

Chapter 76

Public Financial Management and Systems of Accountability in Sub–National Governance in Developing Economies

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ABSTRACT

There is an increasing focus worldwide on improving the quality of public financial management, with many countries in both the developed and the developing world making important and impressive achievements in strengthening public financial management and governance. This chapter explores how subnational government financial management can be improved and capacity strengthened in developing economies. Using Ghana's subnational financial management and accountability system as illustration, this study shows that improving public financial management leads to better quality of public services. The subnational government landscape is rapidly changing, with increasing emphasis on fiscal management and discipline, prioritization of expenditure, and value for money. It is even more important that international donors, governments, and national and local institutions, including regulators and professional accountancy bodies, work together in partnership to achieve long-lasting improvements, transparency, and accountability in public financial management.

INTRODUCTION

The public sector landscape is rapidly changing with an increasing emphasis on fiscal management and discipline, prioritization of expenditure, and value for money (Paletta, 2011). As a result, it is even more important that international donors, governments, and national and local institutions, including regulators and professional accountancy bodies, work together in partnership to achieve long-lasting improvements, transparency, and accountability in public financial management. For various reasons, if decentralization is to achieve its purpose it must be characterized by fiscal empowerment and autonomy. However,

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it has become difficult for local authorities to fund services and projects. The numerous functions to be executed raise high expectations among major stakeholders. So how can Public Financial Management (PFM) and systems of accountability be improved in the subnational governance in order to satisfy these stakeholders? Governments have a responsibility to enact legislation, formulate and implement policy, and deliver products and services to their citizens. The decisions and actions needed to fulfil these objectives should be taken in the public interest. Governments have coercive powers to tax, with monies raised being allocated to spending, both recurrent (e.g., paying wages to public sector employees) and capital (e.g., spending on major infrastructure projects, such as roads and railways), for the benefit of the country and its citizens. Governments are also obliged to discharge their accountability by demonstrating the manner in which they have effectively and efficiently used the resources at their disposal. Additionally, where governments have shortfalls between amounts raised through taxation and amounts outlaid as government spending, they raise funds through debt markets and, in this situation, governments have a public interest obligation to market participants to provide timely, reliable, and detailed information of their financial performance and positions.

Good public financial management systems are important for democratic governance, macro-economic stability, effective use of resources, and poverty reduction (Achua, 2009). Good public financial management systems can also help to prevent corruption and foster aid effectiveness. A sound PFM system is a precondition for effective channeling of resources to service delivery in sectors such as basic education and health services. Ineffective PFM systems, on the other hand, can hamper development and increase the risk of corruption. This chapter contributes to the literature by extending the existing knowledge in the area of PFM systems of accountability in subnational governance. It draws on the experience of Ghana to examine how PFM systems of accountability in subnational governance can be improved to enhance service satisfaction and value for money. Policy makers globally, professionals, and researchers working in the field of public policy and management, local and regional governance, local economic development, and community development may find the discussion beneficial as the chapter provides new insights into the theory and practice of subnational governance and development from an international perspective to aid knowledge transfer. This research is a useful source of policy-relevant information for policy officials at all levels of government. The rest of the chapter is organized as follows. The next section reviews the literature on PFM and accountability and describes why strong financial management is important. The following section then discusses the role of subnational government through a case study of Ghana's PFM. The final two sections outline possible future research and present the conclusion.

BACKGROUND

Definition of Public Financial Management

Public Financial Management (PFM) in the narrowest, and perhaps most traditional, sense is concerned with how governments manage the budget in its established phases – formulation, approval, and execution. Potter and Diamond (1999) have defined PFM as procedures, established by law or regulation, for managing public monies through the budget process, which includes formulation, execution, reporting, and analysis. PFM systems should include management of revenues as well as expenditures. The narrowest definition confines PFM to the downstream activities of budget execution, control, accounting, reporting, monitoring, and evaluation (Allen, Baele, Horadahl, Krylova, & Monnet, 2004). The definition

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