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**Islamic Republic of Afghanistan
Ministry of Finance
General Budget Directorate
Budget Policy & Reform Directorate
Budget Reform Unit**

Budgeting in Afghanistan

Budget Manual

Volume I

PRINCIPLES OF BUDGETING



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Ministry of Finance**

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Acronyms

AFMIS	:	Afghanistan Financial Management Information System
AFS	:	Afghanistan Unit of Currency
ANDS	:	Afghanistan National Development Strategy
BRU	:	Budget Reform Unit
CoA	:	Chart of Accounts
FPU	:	Fiscal Policy Unit (of MoF)
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
IMC	:	Inter-Ministerial Committees
IRoA	:	Islamic Republic of Afghanistan
MDGs	:	UN Millennium Development Goals
MIS	:	Management Information System
MoEc	:	Ministry of Economy
MoF	:	Ministry of Finance
NGO	:	Non-Government Organization
MTEF	:	Medium Term Expenditure Framework
MTBF	:	Medium Term Budget Framework
MTFF	:	Medium Term Fiscal Framework
PB	:	Program Budgeting
PBIT	:	Program Budget Implementation Team
PFEML	:	Public Finance and Expenditure Management Law
PFEM	:	Public Finance and Expenditure Management
UN	:	United Nations
USD	:	United States Dollar (Unit of Currency)

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SECTION 1 – INTRODUCTION

1.1 Background

1.1.1 In recent years the policy of the government of the Islamic Republic of Afghanistan (IRoA) has been to introduce a number of budget process reforms aimed at strengthening public expenditure management and planning, and improving financial control. The most important pieces of legislation in the field have been the Public Finance and Expenditure Management Law (PFEML) and the Public Finance Expenditure Management (PFEM) regulations. These reforms have two key objectives:-

- to develop expenditure priorities and budget plans over the medium term and,
- to base budget allocation decisions on the economic and social priorities of the country.

1.1.2 These developments have taken place in parallel with the creation of a strategy for the future development of the nation – the Afghanistan National Development Strategy (ANDS). This plan, agreed in August 2008 between IRoA and the international donors supporting Afghanistan’s development, sets out the medium-term development framework covering the social, economic, governance and security agendas for Afghanistan over the next five years. The strategies set out in the ANDS document also work towards the attainment of the United Nations Millennium Development Goals (MDGs).

1.1.3 An important feature of ANDS is a ‘**results framework**’ – a set of aims, objectives and planned outcomes which the strategy will need to achieve over its lifetime. However, if these outcomes are to be realised it will be essential that government spending plans be based on this framework. The approach chosen for ensuring that this happens is to replace the traditional model of budgeting with the technique of **program budgeting**.

1.1.4 Because it was new to Afghanistan, program budgeting has been introduced across line ministries and budgetary units of IRoA on a phased basis from 1385 and 1390.

1.1.5 Program budgeting replaces traditional line item budgeting by focusing expenditure estimation, monitoring and control on an organisation’s key outputs rather than on its consumption of resources.

1.1.6 This manual describes the way in which the annual budget process of IRoA operates under this approach and has been prepared to provide guidance to the staff of,

- the Ministry of Finance (MoF) who will coordinate the budget process, and,
- Ministries and other Budgetary Units who will prepare the budgets.

1.1.7 To do this, the manual sets out:-

- the program budgeting framework,
- the procedures involved in developing effective program budget plans, and
- making appropriate annual budget submissions to MoF.

The manual will be of use to all personnel of the government who are responsible for executing and managing IRoA’s budgeting, accounting and other fiscal responsibilities. In conjunction with its three companion volumes – on budget preparation, budget execution and budget evaluation - it provides a comprehensive explanation of the budget and financial

administration arrangements of government, and can be used to inform existing and new employees about various aspects of government financial administration

1.2 Structure of the Manual

1.2.1 This budget process manual is organized into the following sections:

- Section 1: introduction and background
- Section 2: Ministry or Agency results frameworks (based on the ANDS) and the budget
- Section 3: What is program budgeting?
- Section 4: The budget timetable and the role of MoF

At various points the main text of the manual is supplemented by annexes providing supplementary detail and/or additional information.

1.2.2 The contents of the manual will be supplemented by an annual round of training and mentoring conducted by the Ministry of Finance. This will be supported during the course of the budget setting and execution process by technical assistance supplied by a number of donors. If on reading this manual you have any questions on any of the material covered, please use the opportunity of the training to seek clarification, or contact your MoF Focal Point who will be able to provide assistance.

SECTION 2 - THE ANDS RESULTS FRAMEWORK AND THE BUDGET

This chapter shows that the ANDS Results Framework is the foundation of program budgeting and aims at conveying:

- the importance of aligning program budgets to the ANDS results framework; and
- the definition and role of medium term budgeting.

By the end of this chapter, you should be able to...

- understand the importance of aligning ministerial budgets with the ANDS framework; and
- appreciate the importance of the medium term budget, expenditure and fiscal frameworks to the budgeting process

2.1 Introduction

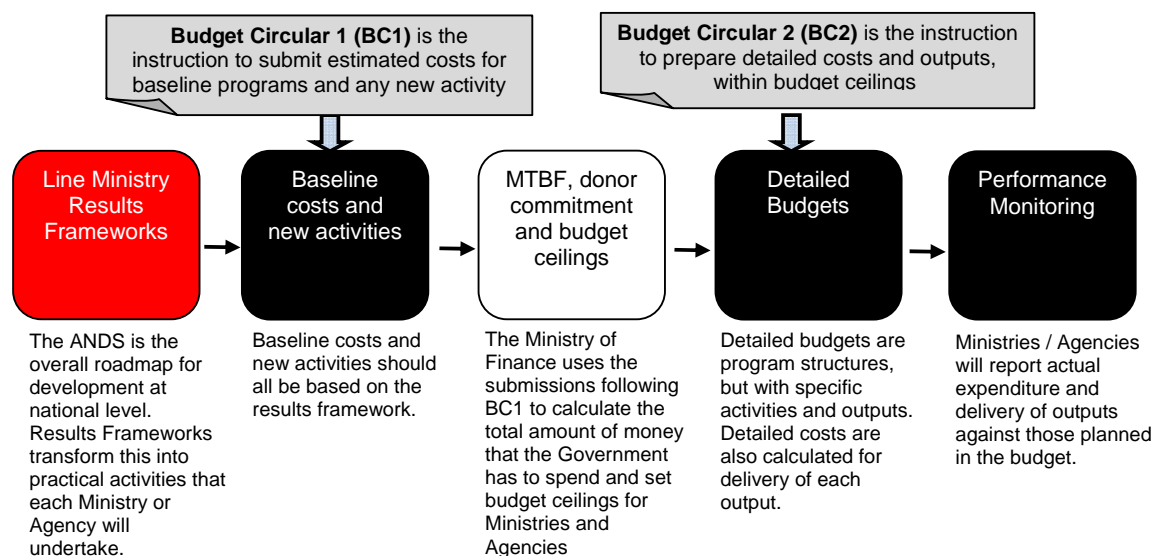
2.1.1 The national budget is the primary tool for implementing the priorities and policies of the government as a whole. Since those priorities and policies are in ANDS, it is essential that the budget reflect that document. Furthermore, since ANDS is results-based, the government intends to adopt a **results based management framework** to underpin the annual budgeting process.

