

SEMINAR
ON
RESULT BASED BUDGETING:
OBJECTIVES, EXPECTED RESULTS AND PERFORMANCE INDICATORS

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Notes from Ian C. Davies

“... a puzzling limitation of our mind: our excessive confidence in what we believe we know, and our apparent inability to acknowledge the full extent of our ignorance and the uncertainty of the world we live in. We are prone to overestimate how much we understand about the world and to underestimate the role of chance in events. Overconfidence is fed by the illusory certainty of hindsight.”

“... conversations that intelligently explore the lessons of the past while resisting the lure of hindsight and the illusion of certainty.”

Daniel Kahneman – *Winner of the 2002 Noble Memorial Prize in Economics – from his recent book: Thinking, Fast and Slow – 2011 – Penguin*

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Mr Davies has been deeply involved in performance based reforms of public administrations since the early eighties. He has carried out, evaluated, written and advised on, performance oriented initiatives in government, public agencies and multilateral organisations nationally and internationally. Mr Davies has been Advisor to the President of the Treasury Board of Canada on performance reporting to Parliament, Advisor to the European Commission on evaluation and administrative reform, Advisor to the European Court of Auditors on sound financial management, Director of performance audit and accountability for the Auditor General of British Columbia and Coordinator of Programmes for the Ministry of Health and Social Services of Québec. He advises regularly governments, multilateral organisations, UN agencies and private sector companies on questions of corporate and institutional governance, organisational and management performance, accountability, transparency and corporate social responsibility.

Principles and lessons for performance oriented reform

Performance oriented reforms and initiatives have been a feature of efforts by governments and public sector organizations to improve their overall effectiveness and accountability for well over 30 years now.

From these experiences some general lessons and principles have emerged to avoid common pitfalls and increase the likelihood of success.

In no particular order:

- Initiatives of this type have more to do with behaviours and organizational culture, i.e. social challenges, than with the development and implementation of tools and techniques, i.e. technical challenges. Efforts that do not at some point recognize this reality and address it are at a greater likelihood of failure than those that do.

- There is no one single right way to carry out performance oriented reforms and initiatives. Most begin in the context of financial constraints such as budget reductions and by tackling the reform process from a technical perspective, i.e. adopting measurement techniques, training staff in these, developing information systems support, etc. it is key however to include cultural and behavioural dimensions of change in the reform process at the earliest possible stage.

- Reforms and initiatives such as results based management and results-based budgeting revolve to a significant extent around the production and reporting of so-called performance information. It is a truism that, in order for behaviours and processes to change and for performance to improve, information should be meaningful and most importantly used.

- This means that performance information should be useful to managers for making management decisions and to members of governing bodies for making governance decisions. A common mistake made in the implementation of reforms is to think and act as if management and governance require the same information. There is an inherent risk in generating and providing the same information to both management and governance functions that it serve neither one well.

- A common problem faced by governments and multilateral organizations in coming to grips with their performance is finding appropriate and credible ways of valuing and communicating what they do. The great majority of performance monitoring tools and techniques are causal in nature, e.g. program logics, logical frameworks, hierarchy of objectives, results chains, etc. and particularly well-suited to operational "production" processes. However, many public organizations including multilaterals such as the Council of Europe, engage in activities that are political and normative in nature. As such, the typical armamentarium of causal techniques may not be particularly well-suited to valuing appropriately and communicating effectively the worth of activities and of the enterprise.

- Program performance and organisational performance are two distinct constructs. Levels of analysis are different as are degrees of complexity. The sum of the former does not equate to the latter.

- The risks associated with poorly thought through performance based reform or change initiatives may be significant and should be taken into account when developing and implementing:

1. Reducing performance by focussing on the "wrong things", i.e. perverse incentives, incurring important new costs, making for additional work, creating internal competition for resources which reinforces silos
2. Stifling innovation, restricting professional judgment, increasing risk aversion, demotivating staff, preventing learning
3. Substituting funders' requirements for mandate and mission consistent governance and strategic orientation, i.e. mission drift

Highlights from recent literature on results-based budgeting¹

Literature on results-based budgeting covers the three main aspects of conceptual knowledge/theory, practice, and guidance. It is produced mainly in the field of development cooperation, in the context of United States government (mostly at state level), and on experience acquired in OECD countries (mostly published through the OECD itself). Most of the literature deals with performance budgeting at some level of government; only very few documents look at performance budgeting within organizations or institutions.

