

# Performance Budgeting in Poland: An OECD Review

by

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*Poland currently has a traditional budget system that is primarily based on organisational units and control of inputs. But Poland is in the process of introducing a new budget system, the performance-based budgeting system, in order to improve public finance management and strengthen allocative and operational efficiency, multi-year budgeting, and transparency and accountability. Poland faces hard choices on how to harness the advantages of performance management while minimising the costs in terms of organisational capacity and funding. This article assesses the reform process to date, examines cross-cutting institutional, technical, and strategic issues, and provides a series of recommendations for each stage of the budget process: budget preparation, approval and execution, and reporting, accounting and audit.*

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*Keywords: Poland, budget process, performance budgeting system, performance-based budget, PBB, public finance management, allocative efficiency, operational efficiency, multi-year budgeting, transparency, accountability*

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## Preface

The Department for Public Finance Reform in the Ministry of Finance of Poland invited representatives of the OECD Budgeting and Public Expenditures Division of the Public Governance and Territorial Development Directorate to review Poland's evolving performance budgeting system. The OECD delegation comprised Ian Hawkesworth (lead) and Lisa von Trapp (both of the OECD Secretariat), and David Fjord Nielsen (consultant).<sup>1</sup>

The delegation visited Warsaw from 13 to 17 September 2010 and held discussions with relevant departments in the Ministry of Finance and with representatives of the Chancellery of the Prime Minister, line ministries and agencies, parliamentary staff, and the Supreme Audit Office (NIK). The delegation also drew on responses to a questionnaire filled out by the Ministry of Finance. The OECD would like to thank the ministry staff for their assistance in arranging the mission and their gracious hospitality throughout.

In addition to a more general description of the Polish performance budgeting system, the review seeks to provide comparisons to other OECD countries and suggests areas for potential improvement. The review takes as its structure the stages of the overall budget process.

## Executive summary

Poland currently has a traditional budget system that is primarily based on organisational units and control of inputs. In addition, Poland is in the process of introducing a new budget system: the performance-based budgeting system. This dual system will come into force in 2013. It is unclear whether the two budgets will remain in parallel or whether Poland will progressively abandon the traditional budget in favour of the performance-based budget (PBB). The purpose of introducing performance-based budgeting is to seek to improve public finance management and strengthen allocative and operational efficiency, multi-year budgeting, and transparency and accountability. This is in line with the vast majority of OECD countries where the use of performance information in public sector operations is now a uniform trend. The scope and ambition of Poland's reforms are striking, and great ingenuity and effort have gone into their design and implementation so far. With the 2009 Public Finance Act now in force, the scaffolding for the reforms is in place; however, many of the details have yet to become concrete. Poland faces hard choices on how to harness the advantages of performance management while minimising the costs in terms of organisational capacity and funding. A certain amount of flexibility and potential adjustments to areas of the reform in the coming years are to be expected. Keeping in mind the many challenges in store, this report nevertheless supports the efforts of the Polish government to use performance information and to move the reform process forward.

This report assesses the reform process to date, examines cross-cutting institutional, technical, and strategic issues, and provides a series of recommendations along the budget cycle.

### ***Institutional issues***

In order to ensure line ministry support, the Ministry of Finance set up two groups of senior line officials. Staff in the Chancellery of the Prime Minister have also played an active role. As with reforms in many countries, it has been a challenge to keep the political level focused on the reform's implementation. Strong support and political will on the part of the Chancellery of the Prime Minister, the Minister of Finance, and line ministers and their deputies are necessary for the reform to move forward.

The Department for Public Finance Reform and the State Budget Department (which prepares the traditional budget) are located under the same Deputy Minister. In order for the PBB to be fully accepted and integrated into the budget preparation and budget execution phases, a strong link must be established between the performance-based budget and the traditional budget work. This implies increased co-operation between the budget department and the PBB reform department.

### ***Technical issues***

The overall structure of the Polish performance system is well designed, but a number of technical issues remain unresolved. The most pressing technical issue concerns IT systems. There is no chart of accounts or accounting system that can provide financial information based on the PBB structure. Such information is necessary to enable the Ministry of Finance to monitor budget execution and the integrity of the accounts, particularly if the performance-based budget becomes the only budget in the future.

### ***Strategic issues regarding implementation***

The Polish performance budgeting system is designed to fully and equally cover all activities in the central government. The value of the PBB for the work of certain agencies has already been proven. However, the reform could be geared more towards the internal management of line ministries. The new initiative regarding contracts between the line ministers and the Prime Minister that will be agreed each year would seem to support such an approach.

Poland must decide whether to continue with a parallel system or switch to the PBB system only. For a switch to happen, unambiguous political support at the highest level is needed. It is likely that this will only be forthcoming if the PBB system quickly shows how and why it adds value.

### ***Summary of conclusions and recommendations***

#### ***Budget preparation***

The PBB structure for the 22 state functions and the nine national development plans is helpful for the development of good performance objectives at lower levels of the state administration. The process of top-down imposed objectives combined with bottom-up input from budget holders provides a useful framework and supports subsequent refining of objectives and indicators. A number of initiatives would increase the value of the PBB system in the short to medium term:

- Consider selecting the areas most suited for performance budgeting and develop indicators and targets further in these areas, while at the same time relaxing requirements in other areas where the benefits are less apparent.
- Limit different organisations sharing the same programmes. In the longer term, align the new performance-based budget structure and the organisational structure of government.
- Focus on the operational efficiency of agencies. Support from the Ministry of Finance in terms of standards for preparation and reporting should continue, with the aim of ensuring that the PBB system adds concrete value to the work of budget holders at the implementation level.
- Work to increase the use of output and outcome indicators, rather than activity indicators. The type of indicators should be chosen according to the policy area and purpose of the performance information. It is noted that the use of activity indicators is planned to be gradually limited.
- Introduce multi-year agreements connected to the Multi-Year Financial Plan (MYFP) as a way to align budgeting and target setting while preventing overload in the annual budget process. In many areas, relevant outcome and output targets can only be reached within the medium term.
- Introduce spending reviews within specific expenditure areas to support the performance budgeting process. The reviews should be the basis for the multi-year agreements. Sufficient capacity in the Ministry of Finance must be made available, and the relevant regulation allowing reviews must be put in place. These actions are currently being discussed in the Ministry of Finance.
- Connect the new performance agreement system (“contracts” between the Chancellery of the Prime Minister and each spending ministry) to the MYFP, thus improving the conditions for formulating outcome targets and for linking agreements to budgets.

### ***Budget approval***

The Polish parliament’s role in the budget process is clear and well developed. According to outside observers, budget oversight by Poland’s parliament is generally strong. There is adequate time to examine the draft budget, in line with OECD best practices for budget transparency, and the parliament has a strong independent analytic capacity. The Supreme Audit Office (NIK) is also an important partner in terms of analysing and providing information on performance results. The performance-based budget adds new dimensions to the budget process and can be expected to increase the workload of parliament given that it is presented alongside the traditional budget. Recommendation:

- Enhance Ministry of Finance dialogue with parliament, particularly regarding how performance information is best presented to parliament, what types of performance information are most useful to parliament (*e.g.* which indicators are most relevant), and examples of good practice since the introduction of the PBB.

### ***Budget execution***

The current Polish system for reallocation seems to be sufficiently flexible and should be continued. The reserve system gives the government additional leeway during budget execution. Carry-over rules, on the other hand, are rather strict compared to most OECD

countries. The PBB introduces decentralised responsibility to budget holders for them to monitor agencies and units, which should improve both allocative and operational efficiency over time. In order to harness the potential of the performance-based budget in the budget execution phase, the Ministry of Finance should:

- Support budget holders in their tasks of monitoring and controlling performance by developing guidelines on appropriate controls that can be used by ministries and agencies.
- Consider relaxing the rules for carry-overs in order to support multi-year agreements or to act as an incentive for efficiency in agencies.
- For a certain period, collect and analyse data on in-year transfers in order to ensure that transfers are used appropriately in the new structure. (Poland should strive to keep the rules for in-year expenditure transfers as flexible as in the current system.)

### ***Reporting, accounting and audit***

Reporting and accounting remain some of the greatest challenges faced by the Ministry of Finance. The ministry has invested heavily in an assessment of the development of an IT system for reporting and accounting for the PBB system. The experience of many OECD countries has shown that reforming IT systems for reporting and accounting can be a very difficult and costly affair. Given the directions of Poland's reform and the continued existence of the traditional budget alongside the performance-based budget, the Ministry of Finance should continue developing an integrated IT system for reporting and accounting. Such a system should include automated bridges between the traditional budget and the performance-based budget.

The scope of internal evaluation of the performance-based budget (including its organisational, financial and methodological dimensions) still needs to be decided. A small Performance Audit Unit has been set up in the Ministry of Finance, but its mandate remains somewhat unclear. The new unit should be clearly tasked with developing guidelines for performance audits. Training may also be necessary to increase the capacity of the auditors to carry out performance audits.

The Supreme Audit Office (NIK) is supportive of efforts to introduce performance-based budgeting and is committed to its success. It will remain a key partner for the Ministry of Finance (and the parliament) in moving the reform forward and refining elements of the PBB system, particularly in terms of indicators, through its continued assessments and recommendations. The PBB initiative dovetails nicely with the direction the NIK is already taking in terms of increasing performance audits.

## **1. Special cross-cutting issues**

Sections 2-5 below discuss the PBB system according to the phases of the budget process (preparation; approval; execution; and reporting, accounting and audit). However, there are a number of more cross-cutting issues that touch on all phases of the budget process; they are discussed in this first section.

### **1.1. Institutional issues**

The introduction of performance-based budgeting in Poland is anchored within the Department for Public Finance Reform, which is part of the so-called budget area of the

Ministry of Finance led by a Deputy Minister.<sup>2</sup> The Deputy Minister is responsible for the co-ordination of the Department for Public Finance Reform and the rest of the budget area with regards to the reform. The department includes units working on the legal aspects of the reform, analytical aspects, IT support, international co-operation, and EU projects. Since 2008, it has been charged with introducing the performance-based budget throughout the central government in preparation for its implementation alongside the traditional budget in 2013. Located within the Department for Public Finance Reform is the National Co-ordinator for Performance Budget (NCPB), a deputy director appointment with certain duties regarding the performance budget reform. The NCPB is a statutory body created by Article 95 of the 2009 Public Finance Act.<sup>3</sup>

For performance-based budgeting to work, line ministry ownership is paramount. In order to ensure line ministry support and technical insight, the Department for Public Finance Reform has set up two groups which deal with performance implementation. One is the Strategic Group, which consists of a dozen managers representing budget holders (these are either secretaries/undersecretaries of state or director generals in the ministries). The second group comprises departmental (ministerial) co-ordinators (usually directors of budget departments in the ministries or heads of division responsible for implementation of the performance-based budget). The role of the Strategic Group is to ensure the support of top management for PBB implementation. The role of departmental co-ordinators is to co-ordinate PBB implementation in the ministries.

As with all large reforms of the public sector, it is important to have sufficient political and bureaucratic support at the top level for a reform to move from theory to reality. While the enactment of the new 2009 Public Finance Act testifies to the existence of the political will to introduce this reform, it has proven difficult to keep the political level focused on the reform's implementation. A key challenge for the success of this reform will be to maintain the active support of the Minister of Finance and his deputy ministers, as well as their counterparts in the line ministries. It is encouraging to note that the PBB complements the new strategic national development plan anchored in the Chancellery of the Prime Minister which defines strategic priorities. Strong support from the Chancellery is necessary for the reform to move forward.

In order for the PBB to be fully accepted and integrated into the budget preparation and budget execution phases, a strong link must be established between the performance-based budget and the traditional budget work. While co-ordination is taking place today, more is needed. This implies increased co-operation between the budget department and the PBB reform department. One option might be to form a standing internal steering group led by the Deputy Minister to ensure regular co-operation. The budget department in the Ministry of Finance should become more active in design, promotion, and training efforts regarding the PBB. The use of spending reviews could be an important tool in proving the value of the performance-based budget to the broader work of the Ministry of Finance.

## **1.2. Technical issues**

The overall structure of the Polish performance system is well designed, but a number of technical issues remain unresolved. These include, for example, the development of a new chart of accounts and a new IT system, and ongoing work to refine and improve indicators. Another issue to be addressed is the lack of clear “bridges” between the traditional budget and the PBB system. While these issues do require attention, they are to be expected in a reform process of this size, and the Ministry of Finance is clearly working to address them.

The most pressing technical issue concerns IT systems. First, there is no chart of accounts or accounting system that can provide financial information based on the PBB structure. Such information is necessary to enable the Ministry of Finance to monitor budget execution and the integrity of the accounts, particularly if the performance-based budget becomes the only budget in the future. Second, there is no central IT system that can generate non-financial performance information on a whole-of-government basis. The first issue is important, the second less so. There is every reason to expect that rectifying the first issue will require substantial resources and funding. The Ministry of Finance is aware of this problem and is actively working to solve it with funding from the European Union. Experience from other countries points to the dangers of moving to tailor-made IT systems for the entire central government. In many cases, it is preferable to use existing off-the-shelf solutions.

### **1.3. Strategic issues regarding implementation**

The Polish performance budgeting system is designed to fully and equally cover all activities in the central government. While this is commendable, it is also a heavy task. There is no reason to move backwards: the value of the performance-based budget for the work of certain agencies has already been proven, and no doubt more public entities will find it useful over time. However, the reform could be geared more towards the internal management of line ministries, giving greater autonomy to the line ministers to set standards and negotiate targets and indicators with their agencies. Such an approach could be supported by the new initiative regarding contracts between the line ministers and the Prime Minister that will be agreed each year. Clearly it would be important that the new contract system builds on the work already done in the PBB system and does not invent a parallel structure. Ensuring such coherence will entail a continuous dialogue regarding the performance-based budget and the contract system which is only to be recommended. The role of the Ministry of Finance as standard setter would remain, but the focus could shift to defining particular areas where performance information more easily produces value for the top level of the government. Health and education might be two such areas, both of which already seem to be at the forefront of the Polish performance budgeting reform.

Finally, Poland must decide whether to continue with a parallel system or switch to the PBB system only, and within what time frame. Once technical issues are resolved and institutional support in the Ministry of Finance and line ministries is secured, the only other requirement is clear political support at the highest level. There is an evident danger that, if this support is not forthcoming, performance-based budgeting will wither away and become a paper exercise which will not add value to the Polish public sector. It is therefore paramount that the performance-based budget quickly shows how and why it adds value and deserves to be brought forward.

## **2. Budget preparation**

This section describes the budget preparation process as of the fourth quarter of 2010. It describes both the traditional system of budget preparation and the operation of the new performance-based budgeting system that is still being developed. The section addresses current issues facing the reform work and gives examples of how other OECD countries have tried to tackle these issues.

It should be noted that the application of the PBB has been gradual. In 2007, the PBB pilot covered only two parts of the budget (namely 28-Science and 38-Higher education). In 2008, the PBB covered 44% of the state budget expenditures, and in 2009 it covered all expenditures incurred from the state budget. Following the adoption of the new Public Finance Act in 2009, the PBB in the 2010 draft budget covered all expenditures of the state budget as well as expenditures/costs of 14 entities of the public finance sector operating on an extrabudgetary basis. The presentation of the PBB in the *Justification to the Budget* for the 2011 draft budget comprised all entities of the public finance sector (excluding the territory self-government sector and the National Health Fund).

