



**UPDATE ON THE PERFORMANCE BASED
BUDGETING PILOT PROGRAM CALLED FOR
IN HB 502 OF THE 2000 REGULAR SESSION**

June 14, 2001

EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS
www.kyauditor.net

**144 CAPITOL ANNEX
FRANKFORT, KY 40601
TELE. (502) 564-5841
FAX (502) 564-2912**



EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS

DIVISION OF PERFORMANCE AUDIT
Presentation to the Program Review and
Investigations Committee
June 14, 2001

Summary

The Commonwealth's current budget process does not preclude consideration of performance information during the budgeting process. Although budgeting currently focuses upon fund sources and expenditure categories, performance information could enlighten budgetary decisions and make them more rational.

We found that the current budgeting process must be improved if performance information is to become a meaningful component of the process. We have included an appendix that contains flowcharts of the Commonwealth's current budget process as well as the submission process for the four pilot programs' budgets.

Currently there is no consistency in the development, reporting, and verification of performance information by submitting agencies. Although the *Budget Instructions* clearly solicit this information, they do not specify the type and amount, nor whether or how the information should be verified. In addition, there are no GOPM policies and procedures in this area. As a result, performance information is inconsistently reported, and it may not be valid, reliable, or relevant.

We reviewed performance information compiled for the last two biennia by the four agencies designated as pilots for the performance based budgeting initiative set forth in HB 502. The information was inconsistent. For example, required performance information for new or expanded program requests totaling over \$10 million for Fiscal Budget (FB) 1998-2000 was not included in the Fiscal Budget (FB) 2000-2002 as required by the *Budget Instructions*. In addition, other performance information consisting of quantitative data was inconsistent, and did not include a comprehensive variety of objectives and indicators (e.g. input, output, outcome, efficiency, and explanatory).

Another factor to the development of reporting consistent performance information is the agencies' organizational structures at the program level. The budget processes and related costs vary among the selected programs according to their size and administrative organization.

Finally, performance information is not entered into the Budget Reporting and Analysis Support System (BRASS). While the information may be accessed through BRASS, standard budget reports containing performance information cannot be generated by BRASS. This means that performance information cannot be tracked in the same manner as financial and personnel information.

Background

During the 2000 Regular Session of the General Assembly, funding for executive branch strategic planning and a performance based budgeting pilot program was included in HB 502 (Kentucky Acts 549). In March 2001, the Office of the State Budget Director selected the programs that will be used during the state performance based budgeting pilot program. The pilots selected by the State Budget Director are as follows:

- Program Operations, Department for Juvenile Justice, Justice Cabinet (Juvenile Justice Program Operations)
- Division of Forestry, Department for Natural Resources, Natural Resources and Environmental Protection Cabinet (Natural Resource Forestry Program)
- Division of Motor Carrier, Department for Vehicle Regulation, Transportation Cabinet (Transportation Motor Carrier Program)
- Office of Infrastructure Services, Governor's Office for Technology (GOT Infrastructure Services Program)

Flow of Information During the Budget Process

KRS 48.020 states that each branch of government should continually involve itself in the preparation and revision of budget recommendations for the upcoming biennium. Each Branch accomplishes this through "direct studies of the operations, plans and needs of its budget units ..." This type of preparation and revision is essential to ensure that financial and other information flows smoothly from executive branch programs to various policy-making entities.

Cabinets use the BRASS component of MARS to submit budget requests to GOPM and the LRC. Budget submissions include financial, performance, and personnel information that flow from agencies during the budget process. Agencies are required to report five years of each type of information: (two previous fiscal years, the current budgeted fiscal year, and the upcoming fiscal years).

By November 15th of odd numbered years, GOPM and LRC receives budget submissions from Cabinets and General Government agencies comprising the Executive Branch. GOPM and LRC receive hard copies, as well as electronic versions through BRASS. These budget submissions contain financial, performance, and personnel information for 191 appropriation units, consisting of 675 programs, 168 sub-programs, and 62 posting units. For purposes of this update, we use the term *program* to refer to programs, sub-programs, and posting-units.

The flow of this information begins with a series of uniform budget forms that are issued by LRC on July 1st of odd numbered years. The forms include a series of reports that provide detailed financial, performance, and personnel information for current services budget requests and for additional budget requests (maintenance of existing services, expansion of current services, and new services). In addition, summary reports are automatically generated by BRASS and are used to roll up financial and

other information in the current services and additional budget request reports.

For each program, the following reports are submitted as part of the budget process.

Current Services

- Financial Record (A-1)
- Fund Source Record (A-2)
- Expenditure Detail Record (A-3)
- Capital Outlay Expenses (A-3a)
- Program Narrative/Documentation Record (A-4)
- Personnel Budget Summary Record (A-5)
- Budget Positions Record (A-6)
- EMPOWER Kentucky Cost Savings Record (EMP-1)
- Restricted Funds Summary Record (D)
- Restricted Funds Record (E)
- Federal Funds Summary Record (F)
- Federal Assistance Program Record (G)

Additional Budget Requests

- Financial Record (B-1)
- Position Detail Record (B-1a)
- Fund Source Record (B-2)
- Expenditure Detail Record (B-3)
- Capital Outlay Expenses Form (B-3a)
- Program Narrative/Documentation Record (B-4)
- Priority Ranking Summary Record (P)

Budget submissions are reviewed concurrently by GOPM and LRC for compliance with the budget instructions. If agencies have not complied with instructions, GOPM will make technical corrections to the various forms in BRASS. Once a budget submission is transmitted to GOPM, the agency's ability to make changes in BRASS ends. LRC receives changes through regular nightly downloads through BRASS. Finally, the branch budget recommendations are compiled by GOPM. GOPM generates the Executive Budget that is submitted to the General Assembly.

