

Seminar on
Enhancing Performance through Improved Budgeting
held on 18-19 May 2015

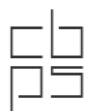
A Brief Report

(August 2015)

Submitted to

The Expenditure Management Commission
Government of India

By



**Centre for Budget
and Policy Studies**

The Seminar was jointly organized on 19-20 May 2015 by



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A Brief Report

1. Introduction

Budget is an instrument that helps translate public policies into concrete actions and desired outcomes. It is a blue print for converting intentions into reality. Like any tool it needs continuous honing. The budgetary practices in India have, however, largely remained unchanged over the years. A few ‘innovations’ such as the performance budgeting introduced in seventies as recommended by the first Administrative Reforms Commission and the subsequent ‘zero based’ budgeting have been outside the mainstream budgeting. The outcome budgeting introduced in 2005 has similarly remained on the margins. They have not had the desired impact on public expenditure management.

Budgeting is intimately linked with the way transactions are classified. The chart of accounts used to classify budget and expenditure has similarly not kept pace with the changing needs of the times. For an efficient public expenditure management, the accounts need to be computerized in such a way that they provide useful information in real time to managers of public funds. While accounts at both the union and state have been computerized, the software systems are fragmented and, are therefore, sub optimal. Only lately has there been some attempt at integrating the different systems into an Integrated Financial Management Information System (IFMIS).

The Seminar jointly organized by Centre for Budget and Policy Studies (CBPS), National Institute of Public Finance and Policy (NIPFP) and the World Bank on ‘Enhancing Performance through Improved Budgeting’ attempted to look at the above issues. The seminar was attended by officers from Finance and Planning departments of 16 States and from Ministry of Finance and other departments of Government of India (List of Participants attached at Annexe A).

The Agenda for seminar included a mix of international presenters and public financial management practitioners from India (Agenda is attached at Annexe B). A notable feature of the Seminar was the support extended by Expenditure Management Commission. While the Seminar began with a key note address by Mr Sumit Bose, Member, EMC, Mr Subir Gokarn, Member, EMC chaired the first Technical Session and Mr. Vijay Singh, Adviser, EMC participated as a panellist in discussion on key take ways at the end of the first day’s deliberations.

Mr. Sumit Bose set the tone for the discourse in the seminar by raising the following points pertaining to budgetary reforms in India in his keynote address:

Some of the practices followed in Indian budgetary practices need immediate attention and relook, especially if fiscal prudence is the goal and budget is an important means towards that. The artificial division between plan and non-plan, which are non-economic categories and followed largely only in the Indian sub-continent, leads to confusion and hides the real status of budget and expenditure. Similarly, the practice of having Revised Estimates, which are often at great variance from Budgetary Estimates also at times gives misleading picture. This also undermines the budgetary exercise as a number of inflated figures are included despite clear knowledge that it would change at the time of revised estimates.

Another practice relates to the lack of clarity regarding depiction of unspent balances by Societies that implement major development programmes funded usually jointly by the union and state governments e.g. Sarva Shiksha Abhiyan – the major flagship programme for universal basic education; and National Health Mission – the major health sector programme aimed to reforming the health service delivery through public institutions. While these Societies report expenditure having taken place, huge sums of money are often found to be resting at some level of the implementation machinery. There is a need to debate if now is the time to change such practices in a manner that budgetary exercise becomes a more evidence-based practice that provides the real economic picture of the nation at that point of time.

Linking / integrating the planning, budgeting and performance review exercises through a process of outcome budgeting where outcomes include final as well as intermediate outcomes would be important in Indian context. For instance, in the context of education, while final outcomes in terms of school attendance and learning outcomes are critical, input indicators such as availability of adequate, well-qualified teachers or appropriate physical facilities is also as important, and should be included as outcome intermediate indicators.



Mr. Sumit Bose delivering the inaugural address

The budgetary mechanism should be able to deal with the issues of addressing needs and rewarding performance; this becomes crucial in a large federal economy where three levels of governments function and control resources. It is also important from the perspective of major inter regional socio-economic differences within the country and at sub-national levels.

Most budget reform discourses in India take only the union and state governments into account, leaving the third level of government: urban municipalities and rural panchayats, outside the purview. While this is understandable in one sense as this level is highly dependent on the grants received from other two levels of government, this needs to change for a number of reasons. One, this level was visualised as growing in importance with passage of time and maturity of the institution, and two, transfer of substantial sized untied grants to these bodies as suggested by the 14th Finance Commission means greater responsibility for planning, budgeting and performance at that level as well. Therefore, it has become increasingly imperative to include these bodies also in the purview of the discourse on budgetary reforms.

Some of the points raised by Mr. Sumit Bose in his address reinforced that budgetary reforms have generally sought to enhance accountability, efficiency and transparency of public expenditure. This Report captures briefly the deliberations in the Seminar broadly under the following themes:

Section 2 looks at the trajectory that budgetary reforms have taken internationally. Performance budgeting has been considered worthy of emulation as its emphasis on results brings focus on fiscal discipline and, efficiency and effectiveness of public expenditure. Not all experiments with performance budgeting have been successful. International experience in performance budgeting, particularly in Chile, South Korea and South Africa, is examined in Section 3. Indian experience in budgetary reforms has been limited. While the Indian PFM system has many strengths such as Treasury Single Account (TSA) and fairly robust computer systems, it has fairly outdated chart of accounts which is backbone of both budgeting and accounting. In Section 4, the Indian PFM system is seen from the perspective of the international good practices. Section 5 looks at international experiences in Integrated Financial Management Information System (IFMIS) (case studies of South Africa and South Korea) and also examines the Indian situation. A road map for budgetary reforms for India is indicated in the last section based on the lessons that the international experiences suggest for India combined with its own ground realities.

2. Budget Reforms – International Perspective¹

Main expectations from budget are that it encourages aggregate fiscal discipline (‘spending control’), enables expenditure prioritization (funds are directed to where they are most needed) and achieves effectiveness (services achieving intended outcomes) and efficiency (services delivered without waste). These higher order objectives have often been ascribed to performance budgeting.

Performance budgeting is a set of methodologies, processes and instruments that allow the decision-making of a budget to systematically incorporate considerations about past and future results into the application of public resources. More specifically, it is the use of performance information to:

- a. inform budget decision-making processes (as one of forward-looking considerations, not a mechanical conditioning of budget allocations to past performance); and
- b. instill *greater transparency and accountability* throughout the budget process (by providing information to the public on performance objectives and results).

Some critical requirements of performance budgeting are:

- a. Availability of comprehensive performance information
- b. Ability of budget process to incorporate performance information into decision-making process
- c. A structure of incentives motivating public institutions to achieve better results
- d. Public institutions are granted some flexibility in resource management to improve efficiency and achieve better results
- e. Sufficient and timely performance information underpinned by monitoring and evaluation (M&E) systems

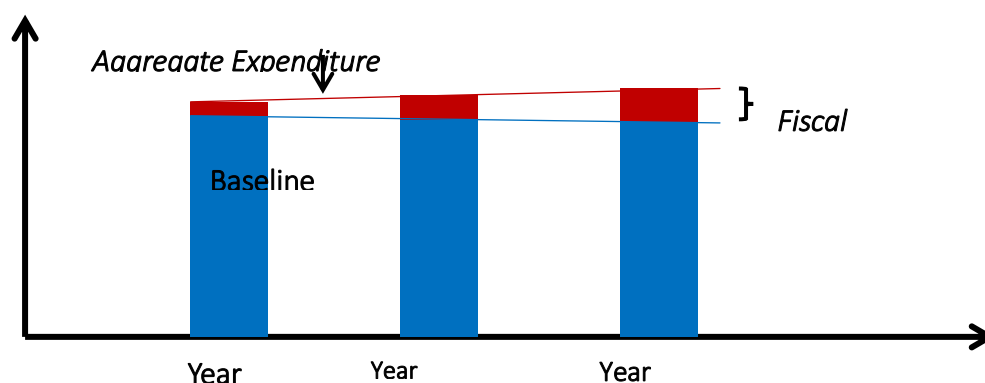
Program budgeting, which is the most important form of performance budgeting, was adopted in order to promote effectiveness and efficiency. The pressure on entities to perform was judiciously combined with increased freedom to perform. Moving beyond traditional line item budgeting, program budgeting helped improve prioritization of expenditure. Important principles of program budgeting are that performance must determine the budget allocation, or else, the system will be just paperwork.

¹ This section is based on the presentations by Mr. Mario Marcel, Senior Director, Governance Global Practice, The World Bank and Mr. Mark Robinson, International Consultant and Author on Program Budgeting

The other major budgetary reform has been medium term budgeting. There have been a range of models in medium term budgeting and experiences of countries have been varied – Australia and United Kingdom are among the successful ones. There are many countries where it has just been a piece of paper.

Taking a medium term perspective of both revenues and expenditure helps government to stay on the course of broad fiscal objectives and undertake new spending only to the extent that ‘fiscal space’ is available or can be expanded.