### **2.1. Phases of budget preparation**

At present, the traditional budgeting process governs budget preparation. The performance-based budgeting reform has introduced a new structure and other elements that add transparency and introduce new dimensions to the budget process. The performance-based budget does not have a legally binding status at this point. The PBB system has introduced policy objectives and indicators and a Multi-Year Financial Plan (MYFP) which exists in parallel to the traditional budget structure. The MYFP does have a somewhat formal role, discussed below. The aim is for both the traditional and performance systems to have formal status as of 2013 with the intention of eventually only using the performance-based budget (Perczynski and Postula, 2010, p. 32). However, whether Poland can gain real benefits from these ambitious new systems and tools depends on their design, on political will, and on the administrative ability to implement and make them work in practice.

The preparation of the draft budget begins in January-February in the Ministry of Finance. The budget draft's parameters are based on the ministry's financial strategy, consisting of projections of aggregate revenue, expenditure and deficit. The finance minister submits the fiscal strategy and overall targets to the Council of Ministers which discusses and approves them. The Public Finance Act (Article 138, Section 1) states that the convergence programme<sup>4</sup> as well as the newly imposed MYFP must be considered during the preparation process. In addition, Article 105, Section 1, of the Public Finance Act specifies that the MYFP shall constitute the basis for preparing the budget bill for the subsequent budget year. In principle, the level of deficit in the budget proposal should not exceed the deficit planned in the MYFP, though there can be "justified" exceptions. Finally, specific debt rules apply if public debt is above 50% of GDP, seeking to limit the government's possibilities for increasing debt through running deficits. If debt should surpass 55 or 60% of GDP, the government must submit (respectively) a corrective or recovery programme to parliament aimed at reducing this ratio. The Public Finance Act provides certain other measures restricting public spending.

Around April, a circular regarding ministries' budget submissions is sent to line ministries. The Council of Ministers discusses funding priorities based on the government's current goals and strategies. Individual discussions may take place between the Prime Minister and line ministers at about the same time, and top-down envelopes are set by the Council of Ministers on the basis of a suggestion by the Minister of Finance. Envelopes are set at the level of the 84 budget parts (the highest level in the current budget classification), not at ministry level. Cuts are decided before budget envelopes are sent to the budget holders.



After the ministries have received their envelopes, administrators of budget parts (ministry departments, agencies and other organisations) must prepare and submit draft financial plans to the Ministry of Finance within three weeks. Timelines and formats for the preparation of these plans are stated in a circular from the Ministry of Finance. The plans are the proposed detailed budgets which must stay within the aggregated ceiling established by the Council of Ministers.

Subsequently, the Ministry of Finance has both a technical and a traditional budget discipline role. The ministry checks that the ceilings have been respected and conducts a number of bilateral discussions regarding requests from line ministries for additional funding. Such requests are common and substantial. Finally, in September, the Council of Ministers finalises the draft budget bill and submits it to parliament.

In the Ministry of Finance, several departments are involved in the budget process, totalling over 300 staff. Depending on their scope of activity, they are organised in divisions mirroring the public sector (health, education, higher education and science, labour and social policy, foreign affairs, interior affairs, and defence) as well as in divisions working on macroeconomics, tax collection, budget formulation or budget execution issues, and performance budgeting.

Traditionally, performance information is not used in the budget decision-making process. During this introductory phase of the PBB, the use of performance information remains limited and is not a deciding factor in budget allocation decisions. In some areas, though (such as education), performance information already plays a role in the budgeting process. The performance-based budget classification structure is presented to parliament as part of the *Justification to the Budget*.

The process of budget preparation in Poland is similar to many other OECD countries. The Ministry of Finance holds a central co-ordination role, and performance information is only used in the process in special situations or in specific areas.

## **2.2. The budget structure**

The new performance-based budget structure works in parallel to the traditional budget structure. The latter defines the legally binding main part of the budget act, while the former is part of the *Justification to the Budget* in a non-legally binding annex. It should be noted that multi-annual programmes are prepared in a performance-based format and are part of a legally binding annex to the budget act. In 2013, the two budget structures will be included in the budget act, and both will be legally binding as mentioned above. No decision has yet been made as to any changes after 2013.

The PBB structure is the basis for the development of performance information. The preparation of the annual budget in the performance-based budget structure takes place in parallel to the preparation of the traditional budget. The regulation for the draft financial plans has added an extra form for drawing up performance-based financial plans for the relevant budget year and the two subsequent years. In this form, budget holders translate their appropriations from the traditional budget into the expenditures that will be incurred in the PBB structure. The traditional budget structure is based on parts, sections, chapters and paragraphs (see Table 1).

As the top classification level, the parts specify mainly high-level organisational units – e.g. ministries and other bodies like chancelleries, commissions, inspections, or agencies.<sup>5</sup> An administrator of a budget part is the official responsible for one or more parts. A budget

part cannot be shared by more than one administrator. Sections denote the type of activity and area such as industry, agriculture or transport; chapters denote sub-activities or areas; paragraphs are mainly an economic classification, specifying the type of revenue, income or expenditure. Envelopes settled in the budget preparation with the Ministry of Finance are fixed to parts and categories of expenditures in the paragraphs (wages, capital expenditure) while the budget holders themselves allocate to sections, chapters and paragraphs within the previously set limits on wages and investments.

Similarly, the PBB structure also presents four levels, but in a clear hierarchical structure. Twenty-two state functions have been defined as the main classification level, representing the main areas of state activities. Each function breaks down into a number of tasks, sub-tasks and actions.

Tasks are set to achieve broad policy objectives. An example is “Crime reduction and activities for the improvement of social feeling of safety” which covers all the actions used to achieve this objective. The tasks should fit the structure of the national development plan, but this principle has not yet been applied.

**Table 1. Budget classification<sup>1</sup> in Poland, 2010**

Traditional budget structure	Example	Performance-based budget structure	Example
Parts (84)	Ministries, institutions, EU funds, local government grants, debt servicing	Functions (22)	Main policy areas such as Function 3: Education, upbringing and care, or Function 6: State economic policy
Sections (33)	Activities/areas such as industry, agriculture or transport	Tasks (145)	Main programmes such as 4.4: Public debt management, or 6.1: Increase of competitiveness of the economy
Chapters (576)	Sub-areas regarding sections such as industry, agriculture or transport	Sub-tasks (698)	Sub-programmes such as 6.1.3: Creating conditions for increasing the innovativeness of enterprises
Paragraphs (229)	Economic classifications such as wages or investment	Actions (<4 000)	Sub-activities such as 6.1.3.1: Creating conditions for functioning of enterprises

1. The horizontal rows of the table should not be read as though the levels of the traditional budget structure and the performance-based budget structure correspond.

Since the introduction of the new classification, the Ministry of Finance has worked extensively on the development of clear and easily understandable labels for the functions and tasks. For example, Function 10 changed from “Science” to “Supporting the development of Polish science”, and the tasks have been regrouped and given new labels.

The framework for the new classification was outlined by the Ministry of Finance with input from budget holders, and the number and the division between tasks and sub-tasks have been adjusted several times. The catalogue of tasks developed for the budget year 2010 will now provide the basis for the PBB structure.

An example of how the PBB is used is found in the Agency for Reconstruction and Modernisation of Agriculture. It prepared its first PBB for the year 2010, and has prior experience with a performance management framework due to its administration of various EU funds (co-financing and farm subsidies, etc.). The entity’s tasks are executed under two functions: Function 21: Rural and fishery policy, and Function 22: Strategic planning and administrative activities.

Function 22 covers expenditures that cannot be directly related to the execution of specific tasks. In essence, Function 22 concerns administrative overhead such as wages

paid to employees involved in co-ordination of budget holders' activities, strategic planning, administrative activities (accounting units, HR units, etc.) and technical maintenance.<sup>6</sup> No cost distribution of this overhead cost is in place at the moment. An argument for a cost distribution of the indirect administrative cost (overhead) is to have a full and accurate picture of all costs connected to a task. For very specific purposes, such as full cost recovery from users, this is important. However, for many other purposes, this is less vital. Good cost distribution depends on the accuracy of the cost allocation system, such as a good IT system to manage the allocations (based on distribution keys, information about the cost centres, etc.). Before such a system is in place, it would be in line with good financial management to make a rough assessment of how the costs should be distributed and who are the main users of the administrative services.

The selection and establishment of the relevant functions, tasks and sub-tasks was done in co-operation with the Ministry of Finance and was based on the traditional budget and organisational structure of the entity. The new budget was presented to the Minister of Agriculture and Rural Development for approval at task and sub-task level, as were the accompanying indicators (approximately 18 targets in all). An example of an indicator was "per cent absorption rate for EU development funds". The set-up and operation of the entity are aligned with most OECD country practice.

In the following sections, the two budget structures are evaluated according to their relevance to the existing organisational structure and usefulness for internal management, expenditure control and IT system support. A main issue is that there is no direct translation key (bridge) from the traditional structure to the new performance structure. The functions and tasks denoting the new expenditure areas cross-cut the old parts and sections. As regular accounts have not yet been established to cover the new structure, there are worries about the one-to-one translation between the old and new expenditures as well as about the correct allocation of funding and expenditure control in the new system.

### **2.2.1. Issues regarding the budget and organisational structure**

The traditional budget structure is based on organisational units, while the new PBB structure is based on functions (broad policy areas) and objectives. The assumption for the PBB is that both a function and a task can be executed by multiple budget holders (whereas in the traditional budget, parts could not be shared). One function (*e.g.* foreign policy) can have contributions from several budget holders under the jurisdiction of different ministers, as is the case for the Polish Agency for Enterprise Development. A minister can be responsible for the function, but must depend on other ministries to fulfil certain objectives. Similarly, multiple agencies can contribute via defined sub-tasks to one task, although this is uncommon.

On one hand, the organisational cross-cutting allows the budget to be presented according to a hierarchy of activities (*e.g.* sub-tasks or actions) with a cascading relationship to superior objectives (stated in functions or tasks) irrespective of organisational structure. This arrangement may support transparency, strategic planning and the planned systematic use of performance information in the budget process by presenting the different levels of tasks and their internal hierarchical relationship in a clear way.

On the other hand, a budget structure with cross-cutting organisational responsibility may cause unclear accountability between organisations and inflexibility within them. Shared resources and responsibility for tasks and functions could increase the risks

of organisational rivalry, strategic behaviour and suboptimal resource focus in both the budget preparation and budget execution stages. If a budget holder acting within a function wishes to reallocate funds, it may not be possible in some cases – probably limited – because reallocation would cross ministerial jurisdictions, thus requiring negotiations and high-level co-ordination. Likewise public finance sector entities which (via their tasks) contribute to different functions might have difficulty reallocating internally between different areas of the entity, because it would influence the objectives of another ministry. It is therefore advisable to keep the sharing as limited as possible or to make adjustments so that ministerial responsibility is closely aligned with the functions.

**Box 1. Contents of the Justification to the Budget for 2011  
(in compliance with Article 142 of the 2009 Public Finance Act of Poland)**

Volume 1: Descriptive part

Chapter I – Evaluation of the macroeconomic situation of Poland and directions of fiscal policy

1. Evaluation of the macroeconomic situation of Poland
2. Directions of fiscal policy

Chapter II – The projected out-turn of the 2010 budget year

Chapter III – Basic data of the 2011 state budget

Chapter IV – Revenues of the state budget

1. Conditions of execution of revenues of the state budget in 2010
2. Revenues of the state budget in 2010
3. Tax and non-tax revenues
4. Tax revenues
5. Non-tax revenues
6. Non-reimbursable funds coming from the European Union and other foreign sources

Chapter V – Expenditures of the state budget

Chapter VI – Multi-annual programmes

Chapter VII – State special-purpose funds and executive agencies

1. State special-purpose funds
2. Executive agencies

Chapter VIII – Settlements with the European Union

Chapter IX – The European funds budget

1. Revenues of the European funds budget
2. Expenditures of the European funds budget

Chapter X – The financing of the state budget deficit

1. Domestic financing
2. Foreign financing

Chapter XI – Receivables of the State Treasury

Chapter XII – Public finance sector

1. Revenues, expenditures and balance of the public finance sector
2. Public debt

Chapter XIII – Directions of privatisation of the State Treasury assets

1. Legal basis
2. Considerations of privatisation processes
3. Planned privatisation activities
4. Expected incomes for 2011 from privatisation and revenues from dividends
5. The promotion of privatisation

Chapter XIV – Description of the articles of the 2011 budget act

Volume 2: Descriptive part – Expenditures of the state in performance-based form

Chapter I – Performance budget as an instrument of management of strategic spheres of state

Chapter II – 2011 state budget in performance-based form

Chapter III – 2011-13 financial plans of entities of the public finance sector in performance-based form

Chapter IV – The European funds budget

Summary

Volume 3: Tabular presentation – Expenditures of the state in performance-based form

### Box 2. The Swedish experience with performance management

In Sweden, the government has worked with performance objectives since the 1980s. Reforms were enacted in 1997 and more reforms are currently under way. The Swedish performance system is based on 27 expenditure areas determined by the parliament. The expenditure areas are divided into 47 policy areas. Most of the policy areas are subdivided into activity areas. There are goals for the policy areas and activity areas which are formulated within the budget process. The purpose is to give a transparent picture of the objectives and the actual impact of the activities in the different policy areas.\* The goals are proposed by the responsible minister and approved by parliament and have proved stable over time.

The Swedish appropriation system is based on rather small ministries and large, independent and powerful agencies. The main governing mechanism for the government is the annual “Letter of Instruction” based on the passed budget. In this letter, the responsible line minister specifies the objectives and the reporting requirements. The letter is drafted with input from the Ministry of Finance and on the basis of a preceding dialogue with the agency.

The performance information is normally not used as a basis for negotiations on future funding. This is true for both the relationship between the line ministries and the Ministry of Finance’s budget department, and for the relationship between the line ministries and their subordinate agencies. The reasons are that the goals are diffuse and inexact, and that performance as reported by the agencies only reflects certain measurable dimensions of an agency’s activities. Nor is it possible – or desirable – to base agency performance on data compiled by that agency.

Experience from Sweden points at the following:

- Performance targets, indicators and appropriations are directed at agencies, not programmes. The link between tasks and organisations is thus vital if performance information is to be used.
- It is advisable to keep the system of targets, objectives and evaluations as simple as possible. This limits the risk of information overload for the line ministry, the Ministry of Finance and parliament, and strengthens the focus on the value added of the performance information.
- A performance system needs continual pruning, as there are always arguments for making it more detailed, but too much detail will detract from its usefulness.
- It is difficult but important to keep the information relevant for the political level.
- While performance information should be used selectively in the budget process, government performance needs a multi-year perspective.

\* Küchen, T. and P. Nordman (2008), “Performance Budgeting in Sweden”, *OECD Journal on Budgeting*, 8(1):49-59.

In a number of ways and in overall approach, the Polish performance-based budget structure resembles the French system more than the Swedish, especially with regards to the overall notion of covering the entire central government equally. Basically, the Polish tasks are equivalent to the French missions. All country systems, however, seek to develop a transparent budget structure that shows what the government’s main goals and targets are and help build an accountability framework. There are obviously substantial institutional differences between the three countries – e.g. the independence of the Swedish agencies

### Box 3. France's experience with performance management (LOLF: Loi organique relative aux lois de finances)

In August 2001, the French parliament adopted France's new organic budget law introducing the performance-based budget. The reform was planned to be phased in over a number of years, and the 2006 budget was the first to be fully prepared, adopted and enforced under the new PBB framework. A testing phase occurred in 2005. The government prepared objectives and indicators which were reviewed by various institutions (parliament, Court of Audit, Inspectorate General) leading to some modifications in the programme organisation. The French PBB reforms sought to give greater budgetary authority to parliament, to modernise public financial management, and to increase transparency. Prior to the reform, parliament debated only those expenditures that had not appeared in the budget before (around 6%). Under the present PBB system, parliament debates the entire budget, votes to approve "missions", and may reallocate appropriations between programmes within a mission.

