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Achieving Quality Outcomes: The Management of Public Expenditure

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ABBREVIATIONS

ASD	Alternative Service Delivery
C&AG	Comptroller and Auditor General
CCI	Chambers of Commerce of Ireland
CDB	County/City Development Board
CIF	Construction Industry Federation
CORI	Conference of Religious of Ireland
CSF	Community Support Framework
CSO	Central Statistics Office
CPG	Corporate Policy Group
CWC	Community Workers' Co-operative
ERI	Expenditure Review Initiative
ESRI	Economic and Social Research Institute
EU	European Union
FMIP	Financial Management Improvement Programme
GDP	Gross Domestic Product
GNP	Gross National Product
GPRA	Government Performance and Results Act
IBEC	Irish Business and Employers Federation
ICMSA	Irish Creamery Milk Suppliers Association
ICOS	Irish Co-operative Organisation Society
ICSTI	Irish Council for Science, Technology and Innovation
ICTU	Irish Congress of Trade Unions
IDA	Industrial Development Agency
IFA	Irish Farmers' Association
IMPACT	The Public Sector Union
IMF	International Monetary Fund
INOU	Irish National Organisation of the Unemployed
ICSTI	Irish Council For Science, Technology and Innovation
ISP	Integrated Services Process
IT	Information Technology
KRA	Key Result Area
MBO	Management By Objectives

MIF	Management Information Framework
NAPS	National Anti-Poverty Strategy
NDP	National Development Plan
NHS	National Health Service
NPC	No Policy Change
NPM	New Public Management
NPR	National Performance Review
NWCI	National Womens' Council of Ireland
NYCI	National Youth Council of Ireland
OECD	Organisation for Economic Co-operation and Development
OMB	Office of Management and Budget
PAC	Public Accounts Committee
PBB	Performance-Based-Budgeting
PCP	Public Capital Programme
PEMS	Policy and Expenditure Management System
PMDS	Performance Management and Development System
PPB	Planning Programming Budgeting system
PPF	Programme for Prosperity and Fairness
PRSI	Pay-related Social Insurance
PSA	Public Service Agreement
RAPID	Revitalising Areas by Planning, Investment and Development
SIPTU	Services Industrial Professional and Technical Union
SOA	Special Operation Agency
SMI	Strategic Management Initiative
SPC	Strategic Policy Committee
SRA	Strategic Results Area
SSC	State Services Commission
VEC	Vocational Educational Committee
VFM	Value for Money
ZBB	Zero-Based-Budgeting

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CHAPTER 1[1]

INTRODUCTION

1.1 MOTIVATION

The Council's interest in the management of public expenditure has been motivated by a number of factors. Firstly, public expenditure in Ireland in 2002 represented around 42 per cent of GNP[2]. This is a substantial share of GNP. The management of these resources, in terms of the process used in allocating resources and the efficient use of any given allocation of resources, has significant implications for the performance of the economy, the quality of life and the achievement of social justice.

Secondly, the Council has been aware of concerns regarding the quality and adequacy of the provision of services in several areas including health and public transport. Problems in relation to the quality of public services raise issues in relation to the appropriate total level of expenditure and issues specific to the delivery of each service. In addition, the problems that have emerged also raise general issues in relation to the process of managing public expenditure. It is these general management issues that are the focus of this report.

Thirdly, there are significant issues raised by the trend in public expenditure since the 1980s. While there were reductions in public expenditure during the late 1980s, there has been significant growth in expenditure during the 1990s. In each case there are questions about how well the system has worked in terms of either cutting or increasing expenditure in the most effective manner possible, where effective is defined in terms of meeting economic and social priorities.

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1 This report was drafted by Noel Cahill, Orla Lane and Colm O'Reardon of the NESC Secretariat.

2 This is based on the European definition of General Government expenditure and includes both central and local government.

Finally, the Council's interest is heavily influenced by the relationship between the overall level of public expenditure and the generation of resources to finance these outlays. The greater the levels of public expenditure, the greater the level of taxation. The right mix of policies in relation to the public finances, as between the level and composition of expenditure and taxation, are of major importance to the economy.

1.2 OUTLINE OF REPORT

To provide context for the issues considered in this report, Chapter 2 provides a statistical review of public expenditure at national and local level. The level and composition of public expenditure and trends since 1980 are reviewed.

Improving the management of public expenditure is a widespread concern among OECD countries. Chapter 3 provides an overview of the approaches adopted among a number of these. The OECD countries that are included are the UK, Australia, New Zealand, Sweden, Canada and the US. Both budgeting and management in the public sector across the OECD have traditionally focussed on inputs (money and its expenditure on salaries, rent and so on). Public sector reforms to budgeting and management systems in several OECD countries have sought to place more emphasis on outputs (what is produced with public expenditure, for example, health services) and in the most recent years on outcomes (the objectives of policy, for example, improved health). One dimension of this change in emphasis has been greater devolution of the control of inputs from the centre to line departments and agencies paralleled by more emphasis on accountability for the results achieved with public expenditure. Another significant reform in some countries has been the separation of the policy work from the delivery of services. The experience of OECD countries in relation to these and other reforms is discussed in Chapter 3.

The management of public expenditure at national level in Ireland is described in Chapter 4. This Chapter provides an outline of how the Budget/Estimates system works and explains the roles of the key actors in the system. Aspects of the SMI that are relevant to the management of public expenditure are discussed.

This description of how the system works is followed by a discussion of some issues in the Irish system of managing public expenditure in Chapter 5. This Chapter does not seek to identify or define any 'ideal' system of public expenditure management; rather the Chapter poses three simple questions as follows:

1. Are there incentives or constraints within the existing system of public expenditure management that bias the system towards 'bad' decision-making, or which make 'good' decision-making more difficult?

2. If such incentives or constraints exist, how might they be alleviated or removed?

3. In addition, are there ways of adding to, or altering, the existing system to facilitate or promote 'good' decision-making?

Here the terms 'good' and 'bad' relate, not to the actions of individuals, but to the product of the decision-making system as a whole. In other words, 'good' decision-making results in the alignment of strategic objectives with expenditure allocations, and with efficient and effective public expenditure in the long run, while 'bad' decision-making means that the system is not producing those results. The analysis in Chapter 5 is largely informed by a series of interviews held with senior civil servants who are involved in the management of public expenditure.

Chapter 6 examines the systems in place for managing expenditure at local government level. This Chapter includes a review of recent reforms to local government expenditure management systems. The emphasis in the Chapter is on local government in the aggregate; management systems of individual local authorities are not examined. The chapter also draws comparisons between the management of expenditure at local and national level. Finally, conclusions and recommendations are presented in Chapter 7.

CHAPTER 2

PUBLIC EXPENDITURE TRENDS SINCE THE 1980s

2.1 INTRODUCTION

This Chapter provides a statistical analysis of public expenditure trends since 1980. This period covers phases of both recession and expansion and hence provides an opportunity to see how expenditure has been adjusted in different economic circumstances. Section 2.2 examines the trend in public expenditure at national level. The expenditure of local government is examined in Section 2.3. In each case the analysis distinguishes between current and capital expenditure.

2.2 PUBLIC EXPENDITURE TRENDS AT NATIONAL LEVEL

Public expenditure is usually defined as the expenditure by central and local government, excluding commercial state organisations and is recorded by the CSO in the national accounts on this basis. The more widely used budgetary data are less comprehensive as these data mainly cover central government expenditure – local authority expenditure is included only to the extent that it is funded by central government. The European Commission publishes internationally comparable data on public expenditure and its concept of public expenditure is similar to that used in the national accounts (i.e., it covers both central and local government) although Eurostat makes further adjustments in order to achieve international comparability.

In relation to the budgetary data, procedures vary according to the type of expenditure. Expenditure that requires annual approval by the Oireachtas is referred to as supply services or voted expenditure.

This refers to ordinary expenditure on most public services and may be either capital or current expenditure. *Central Fund* or *non-voted* expenditure is expenditure for which annual approval by the Oireachtas is not required; this expenditure takes place on the basis of legislation that provides continuing authority for this expenditure. The major items of Central Fund expenditure are debt service, EU contributions and the prefunding of pensions. Other elements include judicial salaries and the expenses of the Comptroller and Auditor General.

Another distinction is that between net and gross expenditure. Gross expenditure is total expenditure from the Central Fund and by Government Departments and Offices. Net expenditure is gross expenditure less expenditure financed by PRSI contributions, as well as 'appropriations-in-aid'; these are receipts received by Government Departments or Offices that may be retained without being paid into the Exchequer. In this analysis, the more comprehensive gross figures are used.

These definitions are used in the analysis of public expenditure trends in the remainder of this Section. The aggregate trend in public expenditure and revenue is first examined using budgetary data. This is followed by an analysis of the broad composition of total public expenditure in terms of expenditure on services, transfers and investment and a comparison of the level of public expenditure in Ireland with other countries. The final parts of this Section provide a more detailed examination of current and capital expenditure using budgetary data.

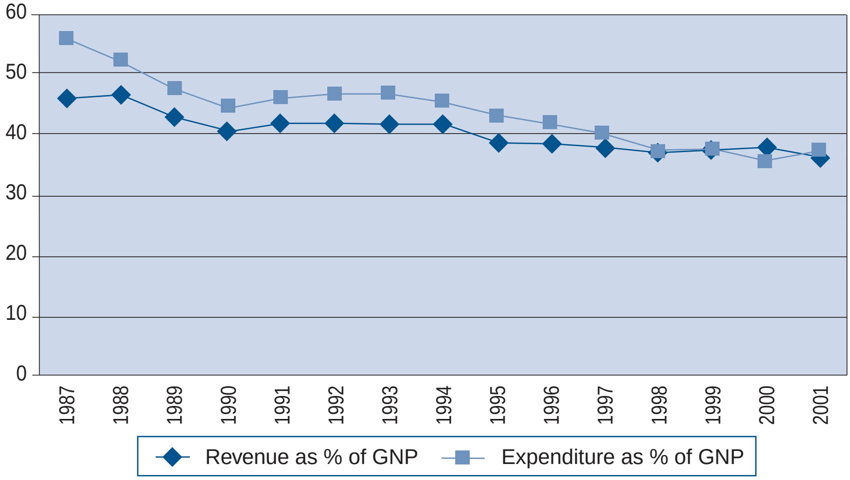
2.2.1 Aggregate Trends

The overall trend in public expenditure and revenue is shown in Figure 2.1. Total public expenditure is gross current expenditure and Exchequer capital expenditure. The share of total public expenditure in national income expenditure has fallen sharply from the early 1980s when, at a time of unsustainable deficits and debt levels, it peaked at over 60 per cent of GNP in 1983. The reduction in the share of expenditure in GNP was concentrated in the years

1987 to 1989 when this ratio fell by 8.5 percentage points. After several years of decline, this share increased from 35.3 per cent of GNP in 2000 to around 39 per cent of GNP in 2002. The contribution of different elements to the change in the share of expenditure in GNP is analysed below.

The share of total current revenue in GNP has been more stable. This share fell by 3.4 percentage points in the late 1980s. It has fallen slowly in the 1990s, from just over 40 per cent in 1990 to 36.5 per cent in 2001. Current revenue consists of tax revenue, PRSI and levies, non-tax revenue accruing to the Exchequer (including the surplus of the Central Bank, the National Lottery surplus, dividends from State companies) and miscellaneous receipts of Government Departments known as appropriations-in-aid (current EU receipts are included as appropriations-in-aid). If one focuses specifically on tax revenue (excluding PRSI), this has shown even greater stability during the 1990s. The share of taxation in GNP in 2000 at 31.1 per cent was essentially unchanged from its 1990 level. There was, however, a significant fall in the tax share in GNP in the years 2001 and 2002.

Figure 2.1
Total Government Expenditure as a Percentage of GNP 1987 - 2001



Source: Department of Finance.
Note: Revised GNP series from 1990.

2.2.2 Broad Composition of Public Expenditure

In macro-economic terms, it is possible to identify three types of expenditure: direct current expenditure by the public authorities on goods and services, transfer payments and public investment. Expenditure on goods and services represents spending by the public authorities on real resources (labour, office rents and so on). Transfer payments are transfers to individuals, companies or voluntary institutions that are not in direct exchange for goods or services provided.

The composition of public expenditure (including both central and local government) in Ireland is shown in Table 2.1 below. The largest single item is current expenditure on goods and services. This represented 15.7 per cent of GNP in 1999 or 43.1 per cent of public expenditure. A number of different types of transfer payments are identified in the Table. The largest of these are current transfers which accounted for 12.4 per cent of GNP in 1999; social welfare payments are the most significant element in this category.[1] Payment of interest on the national debt (below 3 per cent of GNP in 1999) and subsidies (less than 1 per cent of GNP) are other types of transfer payments. Subsidies include agricultural subsidies, non-capital IDA grants and grants to CIE. Capital transfers (just over 1 per cent of GNP) include capital grants for industry, tourism and housing.

1 Expenditure on secondary education is classified as a transfer payment in the national accounts although it would be more appropriate to include this as expenditure on service provision. External transfers in the form of GNP-related contributions to the EU budget and overseas development assistance are also included as transfers.

Table 2.1

Government Expenditure as a Percentage of GNP

	Current Services	Current Transfers	Interest	Subsidies	Invest-ment	Capital Transfers	Total
1980	19.7	12.2	6.2	3.6	5.6	2.7	49.9
1987	19.6	18.0	9.7	2.9	2.8	1.6	54.6
1989	17.5	15.8	8.4	0.7	2.0	1.1	45.5
1994	18.9	15.8	6.8	1.2	2.6	1.6	46.9
1999	15.7	12.4	2.8	0.8	3.6	1.1	36.5

Source: CSO, *National Income and Expenditure* Table 21 and ESRI Databank.

Following strong growth of public expenditure during the 1970s, public expenditure continued growing in the 1980s. Up to 1987 the growth in expenditure was driven by the growth of transfer payments and interest, as has been pointed out by Honohan (1999). A significant influence on the growth of transfers was the rise in unemployment. Interest payments grew as the debt increased and real interest rates increased. The Government was, however, successful in controlling other items of expenditure. The share of expenditure on goods and services was held constant as a share of GNP. Meanwhile the share of public investment in GNP fell as the real volume of public investment was sharply reduced. Notwithstanding the control of expenditure in these areas as well as significant increases in taxation, the public accounts continued in deficit and the debt spiralled upwards.

The fiscal retrenchment of 1987 to 1989 involved significant reductions in public expenditure with the share of total public expenditure in GNP falling by approximately nine percentage points between 1987 and 1989. This reduction took place across all types of expenditure. There were real cuts in public services, as discussed below. A fall in unemployment was a key factor in the decline in the share of transfer payments.

Following the resolution of the fiscal crisis, growth of public expenditure has resumed since 1990. With the slower economic growth of the early 1990s, public expenditure as a share of GNP initially increased but has fallen since the mid-1990s. The decline in interest payments is the most significant factor in this reduction, with these payments accounting for 5.6 percentage points of the decline in the total expenditure share of 9 percentage points in the period since 1989. The public investment share of GNP increased by 1.6 percentage points over the same period.

2.2.3 International Comparisons

The level of public expenditure in Ireland and other EU countries is shown in Table 2.2. If expenditure is measured in terms of GDP, the level of expenditure in Ireland at 33.3 per cent in 2000 was the lowest in the EU. However, in the case of Ireland GNP is a more appropriate measure of for comparison: there is a very large gap between GNP and GDP for Ireland and for the most part this gap is not part of the tax base of the economy as it represents profits of foreign-owned companies and interest payments on foreign debt. When measured as a share of GNP,[2] public expenditure in Ireland in 2002, at 42.5 per cent, was the third lowest among EU countries, with the UK and Spain having a somewhat lower expenditure share in GDP and below the EU average of 45.7 per cent.[3]

2 The main difference between GNP and GDP is the profits of foreign multinationals with operations in Ireland. These profits are part of GDP but not GNP. To some extent these profits are part of the tax base as they are subject to corporation tax. However, they are not part of the other tax bases that constitute most of the total tax base.

3 The level of public expenditure as shown in Table 2.2 is higher than the figures quoted earlier from national sources. The level of public expenditure as estimated by European Commission is higher than that shown by the budgetary figures as the budgetary figures refer to central government expenditure while the European Commission figures refer to general government (central and local government). European Commission figures on public expenditure are close to but slightly higher than public expenditure as reported by the CSO in the national accounts. This is because of adjustments made by European Commission for reasons of international comparability. The largest single difference between the CSO and European Commission figures concerns the treatment of the imputed pension costs of public servants. The European Commission figures include the estimated imputed costs of the future pension entitlements of public servants, which are not included in the national figures on public expenditure.

There are, however, many reasons for different levels of public expenditure that are particularly important to bear in mind when comparing Ireland with some other countries. To take just two examples, Ireland has a younger population than other European countries, which reduces Irish social security, and health spending and it also has a more developed occupational pension system.

Table 2.2

General Government Expenditure as a Percentage of GDP

	1991	1995	2002
Belgium	54.1	52.8	48.9
Denmark	57.8	60.3	53.3
Germany	47.1	49.6	48.9
Greece	n.a.	50.5	47.4
Spain	n.a.	45.0	39.7
France	51.6	55.2	52.9
Ireland (GDP)	44.8	41.5	35.4
(GNP)	50.2	46.8	42.5
Italy	55.5	53.4	47.3
Luxembourg	45.5	45.1	43.2
Netherlands	54.8	51.4	44.8
Austria	54.2	57.3	51.6
Portugal	n.a.	44.9	46.1
Finland	58.5	59.9	49.9
Sweden	n.a.	67.6	57.3
United Kingdom	44.0	44.6	41.2
EU 15	n.a.	51.3	47.2

Source: European Commission (2002), *European Economy*, No.4. The GNP figure for Ireland has been calculated by applying the ratio of GDP to GNP to the Eurostat figure for public expenditure as a percentage of GDP.

In the mid-1980s the share of public expenditure in national income in Ireland was above the EU average but the level of public expenditure at that stage was unsustainable. The share of public expenditure in national income has fallen in a number of EU countries (notably in the UK, Germany and the Netherlands) but the decline has been larger in Ireland. The greater decline in the public expenditure share in Ireland reflects the exceptional economic growth achieved in Ireland since 1987. The actual growth rate of public expenditure has been relatively high in Ireland; over the period of 1990 to 1999, the annual average rate of growth of total public expenditure in Ireland in real terms was over 4 per cent and second only to Luxembourg in the EU and more than double the EU average of 1.75 per cent. Over the more recent period of 1995 to 1999 the real rate of growth of public expenditure in Ireland was over 5 per cent per annum and was the highest among EU countries, as was the rate of growth of GNP.[4]

2.2.4 Current Expenditure by Central Government

2.2.4.1 Functional Composition

The level of gross current expenditure in 2001 was €29.9 billion, consisting of Central Fund expenditure of €3.6 billion and supply services expenditure of €26.3 billion. The composition of current supply services expenditure is shown in Table 2.3. It is clear that supply services expenditure is dominated by three major areas of social services: social welfare (29.7 per cent), health (25.3 per cent) and education (16.1 per cent). These three areas represented over 70 per cent of supply services expenditure in 2001. Housing is a minor item in current supply services expenditure but is a more significant element in capital expenditure (see Section 2.2.5) and local government expenditure (see Section 2.3). Expenditure on economic services was equal to 10.3 per cent of supply services expenditure in 2001. This category includes the current expenditure of agencies such as IDA Ireland, Bord Fáilte and support services for agriculture. Expenditure on security (army, gardai, prisons, and the

4 The real growth rates of public expenditure quoted in this paragraph are from Department of Finance calculations based on Eurostat/OECD data.

legal system) represented 8.5 per cent of total supply services expenditure.

Table 2.3

Current Supply Services Expenditure by Function, 2001

	Expenditure (€ millions)	Percentage of Total
Economic Services	2,722	10.3
Infrastructure	128	0.5
Social Services		
Health	6,657	25.3
Education	4,241	16.1
Social Welfare	7,827	29.7
Housing	116	0.4
Subsidies	222	0.8
Subtotal	19,063	72.4
Security	2,229	8.5
Other	2,198	8.3
Gross Total	26,340	100.0

Source: Calculated from Department of Finance (2001), *Revised Estimates for Public Services 2001*, Dublin: Stationery Office.

2.2.4.2 Trends in Current Expenditure

During the first half of the 1980s, real current spending grew by an annual average rate of just under 2 per cent. Expenditure was cut sharply in the period of adjustment 1987 to 1989, with a real annual fall in expenditure of 2.3 per cent between 1987 and 1989. Spending growth resumed in the 1990s. The average annual rate of growth of current expenditure between 1989 and 2000 was 4.5 per cent in real terms. Growth rates have been particularly high in more recent years. The annual average increase between 1999 and 2002 was around 15 per cent in nominal terms and 10 per cent in real terms. If the planned increase in expenditure for 2002 (including supplementary estimates up to November 2002) is adhered to, the increase in nominal expenditure in 2002 will be close to 15 per cent in nominal terms and 9.3 in real terms.

The growth of supply services expenditure by function is shown in Table 2.4. During the first half of the 1980s, expenditure on health declined in real terms, while there was strong growth of expenditure on social welfare with annual average real growth of over 6 per cent, reflecting the growth of unemployment. Spending on economic services grew by 2.7 per cent per annum.

Table 2.4

Current Public Expenditure: Supply Services, 1980–2001 (Average Annual Percentage Change in Real Terms)

	1980 -1987	1987 - 1989	1989 -1994	1994 -1998	1998 -2000	1989 -2000	2001
Economic Services	2.7	-11.4	6.0	2.9	8.1	5.3	23.1
Infrastructure	-5.5	-5.2	3.0	1.2	-19.0	-2.0	36.1
Social Services							
Health	-1.0	-1.9	8.3	5.4	12.4	8.0	18.2
Education	3.6	-1.1	5.8	2.6	5.4	4.5	7.9
Social Welfare	6.1	-2.1	4.3	1.0	1.6	2.6	10.2
Housing	-16.1	-21.9	-32.0	60.1	30.6	4.5	51.6
Subsidies	-11.6	-6.3	-2.5	-14.4	14.1	-4.3	10.1
Subtotal	2.2	-2.1	5.3	2.4	6.0	4.4	12.5
Security	0.9	-2.3	4.8	3.3	3.7	4.1	5.5
Other	0.2	-4.0	6.0	2.3	15.8	6.4	15.1
Exchequer Pay	0.4	-1.7	5.4	3.2	5.7	4.6	10.7
Gross Total	1.9	-3.2	5.4	2.5	6.5	4.5	13.2

Source: Calculated from *Revised Estimates for Public Services*.

Note: Real growth rates have been calculated using the GNP deflator from the ESRI databank and updated using CSO *National Income and Expenditure 2000* and *Quarterly National Accounts* (Q4, 2001). The decline in infrastructure expenditure between 1998 and 2000 is due to the fact that ongoing expenditure on non-national roads has been funded from the Local Government Fund from 1999 and there has been a corresponding reduction in Exchequer funding.

During the period of retrenchment of 1987 to 1989 there were real spending cuts across all the main functional areas. The rate of decline in social services was less than other areas: social spending fell in real terms by an annual average rate of 2.1 per cent compared to a rate of 3.2 per cent for total spending. However, since social services represent over 70 per cent of current spending, the reductions in these areas represented a very significant share of the expenditure cuts. The fall in social welfare expenditure in this period was due to the decline in unemployment.

Spending has increased substantially in real terms across virtually all functional categories since the beginning of the 1990s. There has been particularly strong growth of expenditure in the health area (8.0 per cent per annum in real terms).[5] Spending has grown by an annual rate of 4.5 per cent in education and by 2.6 per cent in social welfare. There was also strong expenditure growth in the area of economic services (5.3 per cent per annum).

The growth of the economy was far higher in the post-1994 period, which corresponds to the emergence of the Celtic Tiger. This was reflected in a decline in the share of expenditure in GNP in the post-1994 period (see Table 2.5). The largest decline relative to GNP was for social welfare, with a fall of 4.1 percentage points between 1994 and 2000 while the share of education expenditure fell by 1.4 percentage points. With the faster growth of public expenditure in 2001 and slower GNP growth, the share of current supply services expenditure is estimated to have increased by two percentage points.

The significant growth of expenditure raises the question of what has been achieved with the extra expenditure. A substantial share of the increase in expenditure is absorbed by cost increases including higher wage costs. Due to the labour intensive nature of public services, the cost of services typically rises by more than average inflation because wage costs typically rise by more than average inflation.

5 The health sector is noted for its above average inflation so that this is not necessarily an indication of the increase in real health services.

Table 2.5

Current Public Expenditure by Function as a Percentage of GNP

	1980	1987	1989	1994	2000	2001
Economic Services	3.3	3.7	2.8	3.0	2.4	2.8
Infrastructure	0.5	0.3	0.3	0.2	0.1	0.1
Social Services						
Health	6.6	5.9	5.3	6.4	6.1	6.9
Education	4.7	5.8	5.3	5.7	4.3	4.4
Social Welfare	9.0	13.1	11.8	11.8	7.7	8.1
Housing	0.6	0.2	0.1	0.0	0.1	0.1
Subsidies	2.2	0.9	0.7	0.5	0.2	0.2
Subtotal	23.2	25.8	23.2	24.5	18.4	19.7
Security	3.3	3.3	3.0	3.1	2.3	2.3
Other	2.5	2.5	2.1	2.3	2.1	2.3
Gross total	32.7	35.6	31.4	33.1	25.2	27.2
Exchequer Pay and Pensions	14.0	13.8	12.5	13.2	10.2	10.8

Source: Calculated from *Revised Estimates for Public Services* and CSO, *National Income and Expenditure 2000* and *Quarterly National Accounts* (Q4, 2001).

There are methodological difficulties in measuring the output of public services. There is no straightforward way of establishing the extent to which the real growth of expenditure has resulted in improvements in the quantity or quality of public services. There are, however, data available on employment across the public service. Employment is obviously a measure of input rather than output but one would expect some relationship between employment levels and the delivery of services. Public service employment grew by an annual average rate of 1.8 per cent between 1989 and 2001. This increase followed substantial reductions in the 1987 to 1989 period. Over the extended period since 1987 public service employment has grown by an annual rate of 0.9 per cent. The fastest areas of employment growth within the public service have been health and education. Over the period 1989 to 2001, employment grew by an annual average rate of 2.9 per cent in health and 2.1 per cent in education. The numbers employed in health in 2001 were up by around 17,500 compared to 1987, while employment in education was up by around 12,850. Employment in local authorities and defence in 2001 was below its 1987 level. Total public service employment increased by over 27,500 over the 1987 to 2001 period.[6]

These figures on public service employment show that the rise in expenditure has *in part* been used to provide substantial increases in employment in key social services areas. This does provide the potential for improved services although the extent to which this potential has been achieved cannot easily be determined.

2.2.5 Capital Expenditure

Comprehensive data on capital expenditure in the public sector are provided in the Public Capital Programme (PCP). This sets out planned capital expenditure by central government, local authorities and state agencies, including commercial state agencies.

While current expenditure is dominated by social services spending, the largest element of the PCP is productive infrastructure (investment in transport, energy and telecommunications infrastructure, see Table 2.6 above). This accounted for 47.8 per cent of the PCP in 2001 (€3.5 billion). The largest element of infrastructure spending was investment in transport (25.7 per cent of the PCP in 2001). The next largest element of infrastructure investment was energy (12.7 per cent of the PCP). This mainly covered investment by the ESB and Bord Gáis Éireann and so could be considered as more commercial investment than pure public investment. The low level of investment shown for telecommunications reflects the fact that Eircom was privatised in 2000 so that its investment is no longer included in the PCP.

6 Based on Department of Finance data on public service employment. Employment is defined on the basis of full-time equivalents.

