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# *Governmental experiment for the introduction of zero-base budgeting*

*Presentation and criticism of the programme proposal system of 2004, suggestions for moving forward*

**I**n 2004, during the preparation of the budget for the following year, the budget chapter managers<sup>1</sup> were required to submit claims for chapter managed appropriations and other development funds broken down by programmes, and the government decided about the distribution of public funds on the basis of these claims with a view to implement the government's programme, social and development policies, to establish a more cost-efficient state, as well as to curtail absolute and relative squandering. The experiment was unique, since as it is now known such professionally developed techniques were used by the government neither before, nor after that year. This study explores the usefulness and the possible future of this initiative.<sup>2</sup>

In the past years dozens of plans and proposals have been developed in various scientific and other professional workshops<sup>3</sup>, as well as within the government<sup>4</sup> for the possible introduction of task, performance or programme based budgeting in Hungary.<sup>5</sup> International organisations, especially the OECD, have also shown interest in this topic and have made recommendations to the countries of Central and Eastern Europe.<sup>6</sup> These initiatives contain the most diverse professional contents, but despite the major differences they share common ele-

ments such as the need to move away from the classical base approach and institution financing, greater focus on the completed task and performance in budgeting, or on the whole: the modernisation of the system, shaking it up from its “sleeping beauty's dream”. A serious counterpoint to, and at the same time justification for this professional desire was formulated in the general explanation of the act on the legal status and financial management of budgetary organisations<sup>7</sup> at the end of 2008: “For the lack of mandatorily required content and practice, the basic budget and the related documents cannot be considered to contain the annual (real) expectations of the taxpayers towards the budgetary organisations, and cannot be considered to guarantee enforceability and accountability, because they fulfil mere fiscal functions, and only cover and neglect the management of real processes. *Budgetary discussions* that contain such contents, too, and moreover, put the emphasis on such contents, *have become almost non-existent in the past decade.*”

The government's recent attempt, which forms subject of this study, and has entered the professional consciousness<sup>8</sup> under the name *programme proposal*<sup>9</sup> is regarded as a refreshing

exception. In many aspects the procedure was characterised by the specific features of the classical zero-base budgeting method, however only in relation to a small group of central budgetary appropriations (see later). Expenditures under other legal titles did not need to be justified – using the base approach<sup>10</sup> – and the provision of funds for such expenditures was left in the competence of the chapter managers. In the central budget in the case of institutional budgets proposals had to be submitted for increments, the base was acknowledged at the time of the construction of the budget.

This study does not aim to present the theoretical background of zero-base budgeting, or to compare it with other methods and theories aiming at the renewal of budgeting. Finally, this study does not aim to meticulously compare the theoretical premises with the implemented practice. Instead, it presents the causes, objectives and processes of the *applied* budgeting procedure, the roles and activities of those involved in this procedure, the decisions and the end results of the procedure, and eventually formulates a professional evaluation and criticism thereof, while taking into account the tasks aimed at the development of the method. It must be pointed out that the application of the zero-base procedure, i.e. the procedure that questions the task assumption and resource allocation of the former years, is itself *forward-looking and value generating*, and may serve as a good foundation for the elaboration and introduction of a budgeting methodology or procedure that puts a greater emphasis on professional and social preferences than the current procedure.

This study demonstrates no scientific rigour in that it formulates subjective opinions, too, as well as statements that have not been tested scientifically. This is justified by the fact that the more varied approach obtainable in this manner – as the author hopes – gives much

more significant added value than is taken out by subjectivity.

## BACKGROUND

### Governmental decision related to the programme proposal

During the planning of the annual budget for 2005, the implementation of the government's programme, social and development policy, the creation of a more cost-efficient state, as well as the curbing of absolute and relative squandering required the chapter managers to apply for the so called chapter managed appropriations<sup>11</sup> (and later for other funds, as can be seen later) *in the form of proposals, broken down by programmes*. The size and structure of the programmes could be decided by the ministries. Optimum task performance was intended to ensure transparency on the one hand, and the differentiated manageability of claims on the other. The breakdown of the programmes made it possible to evaluate the state's responsibility in the completion of each task. The proposals not only had to present the individual programmes, but they also had to contain *the real prioritisation* thereof.

The *objectives* of the proposal system were as follows.

- For the consideration of budgetary needs abandonment of *base budgeting*, and thereby
  - ensuring the selection of *professionally justified programmes* that yield significant synergic effects and *meet political priorities* on the one hand, and programmes *that cannot be undertaken* in the given circumstances; as well as *relieving the tension* between the accumulated new needs and the possibilities on the other,
  - making it mandatory to prove the social necessity of the programmes, as well as elaborate and *efficient implementation*,

- enforcing the *review* of all chapter managed appropriations and programmes by the ministries,
- *encouragement* of the use of modern budgeting, financing and evaluating techniques in the utilisation of public funds.

■ Ensuring that allocation related issues requiring a political decision *should really be decided at political level*, which can also contribute to the enforcement of government priorities in the construction of the state budget.

The proposal system was an internal government procedure for the selection of programmes to be financed, the objective of which was – as described above – *not* preplanned resource *withdrawal*, but rather *the encouragement of chapter level inspections*, as well as the *submission* of programmes for *consideration at the level of the government* – and not the Ministry of Finance.

During this procedure the *raison d'etre* of not all legal titles or claims was questioned. On the contrary: claims having a *raison d'etre* had to be selected (the attainment of this objective was fostered by the set evaluation priorities and criteria). At the same time the government declared that the *various legal and other norms were not unchangeable* due to the fact that these modifications had to be implemented after the evaluation of the proposals, but before the adoption of the Budget Act.

The proposal forms were contained in the issued planning circular. On the basis of the circular, the proposals had to be submitted for the following claims:

- *objectives fundable from chapter managed appropriations* (including subsidies to the local governments<sup>12</sup>): professional programmes or investment projects,
- enlargement of the *professional capacity* of existing institutions,
- operational budget of potentially *new institutions*,
- additional funding needs of the *Health*

*Insurance Fund* for curative and preventive services and for subsidies to medical devices.

### The role of the competent ministries<sup>13</sup>, the Ministry of Finance and the government in the distribution of public funds

Although theoretical considerations deliberately have a peripheral role in this study, at this point we need to declare that by keeping the public interest in sight, the distribution of funds to be spent in the respective institutional systems and in other ways *cannot be fully trusted to the ministries*.<sup>14</sup> This problem, the details of which are investigated by the sub-disciplines of economics (first of all by those studying community decisions and game theory) is especially topical due to the fact that in the budgeting procedures of the last few years after the determination of the budgets for the ministries, the ministries *were given extremely significant independence* in the allocation of the funds assigned to them. This means that there was no need for “open fights” with the competing ministries for the shrinking funds, however this was of little comfort since all ministries had to distribute diminishing funds – albeit the rate of reduction varied – while the structure of tasks remained practically unchanged.<sup>15</sup>

Competent ministries have a double identity. During the distribution of state funds they act as claimants, while during the distribution of “awarded” funds within the chapter they act as allocators. Their decision-making mechanism – in both roles – is naturally at the mercy of the current interests, power relations, the fights for power, since the ministries are live organisations.