The French PBB structure is broken down into three classifications:

- Missions (currently 34): missions correspond to major government policies. A mission may fall under one or several ministries. This is similar to the current Polish structure.
- Programmes (currently 133): individual programmes fall under a single ministry. They are tied to strategic plans with explicit performance goals and indicators. On average, there are around five goals per programme and two indicators per goal, although there has been some adjustment downwards of goals and indicators over the years. There are three main types of indicators related to i) socio-economic effectiveness, ii) quality of services provided, and iii) management efficiency.
- Actions (currently 580): specify how funds are to be spent.

Each programme's strategy and objectives are defined by the relevant minister with the help of the programme manager. The strategy, indicators and objectives are presented to parliament in the annual performance plan appended to budget bills. The French parliament conducted an evaluation of the new performance management system in 2009.\* Among the key findings and recommendations:

- Indicators need to be more reliable and result from better information systems, involving less manually collected data.
- Comparison between indicators should be enhanced through the development of more standardised indicators for comparable programmes.
- A better ownership of indicators and objectives should be sought.
- Often the performance-based approach is disconnected from operational management.
- There should be a stronger relationship between performance measurement and the budgetary process. The relationship should not be automatic, but performance should be part of the process.
- The involvement of parliament is necessary to maintain the momentum gained with performance-based budgeting.
- Managers have complained about complex procedures and burgeoning bureaucracy, in particular a significant lengthening of administrative channels and an increase in payment delays.

\* National Assembly (2009), "Rapport d'information déposé en application de l'article 145 du Règlement par la Commission des Finances, de l'Économie générale et du Plan relatif à la performance dans le budget de l'État", Paris, [www.assemblee-nationale.fr/13/rap-info/i1780.asp](http://www.assemblee-nationale.fr/13/rap-info/i1780.asp).

which is unique compared to most OECD countries. Sweden is also special as to the importance given to the Letter of Instruction from the government to the agency. The Swedish system is based on a continuous dialogue regarding goals and results, and the dialogue is both qualitative and quantitative in nature. Both the French and Swedish cases point to the fact that, while performance information is important for any government, the performance management system needs to be re-evaluated continuously to ensure that it continues to add value.

While the Polish system is not yet operational, it could perhaps be beneficial to look at ways of developing a dialogue process between the Prime Minister, the Minister of Finance, the line minister and his/her executive public finance sector entities as a supplement to the broad-based indicator system. Some elements are already visible in the newly proposed system where each minister picks certain key areas on which he/she wishes to focus in the coming year and then makes a report to the Prime Minister a year later. Obviously such key areas must fit with the national development plans, the medium-term strategy and the priorities of the Prime Minister and Council of Ministers. This procedure could provide the basis for setting up a dialogue between the Prime Minister/Minister of Finance on the one hand and the relevant line minister and his/her executive agencies on the other. The outcome of this dialogue would be a letter, or “contract”, where the coming year’s objectives are set.

### **2.3. Internal management**

A key issue is for budget systems to support the efficiency and internal management of government organisations. Based on the experience of a number of different Polish pilot agencies and ministries, the evidence is mixed. In one public finance sector entity that was interviewed, the management had difficulties in seeing the connection between the new PBB structure and the entity’s internal organisation and activities. In addition, the PBB was very general and more unclear than the traditional budget. Preparation, reporting, and information handling using the PBB was perceived as an extra bureaucratic burden rather than a support for management. The entity emphasised that a choice of systems had to be made so that the double work of two budget systems could come to an end.

In other ministries and agencies, such as in the field of education and defence, the management saw a clear link between the performance-based budget structure and the actual tasks and operations inside their organisations. Hence the work with the new structure had brought gains in terms of improved understanding and presentation of the work performed by the organisations, compared to the traditional budget structure. The Ministry of Education highlighted that the PBB introduced new useful information as well as a new way of thinking with regard to policy preparation and execution on the part of the senior management in the ministry.

The budget department of the Ministry of Finance has indicated that the performance-based budget currently adds value to the budget process in the form of transparency about activities, targets and purposes of various agencies. The performance-based budget has helped the budget department conduct better examinations of public spending than before. In addition, it was also highlighted that the traditional system is currently particularly useful for maintaining budget discipline.

The expectation of reformers is that the Polish performance system will have to be in place for a number of years before it will provide meaningful information for the budget

process and before it can be used to improve allocative efficiency. This expectation is aligned with experiences from other countries which have encountered difficulties, even after years of work. In the meantime, the success of the Polish system will mainly rest on whether it will provide benefits to internal management. Agencies need to use the system and the indicators if they are to be worthwhile in the long term. In addition, indicators from other suppliers need to be used, such as those in statistical agencies and from research institutes, inspectorates and universities. The current methodological support provided by the Ministry of Finance to line ministries should be continued, as well as dialogue on how to calibrate the system so that budget holders have the best opportunities to harvest operational efficiency dividends.

#### **2.4. Expenditure control and IT system support**

The budget department is confident that it can maintain fairly strict discipline with the traditional structure. The department responsible for line ministries' spending is concerned that if the PBB were to become the only binding document, fiscal discipline and financial oversight would suffer. A concern with a transition to a new structure is that the Ministry of Finance will lose control and oversight in the process. The change from the traditional to the performance-based budget is perceived as radical in the sense that there is no direct link from the traditional appropriations of parts and sections to the new functions and tasks. The lack of a direct link is further complicated by the organisational cross-cuttings of the new system. There is a risk of double funding and lack of experience and clarity concerning new appropriations.

Apart from the vital problem of not having a clear one-to-one bridge from the traditional structure to the PBB structure, an element in understanding this scepticism is that the new performance-based budget structure does not include a level of economic classification – the paragraphs in the current traditional structure (see Table 1 above). The exclusion of this level reflects a trend in OECD countries where a number of countries have moved towards fewer input controls and more lump-sum budgeting under the heading “let managers manage”. There are certainly arguments for maintaining some input controls for selected items, but the argument is less strong for preserving other input specifications of the economic classification. It might be a good idea to introduce ministry-wide ring fencing of salaries, capital and transfers, so that no funds can be transferred between these categories. Salaries should be capped by the Ministry of Finance, in that there will be strong pressure to increase salaries in the public sector, but little countervailing market pressure. There are two main arguments for ring fencing capital expenditures: the technique is often used as a counter-cyclical tool, and thus needs to be visible; and there has been a tendency to under-invest in maintenance, because current expenditure is more pressing, leading to larger spending eventually. Transfers should be capped, in that the line ministry is in effect only a handler of payment where the expenditure level is exogenously given.

Directly linked to the question of budget discipline is the issue of IT system support. The lack of a functioning IT system in PBB format is a threat to spending control and budget discipline, as automated in-year spending information will not be available to finance and line ministries. The new performance-based budget structure is not underpinned by the current chart of accounts or the budget IT system, and the structure of a new chart of accounts and bookkeeping system has yet to be elaborated. This problem also impedes a clear transition from the old system to the new one. At present, budget holders have to develop their own solutions in order to translate the traditional budget structure into the performance-based



structure when preparing their financial plans and reports. The implication is that, in the preparation of the budget, numbers from the traditional budget structure need to be manually translated into the PBB structure through bridges and estimates developed by the individual budget holders. Some budget holders (*e.g.* the Ministry of National Education) have developed their own system enabling parallel bookkeeping, but these are exceptions. The accounting system is decentralised, and administrative units hold their own (different) accounting system software. Many of these systems cannot integrate a new chart of accounts or even adjust the current chart in a sufficient way. Clearly, without a reform of the accounting system, a transfer to the PBB is not possible. The issue of accounting system reform is thus a central concern.

In conclusion, the PBB structure classifies expenditures according to functions and tasks (programmes) in a hierarchical order. This new structure enables formulation of objectives and indicators which can be logically attached to each expenditure level. The purpose is to apply performance information to the budget process.

Since the PBB structure is classified according to functions and tasks, it cross-cuts the organisational structure which can cause co-ordination problems and suboptimal behaviour. Experience shows that the organisational units are still the basic hubs of funding, operation and accountability.

In time, performance-based budgeting should result in a marked improvement of internal management and increased efficiency and effectiveness. In the short term, however, the reform has caused extra burdens on ministries and agencies. It is important that the reform continues to focus on how the PBB can be of use to the management of agencies and line ministries to ensure their support and buy-in.

Finally, the PBB structure is not yet supported by a chart of accounts or an accounting system. This is a major challenge which should be solved if the new structure is to be used. Actual spending controls are not possible in the new system, so spending will have to rely on the traditional chart of accounts. In addition, there is no central budget structure “bridge” between the traditional budget and the PBB, so translations are performed manually by budget holders. This could cause concern about budget discipline.

### **2.5. The Multi-Year Financial Plan, spending reviews and performance information**

The Multi-Year Financial Plan (MYFP) is a new concept in the Polish budget process that was adopted by the Council of Ministers in 2010 (for the period 2010-13). The plan has a rolling four-year horizon and covers general fiscal policy, economic projections, revenue and expenditure estimates, budget balance and debt. The plan is updated yearly in light of budget changes and is approved by the Council of Ministers. The plan does not set binding top-down expenditure limits, but the Public Finance Act states that the deficit targets of the plan should be respected except in “justified cases”, in which an explanation must be given to parliament detailing the reasons for the exception. The plan is to be the basis for the preparation of the budget and is meant to support the Polish Convergence Plan that aims at reducing the deficit to 3% of GDP by the end of 2012 with a view to euro adoption in 2014 or 2015. This target seems realistic given the strong economic performance Poland has exhibited after the global financial crisis and in contrast to many of its neighbours.

The MYFP is a central element in the development of the PBB reform in Poland. The plan is prepared according to the new PBB structure covering the functions of the state along with the PBB objectives and related measures. The plan provides an additional platform

for presenting and reporting on performance information. Ministers must annually submit information about the implementation of the MYFP to the finance minister, including information about the extent of achievement of their objectives. This information is then submitted to the Council of Ministers and published. A number of countries have introduced medium-term expenditure frameworks and performance budgeting as part of the same type of reform package – for example, Austria, France and Korea (OECD, 2008).

As the MYFP was only introduced in 2010, there is limited evidence as to how it will actually influence budgeting. For now, expectations in the line ministries seem to be that the allocation among functions in the MYFP will only be indicative. The Swedish experience shows the importance of institutionalising a medium-term expenditure framework so that all actors are aware that the government is committed to it (see Box 4).

**Box 4. Medium-term expenditure framework and expenditure ceiling in Sweden**

In Sweden, the parliament sets an expenditure ceiling for the next three years at the same time as it decides the limit for total central government expenditure for the coming budget year. The ceiling applies to all expenditure in the central government budget as well as the old-age pension system; only interest on national debt is excluded. Importantly, the ceiling includes transfers and other mandatory expenditures. The expenditure ceiling is given in nominal terms and works on a rolling basis as proposed by the government.

The total expenditure ceiling contains a “budgeting margin” for unforeseen expenditures, and parliament has full discretion to revise the ceiling. These are elements of flexibility, but also elements which can undermine the function of the medium-term expenditure framework. Thus, the ceiling not only builds on realistic and reliable projections but also on the fact that parliament and the government are interested in actually restricting their own discretion over the annual budget process according to medium-term fiscal targets. In other words, the government and parliament have to be committed to medium-term objectives, which has been the case in Sweden where the medium-term fiscal targets and the expenditure ceiling have become highly institutionalised.

Constructing the MYFP in the PBB structure with PBB objectives and indicators shows the intention of utilising performance information in multi-year budgeting. Poland has some experience in this regard through the co-financing programmes with the EU.

It takes time for policy to fundamentally have outcome effects – *e.g.* to reduce crime, improve the qualifications of students, reduce the number of road deaths, and increase the environmental health of lakes and rivers. A multi-year perspective is thus necessary, and may also be supported better by the MYFP than by attaching targets to the annual budget. A multi-year strategy for a particular area requires performance data as well as cost information and organisational data. It could therefore be helpful to introduce reviews of spending areas or programmes using performance information. These reviews could be used to settle multi-year envelopes with clear performance targets to be reported and re-evaluated in, say, four years along the lines of the Australian “strategic reviews” as discussed in Box 5.

However, the current regulation in Poland does not provide the Ministry of Finance with a mandate to engage in spending reviews. New initiatives and programmes are scrutinised,

but the Ministry of Finance does not perform spending reviews on existing programmes or sectors. This situation is quite unusual compared to most OECD countries. The introduction of a spending review system would require improved analytic capacity in the Ministry of Finance as well as adjustments to the Public Finance Act. Moreover, budget holders must accept and co-operate if spending reviews are to be successful. With this in mind, it is suggested to introduce a system of spending reviews on a very limited scale, where areas or programmes are strategically selected a few at a time. The reviews should support the use of performance information in multi-year budgeting.

#### Box 5. **Strategic reviews in Australia**

Australia has been grappling with the optimal manner in which to systematically review existing programmes. The most common method during the last decade was the use of so-called “lapsing reviews” whereby programmes would sunset if not renewed by a decision of the government. While this method ensured that a review was done, such reviews became a mechanical and ineffective exercise which rarely resulted in any significant changes to the programmes, despite an abundance of reviews – there were 149 lapsing reviews between the 2004/05 and 2006/07 budgets.

A new system of strategic reviews was launched in 2007 as the lapsing reviews were being abolished. The strategic reviews aim to take a holistic look at major clusters of programmes. The objectives are programme appropriateness, efficiency and effectiveness, and making sure that the programmes are aligned with government priorities. The focus is not to achieve savings. The reviews are commissioned by the Strategic Budget Committee and/or the Expenditure Review Committee (both Cabinet committees) based on recommendations of the three central agencies (the Department of Finance, the Department of the Treasury, and the Department of the Prime Minister and Cabinet). Areas to be reviewed are decided on the basis of criteria such as government priority, growth rate of the programmes, and the time elapsed since they were last reviewed. It is envisaged that up to seven large and seven smaller reviews take place each year. The reviews generally originate in January or February and take 3-6 months to complete – i.e. so that their results will be known prior to the following year’s budget formulation. The review teams are based in the Department of Finance, and the reviews are undertaken independently of the agencies responsible for the programmes; outside expertise is often used. The reviews can be led by academics, business leaders, former senior public servants, or current senior public servants seconded for the purpose. Agencies being reviewed and related bodies are encouraged to second staff to work on the reviews. A special unit in the Department of Finance has been set up to co-ordinate and contribute to the reviews. Importantly, the desk officers in the Department of Finance who handle daily contact with the agencies are not directly involved, reducing the likelihood that agencies perceive the reviews as savings exercises.

Source: Blöndal et al (2008), “Budgeting in Australia”, *OECD Journal on Budgeting*, 8(2):133-196.

Given that the spending reviews would entail the setting of performance targets for a sector for a certain period, the reviews could fit with the new initiative already planned which introduces ministerial targets that are to be reported to the Prime Minister yearly. These targets could be linked to the Multi-Year Financial Plan. A source of inspiration, albeit on another scale, could be the British public service agreements (PSAs) based on spending reviews and binding medium-term envelopes for line ministries (see Box 6).

The MYFP would benefit from being more closely tied to the annual budget process, especially if expenditure levels in the out-years for the functions are meant to be binding. At the same time, expenditure levels expressed in the MYFP should not turn into “floors” in the form of minimum envelope rights for spending ministries.

Utilisation of the MYFP – in terms of preparing performance information and executing spending reviews to establish multi-year envelopes and targets – will require investments in Ministry of Finance capacity, carrying out of spending reviews in co-operation with budget holders, and a process for negotiating and agreeing on multi-year envelopes. The Ministry of Finance should focus on targeted areas where in-depth analyses will result in savings and increased outcomes/results.