Table 2.6

Composition of the Public Capital Programme, 2001

Composition of Expenditure	Expenditure (€ millions)	Percentage of Total
Sectoral Economic Investment		
Industry and Labour	405	5.6
Agriculture and Food	121	1.7
Fisheries	44	0.6
Forestry	122	1.7
Tourism	56	0.8
Subtotal	748	10.3
Productive Infrastructure		
Energy	924	12.7
Telecommunications, RTE, Postal services	98	1.3
Transport	1,877	25.7
Environmental Protection	593	8.1
Subtotal	3,491	47.8
Social Infrastructure		
Hospitals	400	5.5
Education	561	7.7
Housing	1,297	17.8
Government Construction, etc	799	11.0
Subtotal	3,057	41.9
Total	7,296	100.0

Source: Department of Finance (2001), *Public Capital Programme 2001*, Dublin: Stationery Office.

The other major component of the PCP is investment in social infrastructure (housing, education, health facilities and general government construction) which represented 41.9 per cent of the PCP in 2001 (€3.1 billion). The largest component of social infrastructure was investment in housing (17.8 per cent of the PCP) reflecting the recent expansion of public housing investment. Finally, investment in hospitals and education facilities represented 5.5 per cent and 7.7 per cent respectively of the PCP in 2001.

The remainder of the PCP is sectoral economic support (capital support for industry, agriculture and so on) accounting for 10.3 per cent of the PCP in 2000 (€748 million). The share of this element of the PCP has been declining in recent years.

Capital expenditure was cut sharply during the 1980s: the real volume of the PCP fell by around one third between 1982 and 1990. With EU assistance it recovered during the 1990s and by 1997 the real volume of public capital expenditure had been restored to its previous peak of 1982. Public investment has grown by an average annual real growth of over 16 per cent between 1998 and 2000 while it grew by an annual rate of close to 11 per cent in 2001. Public expenditure on sectoral investment only increased slightly between 1998 and 2000 and has declined in 2001.

Table 2.7

Public Capital Programme, 1980–2001
(Annual Percentage Change in Real Expenditure)

	1980 -1987	1987 -1989	1989 -1994	1994 -1997	1998 -2000	2001
Sectoral Economic Investment						
Industry and Labour	-7.7	1.4	1.0	26.0	-2.4	-21.8
Agriculture	-16.9	7.0	19.7	-3.4	-0.5	-27.7
Fisheries	-14.8	2.2	-0.7	18.1	38.8	-25.0
Forestry	3.8	11.9	15.8	-5.6	8.5	-12.4
Tourism	5.6	33.8	23.0	13.2	-3.1	-23.5
Subtotal	-9.0	2.9	6.7	16.0	0.9	-21.8
Productive Infrastructure						
Energy	-7.6	-15.6	11.9	5.2	5.6	20.9
Telecommunications, RTE, Postal services	-4.1	5.2	-1.7	14.0	15.3	18.2
Roads, Sanitary services	6.7	-0.9	5.3	9.2	24.6	
Transport	-2.0	12.5	-0.4	5.5	31.3	
Subtotal	-1.9	-0.4	3.8	8.7	19.7	14.7
Social Infrastructure						
Hospitals	1.1	-13.9	2.7	21.6	18.8	16.5
Education	-0.1	-27.9	9.1	4.1	11.1	0.3
Housing	2.6	-42.8	11.9	3.3	23.5	36.7
Government Construction	8.0	-19.6	12.7	12.8	23.6	10.6
Subtotal	2.6	-33.8	10.2	7.9	19.8	18.8
Total	-2.7	-10.8	6.2	11.0	16.4	10.9

Source: Calculated from Department of Finance data and *Public Capital Programme 2001*.

Note: The above trends in real expenditure have been calculated using the gross domestic fixed capital formation deflator taken from the ESRI databank and updated using CSO *National Income and Expenditure 2000* and *Quarterly National Accounts* (Q4, 2001). Until 1997 loans by the ICC and ACC Banks were included in the Sectoral Economic Investment part of the PCP. For this reason this table shows slightly different time periods than the corresponding current expenditure Table to achieve consistency. Investment by Eircom/Telecom Éireann was included in the PCP until the privatisation of Eircom in 2000. This investment has been excluded from the 1998 figures to achieve consistency for the 1998–2000 period. The health figures from 1997 include investment funded by Health Boards from property disposals. The increases for roads and transport in 2001 are not shown due to changes in classification of these items.

2.2.6 Conclusion

There have been major changes in the Irish public finances over the past two decades. Since 1983 the expenditure share of GNP has fallen by over 20 percentage points. The fall in the expenditure share of GNP reduced the size of the deficit and eventually moved the public finances into surplus. Changes in the tax share of GNP have been more modest. The tax share rose in the first part of the 1980s and fell in the late 1980s and was fairly stable throughout the 1990s. It fell by around two percentage points in 2001. After several years of decline, the expenditure share of GNP increased in the past two years. Total Government expenditure (based on budgetary data) increased from 35.3 per cent of GNP in 2000 to a budgeted level of 39 per cent in 2002.

During the 1990s a falling expenditure share in GNP was consistent with significant growth in the real level of public expenditure. Current supply services expenditure grew by an annual real average rate of 4.5 per cent during the 1990s with considerably faster growth in the most recent years. The growth of expenditure has in part been used to finance higher social welfare benefits and a significant expansion of employment in the key social service areas of health and education, but it also reflects increases in the cost of services. The pattern of capital expenditure growth has been more erratic than that of current expenditure. Capital expenditure was cut earlier and more sharply during the 1980s while it grew at a faster rate during the 1990s.

2.3 LOCAL GOVERNMENT EXPENDITURE

2.3.1 Introduction

A significant proportion of public expenditure is managed by local government either directly or as an agent of central government. In 2001, the local authorities were responsible for an estimated €2.7 billion of current expenditure and a further €3.9 billion of capital expenditure. Combined this represents approximately 5.3 per cent of GNP (4.5 per cent of GDP). This Section examines both the current and capital expenditure of local government. Unless otherwise stated, all data in this Section refer to Estimates rather than actual outturns.

2.3.2 Current Expenditure of Local Government

2.3.2.1 Functional Composition

Local government current expenditure can be decomposed into eight functional programme groups that relate to the primary service delivery functions of local government. These functional groups are: Housing and Building; Road Transportation and Safety; Water Supply and Sewerage; Development Incentives and Controls; Environmental Protection; Recreation and Amenity; Agriculture, Education, Health and Welfare; and other Miscellaneous Services.

Table 2.8 shows that Road Transportation and Safety was the biggest programme item in 2001, accounting for over 30 per cent of total current expenditure. Most of this went towards the upkeep and maintenance of non-national roads. The next largest item was expenditure on Environmental Protection which accounted for just over 17 per cent of total local government expenditure, mostly related to waste disposal and fire protection services.

Housing accounted for the next single largest current expenditure item, at 15.6 per cent of total expenditure in 2001. However, the proportion of current expenditure directed towards housing has declined significantly over the years. While much of this fallback occurred over the 1987-1989 period of fiscal retrenchment, even in recent years, expenditure on housing and building has taken up less and less of day-to-day local government spending and has actually declined five percentage points as a percentage of total local government spending in the 1994–2001 period. However, these figures need to be interpreted with caution. This decline does not necessarily say anything about service provided and indeed could simply mean that monies are being spent more efficiently. It also coincides with a period when the stock of local authority housing was in decline (see NESC (1999: 495)), which would have directly led to reduced management costs.

Table 2.8

Local Government Current Expenditure by Programme Group, 2001

Programme Group and Programmes	**Expenditure (€ millions)**	**Percentage of Total**
1. Housing and Building	417.2	15.6
2. Road Transportation and Safety	804.5	30.2
3. Water Supply and Sewerage	304.7	11.4
4. Development Incentives and Controls	129.1	4.8
5. Environmental Protection	464.5	17.4
6. Recreation and Amenity	245.1	9.2
7. Agriculture, Education, Health and Welfare	159.9	6.0
8. Miscellaneous Services	140.6	5.3
TOTAL – ALL PROGRAMMES	**2665.6**	**100.0**

Source: Department of the Environment and Local Government (2001), *Local Authority Estimates 2001*, Dublin: Stationery Office.

Water Supply and Sewerage accounted for 11.4 per cent of current expenditure in 2001, the vast bulk of which went towards the operation and maintenance of the public water supply. Recreation and Amenity includes the operation of the public library system, the maintenance of parks and other open spaces, as well as the operation of a number of local authority swimming pools. Expenditure on this item has increased steadily over the last 20 years, representing

9.2 per cent of total current expenditure in 2001 up from 6.3 per cent in 1980. Programme Group 7, Agriculture, Education, Health and Welfare accounted for 6.0 per cent of total local government current expenditure. Despite its name, this item actually consists almost entirely of the payment of grants to third level students, in addition to pensions to former VEC teachers. After Miscellaneous Services (5.3 per cent of total), the smallest programme group expenditure goes towards Development Incentives and Controls, which accounted for 4.8 per cent of total current expenditure in 2001. This item refers to the development planning, promoting and controlling functions that local authorities perform in their own areas.

2.3.2.2 Current Revenues

Local authorities receive revenues to meet these expenditures from a variety of sources. In general, about half of all revenue receipts come from central government with the remainder coming from a mixture of revenues earned from goods and services (housing rents, planning fees, etc.), and commercial rates. The balance amongst these revenue sources varies depending on the type of local authority area. Table 2.9 shows the source of revenue receipts by local authority area in 2001. This reveals that county councils have a much heavier reliance on central government funding than county boroughs or urban district councils. This largely reflects the different geographical areas (and their associated characteristics: size, population density, economic activity, etc.) covered by the individual local authorities and their related ability to earn income from other sources such as domestic service charges or commercial rates. The abolition of rates on agricultural land in 1982 also resulted in the heavier reliance by county councils on central government grants relative to county boroughs or urban district councils.

Table 2.9

Sources of Current Income by Type of Local Authority, 2001

	Government Grants	General Fund(1)	Goods and Services	Commercial Rates	Totals
County Councils	31.9	24.1	24.5	19.5	100.0
County Boroughs	19.6	12.9	33.9	33.7	100.0
Urban District Councils	9.1	19.7	36.2	35.0	100.0

Source: Department of the Environment and Local Government (2000), Local Authority Estimates 2000, Dublin: Stationery Office.

Note: (1) This refers to the amounts received from the Local Government Fund less non-national roads. The Local Government Fund is discussed in more detail in Chapter 6.

2.3.2.3 Recent Trends in Current Expenditure

Table 2.10 shows the growth in current expenditure across programme groups, expressed in real terms. Annual growth rates are calculated for a number of periods reflecting the early 1980s, the period of fiscal retrenchment in the late 1980s, the recession and recovery period up to 1994 and the ‘Celtic Tiger’ period since then.

In the earlier 1980 to 1987 period, real current spending increased at an annual average growth rate of 4.1 per cent, although some categories of expenditure, such as Recreation and Amenity, and Water Supply and Sewerage, experienced growth rates nearly double that average. The only programme group to achieve a growth rate significantly less than the total was Agriculture, Education, Health and Welfare, which registered an annual average growth rate of just 0.8 per cent over the 1980 to 1987 period. This was largely due to the elimination of supplementary welfare allowances from the rate support grant to local authorities in 1986, which substantially affected the growth rate of expenditure on Agriculture, Education, Health and Welfare over this period.

Table 2.10

Local Authority Current Expenditure, 1980–2001
(Average Annual Percentage Change in Real Terms)

Programme	1980 -1987	1987 -1989	1989 -1994	1994 -2000	2001
1. Housing and Building	6.5	-31.0	-2.5	-0.7	11.6
2. Road Transportation and Safety	4.2	-10.5	-4.1	7.2	6.0
3. Water Supply and Sewerage	7.6	-35.3	3.1	3.2	7.9
4. Development Incentives & Controls	4.0	-13.4	4.9	10.4	21.4
5. Environmental Protection	6.2	-16.7	4.4	6.2	17.0
6. Recreation and Amenity	7.8	-14.1	3.2	2.6	8.4
7. Agriculture, Education, Health & Welfare	0.8	-15.4	7.5	0.5	0.2
8. Miscellaneous Services	6.7	-12.4	-3.6	2.4	10.1
TOTAL	**4.1**	**-15.7**	**-0.7**	**4.0**	**9.6**

Source: Department of the Environment and Local Government, *Local Authority Estimates*, various issues.

Note: Current expenditure is deflated using the GNP deflator. Data on deflators are from the ESRI databank, updated using CSO *National Income and Expenditure 2000* and *Quarterly National Accounts* (Q4 2001). Certain categories of local government current expenditure have been reclassified as capital expenditure over the years. See text for more detail.

Local government expenditure declined sharply in the 1987 to 1989 period, experiencing an annual average rate of decline of 15.7 per cent. While some of this decline was in line with the fiscal retrenchment that was evident across the whole public sector during this period, there were also a number of changes in the financing of local authorities at this time that directly affected the level of current expenditure. Among these, the most significant was the reclassification of certain grants made by central government to local authorities from current expenditure to capital expenditure in 1988. Up to this point, local authorities funded capital projects by borrowing from the Local Loans Fund, which was administered by the Office of Public Works. Central government grants were provided to repay these loans and these grants were treated as current revenues[7]. Since 1988, however, the Department of the Environment and Local Government has paid the grants directly to local authorities and the grants have been treated as capital revenues. This reclassification of expenditures had a significant impact in areas such as Water Supply and Sewerage where the average annual growth rate in current expenditure fell by over 35 per cent, and Housing and Building where annual real current expenditure declined by 31 per cent on average.

There was some recovery in expenditure growth in the subsequent 1989 to 1994 period, although total current expenditure still fell by nearly 1 per cent in real terms on average per year over the period. Most of the programme groups experienced a significant recovery in their expenditure growth. The exceptions were Housing and Building (average –2.5 per cent per year), Road Transportation and Safety (average –4.1 per cent per year) and Miscellaneous Services (average –3.6 per cent per year). Part of the continued decline in Road Transportation and Safety can be accounted for by the reclassification of grants paid by the Department of the Environment and Local Government to local authorities for the maintenance and improvement of national roads in 1993 from current expenditure to capital expenditure.[8] As discussed earlier, the continued decline in the annual growth rate of Housing and Building expenditure likely reflects the fall-off in social housing completions in the 1987 to 1989 period and the effect of a massive sell-off of local authority housing at the end of the 1980s, both of which resulted in a substantial decline in the stock of local authority housing at this time, thereby reducing management and maintenance costs.

In the most recent 1994 to 2000 period, total real current expenditure has grown at an annual average rate of 4.0 per cent.

7 This resulted in a circular system of payments for capital projects with central government providing loans to local authorities and then subsidising the repayments to itself.

8 However, expenditure on non-national road improvement is still treated as current expenditure.

However, current spending on Housing and Building has remained negative, falling at an annual average rate of 0.8 per cent over this period. A significant proportion of this expenditure category is made up of repayments by local authorities to the Housing Finance Agency, following borrowing by them to finance loans to individuals for house purchase and improvement. The negative growth rate is therefore largely due to the significant fall in loan costs following the rapid fall in interest rates in the late 1998 to 1999 period. The largest annual growth rate was in Development Incentives and Controls, which probably reflects the sudden rapid pace of planning and development over this period. Expenditure on Agriculture, Education, Health and Welfare fell back to a 0.5 per cent growth rate. This programme is a ‘catch-all’ expenditure group covering a wide range of expenditure items. The trend is therefore more susceptible to the ‘peaks and troughs’ created by ‘one-off’ expenditure items. As with central government expenditure, expenditure growth in the current year 2001 is higher than in earlier years with an estimated real increase of over 8 per cent.

2.3.3 Capital Expenditure of Local Government

Capital expenditure undertaken by local authorities is financed largely by central government, either directly or through EU funding. Local authorities’ expenditure on national roads is funded by the National Roads Authority. Up until recently, local authority expenditure on capital projects could only be examined through the detail given in the Public Capital Programme and reproduced in the Local Authority Estimates, but the Local Government Act, 2001 directs local authorities to individually report on their capital projects each year.

Table 2.11 shows the annual average real growth in local authority capital expenditure over the period 1980 to 2001. Total expenditure on capital projects grew at an annual average rate of 3.9 per cent in the 1980 to 1987 period, before experiencing a significant fall-off in the 1987 to 1989 period when it registered a 20.3 per cent annual decline. Expenditure subsequently recovered in the 1989 to 1994 and 1994 to 2000 periods to a 10.9 and 12.4 per cent rate respectively. In 2001, the real increase in capital expenditure was over 13 per cent.

Table 2.11

Local Authority Capital Expenditure, 1980–2001
(Average Annual Percentage Change in Real Expenditure)[1]

	1980 -1987	1987 -1989	1989 -1994	1994 -2000	2001
Housing [2]	1.2	-41.6	18.1	10.8	27.4
Roads	15.1	3.9	5.1	11.9	18.2
Water & Sanitary Services	1.0	-7.9	10.4	15.3	-17.4
Environmental Services	-0.1	-26.4	28.3	11.2	17.7
Fire & Emergency Services	5.2	1.4	-9.0	5.6	73.0
Miscellaneous	-	-	19.6	36.1	-20.4
TOTAL	**3.9**	**-20.3**	**10.9**	**12.4**	**13.3**

Source: Department of the Environment and Local Government, *Local Authority Estimates*, various issues.

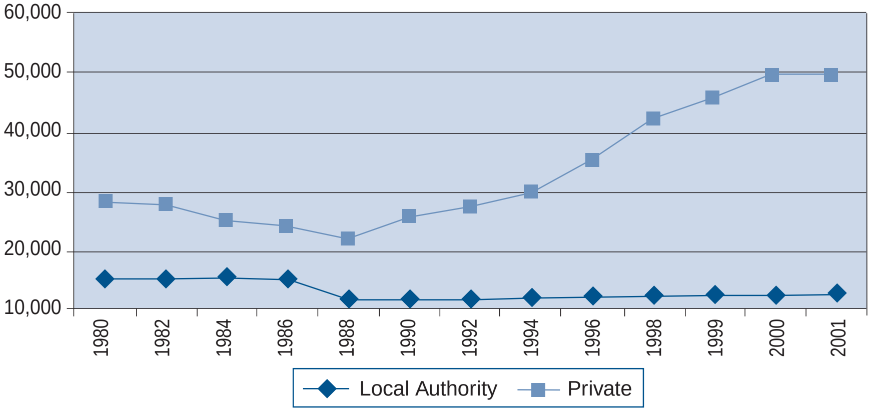
Note: [1] Data have been deflated using the gross domestic fixed capital formation deflator. Data are from the ESRI databank and updated using CSO *National Income and Expenditure 2000* and *Quarterly National Accounts* (Q4, 2001).

[2] The data for local authority capital expenditure on housing includes expenditure on Local Authority and Social Housing, Loans for Shared Ownership Scheme, Rental Subsidy, House Purchase and Improvement Loans (including Housing Finance Agency loans) and other housing expenditure classified as capital expenditure.

Looking at the different components of capital expenditure reveals a similar pattern for most. The main exceptions are in Housing and Roads. Capital spending on local authority housing fell throughout the 1980s before recovering in the 1990s. The growth of expenditure on housing was lower than total capital expenditure for most of the 1990s, but has increased very substantially in the past two years. The implications of this investment trend can be seen in the trend in local authority house completions. Local authority housing completions peaked at a level of 7,000 in 1984 and then fell sharply to a low of less than 1,000 in 1989. The output of local authority housing subsequently recovered during the 1990s and there were 3,622 local authority completions in 2001. Over the period 2000-2006, the National Development Plan (NDP) is committed to achieving 35,500 additional units of local authority housing.[9]

Figure 2.2

Private and Local Authority Housing Completions 1980–2001



Source: Department of the Environment and Local Government, Housing Statistics Bulletin.

Capital expenditure on roads also reveals a slightly different picture over the 1980 to 2001 period. Unlike most other categories of capital expenditure, spending growth on roads has remained positive over the entire period. Even during the 1987 to 1989 period, spending on roads grew at an annual average rate of 3.9 per cent. While this is a slower rate of growth than in previous years, it is in contrast to most of the other categories of capital expenditure which exhibited marked decreases over the same period. It is likely that this reflects the extent of EU co-financing of road building during this period.

9 Voluntary housing is another way of providing social housing but the level of voluntary housing output is fairly low with 1,253 completions in 2001. Private housing output was at a record level with close to 48,000 completions in 2001.

2.4 CONCLUSION

The share of public expenditure in GNP has declined sharply since the mid-1980s reflecting the high growth of GNP. The growth of real expenditure during the 1990s quickly reversed the cuts of the 1987 to 1989 period. Current supply services expenditure grew by an annual average rate of 4.5 per cent in real terms during the 1990s while there has been faster growth in the most recent years. There was a particularly large real increase of close to 20 per cent in nominal terms and over 13 per cent in real terms in current supply services expenditure in 2001. If the planned increase in expenditure for 2002 (including Supplementary Estimates up to November 2002) is adhered to, the increase in nominal expenditure in 2002 will be close to 15 per cent in nominal terms and 9.3 in real terms. The share of current supply services expenditure in GNP fell from 33.4 per cent of GNP in 1993 to 25.2 per cent in 2000. Its share of GNP increased to 27.2 per cent in 2001 and will be in the region of 29 per cent of GNP in 2002. Capital expenditure was cut more severely than current expenditure during the 1980s, and during the 1990s it showed faster growth than current expenditure.

The growth of expenditure has been reflected in a significant increase in public service employment in the key social services areas of health and education. This provides the potential for improvements in the delivery of public services although realising this potential depends on effective management. Higher public expenditure has been associated with improvements in the provision of some public services.

While examination of the trends in local government expenditure over the last 20 years has been complicated by reclassifications of expenditure items, certain patterns are evident. As with the trend in overall public expenditure, local government expenditure (current and capital) experienced a significant deceleration in the 1987 to 1989 period. Indeed, the downturn in expenditure growth over this period was even more marked in local government than central government. Expenditure growth in most service categories has subsequently recovered, although it is still growing at a slower pace than at central government level.

The approaches that have been adopted to the reform of the management of public expenditure in a range of OECD countries are discussed in the next Chapter. Subsequent Chapters will describe and analyse the systems in place in Ireland for the management of public expenditure at both national and local levels.

CHAPTER 3

THE MANAGEMENT OF PUBLIC EXPENDITURE: REFORM EXPERIENCE IN OECD COUNTRIES

3.1 INTRODUCTION

This Chapter illustrates the type of reforms in relation to public expenditure that are occurring in a number of OECD countries. The general objective is to examine reforms that can contribute to the effective management of public expenditure. Section 2 discusses the dimensions of managing expenditure and considers the limitations of traditional budgetary systems. Subsequent sections discuss the reform experiences of a range of OECD countries: the UK, New Zealand, Sweden, Canada, the US and Australia. The US, notwithstanding its vast size, is included because its experience of the Planning Programming Budgeting (PPB) system in the 1960s represents perhaps the best known example of an attempt to develop a public expenditure system based on relating budgetary decisions to policy objectives in a systematic way. Conclusions are presented in Section 10.

3.2 CHARACTERISTICS OF PUBLIC EXPENDITURE MANAGEMENT SYSTEMS

3.2.1 Introduction

The management of public expenditure is concerned with both planning and control. Planning involves: (1) deciding on the overall expenditure totals and ensuring that they are in line with macroeconomic and budgetary requirements; (2) the determination of priorities and the allocation of expenditure to reflect these priorities; and (3) the deployment of expenditure to achieve these priorities. Control involves: (1) ensuring that public funds are spent only for the purposes specified and that appropriations are not exceeded; (2) ensuring that public expenditure provides value for money in terms of both efficiency and effectiveness; and (3) taking corrective action when plans are not achieved (NESC, 1990: 327).

3.2.2 Limits of Traditional Budgeting

Public expenditure systems vary in the extent to which they successfully meet these planning and control requirements. Traditional budgetary systems are mainly focussed on the first dimension of control outlined above – ensuring that public expenditure is spent for the purposes specified. Expenditure is approved by the parliament and monitored to ensure that the expenditure is in accordance with the legal requirements. This prevents fraud in public expenditure, a basic requirement for a system of public administration.

While traditional budgetary systems achieve narrow financial control, they suffer from several limitations. These limitations are not specific to Ireland but reflect features of traditional budgeting in many countries.

3.2.2.1 A Focus on Inputs

Traditional budgetary systems are focussed on inputs (money and its expenditure on specific inputs such as salaries, and so on) rather than on the output that the expenditure finances. Traditional budgets do not provide useful information on the cost of achieving policy objectives. Public expenditure decisions should be informed by a comparison of costs against the expected benefits of expenditure. The detailed information on the costs of inputs provided by traditional budgets does not provide a basis for considering both the costs and benefits of expenditure and making decisions on the basis of priorities (Mikesell, 1995). The presentation of traditional budgets in terms of inputs is also one obstacle to transparency as it is not obvious to the reader of a budget what services will be provided with the money included in the budget.

3.2.2.2 Incrementalism

The dominant concern of decision-making in traditional budgetary systems is the affordability of increases in expenditure. The value of existing patterns of expenditure is not regularly considered in the decision-making process. As policy priorities change over time, this makes it difficult to direct expenditure to the most important priorities. New initiatives may be crowded out by existing lower priority commitments.

3.2.2.3 Compliance

The focus on inputs of traditional budgets has implications not only for budgetary decisions but also for the management of the public service. Traditional budgets are associated with the proliferation of detailed rules in the use of resources. This may result in managers being more concerned with compliance with the rules rather than with the effective achievement of objectives.

3.2.2.4 Cash Costs

While traditional budgetary systems focus on costs, costs are not measured comprehensively. The focus is on costs in cash terms; non-cash costs such as depreciation of capital equipment, non-funded pension liabilities and wider social costs such as environmental costs are neglected. Furthermore, the focus is on flows and there is little consideration of the stock of assets or liabilities. One exception is that the stock of financial debt receives attention in traditional budgetary systems, but this again reflects the cash orientation of these systems.

3.2.2.5 Annual Basis

The traditional budget is based on a single year. The implications of current decisions for future costs and benefits do not receive sufficient attention.

3.2.3 Implications

In some respects, reforms to the Irish system have moved it significantly from the above characterisation of traditional budgetary systems. For example, public investment decisions are informed by a planning process; there is growing use of evaluation;

multi-annual projections of expenditure and revenue are produced and the remit of the Comptroller and Auditor General has been extended to cover value-for-money questions in addition to the traditional focus on financial regularity. Nonetheless, the budgetary system in Ireland and other countries continues to have many of the characteristics of traditional budgetary systems. The current Irish system is examined in subsequent chapters. Recent and proposed reforms are outlined and assessed, including aspects of the Strategic Management Initiative (SMI) that are of relevance to the effective management of public expenditure.

3.3 OECD REFORM EXPERIENCE

Public sector reform in several OECD countries seeks to move from a traditional 'command and control' model to one that is decentralised and more flexible. The key feature of the traditional model is that the control of human and financial resources is concentrated at the centre while operational responsibility for delivering services is located in spending organisations. This division between control and responsibility proved problematic:

> The centre issued rules, monitored compliance with the rules, and intervened, as it thought appropriate; the operating echelons complied, or at least pretended to. With control in one place and responsibility for producing in another, public sector managers often were managers in name only.
>
> (OECD, 1997a: 11).

The general direction of reform is that spending agencies are given greater flexibility in using resources in exchange for being held responsible for results. The first step of reform, the scaling down of central control, proved to be relatively unproblematic in many countries. The second step of getting civil servants to manage for results and changing state agencies into performance-driven producers of public services has proved more difficult. In fact, an OECD (1997a) report wonders whether this will ever be fully achieved.

The rest of this Chapter is concerned with reforms adopted in a number of OECD countries. The reforms discussed relate to both direct changes in budgetary procedures (such as performance-oriented budgeting) as well as performance management reforms to improve the effectiveness of public expenditure.

