



## **SEQUENCING AND PACING OF PERFORMANCE BUDGETING REFORMS:**

**Summary of the 5<sup>th</sup> annual meeting of the  
SBO Network on Performance and Results  
27-28 October 2008**

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## **SEQUENCING AND PACING OF PERFORMANCE BUDGETING REFORMS: SUMMARY OF THE 5<sup>TH</sup> ANNUAL MEETING OF THE SBO NETWORK ON PERFORMANCE AND RESULTS, 27-28 OCTOBER 2008**

### **Introduction**

The OECD Senior Budget Officials Network on Performance and Results provides member countries with a forum to discuss the opportunities and challenges of implementing performance budgeting and management. The 5<sup>th</sup> annual meeting of the network took place in Paris on 27-28 October 2008. Over 70 delegates representing 30 delegations attended. This meeting examined the issues surrounding the pacing and sequencing of performance budgeting and management reforms.

Effective performance budgeting initiatives require well-defined reform objectives and implementation strategies. These strategies should include: the overall approach (top-down, bottom-up or some combination of both); the process for introducing and managing reforms; and the institutional and human capacities needed to drive and support the reforms and the sequencing and pacing of reforms.

Appropriate sequencing and a realistic timetable are crucial for successful implementation of performance budgeting. It is vital to consider the necessary building blocks or reform components, the relationship and interdependence of different reforms, and the appropriate order in which to introduce specific actions or reform components. It is also important to consider how countries can build on short-term results to help achieve longer-term reform objectives, and how to maintain the coherence of, and interest in, these reforms over the long term.

The pace of reforms varies across OECD countries: some have taken a “big bang” approach and others have adopted a more incremental method. Both Canada and Denmark have been working on performance budgeting and management for over two decades. They have taken an incremental approach to introducing performance budgeting reforms.

On the other hand, both Austria and Korea have adopted performance budgeting more recently and have taken a “big bang” implementation approach. Both countries have introduced it as part of a larger reform package including other

major fiscal reform initiatives such as medium-term expenditure frameworks. In Korea, the government began experimenting with performance budgeting and the adoption of performance management initiatives before the reforms were enacted into law in 2006. In contrast, given the Austrian cultural and institutional context, it was necessary to first have a legal framework in place in that country before the reforms could begin. The bill introducing the legal framework was passed in December 2007. The implementation of the whole reform package, including accrual accounting and medium-term expenditure frameworks, is being phased in between 2009 and 2013.

Despite these differences, all experiences indicate that it is important to develop a realistic time frame and to be practical about the time it takes to achieve significant results. Successful sequencing and pacing requires not just taking account of technical and institutional aspects of reform but also understanding how the political context and electoral cycles can influence the support, sequence and timing of reforms, and the demands for results.

A country's existing budgeting and public management system and its institutional capacity and constraints will affect its choice of sequencing strategy. While reform sequencing is thus country specific, it is possible to draw out some general guidelines, highlighting the necessary components of performance budgeting and possible different steps or sequencing approaches for implementing them.

The meeting of the network addressed the building blocks or reform components for successful adoption of performance budgeting, listed below. A session was devoted to discussing each component. (The exception is integrating performance information into the budget process which was the subject of a separate meeting in 2006.)

- Developing programme budget classification and/or developing knowledge of the programme base; presentation of performance information and budget documents.
- Developing performance information (performance measures and evaluations) and the design and implementation of information systems.
- Linking medium-term expenditure frameworks with performance budgeting and planning and objectives and/or programme budgets.
- Integration of performance information into budgetary decision-making processes.
- Integrating accounting systems with performance information systems.
- Managerial and financial flexibility and performance budgeting.

The meeting highlighted that countries have taken different approaches to these reforms. It also emphasised that there are ongoing debates about the importance of some reform components or building blocks for performance budgeting and about the order or sequence in which they should be introduced. The discussion and conclusions of each session are set out below.

### **Developing programme budget classification and/or developing knowledge of the programme base**

This session examined how countries designed their programme budget classifications, if a programme budget structure was essential for performance budgeting and what are the alternatives to a programme budget structure.

Countries agreed that it is necessary to have good knowledge of their programme base in order to implement performance budgeting and that this should be one of the first steps in the reform process. Without this information, it is not possible to link objectives to programmes and programmes to funding or to measure programme results. An important challenge facing countries is to clearly define what constitutes a programme.

Countries took different approaches to obtaining information on their programme base. Some countries such as France, the Netherlands, Sweden and the United Kingdom have changed their budget structures to focus on programmes or objectives. Others have not altered their budget structure but have obtained detailed knowledge of their programme base – for example, in the United States with the PART system (Program Assessment Rating Tool) which works alongside the budget.

