

Capital Budgeting in Ukraine

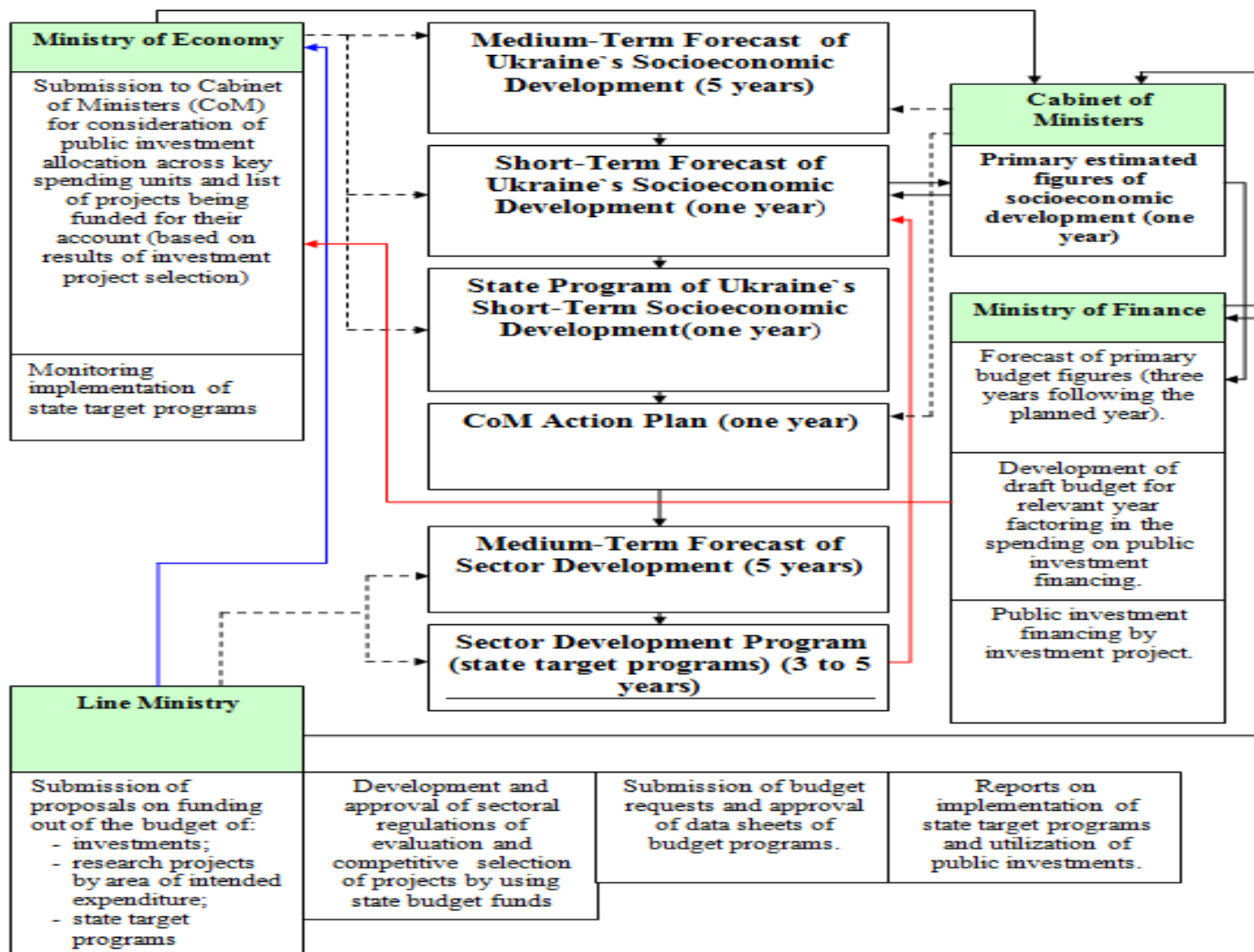
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Characteristics of Capital Budgeting Today

- Capital expenditures as a share of GDP have declined significantly in recent years
- New projects often have priority over those that have already been launched
- The combination of strategic planning and capital budgeting is not realized. There is no clear hierarchy among strategic planning documents, and no correlation between the capital budgeting process and strategic planning
- Capital spending is planned by the Ministry of Finance (MoF) together with the key spending unit concurrently with the draft budget formation, and the Ministry of Economy (MoE), which is a leading agency in the implementation of national investment policy, is not involved in the process.
- The process of selection of projects begins in the year in which they are planned for implementation. As a result, the one-year budget cycle leads to many projects remaining underfunded and unrealized.