Figure 1



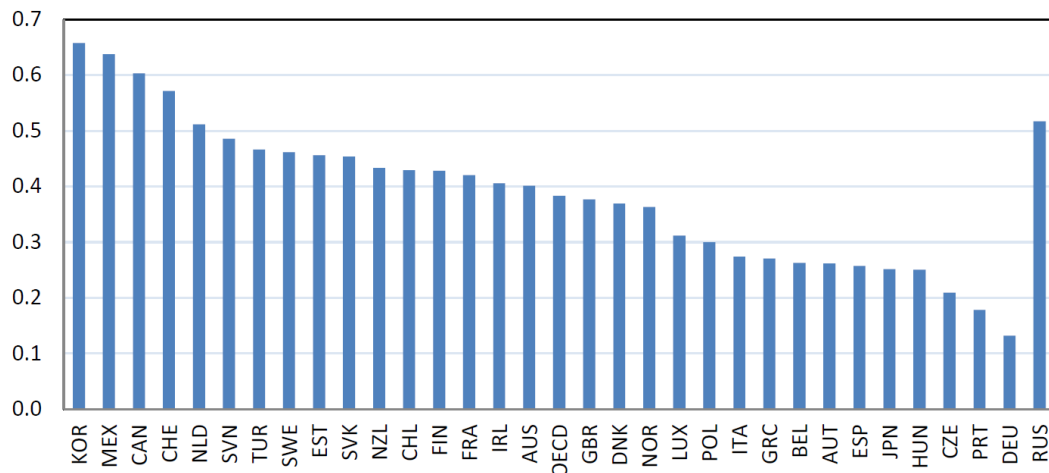
The other important budgetary reform was to integrating planning and budgeting. ‘Plan first, then budget’ model does not work. What is required is that there must be a process to take on board priorities of political leadership and integrate strategic discussion into budget preparation. This enables cutting spending which is ineffective, inefficient or duplicative and reallocating funds so released to more productive and essential programs and projects.

Spending reviews are important means of identifying and adopting *savings measures*. They may be efficiency savings (services produced at lower cost) or as strategic savings (programs scaled back or eliminated). Spending Reviews should be a routine part of the budget process and not just a one-off exercise when times are really tough. Australia follows an annual Spending Review model, while UK, Netherlands, etc. conduct periodic reviews. (Please see Annex C for a short note on spending reviews)

The important principle of budgetary reforms is ‘substance rather than form’. New systems must be designed to have an impact and not just to produce new documents and information. Also of equal importance is sequencing of reforms. It is good to get the basics right first and attempt more sophisticated reforms after. Importance of clear and realistic implementation strategies, political mandate, realistic timelines and good project management can hardly be over emphasized.

OECD Countries that receive a high score have created a comprehensive, government-wide framework for developing performance information (evaluations and performance measures), integrating performance information into budget and accountability processes, using it in decision making, and monitoring and reporting on results. It does not capture how successful these frameworks are.

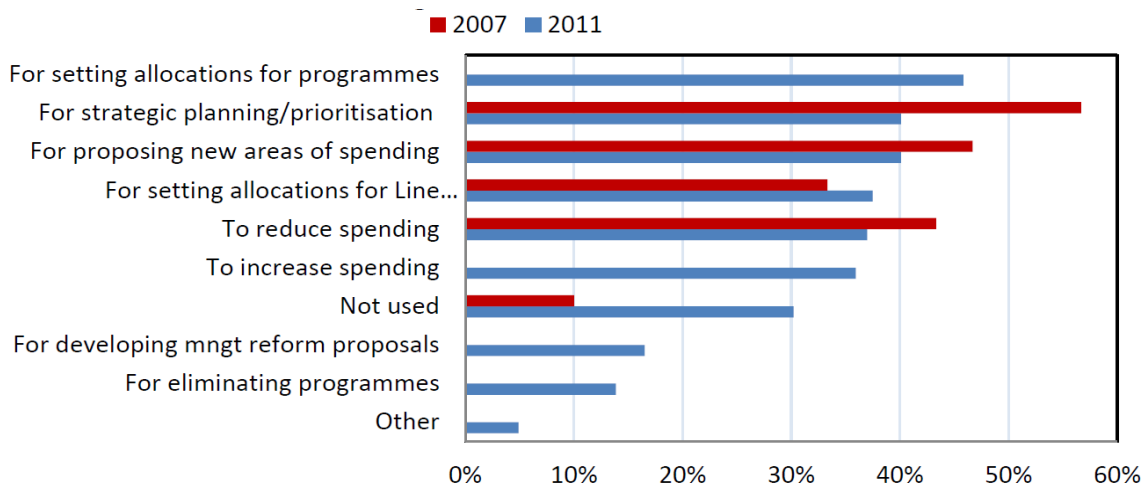
Figure 2: OECD Performance Budgeting Index (2011)



Main findings from 2011 OECD Performance Budgeting Survey show that (please see figure 3 below):

- In negotiations between line ministries and Central Budget Authorities (CBA), 2011 results suggest that performance information is generally used less for strategic planning and to a growing extent not used at all.
- Compared to 2007, results in 2011 show an increase in the role of Line Ministries and agencies as the main institutions responsible for setting performance targets.
- Performance budgeting frameworks are abundant in the OECD, but are generally flexible and not linked with allocation decisions.

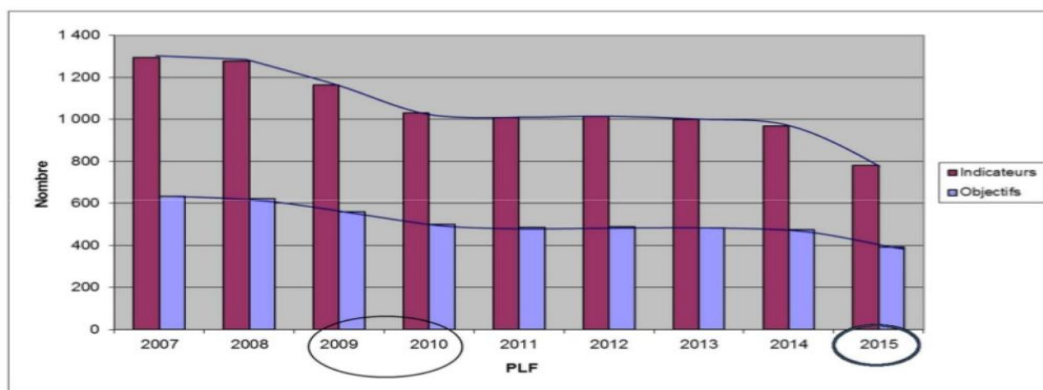
Figure 3: Recent Trends in OECD Countries



- d. Performance budgeting is generally a decentralized practice within the central/federal government.
- e. Line ministries all generally use performance information to increase spending and to reduce it and for strategic planning in negotiations with CBAs.

It was observed that between 2010 and 2015, a noted decrease in the number of objectives and indicators included as part of France's performance budgeting framework (LOLF); this is indicative of a larger trend as has been seen elsewhere.

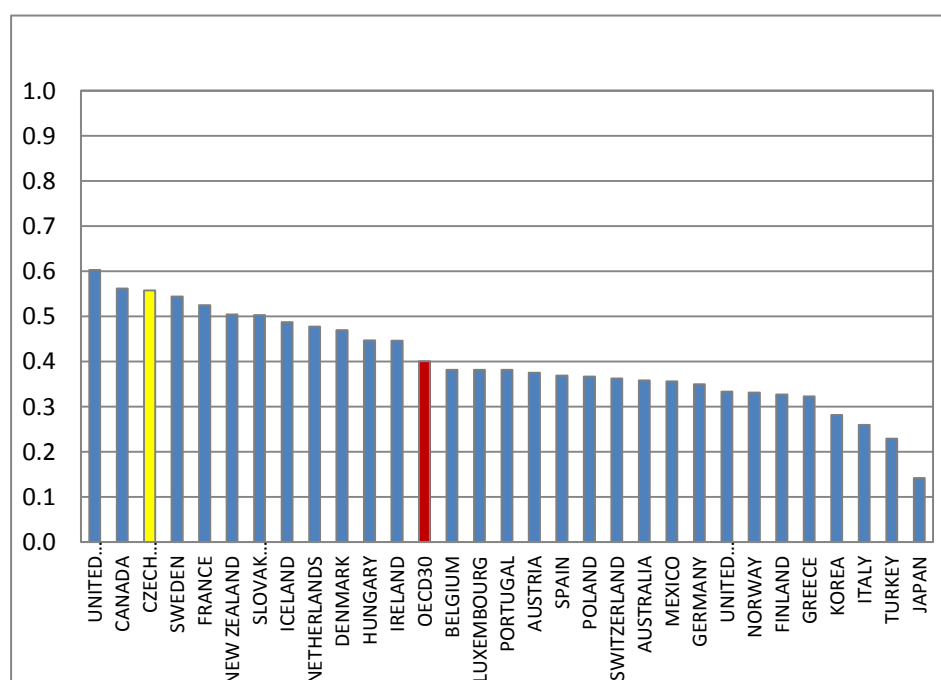
Figure 4



Source: Veronique Fouque, "Performance Budgeting: The French Experience," Presentation to the OECD 10th Annual Performance and Results Network Meeting, Nov-24-25, Paris, France.

The principle of 'Let the manager's manage' is central to performance budgeting, which means that there is considerable flexibility and autonomy vested with the line ministries and agencies.

