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Some Notes on Performance Management among Agencies

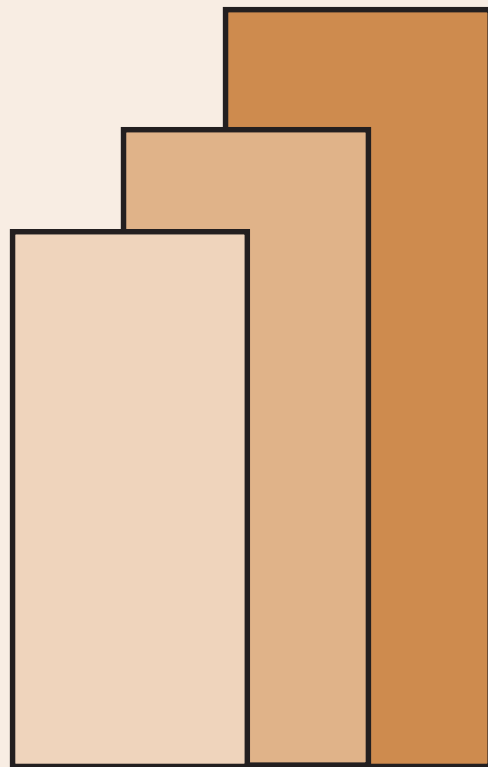
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SOME NOTES ON PERFORMANCE MANAGEMENT AMONG AGENCIES

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Abstract: In the past few years, the government has developed and installed a unique model of performance-based budgeting known as the Organizational Performance Indicator Framework (OPIF). The OPIF demonstrates the relationship between an agency's programs, activities and projects (PAPs), the goods and services produced or delivered (major final outputs or MFOs) and organizational outcomes and goals. This paper argues that in the short-term, the government should first focus on achieving operational efficiency rather than move toward the goal of achieving allocative efficiency. To improve operational efficiency, the government through the Department of Budget and Management should develop an integrated performance management framework that emphasizes performance on two fronts: (a) building the capacity of agencies to manage on a performance basis and (b) ensuring that the environment at the oversight level is performance-orientated.

Key words: performance-based budgeting, organizational performance indicator framework (OPIF), major final outputs, allocative efficiency, line item budgeting, operational efficiency

INTRODUCTION

In the past few years, the government has invested significant time and effort to develop and install a unique model of performance-based budgeting known as the Organizational Performance Indicator Framework (OPIF). The OPIF was introduced by donors to the government in 2000. The Organizational Performance Indicator Framework (OPIF) demonstrates the relationship between an agency's programs, activities and projects (PAPs), the goods and services produced or delivered (major final outputs or MFOs) and organizational outcomes and goals (See Figure 1). OPIF indicates what, why and how government agencies fulfill their mandates, that is, deliver public goods and services. It tells what an agency plans to undertake with the budget given to it during a period of time, e.g., one fiscal year. Properly developed, it is a tool for ensuring the efficient allocation of resources and the effective delivery of goods and services in the public sector.

With the assistance of the Australian Agency for International Development (AusAID), the Department of Budget and Management has developed and has rolled out OPIF logframes and output performance indicators in twenty national government agencies¹. This paper discusses what the national government should do next in order to strengthen performance-based budgeting among the agencies².

In some future time, the government should hopefully shift to output budgeting. However, given the current climate³, it would be a mistake to focus on achieving allocative efficiency by moving to output budgeting in the short term. This will require costing outputs and shifting to output-based appropriation from the current line-item or input-based appropriation. This will be technically difficult to implement because it does not have an appropriate institutional framework at the center and may lack the necessary

¹ These two terms 'department' and 'agency' are used interchangeably in this paper.

² The terms 'performance-based budgeting' and 'performance management' are used interchangeably with 'results-based budgeting/management'.

³ The current climate is characterized by an uncertain political situation, coupled with recent leadership changes in DBM and NEDA, and numerous reform initiatives within DBM that are in competition for the limited time and capacity of few change champions within DBM.

political will and support. Frustration with output budgeting may unfortunately lead to an abandonment of OPIF.⁴

There are concurrent reform initiatives⁵ that also require the attention and effort of the oversight agencies (DBM and NEDA) that have led efforts at establishing OPIF. There is a risk of unduly creating high expectations among those overseeing OPIF implementation and the government departments/agencies affected by the transition⁶. The potential for reform fatigue among the change champions in government, particularly in DBM and NEDA, is real and scarce political capital for reform should be carefully focused on the next important step in developing a performance-based framework among agencies.

There may also be a large risk that the departments/agencies may abandon OPIF or even treat it as a mere compliance exercise if poor output costing practices ensue. The current environment is characterized by a lack of adequate funding with the fiscal deficit becoming a major constraint to the development agenda. The recent experience with re-enacted budgets caused by the failure of legislators to enact the General Appropriations Act has resulted in unfunded agency mandates. Before agencies could be expected to ‘manage for results’ or shift to ‘output- or performance- based budgeting’ they need to have greater certainty with respect to policy and budget. It would be a pity if OPIF were abandoned for these reasons, hence the need to focus on what we see as important intermediate steps toward performance or output-based budgeting.

We submit that the short-term focus should be on improving operational efficiency by creating an environment that both supports and demands improved performance from the departments/agencies. Implicit in this will be the implementation and institutionalization of OPIF. Even without immediately addressing allocative efficiency, OPIF is still a useful tool to contribute to operational efficiency. In the long term, there would be both allocative and operational efficiency in budgeting.

⁴ The only extent to which outputs costing needs to be pursued in the short-term is the link with the evolution of forward estimates.

⁵ Such as Rationalization Plans and MTEF process.

⁶ Particularly in terms of the speed in which some expect the transition to output-based costing to be made.