Even the distribution of state funds requires an allocator, an external organisation, the employees and decision-makers of which are

quite unlikely to be biased to certain programmes or ministries, and whose considerations are not likely to be significantly influenced by their own subjective sympathies. Furthermore, the allocator must possess sufficient professional knowledge required for deliberation. In 2004 this role was assigned to the Ministry of Finance.<sup>16</sup>

The Hungarian reality provides an excellent general example for the fact that claimants apply to the allocator for extra budgetary funds not always in full compliance with the public interest and the requirements of professional task performance. Knowing the most general statistical correlations, it can be easily seen even without proof that *at least sometimes*, in a few cases and in relation to small amounts, it should happen that the claimant *proposes the reduction of the amount allocated* for some of its own tasks, or institutions. The reason behind this could be increased efficiency, reduced social demand for the given activity, or the impact of changes in the legal regulations, which circumstances often occur. It can be stated that such a suggestion is never made in the process of budgetary negotiations, and the phenomenon that Csaba László named “hunger for appropriations” holds perfectly true (László, 1994, pages 125–126). The existence of this phenomenon proves that *in the capacity of claimants* the ministries cannot necessarily be considered as the representatives of public interests, wherefore it is likely that *we cannot make this assumption even in their capacity as allocators*, which is supported by the emergence of the problem of claimants (organisations, organisational units, interest groups, “strong” people, etc.), and consequently of allocators and claimants.

Finally: when compiling the budget of a state not only the different needs of a sector must be forced to compete, but also the sectors themselves, or rather all claims of all sectors, which evidently requires the existence of a decision-

making and selection mechanism that stands above the sectors (chapter managers, ministries), the existence of an organisation in charge of the decision-making and selection mechanism, as well as the actual decision-making process and a decision-maker. In a democratic country the latter role must be assumed by the government, while the former one can usually be best fulfilled by the ministry of finance (or by any other organisation responsible for the preparation of the budget and vested with similar rights). At the same time it poses a serious problem here that the members of the government are in fact the claimant ministers and the minister of finance, and it is not realistic to assume that once these person form a body they will immediately undertake a new role. The key to the solution can be the *prime minister himself*, who is not formally linked to any ministry, and is constitutionally the most important member of the government, the first among the non-equals.

## EVALUATION OF THE PROPOSALS

### Evaluation criteria

Coming back to the preparation of the budget for 2004: in order to evaluate the programmes the ministries had to prioritise their own proposals according to a pre-defined system. When drawing up this priority list, the following *determination* (points A to C) and *other priority* (points D to F) categories were established.

**A** Processes to be financed in any case (e.g. provision of normative subsidies, operation of new institutions that come into play as a result of investment projects).

**B** Unamendable legal regulatory conditions.<sup>17</sup>

**C** Commitments burdening year 2005 (in case non-compliance with the private law or

international commitments or final resolutions is impermissible).

**D** Government programmes, other political preferences (government decrees stipulating such programmes or preferences), including:

- Social policy priorities:
  - ♦ promotion of employment, job creation (training related to large investment projects, job creation in small and medium-sized enterprises, contract work, export, job retention, public work and public purpose employment programmes),
  - ♦ subsidisation of low-income families with children, improvement of the condition of disadvantaged groups of the population (people with disabilities, people with low education and income, people living in distressed regions),
  - ♦ facilitation of the situation of career starters and young families (discounts, subsidisation of first-home buyers, etc.).
- Development policy priorities:
  - ♦ ensuring co-financing required for the reception of EU funds,
  - ♦ development of express road network,
  - ♦ increasing performance oriented R & D grants.

**E** Decentralised programme organisation.

**F** Efficient task performance, synergy.

In addition to these priorities, decision-making about allocation was fostered by other material information that could be determined on the basis of the proposal form.<sup>18</sup>

Furthermore, special evaluation/inspection criteria were determined:

- in the case of programmes co-financed by the EU the share of national resources should not be higher than the required minimum,
- programmes the objectives of which are identical with the objectives of programmes co-financed from EU funds should not be approved,

- “parallel” claims (programmes with identical objectives) must be rejected,
- only such programmes should be approved the funding needs of which indicated for the forthcoming years can be satisfied irrespective of the sum indicated in the proposals.

During the procedure the *draft* of the proposal system was supplemented with the following.

■ During the elaboration of the budget bill *guarantee elements* must be incorporated so that

- the budget bill would include precisely the *funds* required for the programmes to be approved by the government,
- chapter managed appropriations approved in the Budget Act could not be used for purposes other than the programmes approved by the government.

■ A *separate budget* shall be ensured for small-scale projects that the ministries find important.

■ The legal and other conditions of task performance, and of the abandonment of the task shall be elaborated.

■ During the evaluation process it should be a basic principle that in the case of supported programmes the *funds to be required in the forthcoming years* should also be ensured by the approval of the budget bill for 2005, and these funds are not necessarily identical with the amount indicated in the proposal. In other words, one must take into account the simple correlation that a not yet determined programme, which can be subjected to consideration, will – if accepted – generate an expenditure determination in the coming years.

### The planned four stages of the evaluation process

① The submitted proposals are examined by the Ministry of Finance, primarily in order to determine

- whether prioritisation by the chapter managers is acceptable (from two aspects: to determine whether the Ministry of Finance is of a different professional opinion, and whether the ministry concerned uses “trickery” to gain advantage<sup>19</sup>),
- whether the amounts required for the individual programmes are justified (whether under- or overplanning can be detected).

After the evaluation of the claims – and after clarifications with the chapter managers – the Ministry of Finance prepares a document for the preparation of further decision-making.

② The *interministerial work groups* review the claims, examine the social, economic, political and legal consequences thereof, classify and – on the basis of the examination – quantify the determinations.

③ The evaluated claims – including determinations and optional programmes, as well as their budgetary impacts – are discussed by *the governmental forums* (Economic Cabinet, Social Policy Cabinet).

④ The *government* discusses the claims modified pursuant to the criteria established during the previous stages. The government decides about the programmes to be supported, the size of subsidies as well as about the required programme modifications (restructuring, reconsideration of programmes developed in detail on the basis of government decisions made during the process, etc.).

### Process of selection of programmes to be funded

After the receipt of the nearly 1,000 proposals (almost 35% of which were new programmes) it immediately became evident that the total of the required subsidies (equalling nearly HUF 2,250 billion together with the claims of the local governments and the social security funds over their preset budgets) significantly exceeds

the available budgetary funds. These latter funds could not be precisely determined since the major figures at the level of the budget proper were being determined at that time, and within this the “proposal budget” was in fact the flexible and adjustable element; its planned amount totalled approximately HUF 700–900 billion.

Due to the substantially excessive claims, the number one task of the staff of the Ministry of Finance was to determine – in cooperation with the ministries and on the basis of information provided by the ministries – *the amount that needed to be ensured in any case*. On the basis of the first negotiations and calculations this amount totalled HUF 1,051 billion, broken down as follows according to the types of determinations.