Current System of Formation of Investments and Capital Expenditures



Problems of Capital Budgeting System

- The current system of capital budgeting does not ensure effective use of budget funds allocated for capital investments, nor does it ensure implementation of the country`s socioeconomic policy
- Therefore, it calls for development of new approaches to its operation. A system of investment formation based on clear-cut strategic priorities needs to be put in place.

The Required Changes The Government Is Working On

- Establish a relationship between strategy and capital budget
- Adopt a system of project evaluation and selection
- Adopt a system of management of state-owned assets



Sequence of Formation of Forecasting and Strategic Planning Documents and Budget Expenditure

- 1. State development strategic plan identifies:**
 - sectoral and multi-sectoral objectives
 - tasks designed to achieve them
 - sources of financing
- 2. State target programs identify activities to achieve the goals and objectives set out in the State development strategic plan**

Sequence of Formation of Forecasting and Strategic Planning Documents and Budget Expenditure

3. State investment program (for 3 years):

- identifies areas of public investment and annual financing
- takes into account data of the asset register and asset management activities
- is developed towards achieving state target program objectives

Establishing a Relationship between Budget and Strategic Development Plan

- 1) Only projects approved under the State Investment Program are funded out of the budget
- 2) Given the provisions of Article 21 of the new version of the Budget Code, budget expenditure is planned for 3 years
- 3) Stages of the medium-term investment calendar should be coordinated with the beginning of the budget planning process

Major Stages of Medium-Term Calendar of Public Investment

- **Stage I** (*first half of the base year*) – selection of project proposals (key spending unit)
- **Stage II** (*Q3 – mid-Q4 of the base year*) – formation of investment programs/projects register (e.g, *MoE*)
- **Stage III** (*mid-Q4 of the base year – Q1 of the year preceding the planned one*) – determination of limit spending on investments and the limit amount of guarantees (MoE, MoF)

Major Stages of Medium-Term Calendar of Public Investment

- **Stage IV** (*Q2 – mid-Q3 of the year preceding the planned one*) – allocation of investments among key spending units (MoE); compilation of budget programs (key spending units); development of project estimates (key spending units)
- **Stage V** (*mid-Q3 – the end of the year preceding the planned one*) – the MoE takes part in the consideration and passage of the law on state budget in its part concerning investments

Major Stages of Medium-Term Calendar of Public Investment

- **Stage VI (*Q1 of the planned year*)** – key spending units ensure approval of data sheets of budget programs, with an indication of funds necessary for completion of the investment program/project
- **Stage VII (*Q2 – Q4 of the planned year*)** – key spending units:
 - complete development of project estimates (as appropriate);
 - carry out the investment program/project

MoE (or any other authorized agency):

- **Organizes, provides and monitors the planning and allocation of capital expenditures for investment projects/programs:**
- carries out selection of project proposals submitted by key spending units;
- registers selected projects and maintains the register on a permanent basis;
- ensures the asset management process and maintains the asset register;
- identifies and coordinates overall planned expenditures for investments with the MoF;
- provides a letter of project approval to the key spending unit, which is a basis for the preparation by the unit of the relevant budget program and budget request;
- **Takes part in budget program monitoring and performance evaluation.**

Major Activities Necessary for Putting in Place an Efficient System of Budgetary Funds Management

1. Inventory of property assets of state enterprises and state-financed institutions and establishing a General Register of Assets
2. Development and implementation of a system of analysis and efficiency evaluation of asset management
3. Considering the results in the planning of investments.
4. Introduction of the Medium-Term Plan for Asset Management as part of public investment
5. Establishment of a procedure for budget formation factoring in the Program of Public Investment
6. Adoption of the Medium-Term Calendar
7. Establishment of a procedure for investment project selection
8. Introduction of the appropriate management structure (optimization of structure, definition of responsibilities of participants, establishment of procedures, etc.)
9. Staff training
10. Development of necessary software.

Capital Budgeting Reform Should Result in a New Simplified System That Will Improve Public Investment Efficiency

