

**FINANCE COMMITTEE****AGENDA****20th Meeting, 2001 (Session 1)****Tuesday 23 October 2001**

The Committee will meet at 10.00 am in Committee Room 1 to consider the following agenda items:

1. **Committee Business:** The Committee will consider whether to take agenda items 2, 5 and 6 in private.
2. **2002/03 Budget Process:** The Committee will consider its lines of questioning for agenda item 3.
3. **2002/03 Budget Process:** The Committee will take evidence on the draft Executive Budget from Scottish Executive officials.
4. **External Research:** The Committee will receive a presentation from Norman Flynn on the external research commissioned by the Committee.
5. **Adviser on the Budget Process:** The Committee will consider a draft specification.
6. **Inquiry into the Application of Consultative Steering Group (CSG) Principles in the Scottish Parliament:** The Committee will consider a draft submission to the Procedures Committee.

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The papers for this meeting are:

Agenda item 2

Paper from Professor Brian Ashcroft, Budget Adviser to the Committee

PRIVATE PAPER
(to follow)

Agenda item 4

Paper by Mr Norman Flynn

FI/01/20/1

Agenda item 5

Draft specification for Standing Adviser on the Budget Process

PRIVATE PAPER

Agenda item 6

Draft submission to the Procedures Committee

PRIVATE PAPER

Towards Outcome Budgeting

Note for Finance Committee 23 October 2001

This note, which is extracted from the bid for the research, sets out the method by which I am conducting the research on outcome budgeting.

Purpose of the project

The budget process has several purposes: planning, control and (in some cases) evaluation. The emphasis among these purposes varies with circumstances. In times of financial stringency the process is designed to find and then control for expenditure cuts in various ways. In times of expansion, the emphasis is more on the planning of expenditure growth in line with priorities. The desire for more control by politicians has led to flirtations with Zero-Based Budgeting to escape from the tyranny of historic expenditure distributions and with Programme budgeting to avoid narrow departmentalism. More recently it has led to the development of budget processes in which the budget process is seen as an exchange between purchasers and providers of services. The desire for better performance and accountability has led to a variety of experiments in output-based, performance-based and outcome-based budgets. The Committee is concerned to ensure that the budgeting process in Scotland is able to take account of political priorities including priorities among service areas and in equalities, is transparent and provides accountability. It wishes to ensure that RAB delivers its promises and that it is enhanced by an outcomes-based approach if possible.

Other governments' experience

Many governments have reformed their budgeting processes so that the decisions made at budget time are more than a technical exercise in financial forecasting. Two objectives have been evident in these reforms: to make the process reflect political priorities and to enable politicians rather than officials to make strategic decisions and exercise control over public spending. New Zealand's experience¹ in budgetary reform is well known especially the division of the budget makers into 'purchasers' and 'providers' and the definition of outputs to be purchased. More recently there have been efforts to go further and include outcomes in budgets. In the United States the Government Performance and Results Act 1993 mandated Federal agencies to produce performance budgets and outcome definitions to be implemented by all agencies by 2000. Similar efforts have been made to reform budget process at state and city level. Less well publicised have been Sweden's efforts to produce output and then outcome based budgets for its Executive Agencies². The UK government is committed to an element of outcome budgeting in the next budget round.

Experience so far has not been as positive as some of the advocates of outcome-based budgeting had hoped but there are valuable lessons for newcomers to the process. One purpose of the proposed research is to distil these lessons but some pointers can be identified now:

¹ Boston J et al, *Public Management: The New Zealand Model*, Oxford UP 1996

² Norman Flynn and Franz Strehl (Eds.) *Public Sector Management In Europe*, Prentice Hall 1996

1. There are problems with high level outcome indicators and their use for control purposes. As Kevin Simpkins, Assistant Auditor General for New Zealand reported: 'those leading the New Zealand reforms recognised that outcomes provide the justification for Government intervention and are ultimately the measure of success. They had significant reservations, however, about the ability to enforce accountability of chief executives in outcome terms. Their reasons included problems in measurability, causality, control and timeframes.'³ The higher the level of outcome (such as morbidity rates, educational attainment, environmental quality) the less easy it is to attribute those outcomes to the actions of a specific agency or department over a short time period.
2. The Swedish experience was to divide of the public sector into those 'purchasing' and those 'providing' services with the onus on the 'purchasers' to create both output and outcome measures. There was a skills deficit on the purchaser side which made necessary close working between the two sides to produce credible output measures and useful outcome definitions.⁴
3. There has been a progression in the USA from input-based to output-based to performance based to outcome based budgets. Experience seems to have been that this progression enables staff to learn the skills required and enables decision makers to use the information provided to make informed policy decisions on the incremental parts of budgets.⁵ It is clear, as in the Sweden case, that the process requires the involvement and commitment of those providing services to make the process effective and workable.
4. Several Australian states, including Queensland, South Australia and Victoria have attempted output and outcome-based budgeting and have in practice found the process slower and more difficult than was anticipated. One review suggests that State governments are reluctant to own up to the difficulties and continue to publicise successes.⁶ This should lead us to be cautious of the claims made by enthusiastic proponents.