#### **Box 6. Spending reviews and public service agreements in the United Kingdom**

Starting in 1998 in the United Kingdom, the comprehensive spending reviews involved in-depth reviews of departmental aims, objectives and spending plans for each department for a three-year period. The comprehensive spending reviews of the first decade focused on combining multi-year spending plans with policy outcome targets for the period. This gave birth to public service agreements (PSAs) which set measurable targets for the government’s objectives for public expenditure programmes. Each department had its own PSA (quasi-contract) negotiated with the Treasury to present the outcome delivered according to the funding level for a three-year period. Thus, the Treasury had a main role both in the development of the PSA performance framework and the departments’ actual PSAs, and in the spending review process directed at each department.

The PSAs were introduced as *ex post* measurement of output/outcomes in relation to expenditures, but also as an *ex ante* tool to motivate departments to direct operations to deliver the right results. However, it was also recognised that the PSA performance measures and target setting could not be applied to all government expenditure.

Later comprehensive spending reviews took a deeper approach, turning from allocating incremental increases in expenditure to performing a set of zero-based reviews of involved departments’ baseline expenditure. Departmental expenditures were analysed against the background of the government’s long-term objectives in order to assess the departments’ effectiveness in delivering and fitting expenditures to current priorities.

The 2010 spending review focused on establishing an encompassing framework for reducing the budget deficit involving budget reallocation, value for money and targeted savings. PSAs are also evolving from a top-down performance management system to “departmental business plans” which will provide information on performance and spending, including each department’s:

- vision and priorities to 2014-15;
- structural reform plan, including actions and deadlines for implementing reforms over the next two years; and
- contribution to transparency, including the key indicators against which it will publish data to show the cost and impact of public services and departmental activities. This section will be published for consultation to ensure that the government agrees the most relevant and robust indicators in time for the beginning of the spending review period in April 2011.

## 2.6. Objectives, indicators and targets and their role in budget preparation

Along with the introduction of the PBB, the Department for Public Finance Reform of the Ministry of Finance has developed a framework for how budget holders should work with objectives and indicators. Starting with the 22 functions (the highest level in the PBB structure), the ministry has led the process of selecting and defining the functions and setting overarching strategic objectives.

In addition to the development of the 22 functions (involving the Ministry of Regional Development, the Ministry of Finance and the Chancellery of the Prime Minister), the Chancellery of the Prime Minister is leading a reform of strategic planning. The aim is to amalgamate the many existing governmental strategies developed by various institutions into nine strategies covering the public sector. It will be possible to translate the expenses incurred in the 22 functions into these nine strategies. The strategies cover: innovation and effectiveness of the economy; transportation; human capital; social capital; environment and energy; an efficient state; regional development; national security; and rural areas, fishery and agriculture. The MYFP has been prepared in compliance with these nine strategies just as each task in the performance-based budget structure has been matched with a strategic field. Essentially this is a controlled top-down process of setting the overall strategies and objectives of the state, which the lower level objectives should reflect.

The role of the Ministry of Finance in the formulation of objectives at the lower levels of the budget structure has been more limited. The ministry has not been involved in the content, but has described the methodological approach. The objectives have been defined as:

- Strategic: set at the highest level and constituting tasks for the highest level of organisational management;
- Tactical: set at a middle level and related to sub-tasks for managers of the middle organisational level;
- Operational: set at the lowest level and usually formulated at the level of actions for managers at the lowest organisational level.

Hence, the objectives as well as related indicators and targets are strictly ordered according to the new PBB structure. For each task, budget holders must choose one objective/indicator, and for each sub-task a maximum of two are allowed. The result might be more than 1 000 objectives, which is not uncommon (as seen in the targets in Table 2) but still on the high side. The Ministry of Finance envisages a gradual reduction of this number.

Table 2. Number of performance targets in selected OECD countries

Country	Number of targets
United States	3 700
Slovak Republic	1 641
Korea	1 033
France, Japan and New Zealand	500-600
Sweden	48

Source: OECD Budget Practices and Procedures Database, [www.oecd.org/gov/budget/database](http://www.oecd.org/gov/budget/database).

### 2.6.1. Formulation of objectives, indicators and targets

The performance reform has introduced a substantial amount of performance information in the budget documents (the annual budget, the MYFP, and the reports on execution).

The Ministry of Finance collects performance plans covering the budget year and the two subsequent years from all budget holders (of budget parts). The information collected is presented in both the annual performance-based budget and in the MYFP. Performance information in the MYFP is only presented on the level of functions of the state (with targets and measures for each target), whereas the budget bill presents performance information for tasks and sub-tasks within the functions. The performance plans entail objectives, indicators and targets defined by the budget holders. Targets are annual: expected values (results) are stated for the coming budget year and two subsequent years. The Ministry of Finance has a co-ordinating and advisory role and does not impose the use of a certain indicator or target upon budget holders.

Instead, the ministry has established a database of indicators to support and increase the quality of indicator formulation. The indicators in the database were prepared for the Ministry of Finance by external experts in consultation with the budget holders. The use of the indicators in the database is not mandatory, although it would seem that many agencies do use them.

The Ministry of Finance does not have a powerful role in setting targets, which is in line with practice in many OECD countries. Instead the focus is on letting the line ministries and agencies choose what they wish to be held accountable for. However, there is an issue regarding the capacity of line ministries and agencies for handling this task, and the evidence gathered suggests that this is still a concern.

### 2.6.2. Quality of objectives, indicators and targets

The indicators and targets currently in place vary considerably across areas. One example is the Polish Agency for Enterprise Development (PAED). The entity has tasks within four different functions; the related tasks, sub-tasks and actions, and their indicators and targets, are shown in Table 3. Most of the indicators measure activity (*e.g.* “number of implemented projects” or “number of promotional activities carried out”) but do not focus on the output, outcomes or quality of the activities. As the principals (*e.g.* the minister) are seldom interested in the specific internal activity of agencies, these types of indicators are not very useful, but should instead focus on outputs and later outcomes.

The Ministry of Interior and Administration is another example with both activity targets and outcome targets (*e.g.* “number of traffic accidents with fatal outcome” for the sub-task “Securing the operations of traffic service”; see Table 4). Here the indicator for “Securing the citizens’ safety” shows the possibilities for setting outcome targets (number of crimes registered) within areas where measurement is already more common. This is supplemented by an additional indicator measuring public perception of safety. In general, this type of information on the effects of the ministry’s operations is more relevant for decision makers whereas it may be less relevant for the budget process. Moreover, the outcome indicators are based on the assumption that there is a causal relationship between the entity’s activities and these outcomes, which may not always be the case. These issues are not solvable as such, and all countries need to negotiate them.

Outcome and output indicators are better suited than activity indicators to inform the budget. But for a purely mechanical relationship between results and funding in terms of, for example, “taximeter” budgeting (see the example from Denmark in section 2.6.3), the indicators will have to be developed.

The head of the PAED explained that finding and selecting relevant objectives and indicators had been a difficult task. “Due to the nature of activities carried out by the PAED, indicators relating to the whole PAED operational plan were assigned to individual tasks in the performance budget.” In other words, aggregate – but not necessarily relevant – indicators have been chosen in order to cover all parts of the entity’s operations and to translate the agency’s operational plan into the performance system.

In contrast, the Ministry of National Education perceived the process of developing indicators and targets as a contribution to internal management, giving clear targets to work towards as well as the possibility to present what the ministry intends to achieve for taxpayers’ money. Both the process and the results of working with performance information have varied across agencies.

**Table 3. Examples of objectives, indicators and target values for the Polish Agency for Enterprise Development (PAED)**

Tasks/sub-tasks	Objectives	Indicators	Base value	Value in 2011	Value in 2012	Value in 2013
6.1.2. Increase the competitiveness of the economy	Increasing the share of enterprises conducting innovative activity	Number of implemented projects supporting innovation	1 640	3 395	3 556	2 490
6.1.3. Create conditions for increasing the innovativeness of enterprises	Providing stable and development-friendly conditions for the functioning of enterprises	Number of enterprises, etc., which benefitted from advisory, training, information and financial services offered by business environment institutions supporting the development of entrepreneurship	247 680	229 449	253 857	246 917
6.1.3.1 Create conditions for the functioning of enterprises	Adjusting the structure of personnel to the needs of a modern economy	Number of persons who received training, a diploma, etc.	56 090	198 285	78 780	37 322
15.4. Support the adaptability of enterprises	International promotion of an appropriate image of the Republic of Poland	Number of implemented projects	474	1 467	1 911	1 509
15.4.1. Develop the international image of the Republic of Poland	Strengthening the positive image of Poland abroad	Number of promotional activities carried out	6	12	11	8
15.4.1.1. Promote the country	Creating favourable conditions for conducting business activity abroad by Polish traders	Number of assessed documents related to the development of economic policy	24	20	20	20
15.4.1.2 Co-develop economic policy and a common trade policy of the European Union which take account of Poland’s interests	Increasing the number of foreign co-operative links of Polish enterprises	Number of enterprises granted support	2 092	2 501	2 800	146
17.1. Intensify the exchange of products, services and capital	Improving the competitiveness of the regions, as well as the socio-economic and spatial cohesion	Number of implemented projects	69	122	88	151
17.1.3. Support regional development of the state	Speeding up the socio-economic development of eastern Poland’s voivodeships	Number of implemented (concluded) projects	1	36	27	30

Table 4. **Function 2–Internal security and public order**

Function	Responsible body	Part	Goal	Indicator			Predicted budget expenses in 2011 (PLN thousands)
				Name	Base value	Value in 2011	
2.1: Protection of citizens and maintaining of public order	Ministry of Interior and Administration	42	Securing citizens' safety	Indicator of the dynamics of the crimes in general terms (including the traffic regulation offences); as number of crimes registered in the current year to the number of crimes registered in 2008 x 100	100%	Dynamics < 100% in comparison to 2008	5 443 071
	Agency for Internal Security	57	Securing citizens' safety	Current monitoring: logical value YES/NO	YES	YES	491 916
	Voivodeship governors	85	Securing citizens' safety				12
2.1.1: Securing the state's internal security	Ministry of Interior and Administration	42	Improving internal security	Number of participants in basic training	8 702	5 000	31 975
	Agency for Internal Security	57	Improving internal security	Current monitoring: logical value YES/NO	YES	YES	491 916
	Voivodeship governors	85					12
2.1.2: Securing the safety of the most important persons, facilities and equipment in the country	Ministry of Interior and Administration	42	Improving safety connected with protection of persons and facilities vital for the country	Logical value YES/NO	YES	YES	177 468
2.1.3: Securing the operations of the prevention service	Ministry of Interior and Administration	42	Limiting the number of crimes	Indicator of the dynamics of the crimes especially in the categories of theft, theft with burglary, fights or physical assault; as number of crimes registered in the current year to the number of crimes registered in 2008	100%	Dynamics < 100% in comparison to 2008	4 502 957
2.1.4: Securing the operations of the traffic service	Ministry of Interior and Administration	42	Improving traffic safety	Number of traffic accidents with fatal outcome	4 862	Dynamics < 100% in comparison to 2008	675 620
2.1.5	...	...	...	...	...	...	...
...							
<b>TOTAL</b>							<b>14 085 755</b>

Source: Extract from the 2011 draft budget bill of Poland, performance-based budgeting framework.



Clearly, Poland is still in an early stage of using performance information. With time, budget holders will gain experience, targets will be formulated more precisely and better indicators will be developed. However, even if some improvements can be expected through the continuous effort of ministries and agencies, experience from other OECD countries that are further along demonstrates the difficulties in developing good targets and indicators. Moreover, some areas of the public sector do not lend themselves to this exercise.

### **2.6.3. Performance targets and use of performance information in Denmark**

In Denmark, line ministries and agencies have worked with performance targets for two decades. The performance information system is designed as “contracts” between the core ministry and its underlying agencies. The performance contract management system in Denmark contains three core elements: setting targets, developing contracts, and annual reporting. Its implementation was intended to serve several functions. First, it was expected that an increased focus on outputs would make it easier for political decision makers to prioritise among competing government objectives. Second, focusing on outputs would improve the quality and efficiency of government services. Finally, this results-based management was expected to improve operational efficiency by reducing information imbalances between ministries and agencies.

The performance contract system is very rarely used for budgeting purposes, but is rather a tool to promote dialogue and control flows between the core ministries and their agencies.

The system was last reviewed in 2009/10 when the Ministry of Finance adjusted its guidelines for the performance management framework. The review showed that:

- Agencies in some areas have developed very good targets and indicators to measure and present their operations; however, in many policy areas, agencies were still struggling with the formulation of strategic, relevant targets and related indicators.
- In a few policy areas, quantitative targets and indicators have been assessed as useless for both management and control purposes and have been replaced or supplemented by a dialogue of qualitative objectives between the principal and the agency. The idea of “one size fits all” does not apply.
- Outcome targets and their measurement are particularly difficult to formulate, and agencies cannot always remain fully responsible for an outcome target due to multiple causal relationships. Central support is necessary and has been increased.
- In some cases, the requirement to have annual targets and annual evaluations following the budget year hampers the ability to formulate multi-year targets which would be more relevant and useful for steering and internal management.
- The performance management process is separated from the aggregate budget process, and performance information is seldom used internally in the line ministries for budgeting. However, targets in the performance contracts often reflect agreements made during the preparation of the budget.
- The vast majority of ministries and agencies benefit from the performance management system which has increased information for decision makers. The system has also served to promote dialogue and clarify agencies’ objectives in the planning process while providing benchmarks for evaluation. As such, there are only a few examples of agencies

where the performance process is merely a symbolic exercise isolated from real strategic, operational and budgetary planning.

Besides the contract-based performance management system, Denmark has a formula for performance budgeting (the “taximeter” model) in a number of policy sectors. These include the Ministry of Education (vocational schools, upper secondary education), the Ministry of Science, Technology and Innovation (universities), the Ministry of Interior and Health (hospitals) and the Ministry of Employment (the Public Pension Agency). There are different methods in each sector (*e.g.* average vs. marginal budgeting), but in all cases the funding is based on annual statements of activity levels (actual number of units performed) and previously agreed unit prices along with quality requirements.

One example is the appropriation model from the Ministry of Education. Within the taximeter system, grants to schools are linked with a school’s direct results, which are measured in terms of the annual number of full-time students or student full-time equivalents. The rate system that is applied at medium-level higher education institutions is structured around three basic rates: a teaching taximeter, a building and maintenance taximeter, and a collective expenses taximeter.

The majority of the educational programmes are distributed and placed in rate groups with common rates, which makes it possible to compare the different programmes’ financial situations. The placement in these groupings should be justified by actual differences in the demands placed on the programmes and in the teaching and organisational formats.

In light of the Danish case, the uniform structure of the Polish performance system could potentially be relaxed as the system matures. Some government areas are more suitable for performance budgeting than others, and a larger differentiation may be beneficial for the Polish system.

The main focus of the Polish reform – as it is stated by the Ministry of Finance – is directed at collecting and presenting aggregate indicators and targets to be available for future central budget decision making. However, the experience from Denmark points to increased operational efficiency in agencies as a possible benefit of performance management. Reformers in Poland – both at this stage where performance information is less integrated in the budget process, but also after 2013 – may wish to focus more attention on this area. Currently, budget holders must elaborate a plan to attain the performance targets. This exercise forces budget holders to integrate day-to-day operational management and planning with the performance system. One way to support the reform’s improvement of internal management in the agencies and other budget entities could be an increased focus on follow-up and evaluation. The reporting on performance results is currently a part of this follow-up, but there is not necessarily a counterpart (*e.g.* the line ministry, Chancellery of the Prime Minister, Ministry of Finance) giving feedback on the information reported. Introducing a systematic use of performance dialogues would add value to the system. This is discussed further in Section 4 on budget execution.

