FRAMEWORK ON STATE PUBLIC FINANCIAL MANAGEMENT REFORM

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1. PURPOSE OF THE FRAMEWORK

The purpose of this State Public Financial Management Framework document is to set out the reforms in public financial management that the GoSS Ministry of Finance & Economic Planning (MoFEP) expects States to undertake. These reforms are required to ensure that all levels of government in Southern Sudan operate on a standardised public financial management system. They are also required so that MoFEP discharges its duty under the Presidential Decree on Functions & Duties of GoSS Ministries to "develop and implement a sound public financial management system for Southern Sudan."

The reforms States must introduce to their PFM systems will mirror those that have already been, or are in the process of being, introduced at the GoSS level. These reforms will be adapted so that systems, processes and procedures are suited to the circumstances faced by the States.

MoFEP has already produced Guidelines for Integrated State Planning & Budgeting. This framework therefore deals with the remaining steps in the Public Financial Management cycle: Budget Execution, Accounting and Reporting, and Internal Audit. The remainder of this document sets out the reforms required in each of these areas.

The reforms States must introduce are as follows:

1. Appropriation Act

All States must enact an Appropriation Act. The Appropriation Bill is passed by the State Legislative Assembly when it approves the Annual State Budget. The Appropriation Act provides the required legal framework for budget execution and the legal basis for expenditure procedures. It ensures that there is legal authorisation for expenditure of States resources.

2. Treasury Single Account and Centralised Payment System

All state governments are required to implement a centralised system of cash management, the Treasury Single Account system (TSA). This centralised system of cash management will be accompanied by a centralised payments system. This is to ensure that the State has a complete and accurate record of all financial transactions. States will either manage this through a system of manual registers accompanied by simple spreadsheets, or through an electronic Financial Management Information System (FMIS). This will be rolled out to five States in 2010, and a further five States in 2011.

3. Commitment and Payment procedures

All State Governments are required to develop Procedures for controlling commitments and payments. These procedures set out the processes for managing the Treasury Single Account and centralised payment system. The payment procedures set out how State Spending Agencies gain access to the resources they are allocated in the State Budgets. These payment procedures will also enforce internal controls to ensure that the State PFM system is being managed effectively and efficiently. Procedures for the use and reporting of petty cash advances will also be introduced at State level.

4. Internal audit

State Internal Audit Units must be established where they do not exist, within the State Ministry of Finance, to advise and carry out reviews on internal controls, in addition to the performance of the audit function.

5. Budget Execution Reports

States must be able to produce in-year budget execution reports showing the expenditure of different agencies against their approved budget. These will show the total expenditure of the State against each item in the budget, as well as the expenditure of each State Agency against each item in its budget. Where a State has implemented an electronic FMIS, this will generate budget execution reports and help the State ensure that reports are accurate, timely and reliable. Where an FMIS is yet to be introduced, these reports must be generated manually.

6. Financial statements

As well as preparing in-year Budget Execution Reports, States must also prepare final financial statements. An accounting manual will be developed by MoFEP which will provide the necessary rules and guidance for preparing financial statements. Financial statements must be prepared on an annual basis. They are then subjected to an external audit by the Southern Sudan Audit Chamber.

MoFEP has a realistic assessment of the speed with which States will introduce these reforms. They will take time. However, it is up to each State to ensure that it starts taking steps to achieve each of these reforms. MoFEP will continually engage with States to assess their progress. It is recognised that each State is unique, and the progress they will make is dependent on their existing capacity and the level of support they receive, both from MoFEP, and from development partners.

MoFEP expects development partners to help States implement the reforms set out in this Framework on State Public Financial Management Reform, and to ensure their support is aligned with this Framework. This is important so that there is uniformity in the public financial management systems across the various levels of Government in the States and GoSS.

2. BASIC PRINCIPLES OF A PUBLIC FINANCIAL MANAGEMENT SYSTEM

Definition of Public Financial Management

Public Financial Management (PFM) supports the effective and accountable use of public resources and helps to underpin fiscal discipline.