3.4 UNITED KINGDOM

3.4.1 Introduction

The UK has recently reformed its budgetary system in order to strengthen the links between higher level spending allocations and the achievement of policy outcomes. These reforms follow two decades of reform across the UK public sector that have sought to improve efficiency and effectiveness as well as accountability for results. Key reforms have included the separation of service delivery functions from policy work in the civil service and the subjecting of public service delivery to market testing.

3.4.2 Next Steps

This initiative involved the establishment of executive agencies responsible for the delivery of services with some degree of independence from their overseeing departments. This has greatly reduced the size of government departments whose role is now to concentrate on policy and central management operations. The relationship between departments and agencies is governed by a framework document. This sets out among other things, the agency's role, aims, objectives as well as the delegation of responsibilities. The extent of delegation has been controversial. As agencies have matured they have acquired more operational independence. Chief executives of these agencies and the agencies themselves are assessed in terms of annual performance targets. Progress in meeting these performance targets is reported in annual reports (OECD, 1997a).

It is argued by Rhodes in *Understanding Governance* (1997) (as quoted by Sabel, 2001) that the division of responsibilities between agencies and departments has not worked as originally planned. Agencies (to be responsible for implementation) actually develop a near monopoly of policy expertise. Policy emerges from the numerous decisions of agencies. If the results are disappointing, the minister can exploit the ambiguity between policy and management to avoid responsibility. Rhodes argues that this has led to a significant decrease in the political accountability of British government.

3.4.3 Market Testing

A 1991 White Paper, *Competing for Quality*, formulated the principle that, wherever practical, the provision of public services should be put out to competitive tendering. Under Compulsory Competitive Tendering, local authorities were required to subject their services to competitive tendering but this has been replaced by a requirement to undertake more general reviews (see below). There are a number of studies from the UK and elsewhere indicating that the contracting out of services can achieve cost savings (see Domberger and Jensen, 1997 for a review of the evidence). Notwithstanding the evidence of cost savings in individual areas, it is argued by Flemming and Oppenheimer (1996) that it has not been shown that such economies are big enough to have perceptible effects on aggregate expenditure.

3.4.4 Citizen's Charter

The Citizen's Charter programme was introduced in 1991. This requires government agencies to produce a short document (charter) setting out their service commitments and also requires publication of performance information against the standards set. Humphreys (1998) provides a mainly positive assessment of this initiative which has since been re-launched by the current administration as *Service First*.

3.4.5 Local Services

Authorities responsible for the delivery of local services (including education, health and police services) are required by statute to publish performance indicators. These are published in local newspapers and the Audit Commission also publishes national comparisons. From 2000 onwards, local authorities are required to publish a new set of indicators: best value performance indicators. Local councils are expected to reach the standards of the top performers within the next five years. Further, every five years, councils are required to review all their services: councils are required to review why and how a service is being delivered and to compare their performance with others (including the private and voluntary sectors). This best value initiative replaces the former Compulsive Competitive Tendering process.

3.4.6 Limits to the Reforms

In its White Paper, *Modernising Government* (1999), the UK Government acknowledged that the management reforms introduced by previous government administrations had achieved improved productivity, better value for money, better quality services and expressed its commitment to build on this success. On the other hand, the White Paper indicated several changes of emphasis in the approach to public service reform. The White Paper identified the following problems with previous reforms:

- too little effort has gone into making sure that policies are devised and delivered in a consistent and effective way across institutional boundaries;
- issues like crime and social exclusion cannot be tackled on a departmental basis;
- an increasing separation between policy and delivery has acted as a barrier to involving in policymaking those people who are responsible for delivering results in the front line; and
- too often the work of departments and agencies has been fragmented and focus has been on the individual achievements rather than on the contribution to the government's overall strategic purpose (*Cabinet Office*, 1999:15-16).

A theme in the White Paper is the desire to go beyond achievements in relation to value for money/efficiency to more emphasis on the underlying policy objectives. Thus, it signals an emphasis on outcomes more than outputs and a desire to develop ‘joined up’ government.

The challenge of cross-cutting issues is further explored in a paper produced by the UK Cabinet Office, *Wiring it Up* (Performance and Innovation Unit, 2000). This paper identifies several factors that inhibit the tackling of problems that cross departmental boundaries:

- there is a tendency to take a provider-centred perspective rather than that of the service user;
- there is little incentive or reward for organisations or individuals who contribute to corporate goals or the goals of another department or organisation;
- the skills and capacity to develop and deliver cross-cutting solutions are often absent;
- budgets and organisational structures are arranged around vertical, functional lines (education, health, defence etc.) rather than horizontal, cross-cutting problems and issues (social exclusion, sustainable development etc.);
- systems of accountability and the way risk is handled can militate against innovative cross-cutting working;
- the centre is not always effective at giving clear strategic direction; and
- mechanisms for resolving conflicts between departments can be weak, leaving local service providers to wrestle with the consequences (Performance and Innovation Unit, 2000: 6).

The paper recommends action in six key areas to address these issues:

- stronger leadership from ministers and senior civil servants to create a culture that values cross-cutting policies and services, with systems of rewards and recognition that reinforce desired outcomes;

- improving policy formulation and implementation to take better account of cross-cutting problems and issues, by giving more emphasis to the interests and views of those outside central government who use and deliver services;
- equipping civil servants with the skills and capacity needed to address cross-cutting problems and issues;
- using budgets flexibly to promote cross-cutting working, including more cross-cutting budgets and pooling of resources;
- using audit and external scrutiny to reinforce cross-cutting working and encourage sensible risk-taking; and
- using the centre to lead the drive to more effective cross-cutting approaches (Performance and Innovation Unit, 2000: 5).

O'Donnell (2001) has identified a significant tension in this paper. On the one hand, the paper emphasises the need for a strong centre to provide co-ordination: "conflicting priorities will be sorted out at a strategic policy level and not allowed to undermine efficient and effective service delivery" (Performance and Innovation Unit, 2000: 27). But the paper also insists on "the need for the centre to recognise its limitations and … to look to service deliverers and end-users to signal where there are existing (or potential) failures to work cross-departmentally" (Performance and Innovation Unit, 2000: 63). The paper does not explain how to resolve the conflict between the need for, on the one hand, strong co-ordination at the centre and, on the other hand, local knowledge and responsiveness. It is argued by both O'Donnell (2001) and Sabel (2001) that there are organisational innovations that can overcome this tension with a new type of relationship between the centre and the local. The features of this new model are discussed in Section 5 on devolution in Chapter 5.

3.4.7 Public Service Agreements

A potentially significant reform in recent years in the UK, has been the introduction of Public Service Agreements (PSAs). These were first produced in 1998, alongside departmental spending plans for the next three years. The idea is that, in exchange for spending commitments, departments commit to achieving tangible results that are specified in the PSAs. The PSAs include aims, objectives and high level targets. For example, the aim for the PSA for the Department of Health is to change the health and social care system so that it produces services that deliver better health and tackle health inequalities. Objectives include improved health, improved patient experience of the NHS, fair access and value for money. The most demanding aspect of PSAs are the specific performance targets: for example, in the case of health these include commitments such as reduced mortality rates from heart disease by at least 40 per cent in people under 75 by 2010; a reduction in the maximum wait for an outpatient appointment to three months and the maximum wait for inpatient treatment to six months by the end of 2005. Progress towards meeting the targets in the PSAs is reported in annual reports produced by each department. A cabinet committee monitors progress towards targets set in the PSAs. There is also a public service productivity panel to help departments improve productivity.

PSAs have been subject to considerable criticism by public commentators in the UK. For example, John Garret (a public management consultant and former Labour MP) argued that the targets were over ambitious and lacked focus. Examples of inappropriate targets cited by Garret included: the percentage extension of coverage of new software for the principal civil service pension scheme; success in introducing a robust system for recording sickness leave; and the percentage change in the number of visits to the countryside (*The Guardian*, 5 April, 2000).

It has also been pointed out that some of the PSA targets have had counter productive effects. For example, setting a target for a reduction of National Health Service (NHS) waiting lists has had the effect of increasing waiting times. Targets for improved exam league tables led some schools to expel more disruptive pupils, while at the same time other targets called for fewer expulsions (*The Guardian*, 30 May, 2000).

A speech by the Chief Secretary to the Treasury in April 2000 accepted that many of the targets under the first round of the PSAs had shortcomings. He argued that this was the inevitable result of the radical nature of PSAs: “some of our targets are simply not very good because we were new to the business” (Smith, 2000). He stated that a new set of targets would be more focused on a limited number of key priorities.

A new, refined set of PSAs along with spending plans was published in July 2000. The first set of PSAs included 600 targets while the new PSAs concentrate on 160 high level targets. The PSAs are complemented by more detailed Service Delivery Agreements (SDAs). These set out in detail how the targets are to be achieved. Another feature of the new PSAs is the inclusion of a number of floor targets. The idea is that progress is made not only in terms of national averages but that all areas benefit. For example, no local authority is to have a domestic burglary rate more than three times the national average by 2005.

An interesting feature of the PSAs is the inclusion of a number of cross-departmental PSAs. These relate to areas such as crime and illegal drugs. For example, a PSA in relation to welfare to work is the joint responsibility of the departments of education, social security and the Treasury.

One limitation of the system of PSAs is that there is no provision for independent assessment of progress towards meeting targets: the government itself reports on progress. Further there are no formal penalties incurred when the targets are not met; the penalty is essentially the political cost of not meeting publicly set commitments.

The spending plans announced in July of 2000 indicate significant real increases in public expenditure over the next three years. The PSAs represent the government’s commitment to deliver improvements in public services on the basis of the increase in expenditure. The PSAs and associated annual reports are envisaged as the mechanism for measuring the extent to which the increase in expenditure is translated into real improvement in public services.

As such, the PSAs are of considerable political significance. It remains to be seen whether the revised PSAs system is a useful mechanism for relating public expenditure to the delivery of public services.

3.5 NEW ZEALAND[1]

3.5.1 Overview of Reforms

Reforms to the management of the public sector over the past decade in New Zealand have been more comprehensive and radical than those undertaken elsewhere. As in many countries, the reforms have been characterised by devolution of power from the centre and new arrangements for holding managers accountable for results. However, the devolution of authority to managers has been more extensive than that undertaken elsewhere and the new mechanisms for achieving accountability also go beyond those introduced in other countries. Reform of the management of the public sector has been part of wider reforms undertaken in New Zealand including deregulation, privatisation of state enterprises and reform of monetary policy. Our focus here is on reforms to the core public sector.

Public sector reform in New Zealand has a strong legislative basis. The two key pieces of legislation which initiated the reforms were the State Sector Act, 1988, and the Public Finance Act, 1989. Under the State Sector Act, the heads of Government Departments were replaced by chief executives with fixed term contracts. A change in the role of these chief executives has been central to the reforms. Chief executives have real authority and responsibility to manage their departments. The responsibilities of chief executives are negotiated in annual performance agreements between the chief executive and the minister.

The role of the chief executive is strongly distinguished from the role of the minister. The chief executive is responsible for providing services while the minister ‘purchases’ these services. The services

1 This Section draws on OECD (1997a) and Schick (1996).

provided by government departments are referred to as outputs. The chief executive is formally accountable for producing the required output. Output targets are set out in annual purchase agreements between the minister and the chief executive and progress in meeting the output targets is closely monitored. The impacts of the outputs produced by a government department or a government agency are referred to as outcomes. The outcomes are the responsibility of the minister rather than the chief executive. The distinction between the purchaser and provider has been used elsewhere in public sector reform but New Zealand is unique in applying this distinction at the level of a head of a government department and a minister.

Another significant distinction in the New Zealand model is that of the government interest as a purchaser and as an owner. As a purchaser, the minister's interest is in obtaining best value in the purchase of services. The minister may purchase services from more than one government department, other public organisations or from private suppliers; in practice most purchases are from government organisations. While a minister may purchase services from more than one department, a minister will have ownership interest in only one department. As an owner, a minister is concerned with the capabilities and performance of the department and has responsibility for providing capital to the department. According to a review by Schick (1996), in practice ministers have devoted most attention to their purchase rather than their ownership interest.

The approach to budgeting and accounting was fundamentally changed as part of the reform process. In place of conventional input-based estimates, appropriations are now made in the estimates for three areas: (i) the groups of outputs the government intends to buy from government departments, other public agencies and other sources (these are referred to as output classes); (ii) capital allocations to public organisations, transfers and grants; and (iii) other payments by the government. The estimates set out the outputs in broad terms. These are then refined in purchase agreements between the minister and chief executives of government departments.

Outputs are central to the accountability regime in New Zealand. In addition to the estimates and the annual purchase agreements, output targets may also be specified *ex ante* in strategic plans and other internal documents. The output targets that are specified are then closely monitored. Typically, there is provision for quarterly reports by chief executives to ministers on the progress made in producing the specified outputs. At the end of the year, annual reports are produced by chief executives covering financial and output performance. According to Schick, the monitoring arrangements have an enormous influence on the behaviour of chief executives and their departments. Chief executives organise their departments in order to maximise the achievement of the performance targets. This makes managers accountable in a very real way although Schick wondered whether this approach might unduly narrow managerial perspective. It tends to produce a ‘management by checklist’ mentality so that judgement and leadership may get sacrificed in order to achieve compliance.

It is possible to identify two overlapping sets of ideas that have provided the intellectual basis for the New Zealand reforms. It is worth briefly considering these as they help to illustrate both the strengths of the New Zealand reforms as well as some of the limitations. The first set of ideas involves the application of management principles in the public sector. Managerial reform is based on a simple principle: if managers are to be held responsible for results, they must have genuine autonomy to act in achieving the organisation’s objectives; this implies, for example, freedom to spend within agreed budgets, to make choices regarding office accommodation and so on.

The second set of ideas on which the New Zealand reforms are based is derived from a number of related areas of economic theory: new institutional economics, agency theory and transaction cost economics. These theories extend the assumption of self-interested behaviour beyond market transactions to other contexts such as the public service. This branch of economics views all economic relations as either implicit or explicit contracts. However, due to self-interest the parties may seek to behave opportunistically.

Another factor that promotes opportunistic behaviour is bounded rationality. All parties to a contract do not have all the information to ensure that the terms are being fully honoured. This approach points to the importance of minimising the scope for opportunistic behaviour in the public service and government.

The central assumption in these economic theories is self-interested behaviour. Given the assumption of self-interested behaviour, a central concern is opportunism. Insofar as it relates to the organisation of government, the key insight is that government should be organised so that opportunistic behaviour is minimised.

The two sets of ideas have many common implications regarding the reform of the public sector. Both approaches point to the desirability of clear specification of objectives, good information systems and giving managers the freedom to manage resources. However, the implications of new institutional economics/agency theory go further than the managerial approach and explain some of the unique features of the New Zealand reforms. Many of the contractual and quasi-contractual reforms introduced in New Zealand reflect ideas in new institutional economics. These include the use of formal purchase agreements between ministers and chief executives, the distinction between purchase and ownership interests and the extent of the formal accountability requirements that have been established (Schick, 1996).

3.5.2 Strategic Goals and Prioritisation

The highest level outcome goals are set by the government. They are currently referred to as "key government goals to guide public sector policy and performance" (previously referred to as strategic results areas, SRAs). The key government goals in conjunction with what are known as 'fiscal provisions' (the planned level of discretionary expenditure for the next fiscal year and following two years) are useful in prioritising public expenditure. The fiscal provisions set a transparent budget constraint while the key government goals outline the highest priorities within that constraint. The high level goals are translated into the work of departments through a variety of mechanisms including key priorities (previously referred to as key results areas, KRAs). Key priorities are an important part of the chief executives' performance agreements. Chief executives are responsible for the delivery of key priorities which are generally output rather than outcome measures (PUMA, 2001).

3.5.3 Strategic Result Area (SRA) Networks

A paper produced by the State Services Commission (SSC) in 1998 outlined a new model of SRA networks that is designed to strengthen strategic management and in particular strengthen the link between strategic planning and resource allocation in the budget. The basic structure of the SRA network as envisaged by the SSC is as follows. Based on its vision of society, the government identifies a limited number of SRAs (the SSC suggests eight to ten areas). A Cabinet Committee (an SRA committee) is formed around each SRA. This committee is chaired by a senior minister (known as an SRA Minister) who acts as the SRA champion and is responsible to cabinet for the achievement of the SRA. In addition to the SRA minister the committee consists of those ministers whose departments or agencies have a substantial contribution to the achievement to the high level SRA objectives. These ministers are responsible for purchasing the required outputs from their department or agency in support of the SRA. The role of the SRA committee is to identify the mix of policy interventions and outputs to achieve the SRA at an early stage of the budget cycle. The SRA committee in effect directs the purchase decisions of each individual network minister so that the outputs required for the achievement of the SRA are purchased. This paper was initially very influential and led to the Prime Minister establishing a series of ministerial teams to focus on strategic priorities. However, these teams were only in place for a limited time and following an election the new Prime Minister dropped the idea completely (Derek Gill, State Services Commission, personal communication, 2001).

3.5.4 Assessment of Reforms

The New Zealand reforms have been subject to a number of assessments. An assessment of the reforms by an American professor of public policy (Schick, 1996), commissioned by the Treasury and SSC, concluded that:

> Both within government and among outside observers interviewed for this study there is overwhelming consensus on the superiority of the reformed system and hardly any sentiment for dismantling the new arrangements and going back to centralised control. The reforms have improved the efficiency and quality of public services by encouraging managerial initiative and rewarding success. Managers have a much clearer understanding of their role and responsibilities; more timely and complete data on the cost of doing business and what they are accomplishing with public funds; greater awareness of the needs and interests of the clients and customers; and expanded opportunity to change operating procedures, the use of resources, and working conditions (Schick, 1996:14).

The 1999 OECD *Economic Survey* of New Zealand found that the core public sector has been reduced substantially both in terms of its share of expenditure and employment. Given that higher levels of outputs have been produced with lower levels of inputs, productivity has increased, costs have come under better control due to accounting changes and many departments have attained departmental surpluses (OECD, 1999: 88).

Notwithstanding the positive effects of the reforms, a number of problems have been identified in the assessments. Many of these problems concern weaknesses in strategic management. An early review of the reforms published by the SSC in 1991 (known as the Logan Review) identified problems in relation to how governments set strategic priorities and how the public service assists government in achieving its goals. Following the Logan Review, a system of strategic result areas (SRAs) and key result areas (KRAs) was established. Schick (1996) provided a generally favourable assessment of the system of SRAs/KRAs. Nonetheless, he still found that “the New Zealand system is geared more to the short-term production of outputs than planning for the long haul, and to account for what is being produced rather than to evaluate progress in achieving major policy objectives” (Schick, 1996: 53).

In response to concerns about the responsiveness of the public service to strategic goals, the SSC was requested to investigate New Zealand’s strategic management system and the extent to which it is effective in articulating broad government goals and in focusing the public service on the achievement of these goals. The following problems with the strategic management system were identified by the SSC.

First, insufficient attention is given to outcomes. Government departments are very much focused on achieving their output responsibilities and have not tended to focus in sufficient depth on how their outputs related to the desired outcomes of government. Second, while the system of SRAs improved co-ordination, the SSC still found deficiencies in this area. Third, the SSC found that the budget operates independently of strategy and that there was no informed feedback in the budget process to indicate whether the mix, trade offs and amounts in the previous budget were appropriate, given the desired effectiveness goals. Finally, there is little evaluation of the extent to which public programmes achieve the desired outcomes. The reasons identified for this include low demand for evaluation by ministers,[2] the focus by departments on outputs and lack of evaluation capabilities (State Services Commission, 1998).

These types of problems are not unique to New Zealand. However, the persistence of problems of this kind after more than a decade of perhaps the most radical and thoroughgoing reforms is noteworthy. It illustrates that the process of reform is complex and ongoing.

2 The low demand for evaluation from ministers may seem surprising given that there is so much emphasis on results in the New Zealand system. It is worth noting that it is ministers who are responsible for policy outcomes. To the extent that evaluation finds that a policy is not contributing to a policy outcome, this may be more problematic for the minister than the chief executive (head of department) who is only responsible for outputs.

3.6 CANADA

3.6.1 Expenditure Reform in the 1980s[3]

Canada introduced a new system for managing public expenditure known as the Policy and Expenditure Management System (PEMS) in 1980. This was introduced to address a range of problems in management and administration of federal government. Planning and priority setting had become divorced from expenditure decisions; total government expenditure was difficult to control and plan and ministers felt that they had little control over strategic government decisions.

The PEMS involved two key features:

- the preparation of long-term fiscal plans encompassing government revenues and expenditure over a five-year period. This was to set out the overall fiscal constraints within which policy choices would be made; and
- the establishment of a series of envelopes that included all spending in a particular policy area with overall expenditure ceilings for each envelope.

The long-term plan was designed to achieve overall control of expenditure while the new system of envelopes was to address priorities in public expenditure. The budget was divided into ten envelopes. For example, one envelope covered all areas of spending in economic development, including agriculture, fisheries, industry, tourism and so on. Each envelope was administered by a cabinet committee, composed of the ministers whose spending was included in a given envelope. Objectives were set for each envelope by the cabinet. The idea was that each committee would achieve the agreed objective within the resources of the envelope. The grouping of expenditure programmes related to a given objective which, together with limits on expenditure was expected to encourage the reallocation of resources from less effective to more effective programmes.

3 This Section draws on Blondal (1999).

It is widely acknowledged that the PEMS reforms were a failure and were finally abandoned in 1994, the system of reallocation within expenditure envelopes not having worked as planned. It had been thought that the envelope system would facilitate reallocation of resources to more effective programmes within the envelope. However, a report by the Treasury Board Secretariat found:

> The incentive for individual ministers to offer up reductions was weak since the end result would be the reallocation of these resources often to another minister…PEMS was based on a shared approach to fiscal management. It did not succeed because the partnership that was envisaged was never achieved (Treasury Board Secretariat, 1995).

With the failure of PEMS, alternative means were used to control expenditure. The key mechanisms used were wage and entitlement benefit freezes and across-the-board cuts. While this was the most politically acceptable route in the first instance, the reliance on across-the-board cuts served to undermine any sense of priority setting in government (Blondal, 1999: 8). This realisation pointed to the need for reform of the management of public expenditure.

3.6.2 Expenditure Management System

A reformed budgetary system was introduced in 1994/95 in the form of a new Expenditure Management System. The first reform was the introduction of a hard budget constraint: the government committed itself to a deficit target of 3 per cent by 1996/97. The government decided that across-the-board cuts would not be sufficient to meet the new hard budget constraint. Instead, targeted reductions were to be made. To achieve the targeted reductions, a new process of Programme Review was introduced. This was a review of all aspects of spending to ensure that lower priority programmes were reduced or eliminated and that the government resources were directed to the highest priority requirements. The process was directed by a cabinet committee comprised of senior ministers. Departments were first asked to review their own programmes but this did not yield significant savings. Subsequently, departments were given targets, proposed by the Department of

Finance and approved by ministers. The process of Programme Review is considered to have been successful in establishing fiscal consolidation.

3.6.3 Management Reforms

In addition to establishing fiscal consolidation, Canada in recent years has introduced many reforms to the management of the public sector. There has been significant progress in relaxing input controls. Spending agencies now have considerable flexibility to move funds between different types of operating costs but central controls remain significant in relation to human resource management and common service provision. Recruitment to the public service and negotiation of collective agreements are organised centrally. The provision of certain services, in particular office accommodation, is also done on a central basis. Greater freedom from input controls is provided on a selective basis for Special Operation Agencies (SOAs). SOAs are designed mainly to ring-fence activities that generate user charges.

As part of the efforts to improve performance, government departments are asked to examine alternative service delivery mechanisms. These alternatives include SOAs, partnership with the private sector, devolution to the provinces, commercialisation of ongoing services and privatisation of government services.

The introduction of greater managerial flexibility has been paralleled by a greater emphasis on accountability for results. In 1995, the Improved Reporting to Parliament project was introduced. This seeks to provide better information to parliament mainly by augmenting financial information with performance information. There are two aspects to this reform. First, the plans and priorities of government departments are included in the presentation of the estimates to parliament. Second, at a later stage, performance reports on departmental activities are presented to parliament. Departments are given extensive guidance on the performance information that the reports should provide. The aim is to produce reports that enable a reader to judge how well a department is performing.

3.6.4 Conclusion

At a macroeconomic level, Canada has succeeded in establishing control of aggregate public expenditure. In addition, Canada has made progress on a number of dimensions of management and accountability. Centralised controls have been reduced, accompanied by a new focus on reporting for results. A feature of reform in Canada is that it has avoided adopting a ‘big bang’ model of reforms. Instead, it has adopted a more gradual approach characterised by extensive use of the piloting of reforms.

3.7 THE UNITED STATES

3.7.1 Introduction

The US has a long history of seeking to develop a results focus in the management of public expenditure, especially in relation to budgeting. A federal commission in 1949 recommended the introduction of performance budgeting; i.e., the federal budget should be based on functions, activities and projects and performance information provided along with financial reports (Tyer and Willand, 1997:5). Performance budgeting was subsequently adopted by the federal government but was not regarded as particularly successful and also lacked the tools to address long-term problems. Variations of performance budgeting were adopted at state level but a study by Schick (1971) of state budget practices in the late 1960s and 1970s concluded that performance budgeting reforms had been superficial.

3.7.2 Planning Programming Budgeting System

The most ambitious attempt to reform budgeting in the US was the development of the Planning Programming Budgeting (PPB) system. PPB sought to elevate the role of strategic planning in the budget cycle as well as achieving the traditional budgetary goals of control and management. PPB was first developed in the Department of Defence and was extended to all federal agencies in the mid-1960s. It was inspired by developments in macroeconomics, microeconomics and systems analysis. The influence of Keynesian economics encouraged policy makers to view the total level of spending and taxation as significant policy instruments that affected the economy and hence the need to plan for the appropriate level of these totals. Welfare economics encouraged a focus on the social costs and benefits associated with allocation decisions. At the same time it was hoped that systems analysis would make it possible to cope with the informational and analytical burdens arising (Schick, 1966).

PPB called for the clear identification of the goals and objectives of each area of government activity. It emphasised the importance of a multiannual approach to budgeting, both in terms of planning for the achievement objectives and in considering the long-term costs associated with current decisions. A crucial aim of PPB was the analysis of alternative means of achieving policy objectives and the achievement of these objectives at the least cost. It therefore sought to incorporate the analysis of policies and programmes into the annual budget cycle (Schultze, 1968).

The PPB reforms were generally unsuccessful, although elements of the experiment are said to remain in the budget frameworks of several budget agencies (Tyer and Willand, 1997: 6). In the 1970s, PPB was succeeded by Management By Objectives (MBO) and then by Zero-Base-Budgeting (ZBB) although these reforms also proved unsuccessful (Groszyk, 1996:73).

3.7.3 Performance Budgeting at State and Local Level

During the 1990s there was a renewed interest in performance budgeting in the US. One factor that contributed to this renewed interest was the bestselling book on public sector reform, *Reinventing Government* (Osborne & Gaebler, 1992). Osborne and Gaebler advocated ‘results-oriented’ budgeting. They highlighted its successful application in Sunnyvale, a small city (population 120,000) in California. Sunnyvale measures the quantity, quality and cost of every service delivered amounting to thousands of performance measures. Information on the quantity and quality of services provides the basis for the budget. The council decides on the level of services to be produced and the unit cost and then gives managers freedom to achieve these targets.

