will involve politicians at every level in making investment decisions in all areas, which will further strengthen this.
3. Horizontal accountability : Having been involved the decision making process for all local investments, the assertiveness of councillors to hold officers to account for their investment management processes (which has been demonstrated under DDP) will increase.
4. Sustainability : A common policy for local government contributions, combined with an inclusive planning process should enhance local ownership of investments, and therefore improve their sustainability.
5. Efficiency in Implementation: The application of minimum access criteria and incentives for good performance, in line with LGFP modalities, should help improve the value for money and quality of investments being made.
6. Achievement of National Sector Targets : the maintenance of sector development grants will help ensure that, a priori, funds are being allocated towards the achievement of sector targets.

4 THE ANNUAL PLANNING AND BUDGETING CYCLE

4.1 Introduction

It is important that the Local and National Budget Cycles be harmonised, and that the local governments' budget process does give feedback and impact upon the National Budget, whilst both budget cycles are in line with the provisions of the Budget Act 2001. It is also important at the local level that planning and budgeting are integrated in local governments. This will involve linking the process of updating DDP with the preparation of LGBFP. The process outlined below outlines how the RTB and DTB process would contribute to such an harmonisation.

4.2 Local Government Budgets Committee

There is need for a more coordinated and systematic management of the Local Government Budget Process by central government. There is also no forum at which local governments can formally discuss budget related issues with central government. There also needs to be more meaningful negotiations with local governments on the allocation of funds.

A Local Government Budgets' Committee (LGBC), chaired by the Local Government Finance Commission, will be formed. The LGBC will be made up of the LGFC, MoLG, MoFPED and Key Sector Ministries and Local Government Associations.

The LGBC will be responsible for:

- The negotiation and agreement of allocation formulae and grant conditions between sector ministries and local governments.
- The identification of issues for inclusion in the National Budget Framework Paper from analysing of Local Government Budget Framework Papers.
- The advice on and acceptance/rejection of amendments to conditional grant allocations within the RTBs.
- Overseeing the performance of the Comprehensive Local Government Assessments.
- Overseeing the coordination of Local Government Capacity Building by Donors, Central Government and Local Governments.
- Overseeing the coordination of donor support to Local Governments/ Decentralisation.

It is important that the LGBC engages the management of the involved ministries in the decisions relating to local governments at a high level. Therefore the LGBC is made up of senior staff from its constituent organisations. The members must be prepared to contribute to the work of both the setting up and running the RTS and DTS; to ensure that their own institutions contribute on time and in the right way; and to obtain the necessary clearances and approvals from their own institutions.

The LGBC will report, and make recommendations to, the proposed PEAP Support Committee, on key policy issues relating to local governments, which will be made up of the Permanent Secretaries of the key ministries involved. During the Budget process the Chairperson of the LGBC will report to the Permanent Secretary, Secretary to the Treasury, MFPED on all agreements made with local governments which have financial implications on the national Budget, to seek his clearance of those agreements.

The LGBC will also be responsible for ensuring that the conditions and guidelines associated with conditional grants, the RTS and DTS are agreed with Local Governments and consistent with the legal framework for decentralisation before they are implemented. No funds will be channelled to LGs by MFPED until the LGBC has cleared the associated conditions and guidelines.

4.3 Comprehensive National Local Government Performance Assessment

It is important that the annual assessments under LGDP, currently carried out by the LGDP-PMU, are institutionalised into the national processes.

In early September the Central Government, led by the Ministry of Local Government, and with representatives from the different member institutions of the Local Government Budget Committee (LGBC), will carry out a comprehensive assessment of Local Government performance in the previous financial year.

This will aim to verify LG compliance with the overall legal and policy framework, and also sector policies and guidelines. In doing so, the following will be ascertained for each district municipality :

- ?? Whether it meets the minimum access conditions and therefore should qualify for each Sector Development Grant and the Local Development Grant in the following financial year.
- ?? The rewards/sanctions that should be given to the Local Government, in terms of increasing / decreasing the following FYs Development Grant allocations in the following financial year.
- ?? Whether the legal requirements for the Local Government Budget process were met and therefore whether a local government should be allowed to amend the sector grant allocations in the RTB.

This will therefore impact on the recurrent and development grant allocations in the DTB and RTBs for the following financial year. This Assessment should be completed by mid October, so that it can feed into the sectoral-review processes and the forthcoming budget process.

4.4 Establishing the RTB and DTB formats, Allocations and Flexibility

In late September, whilst the LG Assessment is going on, the LGBC will hold consultations with local governments to discuss the following;

- ?? Issues relating to Implementation, Sector Policies and the Budget Cycle,
- ?? The RTB and DTB formats,
- ?? Allocation formulae for all grants,
- ?? Percentage flexibility of conditional grant allocations to recurrent sector budgets and sector budget lines.

The LGFC and sector ministry representatives will need to take a leading role in these discussions.

Taking into account the discussions, the LGBC will then negotiate and agree the following with the Local Government Associations:

- ?? the allocation formulae,
- ?? RTB and DTB formats, and
- ?? the level of flexibility for recurrent grants.

The issues resulting from the consultations with local governments will be presented at the National LGBFP Conference in November, so that they can be incorporated into the national budget process. Any Local Governments unhappy with the agreed formulae will have opportunity to raise these concerns at the Conference.

4.5 Providing the Draft RTB and DTBs to Local Governments

Once the allocation formulae have been established, the comprehensive national Local Government Assessment has been finished and the available resource envelope established, the LGBC will enter actual recommended transfer amounts into the RTB and DTB formats for each local government. The Draft RTBs and DTBs will be disseminated to Districts/Municipalities at the time of the first set of regional Budget Framework Workshops in October. At these workshops the allocation formulae, minimum allocations will be explained fully.

4.6 The Local Government Planning and Budgeting Process

Local Governments should then start their own consultative budgeting and planning processes. The process of updating the DDP will be integrated with the Budgeting Process.

- ?? **The Budget Conference** - As soon as possible after the first Regional LGBFP workshops in October, Districts/Municipalities should call the Budget Conference, bringing together stakeholders in the different levels of local government and civil society. The Draft RTB should be explained and discussed at this forum in relation to local needs and priorities. The Draft DTB should also be discussed and indicative planning figures disseminated.
- ?? **Lower Local Government Consultations** - After the Budget Conference lower local governments should hold planning meetings to discuss their priorities in the different sectors for both recurrent and development activities. At these discussions parishes and subcounties will identify investment activities to be carried out in the following financial year and in the medium term, taking into account the resources available medium term indicative planning figures. On the basis of these discussions the parishes and subcounties will update their Development Plans and forward them to the Districts/Municipalities, along with any sector issues relating to recurrent expenditures.
- ?? **District/Municipality Level Consultations:** At the District/Municipality level meetings should be held with the various Sectoral Committees of the Council, for the purpose of both preparing of the sector components of the Local Government Budget Framework Paper, and updating the DDP. It is important to emphasise that the DDP should be prepared taking into account the available resources available over the medium term. The Planning units and the District Technical Planning Committees will play a crucial role in coordinating the consultations.
- ?? **Drafting the LGBFP:** Any amendments to the RTB will be incorporated into the sector components of the Local Government Budget Framework Paper. At the District/Municipality level the process of the preparation of Development Plans will be integrated into the LGBFP. The development components of the LGBFP will reflect the activities identified in the updating of the LCIII DP and District/Municipality DPs.

The Budget Framework Paper will include an executive summary which should:

- Set out the LGs RTB
 - Highlight changes to the RTBs
 - Give justifications to the changes in the RTB
 - Preliminary the planned outputs from development grants for the medium term.
 - Give Details of any other local government issues that are of concern to central government.
- ?? **Finalisation of the LGBFP** - The draft LGBFPs will be discussed by the District Technical Planning Committee. The LGBC will follow up visits Local Governments to ensure that RTB amendments are in line with the allowed levels of flexibility, clarify any queries, and provide recommendations for improvement. The LGBFP should then be finalised by the local government before being discussed and approved by the District/Municipality Executive. The Local Government should then submit it to the LGBC by mid January.

4.7 Acceptance/Rejection of RTB Changes and Finalisation of the Budget

On receipt of LGBFPs, MFPED will then check whether the proposed changes to conditional grant allocations to sector budget lines are not below the pre-agreed minimum levels, and that

the total conditional grant allocation in the RTB does not exceed the allocation provided in the draft RTB. This does not constitute an approval of the Local Government Budget, which is performed by the local council, it is a simple rules based acceptance/rejection of amendments to allocations of grants from central government.

If the RTB amendments are within the agreed rules Central Government will accept the local government's amendments to the sector grant allocations in the RTB. If not the amendments will be rejected, and the local government will be informed of the same. Again, it is important to emphasise this whole exercise will be objective and rules based and will not be open to subjective debate and value judgements.

The LGBC will then aggregate the amended sector budget and sector budgetline allocations and feed the numbers back into the MTEF in early March, in time for inclusion in the National BFP. After the BFP has been approved by Cabinet in mid March, the draft budget estimates will be forwarded to parliament for discussion. At that time the Final RTB and DTBs will be disseminated to Local Governments.

Districts/municipalities should then immediately disseminate the indicative development planning figures to subcounties and parishes, to initiate the adjustment of annual workplans.

The workplans will be submitted their respective local councils for approval in conjunction with the budget. Local Governments will sign letters of understanding with central government in which they agree to adhere to sector policies and guidelines, and pursue national sector goals.

Local Governments will also be required to inform central government of their overall RTB and DTB allocations (as laid out in their LG budgets), and planned sector outputs for the financial year, before they are allowed to access funds. This will give central government opportunity to compile a comprehensive national picture of overall sector allocations made by local governments, taking into account all funding sources and not just conditional grants.

4.8 Involvement of Parliament in the Local Government Budget Process

The Budget Act 2001 involves Parliament more in the allocation of the National Budget. It is also important that Parliament is involved in the Local Government Budget Process. Parliament should be involved in policy making with respect to local governments, including the process of setting of national standards for service delivery. This should be at both the national and local level.

Therefore a standing committee for Local Government Budgets should be established, to ensure that there is continued focus on Local Government issues throughout the Financial Year. MPs should be required to be present at the Budget Conferences of the Local Councils where their constituency lies. This will ensure that they are aware of the major local government issues in their areas, and help improve the linkage between local and national level politics

4.9 Budget Implementation

After Districts/Municipalities receive their final RT and DT budgets, they would have no discretion to switch expenditures between the sectoral budgets or sub-budget lines.

On the recurrent side local government flexibility would be within the agreed sector budgetline totals (e.g. in Health, within the specified sub-budgets for wages, allowances, drugs, transport and NGO services, not between them). This arrangement would provide the degree of conditionality required for PAF expenditures whilst increasing the flexibility available to the local government during implementation.

BOX 5A: CENTRAL and LOCAL GOVERNMENT BUDGET CYCLES

	Central Government	District/Municipality	Subcounty/Division	Parish
OCT		LOCAL GOVERNMENT CONSULTATIONS Discuss Allocation Formule and Grant Flexibility		
	1ST NATIONAL BFP CONFERENCE			
	Budget Guidelines	REGIONAL LGBFP WORKSHOP Disssmeniation of draft RTBs & DTBs		
NOV	Preparation of Sector BFPs	LG BUDGET CONFERENCE Explain RTB & Discuss options Disseminate Draft DTB to Lower LG		
		Preparation of Draft LGBFP & Updated DDP Sectoral Committee & DPTC Meetings Exec Meetings Ammend RTB	Planning Meetings	Planning Meetingsg
CALL CIRC			Feedback + LCIII DP	Feedback + PDP
DEC	Ministerial Consultations, Preparation of Preliminary Estimates & Finalisation of Sector BFPs	FOLLOW UP ON LGBFPs Visits to review draft LGBFPs & RTB Ammendments		
		Finalisation of LGBFP Changes Incorporated, Approved by Executive		
JAN	PR. EST'S TO MFPED		LGBFP to LGBC	
	Compile BFP	Accept/Reject Ammended RTBs		
		Integrate RTBs into MTEF		
FEB	PR. EST'S TO PRESIDENT			
	Finalise BFP			
MAR	BFP TO CABINET			
	Finalise Prel Estimates			
	PR. EST'S TO PARLIAMENT			
APR	Parliament Discusses Preliminary Estimates	Final RTBs & DTBs to LGs	Dev't IPFs to LCIII	De'vt IPFs to LCII
		Prepation of RTB & DTB Annual Workplans Identify Rec'nt Sector Output Targets Compile LCIII Dev't Activities Identify LCV Dev't Activities	Compile LCII Activities Identify LCIII Dev't Activities	Identify LCII Dev't Activities
MAY	PARLIAMENT RECOMMENDS			Workplan
	Finalising National Budget	RTB & DTB OUTPUTS TO LGFT		
		Sign Letters of Understanding	Finalise Budget	Finalise Budget
JUN	NATIONAL BUDGET READ	DISTRICT/MUN BUDGET READ	LCIII BUDGET READ	

Similarly there would be no discretion across budget lines within the Development Budgets. However for development expenditures there should be limited flexibility within budget lines to switch activities once the workplan is finalised.

