

# Formulation of Performance Based Budgets

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## Performance-Based Budgeting, a Short History

### Background:

For years, many public sector leaders, media organizations and academics have promoted incorporating performance management information as part of the annual budget approval process. This would help focus the budget on results and outcomes vs. a simple comparison of budgeted to actual expenditures. If accomplished correctly, it would change the entire process and mindset around how the public sector allocates resources and evaluates programs. The two processes have the same purpose – allocate limited public financial resources to serve the citizens. However, the foci of different methods are distinct.

Traditional budgeting processes are incremental – they consider what was budgeted last year and how should it change. Many organizations adopted a current services approach. That approach asks: What will it cost in the new year to provide the same level of service provided the previous year?

Performance-Based Budgeting(PBB)\* focuses on outcomes. This approach asks: How can I maximize the effectiveness of public resources to produce the best outcomes?

The table below illustrates key differences:

	Traditional Budgeting	Performance-Based Budgeting
<b>Budget Focus</b>	Cost of services	Value and effective outcomes
<b>Organized by</b>	Departments, Object Codes	Services, programs, populations served and outcomes
<b>Encourages</b>	Low risk, limited innovation	New ideas, innovation, cooperation and improvement
<b>Motivation</b>	Maintain status quo	Improve effectiveness of government services
<b>Inputs</b>	Prior year financial and personnel information	Performance measures and analysis
<b>Outputs</b>	Budgets and Spending Plans	Budgets tied to program performance goals

(Adapted from a Government Finance Officers Association Publication – Budgeting for Outcomes)

## Changing Landscape

There is a long history of attempts to move away from traditional budgeting processes to one that focuses on results, not just expenditures. Planning, Programming, Budgeting Systems or PPBS goes back to the mid 1960's when it started to be used in the Federal government. Later years saw the rise of Performance Management



systems based on Key Performance Indicators or KPI's. KPI's and performance metrics formed the basis of "PerformanceStat," "CityStat," or "CompStat" applications created across the country.

While Performance Management was widely adopted, it was rare that it was closely tied to the budgeting process. Many jurisdictions have initiated programs that focus on establishing strategies and performance indicators to measure activity. However, very few have truly married performance information to the process of allocating and monitoring resources.

There are several reasons why the two processes have resisted being closely coupled:

- PBB requires a total change in the mindset of all participants including managers, legislatures and even citizens.
- Focusing on outcomes often involves crossing department lines to develop and fund programs to achieve results.
- There was a lack of standard methodologies and technology tools to support the effort.

In recent years, this initiative has been raised to a higher level of urgency. Driven by tight resources, public transparency and private sector influence, more governments are exploring PBB. In 2010 the National Performance Management Advisory Commission issue a report entitled, "A Performance Management Framework for State and Local Government." The report urges governments to move from measurement and reporting to management and improvement.

GFOA, GASB, NASBO and other professional organizations have been placing a much greater emphasis on PBB. There is also a steep rise in Requests for Proposals for budgeting software including requirements for linking performance information with line item budgeting information. In July 2014, the National Association of State Budget Officers released a report entitled, "Investing in Results – Using Performance Data to Inform State Budgeting."<sup>1</sup>

The use of the term "Inform" illustrates a key point. PBB does not have to be an elaborate system that automatically makes decisions. But performance data used during the process to influence and guide budget decisions is a technique that can be used by all jurisdictions.

In summary, we believe that PBB has become a driving force toward changing the way governments will budget in the future. Governments can benefit from the fact that PBB can now be implemented with supporting technology.<sup>2</sup>

<sup>1</sup> <http://www.nasbo.org/sites/default/files/pdf/NASBO%20Investing%20in%20Results.pdf>

<sup>2</sup> Various terms for PBB are often used interchangeably such as Budgeting for Outcomes, Priority Based Budgeting or Managing for Results. This document uses PBB to address all.

## Budget Formulation

PBB involves two major activities – (1) establishing strategies, performance targets (outcomes) for public sector organizations, and (2) assigning costs to outcomes and using that information during the budgeting process. In many jurisdictions, the first activity is done quite well. However, that information is not used or only tangentially used during budget deliberations.