LRC downloads the Executive Budget into its BRASS database in order to put the budget recommendations into bill format. Budget bills are introduced simultaneously in the House and Senate and formal hearings take place in both chambers. LRC Budget Review Committee Staff enter legislative changes into BRASS, which generates various summary reports and budget memoranda. According to LRC, budget memoranda compare original branch budget recommendations with budget decisions by the appropriations committees and the General Assembly. Budget memoranda are prepared and distributed at each stage of the budget-enacting process.

Members from both chambers reconcile differences during Conference Committee hearings. A *Conference Budget Memorandum* is generated during these hearings and is adopted by resolution. After the General Assembly's version of the budget bill is sent to the Governor for veto action, LRC produces the Final Budget Memorandum and codifies the appropriations bill. After this, GOPM produces the *Final Budget of the Commonwealth*.

In addition to personnel information that shows funding and staffing levels for full-time, part-time, and interim positions, financial and performance information is reported during the budget process. The following definitions provide additional detail on financial and performance information.

Definitions

Financial Information: (Reported for programs related to the following fund sources and expenditure categories):

Fund Sources

General Fund: State tax revenues collected under general tax laws and other receipts to fund the activities, operations, and services of state government.

Road Fund: State revenues from excise or license taxes on gasoline or other motor fuel products. It may also include money from fees and excise or license taxes on registration and operation of vehicles in the Commonwealth.

Federal Funds: Revenues received by state agencies from grants, contracts, or other federal assistance.

Restricted Funds: Revenues collected by state agencies that are statutorily restricted for specific expenditures. Examples include regulatory fees, occupational licenses, tuition, and service charges.

Expenditure Categories

Personnel Costs: Costs related to salaries and wages as well as per diem payments, fringe benefits, and personal services contracts.

Operating Expenses: Costs related to the operations of the appropriation unit.

Grants and Other Financial Assistance: Costs related to assistance to persons, jurisdictions, and organizations.

Debt Service: Costs related to paying debt on financial obligations.

Capital Outlay: Costs related to purchases of equipment items and capital projects.

Performance Information: Information related to “program performance and outcome measures” which explain a program’s purpose and helps to justify funding requests. For purposes of this update, the term *performance information* is defined to include the following:

Goals: The general end purpose toward which agency or program efforts are directed.

Objectives: A specific and measurable target for accomplishing goals.

Input Indicators: Measure the amount of resource allocation and demand for services.

Output Indicators: Measure the amount of products or services provided or the number of customers served.

Outcome Indicators: Measure the results of program impact and effectiveness.

Efficiency Indicators: Measure the productivity and cost-effectiveness, which reflect the cost of providing services or achieving results.

Quality Indicators: Measure the effectiveness in meeting the expectations of customers, stakeholders, and other groups.

Explanatory Information: Explains why certain targets were or were not met.

*Illustration of the Use of
Performance Information for a
Hypothetical Immunization
Program*

Goal: Improve the health of citizens in rural Kentucky.

Objective: Reduce the instances of flu by 75% in rural areas by the year 2004.

Input Indicator: Number of personnel administering the shots.

Output Indicator: Number of shots given.

Outcome Indicator: Number of flu cases in rural counties in 2004.

Quality Indicator: National or professional program recognition.

Explanatory Information: The existence of a new strain of flu that prevented the program from reaching its 2004 target.

Objective Scope and Methodology

HB 502 (Kentucky Acts 549) requires the Auditor of Public Accounts (APA) to do the following:

- Study and report on the flow of budget information from executive branch budget units (particularly the budget units selected for the pilot program) to various entities including the Governor, Legislative Research Commission (LRC), and the General Assembly.
- Monitor the progress of the performance budgeting pilot and present an evaluation by February 1, 2002 to the Governor and the Legislative Research Commission.

Our first report of October 12, 2000 flow-charted the overall budget process and discussed preliminary findings on the use of performance information and strategic planning. Since the Office of the State Budget Director did not select the performance based budgeting pilot programs until March 2001, that report could not discuss the budget process related to those programs.

Once the State Budget Director selected the pilots, we updated the earlier report. This update presents our findings on the Executive Branch's operating budget process and more specifically describes the features and costs of the operating budget process for the pilots selected. For purposes of this update, we use the term *budget process* to denote the Executive Branch's operating budget process.

To determine the components in the Commonwealth's budget process, we examined constitutional and statutory provisions. Staff reviewed background information from LRC, GOPM, and the selected pilot agencies' budget process, as well as information on the use of the BRASS component of MARS. We also interviewed staff from these entities to obtain information on the Commonwealth's current budget process, as well as to solicit feedback on performance based budgeting. Finally, we reviewed the FB 1998-2000 and FB 2000-2002 budget submissions for selected programs.

The following findings discuss the processes, costs, and flow of information related to the pilots. Some of our findings also focus specifically on performance information as the integral component of performance based budgeting.

Findings

1. Variations and differences exist in the budget processes of the pilot programs.

Because of the variations in the size and administrative organization of the selected programs, their budget processes and related costs vary. The fact that these variations exist underscore the responsibility of GOPM to facilitate the flow of accurate performance information from the program level to the Cabinets.