2.1.2 This section serves briefly to explain what the ANDS results framework is and aims to explain basic supporting devices such as the **Medium Term Fiscal Framework** and **Medium Term Budget Framework**. In following this chapter, readers should come to understand why it is essential to link their ministerial budgets to the underlying strategy of the government.

2.2 Budgeting and your Ministry / Agency results framework

2.2.1 With the development and adoption of ANDS, IRoA now requires a simple way for ministries and budgetary units to plan their priorities and report against them. The diagram below shows the way in which the line ministry results framework is the starting point for program budgeting, as it sets all the activities that the line ministry/budgetary unit would like to undertake (either itself or through other implementers).

Figure 1: ANDS and Budgeting Process



2.2.2 Effective planning is achieved through the development of an overall results framework by the line ministry/budgetary unit. The results framework is based on the sector strategy that is relevant to a specific line ministry/budgetary unit, but takes it to a more detailed level, giving a list of planned outcomes until the end of the ANDS, and activities that will achieve these outcomes through the delivery of specific outputs. Both outcomes and outputs are measured using indicators. This results framework forms the basis of the ministry's/budgetary unit's budget.

2.2.3 Each results framework takes the form of a standard logical framework document in which are listed:-

- the objectives of the line ministry/budgetary unit
- the expected outcomes that the line ministry/budgetary unit will achieve;
- the outputs that the line ministry/budgetary unit will deliver, and which will lead to achievement of planned outcomes;
- the performance indicators that will be used to measure both outcomes and outputs;
- The specific targets for both outcomes and outputs, using the indicators identified;
- the source(s) of information through which these indicators will be verified; and
- the risks and assumptions related to the sector's performance.

A copy of the results framework for one Ministry is attached for information as Annex 1. Much of the terminology used in the framework document is common with that used in program budgeting and will be explained at various appropriate points in this manual.

2.2.4 The central characteristic of program budgeting is that it creates budgets that allocate costs directly to the activities that will deliver outputs, which will achieve objectives that are the policy of the Government. Since in Afghanistan these aims and objectives are now embedded in the ANDS framework, program budgeting is a particularly suitable approach to ensuring clear and firm links between expenditure plans and ANDS objectives at the level of ministries and other budgetary units. From fiscal year 1390 *all* ministries/budgetary units will be expected to base their program structure, outputs, and performance indicators on the ANDS results framework.

2.3 Medium Term Financial Forecasting and Planning

2.3.1 ANDS covers a five year period during which the government is expected to progress towards the achievement of the priorities and outcomes it sets out (and also towards the longer-term UN MDGs). To secure this progress, government needs to spend significant sums of money in improving both the quantity and quality of the services it provides.

2.3.2 The mechanism for managing money in any economic entity is always its budget. In principle, therefore, organisational budgets should always align with organisational objectives – if they do not, the entity will very quickly find itself in difficulties.

2.3.3 Traditionally, governments create budgets with a time horizon of one year. However, as ANDS demonstrates, many government objectives can be achieved only through policy commitments and investment programmes which stretch over multiple-year periods. One-year-a-time budgeting is no longer adequate to ensure that expenditure patterns reflect these long-term objectives, and that adequate funds are available to support the multi-year investment programmes required.

2.3.4 In order to bridge the gap between the long-term perspective of ANDS and the necessary annual budget cycle, the government has developed a series of **medium term**

financial planning tools. These tools are designed to predict and demonstrate revenue and expenditure flows over a multi-year period (the medium term usually being defined as the budget year plus two to five years into the future).

2.3.5 To create the necessary medium term financial infrastructure the government has developed three tools as follows:-

- The Medium Term Fiscal Framework (MTFF) sets the overall available resources for spending by Government for the next three years. The main feature of a MTFF is that it sets out medium term macro-economic and fiscal forecasts and fiscal strategy, so that the annual budget is prepared taking into account the total resources available over the medium term. MTFF provides greater predictability of available funds, which results in fiscal sustainability of budget.
- The Medium Term Budgetary Framework (MTBF) is an approach to budgeting which links the spending plans of government to its policy objectives. The main feature of a MTBF, compared to MTFF, is that it recommends expenditure priorities and splits overall fiscal envelop (available resources) by budgetary units (defines budget unit ceilings) for the medium term. MTBF provides analysis of Government policies, *which results in allocation of funds to where they are most needed* (funds allocated to highest priorities).
- The Medium Term Expenditure Framework (MTEF) is an approach to budgeting which links the government spending plans to performance targets. The main feature of a MTEF, compared to MTBF, is that it allocates budget across different programs and defines outputs expected to be achieved by these programs over the next three years. MTEF introduces performance based budgeting, which results in operational efficiency of budget (best results achieved with available resources).

These instruments have been developed in order to:-

- improve macroeconomic balance by developing a consistent and realistic resource framework;
- improve the allocation of resources to strategic priorities;
- improve the predictability of both policy and funding; and
- provide line budget entities with firm budget constraints against which to determine their own priorities and thereby increase their autonomy.

2.3.6 It is important for ministries and budgetary units to be aware of the role these tools play in determining multi-year financial plans and taxation rates, and in fixing the annual budget ceiling. These tools depend heavily on the accuracy with which line ministries and budgetary units compile their medium term spending plans.

So it is essential that line ministries and budgetary units play their part by responding in a timely and professional manner to requests for information when they are being compiled. Ministries and budgetary units should also ensure that they comply with the deadline in submitting BC1 information to enable MOF prepare the MTBF containing the next year budget ceilings. Once the MTBF is prepared in time the BC2 can be issued in due date giving ministries and budgetary units sufficient time to prepare their budget submissions.

2.3.7 The practical impact of medium term financial planning is that the annual budget cycle now requires ministries and budgetary units to forecast their expenditure needs over a

three-year period, albeit in much less detail for years 2 and 3 than for year 1. With this knowledge, program managers are better able to plan their programs and activities over a longer planning period with a greater degree of confidence that funds will be available.

2.4 Poverty Reduction (Pro-Poor Expenditure Tracking)

2.4.1 A very important part of the ANDS is the Poverty Profile which provides poverty analysis, including information about national and provincial headcount poverty rate, causes of poverty and most vulnerable groups. This analysis has been translated into the priority poverty reduction policies that have been integrated into the ANDS sector strategies. Given that a major objective of the ANDS is poverty reduction, the Ministry of Finance has introduced pro-poor expenditure tracking mechanism within the Budget process.

2.4.2 First, line ministries are instructed to identify their poverty reduction policies and to integrate them into the Result Frameworks. Second, line ministries are also instructed to identify existing and integrate new pro-poor budget allocation into its Budget Circular 1 and 2 submissions with aim to support implementation of the poverty reduction policies. Finally, the Chart of Accounts will be adjusted to ensure pro-poor expenditure tracking and reporting by using the AFMIS. This activity has been introduced into 1390 Budget preparations on a pilot basis and will roll out to all line ministry/budgetary units.

SECTION 3 – WHAT IS PROGRAM BUDGETING?