What is needed is a solution that combines performance information with traditional line item information that can be used during budget deliberations. The goal is a system that allocates public resources in a way that maximizes the desired outcomes. This is in contrast to what most governments are currently doing, e.g., incremental increases over a line item-focused base budget.

There are no doubt significant organizational issues to implementing PBB. It represents a significant change to traditional practices and requires a high level of executive and legislative support. It also incurs an administrative burden that can be an impediment to implementation. Offering technology to ease that burden is where Oracle comes in.

There are essentially three elements to a full PBB solution. Only two elements, Performance Management and Planning Budgeting are typically viewed as being necessary. However, a third element, Cost Analysis, can provide a valuable tool toward reviewing costs and ensuring they are valid.

The chart below describes the elements:

<b>Performance Scorecard</b>	<b>Budgeting and Planning</b>	<b>Cost Analysis</b>
Focus – Strategic	Focus – Strategic and Operational	Focus - Operational
Strategic Goals – Key Performance Indicators	Decision-based budgeting Using KPI's and cost elements	Cost analysis for operational Planning and fee analysis
Forward-Looking	Forward-looking/Situational	Situational

Oracle Enterprise Performance Applications (EPM) offer all three PBB solution elements.

Elements of the Oracle application solution include:

- Oracle Strategy and Scorecard Management – Performance Scorecard is the vehicle that allows users to establish and track strategies and performance measures.
- Oracle Public Sector Planning and Budgeting – This application tracks detailed budget and expense information and allows users to create and finalized detailed budgets.
- Oracle Cost Management – Cost management allows organizations to gather cost information from multiple sources and create models for cost analysis. This information can then be used during the PBB process.

The three applications work well separately. But a complete solution uses performance and cost information during the budget development process done in Public Sector Budgeting and Planning.

Examples of the key elements are illustrated below:

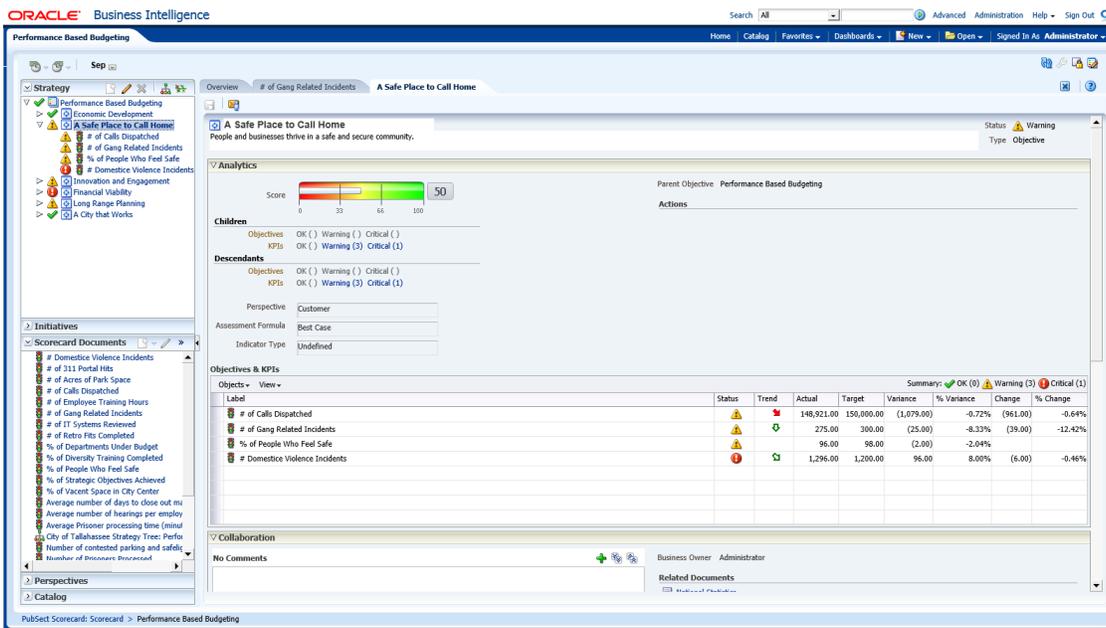


Figure 1: Developing Strategy and KPI's

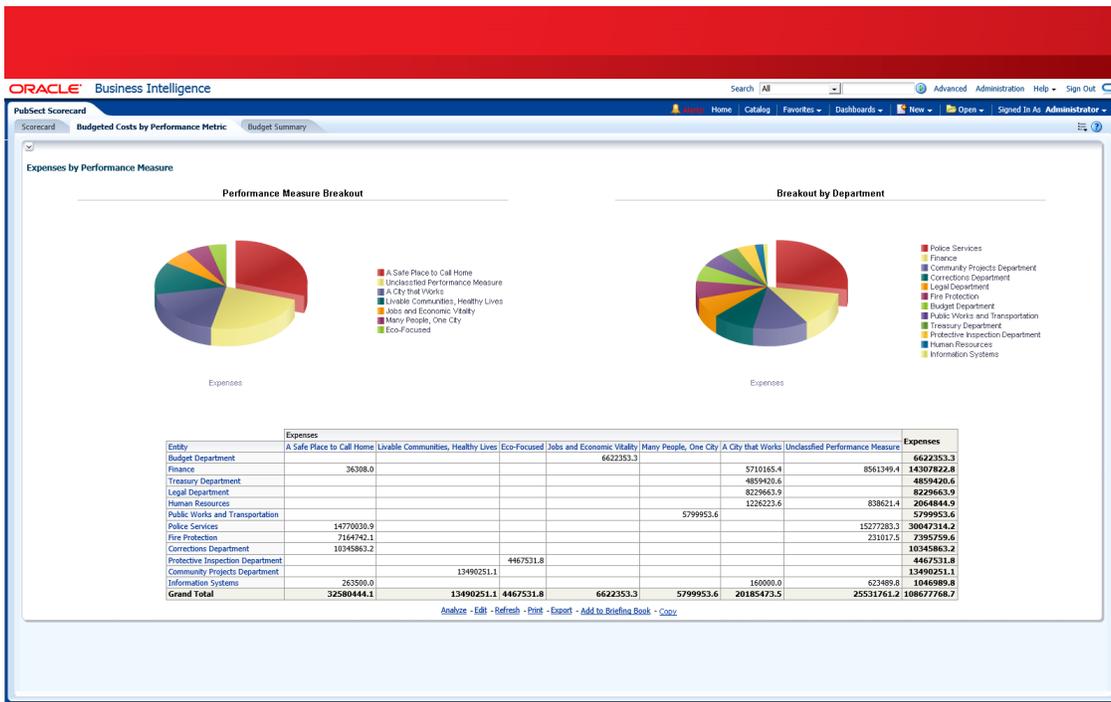


Figure 2: Budgeting by Performance Metrics

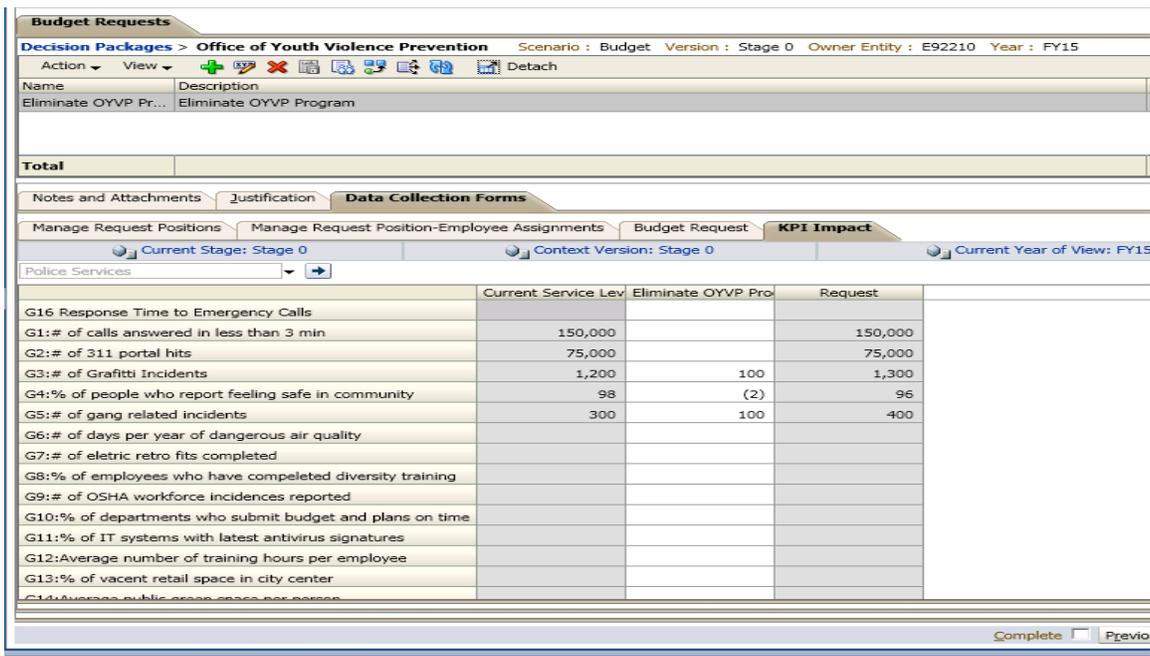


Figure 3: Using Performance Metrics in Decision Packages



## Customer Examples

More and more public sector organizations are using these tools for PBB.

### **State of Oklahoma**

To better allocate and manage its scarce resources, Oklahoma officials plan to use the Oracle Hyperion suite of applications to enable a shift from a traditional “incremental” planning and budgeting approach, based on incremental changes to the previous year’s budget, to a Performance-Informed budget process. This new process is based upon the State developing statewide goals and programs which identify key strategic priorities. Funding decisions will then be informed by strategic priorities and State resources allocated based upon performance information. Subsequently, success will be measured on key financial and non-financial performance indicators.

For Oklahoma, the move from traditional incremental budgeting to Performance- Informed Budgeting represents a major shift in both policy and process, upon which all future Planning and Fund Allocation will be based. For Oracle, Oklahoma is the first statewide implementation to use the full suite of Hyperion products across all departments and agencies, including Public Sector Planning and Budgeting, Hyperion Financial Close Suite and Oracle Scorecard and Strategy Management.

### **Pinellas County, Fla.**

Pinellas County is home to almost one million people on the west coast of Florida. The County has long employed a performance management system to help manage department effectiveness. The system sets performance targets and maps them to the county’s strategies to serve its citizens. But the system was not closely tied to the budget formulation process. It was also primarily manually limiting the speed with which data in the system could be updated.

The county’s goal was to develop a true Performance-Based Budget and Management system that would tie performance information to measurement metrics and link them with the budgeting process. Recently, the County undertook a project to prototype the new integrated PBB process using the Department of Environment and Infrastructure.

The prototype outlined performance metrics and tied them to detailed cost factors. The goal is to use the performance targets, metrics and cost information to examine the impact of changes in service levels during the budget process. The prototype was successful and Pinellas County is the process of implementing the program county-wide. The system will be used during budget deliberations and throughout the year to manage performance.

The county is using Oracle’s Hyperion Public Sector Planning and Budgeting application combined with Oracle’s Scorecard and Strategy Management product. To increase the budget transparency Pinellas officials are also using Oracle Business Intelligence tools to present performance information on a simplified dashboard for citizen use.



## Summary

An increasing number of jurisdictions are moving toward using performance information during their budget preparation and planning processes. Two factors are enabling this move. The first is recognition that while difficult, the value of PBB to citizens is undeniable. Second, enabling technology is available to support the processes in a sustainable and cost-effective way. Oracle is proud to be part this effort to make government as efficient and effective as possible.



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