To improve operational efficiency, the DBM can develop an integrated performance management framework. An integrated performance management framework would mean cascading existing work on logframes and performance indicators, that have been so far constructed, from the departmental or agency level down to the level of individual performance agreements and annual reporting and monitoring of work performance.

Thus, we see the move to performance-based budgeting as a medium to long-term goal. In the short to medium-term, DBM needs to focus on building an environment that emphasizes performance on two fronts: (a) first, building the capacity of agencies to manage on a performance basis and (b) secondly, ensuring that the environment at the center, that is, at the oversight level is performance-orientated. It is obvious that the second front must be pursued in tandem with the first. The oversight agencies, principally DBM should be performance-orientated even as they require the same orientation from the line agencies.

With regard to the first front, DBM should partner with other agencies (that is, the National Economic Development Authority (NEDA); Commission on Audit (COA); and Civil Service Commission (CSC)) to develop an integrated performance management framework that effectively links planning, budgeting and accountability mechanisms. This framework could build upon current pockets of good practice in departments, for example in the Department of Social Welfare and Development (DSWD)⁷. To ensure successful buy-in from agencies, ‘a carrot and stick’ approach should be used to encourage agencies to manage on a performance basis. On the second front, DBM must make it clear what they are offering to agencies with OPIF. If DBM intends to achieve an environment of performance management, it must clearly articulate its intention to devolve responsibility and authority to agencies to make decisions over budgetary inputs and explain how and when this will occur. By clearly stating this intention to devolve controls to agencies, the DBM will thus, create a powerful incentive to agencies to manage on a performance basis. For this to happen, the DBM needs to have confidence that agencies have robust internal management and accountability mechanisms.

⁷ DSWD have already made significant progress in cascading down performance management throughout their agency.

This is the basic principle of the ‘Hurdle Approach’ as first developed in Thailand, which will be explained below. In addition, DBM must move to improve the institutional framework for performance management as a matter of urgency. The greatest limitation to strengthened performance management in agencies is the fact that the current institutional framework (planning and budgeting systems and processes) is not conducive to agencies managing on a performance basis. This requires a major change in DBM’s processes and thinking. DBM will increasingly lose credibility in agencies if it continues to both push forward with OPIF, but maintains a ‘business as usual’ stance of managing and controlling inputs. A cursory evidence of this contradictory behavior is the inconsistency between actively pushing for agencies to develop logical frameworks and performance indicators under OPIF on the one hand, and the continuation of tight cash controls, on the other.

Institutionalizing a performance management framework both at the center and among the line agencies will start build a constituency among agencies who would embrace both performance management and performance-based budgeting⁸. This sequencing will demonstrate the substantial benefits of performance-based management that would lead to operational efficiency both at the centre and among the department/agencies. In addition, it will help build the credibility of DBM amongst the agencies. Once an environment conducive to performance-based management has been created, DBM can then turn its attention to using performance-based budgeting to improve allocative efficiency.

II. SEQUENCING OF FUTURE REFORMS

The following discussion suggests a sequence of activities for future budgetary reform that aims to achieve:

⁸ Performance budgeting exists when the past performance of spending agencies and their statements of future strategy consistent with agency goals or objectives are major criteria over resource allocation decisions. Performance management consists of using performance evaluation feedback to improve the efficiency and effectiveness of expenditure programs.

- a clear and realistic set of reforms given existing constraints;
- strengthened linkages between planning, budgeting and accountability processes;
- greater stability in planning, budgeting and accountability processes, with events and key dates known in advance; and
- institutionalization of the focus on delivery of outputs to achieve government's desired outcomes, rather than inputs and mere compliance.

The centre needs a good understanding of performance-based management concepts. Institutionalizing these concepts in line agencies will encourage operational efficiency.

A performance-based system is not entirely a novel concept in the Philippine bureaucracy. A lot of effort has been put into establishing a performance-based system in the government, e.g., efforts by the Civil Service Commission to introduce and install performance contracts between the agency and its staff. Early initiatives have focused on building an understanding of the core concepts at the center. There is, however, a need to clarify and deepen the understanding of performance management as well as actually apply it among the agencies. It will be very important for the oversight agencies ('the center') to present a united front to the departments and agencies of adopting a 'business unusual' stance in the sense of imposing a performance orientation in the bureaucracy. The next step would be to work with all agencies until they have internalized the performance or result-orientation philosophy. This will take a lengthy period of time given the need to change not only mind sets toward performance management but also behavior. This early we flag the need for a good set of incentives to motivate the change. This sequencing would also allow the government to undertake a number of reforms needed to make this work, in particular the rationalization plan and improvements in reporting systems.

Up until this point, OPIF has primarily been viewed as a tool for performance-based budgeting. The stated objectives of OPIF are to improve allocative efficiency and operational efficiency. Improvements in allocative efficiency are predicated on changes in the method of appropriation, that is, output-based budgeting. Operational efficiency is expected to follow once output-based budgeting has been installed among agencies. For

the reasons outlined throughout this paper, attaining allocative efficiency by changing the budget process, i.e., the method of appropriation should remain a longer-term objective. In the short-medium term, the greatest opportunity for OPIF is to use performance management as a building block for the future goal of allocative efficiency. Real and lasting change occurs when agencies would first institutionalize performance orientation, linking planning, budgeting and accountability processes throughout their organization.

DBM should work with partners to develop an integrated performance management framework and roll this out to National Government Departments

Currently no single agency in government is responsible for performance management. NEDA, CSC, COA and DBM all play different but complementary roles, which may be harnessed in the future into an integrated performance management framework. Some agencies have implemented various aspects of performance management (e.g. individual performance agreements, departmental plans, annual reports, etc), but there is no cohesive, internally consistent or across the board approach mandated from oversight agencies. Herein is an opportunity. A coordinated and integrated approach to performance management will ensure a consistent approach by agencies and strengthen the links of the performance management cycle (planning, budgeting and accountability). Oversight agencies should work together to develop an integrated performance management framework that mandates agencies to deliver on performance management requirements and provides consistent guidance on developing departmental (corporate/strategic) plans, individual performance agreements, and annual reports⁹.