A centrally located budget office at the Cabinet level develops budgets for the Transportation Motor Carrier Program and the Natural Resource

Forestry Program. These programs rely on the central budget office to initiate, prepare, and review their budget information. After the budget information is reviewed at the Cabinet level, it is assembled and then submitted through BRASS to GOPM and LRC.

In contrast, Juvenile Justice Program Operations, which is the largest of the programs, depends upon the Department to prepare its budget information for submission. Once the Commissioner of the Department and assigned budget staff review and approve the budget submission, it is incorporated into the Department's budget request and sent to the Cabinet level for final approval and submission through BRASS. At this point, the involvement of the Cabinet is not as extensive as that involving the other programs.

We also found that only the central budget staff associated with the Forestry Program enters information into BRASS during the initial preparation of the budget. In contrast, information related to the other programs is compiled using various spreadsheets, but is not entered into BRASS until the budget has full executive approval. According to Forestry Program officials, using BRASS throughout the budget process was very time consuming and often frustrating.

The costs attributed to budget preparation for the selected pilots ranged from \$882 to \$48,574 for FB 1998-2000. For FB 2000-2002, costs ranged from \$650 to \$48,600. This cost information is based on an approximation of personnel time allotted to the budget submission for a particular program. It should not be considered an accurate portrayal of costs, since the information was not tracked during the actual budget process. The following is a more specific breakdown of identified costs by programs.

Budget Submission Cost for Selected Programs

Pilot Agency	FB-Cost 1998-2000	Total Budget FB1998-2000	FB-Cost 2000-2002	Total Budget FB2000-2002
Transportation Motor Carrier Program	\$ 882	\$ 4,212,500	\$ 650	\$ 4,614,900
GOT Infrastructure Services Program	14,162	Not Available	24,031	63,508,300
Natural Resource Forestry Program	25,064	23,013,900	25,364	25,655,500
Juvenile Justice Program Operations	48,575	148,459,300	48,600	230,428,400
Total	\$ 88,683	\$ 175,685,700	\$ 98,645	\$ 324,207,100

Source: Auditor of Public Accounts, from information provided by the selected programs and the Fiscal Budgets of the Commonwealth for FB 1998-2000 and FB 2000-2002.

Recommendation:

GOPM analysts should determine how performance information is developed.

2. Performance information is inconsistently reported as part of the budget process.

In our review of the A-4 forms of the four pilots, we found inconsistency in the quantity of performance information reported and an absence of outcome indicators. Although the *2000-2002 Budget Instructions* require the development and reporting of performance information for each program, they are silent on the types and quantity of performance information, which should be developed and reported. For example, the instructions do not define and discuss how to develop goals, objectives, and performance indicators (e.g. input, output, outcome, efficiency, quality, and explanatory measures). Nor, do they discuss what the desirable mix of indicators should be. In addition, GOPM budget analysts do not provide this type of detailed guidance when interacting with their assigned agencies.

The *2000-02 Draft Budget Instructions*, require an *Operating Budget Report A-4* form be completed for current service budget requests. The instructions further require that the A-4 form include "... program performance and outcome measures and any other information which explains the program's purpose and justification for expenditures," and that this information "should be considered by the Agency as the most important part of the budget request." A similar form (the *Operating Budget Report B-4*) is required with the submission of new or expanded budget requests.

We found inconsistencies in the performance information reported for the pilots. For example, the FB 2000-2002 A-4 for GOT's Office of Infrastructure Services contained 33 pieces of quantitative data to support its continued budget request. Much of the information illustrated the number and type of computing equipment which exists in the Commonwealth, (e.g. local area networks, video locations, telephone systems, KEWS microwave towers, etc.) as well as the number of users of various systems such as E-mail users, Internet users, Remote Access users, Wireless Voice users, etc. The amount and type of this information may not be helpful to individuals who wish to know how well the Office fulfilled its responsibility for the "operation of the enterprise computing environment."

The remaining pilots included much less information in their FB 2000-2002 A-4 forms, since they did not include adequate outcome indicators to show how effectively the programs operate. As an example, Juvenile Justice Program Operations listed the number of juveniles served in day treatment, group homes, residential care, community services, private childcare, and detention facilities. However, additional information about the effectiveness of juvenile care, such as recidivism rates was not provided.

Finally, we found that none of the pilots reported objectives or a useful mix of performance indicators on its A-4 forms. Measurable and timebound objectives should be linked to a mix of performance indicators to show progress towards measurable targets. Only then can policy makers make an informed judgment on whether a program is operating effectively.

Clear criteria to help program officials develop and report consistent performance information is essential. States like Louisiana offer comprehensive instructions for agencies developing performance information on strategic planning and performance based budgeting.

Louisiana's *Manageware* provides information on the state's budget processes. More specifically, it defines goals, objectives, and performance indicators, and explains the steps for developing them. In addition, planning analysts assigned to the agencies work with agency officials and appropriations staff to develop appropriate performance information for use in the budget process. By using *Manageware* and collaboration among primary parties, consistent development and reporting of performance information occurs.

Recommendation:

Since performance information is required by the *Budget Instructions*, GOPM should provide detailed guidelines for the development of performance information.

3. Required performance information for new or expanded program requests was not included in the FB 2000-2002 budget submission for two of the selected programs.

Examination of the pilot budgets revealed that performance information for 5 new and 5 expanded program requests funded with \$10,085,000 for FB 1998-2000 was not reported, as required, in the FB 2000-2002 A-4 forms. As a result, legislators or other individuals reviewing these forms may not have been able to determine the effectiveness of the new or expanded programs funded during the FB 1998-1999 period.