Figure 5 - OECD Executive Budget Flexibility Index



3. Case Studies – Chile, South Korea and South Africa²

3.1 South Korea

There had been no major reform in PFM area since the Budget and Accounts Act of 1961, which was based on line-item budget classification. It was focused on resource mobilization to meet the given policy priorities with output-based monitoring rather than on developing policy priorities based on monitoring and evaluation. The pre-reform budget system was characterized by an annual, detailed bottom up and largely incremental budget process that was ineffectual in managing the transformation of public expenditures and redirecting spending.

Initial impetus to reform came from the 1990s financial crisis. Also it was driven by long-term concerns, particularly the need to make fiscal space to manage rising social spending costs. Increasing government debt, aging population and increasing demand for social welfare were other factors that added to the sense of urgency to budgetary reforms.

There were other contributing factors as well. Aspiration for reforms within the central budget office, support from civil society, in particular, strong support from academics and expert groups, played a critical role. Political need of the new government in shifting resource allocation to the new policy areas was equally significant in giving a push to the reform process.

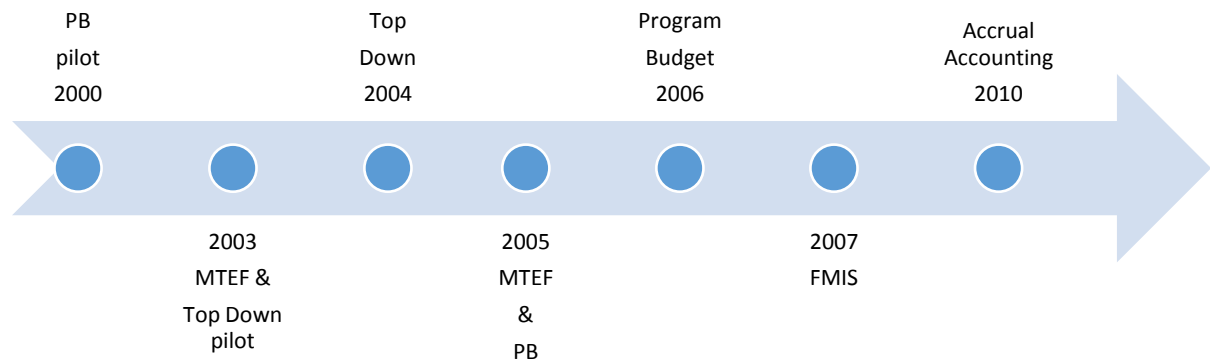
The reform was spearheaded from the center by the former Ministry of Planning and Budgeting (now Ministry of Strategy and Finance) and the President's office. It followed a '*big bang*' approach with the following multiple public finance reform initiatives rolled out fairly rapidly:

- a. A National Fiscal Management Plan (MTFF)
- b. MTEF
- c. Top-Down Budgeting
- d. Performance Management
 - Changes to the program budget structure
 - Developed strategic goals and indicators
- e. IFMIS
- f. Accrual Accounting

The time frame of their implementation was as shown in the figure 6 below:

² This section is based on presentations by Mario Marcel, Senior Director, Governance Global Practice, The World Bank, Mr. Park, No-Wook, Director, Center for Performance Evaluation & Management, KIPFP, South Korea and Mr. Robert Clifton, Senior Technical Advisor, Government Technical Advisory Center (GTAC) South Africa.

Figure 6



The approach taken to program budgeting was very pragmatic. The program structure was made to conform to the existing organizational structure. Programs generally corresponded to office/bureau level, while sub-program corresponded to team level. Thus, a practical approach was adopted to match budget execution unit and budget classification. Another key aspect of the approach was there were no crosscutting programs i.e. programs cutting across different departments or agencies. Also there was no attempt at distributing overheads to programs. Instead, a separate administration and support program was created. Numbers of activities were also reduced to facilitate in-depth, policy oriented analysis (~ no more than 10/program).

Table - 1

Old Structure		New Structure	
Budget Accounts	25	Expenditure Areas/Functions	12
Sectors	79	Sub-Functions	66
Expenditure Accounts	977	<i>Programs</i>	<i>About 1300</i>
Appropriation Accounts	2337		
Sub-Accounts	7,918	Activities	About 7000
Line Item	49	Objects	Less than 10

Example of Korean Ministry of Environment New Budget Structure is shown in figure 7 below:

Figure 7

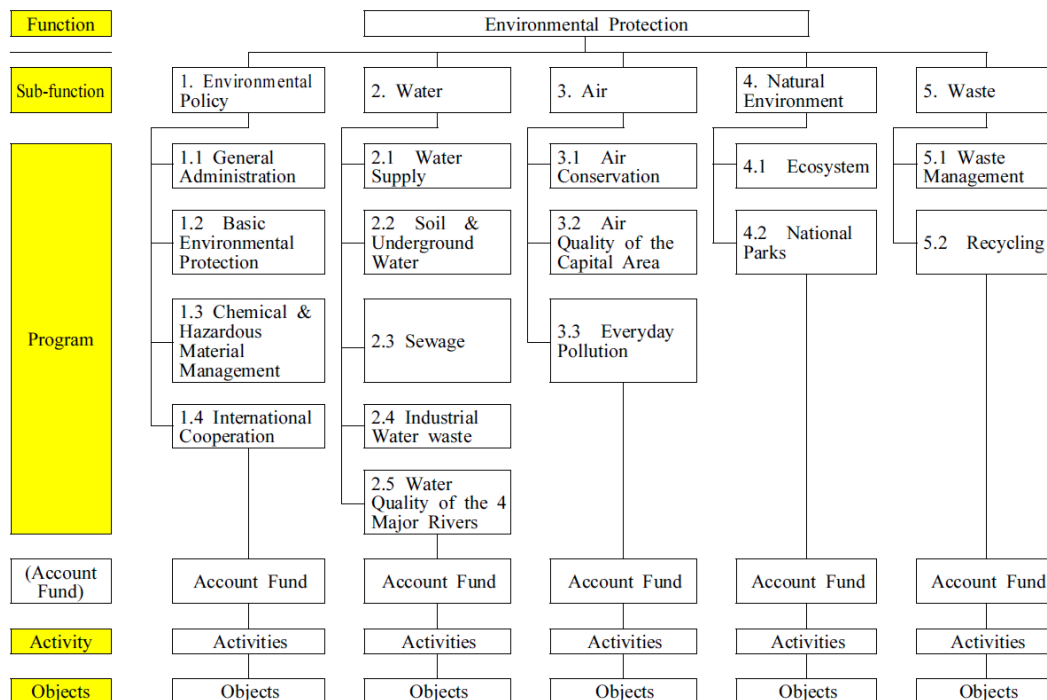
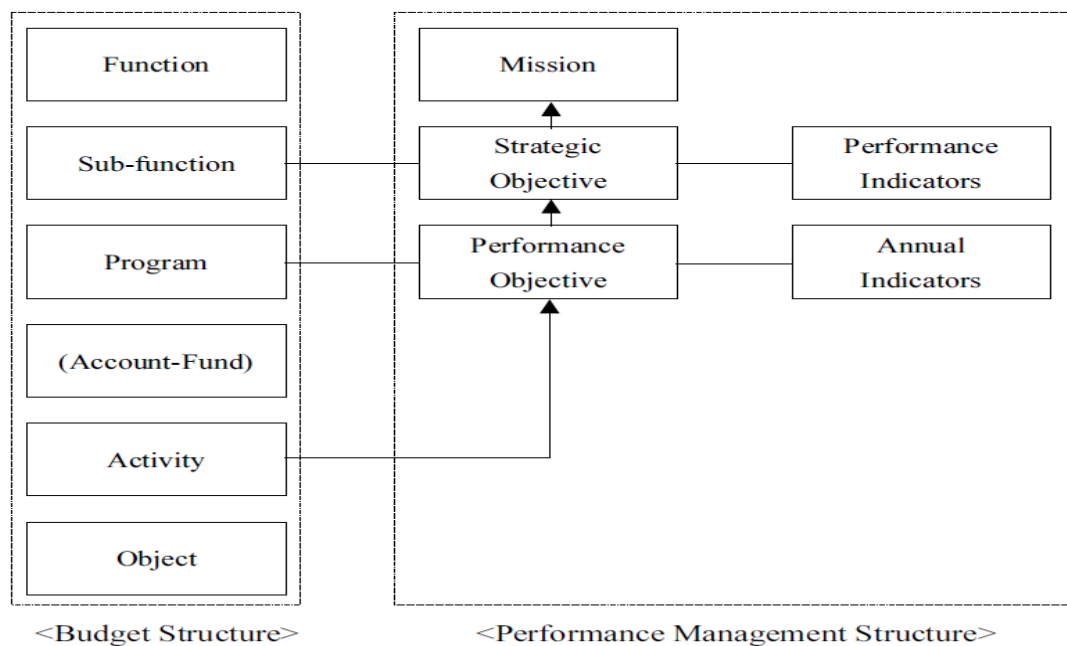