## 2.7. Conclusions regarding budget preparation

The PBB structure for the 22 state functions and the nine national development plans is helpful for the development of good performance objectives at lower levels of the state administration. The process of top-down imposed objectives combined with bottom-up input from budget holders provides a useful framework and supports subsequent refining of objectives and indicators. A number of initiatives would increase the value of the PBB in the short to medium term:

- Consider selecting the areas most suited for performance budgeting and develop indicators and targets further in these areas, while at the same time relaxing requirements in other areas where the benefits are less apparent.
- Limit different organisations sharing the same programmes. In the longer term, align the new performance-based budget structure and the organisational structure of government.
- Focus on the operational efficiency of agencies. Support from the Ministry of Finance in terms of standards for preparation and reporting should continue, with the aim of ensuring that the PBB adds concrete value to the work of budget holders at the implementation level.
- Increase the use of output and outcome indicators, rather than activity indicators. The type of indicators should be chosen according to the policy area and purpose of the performance information. It is noted that the use of activity indicators is planned to be gradually limited.
- Introduce multi-year agreements connected to the Multi-Year Financial Plan (MYFP) as a way to align budgeting and target setting while preventing overload in the annual budget process. In many areas, relevant outcome and output targets can only be reached within the medium term.
- Introduce spending reviews within specific expenditure areas to support the performance budgeting process. The reviews should be the basis for the multi-year agreements. Sufficient capacity in the Ministry of Finance must be made available, and the relevant regulation allowing reviews must be put in place. These actions are currently being discussed in the Ministry of Finance.
- Connect the new performance agreement system (between the Chancellery of the Prime Minister and each spending ministry) to the MYFP, thus improving conditions for formulating outcome targets and for linking agreements to budgets.

### 3. Budget approval

#### Box 7. The Polish parliament

The Polish parliament is bicameral. The Sejm (lower house) is composed of 460 deputies elected for a four-year term by proportional representation. There are thresholds for the allocation of parliamentary seats: 5% of the total votes cast for a party list and 8% for a coalition list, although national minorities' lists are exempt from the threshold requirements. Individual parties normally do not manage to gain power alone and therefore work with other parties to form coalition governments. With some exceptions, members of the government are typically chosen from a majority coalition in the lower house of parliament. The Senate (upper house) has 100 members who are directly elected, also for a four-year term. As Senate elections are not proportional, the party that receives the most votes is more likely to control a majority of seats. Both houses are involved in the budget process but the Sejm has primacy and can overrule the Senate.

Committees play a vital role in the activities of the parliament, particularly in regards to its oversight function. The composition of committees is determined by the Sejm and reflects the political composition of that house. The Standing Orders of the Sejm define committee activities and oblige all ministers and other state officials to supply information at the request of a committee presidium and to participate in committee meetings on matters falling within the scope of their activity. Committees may also invite outside experts to give evidence.

#### 3.1. Parliament and the performance-based budget

Since 2008, the parliament has received a performance-based version of the budget as part of the justification to the traditional budget. As such, the PBB has been more of an informational or supporting document. This situation will change in 2013 when the PBB becomes a legally binding part of the budget law, but the overall parliamentary process for approving the budget will remain the same. Given that the traditional budget will remain in place (currently for an unspecified amount of time), it remains to be seen whether the new status of the PBB will lead to greater interest, debate and ownership by parliament. Despite intensive debate around the new Public Finance Act, parliamentarians generally have yet to take a strong interest in the PBB. Naturally, there has been more interest at the level of the Public Finances Committee and its subcommittees, including extensive discussions on the implementation of the PBB. This situation corroborates the opinions of the Ministry of Finance and the Supreme Audit Office (NIK) that, while the PBB so far has not been particularly popular within parliament, there is support for the idea of performance-based budgeting more generally. There may be several reasons. For example, MPs have a better understanding of the traditional budget structure (and input controls) and may lack the requisite knowledge and capacity to fully understand the PBB, particularly in terms of how to use the PBB process to obtain resources for their constituencies. Having to examine both the traditional and performance-based budgets also increases the already heavy workloads of MPs, and some may choose to only focus on the traditional budget to maximise their time.

Performance budgeting initiatives are often justified as improving accountability to the legislature and, as was the case in France, may even be instituted in response to legislative demands. In practice, however, many parliaments that have experience with performance-based budgeting have ignored, been reluctant to use, or had difficulties using performance information. In some cases, reforms have engendered a certain amount of resistance to the PBB within parliaments. This problem highlights the importance of engaging the legislature early in the process, and of thinking strategically about what information is most useful to the legislature in its budgetary deliberations and decisions. Legislators need an incentive to use performance information, and a large quantity of performance information may make it difficult for decision makers to quickly identify the most relevant information.

In the United Kingdom, parliament's experience with public service agreements (PSAs) sheds light on the potential difficulties of getting parliament to respond to high-level performance reporting. Previous governments committed to reporting performance information to parliament on a twice-yearly basis. As part of a modernisation process within the House of Commons, it was decided that departmental select committees should examine the departments' public service agreements, the associated targets and the statistical measures employed, and report if appropriate. Nevertheless, a study of parliamentary select committees concluded that "PSAs are not scrutinised broadly (only around one-fifth get any coverage) and of those that do get mentioned they are mostly tangential or a relatively small part of reports" (Johnson and Talbot, 2008, p. 123). Evidence from relevant cross-cutting select committees (the Public Accounts Committee, the Treasury Select Committee and the Public Administration Select Committee) was also mixed, although the latter two were more proactive in producing critical reports and recommendations (most of which were rejected by the government). The study went on to suggest that parliamentarians tended towards more traditional scrutiny approaches, and that "both formal and informal institutional restraints are very powerful breaks on change, although some incremental change does appear to be happening" (Johnson and Talbot, 2008, p. 128).

Sweden provides an interesting approach to improving the performance dialogue between the government and parliament. An informal working group of approximately ten civil servants from the Ministry of Finance and parliament's Committee on Finance was set up in 2000 and met over a period of several years. At times, when they were discussing specific budget areas relevant to them, representatives from various line ministries and parliamentary sectoral committees also participated in the group's discussions, thus ensuring that the group's advice and conclusions were available to a broader audience. The frequency of meetings throughout each year varied, with a greater number of meetings occurring after the formal decision on the budget was taken in parliament and before the preparatory work for the next budget bill started in the government. Members of the working group wrote memos and used existing examples of government performance information and committee responses as a basis for the group's discussions. While not binding, conclusions from these discussions were often included by the relevant ministries in subsequent budget bills as proposals or guidelines. The group served as a catalyst, spreading good ideas to governmental and parliamentary actors by identifying the types of performance information most useful to parliament in its deliberations on the budget, as well as how and when such information should be presented. In doing so, the group highlighted examples of best practice and brought them to the attention of the Ministry of Finance and line ministries where appropriate.

In Poland, the Department for Public Finance Reform in the Ministry of Finance is taking steps in the right direction. The department has increased outreach to MPs – for example, writing on performance budgeting in a special issue of the parliamentary newsletter which was distributed to all MPs in July 2010 – and is planning a training seminar.

#### **Box 8. Parliament and the new Public Finance Act of Poland**

The governmental proposal for the new Public Finance Act was presented in the Sejm in August 2008. The act was sent for more in-depth scrutiny to the Public Finances Committee which referred it to its Permanent Subcommittee for Budget Control. The subcommittee alone held 25 meetings on the new Public Finance Act between November 2008 and June 2009. On 23 June 2009, the subcommittee submitted a report on the Public Finance Act to the Public Finances Committee. Implementation of the PBB framework was not questioned in the report, indicating general acceptance of the reform. Moreover, two opinions prepared by the parliamentary Bureau of Research (BAS) supported the idea of the PBB in the act, stating that “it will not only increase the transparency of governmental activities (at national and local level) but it will also be an important evaluation tool, especially in multi-year programmes”. During the subsequent plenary debate on the Public Finance Act on 14 July 2009, MPs from all political parties outlined their viewpoints on the PBB. The chair of the Public Finances Committee spoke in favour of PBB, noting that it would allow Poland to use modern methods of public financial management as well as potentially making the budget bill clearer and more transparent. There was general support for the PBB, although several parliamentarians raised questions on the comprehensiveness of the PBB and the development of tasks and indicators. The act was adopted by the Sejm by 287 in favour, 33 against, and 114 abstaining on 27 August 2009 after the Senate submitted its amendments.

### **3.2. Legal framework**

The Constitution of the Republic of Poland, the new 2009 Public Finance Act, and the Standing Orders of parliament regulate the fundamental aspects of the parliamentary budget process. Article 222 of the Constitution requires the Council of Ministers to submit to the Sejm a draft budget for the next year no later than three months before the commencement of the fiscal year. Typically the draft is submitted by 30 September, although in exceptional instances it may be submitted later.<sup>7</sup> This timing is in accordance with OECD best practices for budget transparency.<sup>8</sup> Currently the performance-based budget is submitted as part of the justification to the traditional budget, although this will change in 2013 when the PBB becomes legally binding.

Parliament is not consulted in the preparation of the national budget and does not hold a pre-budget debate.<sup>9</sup> The government has the monopoly of legislative initiative with regard to the budget, public debt and state guarantee bills, but the legislature nonetheless plays a crucial role in scrutinising, amending (within deficit limits proposed by the Council of Ministers) and approving the budget, as well as overseeing its implementation. Outside of the main budget process, tax and spending legislation<sup>10</sup> and private members’ bills with financial implications may be submitted by parliament and are not uncommon.<sup>11</sup>

### Box 9. Key oversight tools of the Polish parliament

- Hearing in plenary sitting
- Committee hearing
- Commission of inquiry
- Oral and written questions (oral questions are answered directly during the sitting and written questions must be answered within 21 days of receipt)
- Interpellations (answered within 21 days of receipt)
- Supreme Audit Office (appointed by the Sejm with the consent of the Senate, obliged to report to parliament)
- Ombudsman (appointed by the Sejm with the consent of the Senate, obliged to report to parliament)

### 3.3. Parliamentary approval process

Following the introduction of the executive's budget proposal, MPs are given roughly seven days to acquaint themselves with the budget (Rules of Procedure, Article 37, paragraph 4) followed by a one-day plenary debate on overall budget policy (or first reading). The draft budget is then referred to the committees. The main committee charged with budget scrutiny in the Sejm is the Public Finances Committee, typically chaired by a member of the ruling party for the duration of the term<sup>12</sup> with deputy chairs drawn from the largest political parties represented in the Sejm including those in the opposition. The Public Finances Committee has around 50 members and is supported by five staff. The corresponding committee in the Senate is the Budget and Public Finance Committee which is comprised of around eight members and supported by two staff.<sup>13</sup>

Table 5. Parliamentary budget approval timetable

End September	Presentation of the budget.
Early October	First reading and referral to the Public Finances Committee and other relevant standing committees.
End October	Standing committees send their opinions to the Public Finances Committee.
Mid November	The Public Finances Committee issues a first report; second reading.
Second half of December	Third reading and approval of the budget; budget sent to the Senate for review.
Third week of January	The Sejm reviews and accepts or rejects the Senate's amendments and sends the budget bill to the President.

The Public Finances Committee examines the bill and produces a first report, taking into account the views, proposals, and suggested amendments of the other standing committees. It is now common practice for ministries to send materials which contain performance elements to these standing committees. This step is followed by a second reading where MPs may propose amendments to the bill before again referring it to the Public Finances Committee which produces a second report.<sup>14</sup> The third reading and approval of the whole budget bill typically take place in the third week of December.

After approving a bill in the third reading in the House, it is transferred to the Senate. The Senate cannot reject the budget approved by the Sejm (Article 233 of the Constitution), but it can adopt it as is or propose amendments. The Senate must state its position within 20 days following receipt of the budget. In a similar process to that of the Sejm, the Marshal

(Speaker) of the Senate refers the budget statute to the Senate standing committees. These committees, having considered the appropriate parts of the budget, transmit their opinions to the Budget and Public Finance Committee which prepares the draft for the Senate resolution. The Senate resolution is then sent back to the Sejm for consideration. The Sejm has prerogatives over the Senate and can choose to either overrule the Senate's proposed modifications (by an absolute majority vote) or include the Senate amendments in the budget. The Marshal (Speaker) of the Sejm then sends the bill to the President for signature.

**Box 10. Biuro Analiz Sejmowych (BAS), the Bureau of Research in the Chancellery of the Sejm**

In order to effectively carry out their budgetary oversight role, parliamentarians everywhere require access to timely, up-to-date, accurate and well-researched information. This includes information from the government (which tends to have a much higher capacity than parliament in terms of both financial and human resources) as well as information from independent sources such as parliamentary budget offices. The Polish parliament has a well-developed research service including a special division for budgetary research established in 1991. Poland thus follows a growing trend within OECD countries: in less than a decade, the number of specialised budget research organisations serving legislatures has almost doubled.

At present, the BAS is composed of 88 staff within 10 units, including the Department of Social and Economic Research (with around 20 staff in total) within which there is a Group for Financial and State Budget Research (with seven staff, two of whom are tax experts). This group deals with matters of public finance, among which: the state budget (including the PBB) and the budgetary law; taxes and the tax law; banking law; foreign exchange law; financial management of special-purpose funds; discipline of public finance; and administration of public finance.

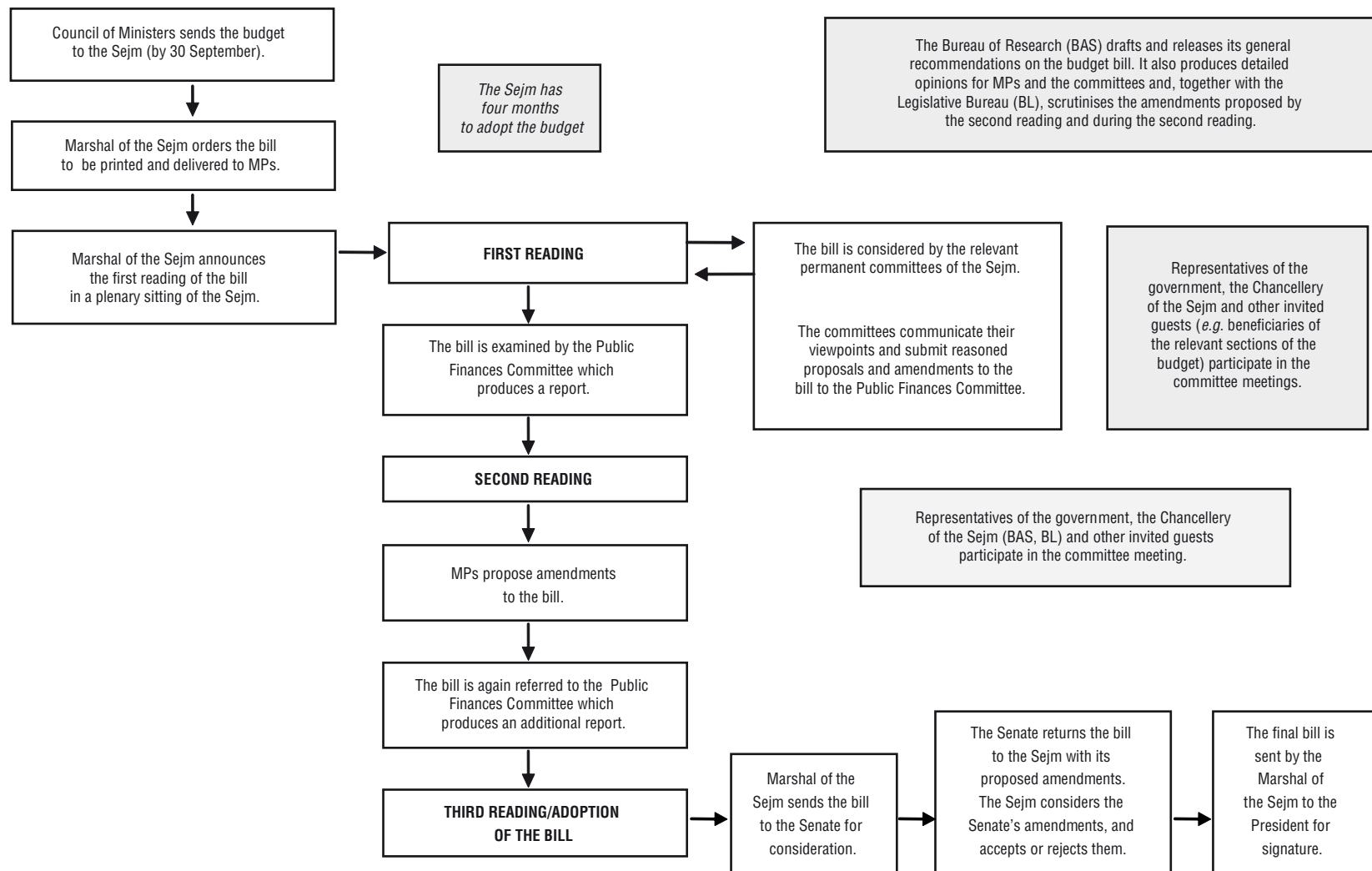
The BAS and the group provide a broad range of services to the Sejm (committees, parliamentary club members, and individual MPs), such as:

- Analysing materials submitted by the government (the draft budget and report on the implementation of the budget), by the Supreme Audit Office, by the National Bank of Poland and by the Central Statistical Office.
- Preparing written opinions on the textual part of a budget bill, on individual parts of the budget, and on the macroeconomic and monetary policy targets.
- Participating in all sittings of the committees and subcommittees during the period of the adoption of the budget.
- Formulating deputies' proposals for amendments to the budget and analysing the financial consequences of the proposed amendments.
- Responding to other requests made by committees and deputies concerning the budget, finances, monetary policy, the taxation system and the banking system. It should be noted that the BAS completes more than 300 written requests in this area each year.
- Organising seminars on various issues in public finance.