Alongside mandating these requirements, DBM and NEDA should develop an integrated performance management calendar that outlines indicative dates for planning, budgeting and accountability (including reporting) requirements for agencies throughout the year. This would include new requirements such as those listed above, but as well, this may require a review of existing requirements such as the Agency Performance Report, Medium Term Philippine Development Plan, etc., in the light of the objective of establishing a performance orientation among departments/agencies. Not only would this

⁹ This would be phase 1 of the performance management reform.

performance management calendar be a useful reference document for agencies, it may also lead to rationalization of agency reporting requirements and greater stability in planning, budgeting and accountability with key dates known in advance. Oversight agencies should also be encouraged to improve their own knowledge networks and provide opportunities for all departments to gain access to this information and share information about best practice planning and budgeting processes.

In order for performance management to achieve operational efficiency, it is critical that the elements of planning, budgeting and accountability reporting be fully integrated, in terms of nomenclature, consistent set of performance indicators, and alignment with strategic planning concepts.

Alongside developing an integrated performance management framework and mandating these requirements from agencies, oversight agencies must consider an appropriate incentive scheme to avoid a situation where agencies would treat the requirement for performance orientation as ‘just another’ compliance exercise. Three critical steps are suggested: (a) committing to a framework and timetable for devolution of central controls to agencies; (b) changing the rules of the budget preparation and execution processes, and (c) giving public recognition for good performance. These steps will represent a tectonic shift in work attitude and approach in so far as DBM budget analysts are concerned, who have been used to controls and inputs as parameters of the budgeting exercise. However, incentives for oversight agencies can also be in-built into the whole budgeting exercise without requiring changes to the resource allocation process. With further development of the performance management framework, additional incentives would need to be considered

There is a need to strengthen the link between planning, budgeting and accountability mechanisms, three important areas of the performance management cycle. .

While not definitive, the following section outlines some suggested target areas for improvement in planning, budgeting and accountability arrangements suggested in Annex 1.¹⁰ Three areas are targeted because they build on current initiatives already

¹⁰ This sequencing assumes an operational MTEF.

being undertaken in the government, and they can be neatly linked with OPIF, thus improving the link between planning, budgeting and accountability:

i) Departmental Planning

Departmental planning processes help departments identify the relationship between Government societal goals, sectoral goals, organizational outcomes and departmental strategic priorities and outputs. Departmental planning processes should enable departments to set strategic directions and outline the outputs to be delivered in order to prepare their annual Budget submissions.

One stated goal of the MTEF process is to improve the link between planning and budgeting. Agency departmental planning should be aligned with the OPIF submission and both feed into and reflect decisions made in the budget preparation phase.

The first meeting of the DBCC is where the whole-of-government short to medium-term strategic directions and budget priorities are set. This high level planning meeting should consider key Government goals and outcomes as articulated in key documents as the Medium Term Philippine Development Plan (MTPDP), Medium Term Philippine Investment Plan (MTPIP), President's State of the Nation's Address) and should also identify emerging priorities and risks and their impact on the strategic direction and activities of departments but always aware of the available fiscal space as determined by realistic revenue projections of government.

The output of this high level DBCC dialogue is that departments are given directions on the short to medium-term strategic policy priorities of Government, and those initiatives that DBCC may consider in later stages of the budget process.

Departments then begin to develop their OPIF submissions following this initial DBCC meeting. Departmental planning and formulating of outputs should take into account key deliverables, risks, resource requirements and service delivery improvement strategies to guide department managers on what outputs should be delivered in terms of quantity, quality, timeliness and cost. The outcome of this Departmental process is an OPIF submission that is presented to DBM and DBCC following the budget call. The OPIF submissions should draw upon departmental planning regarding the proposed major

final outputs (MFOs) and deliverables for the coming years on a no-policy change basis, that is, on the basis of continuing current funding levels..

Any proposals for new funding that are submitted to DBM (and then on to DBCC) must take into account the strategic decisions made by the DBCC in the first meeting. They should also be expressed in terms of likely improvements to MFOs, organizational outcomes and performance indicators.

Depending on the outcome of the second DBCC meeting, departments may modify their OPIF submissions to take into account the funding decisions made by DBCC at the second budget meeting.

At the completion of the annual planning process¹¹, a department should be able to document the strategic context for its key activities and publish details of these activities in departmental planning documents. Typically this information will include the link between the department's activities and Government societal goals, sectoral goals and MTPDP and MTPIP ; the department's vision and mission statements¹², the external context of the department's operations, short to medium-term departmental priorities and strategies.

Departmental planning might be further developed into specific plans for work groups or attached agencies to assist in implementing departmental strategies.

ii) Individual Performance Agreements & Review

The development of individual performance agreements and an associated review mechanism are critical parts of each department's performance management process. It will ensure that individual plans are consistent with other departmental plans and OPIF logframes.

The cycle of individual performance plans should occur over the fiscal year. Individual performance agreements for the forthcoming twelve months are developed concurrently with a review of past performance at the end of the fiscal year. Typically,

¹¹ The specific timing and nature of departmental planning processes should follow a planning calendar determined by NEDA and DBM. The role of NEDA is to ensure that departmental planning adheres to the overall goals and priorities set forth in the MTPDP.

¹² Articulated through departmental planning processes.

individual performance is reviewed by the appropriate manager or director at points through the year, and annually at the very least.

As with other departmental plans, individual performance plans should identify a direct link between the activities to be undertaken and the outputs, organizational outcomes, societal and sectoral goals articulated in the OPIF logframe. If individuals are responsible for discreet projects, activities or programs (PAPs) or even MFOs in the OPIF logframe then these should be written into individual performance agreements.

