



# Performance Based Budgeting in OECD Countries

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Lessons for Poland

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# Overview of Presentation

- Trends and definitions of PBB
- Different Implementation approaches
- PI in budget Process
- Benefits
- Challenges
- OECD Guidelines

# Trends in Developing PI

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

# Performance Budgeting Categories

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



# Reforms and Different Implementation Approaches

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

# Different implementation strategies for PB

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

# Summary of Country Implementation Strategies

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



# Performance Information in the Budget Process

# Integrating PI into government-wide budget process

- Changing the budget structure (e.g Australia, the Netherlands, New Zealand and the United Kingdom)
- Using PI in budget negotiations between Ministry of Finance (MOF) and spending ministries
- Using PI in budget negotiations between spending ministries and their agencies

# Changing budget structures

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

# Budget negotiations between MOF and spending ministries

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

# Budget negotiations between MOF and spending ministries (continued)

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

# Direct/Formula PB

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

# PI in budget negotiations between spending ministries and their agencies

- PI more often used by spending ministries
- Agency performance agreements and contracts e.g. Australia, Netherlands, NZ and Nordic countries
- Depending on flexibility in wider budget structure used to manage programs and redistribute resources
- Across and within countries wide variation in use of PI in decision making.
- Depended on quality of PI, political pressure, and strong organisational leadership

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

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

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

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

# Financial rewards and sanctions

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

# Factors influencing the use of PI in budgetary decision making

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

# Reported benefits

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

## Reported benefits (Continued)

- Signaling device highlights policies and programs that work and those that do not work
- Improving Management
- Informing citizens' choices
- Improving efficiency

# The Challenges

Countries continuing to struggle with

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

## The Challenges (continued)

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

# OECD General Guidelines for Developing and Improving the Use of PI in the Budget Process

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

# OECD General Guidelines for Developing and Improving the Use of PI in the Budget Process

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

# Conclusion

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