This chapter on program budgeting aims at assisting readers to...

- understand the basic distinction between traditional and program budgeting; and,
- understand basic program budgeting terminology.

By the end of this chapter, you should be able to...

- converse using basic program budgeting terms; and,
- understand the difference between input, output, outcome and efficiency indicators.

3.1 Introduction

3.1.1 Program budgeting is a tool for planning, preparing and presenting the government's budget in a manner that provides clear linkages between budget resources and the policy outcomes that government wants to follow.

3.2 What is a Budget?

3.2.1 No organisation, no matter how large or small, can operate without money. This money may be derived in the case of a voluntary organisation from members' subscriptions, in a commercial or manufacturing firm from the sale of products or services, and in government from raising taxes and charging for services.

3.2.2 Every organisation has its own characteristics and its own aims and objectives. In order to achieve these, each organisation employs resources to carry out activities which it feels will further these objectives. The most important resource available to it is money, since money enables it to acquire all the other resources. It is therefore vital above all for an organisation to ensure that the money it has at its disposal is used to for the specific purpose of pursuing the objectives it has set itself.

3.2.3 The instrument which makes this possible is the organisational budget (the word is derived from an ancient Latin word *bulga* which was a purse or small bag carried on a journey in which was contained a fixed amount of money to fund the cost of purchases being made along the way). A budget is a business process which through a sequence of planning, execution and evaluation provides the essential link for an organisation between its organisational objectives and plans, its financial resources and its operational activities.

3.2.4 For governments, budgets have an additional significance. Governments possess no resources of their own – they exist to provide services for citizens who in turn provide the money to fund those services through taxes (and payments for the use of some of them) and other domestic revenues. Since the payment of taxes is not voluntary, it is essential that governments properly plan their use of resources in order to legitimize the amount of funds raised through taxation. The normal procedure is for citizens to elect representatives who make the final decisions on their behalf on:-

- how much money will be spent,
- what it will be spent on,
- how much citizens will pay through taxes and charges to raise those funds, and
- how effectively that money has been spent.

3.2.5 Budget is a tool Government uses to translate its priorities into programs and projects and services in order to meet needs of its citizens. More specific purposes of the budget could be defined as follows:

- It provides a comprehensive and transparent financial plan linking the organisation's available financial resources to its activities.
- It sets a limit on the level of expenditure permitted in carrying out the organisation's activities.
- It provides a structure for releasing (allotment), recording (accounting) and monitoring (auditing) the expenditure of funds.
- It provides authority to managers to spend money on implementing agreed policies and carrying out planned activities without constant reference to top management.
- At the same time it is an instrument of accountability making managers responsible for the financial implications of the operations they authorize.
- In the public sector, it acts as a wider instrument of accountability between citizens/taxpayers and their government.

3.3 Traditional Budgeting

3.3.1 The Government in Afghanistan has traditionally required ministries and budgetary units to use **line-item budgeting**. Each line-item defines a type of remuneration (permanent employees, professional allowances), commodity (stationery, vehicle fuel, office equipment) or service (telephones, maintenance of buildings or machinery) that each ministry/budgetary unit will purchase, followed by an estimate of the total cost of those purchases during the budget period.

3.3.2 In the past, ministry expenses were only categorized according to the economic classification code (21 – salaries and wages, 22 - goods and services, and 25 – acquisition of assets). Each of these main codes were broken down into sub-codes which give further detail of the type of expenditure being incurred. Every ministry and budgetary unit expressed its budget in accordance with these classification codes. This traditional approach to budgeting provided a very useful basis for controlling budget disbursement during the budget execution period.

3.3.3 In Afghanistan, the budget practice split funding into two main streams:-

- the operating budget – Primarily funded by domestic revenues
- the development budget – funded primarily by donors but with some input from government.

3.3.4 Another important distinction to draw within current budget practice is between:-

- the core budget, and
- the external budget.

The core budget consists of all funding which passes through the government treasury. This is made up of the operating budget and those donor funds which are controlled / authorised by MoF. The external budget (which is entirely development related) is donor funding for approved projects but does not pass through the hands of government. Because external funding by definition is outside direct government control, it is also outside the scope of program budgeting, which covers only the **core** budget.

3.4 Limitations of Traditional Budgeting

3.4.1 Budget practice in Afghanistan, as described above, had a number of significant drawbacks. These are set out below.

3.4.2 **Outputs and Outcomes.** Traditional budgeting did not provide any information about achievements or the costs of those achievements. Because the emphasis was on recording and controlling aggregate expenditure, ‘success’ or ‘failure’ in budget management was related wholly to how the budget funds have been disbursed, not to what has been delivered by way of outputs from the expenditure incurred – i.e. it tells us *what* has been expended, not *how* it has been expended.

3.4.3 **Delivering Government policy objectives (in the ANDS).** Focusing only on inputs, rather than outputs and outcomes, also makes it difficult to see how budgets will deliver Government policy objectives. Program budget makes this much easier, by focusing on what will be achieved through the budget.

3.4.4 **Integration.** In the past, ministries and budgetary units used to account for and report on the two different types of budget – operating and core development. While there are similar costs supporting similar activities within each type of budget, there is little, if any, coordination between the two reporting structures.

3.4.5 **Planning Stability.** Budgeting for a single year does not allow decision makers to consider the future year implications of the budget decisions they are making and in some circumstances may lead to an activity having to cease for lack of funds in a future budget period.

3.5 A New Approach: Program Budgeting

3.5.1 The Government of Afghanistan is trying to establish:

- what is actually being delivered with the funds provided;
- whether government spending is aligned with the strategic goals established by the ANDS results framework.

3.5.2 Program budgeting is a business process by which government activities are organized into programs (activities or services with similar or related goals). It follows a distinct structure and is different from traditional budgeting in four fundamental ways:-

- the budget is formulated around the individual operational programs of the budget entity (e.g. primary education, prevention of disease, road maintenance) rather than around its aggregate spending requirements;
- the budgeting process integrates the estimation of service costs with narratives that explain and justify the expenditure being proposed;
- the budget figures are accompanied by narrative descriptions of the aims, objectives and expected achievements of the program during the budget period (and beyond if relevant);
- the budget embeds criteria against which performance in delivering outputs and outcomes can be assessed – this process is often referred to as **performance measurement**.

3.5.3 The overall aim of program budgeting is for ministries and budgetary units to show that their budget spending is aligning with the aims and objectives of their own ministry/ budgetary unit, and through that with the ANDS results framework. Furthermore, by

budgeting on a program basis, ministries and budgetary units will be in a position to identify alternative strategies for achieving each goal by determining the costs and benefits of possible alternative approaches to achieving them.

3.6 Components of Program Budgeting

3.6.1 Table 3.1 below presents a brief overview of the components that comprise a program budget. This is supplemented by a diagram setting out graphically the architecture of program budgeting and this is attached as Annex 2. How each of these fits into the program budgeting process is explained in detail in volume 2 of the manual.