As mentioned below, the CSC has already developed a system of performance agreements. At the moment, these agreements are not aligned with OPIF statements and performance indicators or with departmental plans. An opportunity exists to build upon this existing initiative and improve integration with other performance management systems, e.g. OPIF and departmental planning.

iii) Annual Reporting

An annual report is an important accountability mechanism. It informs the President, Congress, other stakeholders and the general public about the performance of an agency in relation to services provided over the year. Typically, the annual report also presents the department's audited financial statements for the previous fiscal year.

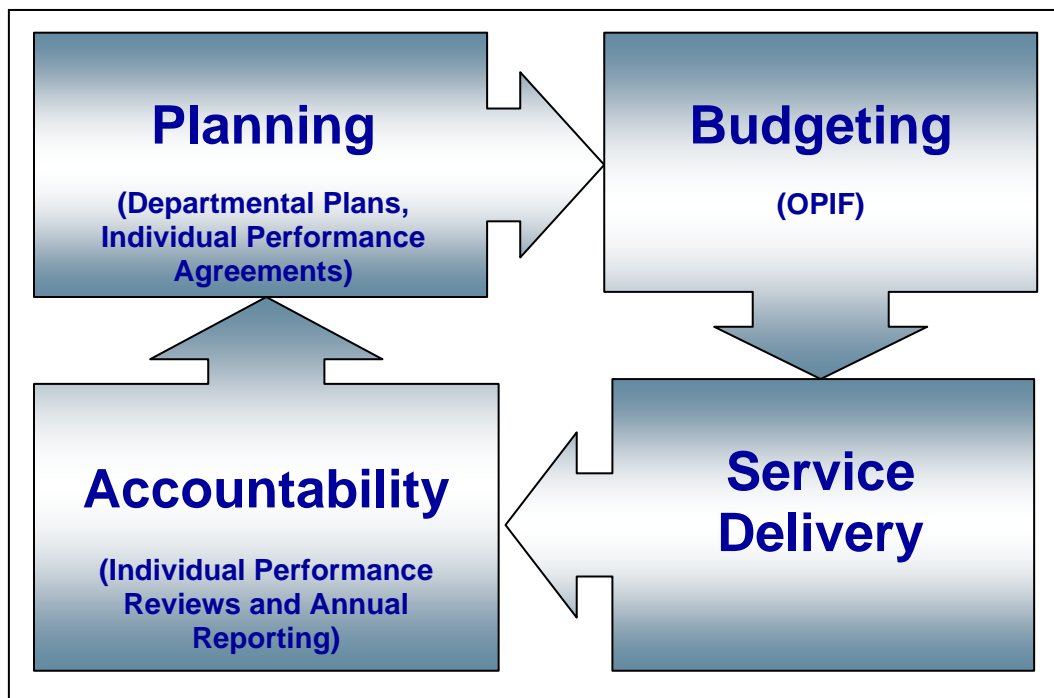
Currently there is no requirement for agencies to present an annual report on agency service delivery or financial management performance. Some agencies will prepare a general report on their accomplishments each year, including policy or program changes that were implemented. However the process of reporting on accomplishments is not rigorous or consistent across departments or agencies and it seems only a few agencies report their financial statements. NEDA does request some information on performance (usually at the outcome level) for the Socioeconomic Report (SER). DBM collects data on physical accomplishments and cash utilization during their Agency Performance Review Process (APR). Oversight agencies should develop guidelines for annual reporting (based on international good practice) and direct all national government agencies to prepare and submit within a specific period of time. This would be an

important step in improving transparency, and would complete the performance management cycle.

Annual reports should be prepared by agencies at the end of each fiscal year with the objective of releasing the annual report approximately 3-4 months after the end of the fiscal year. For consistency, agencies should present their performance for the previous year in terms of OPIF concepts, i.e. MFOs, PAPs, organizational outcomes and performance indicators.

The figure below shows how each of the three target areas suggested fit into the performance management cycle.

Figure 2: How the target areas fit into the Performance Management Cycle



Current good practice in performance management can be the launching pad for an integrated performance management framework.

There are pockets of good practice performance management scattered throughout the Philippine public service. An example is given below to illustrate that the process of

cascading down performance management into agencies is really a matter of building on past successes and tweaking internal procedures (**Box 1**).

Box 1. Civil Service Commission Performance Planning, Performance Monitoring and Performance Review

The CSC developed Performance Management Guidelines for agencies that outline a process for planning, monitoring and review of individual performance agreements.

In signing an annual performance agreement, Division Chiefs agree to be assessed on the attainment of targets and commitments specified in their division work and financial plan. The supervisor (who is also a party to the agreement) commits to provide support, guidance and mentoring in the performance of the Division Chief's functions. The targets and commitments are specified in terms of 'key result areas' and 'major final outputs', but they are not connected to the OPIF process.

Ongoing coaching, monitoring and review are supposed to take place during the year. Each semester, the immediate superior of the signatory to the agreement reports on the officer's accomplishment against targets. This is dependent on a relatively sophisticated ranking system. Agencies are then required to report this information to the CSC.

At the moment, the performance agreement process is limited to senior officers such as heads of departments and division chiefs. Developing an integrated performance management framework presents an opportunity to simplify this process, align the performance indicators in OPIF with the performance indicators in those in performance agreements, and cascade performance agreements to all officers in the organization.

The initiative can start from the center by removing certain dysfunctional practices. DBM should build an environment that is conducive to performance by improving its own internal processes and institutional framework and...