The *2000-2002 Budget Instructions* related to A-4 form preparation states that "agencies which received additional appropriations in FB 1998-2000 for new or expanded services/activities or personnel, as identified in the *1998-2000 Final Budget Memorandum* (House Joint Resolution 34, 1998 Ky. Acts ch. 573) must identify the item(s) and provide appropriate data which indicates the level of activities/services or personnel that was budgeted with the additional funds as well as the level of activities/services or personnel that has been accomplished or delivered in comparison with the budget plan."

The *Budget Instructions* are very clear on this point. However, little or no performance information was provided in the FB 2000-02 A-4 form for Juvenile Justice Program Operations and for the Natural Resource Forestry Program for new and expanded program requests. The A-4 forms should have included this type of information to compare effectiveness as related to previous levels of funding.

For example, the related B-4 form submitted by Juvenile Justice Program Operations for FB 1998-2000 requested additional funding for providing added positions for a 40-bed boot camp in Breathitt County. It stated that the facility would serve 80 persons annually and implied in the program narrative that the program expects to achieve the 15% recidivism rate that a similar facility in South Carolina has achieved. However, the A-4

submitted for FB 2000-2002 only mentioned that the facility had started to operate in Breathitt County. It did not reveal how many persons were served, workload, number of the new employees, nor recidivism.

Another example is the B-4 form submitted by Juvenile Justice Program Operations for FB 1998-2000, which requested additional funding for aftercare services. The program narrative referred to research that claimed a 20% recidivism rate may occur for individuals who do not receive this type of treatment after they are released from a juvenile facility. However, the A-4 form submitted for FB 2000-2002 only stated that aftercare was occurring based on a Consent Decree. It did not state whether recidivism rates are lower for those who are participating in aftercare.

A final example is the B-4 form submitted by the Natural Resource Forestry Program for FB 1998-2000, which requested additional funding to hire Foresters and Forest Ranger Technicians to conduct forest inventories and provide educational outreach to private forest landowners and loggers. The B-4 form stated that the additional positions would allow an increase in the inventory cycle to 20% of established plots (500-600) each year. However, the narrative section of the A-4 form submitted for FB 2000-2002 only mentioned that the inventory is “now underway in Eastern Kentucky.” It made no reference to the 20% target it set for the previous biennium.

This last example underscores the importance of communicating progress toward stated targets because the 20% target was also incorporated into the *FB 1998-2000 Final Budget Memorandum* as a rationale for additional funding. The *Budget Memorandum* states the program managers “...are to inventory 20% of the established plots (500-600) each year which will provide a complete inventory of the state every 5 years.” The following tables show the breakdown of the new and expanded program requests of the pilots.

New Program Requests

Program Service/Activity FB 1998-2000 Appropriation

Program	Service/Activity	FB 1998-2000 Appropriation
Juvenile Justice Program Operations	40 Bed Boot Camp	\$ 2,462,000
	Statewide Juvenile Delinquency Prevention	3,100,000
	Aftercare Services	500,000
	Treatment for Emotionally Disturbed Girls	1,300,000
Natural Resource Forestry Program	Kentucky Forest Conservation Act	\$ 1,076,000
Total Appropriation		\$ 8,438,000

Source: Auditor of Public Accounts from information contained in the FB 1998-2000 Commonwealth Budget Final Budget Memorandum, Volume II.

Expanded Program Requests

Program Service/Activity FB 1998-2000 Appropriation

Program	Service/Activity	FB 1998-2000 Appropriation
Juvenile Justice Program Operations	Salary Upgrade for Youth Workers	\$ 500,000
	Bluegrass Assessment Center	400,000
	Expanded Hours of Day Treatment	624,000
	Juvenile Transportation Network	123,000
Total Appropriation		\$ 1,647,000

Source: Auditor of Public Accounts from information contained in the FB 1998-2000 Commonwealth Budget final Budget Memorandum, Volume II.

According to agency officials responsible for budget submissions, there is awareness that performance information related to additional budget requests should be reported in the A-4 forms. However, specific guidance from the *Budget Instructions* and from GOPM has not been forthcoming. One agency official for the Cabinet for Natural Resources stated that she felt that the information in the A-4 form met the broad budget instructions. As mentioned previously, there is currently no formal criteria for agencies to use when developing performance information for the A-4 and B-4 forms. GOPM officials stated this is an area that could be clarified if there were more emphasis on the use of performance information.

Recommendation:

GOPM should ensure that budget submissions contain adequate performance information.

4. There are no policies, procedures, or guidelines on the assessment by GOPM of performance information for validity and reliability.

The *Budget Instructions* state that the preparation of A-4 and B-4 forms “should be considered as the most important part of the budget request.” In the absence of performance information policies, procedures, and guidelines, assessments and recommendations by analysts may be inconsistent or flawed.

Currently, GOPM uses the performance information submitted by agencies to develop the Commonwealth’s *Executive Budget*. Although budget officers from the agencies, as well as analysts from GOPM and LRC, generally review the information included in the A-4 and B-4 forms, there are no official policies, procedures, or guidelines available to ensure consistent and substantive verification. We believe that guidelines should be formulated requiring the internal assessment of performance information by the submitting agency as well as externally by analysts at GOPM and LRC. Such guidelines will help to ensure that performance information is valid and reliable.

We discussed this issue with staff from GOPM and LRC, who said there are no such policies or guidelines in place. Rather, individual analysts may question performance information if something looks out of place. Although there appear to be some inquiries about the validity and reliability of the performance information, it is apparent that such information is not assessed consistently. As a result, the risk is high that performance information reported on the A-4 and B-4 forms is not valid or reliable.

