



**DEPARTMENT OF TREASURY
Office of the Secretary**

**Telephone: (675) 312 8812
Facsimile: (675) 312 8804**

**Vulupindi Haus
PO Box 542, WAIGANI, NCD**

BUDGET CIRCULAR 7/2009

28 July 2009

CIRCULAR LETTER TO:

All Provincial Administrators

ALLOCATION OF 2010 RECURRENT BUDGET CEILINGS AND PREPARATION OF 2010 RECURRENT BUDGET SUBMISSIONS - PROVINCIAL ADMINISTRATIONS

1. PURPOSE

This Budget Circular is intended to:

1. advise Provincial Administrations/Governments (Provinces) of the 2010 Recurrent Budget Ceilings;
2. advise Provinces of the policy framework underpinning the 2010 Budget;
3. provide guidance to Provinces on the form and content for their 2010 Recurrent Budget Submissions; and
4. seek 2010 Budget Submissions by close of business **12 August 2009**.

**2010 DEVELOPMENT BUDGET CEILINGS AND INSTRUCTIONS FOR
COMPLETING 2010 DEVELOPMENT BUDGET SUBMISSIONS WILL BE
PROVIDED SEPARATELY BY THE DEPARTMENT OF NATIONAL PLANNING
AND MONITORING.**

Provincial Administrators must ensure that their Provinces' obligations are met and that officers responsible for preparing the 2010 Budget Submission are provided with copies of this Budget Circular.

Officers responsible for preparing 2010 Budget Submissions must read this Budget Circular closely and ensure that they comply with the requirements of the Circular.

Please contact Budget Division in the Department of Treasury (Treasury) if you need help understanding this circular.

2. STRUCTURE OF BUDGET CIRCULAR

This Budget Circular includes the following information to assist Provinces to formulate and submit their 2010 Budget Submissions.

- *Section 3* provides details on the **2010 Budget ceilings**;
- *Section 4* outlines the **key dates** for the 2010 National Budget;
- *Section 5* provides the **policy principles** driving the formulation of the 2010 National Budget and the priority funding areas based on the Government's development policies;
- *Section 6* explains the **revised Budget process** for Provinces under RIGFA;
- *Section 7* explains the different **recurrent grants** available to Provinces and LLGs;
- *Section 8* provides the instructions to formulate and submit 2010 **Recurrent Budget Submissions**; and
- *Section 9* provides details of **Key Contacts** within the Department of Treasury (Treasury) and the Department of Finance (Finance).

3. 2010 BUDGET CEILINGS

The 2010 Budget Ceilings have been set to enable the Government to meet its targets under the *Medium Term Fiscal Strategy 2008-2012* (MTFS), the requirements of the *Fiscal Responsibility Act 2006* that the Budget be in balance over the term of the Government, and the improved funding arrangements for Provinces arising from Review of Intergovernmental Financing Arrangements (RIGFA). The ceilings seek to meet these objectives using the latest forecasts of Government revenue and expenditure for 2010 and the medium term.

Attachment A provides the Personnel Emoluments and Goods and Services ceilings for your Province.

Given the devolution of Human Resource functions, a preliminary staff ceiling has not been provided for the 2010 Budget. However, your 2010 Recurrent Budget Submission must include your Province's existing staff structure (including staff on strength, vacancies and unattached officers) and proposed structure and evidence that staffing levels, including public servants and teachers, are within your personnel emoluments ceiling for 2010 and will remain within this ceiling throughout 2010.

4. KEY DATES FOR THE 2010 NATIONAL BUDGET

For Provinces, the following dates apply:

- **July 2009** – Discussions with Treasury on the distribution of the total goods and services grant ceiling between the different grants. See section 6.1.2 below for more details of this process.
- **12 August 2009** – the due date for Provinces to submit their 2010 Recurrent Budget Submissions.
- **7 – 25 September 2009** – Budget meetings between Provinces and the Budget Screening Committee (BSC). These meetings are held to provide Provinces the opportunity to present and discuss their 2010 Budget Submission with senior officials from central agencies. Details of BSC meetings, including dates, time, venue, and format and structure, will be provided in August.
- **10 November 2009** – 2010 Budget tabled in Parliament.

5. PRINCIPLES GUIDING THE FRAMING OF THE 2010 NATIONAL BUDGET

The 2010 Budget will be framed against a background of reduced revenue due to the Global Financial Crisis and increased expenditure pressures. Consequently, there will be limited opportunities for increasing funding. Provinces should consider these constraints when preparing 2010 Budget Submissions.