**A** Processes to be funded in any case

*HUF 489 billion*

**B** Unamendable legal regulatory conditions

*HUF 345 billion*

**C** Commitments that were undertaken in the previous year(s) but will burden the budget of 2005 *HUF 217 billion*

[in case non-compliance is impossible due to international (subcategory C1) or private law (subcategory C2) commitments or final resolutions.<sup>20</sup>]

In addition to the above determinations a list of so called “inevitably necessary” programmes was also drawn up, which included programmes that did not qualify as determinations on the basis of legal title and/or amount, yet required implementation in any case for professional or political reasons. The implementation of such programmes required a total of HUF 189 billion.

This means that together with the determinations a total of HUF 1,240 billion was required from the government's proposal budget, much more than the size of this budget. The total claim for funding, which is nearly three times greater than the available budget,



but not alarming in itself, *in fact implied an extraordinary tension*, since even with the use of additional resources only determinations interpreted in the narrow sense could be supported. Therefore, the task appeared to be the further reduction of the number of determinations, the implementation of measures and regulatory amendments, and on the other hand, the selection of the “inevitably necessary” claims. In the remaining phase of budgeting *practically this double task was implemented*, in part mechanically. Only limited attention was paid to discussions and bargaining about the size, justification and social benefits of the individual claims.

The proposal budget ultimately approved by the planner<sup>21</sup> was developed in the following manner. Determinations related to the individual programmes were put into one of categories A, B, C1, C2 or C3. In the case of category A the planner considered 75% of the set determination as the so called “reduced determination”. This ratio was 65% in category B, and 55% in category C. Without affecting the total amount of chapter managed appropriations, the claimants had the possibility to modify the amounts of the reduced determinations in each programme, i.e. reallocate the approved reduced determination budget among the individual appropriations already in the preparatory phase of the individual programmes and the budget bill. Apart from the reduced determinations programmes belonging to the “inevitably necessary” category were also approved. (An iteration process was carried out in relation to the set of programmes classified as such, and in relation to determining the required funds. During the process this set and the size of the appropriations significantly shrunk.) Obviously, once approved, these sums could not be reallocated by the claimant. The reallocated reduced determination amounts and the “inevitably necessary” sums made up the proposal budget approved by the planner.

Eventually, the iteration process brought the allocated proposal budget close to the level of *the original funding claims for determinations*, and *not to the manoeuvring room* that was initially roughly calculated. The budget figures that appeared in the budget bill included nearly HUF 1,200 billion as appropriations won through a proposal process.<sup>22</sup> (Out of this sum HUF 1,073 billion was determined and approved in the framework of expert level procedure, while the remaining resources were determined and approved as a result of subsequent discussions carried out at ministerial, prime ministerial and government level.)

## EVALUATION OF THE METHOD AND THE PROCEDURE<sup>23</sup>

### Fundamental findings

Before a more detailed evaluation and criticism is made, the most important statements – about which consensus has been reached – can be put down.

■ From the aspect of efficient public fund allocation the application of the method *can altogether be considered as forward-looking*, which can and should be further developed. However, it was debated within the ministry, too, whether the application of this method is adequate if budgeting is first of all about the reduction of resources. In other words it is the deficit rather than the surplus that must be divided. In my opinion it is especially the *zero base that provides a possibility for withdrawal* from state tasks and programmes that lack financing resources, as well from the evaluation of the consequences of reduced funding.

■ *At the same time* it cannot be definitely stated that the concrete application of the method *was altogether useful*. This is in part explained by the fact that no major savings could be achieved with this method, and partly

by the fact that the introduction of the programme based approach could not be enforced.

■ All in all the method got a mixed reception (which was more negative or more positive depending on which side of the process the evaluator was, and how he weighted the advantages and disadvantages he observed).

■ The *public finance system* (required information system, standard definitions, procedures, protocols and adequate legal regulatory environment) and the *public administration apparatus* (professional knowledge, division of work processes between the professional and financial apparatuses, motivation) were not prepared for successful application. It was primarily due to these two factors that the applied method and the concrete procedure suffered from obvious problems and hiatuses:

- the most significant fact is that the key task was not completed: the “usefulness” of the programmes was not really determined, *the need for the programmes of the ministries was not prioritised* (an important reason behind which was that the determined claims appeared as a bottleneck, in other words: no real room for manoeuvring was left for non-determined claims),
- *in the technical sense it did not form a unified system*; disconnected tables that cannot be incorporated in one system were distributed, forwarded, supplemented, summarised, etc., which implied the risk of data loss and distortion, potential misinterpretation and interpretation without context from the beginning,
- it was built on a *scattered and uncontrolled* (but at least uncontrolled) *information base*,
- the interpretation and management of the *definitions*, and consequently the *data contents* were not standard,
- the professional and political *evaluation* of the different programmes was not or not

systemically performed at government level (e.g. in the Cabinets),

- for the lack of a pre-determined system of rules *the method of determining the amounts to be approved and supported* at the ministries and at the individual programmes of the ministries *was not standardised*,
- the programmes and the related appropriated funds *were not managed consistently* during the entire budgeting process (up to the adoption of the Budget Act),
- no *follow-up* was conducted in connection with the programmes after the end of the budgeting process.

It must be considered which is *the right order of priority*: application of the method without the existence of 100% of the conditions (public finance system and public administration apparatus prepared as described above), during the gradual development of such conditions, or the creation of all conditions before the introduction of the method. In my opinion the former way is more favourable, since in the latter case it is feared that real progress will be postponed to the *unforeseeable future*.

### Detailed evaluation

Since the mere attempt of programme based budgeting represents a definite progress compared to the traditional base approach and method, it is reasonable to describe the positive points first. The positive features and relative advantages summarised below did not appear in each programme of each ministry, but were altogether characteristic of the applied method.

■ It helped the Ministry of Finance and the other ministries realise (and it confirmed) that the compilation of the macro-budget(s) is a *fiscal and professional task*, the public finance processes can be managed with the budget breakdown method neither in the short, nor in



the long run. The acceptance and awareness of this method generates a range of tasks.

■ The application of the method provided *the Ministry of Finance and the competent ministries with a significant amount of additional information* about the utilisation of public funds, concrete programmes and appropriations.<sup>24</sup>

■ The completion of the data forms required the formulation and elaboration of such programme parameters – irrespective of future utilisation – (e.g. objective, social impact, output, the indexes thereof, personal and material conditions), which otherwise were not necessarily formulated and elaborated, or were formulated and elaborated not in the budgeting process. The planning of the utilisation of public funds, i.e. budgeting itself became an increasingly conscious process at the level of both the ministries and the Ministry of Finance.<sup>25</sup>

■ The claims *became more transparent*, i.e. the probability of efficient decision-making grew. The real funding requirements of the different tasks and programmes could be more successfully determined.

■ The procedure supported and laid the foundations for a *multi-year outlook*, however there is no doubt that it was not able to considerably fulfil this objective.

■ *No response was received about any extreme budgeting error* that would have occurred due to the application of the method, which definitely supports its *raison d'etre*. (At the same time, outstandingly positive examples were not reported either.)