Most countries supported the idea of including performance information in budget documentation and stressed the need to keep the format simple and easy to read. A few countries thought the information would be better placed in supporting documents, in order to avoid overloading the legislature with information.

### **Developing performance information and information systems**

This session discussed different country approaches to developing performance information. Countries' experiences show that it takes time and practice to develop meaningful performance information. The type of information and systems developed should depend on how the reformers intend to use such information. Is it to be closely linked to budget decisions and overall administrative efficiency like in Chile? Or is it to be used for monitoring government programmes and promoting public accountability for results like in Finland?

If information is to be used for “central” purposes (budget discussions or monitoring a development plan), central requirements for the production of performance information are important to a certain level. This is especially the case if the information is to be used for comparative purposes. Some of these central requirements can relate to methodological principles for constructing indicators, or to the type of evaluations to be carried out and the terms of reference for doing so.

In developing performance information, countries would benefit from using a common sense approach rather than spending time trying to develop the perfect system. Countries should begin simply and ensure that information sources are available and reliable and that they have feasible baseline measurement. Reformers should always keep in mind how the information will be used and should seek to develop a formal quality control process. It is important to avoid starting out with an unmanageable amount of indicators, being careless about baselines and being unsure where the data comes.

A question facing most countries is if and when they should develop performance targets. Some delegates expressed the view that it is best to concentrate initially on developing indicators and measures and only later to develop targets. They argued that this would keep the focus on developing meaningful performance information rather than focusing on achieving targets at all costs. Other delegates, however, felt that as long as the initial targets are not attached to funding, it is better to start developing and using targets as soon as possible. This allows governments to get information on performance and to motivate agencies to improve.

Countries agreed that if targets are produced, they should be a product of a strategic planning process and that there need to be baseline measurement and reliable information sources for monitoring. Good targets should be SMART (specific, measurable, achievable, relevant and timely) and jointly outlined and agreed with those delivering the service.

One of the key issues with which countries are struggling is the development of information systems to support the reporting and use of performance information. In this area there is a shortage of good practices. Systems to deal with the entire end-to-end performance budgeting process or with hierarchical programme structures are not available. It is not clear if existing financial management information systems are suitable for performance information or can be easily adapted for that purpose.

When designing these information systems, it is important to spend a considerable amount of time up front articulating roles and responsibilities, business processes and requirements, and to clearly identify who is producing and auditing the information.

Some countries have developed new information systems. For example, Finland has created the Netra Reporting System which has been operational since 2004. It is an Internet-based tool which includes accounting data and performance data. It can produce pre-defined reports and user-defined reports at all levels. All users have access to this system which is to be used as a tool for performance management and for providing information on decision making and reporting at all levels. Chile also uses a web-based application for transmitting data from ministries and agencies to and from the Ministry of Finance. Colombia has developed a separate information system known as the SIGOB, but it is not connected to the budget process.

### **Linking medium-term expenditure frameworks with performance budgeting and planning**

This session discussed the relationship between medium-term expenditure frameworks and planning and performance budgeting. Medium-term expenditure frameworks can improve transparency and facilitate greater prioritisation of government objectives. They can also improve predictability in funding and planning to achieve long-term objectives. Combining a medium-term expenditure framework with performance budgeting can in theory provide information concerning the political objectives and strategies as well as the degree to which objectives are met, including the long-term financial consequences of decisions.

A number of countries have introduced medium-term expenditure frameworks and performance budgeting as part of the same reform package – for example Austria, France and Korea. In these countries, these reform initiatives are linked. Some countries, however, have a medium-term expenditure framework without performance budgeting or vice versa. Countries agreed it is possible to integrate performance budgeting and medium-term expenditure frameworks although it was not essential to link these reforms.

It is easier to link these reforms at a global level. In Sweden, for example, expenditure areas had set goals and performance information was developed to report on the achievement of these goals. The idea was that performance results would impact on decisions for the future distribution of resources. However, in Sweden the information provided by agencies was not of sufficient quality or relevance to be used in budgetary decision making. The government has recently

reformed the system. From 2009, performance information will be used mostly for accountability purposes. One or more goals for expenditure areas will be proposed by the government and approved by Parliament. The legislative standing committees and ministries concerned must agree upon the performance information that has to be presented.

In other countries – for example Colombia – the performance system is closely aligned to the government's national development plan and the president's overall strategic goals rather than to the budget process or the medium-term expenditure plan. Countries agreed that it is important to have overall governmental objectives and to link these to programmes.

### **Integrating accounting systems with performance information systems**

This session addressed how accounting systems can be aligned with performance information systems and how countries can develop cost information. Delegates agreed that, if countries wanted to directly link activities or performance with funding allocations, it is important to have cost information. Unit cost information and detailed budgeting of specific services/tasks requires detailed cost allocation, no matter whether the accounting system is in accruals or expenditures.