5.1 The Budget Strategy Paper

The 2010 Budget Strategy Paper (BSP) is the key document establishing the broad principles that guide the 2010 Budget process. The BSP establishes the economic and fiscal parameters for the 2010 Budget and draws on the Government's key high level medium term policy.

Using the latest forecasts of revenue and expenditures, the BSP provides for the following broad fiscal parameters that underpin the 2010 Budget Ceilings:

- Total revenue and grants is estimated to be **K5,959.0 million**.
- Total expenditure and net lending is expected to be **K5,959.0 million**.
 - Total recurrent expenditure is estimated to be **K4,050.6 million**.
 - Total development expenditure is estimated to be **K1,908.4 million**.
- A balanced Budget is projected for 2010.

The BSP can be accessed from the Treasury website (www.treasury.gov.pg).

5.2 The Medium Term Fiscal Strategy

The key policy document that informs the BSP is the MTF. The MTF provides a responsible, prudent and sustainable framework for the Government to manage its fiscal resources. The MTF lays out the following three key fiscal rules to assist the

Government with achieving sustainable economic growth through correct management of its resources:

- keeping ongoing expenditure in line with normal, sustainable revenues;
- using additional windfall mineral revenue to pre-fund public investment projects and repay debt and other liabilities; and
- limiting the amount of actual public investment expenditure sourced from windfall revenues to a maximum of 4 per cent of GDP in any one year, in order to promote macroeconomic stability and minimise inflationary pressures. It is expected that there will be no additional mineral revenue available in 2010 to fund additional priority expenditure or one-off investment projects.

The MTFs can be accessed from the Treasury website (www.treasury.gov.pg).

5.3 The Medium Term Development Strategy

While the MTFs provides the framework for determining how much to spend, a key policy document guiding the Government's decisions on what to spend money on is the Medium Term Development Strategy (MTDS).

The MTDS promotes fiscal sustainability as an important Government objective. It aims to strengthen public expenditure management by providing a framework to prioritise the use of fiscal resources (including borrowing) and encourage the cost-effective implementation of programs.

The MTDS identifies the following seven key expenditure priorities for the period from 2005 to 2010:

- Rehabilitation and Maintenance of Transport Infrastructure;
- Law and Justice;
- Primary Health Care;
- Basic Education;
- Promotion of Income Earning Opportunities;
- Development-oriented Informal Adult Education; and
- HIV-AIDS Prevention.

When preparing 2010 Budget Submissions, Provinces should ensure that they have regard to the MTDS expenditure priorities. The Government's contribution to these expenditure priorities in 2009 was 53.0 per cent. This is significantly higher than the contributions of 41.0 per cent and 40.5 per cent in the 2007 Budget and 2008 Budget respectively. Analysis of fixed commitments in the Development Budget is currently being undertaken to determine the Government's development expenditure levels for 2010 whilst achieving a balanced budget.

Further information on the key expenditure priorities can be obtained from the Department of National Planning and Monitoring.

6. REVISED FINANCING ARRANGEMENTS AND INTERIM PROCESSES

Amendments to the *Organic Law on Provincial Governments and Local-level Governments* in 2008 resulted in the implementation of a revised system for funding most Provincial and Local-Level governments. These amendments stem from the *Review of Intergovernmental Financial Arrangements* (RIGFA) which was conducted by the National Economic and Fiscal Commission (NEFC).

For NCD and Bougainville, which are not covered by RIGFA, arrangements remain unchanged.

6.1 Changes to the Budget process

The revised financing arrangements, which were introduced in the 2009 Budget, provide the Provinces with higher levels of funding on average, more certainty over their funding, and detailed information about funding earlier in the year to allow for more effective internal Budget processes.

6.1.1 Determining the equalisation amount

One of the key benefits of the revised system is that it will determine the amount of goods and services funding available to the Provinces and LLGs on a sustainable basis, that will grow as the National Government's net revenue grows.

The legislation sets the total amount of goods and services funding available to Provinces and LLGs (the **Equalisation Amount**). While the system will provide more funding, on average, for Provinces, they will **not** be able to negotiate to have this ceiling increased because the total amount of goods and services funding will be set by law.

6.1.2 Discussion with Treasury on individual goods and services grants

Although Provinces **cannot change** the Total Goods and Services Ceiling, they can propose a different split of the ceiling between the various grants **within** the total ceiling.

- Where Provinces propose an alternative split of grants, they should advise Treasury as soon as possible.
- If you do not raise this with Treasury, the Treasury ceilings will be put forward in the Budget.

Where a Province proposes a different split of Grants, Treasury will assess the proposal and may enter into further discussions with the Provinces.