Performance budgeting of some form is now widely used at state level. Melkers and Willoughby (1998) report the results of a survey on the extent of what they referred to as performance based budgeting (PBB) at state level. They define PBB as "requiring strategic planning regarding agency mission, goals and objectives and a process that requires quantifiable data that provides meaningful information about program outcomes". PBB may also require an assessment of agency progress towards specified targets. They find that almost all states now have some form of PBB defined in this way. The formal adoption of performance budgeting, however, does not in itself imply that performance information has much impact on budget decisions. A 1993 study by the Congressional Budget Office of performance budgeting at state and local level concluded that performance measures did not appear to significantly influence the allocation of budgetary resources (quoted in Tyer and Willand, 1997). A more recent study by Willoughby and Melkers (2000) reported conflicting views on the success of PBB.

Mikesell (1995) distinguishes the performance budgeting in recent years in the US (what he refers to as new performance budgeting) from the traditional performance budgeting in the 1950s. He argues that the new performance budgeting seeks to give more emphasis to outcome measures while older performance budgeting concentrated on activities or direct outputs. He also notes that the new performance budgeting is less ambitious than PPB in that it does not seek to compare similar programmes that are operated by different agencies.

3.7.4 Federal Reform in the 1990s

The experience of Sunnyvale received widespread national attention in the US and, notwithstanding the small size of the city, its success was one source of inspiration for a major performance management initiative at federal level, the Government Performance and Results Act (GPRA), 1993. This act provided legislation for a performance management system covering all federal agencies. The other source of inspiration for the GPRA was the apparent success of performance management initiatives in other OECD countries, such as Australia and New Zealand. The GPRA requires agencies to prepare strategic plans, annual performance plans (setting out performance goals) and annual performance reports while the central budget office (the Office of Management and Budget, OMB) prepares a government-wide performance plan. Although the legislation was passed in 1993, there has been a long phase-in period of implementation, including provision for pilot projects. Federal agencies submitted annual performance reports in 2000 for the first time.

The GPRA was paralleled by another significant federal reform initiative, the National Partnership for Reinventing Government (NPR, formerly the National Performance Review). The NPR has many dimensions, including the establishment of customer service standards, performance agreements between the President and Cabinet Secretary or head of independent agency, and performance partnerships between the federal government and other levels of government. One unusual and interesting feature of the NPR is that it involved an unusually high level of political commitment and political profile to the issue of government reform. An independent assessment of the NPR was produced by a researcher in the Brookings Institution in 1998 (Kettl, 1998). It is not intended here to go into all the strengths and weakness of the NPR but it is worth noting that the review found that there were substantial improvements arising from the initiative even if many performance problems persist. The review argued that reinventing government was more an evolutionary than a revolutionary movement and that it should continue in some form. The review identified a central dilemma to reinventing government as how to define accountability for performance in the many cases where the (federal) government's partners share responsibility for performance.

3.7.5 Conclusion

The US has been characterised by many inititiatives to reform budgeting as well as wider inititatives to reform government. Even where high profile initiatives such as PPB are abandoned there may still be incremental benefits from ongoing reform. It is argued by Cothran (1993:445) that, "although none of these efforts, such as performance, programme or zero-base-budgeting entirely supplanted incremental line-item budgeting, elements of these reforms endure in the budgeting process of many governments" (as quoted by Tyer and Willand, 1997). A consistent theme running through the reforms is a desire to place more emphasis on the outputs to be produced or results of government activity rather than detailed control of the inputs used by government.

3.8 SWEDEN[4]

There have been two broad dimensions to reforms in the area of public expenditure in Sweden since the beginning of the 1990s. One dimension has been budgetary reforms designed to achieve better control of aggregate expenditure. The other dimension has been new public management (NPM) reforms to achieve a better focus on results and to decentralise the management of expenditure.

3.8.1 Budgetary Reform

Fiscal crisis in the early 1990s pointed to the need to establish better control of total public expenditure. An evaluation undertaken in the early 1990s found that the Swedish budget process performed relatively badly by comparison to other European countries with respect to expenditure control. The reforms have involved the adoption of a multi-year budget framework and a more top-down budget process (although management of the public service continues on a decentralised basis, as discussed below). At an early stage in the budgetary process the cabinet approves the level of total expenditure and indicative funding levels for 27 broad expenditure areas. These decisions are taken before approving detailed expenditure plans. These decisions are formalised in a fiscal policy

4 This Section draws on Blondal (1998).

bill; this makes it more difficult to change a decision at a later stage. In the third phase, decisions are taken at a detailed level of individual appropriations. The Ministry of Finance largely withdraws from this stage of the process; allocations within individual spending areas are made by the individual ministers.

It is at this stage (i.e., during the final allocation by ministers) that performance information is first considered in the process. Performance information is provided by the annual reports of government agencies. However, the agencies consider that limited use is made of the performance information provided. In the early 1990s, it was envisaged that performance information would play a key role in the budget process. The idea was that every three years the agencies would prepare an in-depth assessment of their activities, questioning old priorities, identifying new priorities and so on. However, this did not evolve as planned. One problem was that the assessments were universally positive about every aspect of agency activities. This process also resulted in very large budgetary submissions and it was not feasible to process the information. A 1997 OECD report commented that, "budget reformers in Sweden have relearned an old lesson – that the questioning of results and purposes cannot always be done according to calendar and deadlines of budgeting" (OECD, 1997a: 103-104).

3.8.2 Role of Parliament

Because Sweden has a history of minority governments, parliament tends to play a more significant role in budgetary matters than is typical in parliamentary democracies. The budgetary reforms have reduced the influence of the parliament on the budget. Prior to reforms, the budget approval process extended over five months and the level of expenditure would invariably increase during the parliament's discussion of the budget. The reformed process is now more disciplined. Prior to the presentation of the budget, parliament now approves the level of aggregate total expenditure. At this stage of the discussion it focuses on the macro context rather than the details of expenditure. At a later stage the parliament discusses the budget. The parliament first gives final approval for the allocation of expenditure into 27 expenditure areas and subsequently provides approval for the individual appropriations within these areas. Committees play a key role in the parliament's budgetary deliberations. The Finance Committee is responsible for the overall budget proposal and the allocation into the 27 expenditure areas. Sectoral committees are then responsible for allocations within the respective expenditure areas. The focus of these committees has increasingly been on performance, although parliament has expressed dissatisfaction with the type of performance information that is provided.

3.8.3 Management Reform

The basic structure of the public sector in Sweden has not been changed by the reforms of the last decade. While several countries during the 1980s and 1990s reorganised the public sector by separating policy work and operational functions (for example, the Next Steps agencies in the UK), the public sector in Sweden has been structured in this way since the 1700s. Government ministries only account for 1 per cent of government employees. Policy is implemented by government agencies that employ the remaining 99 per cent of employees. This structure of government would appear ideally suited to the development of a result-oriented management system. Prior to reform, ministries issued detailed letters of instructions to agencies. In principle, it would have been a straightforward matter to change this; instructions and reporting requirements in relation to inputs would be replaced by specifications for results and associated reporting on results.

The first part of reform has been implemented. Reforms in recent years have systematically removed control on the use of inputs by agencies including restrictions on personnel management and accommodation. In addition, agencies can carry forward savings from one fiscal year to the next. According to Blondal (1998:24), "in no OECD member country do managers enjoy greater flexibility in the management of their organisations than in Sweden".

The second dimension of reform, switching to a new accountability based regime, has been more difficult. The idea was that the ministries would specify results to be achieved by the agencies and the agencies would then report on the results through annual reports. This has not worked out as originally expected. Ministries have had difficulty in effectively specifying results so that often there are no, or only vague, benchmarks under which the agencies may be held accountable. However, it is not necessarily undesirable that the model had not been implemented precisely as intended. Blondal has pointed out that, if the system had been applied as thoroughly as originally envisaged, it would have represented a culture shock and interfered with the relationship based on informal dialogue between the ministries and the agencies. The ministries would also have had to significantly increase their resources if they were to issue a detailed specification of results without the assistance of the agencies. The value of such investment is questioned by Blondal. Weaknesses in the specification of results have limited the effectiveness of annual reports as a means of holding the agencies accountable. However, the quality of such reports is improving and the fact that the reports are audited (both performance and financial information is subject to audit) provides agencies with an incentive to improve reports further.

3.8.4 Conclusion

Reform has resulted in a more disciplined budgetary process in Sweden. This has somewhat reduced the influence of the parliament on budgetary matters but it continues to have a significant role. The public sector in Sweden has long been organised in terms of small policy-focussed ministries and large service delivery agencies. Recent reform has successfully scaled back input controls but introducing a results-based accountability regime has proved more difficult.

3.9 AUSTRALIA

Reform of the public sector in Australia was motivated by a desire to improve performance. The first wave of reforms in the 1980s emphasised reducing controls that blocked managerial initiative and the devolution of authority to line departments and (to a lesser extent) agencies. Reforms in more recent years have placed more emphasis on market mechanisms as well as the development of accruals-based budgeting.

3.9.1 Financial Management

The Financial Management Improvement Programme (FMIP) sought to improve the performance of public administration by devolving authority to spending departments and agencies. Departments have been given flexibility in relation to their administrative costs: within budget limits there are few restrictions on transferring items within administrative budgets. A contentious aspect of these arrangements has been the efficiency dividend. It has been assumed that departments should be able to achieve efficiencies under the new arrangements. To reflect this, administrative budgets are adjusted downwards by 1 per cent each year. Additional flexibility can also be negotiated between departments or agencies and the Department of Finance through resource agreements. As a result, these agreements may allow agencies to retain revenue from charges or link additional spending to increases in workload (OECD, 1997a).

3.9.2 Forward Estimates

Forward estimates have been identified as an important reform that has helped the system to allocate resources in line with strategic priorities, subject to overall fiscal constraints (Campos and Pradhan, 1999; Dixon, 1996). Forward estimates are three-year forecasts of the costs of existing policies. They are rolled forward each year and updated in a semi-automatic way for parameter changes, in particular, changes in inflation, unemployment and the exchange rate.

This system of forward estimates has a number of advantages. First, it has allowed ministers to devote more time to policy changes. The system provides more time for the analysis of both spending and saving proposals. Second, when a decision on a policy change is being made, attention is given to its impact on expenditure over the three years covered by the forward estimates. Third, departments and agencies benefit from greater certainty in their budgets. Fourth, the inclusion of the forward estimates as an integral part of the budget documentation has aided transparency. Budget documentation shows a reconciliation between this year's estimate and the forward estimate from the previous year. The difference is explained in terms of the differences due to parameter changes (inflation and so on) and differences due to policy changes that either increase or decrease expenditure (see Table 3.1) (Dixon, 1996: 24-27; Campos and Pradhan, 1999: 253-254).

Table 3.1

Reconciliation of Forward and Budget Estimates in Australia 1995–96 A$million

	Forward Estimates (from previous year)	Budget Estimates (current year)	Difference between Budget & Forward Estimates	Parameter & other Estimates Variations	Policy Decisions		
					Increase	Decrease	Net
Defence	10010	9992	-18	-29	26	-15	11
Public Order & Safety	847	942	95	76	31	-13	18
Education	10434	10703	269	292	91	-114	-23
Health	18164	18420	256	331	74	-149	-75
Social Security & Welfare	44373	45237	865	582	444	-162	282

Source: Dixon (1996).

3.9.3 Accruals Budgeting

Australia has been a pioneer in the development of accruals accounting and budgeting (Boyle and Humphreys, 2001). In the 1999/2000 fiscal year, Australia introduced a full accruals-based budget based on an output and outcomes framework. This builds on earlier reforms and is designed to sharpen the focus on developing a performance culture. Appropriations are now made against outcomes (policy objectives). A series of outputs (services to be delivered) that contribute to these outcomes are then identified in the Portfolio Budget Statements produced by each government agency. Progress in delivering the planned outputs and the efficiency of this output is then shown in annual reports. Lastly, agencies are required to clearly show how information on planned performance and actual performance relate to each other. The first experiences of this new output and outcomes framework indicate that it is making a contribution to improving transparency and accountability and enhancing the efficient delivery of services (PUMA, 2001).

3.9.4 Other Recent Reforms

Until recently, a feature of the Australian reforms has been that the reform agenda has not sought to ‘decouple’ policy-making and service delivery. Such decoupling has been a feature of reform in a number of countries, notably the UK and New Zealand. However, in the mid-1990s, a major change occurred in Australian thinking on the relationship between policy and delivery. The combination of policy and implementation had been thought to be desirable in order to maintain effective feedback from those delivering services, but now it is considered that the separation of policy and delivery provides important benefits including greater choice, flexibility and improved accountability (Halligan, 1998).

This new approach was reflected in a requirement by departments and agencies to systematically review all their activities. Departments and agencies were required to consider the appropriateness of continuing all the activities or whether the activities should be devolved to another level of government. If the activity was to be continued, consideration was to be given as to whether performance could be improved by the use of market-based approaches including competitive tendering, benchmarking performance against best practice in the private and public sectors, the use of purchaser/ provider arrangements (with other public, private or voluntary organisations) and partnership arrangements (Department of Finance and Administration, 1998).

Another development in recent years was the introduction of service charters. This move was inspired by the UK experience with the Citizen's Charter. A service charter is a short statement of the service standards that an organisation is committed to delivering. In Australia, this concept has been applied to both direct and indirect service providers and regulatory bodies, with the charter approach being adopted at all levels of government.

3.9.5 Conclusion

The process of public service reform in Australia is continuing. Compared to the New Zealand model with its basis in new institutional economics and public choice theory, reform in Australia has a more pragmatic basis and places greater emphasis on maintaining a unified public service and traditional public service values of commitment, integrity and impartiality (Byrne et al., 1995: 130). A distinctive feature of the Australian model is its widespread use of evaluation. In more recent years, the decoupling of policy and service delivery has been emphasised so that the future is likely to see more contestability of service delivery (Halligan, 1998).

3.10 CONCLUSIONS

One of the most difficult challenges in managing public expenditure is to relate annual public expenditure allocations to the achievement of strategic policy objectives. The experiences discussed above illustrate a number of approaches to this challenge. The PPB system in the US sought to incorporate strategic planning into the budget system: "the PPB system sweeps the specification of objectives, the design of programmes, and the evaluation of benefits relative to costs into the budgetary process" (Schultze, 1968: 14). This attempt ultimately proved to be over ambitious but the US is still seeking to strengthen the links between strategic planning and the budget through its current reforms. The UK system of PSAs is a recent innovation introduced to strengthen the relationship between public spending decisions and the achievement of higher level policy objectives.

Less emphasis on the detailed control of inputs associated with traditional budgeting is a feature of recent public sector reform. There is widespread agreement across many countries that a system of management based on the detailed control of inputs from the centre is not the most effective way of managing the public sector. There are nonetheless exceptions to this trend: countries in which centralised financial control is still regarded as a virtue include Germany and Japan (OECD, 1997a).

The provision of greater flexibility in the use of resources to spending departments and agencies has not compromised spending control. In fact it has proved easier to maintain cash limits when managers have to manage within a fixed budget rather than having the centre controlling the details of expenditure (OECD, 1997a: 23). In exchange for greater flexibility in the use of resources, government departments and agencies are expected to provide greater accountability for the results achieved. All of the countries discussed in this Chapter have devoted considerable efforts to the measurement of performance. The UK, for example, makes extensive use of service charters and the publication of league tables on performance and, in New Zealand, purchase agreements between ministers and chief executives are a key mechanism for focussing on results. The publication of annual reports on performance is an important mechanism in several countries.

A greater emphasis on results in the management of public expenditure has implications for both financial management and performance management systems. The measurement of results is a feature of performance management systems while expenditure decisions are an essential component of financial management systems. Thus, a greater focus on results in the management of public expenditure implies some degree of integration between financial management and performance management. Notwithstanding the advantages of integrating financial and performance management, Pollitt (1999) points out that integration of this kind may be difficult and often does not take place. The role of performance information will vary at different levels. At the higher levels, the most significant factors are political values and macroeconomic considerations. However, performance information (i.e., information on the effectiveness and efficiency of programmes and policy options) can inform political decisions.

Achieving co-ordination across government departments and agencies is a common challenge. It is an issue that is now receiving greater attention in several countries. A criticism of ‘new public management’ reforms is that aspects of the reforms may have made it more difficult to address cross-cutting issues. This may arise from an increased emphasis on horizontal accountability and a focus on purely organisational results. For example, in relation to the British experience, Sabel has argued that:

> Narrowing programmes in the interest of accountability had the unintended consequence of making it difficult to co-ordinate the narrower entities… Given specific tasks, and encouraged by new incentive structures to focus exclusively on them, and contract with others to provide collateral services, what was to induce the agencies to co-operate among themselves to solve problems requiring their joint action? (Sabel, 2001: 129)

A significant issue in the organisation of government is the relative merit of integrating policy advice and operational activities within the same organisation or decoupling these functions in separate organisations. The case for integration is that it facilitates feedback from those involved in implementing policy to those who advise on policy and thus helps policy advisors develop a better understanding of the issues. On the other hand, separating these functions may enhance the efficiency and effectiveness of both: the delivery of services may be more efficient in agencies with clearly defined objectives while, freed from administrative details, senior officials may provide better policy advice. Sweden has a long tradition of small policy focussed government departments; the UK and New Zealand reorganised in this way during the 1980s and 1990s while current policy thinking in Australia favours decoupling. However, in a White Paper (Cabinet Office, 1999), the UK government expressed its desire to strengthen the links between policy making and implementation but it has not proposed reversing the new structures.

Another feature of reform has been more use of alternative delivery mechanisms for public services. These include contracting out the delivery of services to the private and voluntary sectors and also partnerships with these sectors. While the public service has always purchased services from the private sector, in recent years there has been a willingness to consider the possibilities for contracting out a wider range of services in order to improve efficiency and choice.

This Chapter has illustrated the types of reforms of relevance to the management of public expenditure that are being undertaken in OECD countries. This international experience is drawn upon in the discussion of the key issues in the management of public expenditure in Ireland in Chapter 5. As background to this discussion, Chapter 4 provides an overview of the Irish system of managing public expenditure and describes recent reforms.

CHAPTER 4

THE MANAGEMENT OF PUBLIC EXPENDITURE IN IRELAND: A DESCRIPTIVE OVERVIEW

4.1 INTRODUCTION

The purpose of this Chapter is to describe the main features of the Irish system for the management of public expenditure. Section 4.2 outlines how the Estimates/Budget cycle works and describes the roles of key actors in this process. Section 4.3 describes recent and ongoing reforms to the management of public expenditure. These reforms include the development of a new management information framework, a programme of expenditure reviews, devolution of administrative expenditure to Government Departments, changes in the roles of the Comptroller and Auditor General (C&AG) and the development of the Strategic Management Framework under which Government Departments and Offices prepare strategy statements, business plans and annual reports.

4.2 THE BUDGETARY SYSTEM[1]

4.2.1 Outline of the budgetary process

While Budget day is the highlight of the budgetary cycle, the announcements on Budget day only refer to a small portion of public expenditure or receipts. The process of reaching agreement on the components of the Budget extends over most of the preceeding year and the subsequent approval by the Dáil of budgetary measures is only completed in the following year. A brief outline of the main steps of the process is provided in the following paragraphs.

1 This Section draws on the Department of Finance (1998), *Public Financial Procedures.*

The process begins in the spring with the preparation of three-year 'no policy change' (NPC) projections of expenditure and revenue. These are projections of the costs of providing the existing levels of services and benefits and projections of revenue assuming no changes in the tax system. On the basis of the NPC projections, the Government approves initial targets for the main budgetary aggregates; i.e. total taxation, expenditure and the level of surplus or deficit. In June, the Department of Finance issues an 'Estimates Circular' to Government Departments indicating the basis on which Estimates should be prepared for the coming year. Typically, the sum of the Estimates demands submitted by Governments Departments greatly exceeds total resources available.

It is important to understand the background against which decisions on the public services spending side of the Budget are taken. The starting point for discussions between the Department of Finance and the spending Departments is Government policy on specific sectoral policies and the overall stance on budgetary policy. The demands put forward by Departments are discussed against that starting point. The discussions examine all public service programmes whether of strategic national importance or of relatively low priority and also consider the extent of ongoing legal commitments and discretionary expenditure.

Ministers are also deeply involved in the resource allocation process. Proposals submitted to the Department of Finance will be cleared in advance by the relevant Ministers. Before official level discussions, Ministers indicate clearly to their Departments their priorities for the negotiations. When officials have clarified the issues for political discussion, the bilateral negotiations take place between spending Ministers and the Minister for Finance. Issues requiring final political resolution are brought to Cabinet for decision.

The social partnership process has a significant role in relation to the resource allocation process. While the various programmes agreed with the partners serve to promote national priorities for the period of the agreement, they also normally contain commitments sought by particular component organisations within the various groups comprising social partnership.

A crucial aspect of the process is achieving consistency between Departments' spending demands and the Government's overall spending plans. The Department of Finance holds detailed discussions with Departments in order to ensure that strategic Government policy objectives and programmes are prioritised and funded and to reconcile the spending demands with the budgetary strategy endorsed by Government. The Government is briefed on the outcomes and it makes final decisions on resource prioritisation across programmes. This process culminates in a Government decision on detailed expenditure allocations.

A summary version of the Estimates is then published, usually in October or November. This summary version is a significant document as it represents a decision on the main elements of expenditure for the following year. Shortly before the Budget, the *White Paper on Receipts and Expenditure* is published. This sets out projected expenditure (both voted and non-voted) and estimated tax revenue for the coming year, before taking account of any tax or expenditure changes on Budget day. In December, the Minister for Finance produces the Budget. This sets out the Government's overall budgetary targets (for borrowing, expenditure and taxation) for the following year, outlines revisions to the tax system and usually makes significant changes to the previously published Estimates including in particular the cost of changes in social welfare expenditure which are announced in the Budget.

The budgetary process continues into the following year (i.e., the year in which the expenditure and revenue are implemented). In March, revised Estimates are published along with the Public Capital Programme. In April, the Dáil enacts the Finance Bill. This gives legislative effect to the tax changes announced in the Budget. In the middle of the year the Dáil votes on the Estimates. These are approved by way of financial resolutions that provide temporary approval for the expenditure. Over the remainder of the year, Supplementary Estimates may be submitted to the Dáil if required.

In December the Appropriation Bill is passed. This gives statutory effect to the Estimates approved by the Dáil.

4.2.2 Role of the Oireachtas

Formal authority for public expenditure rests with the Dáil. Public expenditure may only be appropriated (i.e., approval granted for a given amount of expenditure for a specific purpose) with the authority of the Dáil. However the right of the initiative in relation to taxation and expenditure matters rests with the Government. Under Dáil standing orders, the Dáil can approve or reject the public finance measures proposed by the Government but it cannot amend these proposals. The Seanad meanwhile does not have the constitutional right to introduce or amend public finance measures, but can make recommendations to the Dáil.

One factor that limits the effective influence of the Dáil in relation to public expenditure matters is the timing of the presentation of the Estimates to the Dáil. The Dáil first votes on the Estimates (in the form of financial resolutions) in the middle of the year to which the expenditure relates. The final legislative approval of the Estimates in the form of the Appropriation Act is only enacted at the end of the year to which the expenditure relates.

4.2.2.1 The Public Accounts Committee

The primary role of the Public Accounts Committee (PAC) is to report to the Dáil on the annual Appropriation Accounts (ie, the accounts of the expenditure approved in the Estimates) and on the C&AG's report on the accounts. It also reports to the Dáil on reports prepared by the C&AG on value-for-money examinations and on other reports prepared by the C&AG. Secretaries General of Government Departments appear before the PAC (in their role as Accounting Officers) to be examined on the monies voted for their Departments. A formal reply to a report of the PAC is prepared by the Department of Finance. Any specific recommendations are carefully considered in this report although the Government is not obliged to accept the recommendations. By tradition, the chairman of the PAC is a member of the Opposition.

The traditional function of the PAC is to ensure that expenditure has been consistent with the Estimates approved by the Dáil. In more recent years, it has examined a broader range of questions as illustrated by its inquiry into the evasion of DIRT tax. However, its role is still a limited one. Specifically its terms of reference state that the Committee shall refrain from "inquiring into the merits of policy or policies of the Government or a member of the Government or the merits of the objectives of such policies".

4.2.2.2 Select Committees

Select Committees examine the Estimates of their respective areas (for example the Select Committee on Social and Family Affairs). The Estimates are presented to each Committee by the Minister of the relevant Department. The examination takes place during the year to which the expenditure relates, so that the money is either spent or committed by the time it is discussed by a Select Committee. In the debates on the Estimates by the select committees, some TDs have expressed their dissatisfaction with the Estimates process and in relation to the type of information supplied to the Committees (see, for example the report of the Select Committee on Education and Science, 21 June, 2000). The potential for enhancing the role of Oireachtas Committees is discussed in the next Chapter.

4.2.3 The Department of Finance

The Department of Finance has statutory responsibility for the administration and business generally of the public finances under the Ministers and Secretaries Act, 1924. The Department was allocated additional functions for economic and social planning under the Economic and Planning Development Order, 1980. These functions are principally the promotion and co-ordination of economic and social planning (including sectoral and regional planning), the identification of development policies, the review of the methods adopted by Government Departments to implement these policies and the provision of advice to the Government on economic and social planning matters.

Every submission to Government and every proposal for legislation is required to include details of estimated costs, both for the current year and the medium term. The Department of Finance has a central role in overseeing this requirement. Every submission to Government must be submitted to Finance in advance so that it may include its comments and advice on the submission to Government.

The functions performed by the Department of Finance in carrying out this role are to assess and advise the Minister for Finance and the Government about (i) the priority attaching to the proposals being made by spending departments; (ii) the likely effectiveness of the policies being recommended to achieve the goal being pursued and (iii) the efficiency of the implementation mechanisms being recommended. The essential purpose of the Finance input is to help the Government exercise independent judgement when assessing proposals being advocated by Ministers.

The *Statement of Strategy 2001–2003* of the Department of Finance provides a recent formulation of the role of the Department. This Statement identifies five strategic priorities for the Department: economic and fiscal policy; the effective management of public expenditure; EU policy development; financial services and wider international economic co-operation; incomes policy; and enhanced management of the public service. Most relevant here is Finance's role in relation to the management of public expenditure. *The Statement of Strategy* includes the following aims in relation to this priority:

- in conjunction with other Departments, to ensure the effective management of, and value for money from, public expenditure;
- to co-ordinate the successful implementation of the National Development Plan and to support the implementation of the *Programme for Prosperity and Fairness*;

- to seek to influence spending priorities which will assist the economy in achieving the maximum sustainable output of goods and services, employment and social progress;
- to assist in the development and co-ordination of policies across the main sectors, particularly in relation to infrastructure and the integrated delivery of services;
- to co-operate with the responsible Departments in their analysis of the relevant sectors and their development of appropriate strategies, and to advise the Government accordingly;
- to promote the systematic review of expenditure programmes as envisaged in *Delivering Better Government*;
- to promote improved service quality and performance measurement (outputs/outcomes), as envisaged in *Delivering Better Government*; and
- in conjunction with the other Departments, to review the objectives and performance of commercial and non-commercial state bodies (Department of Finance, 2001: 18-19).

The achievement of these aims is critical to the effective management of public expenditure

4.3 REFORM OF THE MANAGEMENT OF PUBLIC EXPENDITURE

4.3.1 The Need for Reform

Many commentators have identified the need to improve the management of the public finances and public expenditure. For example, the *Delivering Better Government* report expressed the view that "existing budgetary procedures and public expenditure controls are not, of themselves, adequate to deliver effective management of the public finances" (1996:54). The *Public Financial Procedures* guide produced by the Department of Finance has noted that the existing system is an effective means of achieving parliamentary control over public expenditure by ensuring that public monies are spent legally and properly in accordance with parliamentary grants. However, it acknowledges that “given the growth and complexity of the public sector, the system is not geared adequately to meet the needs of modern financial management with its emphasis on relevant and timely information, better accountability and improved value for money in the use of resources” (Department of Finance, 1998, Section D1).

