



Performance Based Budgeting

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Trends in Developing PI

- **Continuing to move forward with initiatives** to improve the use of PI in budgetary decision making
- **Widespread trend** : 75% of OECD countries include non-finance performance data in budget documentation
- **Long term trend**: 40% of countries working on outputs for over 10 years (*Source OECD 2005 Questionnaire on PI*)
- **Constantly evolving**: 35% of countries introduced a new initiative in past year (*Source OECD 2005 Questionnaire on PI*)

Performance Budgeting Categories

| Type | Linkage between PI and funding | Planned or actual Performance | Main purpose in the budget process |
|--------------------------------|--------------------------------|--|--|
| Presentational | No link | Performance targets and/or performance results | Accountability |
| Performance informed budgeting | Loose/indirect link | Performance targets and/or performance results | Planning and/or accountability |
| Direct/formula PB | Tight/direct link | Performance results | Resource allocation and accountability |

| Country | Most recently implemented Reform | Year | Main Purpose |
|-----------|--|-----------|--|
| Australia | Revision of Expenditure Review exercise | 2006 | Revision of expenditure review to give a greater role to the MOF identifying and managing reviews. |
| Canada | Management, Resource and Result Structure | 2005 | MRRS provides guidelines on how to collect, manage and report financial/non financial information |
| Denmark | Accrual Accounting and Budgeting | 2007 | Accrual accounting and budgeting are being implemented for the central government sector. |
| Korea | Strategic Plans | 2006 | Development of strategic plans which will be updated every 3 years. |
| Sweden | Budget Bill | 2001 | Policy areas are introduced for government activities in order to be able to evaluate them. |
| UK | Comprehensive Spending Reviews and Public Service Agreements | 2000-2007 | Reallocate money to key priorities and to improve the efficiency and delivery of public services |

Different implementation strategies for PB

- Top-down versus bottom-up
- Incremental versus big band
- Comprehensive coverage versus partial

Summary of Country Implementation Strategies

| Country | Strategies More | | Coverage more | | Timescale more | |
|------------------|-----------------|-----------|---------------|---------|----------------|-------------|
| | Top-down | Bottom Up | Comprehensive | Partial | Big Bang | Incremental |
| Australia | | X | X | | | X |
| Canada | | X | X | | | X |
| Denmark | | X | | X | | X |
| Korea | X | | | X | X | |
| Sweden | | X | | X | | X |
| UK | X | | X | | | X |
| USA | X | | X | | | X |

What is relationship between budget allocations and performance?

- Mechanical model – performance changes directly reflected in budget
- Incentives model – performance affects a portion of funding
- Agenda model – performance one factor in budget decisions
- Performance changes not yet reflected in budget

Changing budget structures

- Budget structures more conducive to integration of PI – program structure or outputs/outcomes structure
- Countries change structure as part of efforts to introduce accrual- based budgeting e.g Australia, NZ, and UK
- Does not necessarily change budgetary decision making needs also to alter the budget process and incentives of actors in process

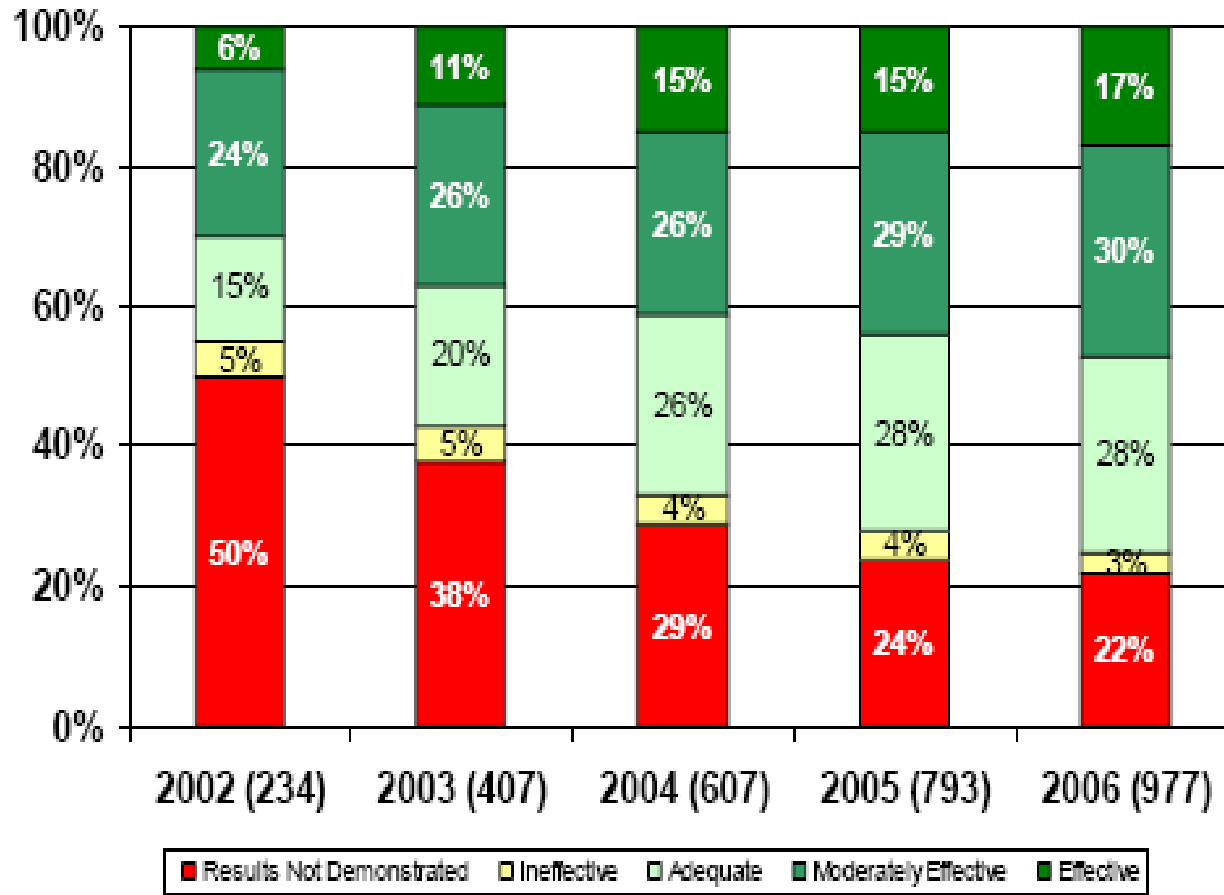
Budget negotiations between MOF and spending ministries