However, because the ceilings provided by Treasury are based on a detailed analysis by NEFC of actual costs, expenditure and resources within each Province, Provinces will have to provide detailed, complete and credible alternative evidence to support their request for a different split of Grants.

In most cases, Treasury will not agree to a variation of more than 10 per cent from the ceiling in **any individual Grant**.

If Provinces would like any assistance in the allocation of the **Total Goods and Services Ceiling** between the Administration Grant and Function Grants, they

should contact Treasury. The NEFC's *Costs of Services Study* may assist Provinces to make decisions about how best to allocate this funding.

6.1.3 Ministerial Grant Determination to set Goods and Services Grants

Once discussions on the individual grants are finalised with all Provinces, Treasury and NEFC will make a recommendation to the Treasurer on the individual Goods and Services Grants for each Province and LLG.

On the basis of this advice, by 3 August 2009 the Treasurer will issue a Ministerial Determination which will set the Goods and Services Grants for the 2010 Budget.

As this determination will be issued before the commencement of the normal Budget Committees, the Goods and Services Grants for Provinces will not be considered further by the Committees.

6.2 Additional grant types

A ceiling has been provided for an **Administration Grant** to fund the general administration of the Province. The NEFC *Costs of Services Study* has demonstrated that, in most cases, Provinces have sufficient funding for administration. For this reason, where additional funding is available it has generally been directed towards the MTDS priority areas. If Provinces feel that they need a higher level of funding for administration, they should use their own internal revenue.

In order to provide funding for all the non-MTDS functions that Provinces are responsible for, an **Other Services Function Grant** ceiling has been provided separately. The purpose of this grant is to provide funding toward the Provincial functions which are not covered by the other sector specific Function Grants.

The Derivation Grant is no longer provided. It has been replaced with an **Agriculture Function Grant** which may also be used to fund Fishery and Forestry activities.

6.3 Conditions on the use of Function Grants

Function Grants are provided to the Provinces by the National Government on the condition that they are used for the purpose provided, in the year that the funding is provided.

The main purpose of Function Grants is to improve service delivery in the MTDS core priority areas by ensuring that these sectors have a minimum level of funding. As with the Administration Grant, it is expected that Provinces will supplement National Government Function Grants with funding from their internal revenues.

Function Grants are to be used to pay for operational goods and services and maintenance costs incurred in the relevant sector. They must not be spent on salaries or capital development.

6.3.1 Budget and Expenditure Instructions

Under the revised system, the Secretary for Treasury can issue *Budget and Expenditure Instructions* to specify conditions on the use of Provincial Grants.

Provinces should ensure that they have the latest *Budget and Expenditure Instructions* and apply them as they prepare their Budgets.

6.3.2 Reviews and Reporting of Expenditure

The NEFC has completed a review of the expenditure of Function Grants for the 2007 Budget year, and is close to completing its review for 2008. These reviews conclude that in order for the Provinces to effectively use the function grant funds, they must:

- Spend **all** the money they receive;
- Spend it in a **timely** manner and avoid holding the money until the end of the year;
- Spend the money on the **functions** for which it was provided, and avoid spending the Function Grants on wages, capital work and non-essential items;
- **Share** financial information with Program Managers to ensure effective implementation; and
- Include the Provincial Treasurer as part of the management team. The Provincial Treasury **must** make financial data available to the Provincial Administration on a regular basis.

The NEFC will continue to monitor the transfer and expenditure of the **Function Grants**. In order to assist the NEFC in future reviews, Treasury has emphasised the importance of Provinces providing expenditure reports for health, education, transport infrastructure maintenance and village court spending from their '200 series' grants and '700 series' revenues, as part of the Quarterly Budget Review process.

7. RECURRENT GRANTS

The following guidance has been provided to assist Provinces to understand the grants that are appropriated by the National Government.

7.1 Personal Emoluments

7.1.1 Public Servants and Teachers Salaries and Allowances Grants

Separate grants are provided for the salaries and allowances of both Public Servants and Teachers. The ceilings are based on achieving a reasonable balance between the actual costs of teachers and public servants over the past few years and requests from Provincial Administrations for funding under these items.

Public Servants and Teachers paid under these grants should be processed through the Alesco 'Concept' payroll system.

7.1.2 Public Servants and Teachers Leave Fares

It is expected that funding for leave fares will be similar to the 2009 Budget, with some indexation. Outstanding leave fare arrears from earlier years for the Provinces should have been met through the recent acquittal process for arrears.

Provinces are required to keep more accurate leave records to ensure that better estimates of leave fare costs can be provided to Treasury. This will allow for more accurate provisions for leave fares in the future.