4.10 Implications of the Budget Cycle

- ?? An important emphasis in the new process will be the integration of planning and budgeting. The preparation of the DDP will no longer be a separate exercise. The LGBF process will involve the updating of the DDP. The LG Budgets Committee will need to train local governments on how this is to be done.
- ?? In order to ensure that the Districts/Municipalities are able to carry out a fully participatory budget process, the Planning Units in local governments will need to have the capacity to manage the budget process. The District/Municipality also needs to play the important role of mentoring subcounties/divisions in planning, if decisions . The MoPS restructuring study will need to establish structures adequate to run the budget process recommended in this Strategy
- ?? The subcounties will be far more substantially involved in the planning and budgeting process. The preparation of the LCIII DP will involve actual planning over resources. The skills and staffing required at the LCIII level to carry this out effectively will need to be examined in the MoPS study.

4.11 Benefits of the Proposed Budget Cycle

- a. Harmonisation of the Local and Central Government Budget Cycles : The proposed cycle addresses the current dislocation of the central and local government cycles. The proposals fit within the national budget process as set out in the Budget Act 2001.
- b. Increased LG influence on National Budget : Planning and budgeting at the local level will feed back into the national budget process, and local governments will have a more meaningful influence on national resource allocation.
- c. Budgetary Information : The requirement for Districts/Municipalities to provide a reconciliation of transfers and expenditure with the RT account bank statement will provide the information on actual disbursements for service delivery which is currently lacking (see below). The simplified output reporting will also allow local governments to collect information on budget achievements more easily.

5 RELEASES, REPORTING AND ACCOUNTABILITY

5.1 Introduction

At present there is a multiplicity of grants, reporting systems and centres and bank accounts. Also the management of central government institutions' dealings with local governments has historically been largely fragmented, inconsistent and inefficient. These problems have led to inefficiencies in the management of local government programmes, and has weakened accountability.

5.2 Releases and Reporting

For recurrent expenditures, Local Governments would receive monthly transfers, and would be required to report quarterly. Transfers would simply be one twelfth of the annual recurrent budget. For development there will be little value added for detailed cash-flow planning at the outset and Districts/Municipalities would receive regular transfers on a quarterly basis. Similar to the RTS Districts/Municipalities would be required to report quarterly.

The release note would indicate the composition of the releases in terms of the amount released against each of the sector budget lines, and be distributed to department heads as well as the local government accounting officer. Districts/Municipalities will be required to publicise the total of transfers received and the sectoral allocations, and a summary of the quarterly accounts submitted.

5.3 Bank Accounts

The aim is to reduce the number of bank accounts in a local government. The bank account structures for LCV and LCIII are set out in Box 6A and 6B. At the District/Municipality there are two collection accounts: the government grant collection account and the local revenue collection account. RTS and DTS transfers will be made directly into the government grant collection account.

District/Municipalities initially will be able to opt for two types of structure for operational accounts:

Separate District/Municipality Sector Operational Accounts - Transfers would be made from the Grant Collection accounts to one operational recurrent and one development account for each sector development and recurrent conditional grant LGs will also transfer any local revenue or unconditional grant funds allocated to sectors into the relevant sector accounts, to supplement the funds from central government.

Apart from the sectoral accounts there will be two other operational accounts for Finance administration and other services in which unconditional grant transfers will be banked, along with a share of local revenue.

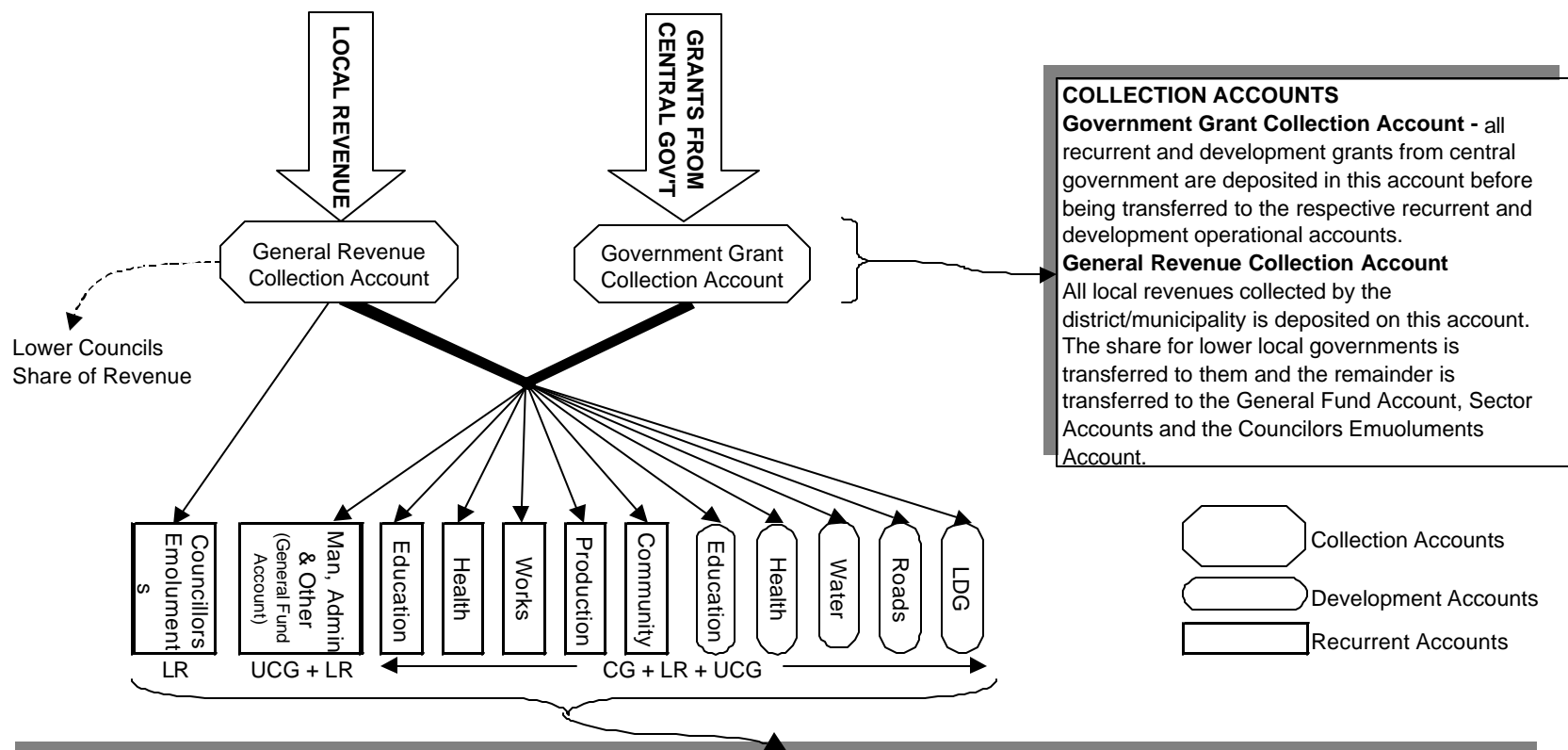
Single Recurrent and Single Development Operational Accounts – Here there will be a single operational RTB account and a single operational DTB account into which all government transfers and local revenue will be banked, excluding the share for councillors emoluments. This is the most transparent arrangement and only requires two bank reconciliations each quarter, and over time all local governments will be required to adopt it.

Under both arrangements there will be a separate account for the operations of council which will be funded directly from the local revenue collection account. This will avoid councillors dipping into central government transfers (see section 8).

From the District/Municipality operational accounts funds will also be transferred to lower level local governments and lower level operational units (e.g. schools and health sub-districts), and bank accounts may be required at this level.

At the LCIII level bank account structure will be simpler than at the District/Municipality, as the volume of funds transferred to them will be smaller. There will be one account for development activities and one for recurrent activities, into which sector funds will be transferred directly. Expenditures will be tracked through books of account. Local revenue will be banked in a local revenue collection account, before being transferred into the recurrent or development accounts. There will also be a separate account for councillors' emoluments. The Sub-Accountant will be a mandatory signatory for all accounts, in addition to the Subcounty Chief.

BOX 6A: DISTRICT/MUNICIPALITY BANK ACCOUNT STRUCTURE & FLOW OF FUNDS



OPERATIONAL ACCOUNTS

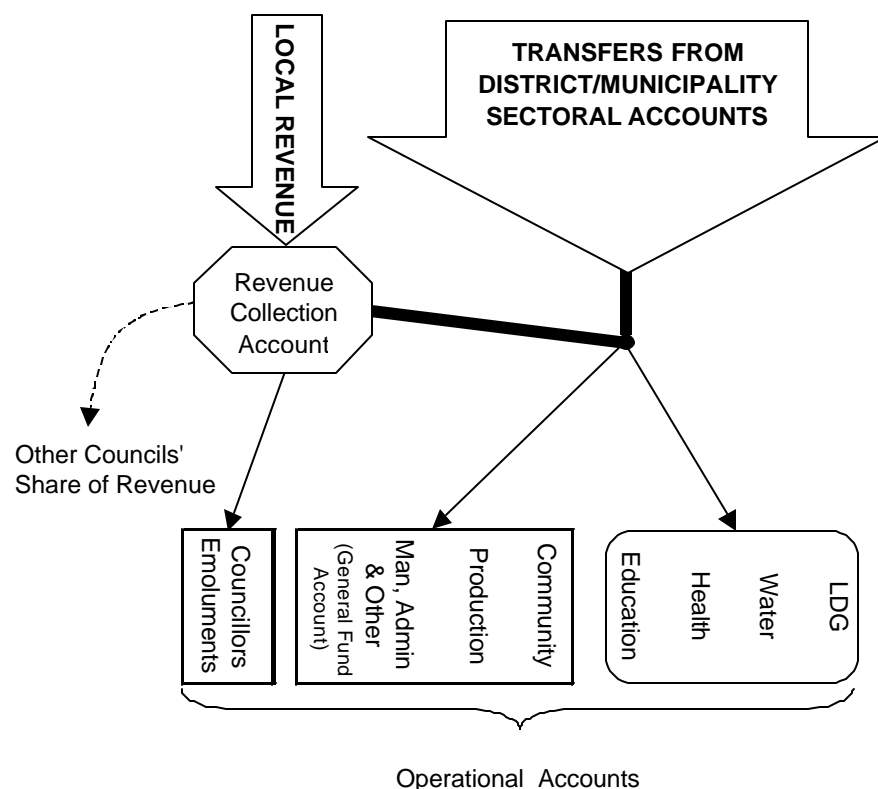
Sector Development Accounts - Each sector will have its own development bank account. Conditional Grant funds and the required contribution from Local Revenue will be transferred into this account. LGs will also be free to allocate additional Local Revenue and unconditional grant funds. Funds will be transferred to lower LGs in line with sector policy, where applicable. The directorate head, CAO & CFO will be signatories to the account.

Sector Recurrent Accounts - Similarly each sector will have its own bank account for recurrent funds into which conditional grant transfers, and any local revenue/unconditional grant funds allocated to the sector will be transferred. Expenditures against sector sub-budget lines will be tracked using books of account. Depending on sector policy funds can be transferred to lower level operational units. The relevant directorate head and the CAO will be signatories to the accounts.

Management Admin & Other - There should be a single operational recurrent account for all management, administration & other functions (excluding council), and funds for different areas should be tracked through the books of account. These will be financed from both local revenue and the UCG.

Councillor's Emoluments - The functioning of the local council should be funded entirely from local revenue, however councillors often dip into central government transfers.. Therefore the operational account for the local council operations should be separate from the General Fund Account and funded directly from Local Revenue accounts.

BOX 6B: SUBCOUNTY/DIVISION BANK ACCOUNT STRUCTURE & FLOW OF FUNDS

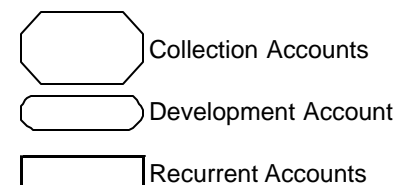


LCIII Bank Structure

Each Subcounty/Division will have three bank accounts:

Revenue Collection Account - At the LCIII level there is only one collection account, for local revenue. All local revenue collected is transferred into this account.

Operational Accounts - For those sector grants where funds are transferred to LCIII, this will be done directly to a single recurrent / single development account from the District / Municipality sector accounts. As with the district, there is a separate account for councillors emoluments with funds directly transferred from the Revenue Collection Account. The remaining Local Revenue will be transferred into the Management Administration & sector accounts. (this will include the local contribution to development)



Expenditures on sector budgets within the RTS and DTS will therefore be tracked through the books of account at all levels as opposed to through bank accounts. Districts/Municipalities would be required to provide reconciliations of these accounts to the LGBC each quarter.

Implications:

- ?? The number of bank accounts at a district/municipalities for government funded activities will be reduced to about 14, from over 50 in many cases.
- ?? A simple set of regulations and guidelines for dealing with local government bank accounts will be required to be developed.