In recent years, there has been a number of reforms that seek to improve the management of public expenditure. Many of these are part of the Strategic Management Initiative (SMI) although in some cases the reforms were originally developed prior to the SMI (for example, Administrative Budgets). This Section provides an outline of reforms relevant to the management of public expenditure.

4.3.2 Multi-Annual Budgeting

A form of multi-annual budgeting is now in place. Projections are prepared on a multi-annual basis for both public expenditure and revenue, given existing policies. These provide the basis for the Stability Programme which is a medium-term programme for the public finances that sets out budgetary objectives, projections and assumptions about future economic developments. This is a requirement in all Member States adopting the euro.

It had been intended that multi-annual budgeting would go beyond projections to the development of a multi-annual planning framework for the public finances. The *Delivering Better Government* report outlined a revised Estimates cycle based on a multi- annual planning approach. It had been planned that departments would be given three-year allocations. The expectation was that this “should encourage line departments to prioritise spending, focus on outcomes and outputs, free up resources for service developments and in general to exercise primary responsibility for managing within approved resources” (Financial Management Working Group, 1999: 8). These multi-annual allocations have been referred to as ‘envelopes’.

In an assessment of developments in Ireland, the International Monetary Fund (IMF) considered that "further progress towards a multi-year framework would be highly desirable. Such a framework becomes all the more important during a period of unusually buoyant growth to maintain fiscal discipline and preserve medium term fiscal sustainability" (IMF, 2000: 36).

There is scope for a more developed multi-annual budgeting framework. The development of such a framework would, however, need to consider how it would relate to other medium-term plans.

4.3.3 A New Management Information System

The Management Information Framework (MIF) is a new management information system that is being developed across the Civil Service. The need for a new financial information system was identified by the *Delivering Better Government* report. The key objectives of the SMI include the delegation of responsibility and more emphasis on accountability on results. The existing system, however, with its cash basis, does not provide adequate information to support key SMI objectives of linking resource allocation to outputs and strategic priorities.

The new system will incorporate both financial information and non-financial measures of performance. It will relate expenditure on a service to the output of that service. It has common features but individual Departments must identify their requirements from the framework and adjust it according to their own requirements. The MIF will have both accruals and cash-accounting capability. It will provide management information at different levels and also be a source of information for value-for-money studies and expenditure reviews. The system will continue to provide the financial information required by statute for the Appropriation Accounts.

The new system is to be implemented over a five-year period and is due to be in place by the end of 2005. In some cases it is envisaged that the system will be implemented before 2005 (for example, the Revenue Commissioners). The development of the new system is being guided by a number of groups/committees with overall guidance provided by a Consultative Committee of senior management from all Departments and Offices. This committee is advised by two groups: a project management group working on project and cost management aspects and a technical issues group working on cost allocation, management accounting, performance indicators, accounting standards and the format of the Appropriations Accounts. Departments have put in place project teams to oversee work on the new framework.

4.3.4 Administrative Budgets

The introduction of administrative budgets is a reform through which departments are given greater flexibility to manage their administrative expenditure. A formal agreement is entered into between the Minister for Finance and the other Ministers and Accounting Officers. Under the agreement, the Minister for Finance commits to providing an agreed level of administrative spending for a three-year period (subject to Government and Dáil approval). The Minister for the line Department agrees to keep expenditure within the specified limits. Departments are given a measure of discretion to manage funds within these limits. The initiative is designed to encourage better planning and to achieve greater efficiency and effectiveness in administrative expenditure. Administrative budgets were first introduced in 1991 and an examination by the C&AG in 1997 expressed the view that administrative budgets seemed to have helped contain the rate of increase in administrative costs, although it was unable to quantify the potential savings (Office of the Comptroller and Auditor General, 1997).

4.3.5 Comptroller and Auditor General

The principal statutory functions of the Comptroller and Auditor General (C&AG) are first, to ensure that the issuing of money from the Central Fund by the Minister for Finance is in accordance with the approval of the Oireachtas and second, to audit government accounts for accuracy and regularity. The functions of the C&AG were extended by the 1993 C&AG (Amendment) Act empowering the C&AG to conduct, on a discretionary basis, examinations of the economy and efficiency of operation of the organisations that are audited as well as examinations of the adequacy of management systems that are in place to enable public agencies to appraise the effectiveness of their own organisations.

One of the challenges that arose in drafting the legislation was the appropriate role of C&AG in relation to examining effectiveness. The potential difficulty arose in that an examination of the effectiveness of expenditure could easily bring the C&AG into policy matters. Policy matters are the responsibility of ministers and ministers are directly accountable to the Dáil and ultimately to the electorate. Interference by the C&AG with this direct accountability was considered to be problematic. The legislation addressed this issue by giving the C&AG an indirect role in assessing effectiveness. Hence, rather than directly assessing effectiveness, the C&AG now has the ability to examine the adequacy of management systems that Departments have in place to examine the effectiveness of their own operations (Carvill, 1993). By contrast, the C&AG in the UK has discretionary powers to directly examine the efficiency and effectiveness with which departments use resources. In the context of the work of the C&AG this distinction between directly or indirectly assessing effectiveness may not be of great practical significance.

Since the introduction of the legislation, the C&AG has published around 40 value for money studies and has examined the impact of those studies that were carried out over the period of 1994 to 1996 (Office of the Comptroller and Auditor General, 2000). A recurring theme in many of these reports was the inadequacy of data collection to support the provision of meaningful performance information. These reports predated the preparation of strategy statements and business plans under the SMI. The C&AG noted that these developments can make a potentially important contribution to the assessment of performance but expressed the view that, "much more work is needed in the development of standards and supporting systems to underpin the routine production of performance reports" (Office of the Comptroller and Auditor General, 2000: ii).

4.3.6 Expenditure Reviews

In 1997 the Government (in *Delivering Better Government*) decided to establish a review of all public expenditure over a three-year period. The idea was that this review would firstly provide a systematic analysis of what was actually being achieved by each programme and secondly, a basis on which more informed decisions could be made on the allocation of resources between spending programmes. Over 60 reviews have been completed to date.

The C&AG recently published the report on its value for money examination of the process of expenditure reviews (Office of the Comptroller and Auditor General, 2001). The objectives of the review were to ascertain whether:

- public expenditure has been comprehensively reviewed over the period;
- the reviews had been carried out well; and
- the arrangements put in place to manage the expenditure review initiative were successful.

The report concluded that the body of completed reviews represented a substantial achievement. While the outcome fell short of the target of 100 per cent of Government expenditure to be reviewed over three years, reports completed and in progress together accounted for a total of 37 per cent of expenditure. Based on an assessment of a sample of the earliest completed reviews, the quality of these reviews was judged as reaching a sound professional standard in terms of how they reviewed objectives and assessed cost efficiency, but less so in terms of identifying and analysing performance indicators and evaluating effectiveness. The report noted that frequently the existing information base was poor and formal performance indicators were mostly absent or under-developed. However, given that only reports completed before 1999 were assessed, it is stated that reviews completed after 1999 may be of a higher standard. Finally, the report concluded that:

> the review process clearly directed some useful attention to many policy areas not regularly or well analysed. Overall,

> the...process provided some additional limited assurance that Government expenditures were being spent to some purpose and in a well-directed manner. [It] also served to help the introduction and development of the concept of evaluation in areas of the civil service where previously it had been non-existent or poorly understood (Office of the Comptroller and Auditor General, 2001: iii)

In June 2001, the Government agreed to a new approach to the expenditure review process proposed by the Minister for Finance to strengthen and develop the process further. The revised arrangements include:

- specification of selection criteria to ensure that future expenditure reviews focus on significant areas of expenditure and critical areas of government policy;
- provision by the Department of Finance of enhanced central supports for staff in Departments/Offices involved in expenditure review activities; and
- encouragement for Departments to publish expenditure review reports.

4.3.7 Strategic Management Framework

The Strategic Management Framework is at the core of the SMI. It has three dimensions:

- strategy statements that set out for each Government Department and Office the organisation's high level objectives, outputs and related strategies;
- business plans that translate the high level objectives into more detailed work programmes; and
- a performance management system that relates the work of individual public servants to the achievement of the organisation's work programme and ultimately its goals and objectives.

4.3.7.1 Strategy Statements

The Public Service Management Act, 1997 requires the Secretary General of a Department or Head of an Office to prepare a strategy statement every three years or within six months of the appointment of a new Government. The strategy statements are submitted to the Minister who may approve them with or without amendment. The aim of strategy statements is to clarify the high level objectives of Departments and the strategies to achieve these objectives. The 1998 strategy statements have been reviewed by Boyle and Fleming (2000). This study found that the statements are playing a useful role in promoting longer term thinking on issues and contributing to more effective management of Departments. However, the study identified several limitations to the statements:

- a weak link in some statements between environmental analyses and the objectives of strategies set out in the statement;
- limited discussion of the resource implications of pursuing objectives, outputs and strategies, and some confusion with regard to the understanding of these terms;
- little evidence of assessment of customer/client needs;
- a tendency to list cross-departmental issues rather than set out what needs to be done and how in order to secure better co-ordination;
- lack of clarity with regard to many of the performance measures used, and only a limited range of activities covered by performance measures; and
- insufficient attention in some cases as to how the strategic management process is to be embedded into departmental practice (Boyle and Fleming, 2000: ix-x).

In relation to the planning of public expenditure, the second point above is most relevant (ie, limited discussion of the resource implications). Boyle and Fleming noted that a central intention of the Public Service Management Act, 1997 was that the resources needed to achieve the goals, objectives and strategies be covered in strategy statements. The limited treatment of resource issues in strategy statements means that it is difficult to determine to what extent the statements represent reasoned and costed actions that have in some sense been prioritised.

It must be acknowledged that there are difficulties associated with the more explicit treatment of resource issues in strategy statements. The responsibility for preparation of strategy statements rests with Secretaries General. Government Departments do not know what resources will be available to them over the period to which the strategy statements relate. If the strategy statements were to identify priorities and to indicate the allocation of resources to achieve these priorities, this could interfere with what are essentially political responsibilities. The appropriate relationship between the political authorities and the public administration is a complex issue. The strategy statement of the Department of Justice, Equality and Law Reform makes a contribution to clarifying this relationship; uniquely among the strategy statements, this strategy statement lists all of the relevant objectives in the Government's Action Programme and identifies the corresponding action to be taken by the Department.

Another review of strategy statements was prepared by Keogan and McKevitt (1999). They argued that the performance measurement frameworks in strategy statements are weak so that the statements do not provide a good basis for assessing progress on the achievement of the objectives in the strategy statement. They argue that the performance measures are not well related to the client or customer concerns.

4.3.7.2 Business Plans

Government Departments and Offices also prepare business plans that translate the goals and high level objectives of strategy statements into more detailed work programmes to inform the day to day activities of work sections and staff. Boyle and Fleming (2000) point out that identifying the expenditure implications of activities in business plans is an area needing further work.

4.3.7.3 Performance Management and Development

A performance management and development system (PMDS) for Government Departments and Offices was launched in May 2000. The PMDS system is a way of linking the work of individual public servants to the strategic objectives of Departments and Offices. PMDS can be seen as a process for establishing a shared understanding of what is to be achieved and how it is to be achieved and an approach to managing and developing people that increases the probability of achieving success. It is a process that involves an employee agreeing a set of objectives with his/her manager, deciding together on how the objectives can be met and then planning what the employee or team need to change or learn to achieve these objectives. At the end of the year the performance is evaluated and the cycle begins again. The new system will be implemented within the culture of partnership.

4.3.8 Programme for Prosperity and Fairness

Public service modernisation is an important component of the *Programme for Prosperity and Fairness* (PPF). It is noted in the PPF that, given the many challenges to maintaining and further advancing economic and social development of the country, greater urgency in progressing the modernisation of the public service is clearly required. Equally, there is a need for the public service to respond better to the aspirations of its staff for more fulfilling work and improved career paths and to create work place conditions and relations that are conducive to increasing the job satisfaction, motivation and commitment of staff.

The parties to the PPF made several commitments to the further development of public service modernisation. The most significant of the commitments in this respect were as follows:

- Specific performance indicators were agreed for each sector. Certain pay increases were linked to the achievement of sectoral targets with progress being assessed at organisational level by, for example, a Secretary-General, County Manager and so on.

- A quality assurance group was established for each sector to ensure that quality improvements in services are made in each sector. These groups were to ensure that sectoral indicators agreed were in accordance with the PPF and that the targets were achieved.
- Reforms to recruitment are agreed in the PPF. While recruitment to existing entry level positions will continue to be the norm, it is agreed that to acquire skills and expertise which are in short supply within a sector, the need to resort to external recruitment levels other that the norm can arise and the public service must be able to respond to such needs in an efficient and timely way.
- Continuous improvements in public service performance require greater organisational adaptability. The parties to the PPF recognised the necessity to address a range of dimensions of new forms of work organisation (such as innovative work practices, flexibility in grading, and so on) while recognising that there are existing agreements on these issues.
- Training and development were to be enhanced in the context of implementing the performance management system and aligned with organisations' human resource management strategy.
- The public service modernisation programme was to be developed in the context of partnership at organisational level (Government of Ireland, 2000).

The PPF also sets out more detailed commitments for public service modernisation in the civil service and the health, education and local government sectors.

4.3.9 Integrated Services Process

The integrated services process (ISP) was a pilot project to address the needs of the most deprived urban communities. The purpose was to develop a new way of doing business that would lead to a more focussed and better co-ordinated response by the statutory agencies in urban blackspots, as a model of best practice. Four urban areas were included in the project (three in Dublin and one in Cork). The ISP has been evaluated by PricewaterhouseCoopers. Based on this evaluation, a progress report (Department of Tourism, Sport and Recreation, 2001) prepared for the Cabinet committee on social inclusion found that significant progress was made in improving the co-ordination and targeting of State service provision. This resulted in real and tangible benefits for the communities concerned and a significant improvement in the services provided by State agencies. However, the report also noted that the process placed considerable demands on Departments and agencies in terms of resources. The ISP was not developed as a separate initiative in view of the development of a new parallel programme, RAPID (Revitalising Areas by Planning, Investment and Development). The progress report recommended that the lessons from the ISP should be reflected in the structures and mechanisms of RAPID. These lessons include the importance of recognition and support from the Secretaries General and the Chief Executive Officers of State agencies for the work involved. The report noted that this was not always as consistently strong as it should have been. This issue of recognition of working in an integrated way across administrative boundaries is an important issue that is further discussed in Chapters 5 and 7 below.

4.3.10 Revitialising Areas by Planning, Investment and Development (RAPID)

Launched in February 2001, following a commitment in the PPF, RAPID is a new programme targeting investment into the 25 most deprived urban areas. The programme involves the front-loading of National Development Plan (NDP) investment in social facilities in the areas concerned and improved co-ordination of services. A plan is prepared for each area by an area implementation team consisting of local state agency personnel, the local partnership company, local residents and, where they exist, the local drugs taskforces. There is a specially appointed co-ordinator for each area. At city or county level a monitoring group ratifies these plans and at national level a monitoring committee exists that reports on progress to the Government. The targeted areas are prioritised for investment and development in relation to health, education, housing, childcare and community facilities including sports facilities, youth development, employment, drugs misuse and policing.

4.3.11 Summary of SMI Developments

The key developments in the SMI have been as follows:

- statements of strategy were published by Departments and Offices in 1996 and 1998;
- business plans have been developed by Departments and Offices;
- customer service plans including standards for service delivery were published in 1997 and 1999;
- financial management systems are being improved, including multi-annual budgeting, systematic programme expenditure reviews and the development of the administrative budget system;
- the Freedom of Information Act was implemented in 1998;
- progress is being reported through the publication of annual reports;
- a programme of regulatory reform is being implemented; and
- a performance management system for individual performance is being implemented.

4.4 CONCLUSION

This Chapter has outlined the basic features of the budgetary system and described a range of ongoing reforms that are seeking to enhance the efficiency and effectiveness of the public service. The question arises as to what impact the reforms are having on how the system operates in practice. The next Chapter therefore looks at the arrangements that are in place to achieve the critical objectives of prioritisation and efficiency of resource use.

CHAPTER 5

ISSUES IN THE MANAGEMENT OF PUBLIC EXPENDITURE

5.1 INTRODUCTION

This project on the management of public expenditure is largely motivated by a concern around the ability of Government to make appropriate public expenditure decisions, using relevant information and taking account of changing circumstances and priorities. Our concern is not with the substance of strategic policy decisions themselves but with the systems that are in place to translate strategic priorities into public expenditure outcomes and to ensure that once a policy decision is made, there is follow-through in terms of adequate monitoring of the efficiency and effectiveness of the resulting expenditures and re-allocation of expenditures as appropriate.

As defined, these are issues that are at the heart of the public sector reform drive that has dominated the public policy-making agenda in most developed countries for the last 10 to 15 years. Previous Chapters have examined the public sector reform experience in OECD countries as it relates to the management of public expenditure and also the reform experience in Ireland, which has been developed under the SMI banner. In the present Chapter, we focus on a number of issues or problems that have emerged in the course of the Council's analysis. Here we draw on the international experience and the on-going process of reform in Ireland.

In order to better understand the systems in place for managing public expenditure and the impact that the SMI reforms are having, the NESC Secretariat conducted interviews with senior civil servants in nine Government Departments. These Departments were chosen in order to cover a range of economic and social areas and a mix of large and small spending Departments. The Secretariat also met with senior staff in the Comptroller and Auditor General's Office, who have a role in auditing Government accounts, ensuring that the issuing of money from the Central Fund by the Minister for Finance is in accordance with the approval of the Oireachtas and in examining the adequacy of the management systems that Government Departments have in place to examine the effectiveness of their own operations. A further perspective and additional information were gained through interviews with four former Secretaries General.

Many of the currently serving senior civil servants that we interviewed seemed reasonably happy with how the current system works. There was particular praise for some of the reforms that have recently been introduced, such as the inclusion of 'no policy change' figures as part of the Estimates process, the increased discretion that line departments now have in relation to administrative expenditure and the increased emphasis that is now being placed on expenditure reviews.

Notwithstanding these favourable perspectives, however, a number of issues that were raised during the interviews and that arose from the Council's other research, are significant and require attention. The remainder of this Chapter outlines these issues. The analytical approach adopted was a comparatively simple one. This Chapter does not seek to identify or define any 'ideal' system or systems of public expenditure management, against which the existing system might be benchmarked. (Although, as identified in Chapter 3, a considerable amount of literature exists in this area.) Rather, we pose three simple questions, as follows:

1. Are there incentives or constraints within the existing system of public expenditure management that bias the system towards 'bad' decision-making, or which make 'good' decision-making more difficult?
2. If such incentives or constraints exist, how might they be alleviated or removed?

3. In addition, are there ways of adding to, or altering, the existing system to facilitate or promote ‘good’ decision-making?

Here the terms ‘good’ and ‘bad’ relate, not to the actions of individuals, but to the product of the decision-making system as a whole. In other words, ‘good’ decision-making results in the alignment of strategic objectives with expenditure allocations, and with efficient and effective public expenditure in the long run, while ‘bad’ decision-making means that the system is not producing those results. The remainder of this Chapter is largely organised around these three questions. Hence, Section 5.2 considers the constraints that exist in the system in reaching good decisions on public expenditure along with incentives that do not facilitate good decision-making. Section 5.3 explores the possibilities of removing these constraints and changing incentives to improve decision-making on public expenditure, while Section 5.4 considers potential innovations to facilitate good decisions. Finally in Section 5.5, we examine the issue of devolution from the centre in public expenditure management, either functionally or geographically.

5.2 CONSTRAINTS AND INCENTIVES THAT INHIBIT GOOD DECISION-MAKING

5.2.1 Strategic Framework at the Centre

One of the most significant issues to emerge from the interviews was the perceived lack of an overall strategic framework at the centre to guide individual expenditure decisions, translating strategic priorities into expenditure allocations at a broad level. There are significant strategic inputs to the budgetary process including Programmes for Government, the National Development Plan, social partnership agreements and NESC Strategy reports. Notwithstanding the value of these inputs, the current priority-setting process for public expenditure is diffuse and involves very complex negotiations. The annual Estimates process is itself only one element of the picture – separately from this process there are many contacts for example between the Department of Finance and spending Departments on policy reviews and developments. As described in Chapter 4, at the start of the annual Estimates process, the Government, advised by the Department of Finance, decides a target for the total level of expenditure. The Department of Finance holds detailed discussions with Departments in order to ensure that strategic Government policy objectives and programmes are prioritised and funded and to reconcile the spending demands with the guidelines set out in the Estimates circular. While much common ground is agreed, many issues are referred to the Minister for Finance and the relevant Minister for political decisions. The Government makes final decisions on resource prioritisation across programmes. This process culminates in a Government decision on detailed expenditure allocations.

While, ultimately, this process results in allocation decisions, many interviewees criticised the absence of an agreed methodology for resolving competing claims on expenditure. As a result, according to more than one interviewee, the Estimates process can sometimes become a “battle of wits” or a “political dogfight”. While in part the perspective of the interviewees may be confined to their own areas, it is a fact that the entire process is very much a “political” one. As noted above, the Department of Finance, the Minister for Finance and the Cabinet decision-making process aims to ensure that resources are prioritised in keeping with Government objectives and policies. While several interviewees noted that final decisions are a matter for Cabinet, it emerged that Cabinet tends only to deal with unresolved issues arising from a series of negotiations as much common ground is reached at official level and Ministerial negotiations.

In the same vein, the incremental nature of the process was emphasised by a number of interviewees. According to one interviewee, despite the rhetoric of outputs, outcomes and quality of service, the reality is “creeping incrementalism”. The system finds it difficult to make explicit choices between competing priorities. Government programmes are rarely eliminated. This results from a number of factors, but the budgetary system in the view of some at least appears to provide little incentive for Departments to eliminate programmes when they have become obsolete. There was, however, some suggestion that this is changing, and that, particularly in the context of some public expenditure evaluations, the Department of Finance does encourage a line Department to find savings with respect to one programme that can be used to expand other programmes.

5.2.2 Departmentalism

A feature of the existing system commented on by several interviewees is excessive 'departmentalism'. There are two main issues here. First, the Estimates process as currently organised is territorial in nature, with each line Department looking out for their own Department's best interests, as distinct from taking a broader perspective. This is only natural and rational from an individual Department's point of view; that is why the overall strategic focus and prioritisation brought to the process by the Department of Finance, Minister for Finance and Cabinet is important so that the bigger picture of national strategic policy priorities is not lost in the process.

Second, the ability of cross-departmental issues to be effectively addressed in the Estimates process needs to be enhanced. Many objectives of policy, such as the promotion of health or a more equitable society, are influenced by the expenditure programmes of several Departments and involve a wide range of agencies. The synergies and consistencies between expenditure programmes should be more systematically examined in the process so that the most effective policy mix will evolve.

There are inter-departmental committees at both ministerial and official level and these should help to bring a wider perspective to the management of public expenditure. Many of the interviewees believed that inter-departmental committees now worked better than before. Cabinet committees on infrastructure and social inclusion were cited as examples that worked reasonably well. However, many interviewees felt that more could be done to ensure that cross-cutting issues are better addressed in the policy and Estimates process.

5.2.3 Focus on Inputs and Avoiding Mistakes

A central concern of the international literature on public expenditure management is the over-reliance of traditional budgeting systems on inputs, rather than outputs or outcomes. In the case of Ireland, while line Departments must justify their expenditure plans to the Department of Finance, from the information gathered at the interviews, it appears that expenditure outputs or outcomes do not form part of the formal Estimates process. There is some discussion of this information during the year in ongoing contacts between the Department of Finance and spending Departments in relation to policy appraisal and development, but it is not part of the Estimates discussions.

The primary documents on public expenditure are all focussed on inputs. The main document that sets out spending plans on an annual basis is the *Estimates for Public Services*. This sets out spending plans in great detail but does not provide any information on what this expenditure is expected to achieve. The main regular *ex-post* report on public expenditure is the annual *Appropriation Accounts*. This report is mainly concerned with issues of the regularity of expenditure and contains some efficiency information on particular areas of the public service. However, it does not provide regular information on what is being achieved through public expenditure, nor is it designed to do so.

One consequence of this focus on inputs that was highlighted during the interviews is the overriding incentive from the point of view of accountability to avoid making mistakes. More than one interviewee suggested that this acts as a constraint on entrepreneurial decision-making. The existing system is designed to avoid public funds being spent for purposes that have not been agreed by the Oireachtas, an aim that is obviously reasonable, appropriate and important. However, the current system of accountability places excessive emphasis on the avoidance of mistakes, rather than accountability for reasonable decisions made in the light of available information and knowledge.

An important manifestation of the incentive to avoid mistakes is the nature of accountability by Secretaries General in their role as Accounting Officers to the Public Accounts Committee (PAC). Accounting Officers are accountable to the PAC for the expenditure of their Department. However, the primary focus of this parliamentary accountability is that the expenditure is consistent with the appropriation of expenditure to the Department. The situation has developed in recent years so that the PAC now also considers value-for-money studies produced by the C&AG. However, the primary focus is still on the regularity of expenditure rather than the results achieved through public expenditure. It appears that the overriding concern of the parliamentary system is still the inputs, while insufficient attention is given to the outputs or outcomes arising from expenditures.

5.2.4 Evaluation and Use of Information

Recent reforms introduced under SMI have included a greater emphasis on evaluation and the use of information. The programme of expenditure reviews introduced in 1997 was cited as a welcome and significant initiative by most interviewees. However, their impact in terms of improving the management of public expenditure appears limited. Many interviewees did not identify a formal link between expenditure reviews and budgetary decisions. Indeed, it appears that in some departments, expenditure reviews were being conducted quite separately from any consideration of their actual impact on expenditure. Thus, in some cases there appears to be too much emphasis on compliance (ie, a successful outcome means completion of a certain number of reviews) and not enough on using the reviews to make better allocation decisions and to improve strategic planning more generally. For example, while a number of interviewees cited examples of how they had used the expenditure reviews to secure increased funding for a particular programme, there was little evidence of expenditure cuts arising from any review.

A disturbing picture to emerge from some of the interviews was the suggestion that in a period of buoyancy in public finances, evaluation may not be regarded as being that important. A couple of interviewees suggested that healthy public finances meant that there was less concern about the continuation of ineffective policy programmes. The inference seemed to be that value-for-money was regarded as being only really important when funds were tight.

Apart from formal expenditure reviews and the comprehensive NDP evaluation process for NDP-related spend, comprising *ex-ante*, ongoing, mid-term and *ex-post* evaluation, there is little evidence of other more systematic evaluation taking place. The ability to undertake quality evaluation of public expenditure on a regular basis is dependent on the availability of performance information in a usable format. The availability of this type of information varies across Government Departments but the ability to undertake value for money examinations of public expenditure is frequently constrained by the absence of such information. The development of the new Management Information Framework (MIF) (formerly referred to as the generic model) is a significant initiative that is seeking to address this gap. The purpose of the new system is to equip Departments with a system of financial accounts, integrated with a system of output measurement. However, the MIF is not expected to be fully implemented until the end of 2005. (See Section 4.3.3 of Chapter 4 for more information on the MIF.)

5.2.5 Resources

Every interviewee from a line Department cited the lack of available human and other resources to collect, organise and analyse the data in relation to the efficiency and effectiveness of expenditure as a fundamental constraint in the system. Similar views were expressed in relation to policy-related research. In a full employment economy that is experiencing labour and skill shortages in a number of sectors, this complaint is perhaps not unusual. However, in addition to dealing with these external constraints, there are also internal hiring constraints. A particular concern that was raised in many of the interviews was the lack of staff with the appropriate skills to properly evaluate and monitor programme expenditures. Effective decision-making and proper accountability for expenditure decisions requires individuals who have the skills and experience necessary to properly track programmes, in terms of their efficiency and effectiveness. It is clear from the interviews that such individuals are in short supply across the civil service. Some of the interviewees also stated that they would welcome more guidance, perhaps from a central policy evaluation unit, as to how to properly evaluate expenditures and, in particular, to help resolve technical questions that might arise during evaluations.