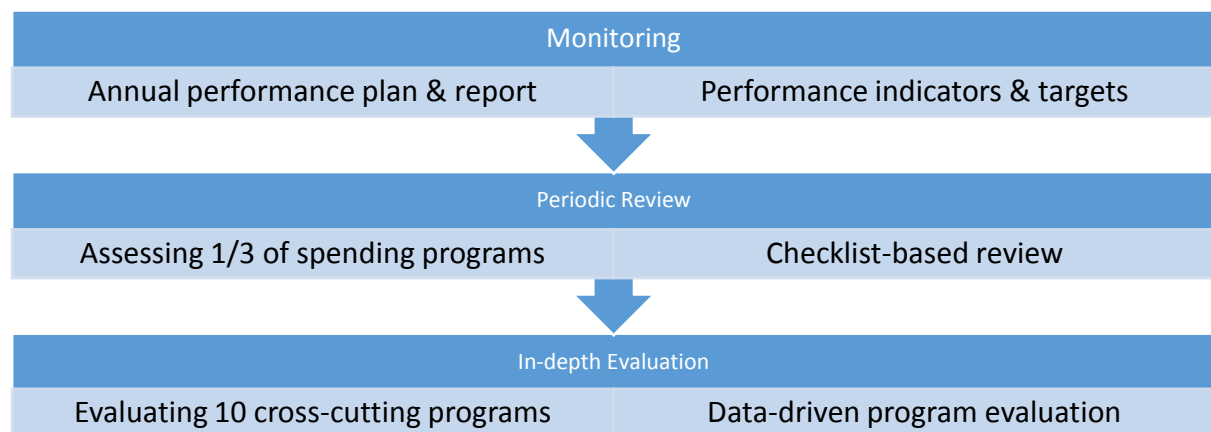
Figure 8 below shows how the program information and performance information was integrated in the budget.

Figure 8



It is obvious that a budget informed by performance or results would use performance information to not only suitably change allocations to more effective and efficient programs but also take corrective action in respect of programs that are important but are not performing well. This implies that there is an established system to collect performance information and carry out performance reviews. Korea had established a three layer system of performance review.

Figure 9



While information from monitoring system (performance plan and report) has not been systematically utilized so far, information from review system is actively used in budget negotiation process. Programs rated as ineffective faced danger of suffering budget cut. Information from program evaluation was found to be usually useful although their use in budget process depends on the quality of evaluation and the will of central budget authority.

Table 2 - Program Review Results

No. of Programs, %

Year	Total	Effective	Adequate	Ineffective
2008	384 (100)	55 (14.4)	226 (58.9)	103 (26.8)
2009	440 (100)	36 (8.2)	311 (70.7)	93 (21.2)
2010	552 (100)	26 (4.7)	393 (71.2)	133 (24.1)
2011	482 (100)	33 (6.8)	317 (65.8)	132 (27.4)
2012	474 (100)	32 (6.8)	330 (69.6)	112 (23.6)
2013	597 (100)	29 (4.9)	424 (71.0)	114 (24.1)

It is important that a reform of this magnitude and significance is driven by a dedicated team adequately authorized with a champion fairly high in the hierarchy. Korea did well to create a small-sized reform team of 5 members reporting directly to

vice minister of MPB on a daily basis. The Vice minister directly reported to president. The team was supported by a research center - Center for Fiscal Analysis – established within Korean Institute of Public Finance (KIPF). The CFA conducted research on PFM reform programs and provided consulting and training services.

Strategic communications was required to overcome resistance within the central budget authority which feared loss of power and control with changes. This was done by:

- a. Sending signals showing support from the presidential office
- b. Providing incentives to line ministries
- c. Promising increased autonomy with top-down budgeting in return for outcome-oriented performance budgeting
- d. Soliciting participation from general public
- e. Establishing the Reporting Center for Budget Waste³
- f. Working with experts, academics and CSOs
- g. Gaining legitimacy by working with international organizations
- h. Seeking support of international organizations to provide opportunities to share best practices among countries

Capacity building of stakeholders was an important element of the reform exercise because best laid down plans would fail if the reforms by the key stakeholders do not understand the essence of reforms underway. Extensive training and consulting programs were organized for line ministries with the help of KIPF. The budget office in line ministries was upgraded by elevating its position from team level to bureau level transforming them from the conveyors of budget requests to budget formulator within line ministries.

There was a major cultural change in Ministries. Monitoring and evaluation activities became essential elements of program design and management. Many big programs set up M&E systems. In particular, subsidy or grant programs were implicitly required to operate M&E system. Performance contracts were tried in some programs to improve program performance. The initial evidence showed big improvement in

³ Through the Budget Waste Report Center citizens can report any suspected cases of budget waste using an online form or a telephone hotline. Citizens can suggest creative ways to save budget resources. Retired Budget Officials manage the hotline, sending cases to relevant departments. Advertising has been used to increase awareness and encourage participation. Public participation in auditing takes place in three ways. Citizens are encouraged to suggest what public entity should be audited. They can request the audit board examines any reports of impropriety and can gather to collectively request audits, not only on budget waste, but also on delays in program implementation and completion and unreasonable public policy. In 2012 the budget office launched its first contest to gather creative ideas from the public on new fiscal projects. A total of 866 ideas were submitted and 12 suggestions were reflected in the budget. [Source: World Bank, PREM Notes]

performance. However, contract management capacity remained an issue to be addressed.

A reform of this size would definitely have some unexpected challenges and require some compromises and adjustments. Lack of cooperation from the central budget office was one of them. Lack of clear ideas about PB implementation and uncertainties over technical difficulties also posed major challenge. Technical difficulties of accrual accounting, for instance, resulted in delaying its implementation. Sometimes power struggle over ownership also meant delicately balancing various interests.

3.2 South Africa

A major feature of PFM reforms in South Africa was the extended time horizon for rolling out all of them across national, provincial and local levels. The following table gives an idea of the scale of reforms and the timelines.

Table 3

Year	Government Level		
	National	Provincial	Local
1998	Medium- term Expenditure framework		
1999	Public Financial Management Act		
2002	Estimation of National Expenditure with budget programmes and measurable objectives	Budget Statements with budget programme and measureable objectives	
2003			Municipal Finance Management Act
2004			
2005			
2006	IFMIS Initiated		
2007	Key Performance Indicators in Estimates of National Expenditure	Uniform programmes and KPIs	
2008	Framework for Managing Programme performance Information		
2009	Standard Chart of Accounts update Capital Budgeting Unit		
2010	Review and Refine Budget Programmes		Local Government Budgeting (norms and standards) and financial reporting (standard chart of accounts)
2011			
2012	SAI Audit of predetermined objectives		
2013		Publication of Provincial Performance Data	
2014	Performance and expenditure reviews		
2015	IFMS Restarted		

Programme budgeting was informed by strategic planning in that strategic goals for institution became its outcomes; and strategic objectives its outputs for programmes. Each entity was required to clearly state what it intends doing (or producing) to

achieve its goals. It described things the institution is directly responsible for doing or delivering under its respective programmes and sub programmes.

Each programme had performance indicators and related targets and on-going performance was tracked. Key performance indicators were aligned to national outcomes indicators. Targets were given for each of 3 years of MTEF. It indicated how budget and MTEF allocations contribute to the realization of the institution's goals

3.3 Chile

The objective of programme budgeting was to improve effectiveness of policy-making and management; create performance incentives for civil servants and make the budget results-oriented.

Overall, it consists of five elements:

- a. The Strategic Framework
- b. Performance Indicators and Targets
- c. Evaluation
- d. Process for Presenting and Appraising
- e. Performance Incentives

While performance information was used in the decision-making process in order to improve efficiency in public expenditures, it was not a mechanical exercise. It was used together with other categories of information, factoring in political priorities and financial constraints.

Programme budget was presented to the Congress along with the Budget Law. Since 2001 public agencies present their indicators and their goals during budget preparation. This aims at telling how a government organization is performing over time.



Dr. Subir Gokarn chairing the first Technical Session

Performance is measured in different dimensions (effectiveness, efficiency, economy, service quality) and at delivery levels (process, output and outcome)

Some of the common points that emerged from these three experiences refer to the importance of

a democratic form of governance, presence of a long term perspective and the necessity of in-built systems for review, monitoring and performance assessment to the practice of budgeting. The Chair of the session on international experiences, Mr. Subir Gokarn from EMC, pointed out another commonality that existed in the form of the presence of some kind of ‘insulated team’ during the phase of transition that remained undisturbed by political shifts and allowed the reform to take roots. He, however, also highlighted the need for also reviewing the failed attempts – it would be important to know why many countries failed in their attempts to introduce performance or program budgeting. The presentation of successful cases alone may bring in ‘survival bias’, and to that extent may hide the issues that those who do not succeed face.

4. Indian Experience with Budgetary Reforms⁴

As mentioned in the introduction the budgetary reforms were not mainstreamed in India. They remained outside the budget law and were merely add-ons. Performance budget earlier and the outcome budget since 2005 are brought out as additional documents and placed in the Parliament while the budget that is voted continues to be the traditional line item budget. Since 2009, the government departments have been preparing what is known as ‘Results Framework Document’ (RFD), which is supported and monitored by the Performance Management Division under the Cabinet Secretariat. The RFD seeks to focus on results that each department seeks to achieve. It is a kind of an agreement on performance signed off by the department, which is reviewed at the end of the year.