5.4 Financial Accountability and Output Reporting

The Districts/Municipalities would record transfers received and expenditures made by sector and sector budget line in a set of books of account for recurrent and development expenditures. The District Council would be responsible for submitting quarterly accounts showing income and disbursements against each sector budget line.

A simple mechanism to enable accounting officers to track and control commitments will be an integral part of the system. If it becomes clear that accounting officers are over committing local governments, simple procedures for sanctioning those accounting officers will prevail.

The balance in the Recurrent/Development District/Municipality books of account must be reconciled with the balance on the Recurrent/Development sectoral account bank statements. Ensuring these reconciliations take place, which are requirements in the LGFAR, would both add vital discipline to the management of district/municipality funds, and would provide the centre with ready information on the level of balances within Districts/Municipalities. Initially sub-reconciliations for transfers to lower level administrative and implementation units may not be required, however this would be subject to review as local government capacities improve.

Districts/Municipalities will also prepare simple sectoral 'one-page' quarterly output monitoring forms for both recurrent and development expenditures. (These key-indicator monitoring formats are to be prepared and tested during the course of the sector transfer policy reviews). On the development side, sector outputs reporting for the sector development grant and LDG will be integrated.

Districts/Municipalities would send one copy of the quarterly accounts, bank reconciliations and quarterly output reports to the Chairperson of the LGROC in MFPED. MFPED would then copy sets to all members – and thus to all concerned ministries and agencies.

Implications:

- ?? Central Government will need to prepare Books of accounts and supporting manuals.
- ?? Central Government will need to prepare the financial reporting forms and sectors will need to prepare simple output reporting forms for all levels of local government.
- ?? LGs will need to be trained in the keeping of books of account and the preparation of quarterly reports. As LCIIIs will be progressively receiving more funds there will need to be increased focus on raising their financial management capacity.

Box 6C : The Importance of Financial Accountability in Local Governments

Districts must be made aware that if they fail to provide an adequate quarterly set of accounts and bank reconciliation, no further transfers will be made. This may appear harsh, but the accounting requirement is a basic task, which any corporate entity should be able to satisfy. With a clear manual, training and TA, the freedom to hire competent and qualified senior staff (or to sub-contract book-keeping and accounting functions) there is no reason why every district should not be able to comply. Councillors and officers must be aware that the ability to provide reconciled quarterly accounts is the minimum condition for the district to be deemed competent to handle funds from the national budget.

The evidence from DDP is that capacity can be up-graded in respect of financial management and control. The short- and long-term benefits of moving to a book-keeping based system, rather than a separate account system are so substantial that the effort is undoubtedly worth making.

5.5 Central Government Operations

At present there is little co-ordination, at an operational level, between and within Central Government actors when carrying out their operations with respect to LGs during budget implementation. The problem is especially acute in the areas of processing releases, and the monitoring and mentoring of LGs.

5.5.1 Local Government Releases and Operations Committee (LGROC)

A Local Government Releases and Operations Committee, chaired by MFPED will be formed to improve the coordination of central government operations with LGs. It will carry out the following activities:

- Study and analysis the financial and output information from Local Governments.
- Processing of releases to Local Governments.
- Overseeing the monitoring and mentoring of the use of and accounting for funds in implementation of Local Government Programmes by Central Government actors.
- Overseeing the provision of feedback to Local Governments on the use of and accounting for funds in the implementation of Local Government Programmes by Central Government actors.

The LGROC will be made up members who deal with the day to day operations of the Transfer Systems from LMs, the MoLG, MoPS and LGFC at a senior level. Members will also be drawn from Accountability Institutions responsible for monitoring Local Government Programmes.

Different institutions in the Operations Committee will take the lead role in implementing in these activities. The important factor is that they are all related to Local Government Transfers, and they need to be carried out in a coordinated way. This coordination of central government actors is the primary role of the Committee.

The LGROC is, however, purely a coordinating body with the purpose of reducing such duplication and does not usurp any legal mandate of any institution. The activities which will be coordinated by the LGROC, will be carried out by the members in the context of their own institutions in line with their legal mandates.

5.5.2 Management of LG Transfers within Line Ministries

A significant problem in the current management of CGs is that the Line Ministry staff involved all have other responsibilities. Without staff assigned full time to the sector issues relating to local governments, it will be difficult to see how Line Ministries will be able to fulfil their roles under decentralisation effectively. Line Ministries have a pivotal role in the successful establishment and the running of the RTS and DTS, as part of the LGROC and the LGBC, and it is important that they are fully able to play that role.

It is therefore essential that each line ministry involved with LG financing establish a cell of staff who are able to concentrate full-time on developing their ministry's work with local governments. These cells should be situated in existing departments within the individual Line Ministries. Most Line Ministries should be able to identify appropriate staff from within their institutions.

5.6 Monitoring and Mentoring

From Central to Local Government - Central Government has a crucial role in the monitoring and mentoring of local governments, which it has not been fulfilling effectively to date. A strong centre is crucial for ensuring the success of local government programmes. Sector Ministries, MoLG and Accountability Institutions all will strengthen the quality and coordination of their monitoring of local government, provision of technical support and feedback to local governments. The importance of sharing of information and coordination of monitoring activities will also be emphasised and the LG Releases and Operations Committee will play a lead roll in ensuring this occurs.

Within Local Governments - Districts/Municipalities are responsible for monitoring activities carried out in their local governments, and for providing technical support to lower local governments. As more funds flow to lower local governments, it is important that Districts/Municipalities fulfil this role effectively.

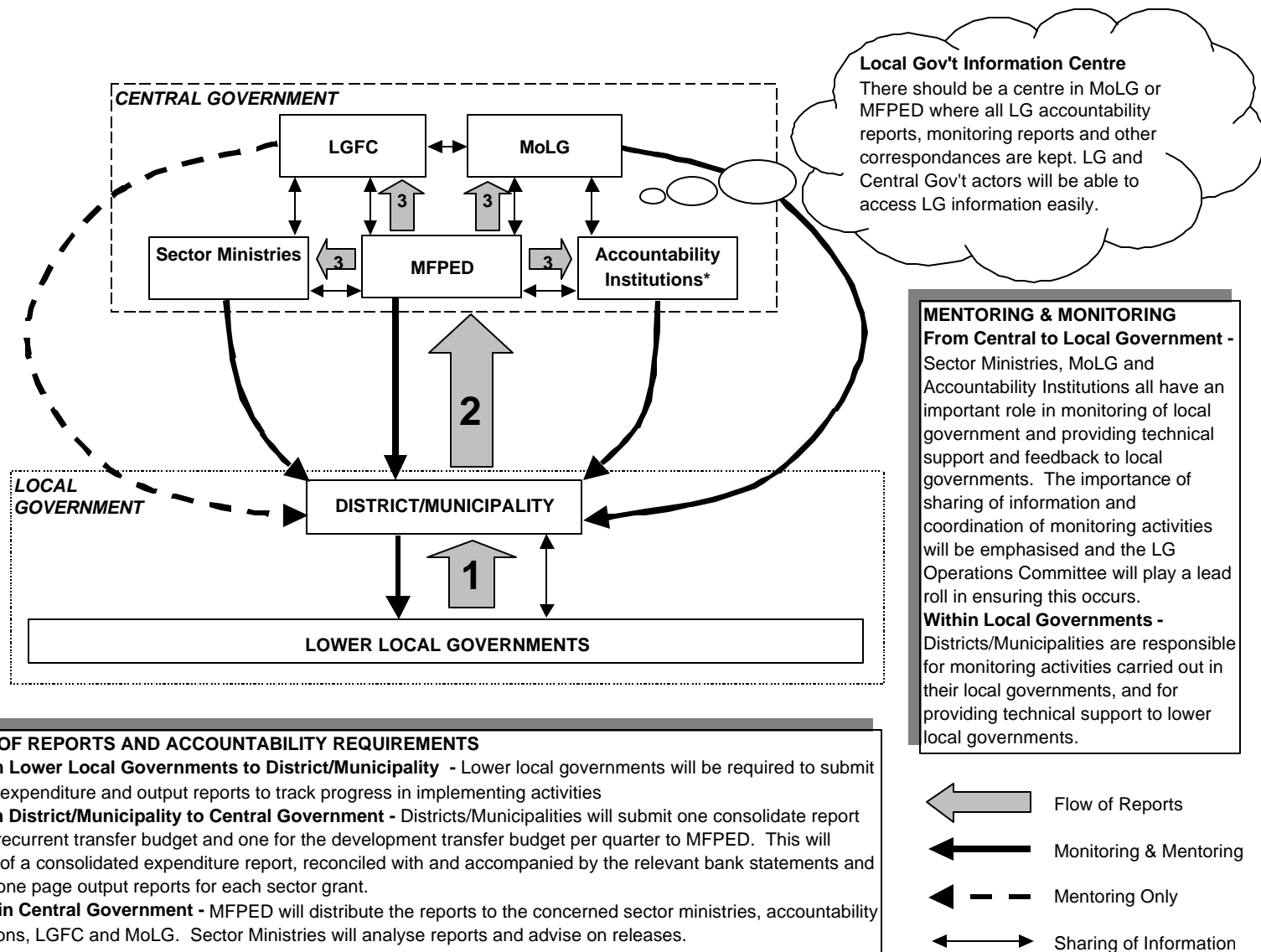
5.7 Reducing or Withholding of Releases

Development or Recurrent Conditional Grant Releases will be withheld if a District/Municipality fails to provide an adequate set of quarterly accounts and supporting bank reconciliations.

Any over-spend on a budget line shown in the quarterly accounts, using conditional grant funds released for expenditure against another budget line, would be deducted from the following transfer. For circumstances where it becomes clear that a LG accounting officer is consistently using conditional grant funds released for one sector budget line to fund over expenditures on another sector budget line, or is over committing the LG, or is building up large balances over time, a simple procedure will be required either to postpone or cancel all or part of later transfers.

Also releases will be adjusted depending on the advice of sector ministries. Sector ministries will analyse and evaluate output reports and conduct technical monitoring each quarter. There again would be simple rules developed regarding the procedures for sector ministries reducing or withholding releases. Not only inadequate financial accountability, but evidence of misuse of funds should have an impact on releases. More subjective factors such as the quality of services being provided and value for money should have an impact on future budget allocations and not releases.

BOX 6D: FRAMEWORK FOR LOCAL GOVERNMENT REPORTING AND FEEDBACK



* Accountability Institutions made up of IGG, Auditor General & Office of the Prime Minister, Office of the President

The levels of releases against each budget line will be discussed each quarter and agreed by the LGROC, taking into account both the financial and technical information.

Implications:

- ?? Clear procedures for reducing or withholding of releases on both technical and financial grounds will need to be developed. Other, non financial sanctions will need to be developed for accounting officers which do not follow established procedures.
- ?? Sector ministries will need to develop clear procedures for reducing releases on technical grounds.

5.8 Audit and DPACs

Internal and external audit will be responsible for checking the integrity of vouchers, and that expenditures have been booked to the correct sub-budget line. Clear instructions to this effect will need to be prepared. As more funds flow to subcounties, internal audit will increasingly need to spend time auditing their accounts.

In line with the Local Government Act and LGFAR, the Local Government Public Accounts Committee will review the Quarterly Accounts, Quarterly Internal Audit Reports and the Annual Audit Report from the Auditor General. The systems for financial accountability and reporting will facilitate the DPACs in performing these tasks better.

In addition mechanisms should be developed and put in place, so that the Local Government Audits and National Performance Assessments should have an impact on future budget allocations. This will provide an ex-post incentive for local governments to improve performance.

5.9 Benefits of Accountability and Reporting Provisions

- 1 LG Financial Accountability : The discipline of reconciling transfers, expenditure and balances with bank statements, is a significant step forward in increasing LG capacity and accountability.
- 2 LG Financial Management Capacity : The discipline of having to maintain proper books of account will be important in developing LG financial management competence and will have multiplier benefits across the range of LG activities.
- 3 Internal and External Audit and PAC : LG internal auditors, the PAC, and the external auditors and inspectors will be able to focus attention on a two budgets, two sequences of releases and two sets of books and fewer accounts for recurrent and development transfers, rather than having to deal with a proliferation accounts and books being operated separately as at present.
- 4 LG Financial Transparency : A single RT and DT Budget, and far fewer releases, makes it possible for Districts/Municipalities to publish budgets, transfers received and quarterly accounts. It is impractical to expect such transparency under present arrangements, due to the sheer number of transfers, accounts and reports.
- 5 LG Political Accountability : Consolidation of recurrent and development transfer budgets, releases received and expenditures into single reports, complemented by sectoral output information, makes it much more practicable for councillors to understand and monitor

what is happening within their councils. The sheer volume of paper, formats, reports and different systems makes political supervision very difficult at present.

