



# CENTRAL BUDGET OFFICES AND LINE MINISTRIES

## The Finance Function in Line Ministries

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# Agenda

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1. Finance Function in Line Ministries and the “Modern Finance Model”
2. Lessons Learned for an Effective “Modern Finance Model.”



# Top-Down Budgeting

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- Top-down budgeting is a fundamental shift in the functioning of the budget process and the role of line ministries
  - Information asymmetry
  - “Ownership of actions”
  - Baselines (*incrementalism*)
- Ministerial expenditure ceilings (caps) (envelopes)
  - Varying degrees of flexibility
  - Annual or multi-year time-frame
  - Entitlement / mandatory spending?
- Top-down budgeting is only feasible if line ministries are capable of implementing such a system of expenditure ceilings











# Finance Function in Line Ministries (1)

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- Conventional Model:
  - Central finance function in line ministries is largely technical and administrative in nature
  - Central budget office interacts directly with sectoral program units in line ministries
- “Modern Finance Model”:
  - Strong finance function in line ministries: “*Each Ministry is Its Own Finance Ministry*”
  - Central budget office does not interact with sectoral program units directly (unilaterally)



# Finance Function in Line Ministries (2)

	Conventional Model	Modern Finance Model
Technical Financial Administration		
Fiscal Discipline		
<i>(Re-) Allocation</i>		
Management of resources		



Cumulative Effect



# Fiscal Discipline

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- **Fosters budget discipline:**
  - Within each ministerial expenditure ceiling
  - Monitors budget preparation and implementation in sectoral programs in order to avoid overspending on the current and multi-year ministerial expenditure ceilings.
  - Acts as an “early warning” system to identify potential problems and concerns
- **Any expected over-spending must trigger action:**
  - Discuss necessary policy corrections in each respective sectoral program to prevent overspending
  - Discuss policy changes in *other* sectoral program to compensate (re-allocate) for the overspending within a ministerial total expenditure ceiling
  - Overspending beyond the total ministerial expenditure ceiling
- **Only a strong central finance function in line ministries can take this whole-of-ministry view:**
  - Close interaction with minister



# Reallocation

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- **Stimulate re-allocation within each ministerial expenditure ceiling:**
  - From sectoral programs that are less valued to those that are more valued
  - “Less with less”
- **Creating “fiscal space” for new policy initiatives:**
  - Incrementalism
  - High degree of trust needed vis-à-vis central budget office
- **React rapidly to ensure budget control (discipline):**
  - Ensuring compliance with total ministerial expenditure ceiling
- **Again, only a strong central finance function in line ministries can take this whole-of-ministry view:**
  - Close interaction with minister
  - Role of central budget office is brokering inter-ministerial reallocation and supporting overall political prioritization



# Management of Resources

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- **Enhance effective and efficient management of resources:**
  - Foster good managerial practices among budget holders within line ministries
  - Devolution within line ministries
- **Inform decisions on reallocations:**
  - Information asymmetry





# LESSONS LEARNED FOR AN EFFECTIVE “MODERN FINANCE MODEL”



# Early and Binding Expenditure Ceilings

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- **Establish ministerial ceilings at the start of budget preparations:**
  - Updating previous multi-year expenditure ceilings
  - Reallocations among expenditure ceilings, or addition/reduction in total expenditures
  - May require moving forward the budget calendar
    - If fiscal year = calendar year, then “single decision moment” in May
    - Can be politically difficult: making difficult decisions earlier
- **Ceilings are binding once established:**
  - If they appear to be negotiable, line ministries will focus their attention on increasing their ceiling, rather than complying with the established one



# Design of Expenditure Ceilings

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- **Sub-ceilings for salaries, other operating expenditure, transfers, and capital expenditure**
- **Avoid multiple expenditure ceilings for each minister**
  - The larger the number of expenditure ceilings, the smaller the opening for re-allocation
- **Avoid “ring-fenced” expenditure ceilings for specific programs**
- **Avoid cross-ministerial expenditure ceilings**
  - Follow institutional boundaries for accountability purposes



# “Budget Holders”

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- For the central finance function in line ministries to be effective in its new role, **sectoral units and agencies should be the “budget holders,”** *i.e.* incur commitments and order payments
- It can then perform – and be seen to perform – its role in **a more neutral and objective manner**
- The central finance function serves as an interface with the budget office in budget policy; this does not prevent **devolving technical financial administrative functions to sectoral units**



# Institutionalisation of Programme Evaluation

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- **Fundamental questions beyond outputs and results need to be asked**
  - Why is this programme a task of central government, rather than lower levels of government or the market?
  - What alternative policy instruments could be used to achieve the same programme objectives? What does each different policy instrument cost?
  - What would happen if the entire programme would be abolished?
- **Little incentive for line ministry to be critical if imposed from the outside...**
- **...but can be seen by line ministries as an opportunity to improve policies and for reallocation and funding new initiatives**
- **Role of central budget office is primarily to provide frameworks and general guidance**



# Finance Function within Line Ministries and the Ministry of Finance

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- **Finance Function within Line Ministries**
  - Varies greatly in practice, depending especially on the devolution of technical financial administrative to sectoral units (or shared services agencies)
  - Establishing relations working relations with sectoral programme units
  - Senior position; generally reports directly to the top civil servant in the ministry
  - Enjoys the confidence of Minister
- **Co-ordination with the Ministry of Finance**
  - The finance function can only be effective if it co-operates closely with the central budget office
  - The central budget office must operate via the finance function in line ministries, rather than directly with its sectoral programs.
  - Heads of the finance function often have a professional background in the central budget office.
  - In some cases, the central budget office has ‘veto’ power over appointment
  - Finance directorate serves as interface with the Ministry of Finance in budget policy, but not necessary for its to devolve technical financial administration.



# Conclusion

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- **A major institutional reform**
  - Requires an integrated package of measures
- **Potential initial resistance in the line ministries themselves**
  - What do they gain by this reform?
  - Greater ownership; establishing trust between the finance function in line ministries and the central budget office
  - As budgets become more flexible within an overall ministerial expenditure ceiling, reallocation of resources (fiscal space) to implement new policies is a key benefit



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