ISSUES FOR DISCUSSION

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This paper suggests areas that the Working Party may want to focus its discussion on.

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The Political Economy of Reforming Entitlement Programmes

1. Reliable and transparent budget information and processes taking into consideration the long-term will not in themselves overcome the short-term nature of annual budgetary decision-making. The budget reflects the political decision-making process. At the end of the day, hard choices must be made by policy-makers in order to prepare for future outlays. Long-term costs must be reduced. This will include decisions to reduce benefits or tighten eligibility requirements for certain government programs. History has demonstrated immense political obstacles to doing so. But the longer such decisions are delayed, the worse the problem becomes and the more drastic the decisions eventually have to be.

2. The Working Party may wish to address the following issues:
   - What is the experience of Member countries in overcoming the inherent political obstacles to reforming longer-term budgetary issues? What can be the “triggers” for political acceptance of such reforms? Some commentators believe that a crisis atmosphere is necessary? What can be achieved in the absence of such an atmosphere?
   - What is the experience with special commissions on longer-term budgetary issues? What is the experience with programmes aimed to educate the public about such issues? What is the appropriate role for budget offices in this area?

3. The single most common motivation for investing in private financial assets by governments is to pre-fund long-term pension expenditure. Over the next decades, OECD Member countries will experience a significant ageing of their populations. This will lead to a substantial increase in age-related public expenditure, notably for pensions. Currently, Member countries are, with significant exceptions, enjoying a rather healthy fiscal position. By accumulating private financial assets during this time period, Member countries can mitigate the fiscal consequences when these long-term expenditures come to fruition as they will be able to draw down on these assets.

4. The Working Party may wish to address the following issues:
   - Is this a viable option especially when governments have debt? Will it serve to increase overall national savings? Is it better to set up separate funds for specific uses or simply use any additional funds to pay down debt?
   - Can the establishment of special funds like this have the perverse effect of delaying necessary reforms to the underlying programmes by giving the impression that the problem has been “solved”?
• If the government does decide to start accumulating private financial assets, it will face the challenge of ensuring that those assets are kept separate from the “normal” budget. How can any such funds be ring-fenced from the rest of the budget?

• Can effective governance arrangements be put in place to insulate the management of the investment portfolio from political considerations? Are there difficulties about government becoming a major investor in the domestic stock market?

Time Horizons in Budgeting

5. With appropriations fixed for only one year at a time, how can policy-makers be encouraged to be sufficiently foresighted and forward-looking? And with objectives set for such a limited time-span, how can managers be stimulated to build sustainable capacity? Both in budgetary politics and in public administration, items and targets in the current fiscal year and in the budget under examination tend to capture almost all the attention, with longer-term consequences disappearing into a haze of incertitude. This may lead to a variety of distortions, such as over-consumption, under-investment, or spending frenzy towards the end of the year. When the budget balance of each fiscal year is played up as the main criterion of failure or success, programmes will be assessed on the basis of their immediate budgetary effects and easily quantifiable results, while more intangible constraints and objectives tend to be disregarded.

6. The Working Party may wish to address the following issues:

• Does the Working Party agree that there is an inherent short-term bias in the budget process? If so, is this solely a function of the electoral cycle?

• What has been the experience with medium-term expenditure frameworks in serving to alleviate this problem? Has the use of very long-term budget forecasts (intergenerational) been of value? Has the adoption of accrual increased the focus on longer-term issues?

• Is a more radical overhaul of the budget process required to overcome the short-term orientation of the budget process? If so, what are the elements of such a radical overhaul?

Budgeting in Finland

7. Finland has had a remarkable budget experience during the past decade. Finland’s public finances have traditionally been fairly balanced. In 1990, Finland had one of the lowest levels of debt among OECD Member countries. Then in the early 1990s, Finland’s economy took a nosedive. This was the consequence of the bubble economy bursting and the collapse of markets in the Soviet Union. In 1991-92 alone, GDP declined by a total of more than 10%. Unemployment rose from 4% in 1990 to 18% in 1993. Government deficits averaged 8-10% of GDP during the early 1990s. Finland’s level of indebtedness increased from about 10% of GDP to reach almost 70% of GDP at its peak.

8. Recognising the severity of the problem, the Finnish authorities embarked in the early 1990s on a fiscal consolidation programme that is without equal among OECD Member countries. In a series of measures, expenditures were significantly reduced throughout the period. By the end of the 1990s, central government expenditures as a percentage of GDP are estimated to be almost 8% lower than they would have been without these measures. Most of the expenditure reduction packages were ad hoc in nature and often assembled at the last minute in response to crisis, especially a run on the currency. In one memorable weekend, the government agreed on measures that decreased expenditures by 2% of GDP. As a result of
these measures and due to strong economic growth, Finland is now once again enjoying budget surpluses and paying down accumulated debt. Finland’s budget position is, however, especially vulnerable as the ageing of the population will affect Finland more significantly than most OECD Member countries.