*The number and range of problems* related to the method and the applied procedure *by far outweigh the positive features*. This can only partially be explained by the fact that the recognition and identification of the problems is more useful (but not more important!) for progress than the identification of the positive experiences. Furthermore, it must be stated that the

applied method and the concrete procedure *implied all those (teething) troubles with which the entire budgeting system has – unfortunately – been struggling ever since*.

■ The gravest, most far-reaching experiences<sup>26</sup> are the following.

▶ *The base approach budgeting was abandoned* neither by the Ministry of Finance, nor by the decision-makers. Most proposals were *not about classical “programmes”*, but contained *budget requirements in the system of the former years*. This is in part understandable, since the “alteration” of the system – if this will be attempted at all – may take years.

Some of the ministries and applicants *did not consider themselves responsible* for the task, they considered it as a mandatory bad thing, the “independent show” of the Ministry of Finance, unnecessary extra work. A smaller part of the ministries and applicants did not understand the objective of the programme proposal, and a significant group of them altogether found the application of the new method unuseful.

▶ In many cases *not even the ministry had information about its own proposal*. This can be attributed to the bitter experience that the ministries manage the system trusted to them *not in the right manner or not to the right extent* (which is assumed to be an important factor in the system of the budget). The proposal was often elaborated by an organisation under control, which significantly hampered further discussions about the merit – even in technical terms.

▶ Apart from other reasons, for the lack of accurate task descriptions known to all players, as well as for the lack of an evaluation and decision preparation process, the *decision-makers did not have the possibility* (energy or time) for the *thorough evaluation of the programmes* (although this was clearly made possible by the method), and they almost exclusively relied on preparations made by experts.

This is a problem for several reasons. On the one hand, the knowledge of experts within the Ministry of Finance about other ministries is limited, and due to the bureaucratic hierarchy they typically carry out instructions (instead of solving problems). On the other hand, as civil servants they cannot represent political priorities.

Therefore, aspects that are not or cannot be considered by experts could articulate only to a very limited extent in decision-making, while aspects that are or can be considered, could be enforced irrespective of the budgeting system, or the principles and results of such system, in the form of the usual bargaining mechanisms.

■ The applied procedure *violated the principles of zero-base budgeting* at several points:

▶ By creating the “inevitably necessary” category the government practically declared that that are programmes that are *more important* than or are equal in importance with accurately deduced *determinations*. This is a serious contradiction, a sort of criticism of the government's work, since especially the most important programmes should be made determined in the form of appropriately elaborated frameworks (legal regulations, calculations, etc.). If a programme is ranked higher than the determined expenditures, it will necessarily lead to a situation – especially in the case of a shortage of funds – that some of the preset determinations will not be financed, which will generate unwanted, but deliberately non-prevented defects in the operation of the public finance system. However, this is a simple arithmetic exercise: consideration of the programmes can be started only if the amount of the determination is smaller than the room for manoeuvring. Otherwise the size of the determination must be modified with appropriate measures.

In 2004, the *determination amounts were curtailed* basically in two ways. To a smaller extent by the careful re-examination, debate and evaluation of the claims, and to a larger extent with

a *differentiated, yet “across-the-board” method*, in which the planner accepted different percentages of the amounts associated with the individual determinations as “new determination amounts”. This was a point at which a merely fiscal, but theoretically unjustifiable mechanical element was incorporated into the professionally sophisticated system.<sup>27</sup>

So what is the issue here? Either the government's apparatus is unable to correctly define the size of the determination, (or the government is unable to encourage it to do so), wherefore the government can *presume* (but cannot *know about*) the overplanned nature thereof (see the section on the claimants' “trickeries”), wherefore it can reduce the accepted rates associated with the legal titles. In this situation the government practically does not know what financial burdens the state must bear year after year, and nor does it know the consequences of the reduction of funds under the different legal titles in relation to the provision of the given tasks.

The other possibility is that the size of the determination is defined more or less well, however in this case by rejecting a significant portion of the determinations the government “programmes” non-compliances with the legal regulations and the unenforceability of the signed contracts.

▶ The applicants also *had the right to modify the amount* of the approved programmes, i.e. *re-distribute* the approved reduced determination budget among the individual programmes, or among the different appropriations in the preparatory phase of the budget bill. This also questions the fact, or at least the level of determination.

■ A significant part of the problems arose from the *insufficient development* and non-observance of the procedure, the shortness of the available time, the lack of the required know-how, in general from the insufficiency of human resources in possession of modern

methodologies, i.e. *from the non-existence of the required boundary conditions*:

▶ By According to the plans, before government level decision-making the working groups (the ministries separately, the Ministry of Justice, the Ministry of Finance) and the different governmental forums (first of all the cabinets) would have discussed the claims. This practically did not happen, programme level discussions and evaluations *were carried out exclusively on bilateral expert level*, between the Ministry of Finance and the ministerial staffs.

▶ Irrespective of the relationship to the proposal system, the quality of form completion, and consequently the evaluability of the data extremely varied. This led to *unintended differentiated treatment*. (Naturally, this factor must be taken into account in the case of any budgeting method.)

▶ The decision-makers typically conducted discussions about the *chapter budgets* that were developed after the expert-level inspection of the programmes (at the same time it was a positive development compared to the practice of the former years that programme-level consideration was also introduced), however *decisions were made not about strictly observable legal titles and budgets*, which would be mandatory in the case of zero-base budgeting.

▶ At the level of decision-making there was *no real transfer among the programmes of the different ministries*.

▶ In part due to the novel nature of the system, the *staff of the Ministry of Finance was also unable to handle the proposals in a standard manner*. This caused problems especially in defining the determination rates, at the approval of the amounts specified by the ministries, and led to unintended differentiated treatment. The possibility to control the data and judge the level of substantiation was not ensured.

▶ Efficiency and social impact (in the positive and negative sense), as well as the measure-

ment and control thereof appeared *as a real selection criterion only to a very limited extent*. However, due to the experimental nature of the programme such an expectation was not and could not be excessive.

▶ The *structure of the proposals* and the *structure of presentation* were not in harmony, wherefore follow-up, checking and feed-back were *a priori* impossible.

■ Other problems and criticisms that were characteristic of the process, or that came to the surface:

▶ In case the ministries detect (possibly on the basis of multi-year experience) that the claim presented as a determination enjoys priority, *they may be interested in undertaking excessive commitments already before the end of the budgeting period*.<sup>28</sup> In the best case scenario legislation and the government are impervious about preventing this, but in many cases the ministries continue this practice on purpose.

▶ There was excessive preliminary expectation (at least at the level of declaration) in that the ministries can and must be “forced” to observe the programmes and amounts approved in the proposal system during finalisation and then during implementation with *legal tools*. It is more reasonable to achieve this objective with governmental *management tools*.

▶ The achievements of the budgeting method *suffered a blow* during the *parliamentary stage* of legislation.