Fiscal discipline means that there is effective control of the budget by setting ceilings on expenditure. It requires overall expenditure control, without which it is impossible to achieve effective prioritisation and implementation of policy priorities and programmes.

The basic objectives of public financial management are to:

1. collect sufficient resources from the economy in an efficient and effective manner that minimises harm to economic activity
2. allocate resources in accordance with government priorities
3. utilise resources in an effective an efficient manner to ensure that services are delivered, and programmes implemented, cost-effectively.

The Public Financial Management Cycle

The Financial Management cycle shows the order of the different processes. These processes include the following activities:

- Planning and Budget formulation: as well as allocation of the State's own resources, there must be coordination with development partners on the activities they will fund and implement in the State
- Budget execution: management of financial operations (revenue, commitments and payments, procurement, controls, and cash management)
- Accounting and reporting and
- Internal audit and evaluation

3. BUDGET EXECUTION

An efficient Budget Execution system requires that:

1. Budget implementation is carried out according to authorisations in the law
2. Adaptations/adjustments can be made during execution of the budget to address significant unforeseen challenges or changes in the circumstances the State faces
3. Problems arising during implementation are resolved and
4. The raising and use of resources are managed efficiently and effectively.

The system of budget execution should ensure:

- Rigorous aggregate expenditure control and
- Effective and efficient use of resources according to budget priorities.

The main features of an efficient budget execution system are:

- Payment processes and internal controls that ensure probity, economy and efficiency in managing public funds, assets and liabilities
- A Cash Management System
- Expenditures are correctly classified and reported, and
- Internal and external audit systems that will provide assurance that public expenditure management procedures achieve the necessary standards of legal compliance, efficiency and effectiveness

Development of Legislation – An Appropriation Act

The starting point to the reform of the State Budget Execution System is the development of an Appropriation Act to provide the legal framework for budget execution, and the basis for the appropriation management rules and payment procedures to follow. The Act will govern how the budgets are to be executed and prescribe rules and regulations to guide budget spending.

A template Appropriation Act will be made available to assist States in developing their own Appropriation Act. State Appropriation Acts should be modelled on the GoSS Appropriation Act 2010. Whilst States will be able to develop an Appropriation Act that meets their State's specific needs, it must contain the following provisions:

(i) Setting of Limits to Expenditure

To ensure that overall public spending is limited to available resources, budget ceilings will be established for each Spending Agency based on revenue availability and expenditure priority within the limits of the appropriations approved for each Spending Agency. No expenditures other than those authorised by the Act can be made. All expenditure must be charged against the relevant Spending Agency, according to the appropriate chapter and budget line. No expenditures can be charged against the reserve.

(ii) Procedures for in year budget revisions

The Appropriation Act will set out procedures to guide an Agency on how to adjust their budgets during the year from within their budget ceilings. It will set out the procedures and approvals for the transfer of funds between budget lines within the same chapter (salaries, operating, capital). Funds cannot be moved between chapters (e.g. from capital to operating) without the approval of the State Assembly through a Supplementary Appropriation Act.

In order to spend surplus funds over revenue estimates or funds, out of the legal reserve, a Supplementary Appropriation Act must authorise the spending.

(iii) Supplementary Budgets

Spending Agencies can only increase their overall expenditure with approval from the Assembly, through a Supplementary Budget presented by the State Minister of Finance on behalf of the Governor. A Supplementary Appropriation Act must also be enacted by the State Legislative Assembly to provide authorisation for the Supplementary Budget.

(iv) Carry over into the following year

Appropriated funds not spent by the end of a financial year cannot be carried over into the next financial year. All funds in Agency's accounts at the end of the financial year will revert to the Consolidated Fund and form part of the General Reserve.

(v) Legal basis for payment procedures

Until the GoSS Public Financial Management Act is passed, and similar Acts are passed at the State level, the Appropriation Act must provide the legal basis for the payment procedures to be established by the Minister of Finance. The Appropriation Act must State that expenditures from the State Consolidated Fund must be made in accordance with the payment procedures.