- 6 LG Costs : The requirement to maintain multiple bank accounts and their associated bank costs will disappear.
- 7 LG Revenue Raising : The combination of separate Local Revenue and Grant Collection Accounts, coupled with fewer bank accounts will increase transparency over sources and uses of LG income. It will be easier for officers and councillors to see the sources and level of local revenue inflows. It will be easier to report information on local revenue raising accurately. It will be easier to see which activities are financed from local revenue and which from transfers. The separate council account will make it more difficult for councillors to access transfers from central government, which is an important pre-requisite in reducing the present tendency for growing transfer volumes to undermine discipline in local revenue collection.
- 8 LG Expenditure Information : One budget, transfer, set of books and accounts for Recurrent Transfers and one for Development Transfers will make it easier to identify areas of cost over-run and under-spend. The “big picture” and its sectoral and sub-sectoral make-up will be more apparent to LG officers and councillors, and to central and line ministries.
- 9 LG Expenditure Control : Reliable information on areas of under- or over-expenditure enables subsequent releases to be adjusted within the year. If expenditure is low against budget, that element of the transfer may be withheld from the next release. Conversely, any over-spend against budget can be deducted – unless there are extenuating circumstances and the District/Municipality has invoked the “emergency” procedure. During the LGBFP process any substantial variations between budget and outturn can be discussed.
- 10 Reduced paperwork : The major reduction in unnecessary and largely-unused paper-work (separate quarterly workplans and reports for each recurrent CG) will increase efficiency, reduce travelling and other transaction costs, and enable all parties to focus on the smaller but more useful set of information provided in a consolidated budget and set of accounts.
- 11 Better Output information : The provision of quarterly one-page ‘key indicator’ output monitoring reports for each sector will sharply improve the availability of usable and comparable information on sector outputs.
- 12 Simplification of Reporting : The provisions for all transfer and out-turn information in a single quarterly report for the RTS and DTS will sharply increase the accessibility and usability of the information provided, for Districts/Municipalities and for central and line ministries.
- 13 Performance League Tables : Readily accessible information on expenditure and outputs achieved, on a common format across all Districts/Municipalities, will enable line ministries and others to produce indicative league tables of performance and cost effectiveness.
- 14 Best Practice Assessment : Performance League Tables alone are notoriously difficult to interpret directly, because so many contingent factors affect outcomes in different Districts/Municipalities. However they do provide an objective basis for asking the question : why do these Districts/Municipalities appear to deliver services more cost-effectively than those ? This provides the basis for line ministry staff and others to conduct more in-depth studies within Districts/Municipalities to understand why some Districts/Municipalities

perform better, and to identify best-practice methodologies, which can then be promulgated.

6 FUNDING OF LG FINANCE, ADMINISTRATION AND STAFF COSTS

6.1 Introduction

At present, the financing of District/Municipality management, accountants, planners, LC3 chiefs etc. is mainly through the unconditional grant. Districts/Municipalities are acutely concerned about the inadequacy of UCG and the anomaly that front-line staff are securely financed through the PAF whilst managers and support staff are not. Managers therefore often are not able to or have no incentive to carry out their support supervision functions properly, which impacts negatively on service delivery.

If effectiveness of local government service delivery is to be maximised then the administration and staff costs of local governments need to be fully taken care of.

6.2 Establishing the Costs of LG Administration and Staff

The pre-requisite for fully funding the administration function at local governments is a thorough review of the optimum management staffing, structure and costs for Districts/Municipalities of different sizes.

A MoPS study financed by the Netherlands is planned and will hopefully be completed during 2001. This study would provide the basis for establishing model LG staff complements and the wage costs for different local governments. This needs to be done in close consultation with the sectors that deal with decentralised functions, to ensure that the sector directorates/department have appropriate staff. The Local Government Finance Commission and the Uganda Bureau of Statistics will also need to be closely involved as factors such as population and land area will have ramifications on the optimal staff structure of Local Governments, and hence the allocation formula for the unconditional grant.

This study will also need to be augmented by investigation into the operational costs for the administration function, so that the entire management and administration cost for different sized Districts/Municipalities is established.

6.3 How to Fund Finance, Administration and Staff Costs

Only once the costs of the wage and operational costs of different sized local governments have been established can the optimal modalities be fully established.

Below are proposals which set out how the financing could work. It centres on the unconditional grant funding the bulk of Finance, Administration and other functions, supplemented by local revenue.

Although it is proposed that the main source of funding for Finance, Administration and Other Services be the Unconditional Grant, it is important to emphasise that the Unconditional Grant remains unconditional, and can and should be used to supplement sector grant allocations in the RTB and LDG allocations in the DTB as well.

7.3.1 The Wage Component of the Unconditional Grant

Once the cost of the wage component of finance administration costs is established, the wage component of the unconditional grant could be increased to accommodate the recommended structures for different local Governments.

Districts/Municipalities would be informed about the staffing structure and salary costs used to calculate the transfer, but they would be free to decide their own precise staffing structure. Although the funding would not be conditional, the allocations would be sufficient for local governments to pay adequate staff, and Local Governments would be clear in that knowledge. Districts/Municipalities could instead, choose to sub-contract some tasks, rather than employing full-time staff.

7.3.2 The financing of the non-wage element of finance and administration costs

The proposed option for financing the operational costs for Local government administration is to increase the non-wage element of the unconditional grant to take care of the estimated costs of administration. Some unconditional grant funds would also be set aside for the funding of other functions, which are outside finance and administration and the priority sectors.

There is concern, however that the UCG may continue be used to fund inefficient activities and not the essential administration functions, and the appropriateness of this option will need to be investigated against the provision of specific budget lines for finance and administration (i.e. a conditional grant).

7.3.3 Budgeting for Finance and Admin. Other Services

In the draft RTB provided to Local Governments in December, the ceilings of the Unconditional grant will be provided. These will be divided into wage and non-wage budget lines, the wage component being based on the recommended structure. During the budget process, the local government will decide on its staff structure, and the functions it may wish to contract out, and therefore the wage, non-wage split for the unconditional grant. The local government should also incorporate the share of local revenue going towards administration and other functions. This will be integrated into its amended RTB submitted to the LGBC.

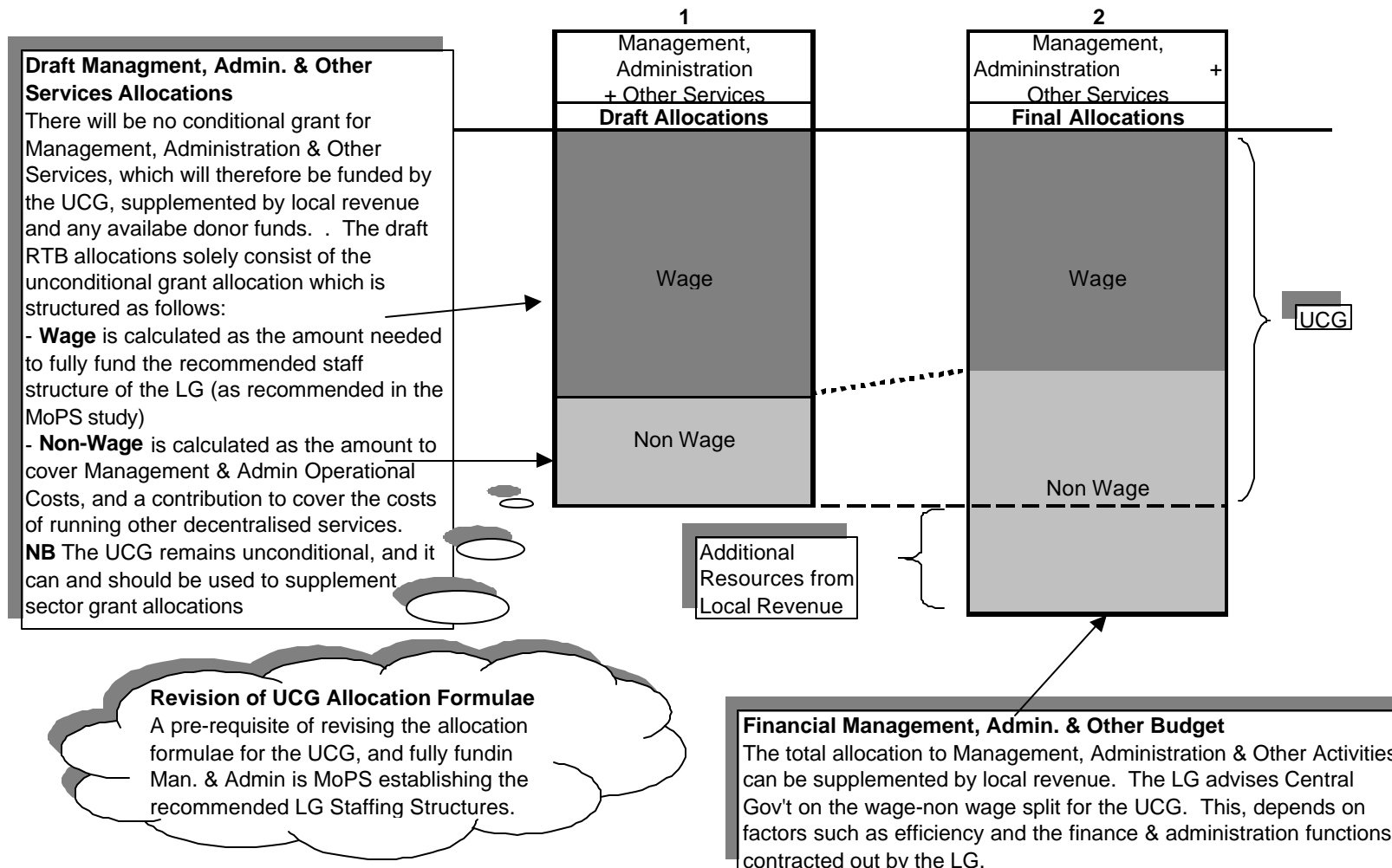
The local government should ensure that the entire staff structure is taken care of within the Unconditional Grant Budget, as this will help prevent the accrual of salary based areas. Additional operating costs and other services would be financed from the local revenue budget, from the remaining UCG or the equalisation grant budget lines.

6.4 Financing the Restructuring and Salary Arrears

It is very important that, if central government commits to financing the wage costs of the new structures of local governments, that a strategy is worked out for the financing of the restructuring process. Otherwise the danger is that local governments will continue to pay inefficient and inappropriate staff structures with the increased funding, and hence limit the benefits of the increase in funding.

Similarly a strategy on how to help local governments clear the salary arrears that have accumulated should be developed, or else a large part of the increased UCG may be used for the clearing of arrears.

BOX 7A: FINANCING OF MANAGEMENT & ADMINISTRATION VIA THE UCG IN THE RTB



7 THE EQUALISATION GRANT

7.1 Introduction

The equalisation grant is provided for in the Constitution as a grant for “giving subsidies or making special provisions for least developed districts”. The equalisation grant will be used as an increasingly important tool to boost the development of those local governments with low levels of services, and those poor Districts/Municipalities with low revenue potential.

The equalisation grant allocation will be simplified and be based on:

- ?? an indicator of poverty – this will need to be developed, perhaps on the basis of human development indices, and will act as a proxy for revenue potential
- ?? objective criteria for expenditure needs – these could include factors such as variations in population, geographical area, infant mortality rates etc.

7.2 Budgeting for the Equalisation Grant

Local Governments will be free to spend the allocations on either development or recurrent activities consistent within the priority sectors.

At the beginning of the Budget Cycle those Districts/Municipalities eligible will be given an allocation for the equalisation grant. They will then need to split this allocation between recurrent and development budgets before the budget conference.

7.3 The Recurrent Component

The recurrent transfer budget will be increased by the value of the recurrent allocation and the local government will be free to allocate these additional resources to any sector budget line within a sector budget in line with local priorities (excluding the budget for finance, administration and other services).

During the process of amending the RTB allocations, the equalisation grant allocation itself will be earmarked to different sector budget lines, as additional resources to the Conditional Grant allocations within the RTB.

Equalisation grant releases will be transferred, via the grant collection account, into the sector recurrent accounts, and be accounted for against the relevant sector budget lines in the normal manner.

7.4 The Development component

The development component will also be discretionary. It will simply be added to the allocation for the Local Development Grant and the procedures for allocating, and planning for funds under the DTS will be followed. Similarly the procedures for reporting and accounting for funds under will be followed.

8 LOCAL REVENUE RAISING

8.1 Introduction

Government will need to ensure that the new transfer systems give incentives towards enhancing local revenue. In recent years the big increase in transfers from central governments has undermined local revenue raising efforts, which are essential to the long term sustainability of local government.

The new transfer mechanisms must serve to support local revenue raising efforts as opposed to undermining them. The following are two essential components:

8.2 Central Transfers Which Provide Direct Incentives to Raise Local Revenue

Some element of central transfers will need to provide a direct incentive for a local government to increase local revenues. Therefore funds will be made available to local governments each year in order to reward those which improve tax administration and tax collection over time. Each year local governments would be scored according to their performance, and the more a local government has improved its tax administration and collection over time, the greater proportion of available funds will be allocated to it.