▶ Until the completion of the budgeting process only part of *the commitments* pertaining to the next year are assumed, other commitments emerge only at a later stage. Naturally, some of the “potential commitments” that emerge after the completion of the budgeting process can be prevented, however others cannot (e.g. a public procurement procedure launched in an orderly manner in January often reaches the stage of commitment assumption only in November). Accurate and standard handling in this respect is crucial for

defining the determinations, however no such practice was established.

► Finally: a major cause of most of the above problems was *the shortness of time*<sup>29</sup> available for the completion and evaluation of the proposals, as well as for decision-making.

## SUGGESTIONS FOR FURTHER DEVELOPMENT<sup>30</sup>

The fundamental finding of the study is that although the experiment cannot be considered successful, it showed enough positive signs and results that justifies efforts for further development. It is a crucial, but not yet answerable question whether *in the medium run* the Hungarian budgeting system (including its major players: the competent ministries and the Ministry of Finance, the technical background, and above all, the way of thinking about public funds and the culture of utilising public funds) can be prepared for the *introduction of a new budgeting regime of this type*, or of any other system focusing on the social rate of return? This chapter describes what preparations are inevitable on the basis of the lessons of the experiment.

### Preliminary works

■ *Claims, programmes to be launched or continued, as well as resources* for which proposals must or can be submitted shall be defined as accurately as possible. (I.e. there should be no “grey zone” left in relation to any forint of the budget from the aspect of the applied budgeting method.) It should continue to basically focus on the chapter managed appropriations, but it is worth considering what other group should be involved in the proposal system.

■ Since apart from the fiscal and other boundary conditions the issue of *determina-*

*tions* is of crucial importance, this element of the method requires very precise and careful elaboration:

- defining the *types* of the determinations, and communication thereof to the ministries;
- exact formulation of the *definitions* of the different types of determinations, so that *the determination nature could* be verified, or at least presentable, and the meaning should be unanimous for everyone in each category;
- ensuring the possibility for the *establishment of clear priorities* among the different types of determinations (It is possible that a given claim is considered as a determination under several legal titles. For example, the payment of EU subsidies is most often based on private law contracts. In case the prioritisation of the types of determinations can be ensured, a given claim is treated adequately if ranked as the highest among the existing types of determinations.<sup>31</sup>);
- *separation* or possibility of separation of the *claim related to the programme and the size of the determination therein*; raising awareness of ensuring the presentability of “importance” and “necessity”;
- ensuring the presentability and evaluability of the consequences and tools of cancellation, reduction, postponement, etc.;
- ensuring the exact formulation and documentation of the definition of “commitment assumption”, with special regard to the time of commitment assumption (before or after budgeting);
- specifying the amount of the determination after multiple discussions with the Ministry of Finance.

■ It must be precisely determined *what can be regarded as a programme*. Since this is the basic unit of evaluation, the different level of aggregation (contentual and not financial aggregation) makes comparison impossible.<sup>32</sup>

■ A solution must be found to detect *same-purpose programmes* on the one hand, and *programmes that can be implemented with EU co-financing too* on the other.

■ The *prioritisation of the submitted programmes* cannot be fully trusted to the applicants (the ministries). Instead, the programmes should be submitted according to the predefined categories, and thus the use of “trickeries” can be prevented. In this respect firm government instructions are needed.

■ It can be proposed that *the maximum number of proposals* to be submitted by the ministries *should be determined in advance*. However, this upper limit shall not guarantee the subsequent acceptance of the proposals.<sup>33</sup> This is the application of a so called “double ceiling”, where the first screening should be performed by the claimants themselves, and only the viable proposals should be considered at government level.

■ The *development* – and naturally the thorough and plastic presentation of the consequences – *of the method of withdrawal from the task* must be an accentuated task.

■ For the lack of a standard public finance information system *the IT background of the method must also be developed*: efficient IT support must be provided

- to simplify the data transfer, data recording and data management system;
- to facilitate systemisation, classification and summarisation according to various aspects;
- if possible, the decision-making mechanism should include objective and comparable factors (ones for which algorithms can be written).

■ The *presentation system* of public finances, including that of the central budget must be restructured so that it would ensure adequate identifiability and flexibility. This also creates the possibility for *reporting* according to programmes/tasks.

## Suggestions fostering adequate application

During the evaluation of the programme proposal system detailed suggestions were formulated. In accordance with the critical remarks described above, during the evaluation of the programme proposal system detailed suggestions were given regarding the measures to be taken by the government for successful implementation. It must be emphasised that this is about the improvement of the applied method. The introduction of a programme, performance or task based budgeting system that would affect the entire budgeting process *was not and has not been on the agenda ever since*. The suggestions are important, often perspective, but here it is no longer reasonable to deal with this level of operativity. Based on the most important suggestions the following findings were made.

■ *Fundamental* suggestions:

▶ In case of the excessive rate of claims that appear as determinations funding should not be reduced proportionately (across the board), but rather *omittable determinations should be selected and then the necessary measures should be taken*. Without this the method will lose its theoretical base, since the essence of the determinations is especially that both political and fiscal consideration can be excluded in connection with them, and that if the circumstances remain the same, funding for such purposes must be ensured in any case.

▶ *Motivating and sanctioning* elements must be introduced to prevent the use of “trickeries” by the applicants in order to gain benefits (additional funding). On the contrary: such conduct must have well perceivable professional, financial and political (and possibly personal) risk.

▶ After an agreement and decision are made about the determinations within each programme, the ministries *shall not be allowed to reallocate the budget so established*. On the con-

trary: separate guarantee elements must be enforced in the conciliatory process so that the approved amounts be included in the budget bill. (Deviation shall only be permitted for especially important reasons, in cases approved by the government.)

▶ A *follow-up* method and system must be developed for the *programmes*. Actual performance (both professional and financial) must be compared with the planned performance. Feedback information (on the concrete programmes, the adequacy of budgeting at the individual ministries, as well as on the programme proposal budgeting system) must be utilised in the next budgeting period.

▶ It must be ensured, at least on the procedural side, that *the boundary* between the approved and rejected programmes and claims at the individual ministries should be drawn *in a standard manner*. This boundary must be drawn at claims having the same margin of profitability at each ministry.<sup>34</sup>

■ Suggestions related to *the nature of the procedure*:

▶ *Sufficient time must be provided for completion* for two reasons: to improve the quality of elaboratedness, to prevent the generation of legal title on the basis of inaccurate, incomplete or inadequate (for other reasons) form completion. Time is needed for preparation and decision-making within the chapter, it must be ensured for the applicant ministry and the institution working out the proposal to cooperate.

▶ *Sufficient time must be provided for the evaluation of the proposals and for decision-making*.

▶ The ministries must agree in advance on which ministry will apply for which programme (this is an important task in the case of programmes co-financed by the EU). The Ministry of Finance must provide assistance in *detecting overlaps and inconsistencies*.

▶ It must be determined whether a programme has revenue and expenditure connec-

tions in more than one ministry, and the *standard treatment* thereof must be ensured. (For example, it should not happen that one “leg” appears as an important determination, while the other is ranked as a subordinated programme.)