DBM cannot continue to maintain credibility in agencies or achieve any of the benefits of performance management if it continues to maintain a rules-based approach focused on input control. Building an integrated performance management framework should strengthen the internal management practices in agencies and should give DBM the confidence it needs in order to devolve responsibility and authority to agencies to manage inputs. But DBM needs to concede that this will be the end-point of the process, and devolving central controls is necessary to improve operational efficiency. Furthermore, this will provide an incentive for agencies to improve their own internal management processes. However, this is not the only incentive DBM needs to offer agencies. DBM needs to make changes to its budget preparation and execution processes to deliver the policy, process and funding certainty to agencies that is necessary in a performance-based management environment. To start with, reforms must be undertaken to secure more predictable funding and greater policy certainty. This is critical to build the credibility of DBM and progress performance management in agencies. All these changes will constitute a major shift in the mind set of DBM officials and staff and change from the “business as usual” approach of controlling inputs to the “business unusual” practice of providing the agencies greater flexibility and control over resources, including the crafting of incentives to motivate this strategic change in the bureaucracy. A key objective is to make departments and agencies accountable for resources but they will need the flexibility to allocate and use funds entrusted to them based on their promised MFOs and organizational outcomes.

...starting with moving to secure more predictable funding with actual allocations more closely tracking projected expenditures for agencies...

One major criticism of performance-based budgeting in developing countries is that budget financing of spending agencies’ programmes is unpredictable, and funds released may be misapplied, making the pursuit of defined results unrealistic. This is a

risk in the Philippines where cash release is a function of wider budget uncertainty stemming from weak revenue collection efforts and leakages in program and project implementation.

Cash release is subject to an in-year squeeze on discretionary expenditure due to unrealistic revenue estimates, the failure of agencies to demonstrate efficient utilization of funds to warrant release vis-à-vis the APR process¹³, and an ad hoc or opportunistic policy making process at the executive level that sees changes to policy directions that have previously been made during budget planning and execution. Here is where closer coordination among oversight agencies (DBM, NEDA, DOF) of the DBCC will play a critical role. Uncertainty generates a “wait-and-see-attitude” or a “business-as-usual” stance that does tremendous damage to innovative thinking and approaches and creates the inertia of inaction among agencies. A situation such as this will make the objective of instilling a performance management framework among the agencies a mere lip service.

Revenue estimates are prepared by the Department of Finance (DOF), which may be modified by the DBCC into more optimistic revenue targets, leading to unrealistic aggregate and sectoral expenditure targets. When revenue inflows are less than projected or targeted, discretionary expenditure is squeezed, in order to maintain the aggregate fiscal deficit reduction targets. In addition, in-year across-the-board expenditure cuts and tight cash controls are also applied to cope with ad hoc policy making during the year, impacting adversely on agencies’ operations. These problems reside not only with having fiscal deficit reduction targets per se, but with the process of budget management used to achieve the result. The end result is the failure to deliver promised outputs and to achieve desired development outcomes, which would weaken or even jeopardize performance management among agencies.

Specifying a medium-term fiscal objective in a medium-term planning document (such as the MTPDP) is an appropriate and common practice. The problem in government is that fiscal targets are specified annually and monitored on a monthly basis. The monitoring process is concerned only with continuous expenditures adjustment, and

¹³ Some agencies would argue that their inability to fully utilize funds is a function of the fact that they are never certain if the funds they are promised will be delivered in a timely manner and in the amount or size expected.

completely overlooks the quality or efficiency of service delivery. This practice makes cash releases (and consequently funding) to agencies unpredictable. However, the DBM with the oversight agencies has recently adopted a Medium Term Expenditure Framework (MTEF) which will hopefully provide greater predictability of the budget, spending priorities and a better understanding of the revenue stream. This augurs well for performance management among agencies. The continuing reduction in the fiscal deficit (**Table – get Gil’s table**) should give greater certainty over budgets but this will really depend on the ability of the government to increase tax effort.

An important element of MTEF is the Budget Strategy process, which offers a potential solution to this problem by providing a framework for choices and trade-offs between competing priorities at the beginning of each budget cycle. The DBCC should be able to see the impact of the choice between a smaller or larger budget deficit or surplus compared with other national priorities. Understanding trade-offs and providing information about trade-offs should lead to greater flexibility in budget management.¹⁴ The Budget Strategy should also be based on realistic revenue forecasts to prevent disruptive in-year expenditure cuts and to minimize DBM’s tendency to control cash release because of unrealized revenue projections.

The outcome of these changes under a MTEF should be an annual budget that is more responsive to economic cycles, with agencies less subject to the expenditure cuts that currently occur as a result of unrealistic revenue forecasts and tight annual deficit targets.

...this, in turn, requires more predictable policy making.

More predictable policy is important in its own right, but it is also crucial to ensure more predictable funding. The current ad hoc approach to policy making also exacerbates the lack of funding certainty for agencies. Rather than providing firm policy priority signals at the beginning of each budget process, current practice in the Philippines sees continuous ad hoc or opportunistic policy making throughout the budget

¹⁴ For example, running a budget deficit in a year of lower economic growth and a smaller budget deficit or budget surplus in a high growth year.

cycle. This damages the process of budget execution, as unfunded mandates contribute to the lack of predictability in both policy and funding¹⁵.

Unpredictability leads to concerns about efficiency of service delivery and makes monitoring performance difficult. The OPIF submissions should see agencies articulate ‘what they do and why’ though specifying MFOs, organizational outcomes and performance indicators for the forthcoming year. Agency OPIF submissions should then create at least an implicit agreement between the DBM at the centre and departments/agencies about delivering those MFOs and outcomes but ad hoc policy decisions introduces a disturbing wrinkle in the relationship. The DBM should go for more predictable cash release and the national (central) government leadership should desist from unnecessary shifting of priorities, e.g., identifying politically-driven projects mid-way during the budget cycle, that leads to unfunded mandates or derailment of on-going projects. Unless this done, it would be difficult to expect the agencies to keep their side of the agreement under OPIF.