3.6.2 In practice, program budgeting follows a clear and distinct hierarchy of aims, objectives and policies. The process starts with:-

- the **overall goals of government** (expressed in Afghanistan in the ANDS); and works through
- the **medium term financial planning** process described in section 2. At the level of individual ministries and budgetary units it requires a transparent definition of:
 - **organisational strategic objectives** supported by a logical division of the main service outputs of the ministry/budgetary unit (and are in your Ministry or Agency results framework) into what are called
 - **programs**. Where an individual program is too large or complex to control as a single entity (and most do fall into this category) then there is a further subdivision into
 - **sub-programs** which exist at the day-to-day operational level of the ministry/budgetary unit.
- **Integration** is achieved by including in these sub-programs both the
 - **recurrent/operating activities** and
 - **development projects** contributing to the achievement of the sub-programs goals.

Table 3.1 – Components of Program Budgeting

Program Budget Component	Description
Narrative	<ul style="list-style-type: none"> • Government Goals – ANDS and sectoral and ministerial results framework • Ministerial strategic objectives – link between work of ministry/budgetary unit and ANDS goals • Program and operational objectives - more specific statements of what ministries aims to achieve in the long (program) or medium (sub-programs) term
Program Structures	<ul style="list-style-type: none"> • Program - a collection of related activities working towards a common purpose within the line ministry. • Sub-program - a group of activities under the same operating or development priority/policy objective (ie part of a larger program). A sub-program essentially defines what the ministry/budgetary unit does • Activities - the work that ministries do within a sub-program.

	<p>They will be either funded from</p> <ul style="list-style-type: none"> • recurrent (operating) budget • development budget or • development and operating budgets
Finance	<ul style="list-style-type: none"> • Medium term financial plan – identifying multi-year financial implications of pursuing government goals and objective; • Budget ceilings – identifying the resources available to pursue those goals and objectives • Annual estimates – specifying the detailed spending plans of individual ministries and budgetary units
Performance Reporting	<ul style="list-style-type: none"> • Performance indicators – measures of success and achievement in pursuing goals and objectives <ul style="list-style-type: none"> ○ A definition of what output will be achieved ○ An indicator for each output • Output baseline and target for the next three years • Identifying the link between program outcomes and activity outputs to ensure the activities undertaken contribute towards attainment of objectives, for example poverty reduction.

3.7 Measuring Performance

3.7.1 The final concept of program budgeting to be considered relates to the assessment of performance. Government performance is of primary concern to every citizen because there is an expectation that all resources will be used efficiently and effectively in providing the highest attainable level of public services. In turn, line ministries and budgetary units have the responsibility to ensure that the programs they provide meet their stated objectives and are cost effective.

3.7.2 If the needs of all these parties are to be satisfied, it is essential that there should be some methodology in place which can provide a basis for a systematic and objective evaluation of government performance. Worldwide, much work in recent years has gone into developing such measures and there now exists a wide range of what are known as **performance indicators** which can be used for this purpose. These indicators are normally used to measure the output, efficiency, and outcome of government activities.

3.7.3 The central reason for introducing program budgeting in Afghanistan is to link expenditure to the achievement of policy goals. It is therefore essential that alongside the establishment of the programs and sub-programs, ministries and budgetary units set up relevant, measurable and robust performance indicators which can be used to assess the extent to which progress is being made towards policy goals.

3.7.4 There are four primary types of performance indicators:

- input,
- output,
- outcome, and
- efficiency.

Table 3.2, below, defines the four principal types of performance indicators and provides some examples of how they might be applied. In broad terms,

- **input** indicators address the amount of resources used in providing a service/

- delivering an activity,
- **output** indicators describe what is produced by the activities carried out in providing a service,
 - **outcome (or effectiveness)** indicators relate to service achievement resulting in tangible development changes, and
 - **efficiency** indicators examine the relationship between the level of resource use and the outputs achieved.

3.7.5 Input, output and efficiency indicators are reasonably simple to define and calculate, can be compiled from data readily available to, or within, ministries and budgetary units, and can measure performance over a short period of time. They are normally related to the amount of resource consumed and the quantity of units of output produced. However, such indicators provide only limited insight into whether the program is achieving the goals for which it was designed.

3.7.6 To overcome these limitations, it is necessary to identify measures of outcome which relate directly to service achievement and/or consider issues such as quality and effectiveness. Outcomes relate to the impact on society achieved after completion of one or more than one activity, but do not show the direct result of an activity, For example “increased school enrolment rate” that is impact of the outputs such as “schools built”, “teachers trained”, and “books printed & distributed”. However, these measures are often not easily measured and require conducting certain studies or surveys.

Much work was done in the creation of ANDS (most specifically in the results framework) in defining a range of sectoral and ministerial outcome measures, and ministries and budgetary units can assist themselves in the program budgeting process by making reference to them as a basis for their own analysis

Table 3.2 – Performance Indicators

Type of Indicator	What it Measures	Example
Input	Quantity of Resources Employed	<ul style="list-style-type: none"> ✓ Equipment required ✓ Employees required ✓ Supplies used ✓ Money spent
Output	Quantity of Service Provided	<ul style="list-style-type: none"> ✓ Number of teachers trained ✓ Number of classes ✓ Number of people served
Outcome/Effectiveness	The degree to which the intended objective of the service is being met.	<ul style="list-style-type: none"> ✓ Percentage change in employment ✓ Percentage change in crime rate ✓ Enrolment rates
Efficiency	Cost per unit of output	<ul style="list-style-type: none"> ✓ Cost per litre of water delivered to a household

SECTION 4 – THE BUDGET TIMETABLE AND THE ROLE OF THE MINISTRY OF FINANCE

This chapter on the budget timetable aims to assist readers in ...

- understanding the budget cycle;
- understanding and appreciating the role MoF plays in the budget cycle.

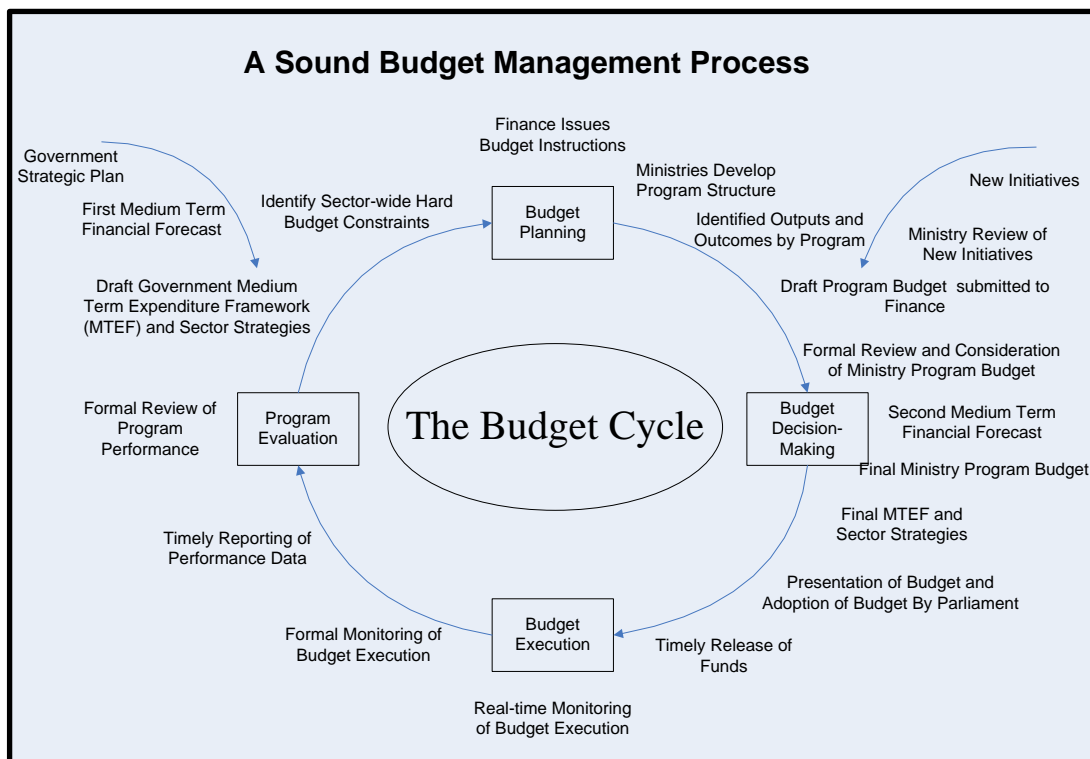
By the end of this chapter, you should be...

