

BREAK-OUT SESSIONS ON KEY BUDGET FORMULATION ISSUES

Considerations in Introducing Program Budgeting

Introduction

It was 11:00 at night as Boris Bakovich placed his glasses down on the desk in his office and rubbed his eyes. Boris was the senior advisor to the Minister of Economy and Finance, and it was another late night of pouring over budget submissions from line ministries. The next day the Minister would make a final budget proposal to the Cabinet before its submission to Parliament. The budget conferences had been completed, but the ministry staff had had a hard time deciding how to make trade-offs between the different ministry proposals. In each of the budget conferences, ministries would argue persuasively about why they needed additional funding for this department or another. Usually their estimates were considerably above the ceilings that MEF had issued, and so there was a process of cutting back on their proposals. It appeared to be an annual tradition – ministries propose dramatic increases without much justification and MEF cuts back.

The meetings with the line ministries were often long and tedious, as discussions would revolve around how much was really needed for a specific line item like fuel, travel, or office equipment. MEF traditionally relied on certain norms for what a ministry of a given size should need. The also looked at last year's level of budget and tried to adjust for inflation and exchange rate changes that might affect cost. Budget examiners did not understand much about the specific strategies and activities of the ministries they met with; instead they tended to concentrate on keeping down the overall cost. The ministries would often cite how their particular programs would suffer, but there was no basis to evaluate how they were using the funds they currently had.

In principle the government's budget decisions were to be guided by the three-year National Development Strategy (NDS) that had been adopted last year. In practice, MEF found it was hard to take the broad strategies that were incorporated in the NDS and to know how they would translate into the budget. The budget was organized around ministries and departments and many of the strategies did not fit neatly into the ministries' organizational structure; some key missions even cut across ministries. Government had a difficult time demonstrating to foreign development partners how the NDS was being implemented; the Parliament also complained that they could not see from the budget documents what changes had been made to reflect the NDS.

Reporting on budget execution helped only marginally in explaining to stakeholders the government's policy direction. MEF could produce annual financial statements that showed how spending was increasing in certain sectors, but the reports were focused on changes in spending for different line items (e.g., fuel, supplies, wages) within a ministry.

Of immediate concern to Boris was that the minister needed a better way to evaluate the different budgetary trade-offs. Fiscal space was limited and so large increases in the overall budget were not realistic. Some ministries needed to be cut back significantly, while others should see increases. But for the MEF it was difficult to evaluate what resources would go for if they were increased. What did it mean for the budget to set as a national goal to increase agricultural production in the North? Could the MEF or the

Parliament be sure that was how funding would be used? Likewise, then MEF wanted to propose cuts in a ministry's budget, it was difficult to assess what the impact might be on specific activities.

One of Boris's colleagues in the MEF had recently been talking to him about budget reforms that had been implemented in many of the OECD countries. It was called program budgeting in some countries and in others, performance budgeting. There were different variations in place, but the main idea seemed to be a focus on managing for results rather than controlling line item inputs. He had heard a lot of discussion about performance indicators and accountability measures, but it all became a bit confusing when they talked about "outputs" versus "outcomes". He had to wonder whether the practices being used in New Zealand and Australia were realistic for a country like his.

As Boris contemplated whether to propose the adoption of program budgeting as a new reform, he carefully considered the likely challenges MEF would face. There were several he could think of:

- a) The MEF has limited capacity. The staff was already busy with the current process for preparing the annual budget, how could they take on an additional activity?
- b) Line ministries have even less capacity than MEF. Usually the budget was prepared in the line ministries by the administrative department, which often did not know the main policy priorities of the ministry; it was a technical exercise for them and little more. Could the line ministries be trained, and if so, over how long a time period?
- c) The MEF's Treasury department and some external partners insist that fiscal control should be the top priority. Yet, what he understood of program budgeting implied loosening control over inputs in order to better focus on outputs. Is this an insurmountable conflict; must you give up one for the other? What changes would it require in the way Treasury tracked and reported on expenditure?
- d) Parliament is accustomed to the present format. Why would they want to change? They also like comparing with the prior year's budget, this will make it harder.
- e) Ministers are accustomed to the present format. Why would they want to change; how would it benefit them? Will they view it as something imposed by MEF?

Before he could go to the minister with a proposal, Boris felt that he needed to begin putting an action plan together in his mind for addressing the challenges. If the Minister or the Parliament thought he was proposing to copy what New Zealand did, he knew that the reforms would never get off the ground. There were elements of program budgeting that he thought made sense, but how could it be implemented successfully in his country.

Put yourself in Boris' position and discuss the following:

1. How does he convince the various budget stakeholders that a change to program budgeting would be worth the effort? What incentives would they have to change what they are used to?
2. How can he overcome the capacity constraints both within the MEF and in the line ministries? What sequencing would be most practical, and what are realistic expectations to set for its use in each of the first few years?

3. What guidance should he give about developing the programs and activities so that (a) they are owned by the ministries themselves and (b) that effectively communicate the government's main priorities?
4. What can he propose as a realistic strategy for developing meaningful performance measures over time, and how might the information be used and by whom?
5. What can he say to Treasury that would persuade them that they will not lose control over the fiscal situation and that arrears will not worsen?
6. What changes, if any, might be needed in the job of MEF budget examiners to make the reform effective? What changes might occur in how MEF interacts with line ministries about their budget submissions?