In order for the Budget Strategy and OPIF process to have credibility among the agencies the national government must commit to setting policy directions upfront, rather than during or even after the budget execution process. The Budget Strategy Paper (PBS) can be used to inject a policy and strategic focus into budget formulation, starting from 2007. The PBS should motivate a robust debate on policy priorities and trade-offs at the beginning of the budget cycle and policy decisions that commit the entire government bureaucracy to a sustainable fiscal policy and to a clear set of sectoral priorities. It is important to stress the importance of recognizing trade-offs among a number of projects given the limited fiscal policy space faced by the government. This also signals to agencies that the government is committed to provide greater policy and funding certainty to identified priorities and that the government will also provide the necessary basis for departmental planning (as detailed above). In addition, a shift from controls over inputs to greater flexibility for line agencies would free resources within DBM that may be devoted to monitoring and evaluating agency performance.

¹⁵ Both in terms of programs and projects funded in the budget.

In addition to changes to its institutional framework, DBM need to consider incentives to encourage agencies to their budgets and deliver public service on a performance basis. The first incentive is committing to, and developing a program for the devolution of managerial decision-making...

Performance management is most effective when managers of spending agencies are devolved powers and some flexibility in resource allocation and management. This provides an opportunity to these accountable managers to determine the best way to allocate resources to reduce costs and increase the achievement of organizational outcomes, in short, impact. It is understandable that the traditional practice of rule-based and input control financial management at the center inhibits the devolution of management powers to spending agencies. The DBM then has to recognize that the devolution of management powers is a critical element of a successful performance management and OPIF. However, any devolution of management and decision-making to agencies requires probity and commitment from agencies, which is predicated on verification through regular monitoring and evaluation by the center. The promise of devolution of managerial responsibility to agencies is an important incentive. DBM must clearly communicate this intention to agencies and outline a program and timetable in order to achieve this. One option open to DBM is a variant of ‘hurdle approach’ developed in Thailand (**Box 2**).

Box 2. Thailand’s “Hurdle Approach”

The Bureau of the Budget in Thailand agreed to relinquish detailed centralized controls over line agencies (on an agency-by-agency basis) conditional on their achievement of hurdle standards. This method provides the central budget agency with reassurance that financial discipline exists in agencies. Thailand developed seven financial and performance management competencies¹⁶ needed by a spending agency before external controls over the detail of expenditure can be safely withdrawn. The seven areas of competencies are: budget planning; output costing; procurement management; budget/funds control; financial and performance reporting; asset management; and internal audit.

The hurdle approach in Thailand has been very much about *quid pro quo*s – in particular the central budget agency agreeing to increase flexibility and/or predictability for line agencies that have achieved the hurdle standards. This is a powerful incentive that provides a clear recognition of good performance.

The hurdle approach of easing central controls *following* the strengthening of agency management has two advantages over the more traditional approach of easing controls for all agencies at the same time. Note that the hurdle approach provides flexibility and management responsibility over budgetary allocation to agencies deemed fit to exercise the devolved power. In other words, this is being done in Thailand on a case to case basis. The first advantage is that it minimizes moral hazard in the agencies being given management powers and flexibility – an important feature where corruption is present. There is no guarantee that devolving central controls to poorly managed line agencies will lead to effective or efficient financial management systems, appropriate and transparent use of funds, or encourage them to manage on a performance basis. The second advantage is that the hurdle approach provides an incentive for agencies to improve their internal management practices. By passing the hurdle standards, agencies are rewarded with increased financial autonomy.

¹⁶ One criticism of the Thai approach was that seven hurdle criteria made the model too complex.

Some similarities between Thailand and the Philippines give merit to further examination of the applicability of the hurdle approach. Firstly, just as in Thailand, the Philippine government is highly centralized with DBM having detailed central controls, e.g. cash release. Secondly, just as in DBM, there was a reluctance in Thailand to devolve controls under the traditional approach of performance based budgeting – i.e. central controls are eased for all agencies at the same time, regardless of their management systems and competencies. In contrast, under the hurdle approach, central controls are reduced on an agency by agency basis based on certain transparent criteria. There is no one-time devolution of control but a step by step process that recognizes the relative internal capacities of line agencies to manage and control their respective budgets. Devolution is conditional on individual agencies achieving hurdle standards, thus giving the center more confidence that devolution of controls will lead to more effective and efficient financial management. The gradual approach also enables the center, which has imbibed an ethos and practice of control to adjust from the shock of shifting from a regime of input-based budgeting and controls to a regime that puts premium on management flexibility and accountability.

...the second incentive involves changing the rules of the budget process...

DBM should also consider additional incentives to agencies. By changing the rules of the budget game, DBM could offer incentives in the budget process for agencies that are able to prove they can manage on a performance basis. As in the hurdle approach discussed above, DBM could specify a set of criteria that it wants line agencies to meet. Once the agency has met these criteria, DBM can then offer them more favorable treatment in the budget process. For example, rather than all agencies submitting numerous proposals for new funding, DBM could just invite selected agencies to submit funding proposals. After the first DBCC meeting, agencies that are identified as agencies addressing sectoral priorities should be invited to submit specific funding proposals. But these agencies must prove their ability to manage on a performance basis. For those agencies with a well developed OPIF and have demonstrated they can manage on a performance basis, DBM might offer their strong support to those funding proposals. However, DBM might subject those agencies that are supposed to address a sectoral

priority but have poor internal management practices to close in-year monitoring. The objective is to demonstrate to those agencies that full support may be given once those weak agencies show some degree of achievement in passing the hurdle. The following matrix demonstrates the application of this incentive (**Figure 2**):

Figure 2 – Incentive Matrix to Encourage Institutionalization of OPIF in agencies

	Priority Sector (as identified by the DBCC Meeting)	Non-Priority Sector (not explicitly identified by the DBCC Meeting)
Demonstrated ability to manage on a performance basis (e.g. well developed OPIF logframe)	Agency is invited to submit funding proposals at the early stage of the budget process. These funding proposals are given DBM's strongest support.	Agency is invited to submit funding proposals at the later stage of the budget process. If the funding proposals are not approved by DBCC, DBM may choose to gradually relinquish greater control over resources to the agency.
Concern about the ability to manage on a performance basis (e.g. poorly developed OPIF logframe)	Agency is invited to submit funding proposals at the early stage of the budget process. If approved, DBM will subject the agency to stricter in-year monitoring.	DBM will subject the agency to stricter in-year monitoring, or prioritize the agency for program or agency review.