- able to describe the budget cycle and the main activities it covers;
- able to describe how the Ministry of Finance intervenes in and impacts upon the budget process
- aware of the stages at which ministries/budgetary units are required to provide inputs

4.1 The Budget Cycle

4.1.1 This section sets out the timetable for developing budgets at ministerial/budgetary unit level.

Figure 4.1 The Budget Cycle



4.1.2 Figure 4.1 above, provides a diagrammatic representation of the budget cycle being developed in Afghanistan. This diagram shows four main stages:-

- pre-budget planning based on the ANDS results framework;
- budget preparation and decision making following guidance laid down by MoF;
- budget execution – disbursement of funds approved at the decision making stage; and

- performance evaluation – comparison between the stated objectives of the budgets and actual achievement, that is the extent of progress made towards meeting planned outputs and outcomes.

From this it can be seen that the budget cycle begins and ends with the ANDS results framework.

4.1.3 The following paragraphs set out briefly the actions required at each stage of the budget cycle. However, this volume is concerned only with the principles involved – the mechanics of budget preparation, execution and review are dealt with in later volumes of the manual.

4.1.4 The Ministry of Finance initiates the budget cycle each year by drawing up a budget strategy in the light of ANDS priorities. This strategy is then discussed at senior levels within government and once it is agreed, MoF issues a timetable covering the budget preparation process and disseminates it to all parties involved – line ministries, budgetary units and the relevant departments of MoF. At the same time it is in the process of finalizing the medium term financial planning exercise to determine the resource levels available for disbursement.

4.1.5 Ministries and budgetary units are then requested to draw up **programs, program narratives, outputs and indicators** in respect of the services they provide which are based on those defined within their Ministry or Agency results framework. These requests come in the form of budget circulars – **Budget Circular No 1** (see sub-section 4.4) requests ministries to submit to MoF only outline (indicative) budget proposals, classified by program and sub-program. Based on the BC1 submissions, Ministry of Finance prepares Medium-Term Budget Framework (MTBF) as “Pre-Budget Statement” setting budget priorities to be funded from the existing fiscal envelope (available resources) and providing draft budget ceilings (see sub-section 4.6). However, **Budget Circular No 2** (see sub-section 4.5) requires the submission of detailed budget estimates, accompanied by definitive program and sub-program narratives. These estimates have to be prepared within a **budget ceiling** which represents the maximum sum MoF estimates should be expended by each ministry/budgetary unit. These processes are explained in detail in the volume 2 of this manual.

4.1.6 Once program and sub-program activities have been fully described and costed, they are submitted to MoF and presented in a budget document. After formal review, and approval, by the Ministry of Finance, and later by the legislature, the budget is adopted by Parliament. At this stage, ministries prepare for budget allotments as they enter the budget execution stage.

4.1.7 Once the fiscal year commences, line ministries and budgetary units are expected to follow GoA procedures for incurring and recording expenditure. Each quarter, every line ministry and budgetary units applies for an allotment of funds which permits it to expend money within the limits laid down in the budget in pursuing its operating and development objectives. Information about all expenditure incurred is communicated to MoF using prescribed templates and recorded in the financial management information system (AFMIS). The primary responsibility for controlling expenditure totals against each line item or program budget rests with the line ministry/budgetary agency concerned, but MoF uses the allotment procedure to ensure that overall budget allocations are not exceeded. The operation of these procedures set out in detail in volume 3 of the manual.

4.1.8 As ministries and budgetary units disburse funds, not only does the efficiency of spending need to be monitored, but it is also essential to establish whether the spending by each ministry or budgetary unit actually achieves its objectives. At the end of the fiscal year, therefore, each ministry's/budgetary unit's spending efficiency and performance will be reviewed to determine if it has effectively achieved the objectives that it had established for itself at the budget preparation stage, and what impact that spending has had on achieving the applicable program objectives, outputs and outcomes of ANDS. The operation of these procedures is set out in detail in volume 4 of the manual.

4.2 Budget Preparation

4.2.1 The most important part of the budget cycle is the budget preparation stage since it sets the framework for the management of the budget (and therefore what the Government can achieve) for whole of the fiscal year. The fundamental steps in the preparation process are therefore considered here, but the detailed procedures are covered in volume 2.

4.2.2. To facilitate and control the process, MoF circulates a budget preparation calendar each year, but under program budgeting the budget preparation stage commences significantly earlier than in the years when only the traditional model was in use. An outline of the basic timeline is provided in Table 4.2 below.

Ministry of Finance 1391 Budget Timetable	
Steps	Deadline
Budget Calendar	
Finalize the 1391 budget calendar in consultation with the Budget Committee.	March 20
Issue budget calendar to primary budget units, Cabinet and donors.	April, 1
Organize conference for donors to explain new approach to donor funding coordination	1-Apr
Budget circular No 1	
Budget units to finalize their Results Frameworks in conjunction with ANDS department.	April, 15
Issue Budget Circular 1, along with costing instructions in consultation with Ministry of Economy.	April, 10
Workshop to explain 1391 budget preparation and BC1 budget submission requirements to budget units. Sector representatives of Ministry of Economy will participate in the workshop.	April 17 - 24
Provincial budget pilot ministries issue BC1 submission request to their provinces and organize workshop with provincial departments.	April 20-25
Ministry of Economy works with budget units to set the priorities based on their Results Framework.	April 17- May 5
Under MOF's facilitation donors to work with budgetary units to ensure BC1 submissions contain enough details for them to be able to make decisions on funding commitments	April 24 – May 22
MOF sector managers assist budget units with preparation of BC1 submissions.	April 24 – May 22
Civil society workshop on BC1	April, 25
Costing workshops for budget units.	April 25 – May 5