One aim of the research would be to see to what extent these and other lessons from other governments could be used to enhance the process in Scotland. The method would be an evaluative literature review and use of personal contacts. The review would cover the following topics: reasons for changes in budget processes; alternative approaches to budget making; experiments with outcome budgeting and their results; impact of outcome budgeting on budget decision-making and implementation.

³ K Simpkins, *Budgeting and Accounting Issues –New Zealand*, International Federation of Accountants Public Sector Committee Executive Forum Washington DC, 1998, p.11

⁴ J Blondal, *Budgeting in Sweden*, OECD Working Papers Vol VI, No 47, 1998

⁵ Much of the US experience has been written up. E.g. Julia Melkers, and Katherine G. Willoughby. The State of the States: Performance Based Budgeting in 47 out of 50. *Public Administration Review* 58 (January/February), 1998, 66-73.

⁶ James Guthrie and Tyrone Carlin, *Australian Experiences with Accrual Output Based Budgeting: When theory and practice don't meet*, The Fourth International Research Symposium on Public Management (IRSPM IV) 10-11 April 2000, Erasmus University Rotterdam, The Netherlands

Jurisdictions to be covered and rationale for their inclusion are shown in the table:

USA	Legislation-backed budget reforms to budgeting in a wide range of services.
New Zealand	Pioneers of resource accounting and budgeting, have attempted outcome budgeting and have met problems.
Sweden	Very long experience of separation of policy and implementation. Three year budget cycle based on outputs and some use of outcomes.
Singapore	Performance-based budgeting, rejected outcome budgeting. Effective system of budgetary incentives
England	Commitment to outcome based budgets, early attempts currently being made.
Australia (state level)	5+ years experience of performance budgeting, attempts in some states at budget process based entirely on outcomes.

Work with service providers and budget holders

One of the lessons from the US and Swedish experience is that for outcome-based budgeting to work there has to be involvement and commitment from those engaged in providing services. The ‘market’ model in which service definition including outcomes is left to the purchasing side and transmitted to the providers has mainly failed⁷. The main reason was that there was an imbalance of skills between the two sides of the transaction: the providers had greater knowledge and were therefore able to dominate the process. The same problem arises with the specification of outcomes in outcome based budgets.

Research on the feasibility of robust outcome measures would therefore involve a selection of those providing services. One of the special features of the Scottish governance system is that a large part of the budget is distributed in grants in aid to other organisations, especially in education and health. Managers and workers in those organisations will have to be involved in the process of outcome definition. At the same time, the budget holders in the Executive need to be engaged in the process if they are to be committed to the results.

It is proposed to test the feasibility of outcome definition and measurement by engaging a small sample of those staff in a trial process of outcome definition. Draft definitions of outcomes, derived from experience in other countries, in a range of services would be presented to groups of staff who would then refine and add to those definitions and provide insights into the feasibility of data collection. Outcome definitions would include a statement of the distributional impact (gender, race, and geography) as a standard feature.

⁷ It failed in the NHS in the UK for similar reasons

Outcomes in incremental budget decisions

Experience with both Zero-based budgeting and Programme budgeting is that a lot of unproductive work can go into producing enhanced systems that result in no change to the actual budgets. If the committee accepts the recommendations of Arthur Midwinter's report that 'it is much easier to secure changes to the Executive's budget with the increment of growth than the base budget' (para 10.3) it could target its efforts in this area in a way that produces demonstrable results immediately and create an impetus and support for extension of the approach.

It is anticipated that the work for phase 2 of the project will produce a proposal to introduce outcome-based budgeting gradually for incremental budget changes, alongside the development of the RAB. Over time, as the incremental decisions form an increasingly significant part of the base budget the budget will be gradually transformed into an outcomes-based format. It is proposed to choose a selection of budget areas in which incremental decisions are likely to be made in coming years, define outcome measures and methods of data collection in the light of Stage 1 results and suggest ways in which outcomes can be used in subsequent budget rounds.

There would also be a method and implementation schedule for applying the approach to further service areas in subsequent years.

Norman Flynn
October 2001