One other incentive for DBM to explore is changing how cash is released during budget execution. Currently, DBM undertakes an Agency Performance Review (APR) mid year to determine whether or not remaining cash will be released to agencies. The

primary performance measure used is fund utilization. In the long-term it is envisaged that APR should morph into a strategic tool for reviewing agency performance (financial and managerial). In the short-term, while APR is still used as a basis to release cash to agencies, DBM may be able to use it as an incentive to encourage agencies to manage on a performance basis. Currently agencies are requested to submit information on inputs to DBM¹⁷. By changing the data that should be provided by agencies DBM can change the basis on which they release cash. This is not without precedent. DBM recently introduced a requirement that agencies submit an ‘MFO Budget Allocation Matrix’. This matrix provided information on physical performance in terms of ‘Units of Work Measurement’. Taking this one step further, if DBM requests performance information from agencies (more in line with those in OPIF), they can release cash on the basis of outputs, rather than inputs. This is still a form of input control, but in the short-term it can be used as an incentive mechanism for agencies to institutionalize OPIF and may also have the added benefit of building the capacity of DBM to monitor agency performance. In the longer term, the APR should be replaced by a process of agency financial and performance review that will demonstrate the capacity of the agency concerned to manage and control its own budget with accountability.

...and the third series of incentives involves rewarding good performance through public recognition.

As mentioned above, current pockets of good practice provide a basis upon which further improvements can be made. One way to leverage off good practice is to tie into the CSC’s ‘Civil Service Awards for Excellence’ scheme. Additional categories could be created such as ‘Best Departmental Plan’ and ‘Best Annual Report’. These categories would give civil service wide attention to performance management and encourage agencies to strengthen planning and accountability mechanisms.

¹⁷ This includes the following: Statement of Allotment, Obligations and Balances; Quarterly Report of Actual Income; Quarterly Financial Report of Operations; Quarterly Physical Report of Operations; and an MFO budget allocation matrix (showing Units of Work Measurement).

There are other incentives that may also be appropriate, including team-based performance bonuses¹⁸ (a variant of which is applied in the United Kingdom). In the longer-term, consideration should be given to develop career structures within the civil service that rewards individual good performance and that provide civil servants with decent wages¹⁹.

A strengthened performance management framework will also help institutionalize ongoing reforms such as the Budget Strategy Paper (PBS) and Forward Estimates (FEs).

The aim of an integrated performance management framework and PBS and FE initiatives are the same – to improve the link between planning and budgeting. Through the PBS and FE process, agencies and decision makers are encouraged to think on a medium-term basis. In the short-term there are plans to achieve this at the center, focusing on developing capacity to prepare forward estimates within DBM and strengthening the DBCC in developing the PBS. In the medium-term there will need to be a shift towards a more sectoral approach to planning and budgeting. Combined, these short and medium-term initiatives should create both a top-down and bottom-up approach to integrated planning and budgeting.

Strengthening performance management in agencies in the manner outlined in the paper will build capacity in agencies to manage for performance and in turn, support a more sectoral approach to planning and budgeting and institutionalization of the PBS and FEs.

Despite existing pockets of good practice, there is still a relatively low level of capacity within spending agencies, as well as the centre. This is a reason to proceed rather than delay the rollout of an integrated performance management framework.

One common criticism is that spending agencies lack the administrative capacity to set targets, evaluate results and make use of performance assessments in their internal resource allocation and management decisions. Those agencies often cite their lack of

¹⁸ A form of individual performance bonuses already exist in the government although the performance bonus on offer is considered too small to impact on performance.

¹⁹ Current salary levels are too low to enable a civil servant to leave comfortable but modest lives.

capacity in relation to data collection, data verification and the technical analysis involved in making performance assessments. At the center, the capacity of oversight agencies to verify data and monitor agency performance is limited.

There is no doubt of the existence of capacity issues. One reason commonly cited is the inability of those agencies to maintain capable technical and managerial people, who would rather work for the private sector. However, a principal reason behind this lack of capacity is not the lack of resources but the absence of incentives to develop these capacities. In other words, it is a demand side rather than supply side problem.

Appropriate incentives for line agencies to manage on a performance basis will lead to a commitment to improve internal practices. In the future, strengthened capacity among those agencies will develop over time. Similarly, as the center changes its perspective and understanding of its role in public service, it will develop the skills needed to monitor and evaluate performance at the agency level. Lack of capacity is not a reason to delay budgetary reform along the areas discussed in this paper, rather, it is the very reason to push forward. This will mean a particular attitude that success in installing an ethos of performance management among line agencies may be realized in terms of incremental improvements rather than absolutes or one-off efforts.

III. CONCLUSION

Our thesis in this paper is that developing a performance management ethos is an important intermediate step toward an integrated planning, budgeting, performance evaluation and reporting system that strengthens public sector efficiency and effectiveness. Performance management is an important component of an efficient public expenditure management. Such efforts will lead to the achievement of the following:

- enhancing responsiveness of the budget to government's desired outcomes and priorities;
- strengthening management processes;
- improving the quality of service provision; and

- facilitating corporate and individual performance assessment and review.