Recommendation:

GOPM and LRC should develop policies and procedures specific to the review of performance information submitted

5. Performance information is not entered or reported in BRASS.

Unlike the financial and personnel information submitted as part of a Cabinet level budget submission, performance information is not entered and reported in BRASS. Rather, performance information related to a Current Services Budget Request or an Additional Budget Request is

prepared in a Word document accessible through BRASS. Even though the document may be opened through BRASS, standard reports like those generated for financial and personnel information cannot be generated for performance information.

Developing and reporting performance information in a Word document does not lend itself to accurate and consistent reporting and tracking. In addition to the lack of criteria governing the development of performance information, having to open up a separate Word document each time an agency wishes to make changes to performance information is not an expeditious method for developing this important information.

Louisiana and Texas use systems to track how well agencies are meeting targets set by their performance information. The systems generate quarterly reports for the Governor's office, legislative oversight entities, legislators, and program managers showing progress. These reports allow interested parties to monitor and influence the progress agencies are making toward their targets during the interim.

As part of the performance based budgeting pilot program, GOPM is working to include and track performance information in BRASS for pilot programs. For example, the *2002-04 Draft Budget Instructions* provide additional forms for selected programs to report objectives and performance indicators. According to GOPM officials, this will allow performance information to be tracked along with financial information.

Recommendation:

GOPM should consider allowing all agencies to use newly created BRASS forms that integrate performance and financial information.

Recommendation:

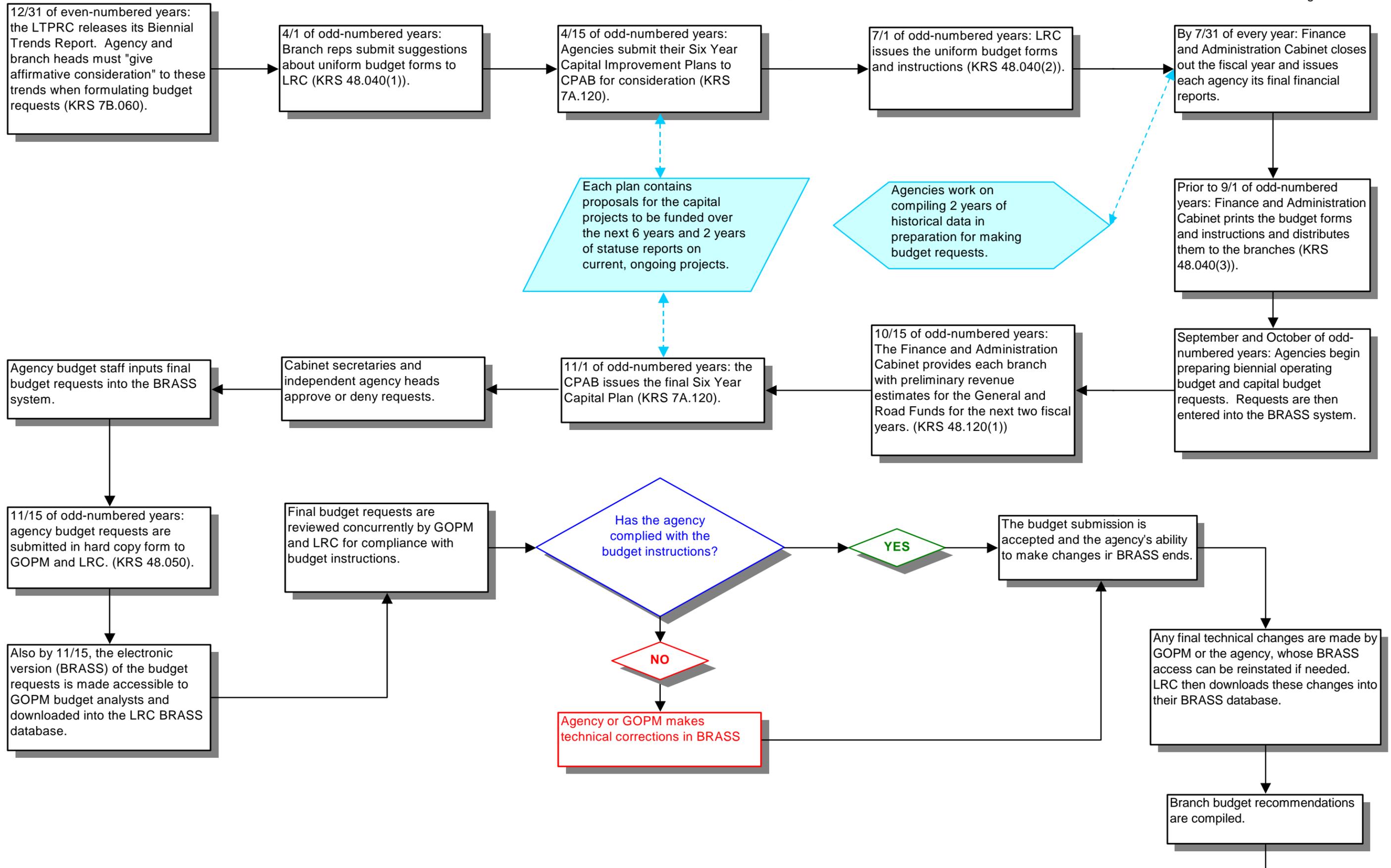
GOPM and GOT should consider developing a tracking system to store and report performance information submitted during the budget process. Either BRASS or the strategic plan database required by HB 502, could serve as a starting point for this enhancement.

