



**Update on Executive Branch  
Strategic Planning and the  
Performance Budgeting Pilot Program  
Called for in HB 502  
of the 2000 Regular Session**

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## **Summary**

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). The Appropriations Act requires the following:

- Executive branch agencies shall submit strategic plans with their 2002-2004 budget requests.
- The State Budget Director shall designate an entity to develop and conduct training related to the development of strategic plans.
- The Governor's Office of Technology (GOT) shall establish a uniform electronic strategic plan submission form, as well as a procedure that allows the plans to be entered into a searchable electronic database.
- The Office of State Budget Director shall design and implement a state performance based budgeting pilot program with no less than three nor more than six budget units in the executive branch. In addition, a performance based budgeting pilot project fund shall be set up in the Office of State Budget Director related to the pilot project.
- Each budget unit selected for the pilot project shall submit a performance based budget request for FB 2002-04 in addition to its regular budget request.

The bill requires the Auditor of Public Accounts (APA) to conduct a 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. The Auditor must also monitor the costs and progress of the performance based budgeting pilot project.

This report is the first of a series fulfilling these two responsibilities of the APA. The Auditor's Office must later present an evaluation to the Governor and LRC discussing the pilot project's implementation and will make recommendations for future implementation.

The Office of State Budget Director received a General Fund Appropriation of \$750,000 for the Performance Based Budgeting Pilot Project. The Auditor of Public Accounts received a General Fund appropriation of \$120,000 to support the Performance Based Budgeting Pilot Project.

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## **Background**

Performance based budgeting links an agency's funding to its success in achieving desired results. The budget process depends upon the development and reporting of performance information by agencies, often as part of a strategic plan. For purposes of this update, the term *performance information* is defined to include the following:

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

Objectives: Show specific and measurable targets 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.

Other states have enacted performance based budgeting legislation for the purpose of encouraging the consistent development, reporting, and use of performance information to achieve budgets that optimize the use of public resources. The following are some of the benefits of adopting performance based budgeting:

- Provides decision-makers with information on past and projected performance and effectiveness of programs before making budgetary decisions.
  - Provides program managers with useful information to assess the effectiveness of their operations.
  - Provides benchmarking information for use by external auditors.
  - Provides information that ensures greater government accountability to citizens.
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## **Use of Branch Budget Bills and Appropriation Units**

Kentucky's current budget process relies upon omnibus branch budget bills for each branch of government (legislative, executive, and judicial). Each branch budget includes operating and capital appropriations and related fiscal provisions for all constituent agencies and budget units. Once approved, branch budget bills are effective for the duration of a biennium.

***Appropriation Units and Budget Funds***

The standard unit of appropriation in a branch budget bill is a department or agency. However, there are times when a division, program, or consolidated organizational units within a department or cabinet may constitute an appropriation unit.

The budget fund classifications for appropriation units in the Commonwealth’s Operating Budget consists of the following:

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.

***Operating Expenditures***

Operating expenditures are also classified in the Commonwealth’s current budget process. Operating expenditures for appropriation units are defined by the following 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.

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**Work Completed By**  
**APA**

In order to determine the components in the Commonwealth’s budget process, we examined constitutional and statutory provisions. Staff reviewed background information from LRC, the Governor’s Office for Policy and Management (GOPM), and various agencies on the budget process and on the use and cost

of the Budget Reporting and Analysis Support System (BRASS) component of the Management Administrative and Reporting System (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 budget submission of the Natural Resources and Environmental Protection Cabinet.

We solicited information from other states and professional organizations in order to ascertain which states employ some form of performance based budgeting. Finally, we interviewed budget staff from other states employing some form of performance based budgeting.

Finally, with feedback from staff of LRC, GOPM, and the Natural Resources and Environmental Protection Cabinet, we developed a flowchart of the budget process to identify the components of the process and to illustrate the flow of budget information (See Appendix).

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### **Work to Be Completed by APA**

The Office of the State Budget Director is currently in the process of choosing the budget units that will be used during the state performance based budgeting pilot program. Once the budget units are selected, we will complete our review of the current budget process and provide specific information on the flow of information from the selected budget units to the Governor, LRC, and the General Assembly. As mentioned in HB 502, "The report shall particularly focus on a detailed baseline description of the features and cost of the budgeting structure of the budget units selected for the pilot program".

Although we will not be able to finish our assessment of the budget process until we learn the identities of the selected budget units from the Office of State Budget Director, we have included preliminary findings in this update resulting from our initial review. We also identify and comment upon issues which we believe deserve detailed and special attention to ensure the success of performance based budgeting in the Commonwealth.