7.1.3 Village Courts Allowances Grant

It is expected that the Village Courts Allowances Grant for 2010 will be similar to what was provided in 2009. This grant may *only* be used to fund the costs of salaries for village court officials.

The Village Courts Allowances Grant is based on data which was agreed between Treasury, the NEFC and the Village Courts Secretariat.

The 2010 Budget also includes a separate *Village Court Function Grant* for goods and services to assist in meeting the operational and supervision costs of village courts.

7.2 Goods and Services Grants

Each Province has been provided with a **Total Goods and Services Ceilings** for the recurrent, non-staffing costs of delivering goods and services. This is a hard ceiling which is **not negotiable**. The ceiling is determined in consultation with the NEFC on the basis of:

- the total amount of funding available to Provinces and LLGs under the revised financing arrangements (known as the Equalisation Amount);
- the amount of internal revenue available to the Province; and
- the fiscal need of the Province as assessed by the NEFC.

The Individual Goods and Services Ceiling has been split into two broadly grouped ceilings as follows:

- **Administration and Function Grant Ceiling** for funding the Administration Grant and the six Function Grants (Health, Education, Transport Infrastructure Maintenance, Agriculture, Village Courts and Other Services). Provinces are able to negotiate with Treasury regarding a revised distribution of the Ceiling *between* the individual grants (see Section 6.1.2 above).
- **Local-Level Government Ceiling** for funding the urban LLGs and rural LLGs. The Local-Level Government Ceiling and the individual LLG grants under it are not open to negotiation. They have been determined on the basis of NEFC analysis of the amount of funding available and the population of each LLG.

More information on the individual Goods and Services grants, and the purpose for which they are provided, is included in the *Budget and Expenditure Instructions*.

8. INSTRUCTIONS FOR COMPLETING 2010 RECURRENT BUDGET SUBMISSIONS

8.1 Format of a Province's 2010 Recurrent Budget Estimates

Provinces are required to prepare a 2010 Budget submission and submit it to the Department of Treasury by **12 August 2009**. Where a Province does not lodge a

submission, or lodges it late, that Province will not be allowed to present to the BSC.

The submission should be consistent with the Budget structure in Volume 2 Part 2 of the 2009 Budget papers. Provinces will need to supply an electronic copy (diskette), a signed hard copy and four (4) photocopies of their 2010 Recurrent Budget Submissions and all attachments.

Provinces must ensure that the submission they lodge with Treasury is their final submission. If a Province tries to present a different submission to the BSC from the one that was submitted to Treasury, it will be rejected and the original submission will be considered.

8.1.1 Electronic (Flat file) Budget Submissions

Provinces are required to lodge a diskette containing an electronic flat file of their 2010 Recurrent Budget Bids for uploading into the Planning and Budgetary System (PBS).

Officials requiring further assistance in the preparation of 2010 Budget Submissions should contact the relevant officers identified in Section 10 below.

8.1.2 Written Budget Submissions

In addition to the electronic submission outlined under 8.1.1 above, Provinces will also be required to provide a signed written Budget submission and four photocopies outlining their planned expenditure for the coming year.

Use Table 2 (included at Attachment B to this circular) to present a Provincial Budget Summary Table. Information should be provided, to the nearest thousand Kina for:

- 2008 (actual expenditure as shown in the final public accounts);
- 2009 (current appropriation); and
- 2010 (the funding sought in your Province's Budget Submission).

Although the Goods and Services grants will be set by the Ministerial determination **before** the submission is due, you must include these grants in your submission. Provinces will not be able to seek to change the goods and services grants through their submission.

Provinces are reminded that there will be minimal additional funding available in 2010. New functions should be funded by prioritising and finding savings from existing activities, or from internal revenue. The fact that the Province has a new establishment or structure does not automatically mean that funding will be provided for additional positions in the establishment.

8.2 Preparation of 2010 Budget Submissions within the Ceilings Allocated

Provinces must ensure that their 2010 Budget Submissions are within the Budget Ceilings allocated to them.

- The Budget Ceilings allocated to your Province are detailed in Attachment A to this Circular.

8.2.1 Guidance to Agencies on Meeting Budget Ceilings

The Budget Ceilings provided are the *maximum* levels of funding that will be available to Provinces. Where Provinces need to find savings to stay within the ceiling, they should look to find them from:

- reductions in operating costs (particularly in head/regional office administration);
- non-core or low priority areas; and
- reductions in non-service delivery activities, such as administration.

8.2.2 Aligning Corporate Plans with the Budget

Some Provinces have indicated to Treasury that they are *under-funded* because they are not allocated the funds they have requested to carry out the work areas identified in their corporate planning documents. Provinces should be aware that there is limited funding available and that the Government allocates funding on the basis of *whole of government* expenditure priorities and its policy objectives.