5.2.6 Multi-annual Budgeting

Some interviewees feel that they are not reaping the full benefits of multi-annual budgeting. Multi-annual budgeting was proposed in the *Delivering Better Government* report and was considered in the report of the SMI financial working group:

> The aim of MAB is to put in place a budgetary framework and decision-making process within which both Government and Departments can consider overall budgetary, taxation and expenditure priorities for a three year period in place of the one year perspective which previously applied and which did not capture fully the longer term cost implications of Government decisions on tax and expenditure. Three year resource allocations should encourage line Departments to prioritise spending, focus on outcomes and outputs, free up resources for service development and in general to exercise primary responsibility for managing within approved resources (Financial Management Working Group, 1999: 8).

Multi-annual budgeting has been introduced to the extent that projections are now prepared on a multi-annual basis of both public expenditure and revenue given existing policies. However, the system still revolves very much around annual negotiations of expenditure; indeed, the negotiations may happen more than once a year.

Clearly, there is a tension here between the need to achieve maximum possible flexibility with respect to aggregate public expenditure for macroeconomic reasons, and the need to plan and deliver public services in an efficient and effective manner. As several interviewees pointed out, public expenditure is largely composed of elements, such as pay, which are not seen as flexible downwards. Maximisation of such limited flexibility as may be possible within the system then implies a concentration on control of those elements that can be readily adjusted, and adoption of short-time horizons with respect to expenditure commitments. The shorter the time horizon, the more flexible aggregate expenditure will be, other things being equal. On the other hand, effective and efficient management of resources may require greater financial pre-commitment. Thus, if a service were to be rolled-out or developed, public service managers would be better able to make efficient use of resources if they could plan ahead with a time horizon of more than one year. The existing system, while containing some elements of forward planning, tends still to be based in large measure on a time horizon of one year, and adjustments to budgets can also be made mid-cycle.

5.2.7 Role of Different Actors in Budgetary Decisions

There are a number of key players involved in managing public expenditure. An interesting feature of the interviews was the extent to which the views of individuals appeared to be influenced by their own role within the system. These views related to the system as a whole, and the role of different actors within the system. This is entirely to be expected, and is a common feature of interview-based research.[1] It is interesting to consider this correlation between individual's views and their roles, however, since it tells us something about how the system functions.

It is clear that the Government plays the key role in final expenditure decisions. Individual Ministers, and the Minister for

1 In any project where interviews are used to gather material, it is important to bear in mind that interviewees are not necessarily disinterested observers, and that their views may be influenced by their experience in a variety of ways. This is to be expected, and should be taken into account by the researcher. See, for example, Richards (1996).

Finance have a major role to play, as have individual Departments and the Department of Finance. The Department of Finance plays an essential role in ensuring overall fiscal discipline. Fiscal discipline is just one feature of a good public expenditure management system. Other essential features include an emphasis on the strategic allocation of resources and on efficiency and effectiveness in service delivery. As noted earlier, this focus is now being given some more emphasis with the encouragement of the Department of Finance which is also, through the Management Information Framework and expenditure review projects, prioritising a focus on outputs and outcomes

Some interviewees in line Departments thought, however, that there was a problem of a lack of understanding of those in the Department of Finance in relation to the expenditure of line Departments. While several interviewees praised the commitment of Department of Finance personnel, they argued that a small number of people working on a particular vote could not be expected to develop the same level of expertise in any given area as officers in the line Department. This led some interviewees to argue that there is a need to find ways of enhancing the expertise of those dealing with public expenditure in relation to the various areas of expenditure.

More generally a number of interviewees emphasised the "game" aspect of the Estimates process and the importance of being able to play the game to secure maximum resources for one's own Department. Interestingly, nearly all interviewees acknowledged that there was an incentive to over-estimate a line Department's budgetary needs in Estimates submissions to the Department of Finance, but all interviewees stated clearly that this was not a practice favoured by their own individual Departments.

These views suggest that the adversarial nature of the system does little to encourage trusting and co-operative behaviour between line Departments and the Department of Finance. This is partly to do with the more general problem of 'departmentalism' described above. In addition, however, the system of public expenditure management is structured in such a way as to further encourage line Departments to concentrate on their own interests, and to encourage the Department of Finance to focus on its policing role. It does less to encourage joint co-operative thinking between different branches of the civil service.

Clearly, it is possible to exaggerate this effect. As described above, several interviewees were anxious to acknowledge the difficulty of the task faced by colleagues on the opposite side of the fence. Moreover, some element of creative tension is likely to be a desirable feature of the system; as again acknowledged by a number of interviewees in line Departments. Several interviewees saw this tension as entirely natural and part of a properly functioning system. Moreover, critical analysis of expenditure proposals is clearly an essential feature of any system of public expenditure management. It is questionable, however, as to whether the system is structured in such a way as to place rather too much emphasis on this tension, and too little on the creative and innovative thinking which greater co-operation and trust between the Department of Finance and line Departments. As has been argued in the context of industrial relations, joint 'puzzling' activity based on a foundation of trust between negotiating partners can often result in mutually advantageous outcomes (Visser and Hemerijck, 1997, Scharpf, 1997). It would appear that the structure of the public expenditure management system does not always lend itself to this kind of activity.

Several interviewees adverted to the political nature of the Estimates process, and the key role played by Ministers and the Cabinet. Individual Ministers play a dual role in the process, acting both as the political heads of their Department, and as part of the collective decision-making process in the cabinet. It is possible that this dual role could create tensions, because as the political head of a line Department, a Minister represents the interests of his/her Department, while as a member of Cabinet, they must address broader national concerns. These are often expressed in a 'Programme for Government' document, that sets out the Government's collective priorities. Achievement of the latter might potentially be inhibited, if the structure of the process is such as to emphasise departmental concerns rather than governmental concerns. Thus, there may be an incentive within the system for

Ministers to focus on their departmental role at the expense of their collective Cabinet role. Whether this potential tension creates real or significant difficulties is unclear, however, because the interview programme did not include former or current Cabinet members.

5.2.8 Other Incentives and Constraints

Much of the discussion in the preceding sub-sections has highlighted that while SMI and the new drive for improved public sector management places particular emphasis on the importance of efficiency and effectiveness of expenditures, service delivery outcomes and the importance of strategic oversight of policy programmes, some of the incentives that arise within the public expenditure management system in Ireland work against these types of reforms. A number of examples illustrate this point.

A number of interviewees complained about the ‘clawback culture’ within the system, which means that there is no incentive to make expenditure savings in particular programmes when individual Departments will ultimately lose these savings back to the Department of Finance. There is some scope for recouping savings under administrative budgets and there is a provision in the system for ‘virement’; ie, the use, with the approval of the Department of Finance, of savings on one or more subheads to meet excess expenditure on another subhead within the same vote. However, savings arising from changes in large programme commitments cannot be kept and used for other purposes within the individual line Department in the following year. This may also be one of the reasons why the experience of expenditure reviews has so far not produced much by way of recommendations for expenditure cuts. A related point is the traditional rush at the end of the year to spend any unused funds.

Equally, the focus on expenditure inputs by the key players involved in the management of public expenditure sends signals out to line Departments that expenditure outputs and outcomes are not as important. As plans to introduce performance indicators and other measures into the system are realised, the system of making budgetary allocation decisions will itself have to change to properly incorporate and use this new information.

A number of interviewees referred to the excessive time and energy involved in the Estimates process. Concern was expressed that there were excessive revisions to the Estimates after they had been agreed. The disproportionality of the bureaucracy was also stressed by a couple of interviewees, with sometimes excessive attention being paid to very small amounts of expenditure. One interviewee argued that the introduction of multi-annual budgeting had added to the demands of the budgetary process because it was in effect operating in parallel with the annual Estimates process. This means that while line Departments have to go through the effort and work involved in multi-annual budgets, the annual Estimates process remains the primary allocation mechanism.

Some interviewees cited the difficulties arising from the separation of the personnel division of the Department of Finance from all other divisions. When a new programme is being introduced, this effectively results in two sets of negotiations: one with the public expenditure division to approve the overall programme budget and another quite separate negotiation with the personnel division to approve the staff to oversee the new programme expenditure. Of course, there is a reason for paying particular attention to new expenditure that involves increases in core public sector employment. Typically public sector employment involves lifetime employment so that staffing decisions cannot easily be reversed. However, a number of interviewees were clearly irritated by the delays and uncertainty arising from the lack of integration between staffing and budgetary decisions and would look forward to some reform in this area.

5.3 OVERCOMING CONSTRAINTS AND CHANGING INCENTIVES

Having examined constraints or incentives in the existing system which inhibit good decision-making, the discussion now moves to examination of how such constraints might be removed.

5.3.1 Central Strategic Function

There is a need to find ways of strengthening the capacity of the system to make strategic choices in relation to public expenditure. The system needs to identify the key policy priorities and to promote consistency between these policy priorities and budgetary allocations. This is necessary to more quickly align spending allocations with national economic and social priorities as the latter develop. There is a particular need to devote more attention to the cross-departmental aspects of expenditure. More effort needs to be devoted to examining the synergies and inconsistencies between different expenditure votes before issues go to the Cabinet for decision.

One proposal emerging from an interview to address this strategic weakness in the system was to appoint a senior minister without a portfolio whose role would be to provide the required co-ordination between Departments. He/she would act as an honest broker between Ministers and the Taoiseach and would have the role of pulling together the overarching objectives. This Minister would co-ordinate a small number of Cabinet sub-committees covering both the economic and social areas. This is an example of the type of reform suggested that could help to bring a more strategic approach to the management of public expenditure.

The greater use of multi-annual budgeting could facilitate planning for new services and re-orientation of existing services to address Government policy within an overall consistent approach to the management of public services and the generation of resources to pay for them on a basis that is sustainable in economic, social and budgetary terms. Urgent consideration should therefore be given to developing the multi-annual budgeting system further.

Another possible proposal, although not one discussed in the interviews, would be to develop a list of a limited number of public policy priorities that would take precedence over and be treated differently to other policy areas. At present, possible examples might include housing, infrastructure and childcare. The identification of such priorities could draw on some of the ‘strategic inputs’ described above, such as partnership programmes. Organisational structures could be put in place to ensure follow-through on policy and expenditure decisions in relation to these areas. This might involve an enhanced role for the Department of the Taoiseach in overseeing these areas or the further development of the Department of Finance’s role in strategic policy oversight. When asked who should perform such a central strategic role, interviewees were evenly split on whether it should be the Department of the Taoiseach or the Department of Finance.

5.3.2 Accountability for Results

The development of a system of accountability for what is achieved through public expenditure requires the development or strengthening of systems of performance information. While there is some performance information available, there are major gaps in the availability of organised information on what is being achieved through public expenditure across the public service, as noted in several of the value-for-money studies of the C&AG. Investment in information systems is necessary for the improved management of public expenditure. It is important that the commitment to developing the new Management Information Framework (MIF) is carried through and that the new system is established within a reasonable time period (see Chapter 4, Section 4.3.3). Investment in IT systems will be a crucial part of the implementation of the MIF to ensure that the information is collected and disseminated in a timely manner.

The establishment of improved systems of accountability could achieve a better balance between the focus on inputs and outputs/outcomes. A greater focus on outputs accompanied by increased empowerment to take decisions through improved delegation and devolution of authority may go some way to supporting a culture of greater prioritisation with decisions made in the light of available information and knowledge, as mentioned in the previous section.

5.3.3 Incentivise Cross-Departmental Action

Addressing cross-cutting issues in an effective way is a challenge that to date many countries have found difficult. Indeed the concern has been expressed that aspects of public management reforms in some countries have exacerbated the problems (see Chapter 3). There was universal agreement among interviewees on the importance of cross-cutting issues, and also that there is scope for further improving the capacity to address them. The cross-Departmental structures which exist to deal with some issues such as infrastructure and social inclusion seem to have proved effective and could be developed further. The inclusion of an individual's or Department's contribution to cross-cutting issues as part of the new performance management and development system (PMDS) might also help to underline, albeit in a small way, the importance of this issue.

5.3.4 Re-energise the SMI

There is a need to re-energise the SMI to ensure its relevance to public servants at all levels. All interviewees stated that they are committed to the SMI and saw the reforms as having a useful contribution to the management of public expenditure. While a wide range of reforms has been introduced, there is an issue as to what extent the SMI has actually changed the day-to-day work of many civil servants. Questions also have to be asked about the slow pace of reform. The overall impression from the course of the interviews is that elements of 'new public management' have been grafted onto the existing system of public expenditure management but it is questionable whether these elements have taken hold and filtered down through line Departments.

5.3.5 Sunset Clauses

It is rarely the case that public expenditure programmes are abolished. While there may be good reasons for this, the inclusion of 'sunset clauses' in legislation relating to new expenditure proposals could be considered. Sunset clauses would require that a proactive decision be taken on the continuation of organisations and expenditure programmes and thus reduce the probability of expenditure continuing that was no longer serving a significant economic or social function.

5.3.6 Promote Co-Operative Interaction Between Departments

Managers in line Departments have considerable knowledge and experience to add to the strategic thinking process which should underpin public expenditure management. It would be useful, therefore, to find ways of engaging line Departments with this strategic thinking process, thereby encouraging line Departments to have a greater sense of ownership over the Estimates process, and to have greater regard for national as against Departmental priorities. This would be preferable to an exclusive focus on limiting expenditure in the interaction between line Departments and the centre.

5.4 WHAT CAN BE ADDED TO SUPPORT GOOD DECISION-MAKING?

In order to improve the system of public expenditure management, it is not sufficient to remove any incentives or constraints that inhibit good decision-making. It is also important to add tools and resources to the system that will facilitate and support good decision-making. A number of possibilities are discussed below.

5.4.1 Accountability for Outputs and Outcomes

A fundamental aspect of the current system of accountability for public expenditure is the statutory accountability of Secretaries General as Accounting Officer for the use of public expenditure by their Departments. Under the Public Service Management Act, 1997 the Secretary General/Head of Office has responsibility for the preparation of Strategy Statements which comprise the key objectives, outputs and related strategies (including resources) of the Department or Office and to provide annual progress reports. The Secretary General is accountable to the Minister for the

Strategy Statement. Under the Act, they, and other officials who have been assigned responsibility under the Act, may be asked to appear before Oireachtas Committees in relation to the Strategy Statement (the Strategy Statement normally forms part of the terms of reference of Joint Committees of the Oireachtas).

The type of formal statutory accountability that applies to Secretaries General as Accounting Officers before the PAC in relation to the regularity of expenditure could not reasonably apply in relation to the results achieved through public expenditure, given the variety of influences that shape the results achieved. In other words, while Secretaries General in their Accounting Officer capacity are personally responsible for safeguarding public funds and have a statutory responsibility to give evidence to the PAC on the discharge of their responsibility, it would not be reasonable to have the same type of statutory, personal responsibility for all performance deficiencies that arise in relation to public expenditure supported by his/her Department. However, it is reasonable for Secretaries General to report on what is achieved through public expenditure in annual reports and to explain this performance to an Oireachtas Committee (the most appropriate Committee may be that charged with the consideration of the Strategy Statement).

For such a system to work effectively, however, Oireachtas Committees would have to be adequately resourced. Thus, not only would Departments have to be capable of providing outcome indicators on a regular basis, but Oireachtas committee members would require the support of professional staff with the time and expertise to analyse the information. Resourcing the institutions of democratic accountability and prioritising accountability for results, not just for inputs, would be essential. On the other hand, it should be noted that Secretaries General are not the political heads of their Departments, and that ultimately it is Ministers who are responsible to the Oireachtas for the policies of their Departments. Developing the role of Oireachtas Committees, therefore, would require a clear demarcation of the respective realms of accountability of Secretaries General and Ministers, that would avoid Secretaries General being asked to comment on political issues, in addition to the prohibition that already exists on civil servants commenting on the merits of policy.

It is undoubtedly the case that many positive developments are taking place with regard to the modernisation of the public service and these have been noted earlier. There is now a need to formally integrate the expenditure process in these developments.

At present the annual Estimates publications give little information on what is being delivered in output or outcome terms. It is suggested that instead of publishing an expense-heads listing of expenditure by vote, each Department would publish a 'business plan' for that year linking the Budget approved by Government with a coherent statement of what is expected to be achieved during the course of the year across the various activities. This would then be followed up at the end of the year with a Report and Accounts type report that would incorporate the Annual Accounts per se, and a statement of what had been achieved. Both the Business Plan and the Report and Accounts would be examined by relevant Committees of the Oireachtas over the course of the year.

Such a process would enhance appreciation generally as to what is being achieved through investment in public services. It would greatly facilitate the Oireachtas in having a soundly based review of what is being achieved through public services and their cost. It would also facilitate an enhanced system of considering proposals for additional resources/shifting resources to address Government priorities during the course of considering public expenditure priorities and the associated processes involving the Government/ Ministers and Departments.

5.4.2 Resource Accounting

Resource accounting is a general framework for the development of financial and performance information. Its significance is that it has potential to support the broader concept of accountability discussed above. There are three elements to resource accounting. First, there is the replacement of cash accounting with accruals accounting. For the most part Government accounts are organised on the basis of cash accounting. This records the inflows and outflows of money when they occur. Commercial organisations on the other hand use accruals accounting.[2] Accruals accounting is based on identifying the costs incurred and revenue earned in a particular period. This can differ from cash flows due to factors such as depreciation and pension liabilities. The second aspect of resource accounting is identifying objectives and allocating the costs of a Government Department or organisation to the various objectives. This has the merit of making an organisation think critically about what costs are contributing to its objectives and clarifies the cost of pursuing various objectives. The final and most significant aspect of resource accounting is output and performance reporting. This is to provide regular reporting on what is being achieved with expenditure. This could include both output measures (what is produced) or outcome measures (the effects of policy).

The Department of Public Enterprise (now Transport) has piloted the development of resource accounts. The first element of resource accounting, accruals accounting, has now been adopted by the Department as a standard practice. The next stage in the development of resource accounts will be to show the relevant expenditure that is allocated to the objectives of a Government Department. Resource accounts are also being developed internally to provide financial information to support business plans.

While resource accounting is still at a pilot stage in the Department of Transport, it represents a potentially significant development towards the reform of public expenditure accounting. It is important that the reform process should press ahead within the context of the MIF and that there should be a move away from the existing cash accounting system (although cash accounting may have to be retained) towards a system based on accrual accounts and which also provides output information. This should be backed up by relevant IT resources. The interviews suggest that there may be some reluctance to embrace such reforms. Experience in the local government sector and in other countries suggests that such initial difficulties can be overcome.

2 Local authorities have recently adopted accruals accounting.

An alternative proposal might be to replicate some variation of the system in place in New Zealand. There, the role of chief executive or head of department is strongly distinguished from the role of the minister responsible for that department. The chief executive is responsible for providing services while the minister ‘purchases’ these services. The services provided by government departments are referred to as outputs. The chief executive is formally accountable for producing required output. Output targets are set out in annual purchase agreements between the minister and chief executive and progress in meeting the output targets is closely monitored. The impact of the output produced by a government department or government agency is referred to as an outcome. Chief executives are not accountable for the outcomes that arise from their activities. The outcomes are the responsibility of the minister. The distinction between the purchaser and provider has been used elsewhere in the public sector reform but New Zealand is unique in applying this distinction at the level of a head of a government department and a minister. One of the difficulties of this system, however, is that of adequately and fully specifying the relevant outputs, and of avoiding an excessive focus on narrow targets.

5.4.3 Annual Reports

The annual reports of Government Departments are a potentially significant instrument in achieving accountability for what is achieved with public expenditure. To date, however their impact has been limited. They present only a limited insight into what is actually achieved with public expenditure. There are also significant delays in publishing some of the annual reports, which obviously limits their usefulness. In some cases (the Departments of Education and Science, and Social, Community and Family Affairs), annual reports are accompanied by statistical reports that contain more detailed information on the activities supported by the Department.

There are two aspects to the accountability of public expenditure of a Government Department. There is the direct expenditure of the Department on its own administration and the funding of public services that are typically delivered by some other agencies. The latter programme expenditure is far higher than the administrative expenditure. Annual reports could show more clearly what is achieved through both administrative and programme expenditure. In particular they should show what the results of increased expenditure are. The ongoing work of the Department of Transport on resource accounts could provide the basis for an appropriate format for showing this information in conjunction with the financial information and, if successful, could be applied more widely.

5.4.4 Overview of Performance

It can be difficult to identify all relevant expenditure across the public service that addresses a particular area of expenditure. Even where the expenditure is identified, it is difficult to manage this expenditure so that all the relevant programmes are contributing to the overall objective. An earlier attempt to provide an overview of what is being achieved through public expenditure was the publication of the *Comprehensive Public Expenditure Programmes*. This provided details of expenditure, organised by programme, a statement of what each programme is seeking to achieve and details of activity in most programmes, but has not been published since the 1980s.

A number of those interviewed in this study pointed out that the division of the Estimates process into agreement on the no-policy-change (NPC) figures and new policy developments/service improvements has helped to clarify the process. It could also be possible to use this information to clarify public understanding. A possible version of this would be as follows: the Estimates would show how much of the increased expenditure in any year is due to increases in the cost of existing levels of services (i.e., increases on a NPC basis) and how much is due to new policy developments/ service improvements. Each of the principal policy changes could be identified and policy changes that resulted in expenditure reductions would also be shown. Given that health, education and social welfare account for around 70 per cent of current expenditure it should be possible to identify the main sources of increased expenditure by identifying either cost increases or service/benefit increases in these areas.

5.4.5 An Evaluation Culture

The effective management of public expenditure depends on the emergence of an ethos or culture of evaluation. The essential feature of this ethos is an ongoing concern to identify the extent to which both existing and new policies contribute to the achievement of policy objectives and a willingness to take appropriate action where this is not the case. Other essential aspects include an ability to pose suitable review questions, a willingness to invest in staff development and a willingness to invest in ongoing data collection to support reviews.

There is a need to strengthen the expertise available to Government Departments to undertake expenditure reviews/evaluation. Those with the expertise to undertake high quality reviews are in short supply and this is evidenced by the scale of expenditure on outside consultants. A strategic approach needs to be taken to building the capacity to undertake reviews. This would involve developing the skills of people in Government Departments and giving greater weight to these skills at the recruitment stage. A number of interviewees referred positively to the 'Analyst' scheme previously run by the Department of Finance as a mechanism that greatly enhanced the human capital of many civil servants. This involved a combination of formal training and practical experience for scheme participants who subsequently applied their newly acquired skills in programme evaluation. The Department of Finance has recently developed a new training initiative in this area and is currently considering options for further developing analytical skills in the civil service.[3]

3 CMOD (the Centre for Management, Organisation and Development within the Department of Finance) has designed and delivered a new six day course in policy analysis skills, initially to its own staff during 2001, and in 2002, to all Government Departments by means of an increased level of delivery. On the wider question of enhancing policy analysis skills across the civil service, the

Expenditure reviews have generally been undertaken by spending Departments with responsibility for managing the programme under review. It is appropriate that Departments should have primary responsibility for undertaking reviews. The recent establishment of a number of central supports by the Department of Finance, such as a dedicated training programme and a best practice network for expenditure reviewers in Departments/Offices, should encourage the production of high quality and rigorous reviews and bring some consistency in approach to methodological issues. The new network of expenditure reviewers, under the central leadership of the Department of Finance, should act as a forum for sharing experiences and for disseminating best practice among those involved in conducting such reviews. However, there may be a need for some central unit playing a role similar to that played by the National Development Plan/Community Support Framework (NDP/CSF) evaluation unit in the context of National Development Plan related expenditure. Such a central unit could also be involved in assisting Departments in relation to evaluation and it could assist evaluation of cross-cutting policies.

Finally, programme review is not an end in itself. There is a need to strengthen the links between the reviews and budgetary decisions. Following a review of the expenditure review process, steps are now being taken to address all of the foregoing issues.

5.4.6 Research

In addition to the evaluation of specific expenditure programmes, good decision-making on public expenditure depends on the ability of Departments to undertake more general research on the policy options for achieving various policy objectives. While evaluation generally involves some research, it tends to have a particular focus on the efficiency or effectiveness of a particular programme.

Department is currently considering options for building on the strengths of the Policy Analysis Training Course which would also take account of the experience and lessons of the previous Analyst scheme, new environmental and organisational challenges facing the public sector and the skills sets of existing and newly-recruited civil servants.

General research work is required, for example, to look at the context for policy formulation, to provide the basis for evidence-based policy making, to identify processes that policy should seek to influence, or to identify areas not currently being addressed by policy. The Council has previously emphasised the desirability of developing policy-relevant scenarios based on expected economic, social and demographic changes in order that the implications for policy be available in time to plan for emerging needs (NESC, 1999). Over the coming decades, for example, ageing and the associated pension and health care demands will have implications for Ireland's society and economy. Shocks and unexpected events will continue to disturb the economy. It is desirable then to consider possible future scenarios in order that the implications for policy be available in time to plan for emerging needs. The importance of such scenarios is illustrated by the current bottlenecks in housing and infrastructure. The Council welcomes the work that the Department of Finance has undertaken in the Long Term Issues Group and notes that further work that addresses the foregoing comments is under way. The Council would suggest that these long term issues should be independently reviewed and the conclusions published. The Council also welcomes the technology foresight exercise undertaken by the Irish Council for Science, Technology and Innovation (ICSTI).

A number of interviewees pointed to important benefits that had accrued to their Department from initiating research projects. Yet, at the same time, several interviewees argued that Government Departments (including their own) do not undertake enough research activity. This is quite striking, particularly given the high priority that Irish public policy currently attaches to encouraging R&D activity in the private sector. Unlike evaluation, research work often requires specialist expertise, and will generally be undertaken by outside consultants, or by staff working within Departments on contracts of defined duration. The latter model has advantages, since the researchers can draw on the experience of Departmental staff, while staff can benefit from interaction with the research work. Developing research activity, therefore, requires resources, a flexible approach to the employment of research staff, and recognition of the importance of on-going research. Just as in the private sector, successful governance will often depend on a firm commitment to R&D, often in the face of long pay-off periods and competing demands on budgets.

5.5 DEVOLUTION

Devolution is an issue that emerged in a number of interviews, and which is sufficiently complex to merit separate treatment. The manner in which service delivery is organised, and the devolution of power from Government Departments, either functionally or geographically, will have a significant impact on the key concerns of this project. In this section, three types of devolution are examined, namely:

1. devolution within Central Government, from the Department of Finance to line Departments;
2. devolution by line Departments to ‘functional’ agencies; and
3. geographical devolution by line Departments to local entities.

In each of these cases, a number of common issues arise. Thus, in deciding where to locate decision-making functions, it is important to take account of information flows, and the advantages of locating decision-making where policy-relevant information can be most readily accessed. This concern has to be balanced, however, against the need to take account of a broader picture, and to ensure that decision-makers face incentives that are in line with the broad national interest. Moreover, it is also important to establish a reasonable division of labour, such that individuals within the system can focus on relevant tasks, and that, for example, policy-setting activity does not become swamped by the tasks of policy implementation. Finally, this Section discusses recent research on new possibilities for the allocation of responsibilities between central and local levels.

5.5.1 Finance and Line Departments

The issue of devolution arises in the first instance in the relationship between the Department of Finance and other line Departments, an issue discussed in the report of the SMI Financial Management Working Group. This Group reported that, for some time, the Department of Finance has been pursuing an active policy of maximum delegation of control over programme spending to line Departments, where the broad parameters for spending on these programmes had been established. According to this report, programme expenditures are in a very large measure already delegated. In relation to capital expenditure it noted that where once-off capital projects give rise to substantial ongoing operational costs, Finance may retain the right to authorise spending on a project-by-project basis. Administrative spending meanwhile is managed within the framework of administrative budget agreements. These arrangements give Departments a degree of flexibility within the total administrative budget.