(vi) Responsibilities of Accounting Officers

Again, until the GoSS Public Financial Management Act is passed, and similar Acts are passed at the State level, the Appropriation Act must also define and set out some of the duties of Accounting Officers. Accounting Officers are the Director General of the State Ministry, or the senior civil servant in a non-Ministerial Agency. They are responsible for making all requests for expenditure from their Agency's budget to the State Ministry of Finance.

4. TREASURY SINGLE ACCOUNT AND CENTRALISED PAYMENT SYSTEM

The Treasury Single Account (TSA) centralises all Government funds in a single set of accounts controlled by the State Ministry of Finance. A centralised payment system ensures that the State Ministry of Finance has an accurate and comprehensive record of all commitments and expenditures of the State Government. It ensures that the cash available to the State can be used effectively and directed to the State's priorities and that the State's expenditures can be reported accurately.

Treasury Single Account

The TSA is a bank account or set of accounts through which Governments transact all revenue and payment transactions. Elements of the TSA include daily cash balances and transactions recorded according to a uniform classification system.

For efficient budget implementation, it is necessary to ensure that revenue is collected and deposited into government's treasury in a timely manner, claims are paid according to contract terms and payments are made efficiently and on a timely basis.

Director Generals of Finance have the responsibility to establish systems and procedures to ensure that there is sound cash management, thereby mitigating the risk of Government running out of cash to meet its cash flow needs.

Cash management is also concerned with the most effective and efficient way of paying approved disbursements.

The main objective of a payment system is to ensure that government's obligations are paid in a timely and cost effective manner, liquidity is managed and opportunities for theft or fraud are minimised or eliminated.

To implement reforms in cash management, States are required to establish centralised systems similar to the system in use at GoSS. This will enable them to implement the payment and petty cash procedures which will be developed as part of the reform process.

Banking Arrangements

Government Bank Accounts include all bank accounts opened for receipt or payment of public funds and includes all revenue accounts, Treasury block accounts, Spending Agencies' operating accounts and accounts for donor projects managed by the State.

Each Spending Agency should have only one bank account for all its operations unless approved otherwise by the Director General of Accounts.

Where there are no banking facilities in a State, MoFEP will work with that State to develop procedures for managing and handling cash which meet acceptable standards.

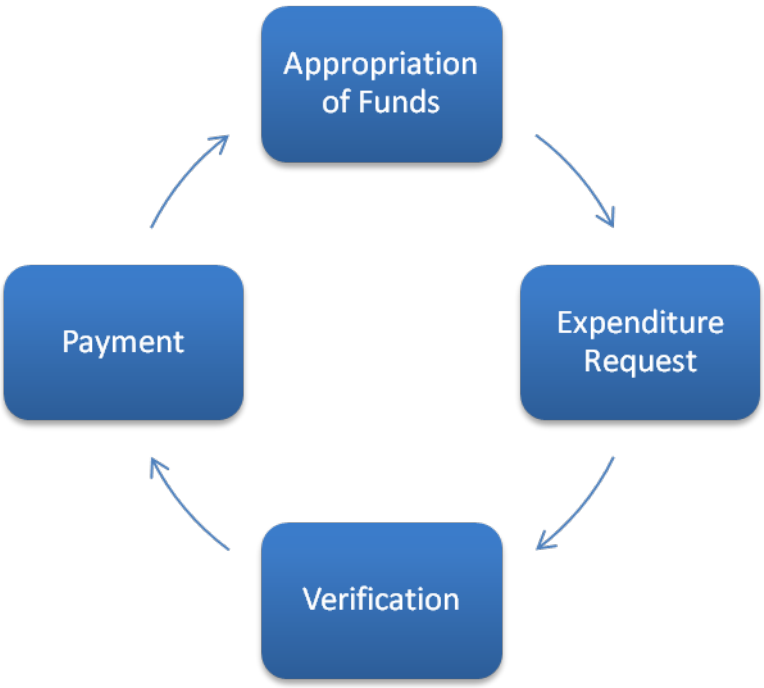
Centralised Payments Process

Payments must be made in accordance with payment procedures which must be set by the State Minister of Finance. These should be based on the GoSS payment procedures.