The outcome budget and the RFD demonstrate the importance the government attaches to results or outcomes. However, both these reforms fall short of the professed objectives for various reasons including the fact that they are not mandated by budget law and remain documents also placed in the parliament. As for the outcome budget, the main flaw is it is a *post facto* exercise and does not serve the purpose of expenditure prioritization or performance based budgeting; nor is the actual expenditure reviewed with reference to performance and suitable corrective action taken. The document merely recognizes that all budget lines (schemes) have outcomes. The RFD, on the other hand, is not connected with the budget. Its emphasis is on accomplishment of activities considered necessary for achievement of the results. In that sense, it focuses more on activities rather than results.

The other major reform began with the Government of India appointing a committee to review the chart of accounts – known as the list of major and minor heads, which

⁴ This section is based on presentations by Mr. Marc Robinson, Mr. Srinivas Alamuru, Mr. Vijay Ramachandran and Prof Pinaki Chakraborty

have seen little change in the past more than six decades. The chart of accounts (COA) is a critical element of the Public Financial Management framework for classifying, recording and reporting information on financial plans, transactions and events in a systematic and consistent way. [IMF Technical note]. The main purposes that a CoA serves are:

- a. Records transaction level data
- b. Enables financial accounting in accordance with prescribed accounting standards
- c. Enables budgetary accounting in compliance with the financial management regulatory framework
- d. Promotes management accountability by providing interfaces with performance (non-financial) information
- e. Enable efficient mobilization and use of financial resources

A chart of accounts may additionally be designed to provide information on sources of funding; particulars of budget holder; geographical area where it is spent; the recipient of funds; and targeted group of beneficiaries (children, women, disabled, etc.).

The existing chart of accounts, which is a single dimensional accounting classification system, has many drawbacks. To list a few major ones – the single dimensional hierarchical classification imposes severe limitation on viewing accounting data from different perspectives. The functional classification mixes up with economic classification (revenue and capital expenditure are identified at functional level). There are far too many ‘functions’. Function (major Head) and sub Function (minor head) would number about four hundred. The second layer i.e. the minor head which was expected to represent program more often represents a type of activity such as training, (procurement of) machinery and equipment; or an organizational unit. More often than not, a program is actually a scheme e.g. National Rural Health Mission, Sarva Siksha Abhiyan or National Rural Employment Guarantee Scheme. The economic classification (object heads) in the present CoA, does not provide for accrual accounting and is not GFMS 2011⁵ compliant.

The committee appointed by the GoI proposed a seven dimensional classification structure in 2010. The committee left the program segment (one of the seven segments) to be developed by the Budget Division, which has, with the assistance of

⁵ GFMS provides for a) uniform classification for budget and accounting; b) standardized groupings and definitions; c) seamless reporting for national statistics; d) Flexibility for migration to IPSAS accounting standards; and e) Well structured coding patterns facilitating configuration of IFMIS G/L

the World Bank⁶, prepared detailed guidelines for the programme classification and programme classification for ten line departments.

The starting point for the exercise in developing a new programme classification was recognition of basic premise underlying the new classification system – that is, going forward budgeting would be based on programs rather than line items. The programme budgeting implies a paradigm shift as discussed in section 3 above. As recommended by the Rangarajan Committee on Efficient Management of Public Expenditure it brings ‘..... some level of budgeting and accounting that relates to broad objectives of the Government ... to which eventually outcomes can be linked’. The essential difference is that budgeting would be based on outcomes and outputs, and not incrementally increasing allotments year-on-year.

The program classification guidelines laid down the basic rules for classification. The problems in the existing CoA arose partly because there were neither such rules prescribed nor any standard definitions of output, outcome, programme, etc. Programmes are defined as groups of services (outputs) provided to external clients i.e. community / groups of citizens; and, which have a common policy objective; e.g. educated students, patients who recover from illness, etc. Outcomes and outputs are clearly distinguished. Outcomes are changes in pre-existing conditions - for example, state of literacy, maternal mortality, etc.

The ten pilots conducted by the Budget Division amply demonstrated the usefulness of concept of programme as the basis for budgeting. It was also observed during the pilots that in course of time some rationalization of allocation of business rules might be required to bring organizational structures to align with programs.

Implications of acceptance of Fourteenth Finance Commission Recommendations

Implications of central government’s acceptance of Fourteenth Finance Commission (FFC)’s recommendations concerned a large number of states. The implications go beyond the short term adjustments to more lasting budgetary practices. There was considerable interest in the subject and discussion on this subject following a presentation by Prof. Pinaki Chakraborty from NIPFP.

Over the years, the centre–state relations came to be largely characterized by:

- Increase in the share of conditional transfers
- One size fits-all-CSS.
- One size-fits all FRBM.

⁶ A team from the World Bank (including Mr. Marc Robinson, International Consultant) assisted the Budget Division in this task under a Non-Lending Technical Agreement in 2013-14.

States were unanimous in their views on reducing the conditional transfers and for rationalization of CSS and their reduction. They also demanded flexibility in FRBM framework and argued for a framework for credible fiscal adjustment at the Union level.

On the other hand, the Union Government wanted the vertical devolution be kept at the level recommended by XIII FC. It argued for conditional grants on the ground of externalities and horizontal equity and corresponding fiscal space for the Union Government. It sought making adequate provision for the committed expenditure of the Union.

The FFC on its part took aggregate view of transfers: both plan and non-plan and aggregate view of expenditure: plan and non-plan. Aggregate transfers vis-à-vis FC transfer became an important consideration. Since aggregate transfer was more than two-third of the divisible pool of taxes and tax devolution was only 32 per cent, a structural shift in the composition of transfer became necessary. Issue of proliferation of conditional transfers raised by the states was found validated when an aggregate view of transfer was taken.

What fundamentally changed after FFC was that:

- FC-transfer has become the primary mode of transfer of resources as envisaged in the Constitution (More than 70 per cent of the transfer would be through FC-route).
- Union government has been provided with adequate fiscal space for its own specified functions in the Union list. But intervention on state subjects through various tied grants have been reduced due to increased tax devolution.
- FC-XIV recognizes the fact that all conditional grants are not bad and adequate fiscal space has been provided to the Union government to have programmes that are nationally important and for externality reason. But that has to be done in the framework of co-operative federalism.



Mr. Vijay Singh, Adviser, EMC, Mr. Marc Robinson, Dr Jyotsna Jha, Director, CBPS, Mr. Arunish Chawla, Joint Secretary, MoF and Mr. Srikanth Baldi, Principal Secretary, Finance, Himachal Pradesh participating in the panel discussion on key take-aways at the end of first day

Undoubtedly this kind of shift is desirable in the context of fiscal federalism. However, the change - a huge reduction in conditional grants coupled with additional unconditional transfers that would lead to major reductions or enhancement for various states - has been introduced without any warning and without a roadmap. The budget for a large number of centrally sponsored programmes, especially in the social sectors such as education, health, women's empowerment and children, has been drastically reduced. Consequently, the states that are likely to face greater deficit due to change in fund-transfer formula would face the immediate pressure of either reducing the budgets or reallocating from other sources. Even states, that are not likely to face any deficit, need to plan and distribute their resources judiciously, and the challenge is to withstand the pressures from competing demands for allocations. The research in the past has suggested that though tied, the guidelines of the centrally sponsored schemes often helped in facing the political pressures of diverting the funds to unproductive investments.

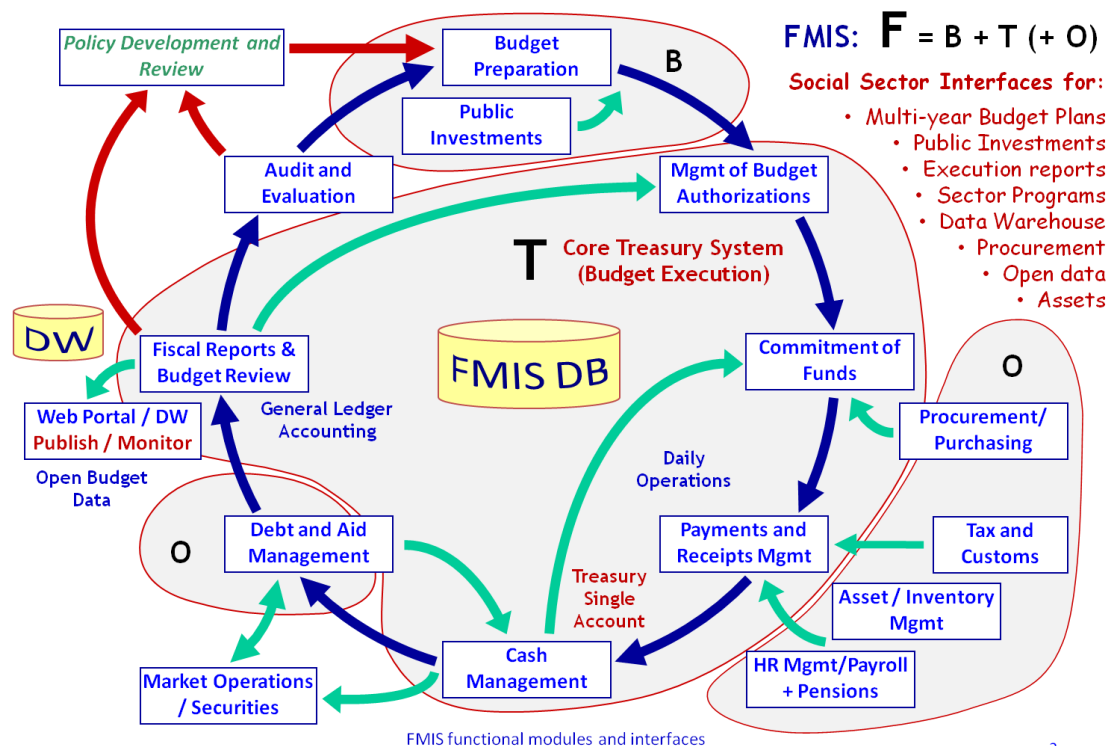
From the perspective of budgetary practice at the State level, although in the short run, it may cause major upheaval, in the long run, there is an urgent need to link outlays to outcome. FFC emphasized formulation of appropriate indicators for measurement of outputs, specification of standards and costs, and establishing a suitable accountability framework. The states also need to work on fiscal reform in terms of expanding the revenue base and increase the fiscal space both by attaining efficiencies and expanding the revenue sources. In any case, with increased untied transfers from the union government, the states need to ensure optimal allocation of resources across department, especially while ensuring adherence to the fiscal deficit target. Departmental Medium Term Expenditure Framework and transition to accrual accounting are also some reforms that require immediate attention. In this context, the issue of capacities acting as a constraint also emerged as a major issue that needs to be addressed in the context of perspective planning and programme budgeting.