These funds could either be transferred as part of the non-wage element of the unconditional grant or as a separate grant. Whichever option is chosen, it is important that the incentive provided is substantial enough to ensure local governments make additional efforts to raise local revenue.

8.3 Preventing Local Politicians from Dipping into Central Government Transfers

A separate bank account for councilors' emoluments will be, and this will only be funded from local revenue transferred from the local revenue collection account (see diagram 6A). Local Councilors will only be able to access funds from this account. It will not be possible for central government funds to be transferred to this account.

The "20% rule", where the expenses of council are not allowed to exceed 20% of local revenue is almost universally broken and therefore should be reviewed. Instead the option of providing realistic ceilings for local politicians' emoluments should be established for different sizes and levels of local government should be considered.

9 IMPLICATIONS FOR DIFFERENT INSTITUTIONS

9.1 Implications for Local Governments

9.1.1 General

Under the RTS and DTS, all transfers to local governments come under only two systems. This would relieve much of the pressure on Districts/Municipalities in terms of multiple procedures, bank accounts and reporting.

9.1.2 Recurrent

Local Governments would have the opportunity to make amendments to their draft recurrent budget allocations (within the District/Municipality total). Minimum criteria for allowing Local Governments to make amendments to their Recurrent Transfer Budgets will, however be applied. Local Governments will have to demonstrate that the previous year's budget process was in line with the legal requirements before any amendments to the RTB are allowed.

After the budgets are agreed, Local Governments will also have complete flexibility within the RTB sector budget lines during implementation.

This means that local governments will be given freedom to budget for and provide services according to their local needs, so long as they are compliant with national policy and overall goals.

9.1.3 Development

Local Governments will need to establish and manage a fully integrated, bottom up planning process for development expenditures, so that the investment decisions made are more in line with communities' priorities.

This will involve:

- ?? Lower Local Governments will need to update/prepare development plans, make informed investment decisions and prepare of development workplans
- ?? Districts/Municipalities will need to support lower local governments in their planning. Thus Planning Units will need to build the capacity of lower local government in this regard and support them in the planning process. This will involve the calculation and timely dissemination of indicative planning figures for sector conditional grants to lower local governments, assisting lower local governments in collection of data.
- ?? Sector Departments in local governments will need to inform lower local governments of national policies relating to making sector investments and train them in the use of sector planning manuals produced.
- ?? Ensuring Local Governments meet LDG minimum access criteria. These performance requirements concern investment planning, project appraisal, allocation of funds to PAF priority areas, financial management and accountability, procurement and tendering, capacity building, mentoring and co-financing using locally raised revenue.

This will require a substantial effort by districts and municipalities to upgrade their own planning capacity and those of lower local governments.

Every Local government will need to be able to demonstrate that they are properly run and managing their finances properly in order to access central government transfers. These include:

- ?? Properly management of Bank Accounts
- ?? Proper and up to-date maintenance of the books of accounts
- ?? Timely and proper quarterly financial reports reconciled with the RT account bank statement and sector output monitoring reports.

Failure to adhere to these basic requirements, which are provided for in the current legal framework, will halt transfers. Thus local governments will need to ensure that they have

adequate capacity carry out these functions effectively. Especial focus will be needed on upgrading the financial capacity of lower local governments.

9.1.4 ULAA

ULAA will have an increasingly important role to play in representing local governments' views at the national level. As a member of the Local Government Budgets Committee, it will play an important role in the establishment of sector recurrent and development policies, and the negotiation of the recurrent flexibility and allocation formulae on behalf of local governments. This means it will have to strengthen its capacity, both in terms of negotiation, and its ability to network effectively with all local governments countrywide.

9.2 Local Government Finance Commission

In line with its mandate for advising on financial issues pertaining to local governments, the Local Government Finance Commission will be influential in the LG Budgets Committee and Releases Operations Committees.

In particular, the LGFC will chair the LG Budget Committee, and play the following role within it:

- ?? To advise on financial (policy) issues relating to the operation of the Transfer Systems, including sector policies and conditions, the RTB and DTB structure.
- ?? To review and negotiate of the allocation formulae and flexibility of Local Government Grants.
- ?? The promotion of revenue collection by local governments.
- ?? Settlement of disputes between central and local governments on financial matters.

The LGFC will therefore need to ensure that it is prepared to undertake these roles within the LGBC, and to carry out the required activities for the setting up of the Transfer Systems.

9.3 Ministry of Finance, Planning and Economic Development

The MFPED will chair the LG Operations Committee, which will be responsible for coordinating the running of the transfer systems during each financial year. MFPED will also have a key role in supporting establishment of the RTS and DTS.

The key roles of MFPED will be as follows:

- ?? Receiving, analysing and disseminating local government reports
- ?? Comprehensive collation and analysis of information on local government budgets, revenues, expenditures and outputs
- ?? Processing and effecting releases to Local Governments

As a member of the Local Government Budgets Committee, MFPED will be responsible for the co-ordination between the local and national budget processes, and provide important input in the negotiation of the allocations of resources to local governments within the MTEF.

In order to play these roles more effectively, MFPED will need to strengthen the Decentralisation Section and the PAF Secretariat, which currently coordinate local government activities, and effect releases. The Treasury Inspectorate will also need to establish the capacity to analyse the financial information in the reports received.

In the short run the MoFPED would also be responsible for the administration of the current system of conditional grants (along with line ministries) whilst the new process is being set up and during the pilot phase.

9.4 Implications for Ministry of Local Government

MoLG will play a pivotal role in the management of government transfers, and the mentoring and capacity building of Local Governments. This will involve the following:

- Coordinate the monitoring and mentoring of the use and accounting for funds in the implementation of Local Governments.
- Inspection of Local Governments.
- Conducting the annual national Local Government assessments.
- Management of Local Government capacity building efforts.
- Advising MFPED on LDG allocations and releases to Local Governments.
- Coordination of donor support to local governments/decentralisation.

The Ministry of Local Government will make the necessary arrangements to put in place the capacity required, and to ensure that the activities currently undertaken by the LGFP PMU are mainstreamed in the main Ministry.

9.5 Implications for Line Ministries

9.5.1 Role and organisation

The proposed systems have important implications for the role and the responsibilities of the LMs. The LMs' role will change from the CG approach of attempting to enforce tight control over inputs and eligible activities, to:

- ?? the development of national sector policy;
- ?? establishment of national service delivery standards;
- ?? support, training and mentoring of LGs;
- ?? monitoring and evaluation of LG outputs and performance;
- ?? advising on releases to local governments.

In short, the LM role will become that envisaged in Section 97 of the Local Governments Act.

This will involve the following:

- ?? Internalisation of the decentralisation policy framework including LMs roles as set out in LGA, LGFAR and The Constitution. The LGDP design concepts will also need to be understood within ministries
- ?? Review of sector policy relating to transfers local governments and development of sector guidelines will be developed in partnership with LG, through the LGBC, replacing current CG guidelines. These will seek to maximise LG flexibility in implementing national policy,

and rely more on the use of checkable key-indicator 'one-page' quarterly output monitoring reports, complemented by periodic field evaluations.

- ?? Clarification of internal responsibilities for work with LG within each sector ministry. There must be a clear line of authority and communication for each line ministry's work with LG on policy development, mentoring, monitoring and evaluation, and for its work within the LG Budget and Operations Committees.
- ?? The prompt establishment of Local Government Financing Units within each involved Sector Ministry (see below). The LGFUs will comprise a small team of full-time staff, without other responsibilities, either working within and existing department or working across departments.

9.5.2 Management of Local Government Issues within Line Ministries

As stated in Section 5, a significant problem in the current management of CGs is that the line ministry staff involved all have other responsibilities. Without a cell staff assigned full time to the sector issues relating to local governments, it will be difficult to see how Line Ministries will be able to fulfil their roles under decentralisation effectively. Line Ministries have a pivotal role in the successful establishment and the running of the RTS and DTS, as part of the LGBC, and it is important that they are fully able to play that role.

Therefore the expeditious establishment of a cell of full-time staff, within an existing department, in each Ministry responsible for the management of CGs, will be essential to the success of the RTS and DTS.

9.5.3 Review of sector recurrent and development transfer policies and guidelines

A major task that sector ministries will need to carry out is a review of their policies with relation to transfers to local governments and these reviews should encompass the following:

- ?? Identification of all the recurrent activities and all the development activities that local governments carry out in the sector.
- ?? Developing one recurrent wage and non-wage policy for each sector, with the minimum number of sector budget lines, in order to maximise LG discretion in adapting national policies to the reality of local conditions
- ?? Development of National Standards for Service Delivery, if this has not already been done so, and the optimal levels of flexibility.
- ?? Developing one development policy for the sector, again maximising the LG discretion.
- ?? Assessing what useful role the whole LG structure (LC5 to LC1, officers and councillors) might play in strengthening the local implementation of sector policy.
- ?? Establishing more transparent, needs-based allocation formulae, which are understood and recognised by all.
- ?? Drafting and field-testing simple quarterly output monitoring formats with a few objective, checkable, key indicators
- ?? Working as part of the LG Operations Committee and the management the RTS and DTS
- ?? Modalities for field evaluation of LG performance, spot-checking the output monitoring data provided, and follow-up training and mentoring of LG staff

- ?? Modalities for exchange of best practice and information dissemination across Districts/Municipalities. By combining quarterly expenditure data with the key-indicator output monitoring data, LMs will be able to prepare indicative local government league tables of costeffectiveness. Such tables are essential in identifying which Districts/Municipalities appear to perform better than others, and which Districts/Municipalities are priorities for training and mentoring. Combining reliable output key indicators with actual expenditure data thus becomes a powerful means for identifying and promulgating best practice.

9.6 Other Central Government Institutions

9.6.1 Ministry of Public Service

The Ministry of Public Service has a very important role to play. If the proposed reforms are to be successful the following must be rapidly concluded:

- ?? Setting of Local Government Staff Structures – the establishment of model local government structures is very urgent – it is imperative that MoPS expedites this exercise, whilst ensuring that other central government institutions are fully involved in the process (line ministries, MoFPED, MoLG).
- ?? Pay Reform – well-motivated public servants in local governments are essential if the benefits of fiscal decentralisation are to be maximised. Clear policies for payment of different cadres of staff, and flexibility in salary levels, are important in giving local governments the ability to attract retain and pay the calibre of staff they require. It is important that when pay reform is effected, sufficient additional funding will need to be allocated to local governments to fund the additional costs.
- ?? Decentralisation of the Payroll – this exercise should be expedited, as it should lead to efficiency savings in the management of local government payrolls. It will, in conjunction with the RTs also give local governments flexibility in determining the levels and payment of staff in the local governments.

9.6.2 Office of the Prime Minister

As it is ultimately responsible for overseeing government programmes, the Office of the Prime Minister should be more involved in the management of Local Government issues at central government, and therefore a member of the Local Government Budget and Operations Committees. The Office of the Prime Minister also has an important role in the policy co-ordination between sectors.

9.7 Implications for Donors

The majority of donors are either providing budget-support or considering the possibility of so doing. The relative efficiencies and benefits of budget support are well established. However it is important to recognise that there is still considerable caution amongst donors about providing budget support, and the proposals in this Strategy have been framed in the light of that.

As with sector ministries the legal framework under decentralisation and the LGDP concept is still relatively new to most donors, and a programme of information meetings at an early stage would be highly desirable. The LGDP methodology is conditional, but based on LG performance criteria (management, planning, accounting, transparency etc.) rather than conditions related to what the money can be spent on under CGs in a given sector. In contrast to the CG sector driven model, the mix of infrastructure and other investments created under LGDP is driven local government and community prioritisation within the budgets allocated.

Government will encourage donors to channel support via national transfer systems for recurrent and development expenditures as this avoids the intrinsic sustainability problem caused by establishing parallel systems. They will also be encouraged not to tie their support to specific sectors as this will allow government to find the optimal balance between discretionary and sector-conditional funding, and enable government to reward good performing local governments with extra autonomy.

10.6.1 Recurrent Transfer System

For recurrent expenditure, the shift to a single RTS continues to provide the degree of conditionality which donors currently require to enable continued sector support through the PAF. Once budgets are agreed, Districts/Municipalities are required to maintain spending within the wage and non-wage sector budget lines. The RTS seeks to preserve and enhance the poverty conditionalities and accountability which donors require. Most of the advantages of the RTS described above are matters of concern to many donors.

10.6.2 Development Transfer System

Similarly the Development Transfer system seeks to provide the degree of conditionality which donors currently require to enable continued sector budget support. There are more important implications relating to support which donors target to individual Districts/Municipalities for the provision of infrastructure.

Government will promote the use of the channelling of investment support through national systems. Therefore:

- ?? Donors with existing support to Local Governments will be requested to align their modalities for providing investment support with the LDG modalities. Where possible existing support should be routed through the LDG.
- ?? For new local government support programmes donors will be requested to make local government investment financing congruent with national systems. This will involve channelling non-sectoral investment support via the LDG. Donors will be requested, if possible, not to earmark this support to specific Districts/Municipalities, as this may result in inequitable distribution of resources countrywide.