If necessary, the BAS can commission outside experts. Experts may be called upon to: present written opinions on a number of subjects, prepare motions to be voted on during the committee and plenary sittings of the Sejm, and assist in the organisation of seminars on various issues in public finance, including – at the beginning of each term of the Sejm – special training for newly elected deputies on the budget and on the procedures for its adoption.



Figure 1. Simplified budget adoption procedure in the Sejm



The President signs the budget (or interim budget) submitted by the Marshal of the Sejm within seven days of receipt, and orders its promulgation in the *Journal of Laws*. While the President has the power to veto other legislation, he/she does not have the power to veto the budget. According to Article 219, paragraph 4 of the Constitution, if a state budget (or interim budget) has not come into force on the day of the start of the fiscal year, the Council of Ministers shall manage state finances pursuant to the draft budget. In addition, if after four months from the day of submission of a draft budget to the Sejm, it has not been adopted or presented to the President for signature, the President may, after 14 days, order the shortening of the parliament's term of office although he/she is not obliged to do so. However, timely approval is the norm.

### 3.4. The impact of parliament

The Polish parliament enjoys wide amendment powers which it uses in practice. Regarding the budget, the parliament can propose unlimited amendments provided it does not change the total deficit/surplus proposed by the executive (the number of amendments from year to year can vary widely, although it is typical to have several hundred amendments proposed during the parliamentary budget process). Unlike many Westminster system parliaments, amendments and the vote on the budget are not seen as a vote of confidence in the government. Table 6 shows the numbers of amendments proposed by both houses and finally adopted in 2008 (the 2009 budget bill) and 2009 (the 2010 budget bill); both bills included performance information in the *Justification to the Budget* documents.<sup>15</sup> The data in Table 7 show that the effects of the amendments submitted and approved by the parliament on the overall budget revenues and spending are minimal. However, change to the various parts of the budget may be more substantial.<sup>16</sup> It is unclear how the amendment procedure will work in the future when both the traditional budget and the performance-based budget are legally binding. However, as long as the traditional budget continues, it is likely that amendments to it will be translated to the PBB, again increasing the workload of parliament.

Table 6. **Parliamentary amendments to the budget bill in 2008 and 2009**

	2009 budget bill	2010 budget bill
Sejm (lower house)		
Amendments submitted	411	194
Amendments adopted	37	51
Senate (upper house)		
Amendments submitted	251	16
Amendments adopted by the Senate	27	16
Senate's amendments adopted by the Sejm	23	16
Total Sejm and Senate combined		
Amendments submitted	662	210
Amendments adopted	60	67

Sources: The Bureau of Research of the Sejm (BAS) and the Senate committees, Poland.

Table 7. **Impact of parliamentary amendments (PLN thousands)**

Specification	Draft of the budget bill for 2009	The budget bill for 2009 passed by the Sejm and published in the <i>Journal of Laws</i>	Per cent change	Draft of the budget bill for 2010	The budget bill for 2010 passed by the Sejm and published in the <i>Journal of Laws</i>	Per cent change
Revenue	303 544 670	303 034 805	0.2	248 983 601	249 006 601	0.0
Expenditure	321 744 670	321 221 112	0.2	301 197 817	301 220 817	0.0
Including <i>inter alia</i> :						
Part 01: Chancellery of the President	188 999	159 779	15.5	162 485	158 485	2.5
Part 02: Chancellery of the Sejm	420 085	382 762	8.9	404 960	395 323	2.4
Part 03: Chancellery of the Senate	162 481	154 915	4.7	163 088	161 970	0.7
Part 09: National Broadcasting Council	19 379	14 682	24.2	19 742	15 742	20.3
Part 33: Development of rural areas	10 116 810	10 316 810	2.0	4 628 065	4 479 065	3.2
Part 46: Health	4 694 696	4 694 696	0.0	3 452 421	3 482 702	0.9
Part 83: Special-purpose reserves	34 084 558	34 473 346	1.1	18 308 768	18 347 076	0.2

Source: The Bureau of Research of the Sejm (BAS), Poland.

### 3.5. Conclusions regarding budget approval

The Polish parliament's role in the budget process is clear and well developed. According to outside observers, budget oversight by Poland's legislature is generally strong. There is adequate time to examine the draft budget, in line with OECD best practices for budget transparency. The parliament has a strong independent analytic capacity in the BAS and its Group for Financial and State Budget Research more particularly. The Supreme Audit Office (NIK) is also an important partner in terms of analysing and providing information on performance results. The PBB adds new dimensions to the budget process and can be expected to increase the workload of parliament given that it is presented alongside the traditional budget.

As Poland makes the transition to a legally binding PBB, the Ministry of Finance should enhance its dialogue with parliament, particularly regarding how performance information is best presented to parliament, what types of performance information are most useful to parliament (*e.g.* which indicators are most relevant), and examples of good practice since the introduction of PBB in 2008. The ministry's Department for Public Finance Reform is taking steps in the right direction, with several recent initiatives to reach out to MPs, but the department should ensure that these efforts are more systematic and not merely *ad hoc*.

## 4. Budget execution

The ongoing reform process introducing performance budgeting elements in the Polish budget system has so far not influenced rules or practices in the execution of the annual budget apart from a few new elements being added to the in-year duties of the Ministry of Finance and budget holders. During the year, the finance minister exercises control over, among other things, "the effectiveness and efficiency of implementing the performance-based budget". The new performance-based budget is still not legally binding, but it is included in the *Justification to the Budget* and shows appropriations for tasks, objectives, indicators and targets that budget holders must take into account as part of budget execution. Until now, Ministry of Finance control of the implementation of the PBB referred to in the Public Finance Act is more related to a continuous dialogue about how to formulate the budget structure, objectives, and indicators than to systematic in-year monitoring of the content and results of these objectives, indicators, and targets.

For the traditional budget, execution reports are produced monthly, and the Ministry of Finance monitors the current accounts of large agencies.

A new element is that budget holders are obliged to “exercise surveillance and control over the effectiveness and efficiency of implementing performance-based plans on the basis of measures of execution of the objectives.” The intra-ministerial surveillance and control is still in an early phase. IT systems for systematic collection of indicator values, and clear process plans for how control should be exercised, are not yet in place. Nevertheless, the responsibility of budget holders to monitor and control their agents could become a central point in the future functioning of the performance-based budget system.

Systemising this element may establish a dialogue on objectives, operations and results. The dialogue can be useful for the units that execute the budget and plan operations (to achieve a clearer definition of expectations and goals for budget execution), as well as for budget holders (to achieve improved information and to be able to exercise not only financial but also performance control). As the monitoring, control and potential dialogue occur within a policy area, the professional and technical knowledge of that area is already in place, thus taking some of the pressure off of the Ministry of Finance as a controller.

From a budget allocation perspective, the decentralised monitoring and oversight may not necessarily improve general allocative efficiency among policy areas. However, as this section shows, budget holders of budget parts have relatively broad freedom to reallocate within budget parts. Thus, one way of utilising the performance information now being generated would be to enhance allocative efficiency within policy areas – in both the budget preparation phase and the execution phase. Under the precondition that the aggregate envelope will not be reduced by the Ministry of Finance (or the Council of Ministers), possibilities of internal reallocation within the envelope of a policy area could potentially lead to improvements in the reallocation from non-efficient to efficient programmes.

In addition to the new budget elements, some of the existing features in the budget execution phase are interesting and important for a well-functioning performance system. These features include the rules for the use of reserves, for internal transfers and for carry-overs.

#### **4.1. Use of reserves**

Poland’s annual budget contains a general reserve of a maximum of 0.2% of budget expenditures, as well as a number of special-purpose reserves. The special-purpose reserves can be used for various types of expenditures – for example, for expenditures not precisely divided into budget classifications during preparation of the budget bill.

Poland has four types of special-purpose reserves (two of which are not allowed to exceed 3% of budget expenditures). This leaves a considerable amount of specific budget allocation to the execution phase. The Minister of Finance allocates the special-purpose reserves in co-operation with other ministers, and the Council of Ministers also administers the general reserve.

While reserves are generally not conducive to maintaining budget discipline, they can be relevant in a performance context. From a performance budgeting perspective, reserves could cover not only new tasks as in the current system, but also changes in activities which need to be financially covered in an activity-based funding model. In suitable areas where the unit price of a product is calculable and variations in production are uncontrollable due to changes in demand, the use of reserves can be a way to fund activities within agencies.

In order to maintain budget discipline, an overall cap on activity-based budgeting funds should be maintained.

#### Box 11. **Activity-based budgeting in Denmark**

In Denmark, one example of how reserves can be used in a simple formula funding model is the processing of public pension applications from Danes living abroad. In addition to the basic appropriation in the budget act, the Agency for Pensions can draw on general reserves if the number of processed cases exceeds the fixed number covered by the basic appropriation. On the contrary, if the number of processed cases is below the number covered by the basic appropriation, the agency must return additional funding. The potential amount of extra funding is very limited in relation to the overall size of the reserve.

#### **4.2. Internal transfers**

Another flexible element in the Polish budget system is the rules for transfers during budget execution. Budget holders of budget parts are allowed to transfer expenditures between chapters and paragraphs within their relevant part and section of the state budget (Article 171 of the Public Finance Act). However, they cannot increase the expenditures planned for wages and for employees. Moreover, ministers administrating several budget parts can transfer expenditures between these parts within one section and chapter of the state budget. To do this, they must notify the Council of Ministers which may overrule the ministers' decisions.

The finance minister must be notified of transfers concerning property expenditures and transfers concerning building investments which require his/her approval. Likewise, transfers involving a reduction or an increase of property expenditures by an amount in excess of PLN 100 000 (approximately EUR 25 000) on a one-off basis require the approval of the finance minister.

Generally, both line ministries and the Ministry of Finance expressed satisfaction with the current transfer rules as allowing flexibility and an appropriate level of control. Following the implementation of the performance budgeting reform, the rules for transfers have to be settled for the performance-based budget. The logic of the current system would suggest that budget holders of a budget function could be allowed to transfer between tasks, sub-tasks and actions within that function. Moreover, ministers or budget holders could be allowed to transfer between functions if they were responsible for more than one function. A typical example would be a public finance sector entity with tasks contributing to several functions. If the latter rule is not applied, it would be impossible for the management of an entity or the accountable minister to reallocate funds within the entity because different units of the entity analytically are related to different functions.

However, applying these two transfer rules to the new performance-based budget structure could entail challenges. The first problem is that reallocation within a function would not take place in an optimal way because different tasks, sub-tasks and actions belong to different line entities. Basic organisational theory would suggest that funds could not be transferred out of entities if no principal can decide on it. This problem is inherent

to the cross-cutting nature of the new performance-based budget structure, and transfer rules cannot change that.

The challenge related to the second rule (transferring between functions) is the risk that ministers or budget holders may reallocate too much. If more ministries and separated organisational units are contributing to the same functions or tasks, sub-optimising may happen as entities hope to rely on the effort and funding of other entities while transferring resources to tasks that are more important for themselves. This risk would be amplified if entities are held strictly accountable for certain objectives and targets.

Nevertheless, the way the Polish performance-based budget structure has been defined – with objectives, indicators and targets for each task, sub-task and action – minimises this risk. Every level is held accountable, and it would also appear in the reporting if extra resources had been transferred to an area. However, appropriate monitoring systems will have to be put in place.

The Ministry of Finance should keep the transfer rules flexible. To ensure that gaming is not taking place, the ministry could collect and analyse data on transfers for a specific period to monitor the development.

#### **4.3. Carry-overs**

A final flexibility issue is the possibility to carry forward unused funds at the end of year. The current regulations state that the “amounts of state budget expenditures which have not been utilised shall expire at the end of the budget year.” After obtaining an opinion from the Sejm Public Finances Committee, the Council of Ministers may define an explicit list and new financial plan for expenditures which will not expire at the end of the budget year. However, a detailed description of their use and a deadline for their implementation are necessary. Moreover, they must be utilised at the latest by 31 March following the relevant budget year. In practice, very few unused funds are carried forward, and the system is very strict.

If appropriations in 2013 become more closely linked to performance, the strict rules and practices for carry-overs may be relaxed, particularly in areas where certain results are agreed for a multi-year period. It should be noted, however, that the traditional budget should still be expected to be dominant after 2013. It should then be reasonable to look at the use of appropriations in relation to the results for the agreed period and not just the single budget year. Also, for areas where activity and performance can be measured accurately, the possibility for carry-overs could be used as an incentive to increase efficiency in entities. If the same activity (and quality) levels are reached with the use of less resources, agencies’ ability to prioritise unused funds within their own area could be part of a reward system. Such a relaxation of the carry-over rules should be administrated by the Ministry of Finance, which may have to submit decisions to a hearing in the Council of Ministers.

#### **4.4. Conclusions regarding budget execution**

The current Polish system for reallocation seems to be sufficiently flexible and should be continued. The reserve system gives the government additional leeway during budget execution. Carry-over rules, on the other hand, are rather strict compared to most OECD countries. The PBB system introduces decentralised responsibility to budget holders for them to monitor agencies and units, which should improve both allocative and operational

efficiency over time. In order to harness the potential of the PBB in the budget execution phase, the Ministry of Finance should:

- Support budget holders in their tasks of monitoring and controlling performance by developing guidelines on appropriate controls that can be used by ministries and agencies.
- Consider relaxing the rules for carry-overs in order to support multi-year agreements or to act as an incentive for efficiency in agencies.
- For a certain period, collect and analyse data on in-year transfers in order to ensure that transfers are used appropriately in the new structure. (Poland should strive to keep the rules for in-year expenditure transfers as flexible as in the current system.)