The perspective above suggests that, overall, there is substantial devolution of the management of expenditure to Departments. However, there was some frustration expressed by some interviewees in relation to control of administrative staff (as discussed above) and other human resource issues. On the other hand, there may be sound reasons for centralised organisation of personnel, such as, for example, to facilitate movement of staff between Departments.

5.5.2 Policy and Delivery

Another aspect of devolution is the extent to which activities are concentrated within a Department or devolved to other organisations. A feature of public service reform across several OECD countries has been an emphasis on the distinction between policy and executive roles. This has meant the devolution of many executive roles to agencies, while core Government Departments concentrate on policy and oversight of agencies. For example, in the UK much of the work of the civil service has been transferred to agencies.

A feature of the organisation of the public service in Ireland is that there is extensive devolution of executive functions to public agencies, such as the IDA, Bord Fáilte, CIE, Health Boards and so on. Recent developments of this kind have included the establishment of the Prisons Service as a separate agency and the further transfer of responsibility for voluntary hospitals from the Department of Health.

The Department of Social, Community and Family Affairs is an exception to this pattern. There is, however, a division of responsibility within this Department between service provision (undertaken by the Social Welfare Services Agency) and policy functions (undertaken by the Aireacht). Another exception of a somewhat different nature is the Department of Education and Science. In one sense, most of its services are delivered by separate institutions in that the actual delivery of education is undertaken by schools and third-level institutions. However, aside from this, the Department's services are administered centrally by the Department itself. This means that the Department is involved in very detailed administrative work. This facilitates tight financial control but has the disadvantage of burdening the central Department with executive functions. Following a review chaired by Mr. Sean Cromien, in June 2001 the Minister of Education and Science has announced structural changes to reduce the burden of administrative work on the Department. An Examinations Commission is to be established that will take responsibility for the running of State examinations and a new National Council for Special Education will provide research, expert advice and a range of educational services for students with disabilities (Department of Education, 2001).

While there is extensive use of executive agencies or organisations in the delivery of services in Irish public service, this does not imply that the relationship between Departments and agencies is always satisfactory. The recent development of Service Planning Agreements by Health Boards is an example of an approach to clarifying this relationship. Notwithstanding the extensive use of agencies in the public service, formal purchaser/provider agreements are rarely used between institutions within the public service. Such agreements could possibly be helpful in many areas in clarifying expectations and improving transparency. In the health area, for example, there may be benefits to developing formal purchaser/ provider agreements between Health Boards and hospitals and other service providers.

5.5.3 Local and Regional Devolution

The extent to which regional and local devolution is an issue varies by Department. A key issue in determining the appropriate level of geographical devolution is the importance of specifically local information in decision-making. The Departments to which local or regional devolution is currently of most significance are Environment and Local Government, Health and Children, and Education and Science. In the case of the Department of the Environment and Local Government, local authorities deliver most of its services. In the case of the Department of Health and Children, there is some regional devolution to the extent that Health Boards have some autonomy in planning services in their regions. In the case of the Department of Education and Science there has been a marked absence of any regional structure for the administration of most of its services although it was announced in June 2001 that a new network of regional offices is to be put in place (Department of Education, 2001).

5.5.4 A New Approach to Devolution: Democratic Experimentalism

Recent research has identified new possibilities for the organisation of local-central relations (Sabel, 2001; O'Donnell, 2001). This approach was inspired initially by the organisational approaches of leading private corporations. It is of particular relevance to cross-cutting problems. These problems typically require both central strategic direction and at the same time local responsiveness that vertically organised departments have difficulty in providing.

The new approach is 'experimental' as it involves providing local actors with scope to experiment with different approaches to problem solving, within certain parameters. The following quotation from Sabel is a concise statement of the essential features of this approach:

> Local actors are given substantial liberties to set goals for improvement and the means for accomplishing them. In return they must propose measures for assessing their progress and provide rich information on their own performance. The centre pools the information provided by local actors and ranks them according to (periodically revised) performance measures that give substance to standards of excellence and definitions of inadequacy. In the best cases the centre provides assistance to those who are not improving as quickly as their likes. In all events it eventually sanctions those whose continuing failure seems incorrigible. The system increases local innovation by allowing those on the spot to test, within broad limits, their assumptions of what works best. At the same time it makes the exercise of local discretion sufficiently transparent to assure public accountability, allowing each locale to learn from the experiences of the others, and the polity as a whole to draw lessons from the experience of all (Sabel, 2001: 137).

While this model may seem removed from real problems, it is emphasised by O'Donnell (2001) that there are many examples of the application of this new approach. It is an approach to devolution that is not limited to devolution between central and local government. The best examples of this in Ireland are the local partnerships formed to tackle social exclusion and promote enterprise development, some of which have been the focus of international attention as exemplars of the experimentalist approach (Sabel, 1996). Other examples identified by O'Donnell of instances of this approach in Ireland include policy initiatives tackling drug abuse, environmental protection, and the approach of some local authorities to waste management.

5.5.5 Conclusions on Devolution

Clearly, the issue of devolution is complex and multi-faceted, raising a range of issues. From the perspective of this report, however, achieving the appropriate level of devolution is important as it will crucially affect the information available for making expenditure decisions, and the incentives facing those who make them. It is also important in ensuring that policymakers have the opportunity to focus on policy decisions, rather than being tied down with executive tasks.

CHAPTER 6

THE MANAGEMENT OF LOCAL GOVERNMENT EXPENDITURE

6.1 INTRODUCTION

This Chapter reviews the management of local government expenditure. In line with the analysis in previous Chapters, the emphasis is on reviewing the processes that are in place to ensure that local government expenditure is managed efficiently and effectively. The discussion does not centre on the strategic policy choices that are made by local government. We take these as a given and focus, instead, on the mechanisms that are in place to follow-through on these choices once they are made. Throughout the Chapter, the emphasis is on local government in the aggregate, in other words, management systems and expenditure trends of *individual* local authorities are not examined. Equally, the financing of local government expenditure is not assessed in any significant way. This issue is only examined in so far as it relates to the management of expenditure.[1] Section 6.2 describes the essential features of the budgetary process at local level while Section 6.3 describes the new systems that are being put in place for the management of local government expenditure. Section 6.4 presents analysis and conclusions.

6.2 THE BUDGETARY PROCESS AT LOCAL LEVEL

The local government budgetary cycle operates on a calendar year basis. Thus, the budgetary process for local authorities begins in the late summer/early autumn when most local authorities gather the necessary data from internal sources and start compiling the

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1 See NESC (1985), KPMG (1996a) and Coughlan and de Buitléir (1996) for a more detailed discussion of issues relating to the financing of local government.

Estimates. The Estimates are usually prepared by the county/city manager (and his/her finance officer) or sometimes by an Estimates committee, with the assistance of the county/city manager. Once the Estimates are prepared, there is a statutory period, usually of about two months duration, given to each local authority by the Minister for the Environment and Local Government to consider the Estimates. For most local authorities, this period falls over the October to November calendar period. During this period, the county/city manager presents the Estimates (renamed the Draft Budget in the Local Government Act, 2001) to the city/county council for debate, amendment (if necessary) and adoption.

From the time that the Estimates are first presented to the city/county council, it has a statutory period of 21 days in which to adopt the Estimates and, where applicable, strike a rate in the pound. The rate in the pound is calculated as a residual based on whatever resources are required to make up any shortfall between the local authority Estimates and its expected revenues from sources other than commercial rates. Since the establishment of the Local Government Fund (see below), the Minister for the Environment and Local Government has limited the percentage increase in rates, at around the rate of inflation.[2] If a council fails to adopt its Estimates during the 21-day period, there is statutory provision for the city/county council to be replaced by a Government-appointed commissioner. This is a relatively rare occurrence.

Once the Estimates are approved, there is provision for the approval of additional expenditure where such expenditure is in excess of already agreed amounts. In such cases, additional expenditure Estimates are presented to the city/county council for approval. Where such expenditure requires local authority borrowing, Ministerial approval would also be required. Once the rate in the pound is set, it cannot be changed for that year. Therefore,

2 Since the abolition of domestic rates in the late 1970s and the introduction of central government grants to meet the cost of the domestic rates income foregone, the Minister for the Environment and Local Government has been empowered to cap rates. See Coughlan and de Buitléir (1996) for more on the history of rates in Ireland.

additional expenditures in any one year cannot be financed by rate changes during the year.

6.3 LOCAL GOVERNMENT REFORM

6.3.1 Background

The SMI, which has been guiding public sector reform at the central level, has also influenced reform at local government level. Many of the reforms that have been introduced have their origins in the 1996 Department of the Environment publication, *Better Local Government: A Programme for Change*. This Section reviews the reform of local government that has taken place in so far as it affects the management of local government expenditure. While much of the reform was only given legislative effect with the enactment of the Local Government Act, 2001, most local authorities had already begun implementing some of the changes prior to the formal enactment of the legislation, including the development of corporate plans and the establishment of new committee systems.

6.3.2 Organisational Reform

The Local Government Act, 2001 provides for the establishment of Strategic Policy Committees (SPCs), composed of elected members and representatives of sectoral/community interests, within each local authority. The role of the SPCs is to *develop* policy under the various programmes operated by the local authority. This is a significant departure from traditional practice whereby local councillors could only *alter* plans and policies that had already been prepared. Cross-cutting issues are to be handled by a Corporate Policy Group (CPG) in each local authority, composed of chairpersons of each authority's SPCs and the Cathaoirleach or Mayor/Lord Mayor. Most local authorities have already established these new committee systems.

In addition to the SPCs and CPGs, County/City development boards (CDBs) have also been established in every county and city of

Ireland. Each CDB is composed of representatives of local government, local development bodies, and the state agencies and the social partners at local level. Their role is to draw up and oversee the implementation of a County/City Strategy for Economic, Social and Cultural Development.[3] The CDB strategies are to have a 10-year focus but will be broken down into three- to five-year targets. It is expected that these strategies will form the template guiding all public services and local development activities, ensuring coherence and avoiding duplication in the delivery of services.

Neither the SPCs nor the CDBs will have much role in managing their respective local authority's expenditure. However, their impact on expenditure is expected to be seen through the increased efficiencies that should result from improved and more focussed planning and policy development. The CPGs, however, have a more direct role in the management of their local authority's finances. The county or city manager must consult with the CPG in the preparation of the authority's Draft Budget. In effect, the CPG replaces the Estimates committee that formerly monitored expenditure in some local authorities.

6.3.3 Corporate Planning

The central focus of local government reform is the maximisation of efficiency in resource use through an increased emphasis on corporate planning. The emphasis on corporate plans rather than the strategy statements typical of central government departments is a reflection of the differences between central and local government organisation and also the perceived need to operate the service delivery functions of local authorities on a more 'business-type footing'.

The Local Government Act, 2001 provides for corporate plans to be prepared by each local authority within six months of a local election, which now must take place every five years. The corporate plan therefore has a medium-term outlook setting out the principal

3 The CDB Strategies are required to have a special emphasis on social inclusion.

activities of the local authority, its objectives and priorities, proposals to assess its performance in respect of its activities and other matters relating to human resources.

The corporate plan must be prepared in consultation with the local authority's CPG and must be approved by the elected council. In principle, the plan should set the framework for the policy-making activities of the SPCs and the CPGs and should also reflect the activities of the CDBs and contribute to their aims. As the 2000/2004 corporate plans have already been prepared in advance of the CDB strategies, the current set of corporate plans are supposed to be amenable to change to reflect relevant aspects of the CDB strategies. Subsequent corporate plans should automatically reflect the CDB strategies.

The guidelines to the local authorities on the preparation of their corporate plans state that the corporate plans should describe the ongoing framework for monitoring and reviewing progress and the procedures that will be used for corrective action where monitoring indicates the possibility of only partial achievement of objectives. In this regard, the City/County Manager must prepare an annual progress report in respect of the local authority's corporate plan. This report is supposed to be based on progress across the range of monitoring indicators identified in the corporate plan and on the regular reviews of the operational plans that are developed within the local authority to implement the detail of the corporate plan. The city/county manager must submit the progress report to the elected council at the same time as the local authority's Draft Budget or Estimates. This goes some way to formalising the link between expenditure plans and the achievement of objectives. In addition, the annual progress report should be recorded in the local authority's annual report.

6.3.4 Financing Reform

As Chapter 2 has outlined, nearly 50 per cent of local authority current expenditure is funded by central government. Since January 1999, this contribution is funded through the newly established

Local Government Fund. The Fund provides finance to local authorities as *general purpose* grants and for non-national roads. As such, the local authorities have discretion in how these monies can be spent. The Fund is itself financed from two sources: an Exchequer contribution (approximately €210 million in 1999) which is increased annually to take account of inflation and changes in the functions of local authorities; and the proceeds of motor taxation.

The establishment of the Fund represents a significant reform because for the first time, it guarantees on a legislative basis (the Local Government Act, 1998) an Exchequer contribution to local government revenues that cannot be eroded in the future and is required to "have regard to" the changing functions of local authorities. This has injected a measure of stability and certainty into local government financing that has been absent. In the past, local authorities had to adopt their Estimates without knowing what their funding for general purposes or for non-national roads would be for the following year. Exchequer funding of local authority current expenditure thus now has a floor indexed to inflation. Indeed, the Fund has led to a substantial increase in funding for local authorities. It also creates a link between motor taxation receipts and expenditure on road upkeep.

In principle, the Local Government Fund should give local authorities greater flexibility in meeting the funding needs of their work. However, there is also an expectation that there will be an efficiency gain arising from prudent management of this new funding. Indeed, in 2000, part of the Fund (approximately €2.3 million) was set aside for specific customer service innovation/ efficiency projects funded on a competitive basis. In this way, local authorities that demonstrate a commitment to innovation and efficiency are being rewarded.

Allocations from the Local Government Fund across local authorities are determined in part by a 'needs and resources' model. This model was first applied on a limited scale in 2000 and its use is being gradually extended. As the name suggests, the model decides allocations based on each local authority's needs (set against expenditure targets at service level) and resources (set against the capacity to raise resources through other means). The model is still under development and it is expected that continued refinement will take place in the coming years. Similar equalisation funding mechanisms have run into problems in the past both in Ireland[4] and elsewhere. For example, it is important that the 'needs and resources' model does not generate perverse incentives, in other words, local authorities that perform well on efficiency and effectiveness grounds should not be 'rewarded' by seeing a downturn in their allocation from the Local Government Fund. At present, the 'needs and resources' model allows local authorities to retain any efficiency savings that they generate. Another way to ensure that the drive for efficiency is maintained might be to extend the mechanism for funding innovation/efficiency projects on a competitive basis. This was included as part of the allocations from the Local Government Fund in 2000 as a one-off exercise while the 'needs and resources' model was still in development. There may be scope for making this a more regular feature of funding from the Local Government Fund.

The Local Government Act, 2001 also permits local authorities to establish a community fund, separate from other funding arrangements, to support specific community initiatives such as amenity, recreational, cultural or heritage facilities, environmental or community development projects. Contributions to the fund may come from local voluntary, business or community groups, the local authority itself or from local community members through the establishment of a scheme designed to collect an annual contribution from local community members. However, there is no obligation on the part of local authorities to establish a community fund. The idea is to give local authorities a mechanism to raise funds for community projects where a specific local need has been identified by the community itself. So far, no such community funds

4 In the early 1990s, there were proposals to establish some kind of formal equalisation model for the allocation of central government grants to local authorities but because of the expected substantial redistribution of grant support across local authorities, these proposals were never realised.

have been established; the relevant section of the Local Government Act, 2001 has not yet commenced.

6.3.5 Financial Management Reform

A new financial management system is being introduced into local government. Accounting procedures are being switched from a cash to an accruals basis; i.e, recording costs and revenues as they occur, whereas cash accounting registers them when payments are made or received. Accruals accounting is generally believed to provide improved management information and can facilitate the integration of financial and performance measurement. In line with this, greater devolution of financial management within individual local authorities is taking place. Significant investment is being made in computer software systems to support these changes. The new system of financial management has been implemented in relation to expenditure but in relation to income is still being developed. A new costing system that will generate information on the true cost of providing individual services is to be developed and it is hoped that it will be introduced by 2003. Combined, the new financial management and costing systems will enable local authorities to relate input costs to outputs produced, which will in turn enable local authorities to make decisions on the allocation and re-allocation of resources in a more systematic way than heretofore.

New organisational structures have also been put in place to underpin the new financial management system. Following a review of the role of the finance officer in local authorities conducted by the Department of the Environment and Local Government in 1999, the grade of finance officer has been increased to the equivalent of assistant city/county manager and steps are being taken to professionalise the finance units within local authorities through increased recruitment of qualified financial and management accountants.

The new financial management system will be complemented and further underpinned by regular value for money audits that have been a feature of local government management for a number of years. The Local Government (Financial Provisions) Act, 1997 established on a statutory basis the Value for Money (VFM) Unit in the Department of the Environment and Local Government. The Unit carries out VFM studies on local authority operations with a view to boosting efficiency and cost effectiveness. To date, 20 VFM reports have been prepared covering a wide range of services from parking charges to waste collection to public lighting. The local government auditors can conduct their own VFM examinations and assess the extent to which local authorities have implemented the changes recommended in the reports issued by the VFM Unit. In general, the VFM studies are seen to have had a positive impact on the operations of many local authorities. A consultancy study has been recently carried out on how to further maximise the role of the VFM studies and recommendations emanating from that work are expected shortly.

6.3.6 Performance Measurement

A greater emphasis is now being placed on performance measurement at local government level. Following consultation with local authorities, the Department of the Environment and Local Government has published a set of 21 indicators against which local authorities and the general public can judge their performance in key service areas – housing, roads, motor taxation, environmental services, planning, revenue collection, corporate health and library services. Local authorities are required to publish their performance results in their annual reports. This will enable local people and businesses to assess whether their local authority is scoring well across key service functions. Local authorities will also be able to benchmark their own performance against that of other local authorities. Following a commitment in *Better Local Government: A Programme for Change*, the service indicators will be combined with other financial performance indicators that will be developed following the full introduction of the new financial management system. This should produce a more comprehensive picture of performance.

A key question to consider, however, is what exactly is being measured. In public policy, there is a very important distinction between programme/policy inputs, outputs and outcomes. In general, it is easier to measure inputs (e.g. cost and number of librarians in public libraries) and outputs (e.g. number of books issued per head of local population) than outcomes (e.g. changes in literacy levels in the community). In line with this (and perhaps by definition), the agreed service delivery indicators for local authorities are largely input and output measures.

Another issue is how the performance information is used. Performance measurement is not the same as performance management. Thus, the performance and financial measures need to be actively used as part of the review of progress of each local authority's corporate plan, with the provision that policy/operational changes can be made when performance measures indicate that such changes are necessary. Following a commitment in PPF, a sector-wide performance management advisory and monitoring group has been established under the auspices of the Local Government Management Services Board to oversee the development and implementation of the performance management system to be introduced into local authorities.

6.4 ANALYSIS AND CONCLUSIONS

It is clear from Section 6.3 above that there is substantial and ongoing reform at local government level, with many changes that will have a significant effect on the management of local government expenditure being introduced in the current year. This makes analysis of the reforms difficult because it is often only in implementation that difficulties arise.

Nevertheless, the changes currently being introduced seem impressive. There is a clear emphasis on developing a management system that integrates financial management and resource allocation decisions with performance management at both a strategic and operational level. Organisational changes have been put in place to ensure that decisions are undertaken in a planned manner and there is provision for continued review and monitoring of local authority activities and procedures for making change where appropriate. Additionally, there is a clear focus on the service delivery functions of local authorities and on the needs of their customers/citizens. Because of this, the management systems at local government level appear to be more open and transparent than at central government level, with statutory obligation to publish corporate plans, progress reports and service delivery indicators. The presentation of local authority Estimates (now called Draft Budgets) in a functional programme format also aids transparency. Finally, significant investment is being made in the development of new financial management and costing systems and there is a commitment to further improve the results arising from the value for money audits.

Notwithstanding this progress, issues remain. Implementation, as discussed above, is crucial. There will undoubtedly be teething problems, some big, some small. The role of the Department of the Environment and Local Government in supporting local authorities through the change process will be important. However, it also seems that there is considerable scope for co-operation amongst local authorities themselves in working through what may be common implementation problems. This might be done through the new organisational structures recently introduced into local government. Thus, for example, the development of networks of CPGs amongst similar-sized local authorities may facilitate the horizontal exchange of ideas and experience and further develop a collegial commitment to the reform process.

Another issue relates to the management of the flow of information that the reforms produce. At the heart of this project are questions around the ability of government (including local government) to make the right expenditure decisions to ensure the achievement of stated priority objectives and to do this continuously, implying the ability to make difficult resource re-allocation decisions when conditions or priorities change or when programmes are failing to meet their objectives. It seems apparent that this cannot be done in any rational way without information, whether it be performance, service delivery or financial.

To overcome information overflow problems, it seems essential that while many information pieces are collected at different levels of each local authority, only key items should be directed to the top levels. This means that devolution of authority, responsibility and accountability within each local authority will be crucial. It also suggests that divisional managers have the capabilities (and the necessary support for those capabilities in terms of training and resources) and the related trust of more senior management.

Another information issue is information in relation to the economic role of local authorities. Local authorities are significant economic entities, but very little information is published in relation to their role in the economy. It would therefore be desirable to publish more economic information on local authorities.

As described above, there is a statutory obligation on the part of local authorities to publish their performance in key service areas. While this will enable individual local authorities to compare themselves against other similar local authorities, there are currently no formal plans to conduct such a benchmarking exercise across the whole local government sector. This might be a useful extension of the functions of the VFM Unit in the Department of the Environment and Local Government. Such an exercise would of course need to be carefully structured and organised in partnership with the local authorities themselves in order to ensure the highest degree of data comparability and a means to take account of the context in which different local authorities work. Elsewhere, benchmarking of local authority performance has proved most useful and gained most acceptance where it has been designed by the local authorities themselves. The establishment of networks of similarly-sized local authorities, such as those suggested above, might provide an appropriate mechanism for benchmarking activities. A central agency could also provide technical assistance and, if necessary, collate the data (Boyle, 2000).

Some of the services delivered by local authorities have implications beyond the boundaries of individual local authorities. Services that have spillover effects include planning, infrastructure, waste management and lake and river catchment policies. Effective planning and delivery of services of this nature requires co-ordination between local authorities. Some co-ordination takes place between local authorities but the Council believes that there is a need for a significantly enhanced level of co-ordination to meet current challenges. The consultation paper (2001) for the National Spatial Strategy, *Indications for the Way Ahead*, proposes that spatial planning be informed by the concept of "functional areas". These are areas that share common characteristics and issues, where people live their working, schooling, shopping and leisure lives, and with which many can identify. A focus on the proposed functional areas could give a useful impetus to stronger co-ordination between local authorities as well as co-ordination between public agencies generally within functional areas.

To conclude, it is interesting to compare what is happening at local government level with developments in central government.[5] Many of the reforms being introduced to central government are similar to those described above for local government (e.g. strategy statements, business plans, improved financial and performance management systems). However, it appears that local government has been ahead in terms of implementing the reforms and more crucially, in seeing how the individual reforms can work as a package. There may be a number of reasons for this.

First, it has to be recognised that central government and local government are different beasts. This can be seen most readily in the different functions that each perform, with local government primarily involved in planning, development and service delivery while central government is primarily involved in policy formulation and co-ordination. Integration of performance management and financial management is generally seen to be less difficult when there are tangible, standardised products and services (e.g. building roads, issuing licenses) than when there are non-tangible ones (e.g. co-ordination of activities; provision of policy advice) (Pollitt, 1999). Thus, local government by its very nature, may be more amenable to the types of reforms that are required.

5 Reforms at central government level are discussed in Chapters 4, 5 and 7.

Second, the Department of the Environment and Local Government has engaged the local authorities in the reform process and has involved them at every stage. Probably more importantly, however, the establishment of the Local Government Fund and the securing of guaranteed additional funds provided the necessary incentive to commit to the overall reform package. No such 'sweetener' has been made available at central government level, which may partly explain the slower pace of reform there. Also, the fact that there are more constraints on the ability of local government relative to central government to raise revenues means that there has traditionally been, and continues to be, more pressure on local authorities to create efficiencies to fund the development of new services.

Third, while some may believe that public sector reform is just the latest 'fad' of politicians and management gurus, its rationale is really much more well-founded. It is motivated by a public who are more demanding of their public services, who are unwilling to pay for these services through increased taxation unless value for money can be demonstrated and by the emergence of new issues that are often cross-cutting in nature and therefore require new approaches to both policy development and implementation. These pressures for reform are likely to be more visible at local government level where the interface between the customer and the deliverer of services is much closer than at central government level.

CHAPTER 7

CONCLUSIONS AND RECOMMENDATIONS

7.1 INTRODUCTION

Drawing together the analysis thus far, this final Chapter sets out the Council's conclusions, and its recommendations for change to the system of public expenditure management. Thus, the Chapter focuses on a number of key themes that have emerged during its work on this project, and thereafter presents a set of related recommendations. The focus of this report is on the administrative processes and structures that support the ability of Government to make public expenditure decisions in accordance with changing circumstances and priorities. These administrative structures exist to support political decision-making and the political nature of the process as a whole should be borne in mind. The political process itself is not addressed in this report. There are issues to be considered on this front in relation to the process by which the Oireachtas considers the expenditure process both in relation to the consideration of the overall medium-term context in which expenditures are settled, and the examination of existing programmes. In this report, however, the primary focus is on the allocation of expenditure across different areas for any given level of total expenditure rather than the appropriate level of public expenditure. The Chapter begins, however, with a brief revisit to the underlying motivation for the project as a whole.

7.2 MOTIVATION FOR THE PROJECT

Ireland's economic fortunes have varied greatly in the past two decades. From the 'bust' times of the 1980s, to the 'boom' period of the 1990s, economic growth and employment have gone through at least one major cycle. Within that experience, there have also been minor cyclical variations, such as are normal for any advanced economy, and which largely reflect the international business cycle.

While the short-term outlook at the time of writing this report is most uncertain, it is reasonable to expect that the Irish economy is embarking onto a period of more moderate growth than was experienced during the boom of 1993-2000. This growth is likely to continue to be high by international standards, but the growth rate is also likely to converge towards that of our European partners. Again, within this scenario, one must also expect short-run cyclical variations in the level of growth and employment.

Given this historical experience and future outlook, the Council wished to consider the efficacy of the Irish system of public expenditure management and to examine how well the public expenditure management system has coped in the context of changing economic fortunes. While the Council recognises that it was necessary to reduce the level of public expenditure during the 1980s, and indeed was foremost at the time in putting forward that view,[1] it is still appropriate to consider whether the cuts were achieved in the most effective manner possible, particularly in terms of the long-term impact on services. Similarly, during the boom period of the 1990s, when new resources became available to the public sector, it is appropriate to consider whether these were deployed in the most effective possible manner.

To some extent, it is perhaps unreasonable to focus on these two periods, since both were somewhat exceptional by the standards of other advanced economies.[2] Certainly, in the period of boom, the problems that the public sector had to address were changing at a most rapid pace. Examining and learning from these experiences is important going forward as the rate of economic growth fades somewhat, and the rate at which new resources become available declines. Within this scenario, when resources become scarcer (although still plentiful by comparison with the 1980s), it is all the more important that the system for managing the allocation of resources should be robust and capable of achieving national

1 See NESC (1986).

2 There have, however, been numerous examples in other advanced countries of episodes of rapid contraction in public expenditure. See, for example, Alesina & Ardagna (1998).

objectives. This involves dealing with the cyclical variations in economic growth that will occur, while also taking a longer-term view of the process of wealth creation and its implications for the resourcing of the public sector.