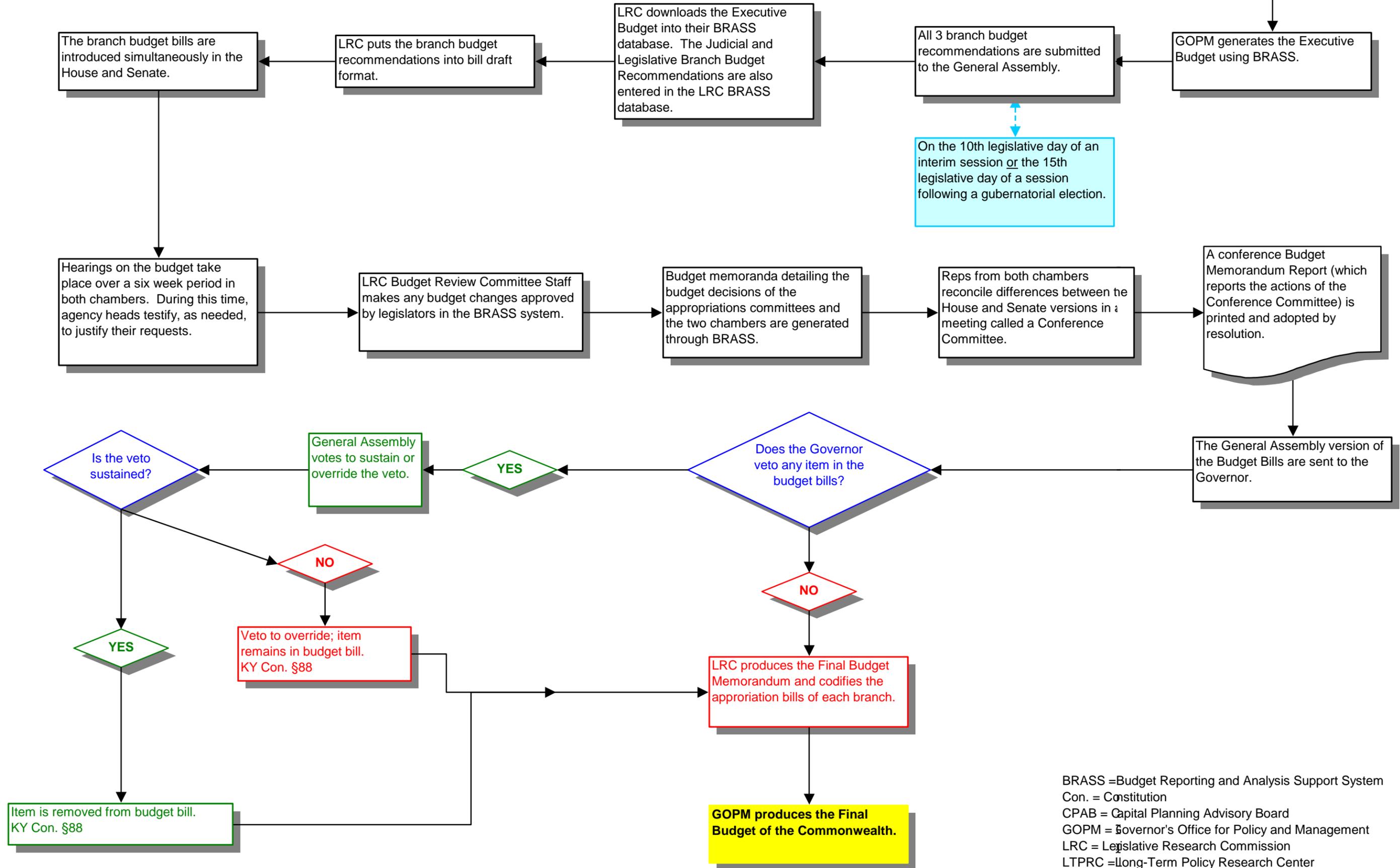
Conclusion

The Commonwealth is poised to take advantage of a legislative framework for performance based budgeting established during the 2000 Regular Session. As the principals identified in HB 502, work together to ensure that performance information is consistently developed, reported, and verified, performance based budgeting can become an integral component of the budget process. This will lead to more informed, rational, and accountable budget decisions.

