

CENTRAL BUDGET OFFICES AND LINE MINISTRIESThe Finance Function in Line Ministries

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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

- 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)

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		
(Re-) Allocation		
Management of resources		





Fosters budget discipline:

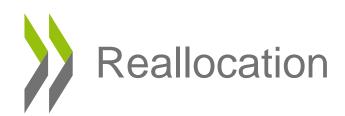
- Within each ministerial expenditure ceiling
- Monitors budget preparation and implementation in sectoral programs in order to avoid overspending on the current and multi-year ministerial expenditure ceilings.
- Acts as an "early warning" system to identify potential problems and concerns

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



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

- 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

• 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

- 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 reallocation
- Avoid "ring-fenced" expenditure ceilings for specific programs
- Avoid cross-ministerial expenditure ceilings
 - Follow institutional boundaries for accountability purposes



- 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

- 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

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.



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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