- Presentational PB – No formal mechanism incorporating PI into budget process e.g. Canada, Denmark, Sweden
- Performance Informed Budgeting- PI informs budget allocation along with other information
 - PI for planning purposes – loosely linking planned performance to funding e.g. NZ , UK, and Australia

Budget negotiations between MOF and spending ministries (continued)

- Performance results for accountability purposes – loosely linking performance results to funding
 - Countries do not automatically link funding to results
 - Weight given to PI depends on policy area, information available and political and economic context
 - Agency performance agreements and contracts e.g. Australia, Netherlands, NZ and Nordic countries
- Performance results as part of ad hoc or systematic expenditure review exercises
 - Ad hoc e.g. Canadian program review exercise 1995-96 and 1998-99. First review cut departmental budgets on average by 21%
 - Systematic review e.g. the Netherlands interdepartmental policy reviews
 - Reviews introduced under conditions of fiscal stress. In conditions of fiscal surplus more difficult to control increases and reduce expenditure

PART Score Trends



Direct/Formula PB

- Directly and explicitly links performance results to funding
- Mainly applied in certain sectors and countries
- Sectors – higher education and health (diagnostic related groups)
- Requires clear and explicit output measures and information on unit costs
- Issues with
 - Dysfunctional behaviour and gaming in health sector- skimping, dumping, and creaming
 - Quality of service provision
 - Implications for control of aggregate financial control

Incentives available to MOF to motivate agencies to improve efficiency and performance

- Financial rewards and sanctions
- Increase or decrease financial and managerial flexibility
- Public recognition

% of OECD MOFs that often use PI for the following courses of action

| Performance measures | Evaluations |
|------------------------------------|-------------------------------------|
| | |
| To eliminate programmes: 4% | To eliminate programmes: 11% |
| To cut expenditure: 10% | To cut expenditure: 15% |
| To determine pay: 11% | To determine pay: 5% |
| | |

Financial rewards and sanctions

- MOFs do not automatically financial reward or punish agencies based on performance results
- Exception Korea- announced a 10% budget cut for ineffective programs
- Most MOF use PI as a signaling device and serves as a trigger to more closely monitor poor performing agencies
- With poor performing agencies most common course of action to hold resources constant and review during the year

Factors influencing the use of PI in budgetary decision making

- Process to integrate PI into the budget process
- Quality of PI
- Institutional capacity of MOF and spending ministries
- Wider economic and political institutional structure and context

Reported benefits

- Greater focus on achieving results
- Mechanism to set objectives and to monitor progress
- Improves planning, especially when used in conjunction with MTEF
- More information on
 - Government goals/priorities
 - How national programs fit in with goals
 - Actual results and performance
- Improves transparency

Reported benefits (Continued)

- Signaling device highlights policies and programs that work and those that do not work
- Improving Management
- Informing citizens' choices
- Improving efficiency
 - Gap in research no comparative cross-country studies on impact on efficiency or even studies within countries
 - Although case studies and anecdotal examples support thesis
 - More evidence to support that direct/formula PB improves efficiency

Reported benefits (Continued)

- PI used to inform budget decision in certain contexts
- A few examples of PI –mainly evaluations- being used a part of expenditure reallocation or prioritization exercises
- Generally not used systematically at a government wide level for reallocation purposes
- No evidence to support thesis that it impacts on aggregate fiscal discipline

The Challenges

Countries continuing to struggle with

- Integrating PI into the budget process in a systematic manner
- Measurement of outputs & outcomes
- Gaining agreement on clear objectives and setting targets
- Improving the quality, credibility, relevance and timeliness of PI
- Perverse incentives

The Challenges (continued)

- Developing the capacity of MOF and spending ministries
- Resistance to change from public servants
- Changing behaviour and culture of politicians and civil servants
- Convincing politicians to use PI in decision making

Lessons Learned for designing budget systems that use PI

- Contextual variables – No one “best” model.
- Aligning financial information and performance information
- Longer term strategy necessary to phase in changes
- Avoiding government wide systems that tightly or directly link performance results to resource allocation
- Improving quality of PI and independence evaluation of information

Lessons Learned for implementing budget systems that use PI

- Finding an implementation approach appropriate to the wider governance and institutional structures
- Importance of leadership
- Developing the capacity of the MOF and spending ministries
- Consultation and ownership
- Having precise goals and measuring and monitoring progress towards achieving them
- Realistic expectations for role of performance in decision-making process

Conclusion

- The road from incremental towards results-based budgeting: long and difficult
- PI has proven useful but not met expectations – problems remain
- However, most OECD countries cannot imagine operating a budget system today without PI
- Countries evolving their performance approach rather than discarding
- There is a need for more realistic expectations and greater efforts to get all stakeholders on board