THIS PAGE LEFT BLANK INTENTIONALLY

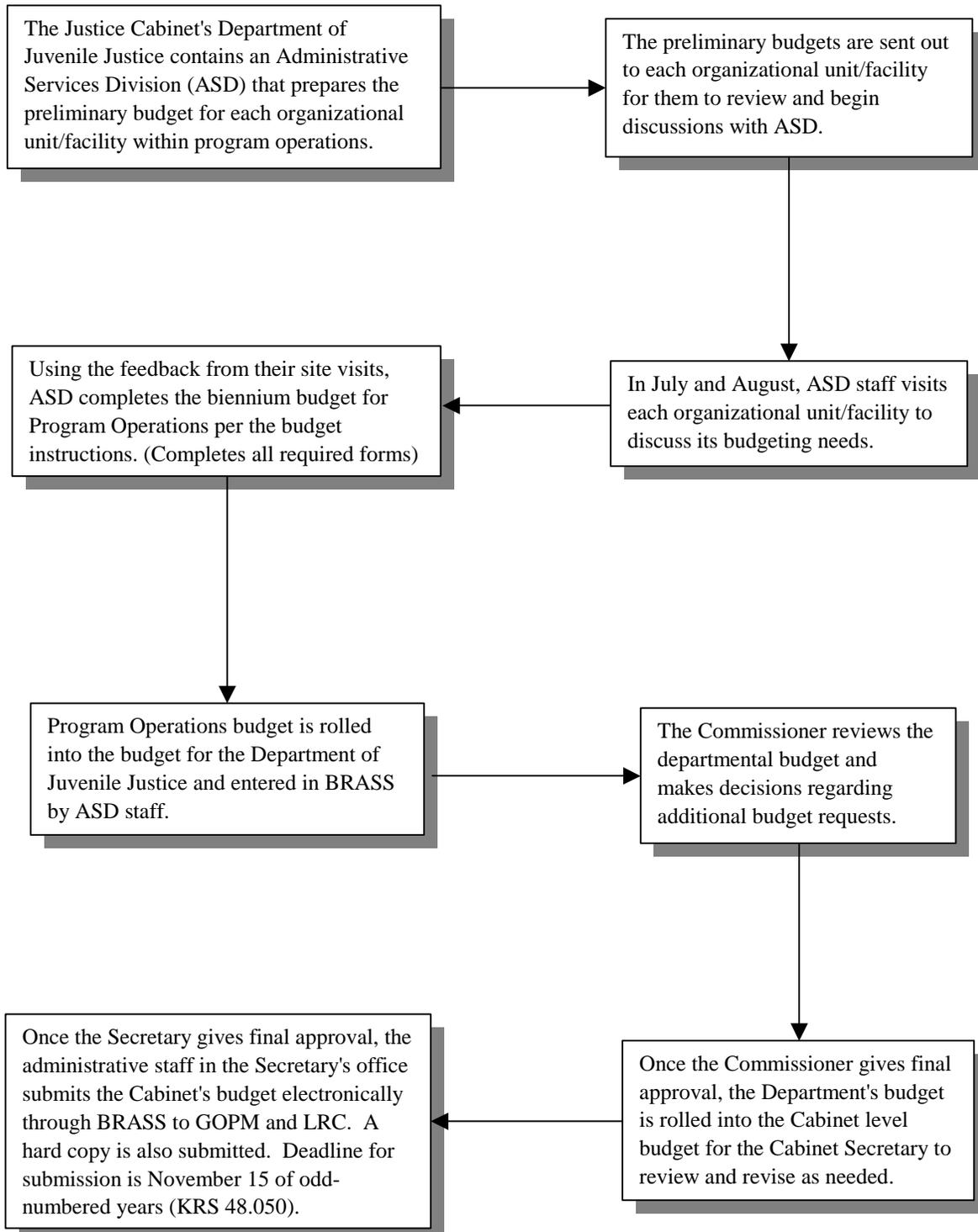
APPENDIX: FLOWCHART OF CURRENT BUDGET PROCESS



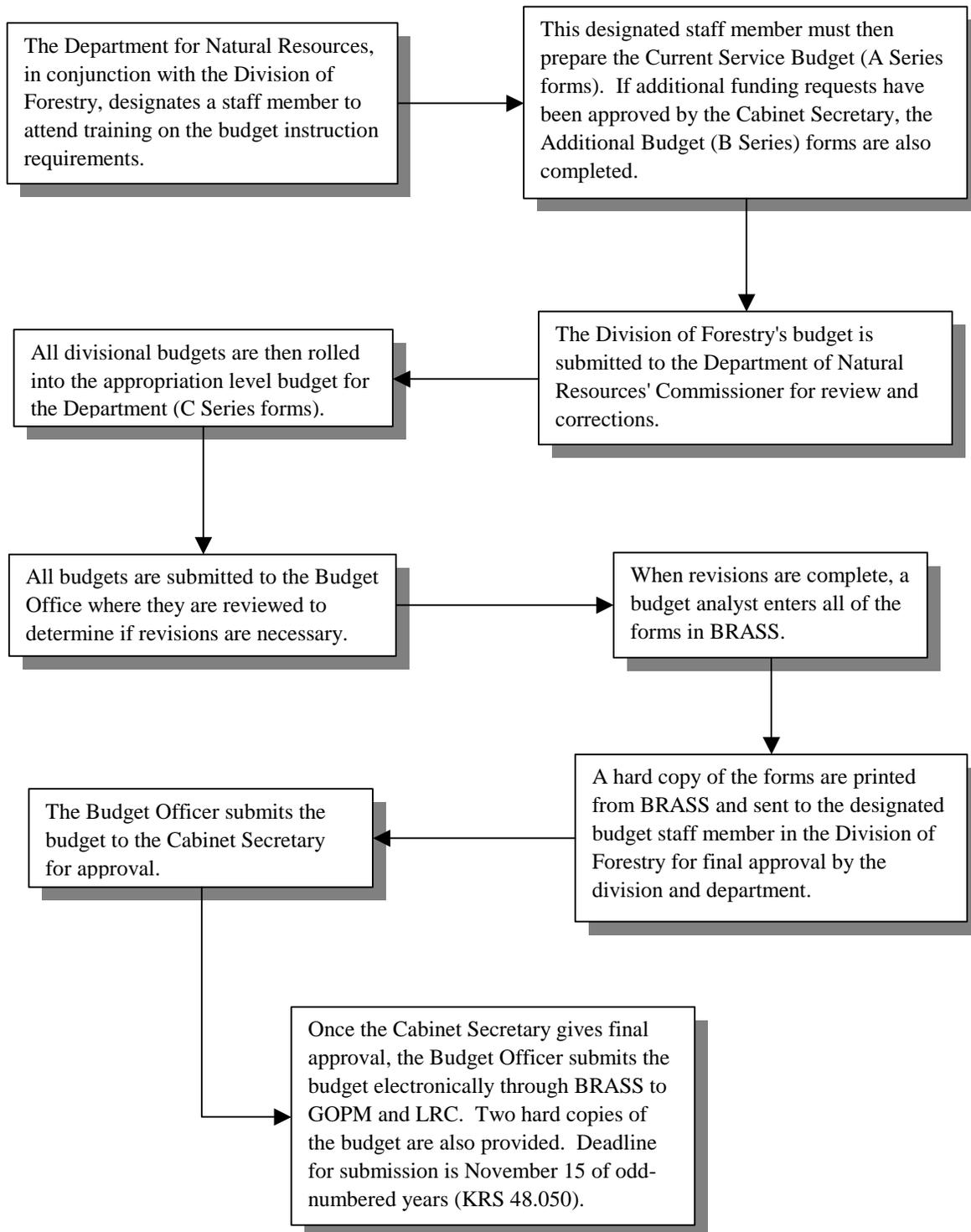


BRASS = Budget Reporting and Analysis Support System
 Con. = Constitution
 CPAB = Capital Planning Advisory Board
 GOPM = Governor's Office for Policy and Management