■ *Further practical conditions* of appropriate application:

▶ It must be achieved that all ministries should be able to *produce proposals of the same quality*. The allocation of public funds shall not depend on the fact that an apparatus is more prepared for this task than the other. The low level of preparedness of ministry employees shall not lead to the inadequate selection of public tasks or to the provision of inadequate funding.

The *applicants must be better prepared* in another sense, too: communication of the objectives and the procedure in due time, request for opinions, etc. Identification with the method – to a certain extent – and the reduction of aversion is also an objective. This significantly affects the success of the method.

▶ The procedure used for the evaluation of the proposals and for decision-making *shall be determined in advance*, including the exact tasks of the entities involved (this is of special importance in the case of the Ministry of Finance and the different government forums).

Although the exact course and manner of the evaluation of the proposals had been developed, the actual process was adjusted to it only partially. A problem may arise in case this deviation is not the result of a deliberate political/upper managerial decision, but that of external factors which are irrelevant from this aspect.<sup>35</sup> Therefore a greater emphasis must be put on reaching a *preliminary agreement* on and continuous *compliance* with the process of evaluation (by allowing deviation only upon government level approval).

▶ The ministries must have such a profound knowledge of all of their proposals that would allow them to conduct negotiations about them.



▶ *Firm governmental support must be ensured to the Ministry of Finance* professionally and politically alike. The competence of the Ministry of Finance cannot be questioned in relation to the coordination of budgeting, in relation to its right to access (or rather to submit to the government) the budgeting requirements derived from the fiscal framework conditions. *This does not mean the delegation of issues requiring government level decision to the Ministry of Finance*, which can trigger the ministries' repugnance threatening all-governmental interests, "empoisoning" budgeting, usually without real foundations.

However, the apparatus of the Ministry of Finance must be left on the "objective" budgeting side (by terminating its bondage to the ministries) and by ensuring responsibility and accountability.

▶ Finally: there are serious requirements against the entire government: the government must be *committed* and *must demonstrate commitment*. "Tricky" proposals should carry perceptible professional, financial and political risks at the ministries. The proposals must be brought to the level of *referrable* budgeting documents. It must be achieved that *the professional and financial apparatuses of the ministries should really cooperate* both in the preparatory and the conciliatory phase.

### Conditions to be created in the longer perspective

In relation to certain programmes and appropriations the successful application of programme based budgeting requires that all those changes be made in the long run that usually emerge in relation to a "public finance reform", and the *resolution of which was and has been attempted in the past years*, sometimes unquestionably successfully. Therefore, here it is not worth going into details about this. The neces-

sary conditions include but are not limited to the following (the list does not reflect the optimum prioritisation of implementation):

- *general review and reconsideration of the tasks and roles of the state*, because a strategic way of thinking and budgeting cannot be substituted with any annual budgeting technique;<sup>36</sup>
- elaboration of *sectoral strategic programmes*, in harmony with medium term (3 to 5 years) outlooks the major figures of which pertain to a longer period (e.g. 10 years), in harmony with the macroeconomic path to be followed, as well as with the current national development plan;
- development of a *public finance information and monitoring system* that can handle professional, financial and financial management contents in a usable manner;<sup>37</sup>
- *development of a legal regulatory environment*, which would foster or "force out" the standard use of terms, as well as the enforcement of the principle of efficiency and performance;<sup>38</sup>
- in order to ensure the *mobilisation* of professional programmes, they must be planned and financed independently from the operation of institutions;
- *controllability* of data provided by the ministries, in the longer run *auditing* of the provided data.<sup>39</sup> This is important especially in establishing the actual rate of determination;
- ministerial apparatuses having appropriate professional, budgetary and economic knowledge, as well as the ability to apply such knowledge.<sup>40</sup>

### CONCLUSION

As a conclusion of the article I attempt to answer a simple question: what can be the cause behind the fact that despite the success of the

experiment – albeit limited – the government still refrains from using this budgeting method?

Before answering this question I find that two topics are worth being highlighted. On the one hand it must be mentioned that at the end of 2006 the government decided on a programme with impressive objectives, i.e. the general review of public tasks.<sup>41</sup> In parallel with the “assumption of excessive tasks by the state” the citizens are – in general justifiably – dissatisfied with the offered services and the functioning of the state. This makes it evident that in addition to reducing the size of the organisation, further reform steps are urgently needed to improve operational efficiency and for the significant enhancement of the prioritisation of the assumed tasks. The review of public tasks intends to serve this latter issue, on the basis of which we intend to achieve that the state should undertake fewer but better services and tasks.” (The review of public tasks 2007, page 3) This means that the government has openly and directly undertaken to start off with a “clean slate” and the *raison d’être*, the optimum manner of performance and the size of all tasks assumed by the state (and by the local governments) should be inspected, and should eventually be reduced and adjusted to the citizens’ preferences and the load-bearing capacity of the country. Today we can already see that this latter objective has not been attained, the tasks of the state and the local governments have not decreased in number, and nor have they been substantively prioritised. It is not my intention to address the underlying causes, in fact they can be the topic of an independent study.

Secondly: it must be pointed out that although the programme proposal initiative was welcome and promising, *it is far from meeting the requirements of classical zero-base budgeting*. Many people share the opinion according to which “with some simplification, the objective of the experiment was to investigate the

well-foundedness of chapter managed appropriations, and to reduce or terminate the funding of programmes that have been found unsubstantiated” (Sebők, 2007a, page 25). The *raison d’être* and forward-looking nature of the initiative is not questioned, wherefore it is not justified to cancel any advancement or steps in other directions.

Exploring the causes behind the question asked it seems that one of the most important causes is – contrary to common belief – not only 2006 which is a watershed year in many aspects, or the general crisis that erupted in 2008, but rather the decreasing room for budget manoeuvring – witnessed for years – in the sense that the amount of non-allocated expenditures that can be spent “freely” is practically zero if not negative. As it was said before, negotiations in 2004 were held practically about the “distribution of the deficit” rather than about the distribution of the surplus. Since then the situation has become even worse. Under such circumstances the government and the minister of finance presumably do not find the shift justified and timely.

Another important cause is that the method would require the state (more precisely the Parliament, the government and the ministries responsible for task performance) to back out from tasks related to the “rejected” claims. The example of the review of public tasks demonstrates that in today’s Hungary decision-makers find it professionally and/or politically impossible to undertake, and therefore they fail to take this step even if this would be in the public interest, and despite the fact that maintaining the task may cause serious financial disturbances.

We must not forget about the fact that in addition to the Status Act, at the end of 2008 the National Assembly adopted another act that affects the foundations of the Hungarian budgetary and public finance system, about cost-efficient financial management by the state and about fiscal responsibility. On the

basis of this act in a few years' time it will be unavoidable for the ministries to create the necessary conditions outlined in the article (conditions that will basically create the possibility to harmonise public task performance with the necessary budgetary resources). This will be the only way to determine and meet the objective of maintaining the primary balance.