The development of cost information is most advanced in the application of direct performance budgeting in higher education and health. Denmark has a very developed system of direct or activity-based budgeting for education and for health (DRG, or diagnostic related group). Both the higher education system and the DRG system operate with a block appropriation and activity-based appropriation. This involves rates being paid to institutions according to the number of full-time students who complete their studies or the number of produced operations. The advantages of this system are that funds are automatically reallocated between different institutions as a result of actual activity/demand. It improves transparency and equality as the allocation of funds is based on objective criteria (number of students or operations). In addition, this system gives an incentive to improve services (to attract students, patients) and output delivery (awarding masters degrees, producing successful operations) to gain funds.

Countries also discussed the disadvantages of this type of system. It can create incentives to lower quality. It is difficult to set rates according to real costs due to information asymmetry and to conduct detailed cost studies to define rates. In addition, institutions and hospitals tend only to draw the government's attention to

increasing costs (and not decreasing costs). Also, in education rates are based on average costs and not the marginal costs of an extra student.

### **Managerial and financial flexibility and performance budgeting**

Introducing performance information into budgeting and management processes, in theory, should be accompanied by a relaxation of input controls and by giving agencies increased financial and/or managerial flexibility in the areas of spending and staffing. Country approaches have varied greatly. More than in other areas, this aspect of performance budgeting and management is strongly influenced by historical factors and a country's existing budgeting and public management system.

Norway historically has a decentralised system of public administration, with the main responsibility for service delivery at the agency level. In the late 1980s and 1990s, reforms gave ministries and agencies increased managerial flexibility in order to improve efficiency and performance and to hold them accountable for results. Extensive improvements were made in managerial flexibility. Among other things, agencies were allowed to carry over 5% of their budget to the next year, to transfer appropriations for operating expenses between budget lines, and to use excess income for operations. In addition, agencies were given greater flexibility in personnel management.

However, the government-wide system of performance budgeting and management has developed slowly in Norway. Many ministries and agencies have made only limited progress in developing meaningful performance measures and using them in the budget process. The Ministry of Finance has so far not put pressure on ministries or agencies to actively implement performance information in the budget process. There are exceptions, and progress does vary with individual ministries and agencies. Norway struggles with problems of goal definition and developing good quality performance measures and data.

In 2008, the Ministry of Finance took an initiative to consider different models of centralised reporting of the results of evaluations. The Government Agency for Financial Management initiated a project to examine the status of performance budgeting in a systematic matter.

In contrast, in the United Kingdom the institutional and public administration system is more centralised. The earlier rounds of the public service agreements (PSAs) were a more centrally driven target-setting exercise. One of the issues resulting from this approach was that those on the front line delivering the services lacked ownership of the targets and goals and perceived them as a paper requirement imposed from above. In 2007, learning from earlier

experiences, the government reformed the PSA framework and sought to move to a more decentralised system which concentrated on outcomes. This new framework seeks to embed the genuine engagement of those delivering and using the service in design, delivery and governance across key public services. It also aims to reduce bureaucracy and unnecessary data burdens on those who deliver services at the front line. In addition, it recognises that targets are not the only tools to improve performance.

## **Conclusion**

The meeting highlighted a number of general issues and points which are summarised below.

- Getting the sequencing and pacing right is important for these reforms, as is developing a realistic long-term timeline with stages and clearly stated goals to be achieved at each stage.
- Sequencing will depend on the existing public administration system and what reforms are already in place. There is no single best model that can be or should be applied in all countries. The political and social context, past history, and other factors require an approach tailored to the situation in each country.
- Performance budgeting and performance management are intrinsically linked. Ultimately the information generated needs to be used by managers to improve programme performance, although the key issue concerns what incentives are available to motivate managers to use this information and to improve performance.
- Considerations of “use” of performance information need to start at the beginning of the process and guide all aspects of the approach.
- Countries strongly indicated that a mechanistic link in the budget process between resources and results is neither possible nor desirable. Nonetheless, information about outcomes can play a very significant role in the overall budgetary process, by supporting decision making. Performance data can inform, but they do not drive budgetary decision making.
- Communication is vital to success. Language matters, as does keeping it simple and not using jargon.
- There needs to be a better understanding of how to present performance information in line with the needs of different purposes and actors including: executives; non-executives; politicians; the public; and the individual citizen.

- Efforts should be made to understand how legislatures can be more supportive of performance budgeting. For example, Austria created an Advisory Council on Budget Reform with parliamentarians of all political parties to support the country's reform initiative.
- More attention should be given to understanding how performance budgeting can work at different stages of the budget process and at different levels of the government – national, departmental, bureau, programme and front line.