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### **Preliminary Findings**

1. *Performance information that is developed as part of the budget process is not reported to the Legislature in the Commonwealth's Executive Budget.*

Although budget units submit some performance information as part of the budget process (see findings #2 and #3 for additional information), the information is primarily used by GOPM and the LRC for initial funding recommendations. While Legislators may view this information upon request, they may not be receiving complete information about the performance of programs and

subprograms within appropriation units prior to making budgetary decisions.

Rather, fund and expenditure category information is primarily reported as part of the Commonwealth's budget process for each appropriation unit. Although this type of information is important for making budget decisions, it may not be sufficient to assure informed decisions about the effectiveness of programs and subprograms within individual budget units.

For example, the Kentucky Natural Resources and Environmental Protection Cabinet is comprised of various appropriation units, one of which is the Department for Natural Resources. The department is comprised of allotment programs, one of which is the Division of Forestry. The recommended budget for the division for FY2001 and FY2002 was \$11,940,700 and \$12,074,800 respectively.

According to the webpage for the Cabinet, the Division of Forestry includes the following programs:

- Forest Stewardship;
- Forest Management;
- Rural Fire Prevention and Control;
- Rural Community Fire Protection;
- Federal Excess Property;
- Water Quality Management;
- State Forests;
- Heritage Land Conservation Fund;
- Forest Resource Education;
- Forest Resource Utilization;
- Urban and Community Forestry;
- Reforestation; and
- Tree Improvement.

During the budget process, the department submits fund and expenditure category information about the division. Comprehensive and consistently developed performance information measuring the effectiveness of the above programs within the division, however, is not part of that submission. As a result, information that could contribute to more informed funding decisions is not submitted routinely for use by the General Assembly when making budgetary decisions.

As mentioned previously, budget units submit some performance information as part of the budget submission process. However, GOPM and the LRC use the information for making initial funding recommendations. This truncated system may not allow the General Assembly to reap the same benefits from existing performance information as GOPM and LRC budget analysts.

2. *Performance information is not developed in a consistent manner.*

According to the 2000-02 *Draft Budget Instructions*, an *Operating Budget Report A-4* must be completed for current service budget requests. The *A-4* should include “specific legal citations, fiscal justification for the program, program performance and outcome measures and any other information which explains the program’s purpose and justification for expenditures.” A similar form (the *Operating Budget Report B-4*) is required with the submission of *Additional Budget Request(s)*.

Although the instructions mention the type of performance information that should be included in the *A-4* and *B-4* forms, there is no guidance related to the development of performance information. Since the information in these forms is used by GOPM and LRC to make initial funding recommendations, there should be more specific instructions for developing performance information.

We found inconsistencies in the performance information included in the *A-4* and *B-4* forms submitted by the Natural Resources and Environmental Protection Cabinet. For example, we found instances where limited performance information was embedded in the Program Narrative and Fiscal Justification sections of the forms. However, it was not included in the Performance/Results Documentation section, where we believe it belongs. This section should be used because it provides a framework for reporting performance information for a five-year period (actual, budget, and requested). We also found certain types of performance information reported on the *A-4* and *B-4* forms for one program, but not another.

***Embedded Performance Information***

During our review of the *A-4* and *B-4* forms we found instances where limited performance information was embedded in the Program Narrative and Fiscal Justification sections of the forms. For example, the Office of Administrative Hearings (Office) provided information in the Program Narrative section that states *...continues to receive approximately 30 formal hearing and 35 assessment conference requests per month*. This is an example of input indicators that show workload. Instead of discussing this information in the Program Narrative Section, however, the Office should have provided five year’s worth of workload data to justify its budget request in the appropriate section. In addition, the Office should provide output indicators related to the actual number of formal hearings and conferences conducted as well as outcome indicators to show impact or effectiveness of the hearings and conferences. In addition, indicators related to staff resources, cost per output and outcome could also be reported.

In this particular instance, the Office is using its embedded workload indicators as a justification for increased funding to



maintain existing services. However, the *A-4* does not provide enough performance information for a legislator to know how well the Office handled the workload in the past, is handling the workload currently, and how they plan to handle the workload in the future. In addition, the *B-4*, which is used to request additional funding, does not include adequate information either. Rather, the *B-4* provides an explanation of how the additional money will be used (e.g. for travel, training, software maintenance, etc.). Again, both forms do not provide adequate performance information related to the Office's performance in this area.