5. IFMIS – International perspective and Indian Experience⁷

Whenever Financial Management Information System and other Public Financial Management (PFM) information systems (e.g. HRMIS/Payroll, Procurement) share the same central database to record and report all daily financial transactions, offering reliable consolidated results for decision support, performance monitoring and web publishing, they are referred to as an 'Integrated' FMIS (or IFMIS) as the figure 9 shows.

⁷ This section is based on presentations by Mr. Cem Dener, Governance Global Practice, the World Bank, Mr. Park, No-Wook, Director, Center for Performance Evaluation & Management, KIPFP, South Korea, Mr. Robert Clifton, Senior Technical Advisor, Government Technical Advisory Center (GTAC) South Africa and Mr. Subodh Mathur, Additional Controller General of Accounts

Figure 9



Initial PFM reforms generally concentrate on establishing well functioning Treasury/FMIS, Tax/Customs, HRMIS/Payroll, and other e-Governance platforms for automating core PFM functions. In most cases they exist on fragmented ICT solutions as they get developed piecemeal over time. In the next generation IFMIS Solutions are designed to combine PFM operational systems with powerful data warehouse capabilities and multi-dimensional analytical queries to assist in effective forecasting / planning, performance monitoring, decision support, and citizen engagement (integrated e-Services). There is a growing interest and demand in using Integrated Solutions for the disclosure of public finance and sector specific information as Open Data, as well as the improvement of Information Management and Public Service (G2C, G2B, G2G) delivery.

Many governments, however, still do not see technology as a collaborative means to shape public governance outcomes. A ‘business as usual’ approach to technology that reinforces existing internal government processes only leads to failed projects and public criticism. The challenge is not to introduce digital technologies into public administrations; it is to integrate their use into public sector modernization efforts. There is a need to use technology to improve government accountability, social inclusiveness and partnerships and creating a data-driven culture in the public sector.

Transition to IFMIS in India has been slow. At the State level, a number of solutions exist to support core budget preparation, execution, accounting and reporting functions. Some of the State Level IFMIS platforms provide budget performance reporting and visualization tools for citizens. Khazaane-II being implemented by Karnataka and the off-the-shelf software (SAP) being implemented by Andhra Pradesh State are based on ERP model (with a data item being entered into the system only once ensuring single source of truth) and involve fair degree of process automation. Some interesting features of these applications and those from a few other states are given below:

Andhra Pradesh

- Commitment Accounting - budgeted amount is reduced by the amount of bill at the time of its preparation itself that precluding any excess expenditure.
- It integrates budget, revenue, expenditure, accounts, debt and investment management modules.

Karnataka

- Ninety percent of government payments are made through e-payment mode
- Automated bill processing and presentation using digital signatures
- There is also a proposal to use a single bank account (for some large schemes such as NREGS) on which various implementing agencies will draw cheques with the support of core banking system. This will help avoid idle cash sitting in multiple bank accounts and also improve efficiency of spending.

Madhya Pradesh

- Almost 99 percent of payments are made through e-payment mode. Total 5.8 crore e-transactions done by treasury system (since 2009)
- Entire budget system is computerised
- Introduced global budget lines i.e. for some budget lines, the DDOs are mapped which enables them to draw funds on the budget without sub allocation by the Budget Control Officer. This has resulted in huge savings in workload.

Rajasthan

- Operational since April 2012, monthly salary payment to around 5.50 lakh employees and all payments relating to third parties, TA and Medical Bills, Grant in Aid Bill, scholarships, Anganbadi workers, service providers, etc. are being made through e-payment mode. It handles a volume of 20 lakh transactions per month

At the Union level, transition to IFMIS is still at conceptual design stage. There is, as compared to the states, less integration with many systems in a stand-alone mode not connected to other modules. Budget and HRMS are not fully computerized and integrated with other modules. Currently, the Public Financial Management System (PFMS) supports funds monitoring, e-payments, and reporting functions through a web-based application. e-Lekha provides consolidated information on all payments and receipts.

IFMIS – South Korea Case Study

As mentioned in section 3.1, South Korea adopted a big bang approach to PFM reforms. IFMIS was part of a slew of reforms undertaken by the South Korean government at one go.

As is the case with the systems that develop bit by bit and in isolation, the FMIS in South Korea were fragmented too. There were several systems serving different clients without all of them being tied together.

- a. Fiscal Information Management System (FIMSys) in the Ministry of Planning and Budget
- b. National Financial Information System (NaFIS) in the Ministry of Finance and Economy
- c. E-procurement system
- d. National Tax Revenue System
- e. Local Financial Information System in the Ministry of Public Administration
- f. Local Education Financial Information System in the Ministry of Education
- g. Defense Financial Information System in the Ministry of Defense

A brief history of IFMIS development in South Korea shows that South Korea has been able to develop and deploy the IFMIS in a relatively short period of three years because it has used commercial off-the-shelf software i.e. dBrain.

Improvements on many fronts were noted after implementation of IFMIS. It was observed that budget execution has become easy and convenient. Monitoring in real-time through Performance Information (PI) Board has been another major gain from IFMIS. User convenience and transparency has improved and reduced the number of accounting frauds. Providing financial information to the National Assembly and others has become easy and efficient.

Some key factors contributing to successful implementation of IFMIS in South Korea were:

- a. Strong commitment from high-level decision makers
- b. The reform team's adaptive capacity to overcome challenges
- c. Strategic communications with stakeholders
- d. Capacity building among stakeholders
- e. Compromise between all-inclusive ambitious reform agenda and actual implementation

IFMIS – South Africa Case Study

The South African experience has been vastly different from that of South Korea.

Currently there are four major systems maintained by the National Treasury viz. Personal and Salary Administration System (PERSAL), Logistical Information System (LOGIS), Basic Accounting System (BAS), and National Treasury also maintains a Management Information System (Vulindlela). These various systems are managed as separate stand-alone applications and not as a single integrated systems unit. Apart from these legacy systems, certain national and provincial departments have acquired a number of software solutions that are operated and maintained as separate "sub-systems". Over time, a number of interfaces have been developed between the legacy systems and the "subsystems" (100 interfaces with BAS).

The IFMIS implementation in SA can be seen three phases. The first phase began in 2005 with Cabinet giving a go-ahead for 5 year IFMS project to be fully rolled-out by 2010. It was a joint project with National Treasury, Department of Public Service Administration and State Information Technology Agency as primary systems integrator. The aim was to provide an IFMS that integrates human resource, payroll, financial and supply chain management and business intelligence functions. The key objectives of the IFMS included:

- a. Replacing aging technologies;
- b. Support implementation of legislation such as the Public Finance Management Act and Public Service Act;
- c. Improving service delivery by automating and standardising processes;
- d. Achieving interoperability, security, economies of scale and elimination of duplicated IT systems; and
- e. Improving quality of data and ease of access thereof within a secure environment

The project was approved with hybrid solution architecture. Commercial Off-The-Shelf (COTS) modules included Human Resource Management and Supply Chain

Management Procurement Management; and bespoke modules included Financial Management, Payroll and Supply Chain Management.

In preparation for the transition to the IFMS, Cabinet approved that all legacy systems continue to be managed as per the status quo at the time, until migration to the IFMS was considered feasible. In addition, a moratorium was placed on the acquisition of new Financial Management, Supply Chain Management, Payroll, and Human Resource Management systems by departments.

By 2013 it was seen that while HR Management, Asset Management, and Procurement Management components had been delivered and installed at a few national and provincial government sites, Inventory Management and Financial Management components had not been completed. Service provider for the development of the bespoke Payroll system has not been appointed. Applications were not integrated, apart from partial integration with legacy systems at lead implementation sites.