7.3 KEY ISSUES IN THE MANAGEMENT OF PUBLIC EXPENDITURE

This Section outlines the key issues in the management of public expenditure in Ireland. It is based on the analysis of the Irish system in earlier Chapters and takes account of relevant developments in other OECD countries in reforming the management of public expenditure.

7.3.1 Strategic Focus

There are several strategic inputs to budgetary decisions. Governments formulate strategic priorities for public expenditure and other policies in Programmes for Government. Other strategic inputs are NESC Strategy reports, social partnership agreements, the National Anti-Poverty Strategy (NAPS) and the National Development Plan (NDP). The Council believes that these inputs are important in influencing the allocation of public expenditure to areas of economic and social priority. The Department of Finance maintains contact throughout the year with Departments in order to ensure that emerging policy developments address strategic Government policy objectives and programmes and are funded and to reconcile the spending demands with the guidelines set out. The Estimates process *per se* is only a very small part of this overall picture. The Government is briefed on the outcomes and it makes final decisions on resource prioritisation across programmes. Nonetheless, the Council believes that there is a need for reform to highlight the link between strategic priorities and expenditure allocations and to encourage spending Departments to take a more strategic focus, outside their own immediate areas and in accordance with economic and social priorities.

Notwithstanding the reforms that have taken place the system still operates in an incremental way. The system is slow in reallocating expenditure from old to new priorities. Expenditure programmes are very rarely eliminated. Boyle and Humphreys (2001) have noted that the incentives in the system tend to encourage a process whereby new priorities may emerge but it is difficult to re-assess existing commitments in this light.

Excessive departmentalism is another feature of the system. While it is rational for individual departments to pursue their own interests in negotiations, there needs to be some counter-balance so that the bigger picture of national strategic policy priorities is not lost in the process. The trust between line Departments and central Departments and the kind of positive strategic thinking that can produce the most effective outcomes need to be enhanced.

Some public management reforms in OECD countries have helped the centre to focus more effectively on strategic policy issues. In particular, the trend in several OECD countries towards less detailed central control of inputs (while not compromising the control of expenditure totals) has provided greater potential for the centre to focus on strategic issues. Similarly, the trend to move certain service delivery functions outside the core civil service in some countries also provides at least the scope for a stronger focus on strategic work by the civil service.

7.3.2 Outputs and Outcomes

The management of public expenditure needs to place much more emphasis on what is produced (outputs) and what is achieved (outcomes) rather than the traditional focus on inputs (money, numbers employed). While some elements of accountability for results have been introduced through the SMI (strategy statements, business plans, annual reports and the performance management and development system, PMDS), the primary documents that guide the management of public expenditure are firmly focused on inputs. The main document that sets out spending plans is the *Estimates for Public Services* and this document does not contain any information on what the expenditure is expected to achieve. The primary *ex-post* report on public expenditure is the annual *Appropriation Accounts* and the focus of this document is on the consistency of the expenditure outturns with appropriations (i.e., planned expenditure). Thus both the planning of expenditure and subsequent accountability direct little attention to outputs or outcomes.

There is a trend in several OECD countries towards greater emphasis on outputs and outcomes in both budgeting and management. Public sector reform across the OECD first sought to shift the focus from the control of inputs to the outputs produced. An output-focussed system emphasises the services delivered and products produced. New Zealand is an example of a country that emphasises outputs in both its budgetary and management systems.

While PUMA (2001) has found that the output approach enhanced the quality of management and increased efficiency, it has a number of limitations. It can divert the attention of government departments and agencies from the impact of their activities on society and insufficient attention may be paid to policy learning from the impact of policy on the desired outcomes.

These limitations have stimulated interest in placing greater emphasis on outcomes in budgeting and management in recent years. An outcome-focussed approach involves the government defining outcomes, allocating resources to produce services to achieve the outcomes sought, evaluating the extent to which the outcomes are achieved and using this information in subsequent decision-making. In Australia and the Netherlands, the main budget and financial reports are now being restructured around outcomes. In Canada, the UK and the US, increasing attention is being paid to output and outcome goals in the budgetary process (PUMA, 2001).

Not all efforts to reform the budgetary process to focus on outputs and outcomes have been successful, as noted in Chapter 3. However, notwithstanding setbacks in budgetary reform, countries have persisted in finding new ways to organise the process. Indeed in recent years there has been renewed interest in many OECD countries in reforming the budget system in this way, particularly with reference to outcomes.

Shifting the focus from inputs to outputs or outcomes also involves a shift in the nature of accountability. Rather than simply focusing on whether *ex-post* inputs matched the level and purposes prescribed in advance, accountability is based to a greater degree on what expenditure has achieved.

7.3.3 Evaluation

A focus on outcomes involves more explicit links between expenditure allocations and the goals of policy. One of the implications of this approach is that it requires analysis of the links between expenditure allocations and the ultimate impact of the expenditure. Evaluation is a way of trying to establish the link between expenditure allocations and policy objectives. Expenditure programmes should be evaluated on a regular basis. Where expenditure is not achieving strategic policy objectives, changes in programmes or reallocation should take place. In this way evaluation has a critical role to play in the strategic management of public expenditure. Ideally, public expenditure management should involve a continuous cycle of *ex-ante* evaluation, allocation, *ex-post* evaluation and reallocation.

The level of evaluation taking place has expanded in recent years in the form of public expenditure reviews, value for money reports of the Comptroller and Auditor General and the system of *ex-ante* and *ex-post* evaluation and reallocation that is an integral part of the NDP process. While the expenditure reviews have had some impact, the links between evaluation and the formal Estimates process are weak. In many cases the expenditure reviews appear to be carried out in order to satisfy the requirements to undertake such reviews rather than functioning as an integral part of a system of managing expenditure in a strategic way. The process has been reviewed recently and a number of initiatives are being taken to strengthen the process and focus on ensuring that it delivers valuable and meaningful impacts across a range of areas, involving process issues, organisational improvement and learning, expenditure management and allocation and quality customer service.

7.3.4 Information

Good information systems are a critical support to the effective management of public expenditure. The role of evaluation in the effective management of public expenditure was discussed above. Evaluation in turn is dependent on the ongoing production of routine information on what is being produced and what is being achieved. The availability of this information is often a constraint on evaluation and therefore investment in improving information systems (including IT systems) is a key requirement. In addition to supporting evaluation, this investment is also essential to support regular monitoring and regular reporting on what is achieved for accountability purposes. Furthermore, accounting systems are central to the provision of timely and relevant information. This is an area where work is on-going in Ireland, and where progress is most desirable. Finally, public expenditure decision-making needs to be supported by high quality research.

7.3.5 The Importance of Skilled People

Perhaps the most important requirement for the effective management of public expenditure is to have a sufficient number of people with the relevant skills employed in key parts of the system. This applies to line Departments, as well as to central Departments. The ability of Government Departments to undertake high quality reviews is constrained by the availability of people with the relevant skills. Oireachtas committees also have limited resources in terms of people to assist them in their work in enforcing accountability for public expenditure. If the system is to develop towards more emphasis on accountability for results achieved with public expenditure, Oireachtas committees will need enhanced resources. They will also need to focus more on outputs and outcomes and to be clear about the respective responsibilities of the various actors, the Minister, central Departments, spending Departments and agencies. The development of the system in this way also points to the need for the Department of Finance to train or recruit staff with the necessary skills and expertise if they are to effectively encourage Departments to deliver optimum value for money in the provision of public services.

7.4 RECOMMENDATIONS

This Section outlines the Council's specific recommendations in order to promote reform of the system in the general direction outlined above. These recommendations are summarised in Table 1, and are explained in more detail below.

7.4.1 Enhance Strategic Direction

Notwithstanding the strategic inputs that already exist in the current system, a key conclusion drawn from the Council's analysis is that the system of public expenditure management should have a greater strategic capacity. This means creating a stronger link at official level that, at the outset of the process and throughout the budgetary cycle, would consider strategic management priorities and impress these on the allocation system. While the primary responsibility for providing strategic direction on expenditure management rests with the Department of Finance it should also involve a greater degree of input to strategic thinking from line Departments.

7.4.1.1 Create a Stronger 'Strategic Mechanism' at Official Level

It is important that stronger strategic mechanisms should become part of the budgetary process. This would involve a broad-level articulation of the Government's strategic economic and social priorities, and inputs to the budgetary process throughout the annual budget cycle, helping to steer the process to ensure that expenditure allocations are in line with broad-level economic and social priorities. The Estimates and budgetary process would have to be amended to provide relevant mechanisms to this end. This would support the ability of Government to allocate expenditure in line with its strategic priorities. This also means extending the focus of strategy beyond the aggregate level of public expenditure, to include the composition of that expenditure and how it relates to Government priorities. This could be done through the Department

Table 1

Recommendations

- **Enhance Strategic Direction**
- Create a Stronger "Strategic Mechanism" at Official Level
- Identify a Limited Number of Priority Areas for Special Treatment
- Initiate Expenditure Proposals from the Centre
- Involve Line Departments in Strategic Thinking on Priorities
- Develop Multi-Annual Budgeting for Priority Areas
- Examine Synergies and Inconsistencies
- Reward Work on Cross-Departmental Issues

- **Focus More on Outputs and Outcomes**
- Provide more Information on Planned Expenditure
- Publish Information on What Public Expenditure is Achieving
- Develop Accountability for Results through Oireachtas Committees
- A Balanced Approach to outputs, outcomes and inputs

- **Develop an Evaluation Culture**
- Strengthen Expertise in Departments
- Develop an Evaluation Network to Share Experience
- Establish a well resourced Central Evaluation Unit to Provide Support and Expertise
- Develop a Policy Proofing dimension to Evaluation
- Strengthen *ex-ante* Evaluation
- Strengthen Links Between Evaluation and Allocation
- Include Sunset Clauses in Legislation

- **Improve Information for Policy Makers**
- Develop IT to Provide Information
- Develop Accounting Systems
- Invest in Research

- **Invest in People**
- Invest in Skills Throughout the Service
- Recruit People with Specialist Skills

- **Local Government**
- Follow through on the Implementation of the Reformed System
- Enhance Co-ordination between Local Authorities and Other Public Service Agencies
- Publish More Information on the Economic Role of Local Authorities.

of Finance involving Heads of Departments in a structured way in the evaluation of proposals on the strategic direction of the overall approach to public expenditure. The Council believes that allocation of responsibility for this strategic function or mechanism is a matter for Government and the Oirechtas.

7.4.1.2 Identify a Limited Number of Priority Areas for Special Treatment

It is important to recognise that resources for public expenditure will always be limited. A central function of the system of public expenditure management, therefore, is to make choices, and to identify areas that should be prioritised in terms of expenditure, and other policy development. The Council recommends, therefore, that the strategic direction of public expenditure should include explicitly identifying a small number of priority areas that would be afforded particular attention and special treatment in terms of the allocation of resources.

7.4.1.3 Initiate Expenditure Proposals from the Centre

This identification of strategic priorities must be matched by a willingness to initiate expenditure proposals from the centre. Existing practice places the burden of initiative largely with line Departments. It is not sufficient to merely identify problems from the centre. A cross-departmental approach to policy problems would be an intrinsic part of this process.

7.4.1.4 Involve Line Departments in Strategic Thinking on Key Priorities

It is important that line Departments should be involved in the process of strategic thinking that results in the identification of key priorities. This would ensure that the considerable knowledge and expertise of line Departments is fed into the process. It is also essential that line Departments have some sense of 'ownership' over the broader process. This effectively means bringing together the Heads of Departments in advance of the annual formulation of budgetary policy and the Estimates round to engage in joint and co-operative strategic analysis. This would make an important contribution to developing greater understanding and trust between Departments and diminishing the 'game-playing' within the Estimates process.

7.4.1.5 Develop Multi-Annual Budgeting for Priority Areas

An important potential benefit of multi-annual budgeting is planning for new services. Where significant expansion of a service provision is required, this will often require more than one year to put the new service in place. Multi-annual budgeting in respect of key priorities would therefore facilitate expansion of services in the areas of key priority.

7.4.1.6 Examine Synergies and Inconsistencies

Expenditure proposals are normally developed within individual Departments without necessarily much examination of the relationship to existing and proposed expenditure programmes of other Departments. While the Council recommends that more expenditure proposals should come from the centre, there will also be an ongoing need for a process to more systematically examine these interactions before decisions are made.

7.4.1.7 Reward Work on Cross-Departmental Issues

A clear indication should be given that an individual's contribution to cross-cutting issues will be taken into account in the new performance management and development system (PMDS) and in promotion decisions. At present, a significant obstacle to the effective management of cross-cutting issues is the weak incentive to address these issues. Promotion decisions are normally based on one's contribution to one's own Department and there is an incentive to promote the position of the Department as assiduously as possible. Commitment to cross-cutting issues does not earn comparable rewards in terms of promotion.

The Council acknowledges that there has been success in some areas in developing an integrated approach to policy. Ireland's success in attracting foreign direct investment, for example, is based on widespread support for this objective and consistent policies across a range of areas (including education, financial incentives, taxation, promotion and incomes policy). Another example is the success of some local partnership companies at promoting an integrated approach to local development (see Sabel, 1996). The integrated services process (ISP) was a recent pilot project that sought to develop a new way of doing business that would lead to a more focussed and better co-ordinated response by the statutory agencies in disadvantaged urban areas. RAPID is a recently launched programme that involves the front loading of National Development Plan investment in 25 disadvantaged urban areas and the co-ordination of the activities of different State agencies to promote the development of these areas.

7.4.2 Focus More on Outputs and Outcomes

The Council recommends that there should be more emphasis on what is achieved through public expenditure in the budgetary system, rather than on inputs of resources. This requires changes in the systems of accountability for public expenditure and has implications for the skills required in key institutions.

7.4.2.1 Provide More Information on Planned Expenditure

The current Estimates publication shows the provisional expenditure outturn for the previous year and the projected level of expenditure for the coming year. Consideration should be given to each Department publishing, and presenting to the Oireachtas, its individual annual Estimates allocation together with details of the outputs which it is intended to achieve for this level of resources – this would effectively represent an integrated business plan for each Department for the year in question. The Estimates information could also distinguish the extent to which increases in planned expenditure are to be used to fund the existing level of services and the extent to which increases are to fund real increases in services. If such an approach is adopted the Department of Finance could also publish an overall summary report on public expenditure in place of the current Estimates Volume.

In relation to the existing information in the Estimates, there is marked variation in the level of detail provided. In some cases, details are provided for very small amounts of expenditure while in others there is no disaggregation for very large amounts of expenditure. It would be desirable to have greater consistency in the information presented in the Estimates with a view to enhancing the presentation of useful information.

7.4.2.2 Publish Information on What Public Expenditure is Achieving

The annual reports of Government Departments contain some useful information, but insofar as public expenditure is concerned they are very much secondary to the annual Estimates Volume and the *Appropriation Accounts*. The annual reports of Government Departments should also be developed to provide clearer information on what was achieved through public expenditure during the period being reported upon. The ongoing work of the Department of Transport on resource accounting could provide the basis for the development of more informative annual reports that would provide integrated performance and financial information

An annual overview report that sets out the objectives, activities, accomplishments and expenditure for each public expenditure programme should be published. This would complement the annual reports of individual Government Departments and agencies. An earlier attempt to provide such an overview was the publication of the *Comprehensive Public Expenditure Programmes*. This was a useful publication but has not been published since the 1980s. The usefulness of the proposed new publication would be enhanced, if over time, reports provided information on a comparable basis for several years.

7.4.2.3 Develop Accountability for Results through Oireachtas Committees

Oireachtas committees have an important role in the process of accountability for public expenditure, but at present this role is underdeveloped. As described in Chapter 5, for example, the role of the PAC is to focus on accountability for inputs. This role, or that of other Oireachtas committees, could be developed to include greater emphasis on outputs, and possibly outcomes. In making this recommendation, the Council is conscious that the primary accountability to the Oireachtas for Government Departments rests with the Minister, and is not suggesting that this should change. Moreover, making Secretaries General accountable to the Oireachtas for outputs and outcomes would require a clear set of rules and procedures which would not involve Secretaries General being asked to comment on political matters or on the merits of policy on which they are already prohibited from commenting. It would also involve recognition that outcomes are dependent on a range of factors, not all of which are within the control of administrators. Given these provisos, however, it would still be desirable for the role of the Oireachtas to be developed in this area.

Implementation of this recommendation would require that Oireachtas committees be provided with the support of professional staff with the time and expertise to analyse information on what is achieved with public expenditure. The flow of such information to the Oireachtas would also have to be developed. It would also be essential that the overall thrust of Oireachtas Committees in this regard would be to support a process of ongoing learning, dissemination of best practice, and constructive evaluation of Government activities.

The Departments themselves, in place of the traditional Appropriation Accounts, should produce a Report and Accounts which would formally account for the funds provided by the taxpayer and report on what had been achieved during the year in question.

7.4.2.4 A Balanced Approach to outputs, outcomes and inputs

In advocating greater emphasis on outputs and outcomes, the Council is not proposing that inputs should be neglected. Accountability for outputs and outcomes achieved should be within given resource allocations: the Council is not advocating that outputs or outcomes be pursued independently of costs. There are also risks that an excessive focus by Government Departments on the short-term production of outputs could lead to the neglect of longer-term strategic planning, as appears to have been the case in New Zealand. The Council recommends a balanced approach to outputs, outcomes and inputs.

7.4.3 Develop an Evaluation Culture

The management of public expenditure should involve a regular cycle of *ex-ante* evaluation, allocation, *ex-post* evaluation and reallocation. Significant success has been achieved in this area with respect to the National Development Plan/Community Support Framework (NDP/CSF) Evaluation Unit, and previously individual Evaluation Units of Government Departments, in evaluating successive National Development Plans. The Council believes that these lessons should be applied with respect to all areas of public expenditure. The Council further believes that more evaluation should be conducted by Departments themselves, and by serving officers within Departments, rather than being contracted out to consultants (although this will be necessary or desirable on occasion). Too much contracting out of evaluation limits the ability of Departments to learn from this experience and to build cumulative expertise over time. The evaluation process should become an integral part of public expenditure management; i.e., the civil service should seek to develop an evaluation culture.

7.4.3.1 Strengthen Expertise in Departments

Developing an evaluation culture will involve strengthening the expertise available to Government Departments to undertake expenditure reviews and evaluations. There is a need to develop the skills of those working in Departments and to give greater weight to these skills at the recruitment stage. Consideration could also be given to the reintroduction of a scheme along the lines of the ‘analyst’ scheme previously run by the Department of Finance (see Chapter 5), building on the Department’s current training initiatives, learning from the lessons and successes of the previous scheme and taking account of the new environmental and organisational challenges and the skills sets of existing and newly-recruited civil servants.

7.4.3.2 Develop an Evaluation Network to Share Experience

In order to enhance the total sum of evaluation expertise within the civil service, it is important that Departments should have an avenue for sharing experience and knowledge of evaluation techniques and approaches. It is recommended, therefore, that an evaluation network should be established to enable those involved in review and evaluation to share experience at both senior and middle management levels. The administrative and servicing arrangements for it are a matter for consideration – the evaluation network can be designed to build on the Department of Finance's newly established expenditure reviewers' network, or set up as a separate entity - but whatever is the chosen model, it is critical that the network be sufficiently well-resourced to ensure it survives on a sustainable basis.

7.4.3.3 Establish a Central Evaluation Unit to Provide Support and Expertise

The development of an evaluation culture would also be enhanced by the establishment of a central evaluation unit, along the lines of the NDP/CSF Evaluation Unit. The Council is also aware of the newly-established unit providing central supports for the expenditure review process within the Public Expenditure Division of the Department of Finance. These supports include training and networking for expenditure reviewers. The function of this unit would be to act as a clearing house for knowledge and skills in the area of evaluation, and to develop common technical standards to be applied across Departments. The unit could also facilitate evaluation itself, in particular on cross-cutting issues, and could advise on the selection of consultants where appropriate. The unit would also be charged with enhancing the evaluation culture within the civil service, and would be involved in the evaluation network.

7.4.3.4 Develop Policy Proofing of Evaluation

Poverty proofing is a new process that was introduced in recent years as part of the National Anti-Poverty Strategy (NAPS). Poverty proofing is defined as:

> the process by which Government Departments, local authorities and State agencies assess policies and programmes at design and review stages in relation to the likely impact that they will have or have had on poverty and inequalities which are likely to lead to poverty, with a view to poverty reduction (Poverty Proofing Guidelines, quoted in Appendix 1 of NESC, 2001).

Poverty proofing is a mandatory requirement for all significant policy proposals that require a Government decision. In addition, other types of proofing have been implemented, including equality proofing, rural proofing and eco-auditing.

It was noted in NESC's review of poverty proofing that public expenditure reviews undertaken by the Department of Social, Community and Family Affairs are being poverty proofed but that reviews completed by other Departments to date have not been poverty proofed. While the relevance of poverty proofing and other types of proofing will vary across policies and programmes, the Council recommends that there should be more widespread application of policy proofing, in particular poverty proofing, in public expenditure reviews and other evaluations.

7.4.3.5 Strengthen ex-ante Evaluation

One aspect of evaluation that receives little attention is *ex-ante* evaluation. This is the examination of the costs and benefits of a programme in advance of a decision being made. The NDP/CSF has resulted in some evaluation of this nature. Policy proofing also involves some examination of policy implications in advance of decisions being made. However, *ex-ante* evaluation is generally underdeveloped in Government Departments. The Council recommends that the *ex-ante* element of the policy cycle should be strengthened.

7.4.3.6 Strengthen Links between Evaluation and Allocation

Programme review is not an end in itself, but should be an integral part of the system of public expenditure management. This means developing mechanisms that will bring the results of evaluations to bear on the Estimates process, and planning evaluations so that they feed into that process. It is important to note that evaluation is not only necessary with respect to new policies, but also should be applied over time and on a regular basis to the ‘stock’ of existing programmes.

7.4.3.7 Include Sunset Clauses in Legislation

One means by which incrementalism can be combated, and evaluation made integral to the policy process, is to include ‘sunset clauses’ in legislation relating to new expenditure programmes. Sunset clauses would require that a proactive decision be taken on the continuation of organisations and expenditure programmes after a specified period. This in turn would prompt full evaluation of a programme before the Oireachtas would be asked to renew it.

7.4.4 Improve Information for Policy Makers

Up-to-date and relevant information is an essential element in all aspects of public expenditure management. While producing and providing information is costly, the resources involved are a small fraction of the amounts that are spent by the public service each year. In order to ensure that these major allocations of national resources produce optimal results, it is necessary to invest in good information.

7.4.4.1 Develop IT to Provide Information

Good information systems are essential to the proper management of expenditure in both public and private sectors. Both the process of evaluation, and the proper functioning of systems of accountability will depend on the availability of information, not just on inputs, but also on what is being achieved through public expenditure programmes. On-going development of, and investment in IT systems, is therefore essential. It is important that the commitment to developing and implementing the new Management Information Framework (MIF) is carried through in a timely way (see Chapter 4).

7.4.4.2 Develop Accounting Systems

Many of the recommendations set out here will depend for their implementation on the availability of relevant, up-to-date, financial information. As was discussed in previous Chapters, there is an on-going process of development in this area within the civil service, including the Department of Transport. The Council believes that this important work should be progressed as rapidly as possible. It should be capable of generating accruals accounts for Government Departments.

7.4.4.3 Invest in Research

In addition to the evaluation of specific expenditure programmes, good decision-making on public expenditure depends on the ability of Departments to undertake more general research on the policy options for achieving various policy objectives. More general research work is required, for example, to look at the context for policy formulation, to provide the basis for evidence-based policy making, to identify processes that policy should seek to influence, or to identify areas not currently being addressed by policy.

The Council reiterates the view expressed in its *Strategy* (1999) report on the importance of scenario identification and planning; i.e., the development of policy relevant scenarios based on expected economic, social and demographic changes in order that the implications for policy be available in time to plan for emerging needs. The work initiated by the Long Term Issues Group in the Department of Finance is welcomed, and should be progressed further. While there are instances of forward looking research and planning in the civil service, this needs to be done more widely and comprehensively.

The relevance of research for public policy follows from the fact that policies are based on explicit or more usually implicit theories of why the particular policy proposed will achieve the desired results (Boyle and Humphreys, 2001). More attention should be paid to the theories and evidence that underpin policy. Significant benefits have accrued to Departments from initiating research projects but Government Departments do not undertake enough research.

7.4.5 Invest In People

As well as investment in information, IT and accounting systems, effective management of public expenditure requires time and high levels of skill and expertise. This means devoting staff time and skills to the full range of management activities, including strategic thinking, evaluation, accountability and information gathering. This requires significant investment, in training staff, in allocating additional staff to expenditure management tasks, and in providing staff time to support senior management in developing their roles with respect to expenditure management. Again, it is important to bear in mind that this investment represents a tiny fraction of the resources that the public sector manages and deploys. Hence, the return on that investment can potentially be significant.

7.4.5.1 Invest in Skills Throughout the Service

The recommendations set out in this Chapter will require high levels of expertise from staff working throughout the civil and public service. On-going investment in education and training will, therefore, be an essential element of effective public expenditure management. The need to develop skills applies to the centre as well as other parts of the public service. If the Department of Finance is to play its role in holding Departments accountable for outputs and outcomes, then it must have the requisite skills. While it is natural that civil servants in line Departments will have a greater knowledge in relation to their particular functional areas (education, health and so on) compared to their counterparts in Finance, the level of expertise of the Department of Finance needs to be strengthened in relation to the different areas of expenditure if the Department of Finance is to support accountability for results rather than mainly monitoring financial compliance. Greater knowledge in the Department of Finance of the different areas of public expenditure would also facilitate improved communication and more trusting relationships with line Departments.

7.4.5.2 Recruit people with Specialist Skills

As well as training existing staff, it is important to recognise that many of the requisite skills will not always be developed 'on-the-job'. This means that public expenditure management skills should be recognised as being important in the recruitment process for civil servants. It also means recruiting people directly into the civil service who have the relevant skills. It is recognised in the PPF that needs can arise for external recruitment at levels other than typical entry level and that the public service must be able to respond to such needs in an efficient and timely way.

7.4.6 Local Government

Local government expenditure represents over 5 per cent of GNP, and local government is responsible for the provision of key infrastructure and services including housing, roads, water supply, planning and environmental protection. There is substantial and on-going reform at local government level, as described in Chapter 6. The changes being introduced seem impressive. There is an emphasis on developing a management system that integrates financial management and resource allocation decisions with performance management at both a strategic and operational level.

7.4.6.1 Follow Through on the Implementation of the Reformed System

The key issue currently for the management of local government expenditure is following through on the effective implementation of the new system. The Department of the Environment and Local Government will continue to have an important role in supporting local authorities through the change process. There is also considerable scope for benefits to be gained from the exchange of ideas and experience between local authorities on the problems and issues encountered in the reformed system.

7.4.6.2 Enhance Co-ordination between Local Authorities and other Public Service Agencies

Some of the services delivered by local authorities have implications beyond the boundaries of individual local authorities. Services that have spillover effects include planning, infrastructure, lake and river catchment policies and waste management. Effective planning and delivery of services of this nature requires co-ordination between authorities. While some co-ordination takes place, the Council recommends that there should be a significantly enhanced level of co-ordination to meet the current challenges. The Government has decided to establish a new regional authority to co-ordinate land use and transport in the Dublin area. This could provide a model for improved co-ordination at regional level.

7.4.6.3 Publish More Information on the Economic Role of Local Authorities

Local Authorities are significant economic entities, but not much information is published in relation to their role in the economy. The Council recommends that more economic information should be published on local authorities.

7.5 CONCLUSION

Over the past decade there has been strong growth of public expenditure but there are still considerable deficits in the quality and provision of social services as well as infrastructural deficits. Addressing these social and infrastructural deficits is critically dependent on the effective management of public expenditure. The recommendations in this report are all designed to contribute to enhanced management of public expenditure.

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