The procedures should provide clear rules and instructions for the expenditure of public funds approved in the annual budget. If the procedures are followed, they will ensure:

- Segregation of duties to enforce internal controls.
- Full accountabilities for all expenditures
- Accurate tracking of the approved budget execution
- Enable accounting of all expenditures using the prescribed Chart of Accounts and
- Comprehensive, accurate and meaningful expenditure reporting

The payment procedures are designed to safeguard government from paying incorrect claims and help control spending within the Approved budget. Internal controls in the payments process aim to ensure that the State finances are efficiently and transparently managed, functions are carried out in the proper manner, accounting records are complete and accurate and fraud and error are prevented. The Director General of Finance is responsible for ensuring that the payments process and the systems of internal controls it sets out are effective and adhered to.



The payment process consists of the following steps:

Appropriations made to spending agencies – the Appropriation Act provides legal authorisation for Spending Agencies to incur expenditures.

Agencies request expenditures – to access their approved funds, Agencies make a payment request to the State Ministry of Finance. The request must come from the Accounting Officer of the Agency, who is the Director General, or other senior civil servant in a non-Ministerial Agency. This payment request should be done on a prescribed from. It should show the budget line against which the payment is being requested, and should be accompanied by supporting documentation (e.g. an invoice) to verify the payment request.

Verification of the expenditure request – the State Ministry of Finance must verify the payment request. It should ensure that the expenditure request is classified correctly, that there are sufficient funds in the budget to meet the request, and that the request has the necessary supporting documentation (such as an invoice or evidence of receipt of goods or services). Once the request is verified, it should be recorded as a commitment against the Agency's budget.

Payment – once the request has been verified, approval to pay can be given if there is sufficient cash available for the payment to be made. The duties of verifying an expenditure request, and giving approval for payment, must be segregated to ensure internal controls are enforced. These internal controls will ensure appropriate procedures are followed, and supporting documents and payment requests are accurate. Once payment is made, the payment must be recorded in a cash book, and also recorded as an expense against the correct budget line of the Agency.

The aim of the payment process to ensure that use of State resources is properly authorised and controlled according to the Budget approved by the State Assembly.

Commitment controls

When an Agency signs a contract to acquire goods or services it makes the government liable to pay on the receipt of such goods or services. This requirement to incur expenditures is known as a commitment.

Commitment controls play an important role in developing an overall expenditure control framework, the key objective being the management of the initial stages of incurring the commitment.

States have to develop commitment controls to address the problem of Spending Agencies entering into contractual obligations for expenditures that are not in the Approved budget. A centralised commitment control system would require:

(a) Spending Agency to submit a commitment request to State Ministry of Finance prior to making the order or signing the contract for goods and services; and
(b) The commitment is recorded against the budget of the agency, ring-fencing the funds to prevent over-spending. If there is not sufficient funding for the contract or order in the Budget, the Ministry of Finance must ensure the agency does not proceed with the order/contract.

To minimise the incidence of Spending Agencies entering into unbudgeted contracts, the Appropriation Act will contain rules to deal with contractual obligations and require all contracts above a certain value to be approved by the State Minister of Finance. This is to certify that there is sufficient budget coverage. The contract can then be presented to the State Legal Affairs Office for authentication.

In addition, all contractual obligations involving payments that fall after 31 December in the budget year are controlled by requiring the approval of the Minister of Finance and if over a limit (to be set), submitted to the Assembly prior to signature.

Spending Units should be required to record as obligations against appropriated funds, all orders for purchases of goods or services at the time the order is placed or contract signed.

Petty cash advances

To ensure that Agencies have enough funds for their day-to-day activities without having to submit a payment request to the State Ministry of Finance, it is permissible for a petty cash advance to be automatically released to each State Agency each month without them having to request these funds through the normal payment process.