9. The Working Party may wish to address the following issues:

- The Finnish budgeting system has demonstrated its resilience in achieving control of the budgetary aggregates. Allocation and reallocation of resources is however a problem. The Coalition Agreement, issued when a new government takes office, is seen by many as the only vehicle for meaningful reallocation? Are there other options available based on Member countries’ experiences?

- In practice, Finland does not employ a rolling multi-year expenditure framework. The Secretariat views this as an important shortcoming of the budget formulation process. Do Delegates agree with this analysis?

- The level of transparency in the Finnish budget formulation process is high. The requests by individual ministries and the overall budget proposal by the Ministry of Finance are both published during the budget formulation cycle. What are the advantages and disadvantages of such an approach? Is this desirable for other Member countries to adopt?

- Finland has embraced managerial flexibility in recent years. At the same time, significant difficulties remain in establishing an effective accountability for results regime. This is a problem shared by other Member countries. What actions have been taken to alleviate this problem?

**Leading-Edge Budgeting Reform: Accruals**

10. Cash and accruals represent the opposite ends of a spectrum of possible accounting and budgeting bases. The cash end of the spectrum has traditionally been applied by Member countries for their public sector activities. In recent years there has been a major trend towards accruals end of the spectrum in Member countries. About half of Member countries have adopted accruals to one degree or another.

11. The Working Party may wish to address the following issues:

- Accruals is increasingly accepted for financial reporting purposes in Member countries. There is, however, much greater hesitation in adopting accruals for the budget. Is this likely to be a permanent situation, or will the budget increasingly adopt accruals as more experience is realised with accrual financial reporting? Are there significant problems with operating the budgeting and financial reporting on different basis?

- Should heritage assets and military assets be reported like other assets, or are they of such special nature that they should not be reported?

- Should historical cost or current valuation methodologies be applied for assets? What has been the experience of countries in responding to changes in current valuations?

- How can the independence of the accounting standard setter be ensured while at the same time respecting the constitutional responsibilities of the finance minister? Are International Public Sector Accounting Standards (as developed by the Public Sector Committee of the International Federation of Accountants) an acceptable and credible option in Member countries?
Leading-Edge Budgeting Reform: Results-Orientation

12. Since the early 1990s, almost all Member countries have been working on improving the quality of their public expenditure by bringing targets, results and performance information into their budgeting and management systems. The approaches to actual implementation have been diverse and adapted to national capacities, cultures and priorities. Notwithstanding these differences, there is great similarity in the conceptual frameworks applied and the thinking behind the reforms in most Member countries.

13. The Working Party may wish to address the following issues:

- Are results-oriented budgeting and management reforms making a difference? What are the conditions under which they work? And do not work? Are there sectoral differences?
- How do countries deal with the vastly increased amount of data that is generated by results-oriented reforms? Is the new information well used in the budget formulation process and in parliament’s discussion of the budget?
- How can performance information be made credible and reliable for accountability purposes?

“Distributed Governance”: Agencies and Other Autonomous Bodies

14. Agencies, authorities and other more autonomous government bodies for non-commercial purposes, are growing in importance in Member countries. Over time it has become evident that in some instances the operational advantages of structural innovations in government, have been offset by a loss of whole-of-government cohesion and of democratic oversight. Some Member countries have also found a need to rethink their processes of control and scrutiny of bodies which have traditionally operated with degrees of autonomy.

15. The Working Party may wish to address the following issues:

- Over time countries spawn a variety of organisational forms in response to ad hoc political and administrative circumstances. The result in many Member countries is a disparate collection of public entities outside of the core administration for which there is no overarching governance policy; indeed a number of governments do not know how many such entities they have. What has been the experience of member countries in making this aspect of government structure more “readable” and in establishing consistent governance standards?
- NPM-style reforms, especially in the UK and Commonwealth countries, have resulted in a systematic process of creating new public agencies over the last two decades. Within this movement, the organisational form which appears to be most successful has been departmental agencies within the legal framework of the public service with oversight boards that are largely advisory and/or representative. More controversial has been the experience of anglophone countries who have sought to replicate in the public sector, the commercial public company board structure with clearly devolved decision rights and accountability. What is the future for this kind of board for non-commercial public functions?
- The long-standing Swedish model of agencies continues to be a strong influence in Scandinavia generally. The success of the model derives at least in part from the characteristics of the political/administrative culture in which it is imbedded. Is this model being successfully adapted to meet the needs of a more responsive and strategic central government perspective and the more formal regional and global constraints under which states now operate?