Conceptual knowledge/theory

Different definitions of results-based budgeting (or “performance budgeting”, as it is called more often) are being used. A basic definition is proposed by the OECD, which defines performance budgeting as “budgeting that links the funds allocated to measurable results” (OECD 2008: 2) In addition to this, some definitions further specify the relationship between funding and results, e.g. “use of formal performance information in resource allocation decision-making” (Robinson & Brumby, 2005: 5). Others identify, which level of results is relevant – usually outcomes (and/or outputs).

There are various types of performance budgeting, which differ mainly in the role of performance information for making decisions on resource allocation.

The OECD distinguishes three types of performance budgeting (see OECD, 2007: 21-22):

1. *Presentational performance budgeting*, in which performance information is presented in some form in the budget, but has no influence on funding.
2. *Performance-informed budgeting*, whereby budgeting decisions are indirectly related to either past or future proposed performance. The link between performance information and funding is neither mechanical nor automatic.
3. *Direct/formula performance budgeting*, which involves the direct and explicit linking of resources to results achieved

Other criteria, by which performance budgeting models differ, are the scope (e.g. government-wide or sector-specific), the objectives (e.g. focus on expenditure prioritization or on improving service effectiveness and/or efficiency) and the type of performance information they principally rely upon (see Robinson, 2011: 14-19).

Practice

The literature on practical experience reports a number of benefits following the introduction of performance-based budgeting systems. In particular, benefits are seen in the area of planning, with performance budgeting leading to a sharper focus on results, a better understanding of goals, priorities and of how the different activities or programs contribute to achieving these. Performance budgeting is also said to enhance transparency and accountability at large.

Conclusions are more careful regarding the benefits of performance budgeting in terms of improved effectiveness, efficiency and cost saving. Some see a potential of performance budgeting to enhance the management of programs as well as the effectiveness and efficiency of public expenditure, especially when it is embedded in a more comprehensive results-based management context (see Robinson, 2011 and OECD 2007).

While there are indications that some performance budgeting reforms have led to improved efficiency (see Van Landingham, Wellman & Andrews 2005), this achievement seems difficult to generalize and some of the literature comes to the conclusion that (at the level of US cities and

¹ References in annex

states) performance-based budgeting “has not been a major revenue saver” (SEIU 1000, 2010: 3). High start-up costs involved in performance budgeting reform are cited as a non-negligible hurdle.

Challenges in the introduction and implementation of performance-based budgeting occur at various levels:

- Technical problems related to the establishment of performance information (measurement, reliability of data...). Especially more intangible services such as policy advice are difficult to apply performance measures to. A specific problem is the definition of relevant outcomes and making them operational. In many cases, establishing attribution between services and outcomes is difficult. Graham Scott goes as far as to say that managing and budgeting for outcomes is “an unattainable myth” (Scott, 2009: 9).
- Process-related challenges, in particular the question of how to link performance information and funding. The OECD cautions against systems that tightly link performance results to resource allocation as they may distort incentives. Moreover, it is difficult to design systems that take account of the underlying causes of poor performance.
- On the human side, many performance budgeting reforms have faced difficulties in getting decision makers (both at the executive and legislative levels) as well as civil servants on board. This can be due to mistrust, inertia or simply a lack of capabilities.

The literature identifies a number of factors that are believed to contribute to the success – or failure – of performance-based budgeting reforms, among them:

- Whether results-based budgeting is embedded into a larger results-based management context.
- The capability of those planning and executing the performance-based budget.
- The degree of (perceived) freedom of managers – some relaxation of central control is necessary to allow for management based on results.
- The nature of a department’s task is seen as related to managerial freedom and it has been found that market-oriented departments are better suited for the use of performance budgeting.
- The process by which the performance targets are set: the involvement of those who are actually supposed to reach these targets is essential.

(see, for instance, Scott 2009, Helmuth 2010)

Guidance

Based on past experience with the introduction of performance-based budgeting systems, the following is some of the guidance that can be found in the literature:

- In choosing a model of performance-based budgeting and the appropriate approach to reform, the context, including existing capacities, needs to be taken into account.
- It is important to embed performance-based budgeting into a comprehensive planning and reporting framework.
- One needs to be realistic about strategy and timetable for a performance-based budgeting reform. The introduction of a performance-based budget system usually takes several years.
- The key stakeholders need to be involved in designing the reform.
- Graham Scott recommends starting to build a performance management system by identifying outputs or services being produced, rather than defining high-level outcomes or objectives, as this would be a more productive way of proceeding.

Case study summaries and highlights from the practice review on results based budgeting and results based management in multilateral organisations

The following summarizes two case studies of multilateral organizations.