The second phase began in 2013 with a rethink on the IFMS architecture. After completing intensive consultations with key stakeholders and completing lengthy deliberations from various vantage points, the IFMS Steering Committee recommended the adoption of a COTS solution. Subsequently, Cabinet approved the revised solution architecture in 2013. The intention is to implement a so-called ‘vanilla’ COTS solution where customization changes to the system are kept to an absolute minimum. It is proposed that procurement of the single COTS solution will be overseen by the IFMS Steering Committee and it will ensure that the procurement of software, licenses and services are in compliance with the Government procurement prescripts and conducted in the most efficient manner. It is expected that the IFMS with fully reengineered processes will roll out by 2021.

Key challenges encountered by SA were:

- a. Poor organisational readiness to adopt and operate modules
- b. Constraints and institutional capacity to acquire, develop, enhance, and integrate inclusive of enhancing transversal contracts functionality to meet business requirements
- c. Unsigned key documentation such as User Requirements Specifications, Project Charter and Concept of Operations
- d. Availability of users to conduct product user acceptance testing
- e. Delay in identifying ownership of master data and establishment a master data governance office
- f. No agreement by SLA Committee operationalisation costs

The key lessons learned were that the programme proved to be more complex than originally envisaged. Longer than planned procurement and contract negotiation processes stymied the implementation. Lack of sufficient capacity in key stakeholders and poor understanding by different stakeholders of respective limitations and requirements also adversely impacted the execution.

6. Way Forward for India

The PFM reforms have been few and far between as far as India is concerned. While there could be a more ambitious reform program as attempted successfully by South Korea, there are three reforms that have been already recognized as necessary at various levels over the past few years. They are:

1. Performance based budgeting
2. Revamping of Chart of Accounts
3. Implementation of IFMIS at the state and union level

These are discussed in turn below and some possible immediate steps required are listed based on the international experience in the field.

That a strong case is already made for performance based budgeting is quite evident from the fact that GoI has considered introducing ‘outcome’ budget and the RFD. Besides, several committees and the Fourteenth Finance Commission have also strongly recommended linking outlays with outcomes. Even the Estimates Committee recognizes that *‘(I)n the Demands for Grants, stress is laid on major programmes and activities of the Department highlighting those aspects of the Budget which are important, for an appreciation of the resource allocation at the national level. The information about the activities are covered by way of Notes’*⁸(emphasis added).

The pilots conducted by the Budget Division show that the current minor heads are far too removed from the concept of program and, therefore, a new classification is very much in order. The experience with the pilots also proved that programs defined as a group of activities with a common objective brought greater coherence to the budget. So the first step would be to develop a common program classification for the federal and state governments as is the case now. This, however, cannot be done in isolation as budgeting is intricately linked with the chart of accounts. Fortunately, the Committee appointed by GoI has already recommended a revised classification structure. This could serve as a starting point for further refinement.

The new structure recommended by the Committee has some limitations. To begin the principles for classification have not been clearly laid down. Internationally, the functional classification, budget classification and accounting classification are

⁸ Budget Manual – Government of India

separate and distinct and for a good reason. The functional classification is used for statistical comparisons of budget and expenditure across nations (health expenditure, defence expenditure, etc.) and it is not a part of the chart of accounts. What is required is for functional classification to be made compliant with the UN Classification of Functions of Government (COFOG)⁹ and delinked from the rest of chart of accounts.

The budget classification normally would include only the program-scheme (minor head and sub head) over which Parliament exercises control. In other words, further details of how much expenditure on different items such as salaries, office expenses, etc. is something too detailed for the Parliament to be concerned about. This does not mean that these items are not controlled. They are controlled at a different level – by the finance department and the line departments. The accounting classification captures both the program-scheme level as also the economic classification. Lastly, the economic classification should be in compliance with the GFSM 2011. In short, there is need to urgently revamp the chart of accounts to bring it to internationally accepted standard that would serve the purpose of efficient public expenditure.

IFMIS is a down stream activity so to say as it needs to be based on the revised CoA.

While the budget classification and CoA revision is critical, it is also important that simultaneously, states start developing their capacities on improved planning and budgeting exercises, with an emphasis on understanding the notion of program budgeting. This would also mean developing greater clarity on intermediate and final outcomes for different programmes. Considering that such capacities are currently weak in most states, it makes sense to see this as a challenge and include a plan for addressing this as well in any reform plan.

The above reforms are challenging tasks which require high level commitment and leadership. There is a need for a dedicated unit under the MoF reporting preferably to the Finance Secretary. The core group should have a complement of subject experts, practitioners and experts who should be available for the entire duration as stability of the group will be important for implementation of far reaching reforms of this nature. Importantly, the group should have representatives from the office of C&AG, CGA and from a few state government Finance Departments. The government should be prepared for rolling out the reforms over a period of three to five years. Considering that the current government is only in its second year of its elected tenure, it is an opportune time to take up a reform of this nature.

⁹ COFOG has three levels of detail: a) Divisions- broad objectives of government; b) Groups-means of achieving the broad objectives; and c) Classes-means of achieving the broad objectives

Annex A

[List of Participants – a separate PDF file sent along with this report]

Agenda

Day 1: 19 May 2015:

Budgetary Reforms: Overview, Prioritization and Performance Dimensions

Timing		Sessions	Speakers
9:00	9:30	<i>Registration</i>	
9:30	9:40	<i>Introduction to the Seminar</i>	Dr. Jyotsna Jha, CBPS
9:40	9:45	<i>Inauguration</i>	Dr. Sumit Bose, Member, EMC, Government of India Dr. Rathin Roy, Director, NIPFP Dr. Jyotsna Jha, Director, CBPS Mr. Mario Marcel, Senior Director, Governance Global Practice, The World Bank Mr. Onno Ruhl, Country Director, The World Bank
9:45	9:55	<i>Welcome Address</i>	Dr. Rathin Roy, Director NIPFP
9:55	10:05	<i>Address by Country Director, World Bank</i>	Mr. Onno Ruhl, Country Director, The World Bank
10:05	10:20	<i>Inaugural Speech</i>	Dr. Sumit Bose, Member, EMC, Government of India
10:20	10:30	<i>Tea Break</i>	

First Technical Session: Budgetary Reforms: International Perspective

Panel: Dr. Subir Gokarn, Member, EMC, Government of India (Chair), Mr.K.V.Eapen, Additional Chief Secretary, Planning and Development Department, Government of Assam (TBC), and Mr. Mario Marcel, Senior Director, Governance Global Practice, The World Bank

Timing		Sessions	Speakers
10:35	11:00	<i>Budgetary reforms – Key drivers and sequencing</i>	Mr. Mario Marcel, Senior Director, Governance Global Practice, The World Bank
11:00	11:30	<i>Budgetary reforms - International Perspective</i>	Mr. Marc Robinson, Consultant, The World Bank
11:30	12:00	<i>Budgetary Reform - International Case Studies – South Korea</i>	Mr. Park, No-Wook, Director, Center for Performance Evaluation & Management, KIPFP, South Korea
12:00	12:30	<i>Budgetary Reform - International Case Studies</i>	Mr. Robert Clifton, Senior Technical Advisor, Government Technical Advisory Center

		– <i>South Africa</i>	(GTAC) South Africa
12:30	12:45	<i>Comments by the Panelists</i>	
12:45	13:00	<i>Q & A session and summing up by the chair</i>	
13:00	13:45	<i>Lunch</i>	
13:45 to 14:00 Launch of Community of Practice for PFM			
Fily Sissoko – Practice Manager – PRMM - Governance Global Practice, The World Bank			

Second Technical Session: Prioritization, Performance, and Programme budgeting for India

Timing		Sessions	Speakers
14:00	14:20	<i>Paradigm shift in Planning; what it means to Central Government and State Governments</i>	Ms. Kusum Mishra, Director, NITI Aayog
14:20	14:40	<i>Implication of FFC's recommendations on States Budgetary practices</i>	Mr. Pinaki Chakraborty, NIPFP
14:40	15:00	<i>Budgeting in Government of India – Impact of recent changes in cooperative federalism and linkage to performance.</i>	Mr. Harish Srivastava, Director (Budget), Government of India
15:00	15:30	<i>Programme Budgeting in India- Lessons from Pilot and Way forward</i>	Mr. Marc Robinson and Mr. Srinivas Alamuru – Consultants – The World Bank
15:30	16:00	<i>Classification system – Linkage to Performance Dimensions</i>	Mr. Vijay Ramachandran - Consultant – The World Bank
16:00	16:45	<i>Q & A session</i>	

16:45 – 17:45 Panel discussion: Key takeaways and way forward for budgetary reforms in India

Panelists: Dr. Arunish Chawla, Joint Secretary (PF-II), Government of India, Mr. Vijay Singh Chauhan (Advisor - EMC), Government of India, Dr. Shrikant Baldi, PS-Finance and Planning, Govt. of Himachal Pradesh, and Mr. Marc Robinson, Consultant – The World Bank

Moderator: Dr. Jyotsna Jha, Director CBPS

Day 2: 20 May 2015:**Budgetary Reforms – Other Key Directions for Reform*****Third Technical Session: Budget Management and IFMIS******Panel: PS Finance of States***