The clear benefit for donors of withdrawing from direct financing of local governments is that the 'exit-nightmare' disappears.

10.6.3 Technical Assistance

For those donors unable to provide investment support via national systems, or who wish to supplement their investment support there remains immense need and scope for direct capacity-building support.

General capacity building will be provided nationally by institutions represented in the LGBC and LGROC (under the coordination of MoLG), and specific local capacity needs will be addressed largely via the capacity building grant. The LGBC will be able to advise donors on those Districts/Municipalities with special capacity building needs, or special national capacity building requirements, however, over time, government may also request donors to finance all capacity building through the national budget.

10 THE WAY FORWARD

The aim is to have the RTS and DTS operational countrywide in FY2003/4. This will be done in three phases.

- In the first phase, from March to September 2002 the modalities for the RTS and DTS implementation will be developed in full.
- In the second phase, from July 2002 to June 2003 the reporting and accountability mechanisms for the RTS and DTS will be introduced tested and refined in 10-15 pilot Districts/Municipalities in FY2002/3, along with the new budgeting modalities for the same Districts/Municipalities.
- In the third phase, from July 2003 onwards, the budget and reporting systems will be up-scaled country wide.

This section elaborates the way forward for implementing the RTS and DTS, and identifies key activities and outputs which will be needed to achieve this and the associated timetable.

10.1 Phase 1: Establishing Operational Modalities for the RTS and DTS

10.1.1 Setting up of the LG Budget and Operations Committees

The first task is the establishment of both the Local Government Budget Committee and Releases and Operations Committee. To achieve effective co-ordination amongst ministries and other agencies, the Committees must be chaired by senior officials from the LGFC and MoFPED, respectively, who are available to work on activities related to the Committees on, say, at least a half-time basis. The Chairpersons must be of sufficient status to ensure that other ministries and agencies respond in a timely and effective manner.

It is important that the members of both Committees become thoroughly familiar with the key features of the decentralisation legal framework and LGDP design. Key issues for review include: the respective roles of Ministries and Local Governments as specified in the Act; the potential and benefits of involving the whole LG structure from LC5 to LC1, officers and councillors; the use of minimum access and performance conditions, incentives and penalties; the way in which fund availability can be used to drive up-graded performance and capacity; the use of performance conditionalities rather than rigid input-output conditionalities.

Output	Actors	Target Date
LG Budget and Operation Committees Set Up	LGFC, LMs, MoLG, MFPED, LG Ass's	Early March 2002
LGBC and ROC Members Trained on Dec. and LGDP	Members LGBC & OC	Early March 2002

10.1.2 Strengthening Line Ministry Management of Local Government Transfers

Line Ministries must then ensure the prompt establishment of cells of staff working on Local Government Transfers within their structures. These LGFUs will comprise of a small team of full-time staff, without other responsibilities, sitting within an existing department. The full-time staff comprising the LGFU in each Ministry will normally be drawn from those currently working part-time on conditional grants.

It is important that, members of these cells are made familiar with the decentralisation framework and the LGDP mechanism as well, and these skills are disseminated within line ministries them.

Output	Actors	Target Date
LM LGFUs Set Up	LMS	Early May 2002
LGFU Members Trained on Dec. and LGDP	LMS	Early May 2002

10.1.3 Strengthening of Capacity of the MoFPED, LGFC and MoLG.

Whilst the Transfer Systems are being setting MoFPED, LGFC and MoLG will need to assess their structures and be realigning their capacity to handle their roles in the management of both the RTS and DTS.

The institutions will need to identify, early on key high performing individuals to handle the new functions, examine the roles of the different departments in handling them. Specifically, the MoLG will need to establish and implement a plan for internalising the tasks associated with LGDP modalities within the Ministry.

This all should be done in close liaison with the LGBC and LGROC, so that when the RTS and DTS are launched, the institutions are fully prepared to take on their roles in the running of the systems.

Output	Actors	Target Date
Assess Institutional Set Up	MoFPED, LGFC, MoLG	Early April 2002
Institutional Reorientation	MoFPED, LGFC, MoLG	Early May 2002
Appointment of Key Responsible Individuals	MoFPED, LGFC, MoLG	Early May 2002

10.1.4 Establishment of Principles Allocation Formulae, and RTB and DTB Modalities.

One of the first tasks of the Local Government Budget Committee is to set out, in detail the framework for operation of the DTS and RTS, and establish the principles for allocating funds to Local Governments.

The first stage of this will be to conduct an overall review of all grant allocation formulae and to establish uniform principles for the allocation of sector conditional grants, in conjunction with those of the for the Local Development Grant, Equalisation Grant, and Unconditional Grant. Embedded within this will be principles for sanction and reward of local governments. This will establish overall principles for allocating funds to local governments which:

- Poverty Focused
- Promote the Achievement of Sector Goals
- Sufficiently cater for finance and administration costs
- Provide an adequate balance between discretionary and non discretionary funding, to enable local allocative efficiency.
- Provide incentives to local governments to improve local performance and

Secondly the LGBC will also need to establish the principles behind the planning and budgeting modalities within the RTB and DTB, before the sectors start their policy reviews. This will involve the following:

- Development Transfer Budget - Principles for establishing the distribution of planning and implementation responsibility between levels of local governments.
- Recurrent Transfer Budget – Principles for establishing the optimal number of sector budget lines, and the flexibility in changing grant allocations.
- the RTB and DTB formats with the phase 1 Districts/Municipalities and ULAA,

Thirdly, whilst the Sector Reviews are ongoing, the LGBC should prepare Budgeting and Planning Manuals for each level of local government, and a training programme to sensitise them.

Output	Actors	Target Date
Terms of Reference for Review of Local Government Allocations	LGBC, LGFC, Sector Ministries, ULAA	Early March 2002
Review of Allocation Formulae Commences	LGBC, LGFC, Sector Ministries, ULAA	Early April 2002
Stage 1: Allocation Principles Established: <ul style="list-style-type: none"> - Uniform Principles for Sector Recurrent and Development Grant allocations - Principles for Local Development Grant Formula, Unconditional Grant and equalisation grant Formulae. - Modalities for performance incentives and penalties - Proposals for providing incentives to mobilise local revenue 	LGBC, LGFC, Sector Ministries, ULAA	End April 2002
Stage 2: Agreed RTB & DTB Frameworks <ul style="list-style-type: none"> - RTB & DTB Format - Guidelines for establishing the number of sector budget lines for recurrent expenditure - Guidelines for establishing the distribution of development grants between levels of local governments. 	LGBC, LGFC, Sector Ministries, ULAA	End April 2002
Stage 3: RTB & DTB Budgeting & Planning Manuals Written, and training programme designed. <ul style="list-style-type: none"> - District/Municipality Budget Manual (including LGBFP/DDP guidelines) - LCIII Planning & Budgeting Manual - LCII Planning Manual - Training Programme Designed 	LGBC, LGFC, Sector Ministries, ULAA	End July 2002

10.1.5 Sector Transfer Policy Reviews

The LGBC will need to prepare terms of reference to guide the line ministry reviews of their policies with respect to transfers local governments, to enable them to realign them with the legal framework and the Recurrent and Development Transfer Systems.

Following the establishment of allocation principles, and the RTB and DTB framework, the sector reviews will commence, in early May 2002.

In the first stage of the review process sectors will need to identify the optimal number of sector budget lines, revise allocation formulae on the basis of the agreed principles.

The LGFUs will have to ensure that sector planning and budgeting manuals are complete by the end of August in time for the First Budget Framework Workshop for the Phase 1 local governments.

Output	Actors	Target Date
Terms of Reference for LM Sector Transfer Policy Reviews developed	LGBC	Mid April 2002
Sector Transfer Policy Reviews Commence		Mid May 2002
Stage 1: Outputs of Sector Transfer Policy Reviews: <ul style="list-style-type: none"> - Recurrent & Development Activities Identified - Sector Budget Lines Identified - Allocation Formulae Revised - Establish Sector Output Indicators - Roles & Responsibilities of Sector Ministries 	LM LGFUs	End July 2002
Stage 2: Outputs of Sector Transfer Policy Reviews: <ul style="list-style-type: none"> - Sector Planning & Budgeting Guidelines - LCIII & LCII Sector Development Planning Guides - Training Programmes Designed 	LM LGFUs	End August 2002

10.1.6 Finance and Administration Costs

The full funding of Finance and Administration Costs depends on the restructuring study for local governments from MoPS, which commenced in December 2001. The study should establish the recommended structures for the phase 1 Districts/Municipalities by the end of November 2001, so that the unconditional grant allocations within the draft RTB can be established before the beginning of the local government budget process in December. Similarly an estimate of the operational costs should be established by December.

Output	Actors	Target Date
LG Restructuring Study Commences	MoPS	Ongoing
Recommended Staff Structures for Pilot LGs	MoPS	End May 2002
Operational Cost Estimates	LGBC, LGFC, MoLG	End August 2002
Draft UCG Allocations	LGBC	End August 2002

10.1.7 Reporting and Accountability Provisions

The LGROC will need to review and prepare any necessary amendments to the LGFAR early on in the process of preparing the accountability provision, preferably by the end of March 2001. Then, on the basis of the agreed RTB and DTB formats the LGROC should prepare Books of Account, Standard Release Notes and financial reporting forms.

The output reporting formats should be prepared by the LGROC in close consultation with sector ministries to ensure it is consistent with their national output indicators established in the Sector Transfer Policy Reviews. Simple formats to collect quarterly information on recurrent output indicators, and development scheme completions and costs which can be aggregated into District/Municipality and national quarterly reports are essential. Inclusion of satisfactory output monitoring on prescribed formats must become a performance conditionality at District/Municipality and sub-county levels.

Once these have been finalised a simple manual should be prepared for local governments which explains the financial management and reporting provisions, and a training programme for local governments should be designed.

Output	Actors	Target Date
Terms of Reference for Producing Reporting & Accountability Systems	LGROC	Mid March 2002
Review LGFAR '98 and recommendations on required amendments	LGROC	End Mar 2002
Reporting & Accountability Provisions Complete: <ul style="list-style-type: none"> - Books of Account Produced - Release Procedures & Standard Release Note - Recurrent & Development Sector Output Reporting Formats Finalised - Financial Reporting Formats - Financial Accountability & Reporting Manual Produced - Training Programme Designed 	LGROC	Mid April 2002

10.1.8 Donor Funding Modalities

Government will need to prepare, discuss and agree a set of principles for future donor support with donors which ensure that donor support is in line with the provisions of the this Strategy. Government and donors will also need to review how existing bilateral district support projects can be harmonised with LGDP for the 2002/3 financial year. Thinking along these lines is already underway within Danida, Irish Aid and the Netherlands.

For any new donor support a mechanism will need to be put in place for government approval, to ensure that they are in line with the agreed principles, and not creating parallel mechanisms.

Output	Actors	Target Date
Discussions With Donors on harmonisation of Donor Support	LGBC, LMs, Donors	March – June 2002
Modalities for Harmonising Donor Support to Local Governments Agreed: <ul style="list-style-type: none">- Principles of Donor Funding Agreed- System for approving New Support- Plan of action for Realigning Existing Donor Support	LGBC	July 2002

10.2 PHASE 2: Pilot Implementation of RTS and DTS in 15 Local Governments

10.2.1 Identification of Pilot Local Governments

The RTS and DTS will be piloted in 12 Districts and 3 Municipalities. The LGBOC will select the a representative sample of local governments ensuring that there is a:

- Range of different financial management capacities
- Range of different sector implementation capacity
- Different levels and types of sector and donor funding
- Geographical Distribution

Output	Actors	Target Date
Pilot Local Governments Selected	LGBC, LGROC	March 2002

10.2.2 Piloting LGs in Financial Management and Accountability

In FY 2003/4 the pilot local governments will implement the new process of financial and output reporting, revise their bank account structures and start maintaining the new books of accounts. The Phase 1 Local Governments will report against budget lines equivalent the pre-existing number of conditional grants, as the reduced number of sector budget lines will not have been agreed by the time of implementation.

Initially all the Phase 1 Districts/Municipalities should then be trained on the financial accountability and reporting modalities before the beginning of the 2002/3 financial year. As of July 1st 2002 the pilot local governments will use the new system of reporting and financial accountability.

Output	Actors	Target Date
Phase 1 LGs Trained in new financial management & reporting procedures	LGROC	April – May 2002
Restructuring of Bank Accounts	LGs	Mid July 2002
Maintenance of new Books of Accounts commences	LGs	1 st July 2002
1 st Quarter Report Prepared & Submitted by LGs	LGs	31 st October 2002

10.2.3 Management of Local Government Budget Process

The Draft RTBs and DTBs should be compiled by entering numbers into the agreed formats. The LGBC will then manage the budget cycle, and carry out the associated activities outlined in Section 5.