Finally, it must be acknowledged that in mid 2009 *Elemér Hankiss* had all the right to write that “the lack of competence in Hungary is unbelievable both in politics and public admin-

istration” (Hankiss, 2009). In the field of human resources significant, seemingly almost impossible development is needed to create at least the basic conditions for the expansion of the use of the modern budgeting techniques. This means that the enhancement of the efficiency of the state apparatus requires us not to maintain performance, or the output by using the continuously decreasing capacity and input, but rather to increase the output, and eventually the outcome, i.e. social benefit by using an input almost identical with the current one.

## NOTES

<sup>1</sup> Officially: chapter managing organisations the detailed list of which can be found in the definitions of Government Decree 217/1998 (XII. 30.) on the rules of operation of public finances. In the following, for the sake of simplicity, I often use the term ministry.

<sup>2</sup> The article exclusively reflects my personal views which are not necessarily identical with the official position of the Ministry of Finance or other government agencies.

<sup>3</sup> An important basis for the preparation of the study was the internal evaluation carried out with the involvement of the staff members of the affected Finance Ministry departments a few months after the conduct of the program proposal system. Furthermore, I am indebted to Zsolt Aradi, László Balogh, Péter Banai, Balázs Romhányi and Zsolt Tavaszi, who contributed to this article with many valuable thoughts and suggestions.

<sup>4</sup> See for example Sebők (2007a, 2007b)

<sup>5</sup> See for example New budgeting system (draft) (2006)

<sup>6</sup> A good overview of this is given by the thematic publications of the State Audit Office, e.g. SAO (2007)

<sup>7</sup> See for example OECD (2007), Hemming et al. (2007)

<sup>8</sup> Act CV of 2008 on the legal status and financial management of budgetary organisations, known as the “Status Act” or “Legal Status Act” in the professional jargon, which is misleading content-wise.

<sup>9</sup> The name of the procedure speaks for itself: the ministries had to submit proposals for state subsidies, and they could participate in this procedure with governmental and sectoral programs.

<sup>10</sup> According to Miklós Sebők, the proposal system of 2004 was by far the most outstanding from among the larger-scale attempts affecting all ministries (Sebők, 2007a, page 19).

<sup>11</sup> It must be noted here that the use of the base approach in budgeting is not an a priori bad or less valuable method than zero-based budgeting, since it starts out of the often fully relevant assumption that public task performance in the plan-year and the required resources show discrepancies from the subject year only at well-definable points, wherefore it is economically and professionally justified to consider the discrepancies only, and that these discrepancies should serve as a basis for budget bargaining and consideration by the allocators. This is especially true if the state/local government performs public tasks through maintaining institutions. It is another issue that even in this case from time to time it is worth questioning the legitimacy of the legal title and size of all cost elements, although it is not reasonable to perform such an inspection every year.

<sup>12</sup> The central budget basically contains four types of expenditure allocations: expenditures of the central budgetary organisations, appropriations that are managed by the different chapters, but cannot be allocated to any budgetary organisations (at least not in the budgeting period) (chapter managed appropriations), and the so called centrally managed

appropriations within which it is reasonable to differentiate subsidies given to the other subsystem of public finances, and the other expenses (individual and normative subsidies, transfers to households and other transfers, consumer price subsidies, debt service, interest subsidies, payments to the EU, etc.). The share of these expenditure groups naturally varies from year to year; the expenditures of the central budgetary organisations accounted for 28.0% of the total central budgetary expenditure of HUF 8,498.1 billion in 2007 (compared to 29.1% of HUF 7,004.4 billion in 2005), while the expenditures of chapter managed appropriations accounted for 21.8% (versus 18.5 in 2005), subsidies to the other subsystems totalled HUF 19.6% (versus 18.9% in 2005), and the other central expenditures totalled 30.6% (compared to 33.5% in 2005).

<sup>13</sup> Under the current legal framework, program based budgeting cannot be applied in planning the financing of the local governmental subsystem. It can exclusively be applied in the case of chapter managed appropriations that affect local governments, too. The specific extension of this budgeting method to this subsystem can be explored within the framework of a reform aiming at the transformation of the local governmental system.

<sup>14</sup> By competent ministries I mean the ministries responsible for various sectors (healthcare, education, defence, etc.). For the sake of simplicity in the following I will use the word ministry.

<sup>15</sup> The problem described here is explained in an excellent and detailed manner by László (1994, pages 125-135), by describing the claimant's and the allocator's behaviour, and the causes and objectives of such behaviour. These terms are used throughout the study in this sense.

<sup>16</sup> For the relevance and failure of the public task review that aimed at changing the task structure see Section 6.

<sup>17</sup> This "casting" is generally accepted in the international arena, however, in the period of 1998-2002 the Hungarian Government intended to assign a similar position to the Prime Minister's Office with the system of offices then developed.

<sup>18</sup> It must be asked what the difference is between amendable and unamendable legal regulatory conditions, since in theory the National Assembly can amend any act, the government may amend any of its decrees, etc. "Unamendable" legal regulatory

conditions mean those conditions within the procedure the amendment of which was practically impossible (e.g. it would have surely been rejected a two-third support, wherefore proposing the amendment did not make any sense), or the public interest in a given condition was so strong that amendment was out of question (e.g. elimination of the law enforcement tasks of the police):

1. the transparency and elaboratedness of tasks, projects and the implementation thereof during the program,
2. ensuring implementation in accordance with the objective,
3. expected consequences of the abandonment or termination of the program,
4. availability of personal and material conditions,
5. harmony between the required additional personal and material conditions, and resources, and task performance,
6. relationship between subsidy resources and implementation,
7. correlation with other chapter managed appropriations/programs,
8. the output and social impact (outcome) of the program, elaboratedness and quantifiability thereof,
9. program inputs, determination and quantifiability of such inputs and the size of the related expenses,
10. elaboratedness and substantiation of the program's cost analysis, as well as that of the expenditure needs broken down by tasks and projects,
11. the relationship between the requirement for 2005 and the expected utilisation in 2004,
12. elaboratedness of the financial schedule of the entire program,
13. acceptability of the financial needs of further years,
14. availability of the professional and financial control of the program,
15. experiences and ratings of the former professional and financial audits.

<sup>19</sup> In the following I will use this not too elegant expression for the behaviour when the claimant does not inform the allocator about the real priorities known to him, or about the really needed amounts, but deliberately modifies (mis-states) the information or forwards erroneous or ambiguous data so that in the budgeting process, or later during the execution of the budget it would receive a greater amount than the one allocated upon an optimum resource allocation decision. Such "trickeries" may include the following:

- a) indication of appropriations with no upper limit

at a smaller sum, underplanning of such appropriations with a view to leave a room for manoeuvring for other programs during budgeting (the consequence of which is overspending in the implementation stage);

b) indicating a higher than real sum for, or overplanning of determinations (in case of approval a room for manoeuvring is created during the year);  
 c) deliberate subordination of a task that must be performed in any case. This creates a chance for the approval of program that would not be approved if ranked properly, however during the implementation stage claims are put forward for the subordinated – yet required – task performance.

<sup>20</sup> During the negotiations a third (C3) subcategory was also determined when drawing up this category of determinations. This subcategory had to include those programs and granted amounts that did not fit into the above determination categories, but were co-financed from EU funds, and in the case of which the unavailability of national resources would have meant losing the EU co-funding, since after 2005 those funds cannot be drawn down.