In the **first** organization in which the focus is on planning, implementation and reporting based on a program and budget approach similar to that of the Council of Europe, the initiative got underway in 2002-2003.

The overall assessment given is that the organization has in place formally the basic tools and mechanisms of results-based budgeting and results-based management however it still needs to go further in order to provide its governing body with better and more meaningful information on its overall effectiveness.

The organization has invested significantly in improving the system and structure of its program and budget and in improving the internal mechanics of its performance measurement, e.g. especially with a focus on the improvement of indicators, however the organization finds that it's in a line of business, i.e. regulatory and process oriented, for which outcomes are not easily measurable and countable. A significant portion of its activities is in the area of capacity building.

The organization has come to realize that beyond issues of systems, structures and methodology, there are deeper questions that need to be addressed such as what is the value and value added of what the organization does and how is this effectively communicated to the governing body and to funders.

With respect to the budget allocation process performance information is taken into account but it is only one factor among others in the discussion. Political and policy priorities are also important and constitute key perspectives in the discussion on budget planning and allocation.

Two key lessons learned are:

- 1) That the program and budget system should be simplified to the extreme. The organization finds that it has gone overboard with measurement and that often indicators and measures tend to be artificial. One should not lose sight that in the end the objective is to facilitate the assessment of performance and inform future decisions. This is difficult to do if there is too much "junk".
- 2) That there is a problem with the word "result" in that it can be misleading with respect to the nature of what the organisation does. The organization is more in the business of developing, implementing and accompanying processes. This is a conceptual issue and the organization has to develop better its ability to describe its processes, find ways to assess their value, learn how to improve them and communicate them effectively to its governing body and to funders.

At present the organization is hampered by not having a programming and budgeting system and approach that yields the kind of information that reflects validly its value in a manner consistent with its mandate and its mission. Clarity of concepts and associated terminology is key.

In the **second** multilateral organization the focus since the beginning of the initiative about five years ago, has been on results-based management. At present the organization is considering improving and strengthening its results orientation by moving towards a results-based budgeting system.

The initiative has had to face a significant number of challenges since its inception. Two however stand out:

The first has been the development of the IT system that has known three iterations that never really worked. It is estimated that their approximate costs run to about €10 million. The second challenge is in finding ways to capture, measure and assess the performance of nonoperational

activities. This is a particularly challenging aspect as the organization has a very wide mandate and complex programs. It is not that the organization does not do good work it's that the results-based management system as it stands now is unable to do justice to the quality and value of that work.

With respect to the nature and use of budget related information the organization finds that it can only be as developed as the ability of the governing body to receive it, understand it and work with it as part of its deliberations on budget allocation.

The overriding question for improving the results based management approach is what is the right information to produce and communicate, at what level, to inform management and governance decision-making.

Success factors for results based budgeting

The purpose of results based budgeting and how it is intended to improve performance is explicit, clear and well understood, i.e. there is a theory of change that is informed by evidence.

Results based budgeting is supported by an explicit, clear, well communicated and well understood conceptual framework. Terminology is consistent with the framework.

Results based budgeting is part of a broader reform effort and its role in the latter is clear and coherent.

Different programs have different performance constructs. Measurement and assessment techniques and approaches should be adapted to each, i.e. no one size fits all.

Different information should be provided and used for different purposes, e.g. management, governance, accountability, reporting to funders, public communications, etc.

Results based budgeting develops based on systematic monitoring and evaluation, i.e. organisational learning.

Implications for a Process Approach to Policy

“Finally, if we accept that our ultimate public policy goals involve managing the process of our social development, and that we can have only glimpses of where we want this development to go, we need to act on our understanding that multiple valuing paradigms are critical to the process of error correction in our policies. Particular paradigms, whether economic analysis or constructivist consensus-building, offer many insights but become increasingly dysfunctional if systematically employed to the neglect of other approaches. Without diluting the virtues of individual paradigms, we need a social consensus that multiple perspectives of valuing are not only valuable but also necessary for desired assisted valuation.”

Julnes, G. (2012). Developing policies to support valuing in the public interest. In G. Julnes (Ed.), *Promoting valuation in the public interest: Informing policies for judging value in evaluation*. New Directions for Evaluation, 133, 109–129.

ANNEX

References for literature review of results based budgeting:

Helmuth, Utz, 2010: Better Performance with Performance Budgeting? Analyzing Cases of Success and Failure in Public Administrations

OECD, 2007: Performance budgeting in OECD countries

OECD, 2008: Performance budgeting: A user's guide

Robinson, Marc & Brumby, Jim, 2005: Does performance budgeting work? An analytical review of the empirical literature, IMF Working Paper

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