Output	Actors	Target Date
Budget Process		
Preliminary RTBs & DTBs compiled for pilot LGs	LGBC, LMs	Early Oct 2002
LGBFP workshop for Pilot LGs	LGBC, LMs	End Oct 2002
LGBFPs Submitted	LGs	Mid Jan 2003
Accept/Reject RTB Amendments	LGBC, LMs	Early Mar 2003
Integrate Amendments into MTEF	LGBC, MFPED	Late Mar 2003
BFP to Cabinet	MFPED	Early Apr 2003
Disseminate final RTBs & DTBs to LGs	LGBC	Mid Apr 2003

10.3 Phase 3: Up-scaling of RTS and DTS Countrywide

The target is to have the RTS and DTS fully operational by the beginning of the 2003/4 financial year.

Upscaling of LGDP - In the FY 2002/3 the LGDP should be up-scaled to cover the whole country to ensure that all local government are familiar with LDG modalities, and have been through one round of bottom up planning. This means the GoU-IDA Credit Agreement must be amended to cover all Districts/Municipalities in the country. At present, the bilateral-supported districts and the DDP districts are excluded. In short, LGDP must become a national system, not a WB project for some Districts/Municipalities. There must, however be a clear understanding of the importance of disciplined application of the access and performance conditions, and ensuring that there are sufficient LDG resources at sub-counties

and parishes to enable realistic choices over schemes. It is also important that the LGDP modalities are internalised within MoLG by September 2002, in time for the beginning of the budget process. The special capacity-building arrangements now being tested in weaker Districts/Municipalities by LGDP must be formalised to ensure that all local governments develop sufficient capacity to handle the new transfers systems effectively in 2003/4.

Updating RTS and DTS Modalities – It is important that, before the RTS and DTS are up-scaled that the lessons learnt from operating in the phase 1 Districts/Municipalities are incorporated into the Transfer Systems, and that the systems' modalities are revised accordingly. The performance of the systems should be reviewed in two phases. The first should review the financial accountability and reporting provisions in January 2003, to allow revisions to be made to the guidelines, and formats. This will also incorporate the agreed number of sector budget lines which will have been established during the sector policy reviews. The Financial and Accountability provisions will then be revised by the end of February.

In July 2003 a review of the Budgeting Modalities will take place. By the end of August the Budget Guidelines and Manuals will have been revised along with the Sector Guidelines taking into account the findings of the reviews.

Upscaling the RTS and DTS – All local governments will be trained in the Financial Management and Accountability Provisions between March and April 2003. All local governments will then implement the new modalities, effective 1st July 2003.

Local Governments will start implementing the budgeting process for the RTB and DTB in June October 2003. They will be trained in the new budget process at regional workshops in October, and the budget cycle will continue thereafter.

Output	Actors	Target Date
Up-scaling of LGDP Countrywide <ul style="list-style-type: none"> - LDG for all districts/municipalities - Internalisation of LGDP Modalities - Capacity Building For Weak LGs 	LGBC, MoLG	June 2002
Review of Operation of Reporting and Accountability Modalities.	LGROC, MFPED, LMs	Jan – Feb 2003
Revision of Financial & Reporting Modalities, Manuals & Guidelines	LGROC, MFPED, LMs	March 2003
Local Governments Trained in Reporting & Accountability Requirements.	LGROC, MFPED, LMs, LGs	April – May 2003
Reporting Systems Effective	LGs	1 st July 2003
Review of Planning & Budgeting Process	LGBC, LGFC, MFPED, LMs	July-August 2003
Revision of Planning & Budgeting Modalities, Manuals & Guidelines	LGBC, LGFC, MFPED, LMs	September 2003
Planning & Budgeting Systems Effective Countrywide.	LGBC, LGFC, MFPED, LMs	October 2003

10.4 Towards a Unified DTS

As stated above it is too early for government to commit to channelling all local government investment funds through LGDP mechanism within a unified DTS, where all local development funds flow via the LDG. There are prerequisites which must be completed before a decision can be made for the sector grants to be merged into the LDG.

Creating Awareness and Building Confidence in LGDP: MoLG must to build confidence amongst line ministries and donors that bi-lateral District/Municipality investment funds and the capital CGs can be safely and effectively routed through LDG, and that there are significant benefits (of governance building, local ownership, local contribution and improved O&M) in so-doing.

Reconciliation Between SWAp and LDG Approach: Extensive discussions need to be held on how the national sector targets set via the SWApS can be relaxed in favour of the community driven decision making process used by LGDP, where investment levels aren't known beforehand. The evidence from the five DDP districts is that DDP-LGDP methodology delivers very similar outputs to the capital CGs, but with major advantages in terms of governance building, local ownership, local contribution and future O&M. However relaxing the national sectoral targets in favour of multi-sectoral local choice (and in the knowledge that some Districts/Municipalities and LC3s may have periods when they are ineligible to access to LGDP funds due to non-compliance) will clearly be a sensitive issue, requiring full discussion with sector ministries, donors and MoLG.

Piloting the merging of capital grants into LGDP: It is not proven that LGDP can deliver investments on the scale needed to rebuild the infrastructure of a sector countrywide – this is ongoing under the SFG programme, and PHC. Before moving towards a unified DTS this must be established.

At present the allocations for SFG are nearly twice the levels as that for the LDG, and overall conditional grant development financing is nearly four times as big. Donors also will be unlikely to switch sector support to the LGDP mechanism if this has not been proven to handle investments at a large scale.

Implementation. After the expansion and piloting of LGDP, the conditional grant mechanism may prove to be the best way for delivering large-scale sector investments. If this is the case the DTS would remain in its original form

If, instead, the LGDP system does indeed prove to be the most efficient and effective transfer mechanism for financing infrastructure provision in Local Governments, then the 3.5 capital grants should be merged into LDG within a unified DTS.

This would simply involve the simplification of the Interim DTS, with the DT Budget having a single component – the LDG, as opposed to having five and increasing the LDG allocation accordingly.

Output	Actors	Target Date
Confidence Building in LDG	LGBC, MoLG	2003/4
Reconciliation of SWApS with LDG approach	LGBC, LMs, Donors	2004/5
Piloting of Unified DTS	LGBC	2004/5
Implementation	LGBC	2005/6

Task	Action By	Target Complete	2001/02		2002/03				2003/4			
			Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
PHASE 1: ESTABLISH THE OPERATIONAL MODALITIES FOR THE RTS AND DTS												
1.1 Setting up of LGBC & LGROC												
LGROC & LGBC Set up	LGFC LMs MLG MFPED	Early Mar 2002	?									
LGFT Trained on Decent. & LGDP	Members LGFT	Early Mar 2002	?									
1.2 LM Cells working on LGs Set Up												
LM cells working on LGs Set Up	LMs	Early May 2002		?								
Cells Trained on Dec. & LGDP	LMs	Early May 2002		?								
1.3? Cap'ty of MoLG, LGFC, MFPED												
Assess Institutional Set Up	MoLG, LGFC, MFPED	Early April 2002		?								
Institutional Reorientation	MoLG, LGFC, MFPED	Early May 2002		?								
Appoint of Key Responsible Officers	MoLG, LGFC, MFPED	Early May 2002		?								
1.4 RTB & DTB Modalities & Allocation Formulae												
TORs for Review of LG Allocations	LGBC, LGFC, LMs, ULAA	Early Mar 2002	?									
Allocation Review Commences	LGBC, LGFC, LMs, ULAA	Mid Apr 2002		?								
Stage1: Allocation Principles	LGBC, LGFC, LMs, ULAA	End Apr 2002		?								
Stage 2: RTB & DTB Frameworks	LGBC, LGFC, LMs, ULAA	End Apr 2002		?								
Stage 3: RTB & DTB Manuals	LGBC, LGFC, LMs, ULAA	End Jul 2002			?							
1.5 Sector Transfer Policy Reviews												
TORs for LM Transfer Policy Reviews	LGBC	Early Apr 2002		?								
Transfer Policy Reviews Commence	LMs	Mid May 2002		?								
Stage 1: Sector RTB & DTB Policies	LMs	End Jul 2002			?							
Stage 2: Sector Manuals and Guides	LMs	End Aug 2002			?							

Task	Action By	Target Complete	2001/02		2002/03				2003/4			
			Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
1.6 Finance & Admin. Costs												
LG Restructuring Study Commences	MoPS	Dec 2002										
Staff Structures for Pilot LGs	MoPS	End May 2002		?								
Operational Cost Estimates	LGBC, LGFC, MoLG	End Aug 2002			?							
Draft UCG Allocations	LGBC	End Aug 2002			?							
1.7 Reporting & Accountability Prov.												
TORs for Rep. & Acc. Provisions	LGROC	Mid March 2002	?									
Review of LGFAR + Amendments	LGROC, LMs	End March 2002	?									
Rep. & Acc. Provisions Complete	LGROC, LGFC, MFPED	End Apr 2002		?								
1.8 Donor Funding Modalities												
Principles of Donor Funding Discussed	LGBC, Donors	March-June 2002		?								
Donor Modalities Agreed	LGFT	July 2002			?							
PHASE 2: Pilot Implementation of RTS & DTS in 15 LGs												
2.1 Identification of Pilot LGs												
12 Districts & 3 Municipalities Selected	LGBC, LGROC	March 2002	?									
2.2 Pilot of Rep. & Acc. Provisions												
Phase 1 LGs trained in Rep & Acc	LGROC, MFPED	April- May 2002		?								
Restructuring of Bank Accounts	LGs	Mid July 2002			?							
Maintain New Books of Accounts	LGs	1 st July 2002			?							
1 st Quarter Report	LGs	31 st Oct 2002				?						
2.3 Pilot of New Budget Process												
Draft RTBs & DTBs for Pilot LGs	LGBC, LMs,	Early Oct 2002				?						

Task	Action By	Target Complete	2001/02		2002/03				2003/4			
			Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
LGBFP Workshop for Pilot LGs	LGBC, LMs, Pilot LGs	End Oct 2002				?						
LGBFPs Submitted by pilot LGs	Pilot LGs	Mid Jan 2003					?					
Accept/Reject RTB amendments	LGBC, LMs	Early Mar 2003					?					
Integrate Amendments into MTEF	LGBC, MFPED	Late Mar 2003					?					
BFP to Cabinet	MFPED	Early Apr 2003						?				
Disseminate RTBs & DTBs to LGs	LGBC, MFPED	Mid Apr 2003						?				
LG Budgets Finalised & Read	Pilot LGs	Mid June 2003						?				
PHASE 3: Upscaling of RTS & DTS Countrywide												
3.1 Upscaling of LGDP												
Up-scaling of LGDP Countrywide	LGBC, MoLG	June 2002			?							
3.2 Upscale Rep & Acc Modalities												
Review of Rep. & Acc. Modalities	LGROC, MFPED, LMs	Jan-Feb 2003					?					
Revise Rep. & Acc. Mod's & Manuals	LGROC, MFPED, LMs	March 2003					?					
All LGs trained in Rep & Acc Modalities	LGROC, MFPED, LMs	April-May 2003						?				
Rep. & Acc. System Effective	All LGs	1st July 2003							?			
3.3 Upscale Plan. & Budget Process												
Review of Plan. & Budgeting Process	LGROC, MFPED, LMs	July-Aug 2003							?			
Revise Plan. & Budg. Mod's & Manuals	LGROC, MFPED, LMs	Sept 2003							?			
Plan. & Budg. System Countrywide	LGROC, MFPED, LMs, LG	Oct 2003								?		
6 TOWARDS A POSSIBLE UNIFIED DTS												
Confidence Building in LDG	LGBC, MoLG	2003/4										
Reconciliation of SWAps with LDG	LGBC, LMs, Donors	2004/5										
Piloting of Unified DTS	LGBC	2004/5										
Implementation (If Agreed)	LGBC	2005/6										

ANNEX 1: RECURRENT TRANSFERS- The Present Situation

1.1 Overview

Recurrent activities of local governments are financed through central government transfers in three ways – Conditional Grants, Unconditional Grant and the Equalisation Grant. These recurrent transfers make up about 80% of total transfers to local governments.

1.2 Conditional Grants

75% of all CG transfers to LG are for recurrent expenditure. The size of recurrent CGs and the flexibility which Districts/Municipalities have in their use is almost entirely determined by line ministry policy as reflected in the CG guidelines (health staff numbers and wage costs, UPE policy, the number of agriculture extension workers and their operating costs etc.)

The vast majority funds for conditional grants are come from the PAF, and are tied to key sectors in the PEAP: Primary Education, Primary Healthcare, Water and Sanitation, Rural Roads and Agriculture Extension.

There is a uniform system for planning, reporting and transfer of funds for grants from the PAF. The key features of the current system are :-

?? Guidelines for the PAF- CGs have been prepared by line ministries on the basis of general guidelines prepared by MoFPED. According to the guidelines, Districts/Municipalities have, in principle, greater discretion in priority-setting, although the real level of discretion remains limited;

?? Quarterly transfers on the basis of quarterly workplans.