The Budget is the Government's money plan for the year and the Government expects Provinces to work within what is affordable for PNG. All Provinces should ensure that the tasks identified in their Corporate Plans and Annual Management Plans are achievable **within** the funding available, including funding allocated to them through the National Budget. Provinces should adjust their work plans (including their Corporate Plans and Annual Management Plans) to ensure that they are able to operate **within** the Budget Ceilings allocated.

8.3 Personnel Emoluments and Staffing Resources

An increase of three per cent has been included in Provinces' allocated Budget Ceiling for personnel emoluments set out in Attachment A to this Circular. This increase is for known and anticipated wage indexation under various industrial awards, including the *Public Employees Association (PEA) Agreement*. This increase is **not** for additional staffing positions.

Provinces **should indicate** in their 2010 Recurrent Budget Submissions any financial implications of annual automatic increment progression expected in 2010 for Public Servants. This cost is the only allowable increase above the personnel emoluments ceiling for 2010. Provinces should refer to the Department of Personnel Management Circular Instruction No. 36 of 2007 for further information on incremental progression, including the new Performance Based Salary Structure.

A key requirement under the devolution of Human Resource functions is managing and maintaining staff numbers **within** the budget funding for personnel emoluments in 2010. Provinces must include as part of their 2010 Recurrent Budget Submission their existing staff structure (including staff on strength, vacancies and unattached officers) and proposed structure and evidence that staffing levels, including public servants and teachers are within the personnel emoluments ceiling for 2010 and will remain within this ceiling throughout 2010. That is, any planned increase in personnel emoluments expenditure in an activity due to recruitment or restructuring must be offset from a decrease in staffing expenditure in another activity.

In addition, to assist government cash flow estimation, Provinces should provide information to Treasury in relation to the level and timing of contract gratuities and expected leave fares for the following year.

Each Province must also advise Treasury of the number of *Casuals* it currently employs, and explain how these *Casuals* assist in the delivery of key services.

8.4 Annual Return on Trust

Section 19(3) of the *Public Finances (Management) Act 1995* (PFM Act) requires Provincial Administrators responsible for managing trust accounts to provide a return for each trust account before the commencement of the following financial year.

Provinces that have trust accounts should use Attachment C to this Circular to provide a return for *each* trust account they operate or have responsibility for. All returns must be included in the 2010 Budget Submission.

Each return should detail an *estimate* of the balance of the trust account and the expected receipts and payments to be made to or from the account over the 2010 financial year.

Officials requiring further assistance in the preparation of Trust Estimates should contact the relevant officer identified in Section 10 below.

8.4 Internal Audit

Under Section 9 of the PFM Act and Finance Instruction 02/2008, National Departments, Provincial Governments and specified Statutory Authorities are required to establish internal audit units and audit committees.

To assist compliance with the PFM Act, all Provinces are strongly encouraged to separately identify in their 2010 Recurrent Budget Submissions the personnel emolument funding and goods and services funding that will be allocated from within 2010 Recurrent Budget Ceilings to resource their Internal Audit Unit.

9. CONTACTS FOR THE 2010 NATIONAL BUDGET

If clarification is required in relation to any section of this Circular, or if your Province requires any further information or assistance in preparing their 2010 Budget Submissions, please contact the following officers:

9.1 Recurrent Budget (Treasury)

Provincial Sector	Mr. Lazarus Enker	312 8739
-------------------	-------------------	----------

9.2 Electronic (flat file) Budget Submissions (Finance)

Information & Communication Technology Division	Mr Paul Murray	328 8498
--	----------------	----------

9.3 Trusts (Finance)

Trust Accounting, Public Accounts	Mr Ralph Joromo	328 8602
-----------------------------------	-----------------	----------

Important Note

I seek your co-operation in ensuring your Province provides Treasury and Finance with accurate information in the format provided in this Budget Circular by the due date so that the 2010 Budget process can be conducted successfully.

In addition, we request that this Circular and attachments be provided to the relevant officers in your Province as soon as possible after receipt. This will ensure that your Province has more time to formulate its 2010 Recurrent Budget Submissions and to clarify any issues with Treasury or Finance.

.....
Simon Tosali
Acting Secretary
Department of Treasury

Attachments:

- A.** 2010 Recurrent Budget Ceilings Allocated to Your Province (**Table BC**)
- B.** 2010 Provincial Budget Summary Table Format (**Table 2**)
- C.** Format of Trust Information Required (**Table 3**)