## 5. Reporting, accounting and audit

### 5.1. Reporting and accounting

According to Article 41[4] of the new Public Finance Act, “the finance minister shall define, by ordinance, the types, forms, deadlines and methods for preparing reports on the execution of performance-based financial plans by state budgetary units, administrators of state special-purpose funds, executive agencies, budget institutions and state legal persons.” The Ministry of Finance provides monthly reports (with roughly a two-week lag), as well as quarterly, mid-year and annual reports. Currently only the annual report contains performance information, although the ministry has indicated that some performance information will likely be added to the quarterly and mid-year reports in the future. Figures are reported at the central government level, ministry level and chapter level. During the year, parliament scrutinises these reports through the Public Finances Committee.

The annual report on the implementation of the budget and the condition of the state debt is submitted to the Sejm and the Supreme Audit Office (NIK) by 31 May of the subsequent year (or within five months of the end of the fiscal year). As noted above, the annual report includes information on the execution of performance-based expenditures which, according to the 2009 Public Finance Act, should contain:

- a review of the implementation of the performance-based plan of expenditures, including the implementation of objectives set;
- a statement of expenditures planned and incurred for the implementation of tasks;
- a statement of expenditures planned and incurred for the implementation of sub-tasks; and
- a statement of planned and achieved values of measures of implementation of objectives (Article 182[6]).

Annual information about the implementation of the state’s Multi-Year Financial Plan, and the extent of execution of objectives, is also published. The Sejm must examine the report and, taking into consideration the opinion of the NIK, decide whether to pass a resolution to grant or refuse approval of the government’s accounts within 90 days of receipt (Article 226 of the Constitution). Refusal to approve the government’s accounts may lead to a vote of no confidence against the Council of Ministers, although this is not automatic.

### Box 12. **New management control and reporting in Poland**

Chapter 6 of the new Public Finance Act specifies management control and co-ordination of management control in public finance sector entities. Management control is defined as “a set of activities undertaken in order to ensure the implementation of objectives and tasks in an effective, economical, and timely manner compliant with the provisions of law”. Among other things, such control seeks to ensure the credibility of reports. The finance minister is required to publish a communication on management control standards for the public finance sector, compliant with international standards, in the Official Journal of the Finance Minister (Article 69[3]). The finance minister and the minister in charge of a department may also publish detailed guidelines on management control for the public finance sector and the department respectively. Each minister in charge of a department must draw up an action plan for the following year which includes “a specification of objectives within individual budget tasks” and “an indication of sub-tasks for achieving the objectives and measures specifying the extent of objective implementation and the planned values thereof”. Reports on the execution of these action plans must be submitted by the end of April along with a statement on the condition of management control for the preceding year (a specimen of which is defined by the finance minister by ordinance). The action plan, the report on the execution of the action plan and the statement on the condition of management control are all made publically available through the Public Information Bulletin. According to Article 71 of the Public Finance Act, the finance minister is responsible for co-ordinating management control in public sector finance entities through:

- propagating the standards referred to in Article 69[3];
- issuing guidelines;
- co-operating with domestic and foreign organisations; and
- co-operating with the auditing committees referred to in Article 288.

In principle, information is collected in good time so that it can be fed into the subsequent budget preparation process. However, as the performance indicators and targets have only been in place for a short time, their usefulness for decision making has been limited. The Ministry of Finance clearly intends to use the reporting on performance results to inform the budgetary decision-making process from 2013 onwards. Performance information should in time constitute an important factor on the basis of which allocative decisions can be taken.

The major challenge facing the Ministry of Finance and budget holders today is the need for a new chart of accounts for the PBB structure and an adequate IT infrastructure for PBB reporting and accounting. The current IT infrastructure does not support translation between reporting and accounting for the traditional budget and reporting and accounting for the PBB, and individual budget holders decide independently on how to keep records of performance-based expenditures. Several entities (for example, the Ministry of National Education) have developed their own system enabling parallel bookkeeping in which all accounting documents simultaneously describe both the traditional and the performance-based classifications. Other entities prepare their plans and reports on the basis of estimates. For many budget holders, this situation essentially means double reporting and an increased workload. Reporting and accounting are further complicated by the fact that, even for the traditional budget, there is no centralised accounting system. Budget



holders use a wide variety of systems, some of which have been tailor-made for them by small Polish firms. It is important to note that the Ministry of Finance reported significant improvement recently in the quality of data submitted for the purpose of preparing the annual report on the execution of performance-based expenditures, indicating that budget holders have improved their methods of collecting performance-based information.

The new Public Finance Act (Article 40[4.1]) obliges the Ministry of Finance to set the parameters for the new accounting system for the PBB. To address the issues raised above, the ministry hired outside experts to provide an in-depth analysis of the current situation, including a survey of budget holders in July 2010. The survey comprised 309 questions and had an 85% response rate (1 940 budget holders out of 2 283). The main findings and recommendations were presented to the Ministry of Finance in the form of a detailed report in September 2010.<sup>17</sup> The report highlighted the diversity of suppliers of accounting systems (around 150) and of types and versions of accounting systems (over 150), as well as licensing issues. In addition, the size of the various systems (number of records, users, etc.) varies greatly from one budget holder to another. Only 190 respondents were able to estimate the costs of adjusting their systems to service expenditure in the PBB format, and only 40% believed that they have the skills necessary to account in the PBB format. IT solutions will have to take into consideration the fact that some units will resist or have difficulty integrating into a single accounting system. Any centralised system will have to be tailored for both very large and very small budget holders, and the latter may not have the capacity to service expenditures in a very complex system (again, for some their accounting system is very simple, often serviced “by hand”).<sup>18</sup>

Three major options exist: i) the development of a totally new system solely for the PBB; ii) adjusting the current Ministry of Finance system that applies to the traditional budget (TREZOR system); and iii) adjusting the various systems used by budget holders. No decisions have been taken yet as to the options presented. As demonstrated by the French experience, the development of a totally new system would likely prove to be a complex and expensive undertaking. Nevertheless, the results of the survey also support this approach and note that the most benefits will be visible at the start of the implementation process of the single accounting system and that the costs of subsequent adjustments will ultimately be lower for a single system. Moreover, the cost issue is mitigated, as the budget for implementation of a new system has already been secured from European Union funds.

Given the enormity of the task (from design, to training of users, to execution) and the potential drain on the capacity of the Ministry of Finance, the survey report recommended that the implementation process, as well as any supervisory activities, could be outsourced. To create a single, centralised accounting system, the survey report indicated that the ministry must address three issues:

- The system should be acceptable to all units.
- Special solutions should be found for very small budget holders, and an equitable system should be set up for sharing adjustment costs among the many budget holders.
- Universal rules (specification requirements) should be developed for large units which are solely responsible for building their own IT system, whether they choose solutions already available in the market or to develop new systems.

The Ministry of Finance plans to commission a feasibility study sometime in 2011 on the implementation issues regarding a new system. Based on the outcomes of this

forthcoming study, the decision will be taken as to what system will be introduced and when. Once a decision is reached, the tender procedure will commence.

## 5.2. Internal audit

According to the 2009 Public Finance Act, the finance minister defines by ordinance the detailed methods and modes of carrying out, and reporting on, the progress and results of the internal audit.<sup>19</sup> In Poland, internal audit follows EU standards and is carried out on the basis of an annual internal audit plan prepared by the end of each year for the subsequent year, although additional internal audits may be done outside of the scope of the audit plan in justified cases. By the end of January each year, the internal audit team must also “prepare a statement on the execution of the audit plan for the previous year” (Article 283[5]). Both the plan and the statement on the execution are made public. The reports of the internal auditors are also available to the Supreme Audit Office (NIK).<sup>20</sup>

Internal audit is considered autonomous and independent, reporting to the management of the budgetary organisation or the line minister. With some exceptions, there are typically 3-5 people responsible for internal audit in ministries and 1-2 people in agencies. To date, internal audit focuses on legality and regularity, and there has been only limited assessment of economy, efficiency and effectiveness (or performance). However, it should be noted that a certain amount of experience in performance auditing already exists within ministries and agencies dealing with EU funds. For example, evaluators have examined performance indicators in operational programmes under cohesion policy in certain ministries and agencies in several evaluations during the past six years.

In accordance with the Public Internal Financial Control (PIFC) framework being implemented by all new EU member states, the Ministry of Finance established a Public Finance Sector Audit Department which serves as a central harmonisation unit supporting managerial accountability (financial management and control) and functionally independent internal audit. In line with EU recommendations on good practice, the Public Finance Sector Audit Department of the ministry is separate from the internal audit unit.

In 2009, as part of the broader reforms, the Ministry of Finance established a new Performance Audit Unit within the Public Finance Sector Audit Department. Like the department does more broadly, this new unit will play a “soft co-ordination” role mainly through networking and providing methodological guidance and training for internal auditors with regard to performance auditing and related issues.

The new Performance Audit Unit faces several challenges. It is currently quite small, with only two staff members, although it does have the capacity to hire external experts and may receive funds from the EU co-financed project on performance budget. While the first internal evaluation of the performance budget is not scheduled until 2013, the Performance Audit Unit is preparing to provide advice (in co-operation with the Department for Public Finance Reform) on a methodological framework, including models of existing good practice they have identified (for example, the work of the Ministry of Regional Development’s National Evaluation Unit). The Performance Audit Unit would like to develop resources such as a website, and ensure that sufficient training opportunities are available in advance. Ideally, the unit would like to provide expertise on up to five budget parts for the internal performance audit, such as the Ministry of Health, the Ministry of Justice, and the Ministry of Finance itself.

At the moment, however, the unit's mandate is somewhat uncertain. There is no legal framework and no binding decision on the part of the Council of Ministers or Minister of Finance about the shape of, or even who is ultimately responsible for, internal evaluation of the performance budget. Questions remain regarding both expectations and quality assurance. It is unclear how existing internal auditors will both organise and carry out performance audits (although it is worth noting that the Ministry of Finance has provided training on performance budgeting which included 323 internal auditors and 180 heads of public finance sector entities). Moreover, concerns have been raised about the additional costs associated with this exercise, in terms of both financial and human resources, and how it will be financed, particularly when EU financing comes to an end.

### Box 13. The EU and Public Internal Financial Control (PIFC)

The PIFC model of the European Union attempts to “assist national governments in re-engineering their internal control environment and in particular to upgrade their public sector control systems in line with international standards and EU best practice.” The main international standards underpinning the PIFC model are the INTOSAI “Guidelines for Internal Control Standards for the Public Sector” and the ECIIA “Position Paper on Internal Audit in Europe”, complemented by the INTOSAI “Lima Declaration of Guidelines on Auditing Precepts” of 1977 which are key international standards for public external audit.

An essential element of the PIFC model is a central harmonisation unit (CHU) that is “empowered to manage the development of PIFC.” According to the European Commission, a CHU is defined as “a policy unit attached and directly reporting to the Minister of Finance on the status of internal control in the entire public sector, responsible for redesigning, updating and maintaining the quality of the internal control systems, for harmonising and co-ordinating definitions, standards and methodologies, for networking between all actors (managers, financial officers, internal auditors), for the establishment and co-ordination of sustainable training facilities, including the setting of criteria for the certification of public internal auditors, and for all other actions to improve public internal control systems.”

Ideally the tasks of a CHU are facilitated by “close co-ordination and co-operation with the State Audit Office, professional private organisations (such as the local Institute of Internal Auditors) and academic circles”.

*Source:* European Commission (2006), “Welcome to the World of PIFC”, Directorate-General for Budget, European Commission, Brussels.

### 5.3. External audit

Poland has a rich historical tradition of state auditing, going back to the 16th century. The organisation and functioning of the Supreme Audit Office (NIK) are set out in the Constitution of the Republic of Poland and in the NIK Act of 23 December 1994. The NIK reports to the Sejm (Article 202 of the Constitution) and acts in accordance with the principle of collegiate responsibility. Several mechanisms are in place to guarantee its independence from the executive. First, according to Article 205 of the Constitution, the President of the NIK is appointed by the Sejm with the consent of the Senate for a six-year term (renewable for one additional term only) which does not overlap with the four-year term of the Sejm.<sup>21</sup> Second, the NIK President is protected by immunity.<sup>22</sup> Finally, the annual plan and budget of the NIK are established autonomously and can only be amended by parliament.

The College of the NIK is composed of the NIK President (chair of the College), Vice-Presidents, Director General and 14 other members (seven representatives of legal and economic sciences, and seven directors of the NIK organisational units or advisors to the NIK President). Members of the NIK College (apart from the President) are appointed by the Marshal of the Sejm for a three-year term of office upon the NIK President's request. The NIK College enjoys a wide mandate. It is involved in the process of approval and adoption of the key documents submitted to the Sejm each year, and approves the draft budget<sup>23</sup> of the NIK, the work plan and the report on NIK activity (also submitted to the Sejm). In addition, the College assesses audit programmes and gives its opinion (pronouncements) on the results of particularly important audits, and considers post-audit claims.

Currently the NIK employs over 1 600 staff<sup>24</sup> and is composed of a central office with 14 departments (eight of which are directly involved in audits of different areas of state activity) and regional branches in each of the 16 voivodeships (administrative regions of Poland), all of which are directly involved in auditing and which may initiate audits on their own. However, while the NIK has begun to undertake performance audits, there is no specific department responsible for performance audits.

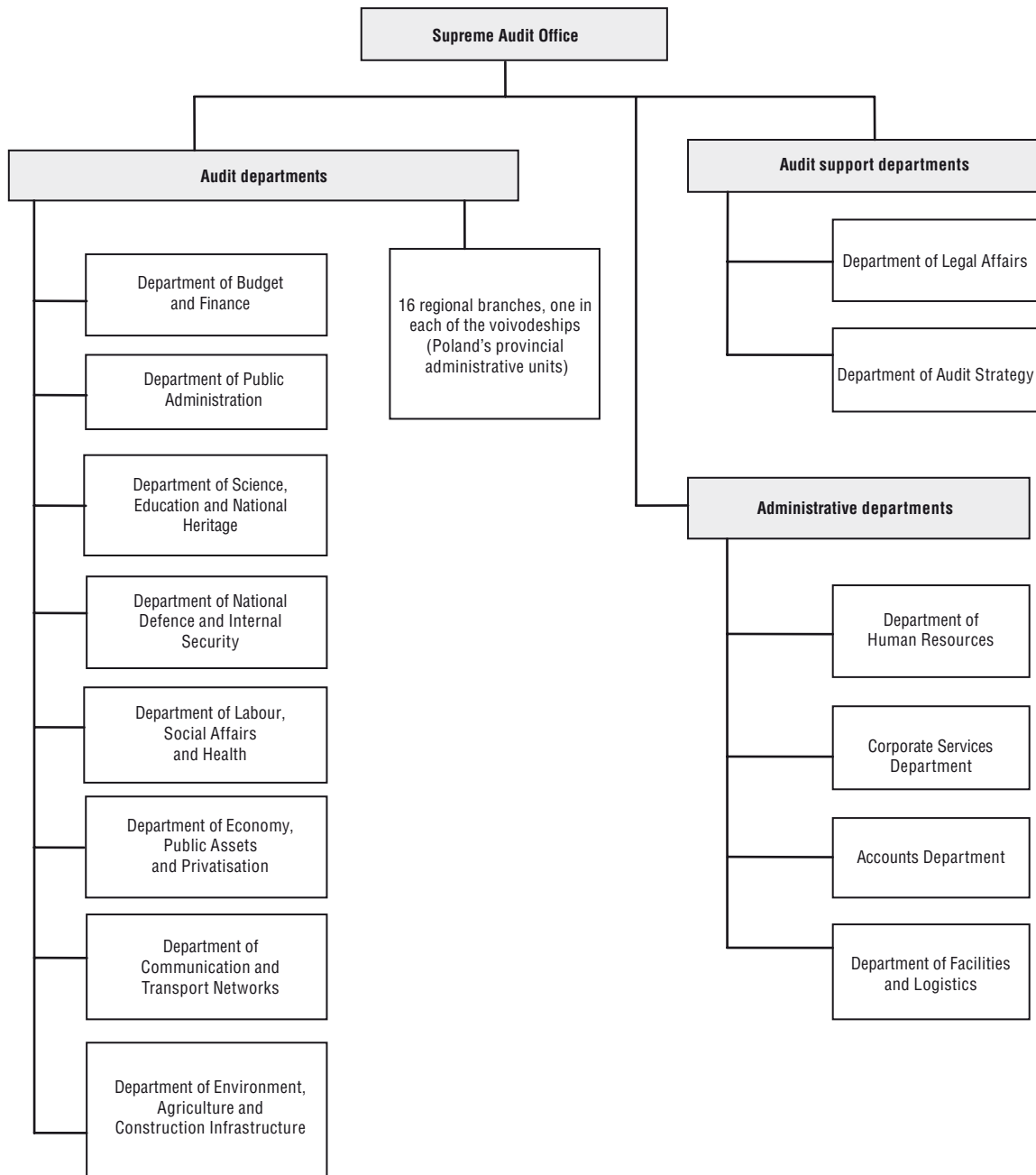
As in most European countries, the NIK maintains close relations with parliament. As noted earlier, the NIK reports to the Sejm and the Sejm (with the consent of the Senate) can both appoint and dismiss the NIK President. The NIK co-operates closely with the various parliamentary committees, and most of the parliamentary committees have an established tradition of reviewing audit reports. Parliamentary committees hold many meetings annually in which matters related to the Supreme Audit Office are featured on the agenda, and NIK representatives are required to participate in these meetings. Moreover, the NIK is notified of all parliamentary committee meetings, and their representatives participate in them regularly. The NIK may also provide additional support to parliamentary committees, such as commenting on draft legislation or preparing analytical papers.