?? Releases are conditional on submission to line ministries of workplans, quarterly reports, and cumulative quarterly reports covering financial and physical progress;

The PAF-system is designed to fit the Budget Framework Paper (BFP) system. Budget ceilings are announced before the LG Budget process begins. LGs use the budget ceilings as the basis for the sector workplans. When the workplans have been approved by the respective LMs, there are limited possibilities to increase or decrease the budgeted amounts, and no reallocations can be made from one grant to another. The access and compliance criteria in the revised PAF system are thus the submission of workplans, budget estimates and quarterly reports to the line ministries.

1.3 Unconditional Block Grant

Section 193(2) of the Constitution defines unconditional grant (UCG - also known as the block grant) as follows : *“Unconditional Grant is the minimum grant that shall be paid to local governments to run decentralised services, and shall be calculated in the manner specified in the Seventh Schedule to this Constitution.”* The Seventh Schedule provides the formula for the annual up-rating of UCG in line with price and wage increases and the *“..budgeted cost of running added or subtracted services”*.

Each year, MoFPED announces the UCG allocation as part of the Budget Framework process to allow LGs to incorporate the allocation in their planning and budgeting process. Over the past three years, UCG has increased in absolute and real terms, but, as a share of all transfers, UCG has fallen from 24% to 15%, due to the rapid growth of CG financing. The UCG is transferred from the consolidated fund. There are no reporting requirements to central government over use of the UCG.

In 2000/01, the budget for unconditional grants is UGS 79 bn.⁵ (\$44m). Until this year, only districts were eligible for UCG, but from 2000/01 13 municipalities benefit as well. The grant makes up about 20% of recurrent transfers.

⁵ The Health Staff Lunch Allowance CG was consolidated into the UCG in 2000/01.

The UCG is distributed across Districts/Municipalities according to a formula including a flat-rate allocation for each District/Municipality (UGS 150m.) plus an allocation based on area (15% weight) and population (85% weight). There are also some minor historic transfer items (accounting for 10-15 % of the total) whereby the UCG for some Districts/Municipalities includes financing for special tasks including security.

Currently the Unconditional Grant is being used almost entirely for management and administrative staff at the District/Municipality level. The reasons behind this is examined in a separate paper on Finance and Administration Costs.

1.4 Equalisation Grant

The newly-introduced Equalisation Grant is meant to provide funds to Districts/Municipalities with low revenue potential, and/or higher costs of delivering services to the people. The allocation is based on a formula which aims to “equalise” revenue potential and service delivery costs. The funds allocated so far have been small and funds can be used in any priority areas, following central approval.

1.5 Successes and Benefits of current system

- ?? The conditional grant system has allowed a dramatic increase in services to the people in the last four years – UPE, Health Services, and Road Maintenance
- ?? In an environment of limited District/Municipality capacity in financial management and administration the conditional grants have ensured that funds are going to directly towards the achievement PEAP goals.
- ?? The requirement of separate bank accounts for different sector grants has compensated for weak book keeping skills and mechanisms for reporting and accountability has limited the misuse of funds.
- ?? The setting of conditions has ensured that local governments adhere to national policies and priorities.
- ?? The provision of funds for monitoring and statutory bodies at Districts/Municipalities from PAF has improved
- ?? Central Government Institutions have been empowered to take on their mandates for the provision of technical support, back up and quality assurance.
- ?? In most sectors the conditional grant system does allow discretion over expenditures within grants.
- ?? The unconditional grant has allowed local government some discretion over central transfers, albeit limited.

1.6 Disadvantages of Current System

- ?? There is no discretion for local governments to change allocations between sectors under conditional grants according to local priorities, and this undermines autonomous local government.
- ?? There are twenty-two conditional grants for recurrent financing, all having different conditions attached, reporting requirements and each requiring separate bank accounts. This multiplicity leads to excessive administrative burdens and affects the utilisation of budgeted funds. The proliferation of bank accounts in itself is a fundamental blockage to improved accountability and transparency and cannot be justified solely as a response to weak bookkeeping capacity.
- ?? There is limited capacity at the centre to manage the reports for all Districts/Municipalities. This devalues the system and turns it into “paper for money”.
- ?? There is little or no coordination of monitoring and technical support provision by central institutions.

- ?? The sector guidelines and policies largely bypass local government structures, and so lower local governments have little involvement in planning and little information about the services that should be being delivered in their areas.
- ?? District/Municipality sector staff are seen increasingly as local officers of the line ministries implementing line ministry programmes. Line ministries often communicate directly to sector staff as opposed to through the CAO.
- ?? There is anecdotal evidence that the Unconditional Grant is financing less productive staff and activities in many Districts/Municipalities, and that, because of mingling with local revenue, councillors can access UCG transfers to supplement their emoluments and expenses.
- ?? Local Government finance and administration costs are inadequately financed through the Unconditional Grant and this is having a negative impact on service delivery. This is a particular problem in small Districts/Municipalities, since the cost of the core District/Municipality staff is effectively fixed, whilst the UCG is determined by area and population.
- ?? There is a clear inconsistency in the fact that nurse and teacher salaries are secured as a result of conditional PAF grants, whilst the financing of the senior and support staff, on whom they depend, is increasingly unpredictable.
- ?? The large increase in resources over recent years from central government has undermined the incentives for local governments to increase local revenues.
- ?? Much of the local government payroll is managed centrally via the conditional grant payroll. This has led to delays in individuals gaining access to the payroll. Pensions are also a major expenditure which has not been catered for properly.

ANNEX 2: DEVELOPMENT TRANSFERS – The Present Situation

2.1 Summary of the Current Situation

At present transfers to local governments for development financing mainly use the conditional grant modality funded via the PAF.

Only three conditional grants: PHC Development, School Facility Grant and Rural Water and Sanitation are mainly for capital development. The Rural Roads Grant is a combination of recurrent (routine maintenance) and capital (periodic maintenance)⁶.

There are also two multi-sectoral donor funded grants which are channelled through the Budget:

- ?? The District Development Grant under the World Bank funded Local Government Development Programme.
- ?? The Netherlands funded District Development Grant for 7 districts, which is under the Poverty Action Fund.

Since 1998, district capital financing under PAF has increased from almost zero to UGS 82bn. in 2000/01. The share of capital funding in the total PAF transfer to Districts/Municipalities is 24% in 2000/01. The sensitivity of the PAF Development financing to PEAP goals is high since all PAF CGs are allocated to the PEAP priority areas 3 and 4.

There is a uniform system for planning, reporting and transfer of funds for grants from the PAF. The key features of the current system are :-

⁶ The Rural Water Grant is a combination of recurrent costs (including salaries), and investment costs., but the investment costs are much the largest element, and this grant is therefore included as a development grant.

?? Guidelines for the PAF-CGs have been prepared by line ministries on the basis of general guidelines prepared by MoFPED. According to the new guidelines, Districts/Municipalities have, in principle, greater discretion in priority-setting, although the real level of discretion remains limited;

?? Quarterly transfers

?? Releases are conditional on submission to line ministries of workplans, quarterly reports, and cumulative quarterly reports covering financial and physical progress;

The PAF-system is designed to fit the Budget Framework Paper (BFP) system. Budget ceilings are announced before the LG Budget process begins. LGs use the budget ceilings as the basis for the sector workplans. When the workplans have been approved by the respective LMs, there are limited possibilities to increase or decrease the budgeted amounts, and no virement can be made from one grant to another⁷. The access and compliance criteria in the revised PAF system are thus the submission of workplans, budget estimates and quarterly reports to the line ministries.

2.2 Benefits of Current System (Conditional Grants)

?? Interventions are directly linked to the achievement of targets set in sector investment plans, and hence PEAP Goals.

?? There has been a huge increase in investments in the infrastructure of key sectors – classrooms, water points and health centres are being built.

?? Sector guidelines ensure that investments are being made in line with central government policy.

?? The investments being made give better value for money than those made under conventional donor funded projects.

?? There is donor confidence that their budget support is being spent on poverty focused investments; i.e. they know beforehand what their budget support will be spent on building of classrooms.

?? Central Government Institutions have been empowered to take on their mandates for the provision of technical support, back up and quality assurance.

?? The conditional grant system enables the tracking of finances going to Districts/Municipalities for different sector interventions.

2.3 Problems with the Current System

In the development of sector policies there has largely been little investigation by line ministries of the relationship between decentralisation and sector wide approaches. This means that the policies and guidelines developed by the ministries for local governments have led to de-concentration rather than decentralisation of service delivery. This has had the following implications:

?? There is little flexibility for investments within sector conditional grants, and so they are not always responsive to specific community needs. (e.g. you can't build teachers' houses or culverts under the current Conditional Grants)

?? There is little local ownership of investments made, which has serious implications on their sustainability.

?? Lower local councils are not involved in the planning, allocation, and procurement of investments.

?? Local Government Heads of Departments are increasingly operating as local officers of line ministries, as opposed to officials working for the local government.

⁷ There are examples of district allocations for particular grants being changed very substantially, necessitating complete redesign of LG workplans.

- ?? Guidelines do not use local government structures, and therefore do not promote local political ownership and accountability.
- ?? At present no development conditional grants remit funds to subcounties, and this means that the LC3 level of local government is almost always bypassed. Many LC3s don't even know what activities should be going on in their subcounties, let alone the intended beneficiaries.
- ?? Criteria used for allocation of funds is often unclear and inequitable.
- ?? The system is sector exclusive – under the conditional grant mechanism, if a sector is not funded by a grant it is not funded at all from central government even if it is a local priority.

ANNEX 3: SWAPS AND DECENTRALISATION

The relationship between sector strategies and decentralisation is currently poorly articulated and unresolved within government. The legislative framework, which, to simplify, makes Central Government responsible for policy, standards and monitoring, and Local Government responsible for service delivery, is poorly internalised. The statements of some senior line ministry officials suggest that they are entirely unaware of the provisions of the Local Governments Act. This is because:

- ?? The way in which sector policy might be harmonised with strengthening local government and local governance has scarcely been examined. Awareness that an issue even exists is low. The need to harmonise central and local budgeting planning processes (as discussed above) depends on reconciliation sectoral and local roles and responsibilities.
- ?? The different approaches of sectoral CGs and the non-sectoral DDP-LGDP and the tension that arise from the top down approach resulting from sector planning and targeting on the one hand and the bottom up approach of community choice and local governance building on the other have not been discussed by central government.

Sector ministries need to take steps to examine the relationship between decentralisation and sector/SWAP strategies. This might include : seminars to raise awareness of the issues; commissioned work on sector-local roles and responsibilities in different sectors at present; the extent to which sector programmes support or undermine local governance; reviews of pipe-line initiatives in terms of their impact on decentralisation and local governance.

ANNEX 4: THE SIMILARITIES AND DIFFERENCES BETWEEN THE PROPOSED AND CURRENT SYSTEMS

4.1 Similarities and Differences of RTS from Current System

4.1.1 Similarities

- ?? Funding is still tied to the achievements of PEAP Goals, and fully consistent with sector wide approaches.
- ?? Unconditional, Conditional and Equalisation grants exist in the current system and the proposed RTS.
- ?? Funds will continued to be released against line items, i.e. sector conditional grants, UCG and EG.
- ?? Programmes funded by PAF can still be supported through the single RTS.
- ?? Releases in a quarter are still based on the submission of quarterly accountability.

- ?? There will remain reporting on outputs in each sector.
- ?? Sector ministries will still play an important role in advising on releases to local governments, and any sanctions required relating to sector performance.

4.1.2 Differences

- ?? Through the RTB process, Local Governments will be allowed some discretion in allocating funds across conditional grants, so long as they have met minimum criteria.
- ?? The number of conditional grants (or sub budget lines) within recurrent transfers will be reduced, resulting in greater LG discretion within sectors.
- ?? Sector policies and guidelines will be more “decentralisation friendly” and take account of local government structures.
- ?? Releases will be monthly as opposed to quarterly, as recurrent activities, on the whole do not require lumpy releases.
- ?? There will be one recurrent release each month per District/Municipality, and not separate releases for PAF and non-PAF.
- ?? Funds will be transferred into reduced number of accounts, either a single RTS account or directorate accounts, as opposed to separate accounts for each conditional grant.
- ?? The quarterly report on expenditures must be reconciled with a statement of the RTB bank account/Directorate accounts.

4.2 Differences and Similarities Between the Current System and the DTS

4.2.1 Similarities of two systems

- ?? Both systems provide investments sensitive to PEAP Goals and in the same sectors e.g. education, health, water, roads and agriculture.
- ?? Sector grant allocations are made specifically towards the achievements of sector targets.
- ?? There is no evidence of difference in quality of investments made by sector grants and the LDG.

4.2.2 Differences with Current System

- ?? Under the proposed DTS there is a discretionary grant providing all investments locally, which supplements the allocation to specific sectors via conditional grants.
- ?? The intended outputs of the LDG allocations are not known beforehand. Access to LDG funds is based on criteria relating to governance, as opposed to just being procedural.
- ?? There is full involvement of local government structures in the planning, reporting and allocation processes under the DTS/LGDP.
- ?? Under DTS/LGDP capacity building is taken care of explicitly via the capacity building grant which local governments can access if they do not meet the required standards.