Deadline for BC1 budget submissions to Ministry of Finance and Ministry of Economy. Note: revisions will not be accepted after this deadline.	May 22
Ministry of Economy in consultation with Ministry of Finance will review the submissions	May 23 – June 1
Medium-Term Budget Framework (Pre-Budget Document)	
Confirmation of existing donor commitments	June 1
MoF collates approved new priority proposals for Budget Committee review.	June 3-9
Budget Committee approves priorities. (MAX 3-5 PRIORITIES PER MINISTRY)	June 12
Government priorities presented to donors (first Donor Financial Review/DFR) to obtain tentative donor commitments for 1391 budget funding.	June 17
Donor consultation process finalized	July 17
MOF prepares MTBF (Pre-budget report), containing MTFF & budget ceilings, and submits to Cabinet for approval.	August 2
Publish MTBF, containing budget ceilings and approved new initiatives online.	August 14
Mid Year Review	
MOF in consultation with MOEC conducts Mid Year Review and prepare MYR Document	September 20
Submission of MYR to Cabinet	September 25
Submission of MYR to Parliament	October 10
Budget circular No 2	
Issue Budget Circular 2, containing budget ceilings approved by Cabinet, costing instructions and project development templates.	August 15
Workshop to explain BC2 budget submission requirements to budget units.	August 22-23
Communicate to civil society start of BC2 process	August 24
Provincial budget pilot ministries issue BC1 submission request to their provinces and organize workshop with provincial departments.	Aug 24-29
Under MOF's facilitation donors to work with budgetary units to ensure projects developed as per their requirements and funding is committed	August 15 - October 12
MOF sector managers assist budget units with preparation of BC2 submissions. Submissions must be in accordance with budget ceilings, though supplementary requests can be made.	August 15 - October 12
Ministry of Economy assists budget units with completion of project documentation in accordance with forms supplied by MOF and MOEC. MOEC also assesses adequacy of project feasibility plans and costing.	August 15 - October 12
Deadline for BC2 budget submissions.	October 14
Budget Hearings	
MOF reviews budget submissions. Only submissions in accordance with budget ceilings will be accepted (but supplementary requests will also be accepted). Failure to submit in accordance with budget ceilings will result in budgets being either cut or held at 1391 levels.	October 16-28
Presentation of BC2 submissions summary to Budget Committee.	November 6
Accepted BC2 submissions published online.	November 7
Government priorities presented to donors (Donor consultations) to obtain confirmation of donor commitments for 1391 budget.	November 10
Donor consultations finalized.	November 20
Budget hearings, focusing on allocation of budget resources by programs and not economic classification. The Ministry of Economy will provide sign off on the technical and costing elements of projects. Projects will be approved only where adequate preparation and costing work has taken place.	November 20 - December 13

Budget units revise program budgeting submissions in accordance with budget hearing decisions.	December 20
Budget Statement	
Finalize Budget Statement	December 18 - January 8
Submission of Budget Document to Budget Committee	January 3
Submission of Budget Document to Cabinet	January 8
Submission of Budget Statement to Parliament	January 18

4.3 Interventions by the Ministry of Finance

4.3.1 The process of preparing and monitoring the annual budget is supported at each stage by the Ministry of Finance (and also by the Ministry of Economy (MoEc) which assesses development projects). Under the constitution of IRoA, the Ministry of Finance is responsible for supervising budget preparation, consolidating the budget and presenting it to Cabinet and Parliament for approval, so it plays the central role in the various stages leading up to its finalization.

4.3.2 MoF's main interventions come through the following activities¹:-

- issuing Budget Circular No 1,
- collecting and summarizing responses to Budget Circular No 1,
- developing Medium-Term Budget Framework, as Pre-Budget Statement,
- issuing budget ceilings,
- providing training and coaching for line ministries and budgetary units in the preparation of budgets (both program and traditional budgets),
- issuing Budget Circular No 2,
- collecting responses to Budget Circular No 2,
- negotiating final budget proposals with line ministries and budgetary units,
- developing National Budget Statement,
- submitting the consolidated budget to Parliament,
- informing ministries and budgetary units of actual budget allocations once parliamentary approval has been given.

The subsequent sub-sections provide details of the MoF interventions which are of direct relevance to the budget preparation process in line ministries and budgetary agencies – the budget circulars and the budget ceiling. There will be many other references to these items in later volumes of the manual and it is important for users to become familiar here with the content and purposes of these documents for the budget preparation process.

4.4 Budget Circular No 1

4.4.1 Budget Circular No 1 represents the essential first steps in:-

- aligning the draft budget of the ministry/budgetary unit with ANDS in a multi-year framework;
- proposing projects and outputs that should align with the ANDS framework;
- developing approximate cost estimates for both operating and development project spending.

¹ For Budget Circular 1 and 2, the line ministries are instructed to pay special attention to integration and identification of the pro-poor allocations in their budget submissions to support implementation of the ministries' poverty reduction policies.

Under current budget preparation procedures MoF aims to circulate this document mid April each year. The details in the Circular will vary from year to year so users of the manual should consult the most recent version to obtain a full understanding of its content.

4.4.2 To achieve these aims, the circular requires each ministry or agency to specify its **priorities for the next three years** by developing new activities which may contain both operating and development budget and are aimed at increasing level of services ministry provides. . Although at this stage only indicative cost figures are required, the priorities themselves must be clearly and precisely defined to reflect ministry/budgetary unit policies and responsibilities, and the applicable sectoral elements of the ANDS framework. These definitions must also be precise as they will eventually be incorporated into programs and sub-programs at a later stage in the process.

4.4.3 The second requirement imposed by this Circular is for line ministries and budgetary units to consider the relationship of their spending plans to ANDS, achieved through program budget documents. It is emphasised that ministries and budgetary entities are not required to finalise these documents at this stage, but they should use Budget Circular No 1 as a trigger point to begin the necessary reviews ahead the more detailed work to follow later in the preparation cycle.

4.5 Budget Circular No 2

4.5.1 This document is planned for release in early August in each annual budget cycle. The details in the Circular will vary from year to year so users of the manual should consult the most recent version to obtain a full understanding of its content.

4.5.2 Budget Circular No 2 requires a much more detailed response from line ministries and budgetary units than Circular No 1. Circular No 2 is the document that requests ministries and budgetary units to prepare their detailed budgets within a series of parameters laid down in the document. This requires the finalization of details of program and sub-program narratives and the classification and prioritization of activities for both operating and development budgets. These narratives will be supported by detailed costing of those activities and these will form the financial element of the eventual budget proposal. .In addition, ministries need to develop and submit detailed project documents for each project contained in their budget submission.

4.5.3 The deadline for submission of budgets is mid October.

4.6 Medium-Term Budget Framework and Budget Ceilings

4.6.1 Following the submission of prioritized plans by line ministries and budgetary units in response to Circular 1, MoF and MoEc jointly review the prioritized budget proposals. Then, MoF holds discussions with international donors during the June–August period. MoF presents the prioritized list of unfunded projects and seeks donor financial support for them. MoF also examines in detail the submissions made by ministries/budgetary units in respect of expenditure priorities to be funded from the operating budget.

4.6.2 In parallel with this activity, MoF finalizes the outcome of the medium term financial planning activity referred to in sub-section 2.3 above. Using this information, it makes an assessment of the likely level of funds available to the government from domestic taxation and other revenue sources, and calculates the total funds available for disbursement during the next fiscal year from domestic sources.

