

Re-Thinking Approaches to Government Reforms
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Public Expenditure Management as an Instrument of Reform
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Systems to manage scarce public resources are the most powerful management tool available to governments. As a result, attention to the way public resources are allocated and managed can focus, sharpen and accelerate government reforms. But experience to date suggests that these gains can only be realised if public expenditure management reform takes four key factors into account. These are: a disciplined, transparent political process of choice between public priorities; a coherent sense of purpose between core funding ministries and spending agencies; a clarity of leadership and direction; and the sequence with which budget management innovations are introduced.

The systems of Public Expenditure Management (PEM) being introduced in many countries around the world consists of four elements:

- strategic planning to define policy priorities in the light of forecasted resources and macroeconomic and fiscal targets.
- budget formulation within agreed financial limits and the approval of the budget by the legislature.
- spending within the budget, subject to accounting and the monitoring of actual service delivery against expenditure.
- an audit of out-turns by the legislature and often by an external auditor to ensure that funds have been spent as intended and to reassure the legislature and citizens that this is so.

Its objectives are threefold. It enhances macroeconomic stability by specifying a resource ceiling within which public priorities must be financed. This forces the cabinet to choose between priorities and to match resources with its most important objectives. It permits a degree of decentralisation of budget management, providing incentives for budget managers to achieve service delivery targets at least cost. It permits real world public services to be delivered to citizens within predictable budget ceilings.

In order to achieve these objectives the PEM system must be transparent, predictable, accountable, and comprehensive. Transparency requires that taxpayers know how resources will be used and what development results they can expect. Predictability implies the dependable delivery of resources over the medium term, allowing managers to plan and citizens to form expectations of the services they will receive. Accountability ensures that expenditures are made as intended, and that outcomes are consistent with anticipated results. Comprehensiveness ensures that resources are allocated efficiently and that wasteful duplication is avoided.

A PEM system must also promote maximum value for money by inducing an economy in the procurement of inputs, efficiency in the production of outputs for the

least cost combination of inputs, and effectiveness by delivering priority services of the highest quality possible within budget. The greatest value for money is likely to be achieved if budget managers have some flexibility in choosing which combination of inputs will generate the best possible services at least cost. This implies some decentralisation of budget authority.

There is no blue-print for PEM reforms. However, reformers need to take four key considerations into account:

1. The budget is a political process.

The budget process frustrates politicians. They are often tempted not to define policy priorities by reference to available resources. Moreover, while each minister may agree to a reduction of the overall budget deficit, each is likely to be reluctant to see a reduction in his or her own budget deficit. These problems have been tackled in Australia through a Fiscal Responsibility Act.

2. The relationship of central ministries and other departments within a PEM system is crucial to the results of the PEM system.

Central ministries need to be co-ordinated and consistent in order to provide budget predictability. Spending agencies, in turn, should be granted flexibility in the ways they manage the resources granted to them. The agencies should then be held accountable to the central ministries for observing expenditure ceilings and achieving output targets.

3. The management of change is important

A PEM reform requires clear leadership that is prepared to 'stay the course'. Consistency between PEM and other reforms is also required.

4. The sequencing of actions is problematic, but crucial in determining results.

The sequencing of actions in the reform of a PEM system is crucial to the outcomes. Yet sequencing can be problematic. The starting point for reforms should be the weakest areas in the budget process, where the greatest gains from reform can be made. Yet all too often reforms commence only where people become motivated to reform. This may relate to broader incentives and restraints within a society (see note on the first seminar in this series).

The subsequent focus of the reform effort usually determines its impact and whether it is sustainable. Reforms should be driven from whichever organisational unit is best placed to deliver results, not necessarily from the Budget Division in the Treasury or the Accountant-General's department, or the agency that initiated the reform.

The manner in which reforms are implemented also affects their impact and sustainability. In Australia, reforms were introduced very quickly. Many Australian public servants who signed contracts under the Fiscal Responsibility Act were unaware how these contracts would bite later. They had work harder in subsequent

years to meet their targets. The rapidity with which reforms were introduced had a sustainable ratchet effect on efficiency.

Many international aid donors, accountable to their home legislatures and electorates for the effective use of resources, now espouse the introduction of improved PEM within their client countries. What do these issues imply? PEM reforms can be nurtured by observing four principles.

1. The recipient budget is at the centre of the relationship between the recipient government and its donors. Donor grants and loans should appear in the recipient government's budget.
2. Policy dialogue, reviews, funding, technical assistance, monitoring, and training should be designed around the budget cycle.
3. Donor should reinforce the relationships between the central ministries and spending agencies, not to undermine or avoid them.
4. Donors should reinforce government mechanisms and procedures. It is preferable to strengthen and develop the government's accounting and accountability mechanisms than to create parallel donor ones.

Adherence on the part of donor governments to these four principles should encourage the development of more efficient systems of public expenditure management in the recipient countries.

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