Recent progress has been made in rolling out OPIF into twenty national government departments. Despite this progress, there are significant challenges facing further implementation and institutionalization of OPIF. The greatest challenge and the one that is the greatest threat to the viability of OPIF is the drive to achieve allocative efficiency vis-à-vis output costing and changes to the appropriation system. In the short-term, this paper submits that it is unrealistic to expect the attainment of allocative efficiency. Instead, the most feasible and realistic way to move forward the installation of OPIF is to first improve operational efficiency through an integrated performance management framework. Building on existing pockets of good practice and capitalizing on the momentum in some agencies that has been generated by the process of developing logical frames and performance indicators, are strong platforms for future reform in expenditure management.

The first phase of developing an integrated performance management framework targets three initiatives with the aim of linking planning, budgeting and accountability elements of the performance management cycles. Oversight agencies should work together to develop consistent guidance and requirements for departmental planning, performance agreements and review, and annual reporting. Oversight agencies should also work together to develop an integrated performance management calendar that lists the key planning, budgeting and reporting dates. The line agencies should build on existing initiatives and ensure that all three elements are consistent with OPIF, both in terms of nomenclature and concept. DBM has to restructure the budget systems and processes to develop an environment that is conducive to performance management and to the improvement in operational efficiency.

The next step in OPIF is an important one. Numerous reforms, while they may be complementary, are nonetheless placing pressure on the capacity and fortitude of change champions within DBM. Lack of political support will make the legislative and political changes needed to change the current appropriation system very difficult in the current climate. By leveraging off existing pockets of good practice in performance management and building on the OPIF momentum, the development of an integrated performance

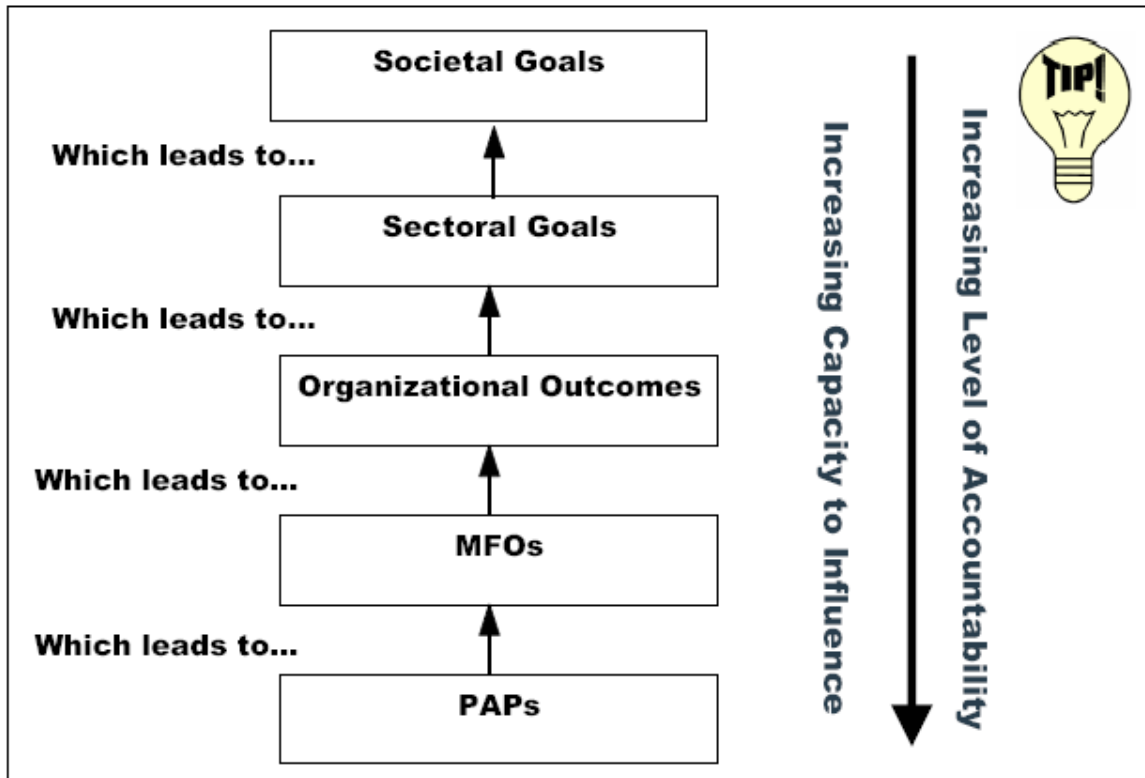
management framework is a lower risk strategy with a greater chance of success and producing tangible change. .

With a performance management framework and results-based management concepts internalized in individual agencies, it is unlikely that performance-budgeting reforms will be abandoned when significant obstacles such as changes to the General Appropriations Act (GAA) and appropriation system are attempted. In fact, an integrated performance management framework (supported by incentives) is likely to build a constituency among line agencies and a demand for further performance-based management reforms at the center.

The center can capitalize on current OPIF momentum and the ever-increasing level of understanding of Public Expenditure Management and results-based management concepts to introduce a performance management framework among the agencies. Developing an integrated performance management framework at the center and cascading this into agencies will achieve the following:

- There will be a clear line of sight between planning and budgeting within agencies (operational efficiency);
- Agencies will be better prepared for the devolution of responsibility and control over resources that will come with a fully operational performance-based budgeting system;
- The center will have more confidence in the ability in agencies to manage on a performance basis;
- The center will have time to strengthen their capacity to monitor and evaluate agency performance – skills required for the change from a regime of rules-based and input controls to a regime of performance-based management;
- An integrated performance management framework paves the way for the consolidation or rationalized of fragmented performance management practices in agencies and other performance management initiatives, such as Rationalization Plans and CSC CESO Performance Agreements; and

Figure 1. Logframe linking goals, outcomes and activities



Annex 1 - Suggested Sequencing for an Integrated Performance Management Framework