The State Ministry of Finance will need to provide guidance on the use and reporting of petty cash. The GoSS petty cash procedures can be adapted and used. For instance, the State Ministry of Finance will be required to determine the amount of petty cash to be advanced to its Spending Agencies, the types of expenditure that can be incurred and the size of payments that can be made using the petty cash advance. Most importantly, the State Ministry of Finance will need to ensure that Agencies account to it for how the petty cash advance is spent, and require accountabilities before the next advance is made.

5. ESTABLISHING FUNCTIONAL INTERNAL AUDIT UNITS

The Ministry of Finance & Economic Planning aims to improve the capacity of the internal audit function across GoSS and States. This is to enable internal audit to assist government institutions and officials to improve their systems of internal control and so reduce the incidence of waste, fraud and corruption. An effective internal audit system will also contribute to efforts to improve the effectiveness, efficiency, transparency and accountability of mobilisation, use and safeguarding of government resources. This objective can be achieved if professional internal audit units are established with sufficient capacity is to enable them conduct professional internal audits that add value to their institutions.

Definition of Internal Auditing

The Institute of Internal Auditors (IIA) defines Internal Auditing as “an independent objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”

As part of its activities, internal audit will examine and objectively appraise the adequacy and effectiveness of internal controls and report to senior management regarding the functioning of its systems.

Objectives of Internal Audit

The Internal Audit unit should appraise the soundness and application of accounting, financial and operational controls and review and report on the following:

- Adequacy of controls over the receipt, custody and use of financial resources
- Compliance with financial and operational procedures
- Correct classification of revenue and expenditure
- Reliability of and integrity of financial and operational data to ensure accurate preparation of financial statements and other reports
- The systems for safeguarding assets and their verification
- Operations or programmes to ascertain consistency of results with established objectives and goals
- Adequacy of management’s reaction in response to internal audit reports
- Adequacy of controls built into computerised systems

Structure of internal audit

The responsibility to ensure that an effective functioning internal audit unit exists lies with the Director General of Finance who should make sure that adequate resources are made available to enable audit plans to be implemented.

Purpose, Authority and Responsibilities of internal Audit

The purpose, authority and responsibilities of internal audit units must be defined in an Internal Audit Charter in line with the standards of the Institute of Internal Auditors. This charter is the terms of reference of the internal audit unit and it must be communicated to all stakeholders.

Independence of the Internal Auditor

The internal auditor should be responsible to the Minister or other head of organisation with no responsibilities for managerial functions to avoid prejudicing his/her objectivity.

Technical Tool Kit

An internal audit tool kit comprising an Internal Audit Manual, Operational Procedures, Work and Report Templates and Audit Programmes will be available to all internal audit units to ensure that they practice in line with the Standards of Internal Auditing and the Code of Ethics.

6. ACCOUNTING AND REPORTING

Accounting and reporting systems are crucial for budget management, financial accountability and policy making. It is therefore necessary to track the uses of budget appropriations at each stage of the expenditure cycle, in order to ensure compliance and proper use of public money.

The Accounting System

The maintenance of good financial records is the basis for sound financial management.

The main purpose of establishing an accounting system is to enable the recording, collecting and aggregating and reporting the effects of transactions, following International Public Sector Accounting Standards (IPSAS). It also ensures that information is made accessible to interested parties about the financial position of the institution.

The essential qualities of an accounting system are that the information contained in the accounts and the supporting subsidiary records are:

- Accurate and include the classification of transactions
- Complete and a true representation of the transactions that took place and
- Relevant and understandable to users of the information

States will keep accounting records in various formats at different stages of reform. Currently, most States keep accounting records may be kept in a manual format – i.e. hardback books of account. States will move towards keeping records in a computerised format, using simple spreadsheets or an electronic Financial Management Information System. The objective, irrespective of the system in use is to facilitate the production of timely monitoring reports and improve information dissemination.

Chart of Accounts – Revenue and expenditure

Establishing Charts of Accounts is an important tool for accounting and reporting purposes. The chart sorts the different types of income and expenditure into a series of pre-determined categories or accounts, typically arranged in a logical order.