4.6.3 During the initial round of discussions, not all donors will make firm commitments to funding particular projects. However, based on those which do, MoF is at this stage in a position to estimate approximately how much money will be available from each of the two funding sources. It aggregates these sums sector by sector and presents draft budget ceilings in the Medium-Term Budget Framework. Budget ceilings, along with the approved spending activities (proposals) are communicated to each line ministry and budgetary unit in early August each year through the Circular No 2.

4.6.4 Budget ceilings represent the maximum each ministry/budgetary unit may spend in the upcoming fiscal year and the financial budget proposal submitted later in the preparation cycle must fall within this ceiling. Separate ceilings are designated for operating and development expenditure, with the former being a firm figure. The development expenditure figure may not be firm since some donors may only commit to funding additional projects later in the preparation cycle (a further round of discussion is scheduled for late October). The impact of budget ceilings on the prioritization of development proposals and the estimation of program costs is dealt with in volume 2 of the manual.

4.7 Other MoF Interventions

4.7.1 The issuing of the two circulars and the budget ceilings are the most important interventions MoF makes in the budget cycle. However, it makes many further interventions in the budget management process during the preparation, execution and evaluation stages. Such interventions take place, for example, at budget hearings, through the allotment and control procedures during execution, and through the finalization of budget outcome statements at the end of the fiscal year,

4.7.2 These interventions relate to the details of the budgets as prepared by ministries and budgetary units and are concerned with day-to-day financial management procedures rather than with the creation of the budget infrastructure. For this reason, such interventions are considered more appropriately dealt with in the respective volumes of the manual dealing with these parts of the cycle.

Government of Afghanistan



Budgeting in Afghanistan

BUDGET MANUAL VOLUME 1

PRINCIPLES OF BUDGETING

ANNEXES

May 2011

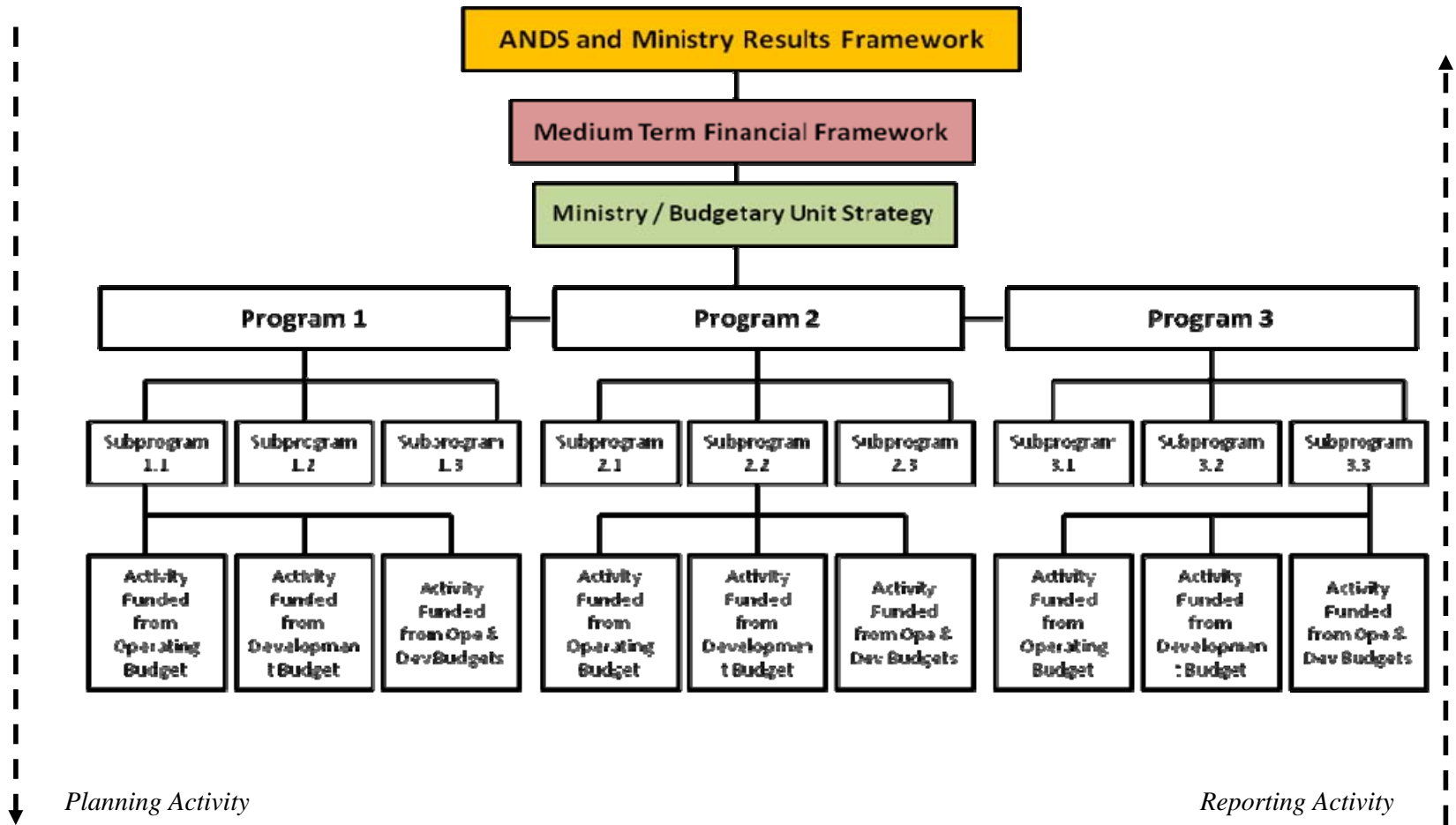
ANNEX 1: Copy of MOCIT Result Framework

Ministry: (Ministry of Information and Communication Technology) Result Framework				
Sector Goals	Impacts	Indicators	Means of Verification	Risks & Assumptions
To rapidly develop ICT sector as an aspect of building infrastructure to promote national growth and productivity.	Well-developed information and communication technology system promotes, business , commerce, private sector development, public service communication and coordination and strengthen good governance system	<ul style="list-style-type: none"> o % of increment in GDP and private sector investment o promote transparency and citizen access to public information 		
Sector Objective:	Sector Outcomes	Indicators	Means of Verification	Risks & Assumptions
To develop and information and communication technology system that will promote development at the national and sub-national level for the benefits of all afghans.	<ul style="list-style-type: none"> o effective functioning of digitalized ICT system for the government at national and sub-national level o Increased access of afghans to information and communication technology facilities. 	<ul style="list-style-type: none"> o % of population have access to ICT services (Gender disaggregated) o # of government offices having official web presence 		
Ministry Objective:	Ministry Outcomes	Indicators	Means of Verification	Risks & Assumptions
To develop and information and communication technology system that will promote development at the national and sub-national level for the benefits of all afghans.	<ul style="list-style-type: none"> o effective functioning of digitalized ICT system for the government at national and sub-national level o Increased access of afghans to information and communication technology facilities. 	<ul style="list-style-type: none"> o % of population have access to ICT services (Gender disaggregated) o # of government offices having official web presence 		
Ministry Inputs	Outputs	Indicators	Means of Verification	Program
Program 1 E- Afghanistan				