Timing		Sessions	Speakers
9:10	9:15	<i>Setting up the context: Role of IFMIS in improving budgeting</i>	Mr. Mohan Gopalakrishnan, Senior FMS, The World Bank
9:15	9:45	<i>IFMIS- an enabler for better performance</i>	Mr. Cem Dener, Senior Public Sector Specialist, The World Bank
9:45	10:15	<i>IFMIS reforms - linkage to improved Budgeting International case study- South Korea</i>	Mr. Park No-Wook, Director Center for Performance Evaluation & Management, KIPFP, South Korea
10:15	10:45	<i>International case study - South Africa</i>	Mr. Robert Clifton, Senior Technical Advisor, Government Technical Advisory Center (GTAC) South Africa
10:45	11:00	<i>Q & A session</i>	
11:00	11:15	<i>Tea Break</i>	
11:15	11:45	<i>Procurement planning in budgeting</i>	Ms. Swayamsiddha Mohanty, Procurement Specialist, The World Bank
11:45	12:15	<i>Public Financial Management System</i>	Mr. Subodh Kumar Mathur, Joint Controller General of Accounts, Ministry of Finance
12:15	12:45	<i>Case studies from Indian States (IFMIS reforms and linkage to improved budgeting)</i>	State of MP
12:45	13:00	<i>Comments by the Panelists</i>	
13:00	13:15	<i>Q & A session and summing up</i>	
13:15	14:15	Lunch	

Round table discussion: Budgetary reforms at State level – challenges and way forward

Participants: PS Finance and PS Planning of states

Timing	Sessions	Speakers
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Timing		Sessions	Speakers
14:15	14:30	<i>Setting up the context: Challenges and opportunities in state budgeting</i>	Dr. Rathin Roy, Director NIPFP
14:30	16:00	<i>Improving institutional environment for strengthening quality of budget and its management.</i>	Round table of PS finance/planning of 6-7 states Moderators: Dr. Rathin Roy, Director NIPFP, Mr. Manoj Jain, Lead FMS, Global Governance Practice, The World Bank, and Mr. Mohan Nagarajan, Senior Economist, Global Governance Practice, The World Bank
16:00	16:15	<i>Q&A Session</i>	
16:15	16:30	Tea Break	
16:30	16:45	Closing Key note and way forward	Mr. Fily Sissoko, Practice Manager, Global Governance Practice, The World Bank
16:45	17:00	Vote of thanks	NIPFP/CBPS

A short note on Spending Reviews¹⁰

What is Spending Review?

Spending review is an institutionalized process for the review of *baseline* expenditure with the primary aim of identifying savings options for consideration in the budget process. *Baseline* expenditure in this context means expenditure on existing programs (existing services or transfer payments) or projects. Spending review is, therefore, not concerned with the budgetary assessment of *new* spending proposals.

Box 1.1. Defining Spending Review: The OECD's Approach

[Spending review is] the retrospective analysis of a programme, policy or organization ... which is commissioned ex ante with a specific objective to identify budgetary savings across government ... [S]pending review can be used to reduce the deficit and/or to make fiscal space for higher priority programmes either through restructuring or cutting activities. While spending reviews can also look at programme effectiveness (i.e., how to improve programme performance and design), their distinguishing feature is the focus on identifying and extracting savings through the budget process.... [There is] an explicit link to budgetary decision-making, both in terms of analysis and recommendations under alternative funding levels (e.g., spending review targets) and in terms of the budgetary process.

Source: OECD 2011, 3.

Why Spending Review?

It is a widely recognized problem that government budget preparation tends to focus disproportionately on the consideration of new spending proposals, with little review of baseline expenditure. This is particularly so where line item budgeting (as against program budgeting) is followed where the current expenditure is incrementally increased from year to year. Spending review—with its specific focus on the baseline expenditure—aims to address this problem.

When expenditure reduction becomes unavoidable, governments generally resort to non specific across-the-board expenditure cuts (the economy drive). A standard percentage reduction to all spending is applied. Spending review seeks to reduce such indiscriminate across the board cuts of spending that adversely affect important and priority programs.

¹⁰ This short note has been prepared on the basis of Chapter on OECD Spending Reviews by Marc Robinson, World Bank for an OECD Publication

Spending Review is a tool not only for reducing aggregate expenditure but also for increasing the room available for priority new expenditure consistent with maintaining a sound aggregate fiscal policy. SR facilitates weeding out ineffective programs and thus helps in re-prioritization.

Although primary focus of spending review is to identify savings that can be realized by improving efficiency or by reducing ineffective or low-priority expenditures, it may also have broader performance objectives. Thus, SR can help improve overall effectiveness of public expenditure. It must, however, be remembered that SR is different from performance evaluation as the former explicitly aims at changing the levels of funding.

Who does the Spending Review?

Spending review is a process that is explicitly intended to feed into budgetary decisions. For that reason, spending review is necessarily a process that is directed and managed—at the bureaucratic level—by the ministry of finance (MOF) (possibly in partnership with any other “central agencies” that may play a key role in budget preparation in particular countries, such as the president’s or prime minister’s office).

What benefits can be expected from spending review?

Spending review can deliver two types of budgetary savings: efficiency savings and output savings. *Efficiency savings* are those achieved by changing the way services are delivered so as to deliver the same quantity and quality of services (outputs) at lower cost — in other words, savings arising from improved technical efficiency. Reduced spending achieved by cutting services does not qualify as efficiency savings.

Output savings — are savings that are achieved by scaling back or eliminating services or transfer payments that are ineffective or low priority. They are referred to as output savings because outputs are services delivered to the community and because output savings involve deliberate and targeted reductions in the quantity or quality of those services.

As noted earlier, savings options identified by spending review are, in principle, specific. This principle means that a government knows how the reduction in baseline expenditure will be achieved—that is, what services will be reduced (in the case of output savings) or what cost-reducing changes to business processes will be made (in the case of efficiency savings). Expenditure reductions achieved through spending review are, therefore, different from nonspecific cuts, defined as cuts that the government imposes on ministries without the ministries knowing in advance how those reductions will be implemented

What does Spending Review involve?

Any spending review process comprises a set of topic reviews. There are three key types of topic review:

- a. *Program reviews*: these examine specific programs (i.e. specific categories of services or transfer payments) and may deliver either efficiency savings (by lowering the costs of delivering services under the program) or output savings (by reducing the services provided by the program) or both.
- b. *Process reviews* scrutinize specific business processes used in the production of government services (e.g., procurement processes, information technology [IT] systems and practices, and human resources management practices). Process reviews aim to achieve efficiency rather than output savings.
- c. *Agency reviews* examine a whole government organization (ministry or other agency) and may in principle cover all of the agency's programs and processes.

Program and process reviews are also referred to as “strategic” and “functional” reviews, respectively (OECD 2011, 3–4). Program or process reviews may be agency specific or they may be horizontal. A *horizontal program review* examines a group of related programs delivered by two or more agencies, while a *horizontal process review* looks at a particular domain of business processes across several (or all) government agencies (e.g., a review of government-wide procurement practices).

Spending review processes never review every government program and every business process, even if governments sometimes describe their spending reviews as “comprehensive.” To do so would be impracticable. The term *comprehensive* should, therefore, not be taken literally. Nevertheless, there is a real difference between comprehensive spending reviews and selective spending reviews.

A *selective spending review* is limited to a specific list of review topics—programs, processes, or agencies—and is set at the beginning of each round of spending review.

A *comprehensive spending review*, by contrast, is a review in which the scope of is not limited by an ex ante list of review topics. Review teams are asked to look at all ministries with the expectation that they will identify, to the extent possible, all of the most important savings options. A comprehensive spending review is expected to have a greater scope—and to yield greater savings—than a selective review.

Spending review processes differ in their coverage (i.e., in the part of government expenditure they cover). Some spending reviews focus only on *budget expenditure* (i.e., on expenditure that is legally authorized in the annual budget law), whereas other reviews also cover *mandatory expenditure* (i.e., expenditure—such as social

security benefits—that is authorized by standing legislation and, therefore, is also known as *statutory expenditure*). Another important coverage issue is whether spending review at the national government level includes national government transfers to sub-national governments such as states or provinces.

Spending review is more than expenditure analysis as it tries to explicitly identify savings options. However, a good SR requires to be supported by a good quality formal expenditure analysis.

Examples of Formal Expenditure Analysis Techniques

The following are some of the expenditure analysis techniques that may be used to support spending review:

Business process analysis: a form of efficiency analysis that is based on the review of existing business processes and their modification so as to lower the cost of delivering outputs.

Cost benchmarking: the process of efficiency analysis that is based on comparing the costs of an output or process with the costs of the same or similar outputs or processes produced by other organizations.

Outcome evaluations: evaluations to ascertain the extent to which an existing program's or project's intended outcomes have been achieved.

Process evaluations: a type of evaluation that reviews program or project implementation, usually with the aim of identifying policy design or management changes to improve effectiveness.

Program logic analysis: a process that looks at the manner in which a particular program or project is supposed to achieve its intended outcome and that asks whether, in the light of relevant theory and experience, it is likely to be effective; also known as *theory-based evaluation* (World Bank 2004, 10).