Every year, the NIK is required to submit three reports to the Sejm in addition to the results of the various audits it has carried out during the fiscal year (Article 204 of the Constitution):

- analysis of the execution of the state budget and the monetary policy guidelines (the NIK carries out audits in 400 entities within the state budget execution audit);
- opinion on whether to accept (grant discharge for) the government's accounts for the preceding fiscal year; and
- the annual activity report of the NIK.

Given that the performance-based budget will be legally binding in 2013, the NIK analysis of the execution of the state budget will be increasingly focused on performance. The types of audits conducted by the NIK include: regularity audits; performance audits; and composite audits, which include both regularity and performance issues. It should be noted that the Sejm and its bodies, in particular the parliamentary committees, may ask the NIK to conduct specific audits.

Figure 2. **Organisation chart of the Supreme Audit Office (NIK) of Poland**



Source: Supreme Audit Office of Poland, [www.nik.gov.pl](http://www.nik.gov.pl).

**Box 14. Some audit-related statistics from the NIK 2008 Annual Report**

- 165 planned audit topics
- 2 624 audited units
- 218 *ad hoc* audit topics
- 2 973 post-audit statements
- 172 pronouncements on audit findings presented to the Sejm
- PLN 16 767 million of financial irregularities found
- PLN 553.6 million of financial impact (roughly 2 PLN for every 1 PLN spent)
- 966 meetings of the Sejm committees and subcommittees attended by NIK representatives
- 43 *de lege ferenda* motions
- 9 audits conducted in parallel with other supreme audit institutions

The NIK is supportive of, and has been continuously involved in, the introduction of PBB reforms. This involvement is demonstrated, for example, by the inclusion of the NIK President's advisor in the Strategic Group to ensure the support of top management for the implementation of performance-based budgeting (see Section 1.1 above).

The NIK has been gradually introducing assessment of the performance-based budget for the past three years. However, the office noted that public institutions, and the NIK itself, have found these assessments challenging, as the Ministry of Finance has yet to determine all of the necessary legal standards for implementation and audit. The first pilot audit of the PBB in 2007 focused on scientific research and higher education. It proved difficult in practice, and the findings indicated that “the PBB was still mainly a paper exercise with no monitoring and impact on efficiency” which is to be expected at this point. Steps forward occurred in 2008, with more ministries introducing performance-based budgeting and the new definition of the “functions” in the PBB. As part of the report on the execution of the state budget, the NIK chose to examine two aspects of the PBB reform: i) tasks, sub-tasks and their relevance; and ii) proper formulation of objectives. The NIK concluded that decision makers were still struggling with the PBB system (particularly in terms of devising tasks and sub-tasks and record keeping which does not translate easily from the records kept for the traditional budget) and recommended streamlining the structure of tasks and sub-tasks. In 2009, the NIK noted a strong ministerial effort to improve the indicators, although monitoring, record keeping and reporting remained weak. In addition, the indicators did not always describe the genuine cost of a given task; some were defined as a percentage of budget execution, but some were simply descriptive. While several entities stand out as making significant progress (*e.g.* the Chancellery of the Sejm, the Polish Academy of Science, and the Ministry of Education), the NIK again concluded that it was difficult, if not impossible, to say whether efficiency has been enhanced, and recommended that the government undertake further analytical work to improve the tasks, sub-tasks and indicators.

It remains to be seen how the audit will progress for 2010, particularly in the light of the new law on public finance which is only just starting to be applied, and some of which will not be applied until 2013 at which point the NIK will carry out a full audit of the PBB. In 2011, the NIK is planning a strategic audit on PBB methodology (planning process, execution,

monitoring, reporting) and spending which should provide useful recommendations for advancing the reform.

#### **5.4. Conclusions regarding reporting, accounting and audit**

Reporting and accounting remain some of the greatest challenges faced by the Ministry of Finance. The ministry has already invested heavily in assessments for the development of an IT system for reporting and accounting for the PBB. The experience of many OECD countries has shown that reforming IT systems for reporting and accounting can be a very difficult and costly affair. Given the directions of Poland's reform and the continued existence of the traditional budget alongside the PBB, it might be useful to focus on building automated bridges between the traditional budget and the performance-based budget.

Internal audit in Poland is aligned with the EU Public Internal Financial Control framework. The Ministry of Finance plays a key role as the central harmonisation unit. A small Performance Audit Unit has also been set up within the Ministry of Finance, but its mandate – which pertains to performance audits at the “higher level” for the whole of public finance sector funds – remains somewhat unclear. The scope of internal evaluation of the performance budget (including its organisational, financial and methodological dimensions) still needs to be decided. The new Performance Audit Unit should be clearly tasked with developing guidelines for performance audits. Training may also be necessary to increase the capacity of the auditors to carry out performance audits.

The Supreme Audit Office (NIK) is supportive of efforts to introduce performance-based budgeting and is committed to its success. It will remain a key partner for the Ministry of Finance (and the parliament) in moving the reform forward and refining elements of the PBB, particularly in terms of indicators, through its continued assessments and recommendations. The PBB initiative dovetails nicely with the direction the NIK is already taking in terms of increasing performance audits.

#### **Notes**

1. Additional assistance, particularly with documents in Polish, was provided by Paulina Biernacka (consultant).
2. The Deputy Minister supervises and co-ordinates the work of the State Budget Department, the Budget Zone Financing Department, the Local Government Finances Department, the Paying Authority Department (dealing with EU funds) and the Department for Public Finance Reform. Each department is led by a director. Certain other departments are also involved in the reform such as, for instance, the National Economy Department.
3. The tasks of the NCPB include in particular: co-ordinating the elaboration of forms used by the entities of the public finance sector for preparing performance-based financial plans for the purpose of elaborating the justification to the draft budget act and report on the execution of the budget act; co-ordinating the works on the catalogue of budget tasks, as well as targets and measures of execution thereof; and ensuring the conformity of the budget tasks with strategies referred to in the act of 6 December 2006 on development policy.
4. According to the EU Stability and Growth Pact, EU countries that are not members of the euro zone annually submit convergence programmes to the Commission that ensure that the SGP deficit rules are not breached. The aim is to ensure more rigorous budgetary discipline through surveillance and co-ordination of budgetary policies within the euro area and the EU.
5. According to Article 114, Section 2 of the Public Finance Act, parts also include certain types of expenditures such as: general funds for local government units, general reserves, special-purpose reserves, servicing of the State Treasury debt, European Union funds, etc.

6. Annex 76 to the Ordinance of the Minister of Finance of 12 March 2010 on the detailed method, mode and deadlines for preparing the materials for the 2011 draft budget act stipulates: “This function comprises activities which are common for (of general character) tasks executed either within the scope of the whole part of the budget or the whole entity, which cannot be measured or linked to individual tasks or if it is not important enough, so that it would be economically justified. They concern issues within the scope of management and administrative and technical services of the budget holder. If the activities of such type are not common for tasks executed either within the scope of the whole part of the budget or the whole entity and they can be measured and linked with individual tasks, they are to be mandatorily presented within proper tasks within the scope of proper functions outside Function 22” (translation by the Polish Ministry of Finance).
7. This has happened rarely, for example in 1998 and 2000.
8. The “OECD Best Practices for Budget Transparency” (OECD, 2002) state that the executive’s draft budget should be submitted far enough in advance for proper review by the legislature – at least three months prior to the start of the fiscal year.
9. However, if an MP or a committee would like to obtain specific information about the government’s intentions for the budget bill, they have the right to submit a formal question or an interpellation to the government, or to invite government officials to participate in a committee meeting.
10. During budget deliberations, the government may also submit additional drafts of acts that are intended to introduce changes to tax or spending legislation.
11. Both houses of parliament can submit bills, including groups of 15 or more deputies, Sejm committees, and groups of 10 or more senators.
12. Although the chair may choose to resign.
13. Committee meetings are open to the public (although there are rare occasions when closed-door sessions are held to discuss issues which require confidentiality). However, this openness is strictly regulated by the rules. For instance, an MP must inform the chair in advance if he or she wishes to invite outside representatives. Accredited journalists can participate in committee sessions provided they do not interfere with the committee’s work. Strict procedures are in place regarding lobbyists, and the average citizen cannot take part in a committee meeting uninvited.
14. A Public Finances Committee member can submit a minority motion (if his or her amendment has not been adopted by the committee). This motion is included in the report prepared for the second reading, and minority motions and amendments to the bill proposed during the second reading are put to a vote in the third reading of the bill.
15. During the parliamentary budget process, amendments may be withdrawn due to the results of the previous votes.
16. Certain institutions such as the Chancellery of the President, the Chancellery of the Sejm, the Chancellery of the Senate, the Supreme Audit Office, and the National Broadcasting Council (among others) draft their own budgets independent of the government, and these budgets (which comprise only a very small portion of total government expenditure) can only be amended by parliament.
17. In 2009, the Ministry of Finance outsourced two studies: “Performance Budget: The initial vision of an IT system” aimed at preparing the concept of an IT system that would support the servicing of the state budget in performance-based form, and “Preparation of description of business processes concerning the servicing of the state budget in performance-based form”.
18. Only 42% of respondents indicated the need to have access to a central accounting system.
19. Additional regulations and guidelines can be found in the “Internal Audit Standards in Public Finance Sector Organisations”, the *Auditors’ Manual*, the “Charter of Internal Audit in Public Finance Sector Units”, the “Code of Ethics for Internal Auditors in Public Budget Organisations”, and the Regulation of the Ministry of Finance of 1 February 2010 on conducting and documenting internal audit.
20. Co-operation between internal audit and the NIK is regulated by the NIK Act of 23 December 1994, by the “Internal Audit Standards in Public Finance Sector Organisations”, and by the “Charter of Internal Audit in Public Finance Sector Units”.
21. According to Article 205 of the Constitution: “The President of the Supreme Chamber of Control shall not hold any other post, except for a professorship in an institute of higher education, nor perform any other professional activities” and “the President of the Supreme Chamber of Control



- shall not belong to a political party, a trade union or perform public activities incompatible with the dignity of his office.”
22. According to Article 205 of the Constitution: “The President of the Supreme Chamber of Control shall not be held criminally responsible nor deprived of liberty without prior consent granted by the Sejm. The President of the Supreme Chamber of Control shall be neither detained nor arrested, except for cases when he has been apprehended in the commission of an offence and in which his detention is necessary for securing the proper course of proceedings. The Marshal of the Sejm shall be notified forthwith of such detention and may order an immediate release of the person detained.”
  23. The NIK College drafts its own budget independent of the government, and it can only be amended by the parliament. The draft budget of the NIK is discussed and recommended by the Sejm’s Public Finances Committee and the State Audit Committee and put to a plenary vote as a part of the state budget.
  24. Auditors follow a “Code of Ethics for NIK Auditors” which was introduced by the NIK in 2002. This code takes into account provisions of the “Code of Ethics” of the International Organization of Supreme Audit Institutions (INTOSAI).

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## ANNEX

### *Milestones of performance budget implementation in Poland (annex provided by the Ministry of Finance of Poland)*

#### **2008**

- Analysis of legal acts for the purpose of performance budget implementation
- Elaboration of methodological foundations for multi-annual performance planning
- Preparation of assumptions for legal acts regulating the functioning of the performance budget, including multi-annual performance planning
- Preparation of projects co-financed from EU funds, aimed at implementation of the performance budget

#### **2009**

- Elaboration of performance budget methodology
- Elaboration of guidelines for preparing a report on execution of the budget in performance form
- Elaboration of assumptions for an IT system for servicing the performance budget

#### **2010**

- Elaboration of a concept of monitoring the execution of the budget in performance form
- Completion of a first stage of works on the performance budget reporting system, enabling the monitoring of public expenditures

#### **2011**

- Completion of works on an indicators database for functions of the state
- Completion of the second stage of works on a performance budget reporting system, enabling the monitoring of public expenditures
- Conducting the first monitoring and reporting on performance budget execution

#### **2012**

- Preparing the first parallel draft budget act (traditional budget and performance-based budget) for the 2013 budget year
- Implementation of the methodology for effective public finance management at the central level by means of multi-annual performance planning and completed database of indicators

**2014**

- Preparation of the report on the execution of the budget act comprising the execution of the performance budget in 2013 (in parallel to the traditional budget)
- Elaboration of a report on the *ex post* evaluation of the execution of the 2013 budget act, as an instrument supporting the preparation of the 2014 draft budget act

**2015**

- Elaboration of a report concerning the impact of performance budget functioning on public finance
- Financial settlement of the projects co-financed from the European Social Fund

**Cyclical budget works (conducted annually 2008-15)**

- Elaboration of the provisions concerning the performance budget for the purpose of an ordinance on the detailed method, mode and deadlines for preparing the materials for the draft budget act (the so-called Ministry of Finance's budget circular)
- Elaboration of information on the execution of the budget in performance form as presented in the justification to the draft budget act (last time for the 2012 budget in 2013)
- Elaboration of a report on the execution of the budget act in performance form (beginning in 2014 for the 2013 budget act)
- Elaboration of the materials necessary for the purpose of justification to the draft budget act (until 2011)
- Elaboration of the draft budget act in performance form parallel to the traditional budget (beginning from 2012)
- Works on the database of indicators (until 2011)
- Monitoring of the execution of the budget in performance form (beginning in 2011)
- Works concerning the implementation of an IT system to service the performance budget (2010-12)
- International co-operation on issues regarding performance budgeting and multi-annual financial planning
- Organisation of conferences and training, as well as providing expertise in the field of performance budget for the public administration
- Execution of the projects co-financed from EU funds (Operational Programme Human Capital financed from the European Social Fund) concerning the implementation of the performance budget.