Sub-Program ICT Infrastructure and International Relations				
Optical Fiber Cable (OFC)	Fiber optic cable completed	Fiber Optic Cable to be completed in Km (Ring)		
Fixed & CDMA Expansion	CDMA expanded	Fiber Optic Cable to be completed in Km (South Eastern)		
Village Communication Network (VCN)	Village communication network expanded	Fiber Optic Cable to be completed in Km central		
Construction of Technical Buildings	Technical Buildings constructed	Expanding Copper Cable Network(25000 Lines)		
Research & Development	Research conducted.	Expanding Copper Cable Network(33000 Lines)		
International Relations (IR)	Relation Strengthened	Number of Villages to be interconnected		
Operational Support for ICT Infrastructure	Operation support provided to ICT infrastructure.			
Sub-Program 1.1 (Postal Modernization)				
Expanding Postal sector services modernization	Postal sector services modernized.	# of post offices to be constructed # of post offices modernized and/or established		
Sub-Program 1.1.2 E - Government				
Afghanistan Network Information Center (Afg NIC)	Afghanistan Network information Center established	Internet Exchange Point developed in Kabul		
ICT Support Institutions	Support provided for ICT institutions	Establishment of NIRA (National Internet Registry of Afghanistan)		
E- Applications	E-Resource Center established	Establishment of Government E Resource Centre		
ICT Policies/ Strategies	ICT Policies / Strategies developed	Established legal secure ICT environment(percentage)		

National Data Center (NDC)	National Data Center established	National ID card system deployed		
Operational Support for E - Government	Support provided for E-Government			
Program: ICT literacy				
Sub-Program 1.1 (ICT Training Centers)				
Training Centers	Training Centers Established	# of students trained in ICT training centers		
Sub-Program: ICT Institute				
ICT Institute	ICT Institutes Established	Number of students trained in ICT institute		
Program 1 (General Administration & Management)				
Sub-Program 1.1 (General Administration and Services)				
Services, Financial Affairs & Procurement	Services delivered on timely manner	# of procurement process completed		
Provincial Directorates	Provincial directorate operational	# of provincial directorates operational		
Internal Audit	Internal audit conducted	terms of internal audit conducted		
Medial & Publications	Publication disseminated	frequency of public dissemination		

ANNEX 2: PROGRAM BUDGETING ARCHITECTURE



ANNEX 3: Glossary of Budget Terms

In the context of program budgeting in the Islamic Republic of Afghanistan (IRoA) the following words are being used and have the following meanings:

Accounting System	The set of accounting procedures, internal mechanisms of control, books of account, and plan and chart of accounts that are used for administering, recording, and reporting on financial transactions. Systems should record all stages of the payments and receipts process needed to recognize accounting transactions, integrate asset and liability accounts with operating accounts, and maintain records in a form that can be audited.
Activity	An activity is generally the smallest building block within a program that has a definable purpose and specific allocated costs. An activity is a thing you do to achieve a policy priority within a sub-program.
AFMIS	Afghanistan Financial Management Information System. A financial management information system such as AFMIS typically integrates a core accounting system to meet basic information needs and containing modules for accounts payable, accounts receivable, and the general ledger.
Audit	Expert examination of legal and financial compliance or performance, carried out to satisfy the requirements of management (internal audit), or an external audit entity, or any other independent auditor, to meet statutory obligations (external audit).
Baseline Budget	This baseline budget includes the costs of the current level of activity, which is the costs of ongoing programs adjusted for inflation services, legally mandated requirements, one-time expenditures, and the impact on a full year basis of decisions made in the current year.
Budget	The budget is generally prepared annually, and comprises a statement of the government's proposed expenditures, revenues, borrowing and other financial transactions in the following year and, in many countries, for two or three further years. The budget is submitted to parliament, which authorizes expenditure by approving either a budget act or an appropriation act that is consistent with the budget proposals.
Budgetary Unit	A Ministry or Government Agency
Capital Investment	An outlay of money to acquire or improve capital assets such as buildings and equipment.
Cash Basis	In IRoA, it is an accounting method that recognizes revenues when cash is received and recognizes expenses when cash is paid out.
Chart of Accounts	A chart of accounts provides the structure for recording and reporting of all financial transactions for a governmental unit, and classifies and determines what financial transactions can be tracked for managerial purposes and reported in the financial statements.
Core Budget	Includes all income and expenditure (including donor fund) that pass through and are administered by the Ministry of Finance (through the Treasury Single Account).
Costing	A management tool used to estimate the overall resources needed for implementation of an activity/program, assuming normal operations.
Development Budget	That part of the core budget that is funded by an aid donor.
Efficiency	Measures the ratio of inputs needed per unit of output produced, measuring the extent to which resources are available for and applied targeted activities e.g. cost of vaccination program/number vaccinated.
Effectiveness	Measures the ratio of outputs (or resources used to produce the outputs) per unit of project outcome/impact e.g. the number of vaccination (or cost) per unit decline in mortality rate.
External Budget	A sub-program/activity that is funded directly from an aid donor and that financing does not go through the Ministry of Finance accounts outside the core.
Financial Management	Financial management includes the raising of revenue; the management and control of public expenditure; financial accounting and reporting; cash management; and, in some cases, asset management.

Indicator	The unit used to measure an outcome or output. International best-practice to list these separately to the actual name of the outcome or output, to ensure clarity.
Line Item	In a line item system, expenditures for the coming year are listed according to objects of expenditure or "line items."
Outcome	Sometimes called the result and is used to describe what is intended to be achieved by the end of implementation on one or more activities. An outcome defines impact or effect we want to achieve in the society.
Operating Budget	Component of the core budget that is raised from government revenue and for which the government has sole charge of. Normally it is used for salaries and wages and goods and services but rarely acquisition of assets (capital) expenditure.
Objective	A concise statement of why a ministry exists, a program objective (often just referred to as an objective) describes one of several responsibilities of a ministry, and an operational objectives describes a task associated with a particular sub-program (in order to achieve the objective of the program).
Outputs	Goods or services produced by an activity e.g. no of vaccinations.
Pillars	3 Pillars (1. security, 2. governance, rule of law and human rights, 3. economic and social development) come from ANDS and represent the IRoA framework and vision for reform.
Program	A grouping of Ministry functions according to a key objective, based on the main functions performed or services delivered by ministry. Normally there would be no more than 5 programs per Ministry.
Program Budget	Program budgeting is linking government budget and other resources to the public policy objective. Program budgeting requires that program objectives stretch beyond a single fiscal year. Program budgeting requires effectiveness measures, which means the measurement of outputs and outcomes.
Project	A donor funded activity
Performance Indicators	Performance indicators or performance measures are defined as "quantifiable, enduring measures of public sector inputs, outputs, outcomes, and efficiency ".
Recurrent Activity	Package of ongoing and reoccurring operations that consumes inputs and produces a consumable good or service.
Strategic Plan	A plan that sets forth an organization's mission, goals, objectives, courses of action, and expected results for a specific time frame, usually five to ten years.
Sub program	For managerial efficiency, programs are often sub divided into smaller units of work. They must have a well-defined purpose, budget, and time line and be related directly to achieving the purpose of the program that is its host.