 LRC = Legislative Research Commission
 LTPRC = Long-Term Policy Research Center

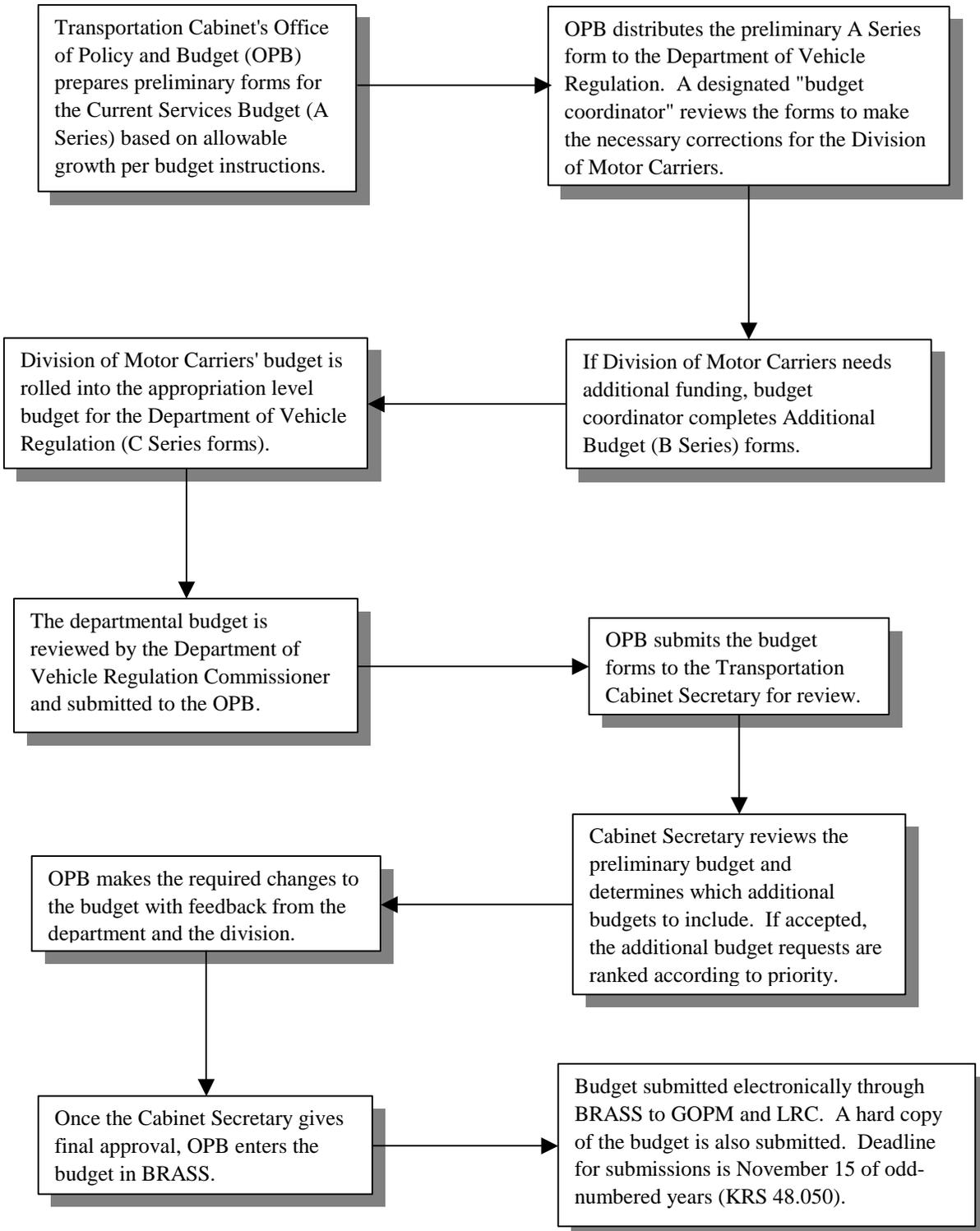
Appendix: Juvenile Justice Program Operations



Appendix: Natural Resource Forestry Program



Appendix: Transportation Motor Carrier Program



Appendix: GOT Infrastructure Services Program