<sup>21</sup> The “planner” indicated several times in the description first of all means the Ministry of Finance, and in many places – for the sake of simplicity – this is how I refer to it. Yet, it is worth separating the two, since during the budgeting process discussions with the ministries were carried out in several iterations (e.g. in relation to the categorisation of the determinations), and several budgeting issues were forwarded to government level. Therefore, the complete identification of the planner with the Ministry of Finance would be misleading. On the other hand, when I use the term “Ministry of Finance”, under the changing circumstances it does not necessarily mean the current ministry of finance, but rather the government member and his work organisation coordinating the budgeting process both professionally and numerically.

<sup>22</sup> Since the set of proposal programs did not fully overlap with the set of chapter managed appropriations contained in the budget bill, this value cannot be learnt from the bill itself. The amounts of the approved proposals were often incorporated into the appropriations of institution titles, in other cases they were merged, restructured, etc.

<sup>23</sup> The evaluation is firstly based on the completed documents, secondly on subjective experiences and oral discussions, and thirdly, on a non-representative survey conducted a few months after the end of

the budgeting process among the staff members of the ministry of finance that were involved in the process.

<sup>24</sup> Several responses were received according to which even the supervising organisation obtained information on certain processes within its institutional system, and about the future plans through the forms. (This is of course not a favourable fact since it reflects the supervisory and management problems that are experienced at every step.)

<sup>25</sup> The obtained knowledge was utilised during the elaboration of Act CV of 2008 on the legal status and financial management of budgetary organisations.

<sup>26</sup> Naturally, these statements are based not only on this experiment, but also on multi-year experiences.

<sup>27</sup> It is another issue that in the given situation this was the best solution, since the rate of determination could not be managed without this “cut”. The economically justified solution, i.e. the careful examination of the claims in order to establish the “real determination” was impossible to implement both in theory and practice in the given circumstances.

<sup>28</sup> This type of conduct does not belong to the category of “trickeries”, since it is not about giving a false picture about reality, but about changing reality.

<sup>29</sup> Hardly two weeks were available for the preparation of the proposals (for getting to know the government's intention, for internal discussions, for defining the necessary tasks and the submission thereof to the appropriate level, for concrete data collection, for consideration, form completion, decision-making, etc.). In the case of the concrete person in charge of form completion this probably requires a deadline of one or two days. Three weeks were left for evaluation and decision-making (physical processing, requesting new data, conciliatory talks, consideration and the repetition of these stages several times). An important role was attributed to the special and atypical circumstance that a government crisis occurred in August 2004, and a change of government took place at the end of the month.

<sup>30</sup> The suggestions show many similarities with other writings prepared on the topic of budgeting, yet with completely different objectives. See for example Sántha–Vigvári, 2006

- <sup>31</sup> For example, the existence of a private law contract in this case is a higher level determination than the fact that it represents the national co-financed part of an EU subsidy, wherefore decision can be made on the basis of the former determination.
- <sup>32</sup> Two extremities: the National Development Fund divided its funding need of HUF 225 billion into 5 programs, of which the program titled “Implementation of EU subsidy programs” totalled HUF 174 billion, and the program titled “Preparation of EU large projects” equalled HUF 50 billion. In contrast with this, the Ministry of Justice presented its claim for HUF 10 billion broken down into 42 programs.
- <sup>33</sup> The advantage of this is that the ministries would be a priori forced to thoroughly consider and pre-select the claims (consequently, only “serious” claims should be processed). The disadvantage, on the other hand, is that – especially due to the zero-based nature – no adequate methodology can be assigned for the determination of the budgets of the individual ministries. Therefore, it is reasonable to define these budgets as a percentage of the planned figures for the previous year, however this would reinstate the base approach in the method.
- <sup>34</sup> Therefore it cannot happen that Ministry *A* approves a program whose margin of profitability, i.e. whose social profit from the last spent tax forint is smaller than the social profit from the first spent tax forint of a program rejected at Ministry *B*. Naturally, the pure theoretical formula cannot be used in itself, however comparison must be carried out at the level of political and professional consideration.
- <sup>35</sup> The dominant cause cannot be determined subsequently and at professional level.
- <sup>36</sup> The strategy requires that the planner ( here: the ministries) should carefully consider the state tasks and programs to be implemented in the medium run, as well as their adjustment to the room for financial manoeuvring, and this must be enforced by the macroeconomic situation and the pressing modernisation of public finances. However, it is a different issue what technique the government chooses to budget the funds required for the claims emerging in a given year. The budgeting technique should not “wait” until after the actual implementation of strategic budgeting, and nor should it wait until after the itemised review and reconsideration of state tasks and roles. Both would mean the unsubstantiated postponement of program based budgeting to the uncertain future. It must be noted here that the review of public tasks was carried out in 2006 and 2007 (see Section 6), however since the review yielded only partial success, this task cannot be regarded as completed.
- <sup>37</sup> The Budgetary Management System (BMS) under construction is in part designed to serve this objective, although it represents a great step forward more in terms of IT solutions than in laying the professional foundation of budgeting and financial management.
- <sup>38</sup> This task was more or less completed by the adoption of Act CV of 2008 on the legal status and financial management of budgetary organisations, but the intended implementation may take years in several aspects.
- <sup>39</sup> Ideally, auditing should be performed by external experts (persons, companies) since this would ensure objectivity and competence to the greatest possible extent. There is no doubt that for the time being the practical implementation of this does not seem possible. It is another question whether auditing should take place already during the elaboration of the proposal (before its submission), or in relation to accepted claims, in the period before deciding on the proposal and the compilation of the budget act. The latter is supported by the fact that in this case only a smaller group of claims would need to be audited.
- <sup>40</sup> During the evaluation of the article it was raised that the Hungarian ministries lack a group of 5 to 10 politically uncommitted people who would form the “general base”, a so called professional “tail” of governmental work, and who could serve as a foundation for the successful implementation of the so called all-governmental projects through collaboration, sharing the same language, using the same terms, and building on more or less similar knowledge. A similar governmental objective was formulated during the elaboration of the legal regulation on the all-governmental project – or the elaboration of the theoretical foundation thereof – in 2006 and 2007, however implementation is still to come.
- <sup>41</sup> For the description of the government's objectives and the applied tools see The review of public tasks (2007). Government Decision 2229/2006 (XII. 20.) on the review of public tasks.



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## LEGAL REGULATIONS, DECISIONS

- Act XXXVIII of 1992 on public finances
- Act LXXV of 2008 on cost-efficient financial management by the state and on fiscal responsibility
- Act CV of 2008 on the legal status and financial management of budgetary organisations, as well as the general and detailed explanation thereof (see <http://www.parlament.hu/irom38/06573/06573.pdf>)
- Government Decree 217/1998 (XII. 30.) on the rules of operation of public finances
- Government Decree 246/2007. (IX. 26.) on the all-governmental project
- Government Decision 2229/2006. (XII. 20.) on the review of public tasks
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