When a transaction takes place, it is recorded and categorised according to the guidance contained in the Chart of Accounts. The same categories are used in all subsequent budgets and financial reports, ensuring consistency and transparency.

States must adopt charts of accounts using the same classification as GoSS.

Cash Basis of Accounting

The cash basis of accounting measures the flow of cash resources and recognises transactions and events only when cash is received or paid. Cash-based reports are required to demonstrate compliance with the appropriations, but must be supplemented with data on commitments and liabilities arising from budget execution.

State government are required to use the cash basis, and the system should generate budget execution reports which keep track of appropriations and uses of appropriations at different stages of the expenditure cycle, especially at the commitment stage.

Main features of sound budget execution accounting

The following information is needed at each stage of the expenditure cycle:

Recording of appropriations

Adequate recording of appropriations, revisions in appropriations, and transfers between appropriations is a prerequisite for good financial management. The information should be updated regularly, to avoid confusion which sometimes occurs over final allocations because decisions regarding allocations and reallocations of appropriations are contained in separate circulars.

Accounting for commitments

Essential for controlling budget implementation is accounting for commitments in order to provide information which will form a basis for budget revisions. Any decision to increase/decrease appropriations and preparations of cash plans must take into account commitments previously made.

Accounting for Expenditure

Accounting for expenditure at the verification stage of the expenditure cycle is important for providing information on the progress of project or programme implementation. Recording expenditure is also required for managing arrears.

Transparency

This requires that all payments are reported in accordance with an expenditure classification system, including payments made but relating to expenditures made in a previous period.

Budget execution reports

When the TSA systems begins to function through the State Ministries of Finance, there will be need for the Ministry to provide budget execution reports to Spending Agencies showing budget execution by budget line item. These reports will show expenditure and commitments against each budget line (Utilities, Domestic travel etc.). State Ministries of Finance should also provide Agencies with detailed reports showing each expenditure item they have incurred.

The detailed expenditure and commitment reports will give Spending Agencies, details of all payments and outstanding commitments and must be reviewed on a monthly basis by the Agencies so that they ensure that they are accurately executing their Approved Budget and directing their expenditures to their priorities.

Progress reports

The State Minister of Finance, under an Appropriation Act will be required to present:

- a quarterly revenue and expenditure progress report to the State Council of Ministers and

- a bi-annual progress report on revenue, expenditure and implementation of activities, to the State Legislative Assembly (SLA) in the second week of the first month of each Session.
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Interim Accountability Reports and Annual Accounts

States are required to make regular interim accountability reports to MoFEP for transfers received. States shall produce accounts within two months after the close of the financial year. The interim reports should show all sources of revenue available and all expenditures incurred. The financial statements are covered in more detail in the next section of this framework. They will be subjected to an audit by the MoFEP DG for Internal Audit and Supervision and the Auditor General. Failure to provide interim accountabilities will lead to GoSS not making any further transfers until accountabilities are received.

7. FINANCIAL STATEMENTS

The end product of a financial accounting system is the production of financial statements. They are a summary of all transactions for a specified period and show the financial position of the organisation.

Financial statements are prepared following the categories defined in the Chart of Accounts. The form or main components of the financial statements will be prescribed by regulations contained in a Public Financial Management Act. All financial statements submitted must be in accordance with International Public Sector Accounting Standards (IPSAS) and must also comply with all regulations and instructions issued by the Ministry of Finance and Economic Planning. Any departure from accepted accounting practice must be disclosed and the reasons for departures stated.

Under the cash basis of accounting, financial statements produced will include cash receipts, cash payments and opening and closing cash balances. Such a financial reporting system has the advantage of being simple and comparable to monetary data.

All Director Generals of Finance administering the accounts of any State receiving transfers from GoSS swill be required to submit financial reports to the DG of Accounts at MoFEP.

Both GoSS and State Financial Statements are annually audited by the Southern Sudan Audit Chamber.

MoFEP will produce an Accounting Manual which will provide guidance and instruction to State Ministries of Finance on preparing their annual financial statements.