***Performance Information  
Not Consistently Reported***

In contrast, the Office of Legal Services (within the same Cabinet) includes more detailed information in the Performance/Results Documentation section of its *A-4*. The Office of Legal Services provides output indicators related to the number of legal opinions and reviews conducted for a five-year period. In addition, they provide an input indicator, which shows the number of attorneys for that same period. Although the Office of Legal Services does not include outcome indicators related to the impact of the legal opinions and reviews, it does provide enough information to make other calculations such as the number of legal opinions and reviews per attorney.

These two examples demonstrate how offices within the same Cabinet (Natural Resources and Environmental Protection) fill out their *A-4* and *B-4* forms differently. Based on these examples, it is logical to contend that there are many other examples of inconsistencies across executive branch agencies. This is why it is important to develop consistent instructions related to the development of *A-4* and *B-4* forms.

***Framework Exists***

Nevertheless, we believe that program managers, as well as GOPM and LRC staff, have developed a framework for understanding the development and reporting of performance information as part of the initial budget process. However, we also believe it is important that comprehensively and consistently developed performance information be used as an integral part of the entire budget process, including being reported directly to the General Assembly.

We discussed with GOPM and LRC staff the possibility of requiring agencies to consistently develop and report performance information. We also discussed the importance of including such performance information in the Commonwealth's *Executive Budget*. They opined that this would not require major changes to the budget process.

3. *There are no policies, procedures, or guidelines on the assessment of performance information to ensure that the information is reliable and valid.*

The *Draft 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 policies, procedures, and guidelines for assessing performance information, however, staff from agencies may be submitting performance information to GOPM and LRC that is invalid or unreliable.

Currently, LRC and GOPM use 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 assessment. We believe that guidelines should exist so performance information is assessed internally by the submitting agency as well as externally by analysts at GOPM and LRC. Such guidelines will help to ensure that performance information is reliable and valid before being used as part of the budget process.

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.

4. *The Commonwealth is not realizing the full benefit of strategic planning.*

The Commonwealth’s strategic planning is a fledgling enterprise. Although some agencies engage in strategic planning, a consistent format for the development of strategic plans has been absent. In addition, there has not been consistent training to help all agencies understand the mechanics of developing, updating, and implementing the plans. As a result, a permanent framework has not been established to ensure that agencies routinely focus on effectively managing their performance.

According to GOPM in the 2000 *State Government Survey*, completed as part of the *Government Performance Project*, five cabinets and the Council on Postsecondary Education (CPE) regularly prepare strategic plans. As mentioned previously, HB 502 requires the development of four-year strategic plans at the budget unit level. It also states the Office of State Budget Director shall coordinate training and guidance on the development of strategic plans.

To develop a framework for strategic planning training, the office has assembled a Process Leadership Team, which consists of members from GOPM, the Government Services Center (GSC), agencies, as well as outside facilitators. The team is working on developing a template and timeline for implementation of statewide strategic planning training. The team plans to submit final recommendations to the EMPOWER leadership team on November 16, 2000. The EMPOWER leadership team consists of Secretaries from the Governor's Executive Cabinets.

Because some agencies already participate in strategic planning, and the Office of the State Budget Director is developing a framework for strategic planning training, the Commonwealth should be poised to meet the mandates of HB 502.

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### **Issues for Consideration**

1. *Strategic planning training should link strategic plans and performance information to the Commonwealth's budget.*

As mentioned previously, the Office of State Budget Director is in the process of developing a framework for conducting training related to strategic planning. In addition, it is in the process of partnering with the Kentucky Community and Technical College System (KCTCS) to provide the training once a curriculum has been established. Although the framework has been set for statewide strategic planning, it is critical at this juncture to ensure that the training links strategic plans and performance information to the Commonwealth's budget.

Various states we consulted require the development and use of strategic planning as part of the budget process. For example, legislation passed by the legislatures in Louisiana and Texas requires the development of strategic plans, which include performance information. In these states, performance information in the form of goals, objectives, and performance indicators are developed for inclusion in the Governor's Budget Request as well as the Appropriations Act. Other states such as Arizona, Missouri, North Carolina, and Virginia use strategic plans as a basis for developing an overall budget request.

Training is at the center of all successful state implementations of performance based budgeting. In the state of Louisiana, the Governor's Office of Planning and Budget developed a training

publication called *Manageware*. This publication is continually updated and includes specific instructions on the development of strategic plans and related performance information. *Manageware* provides agencies with a framework to help managers develop and report consistent and complete performance information.

As the strategic planning process is implemented, we note the importance of a detailed training curriculum emphasizing the connection of strategic plans and the Commonwealth's budget. We also suggest that a balanced array of strategic planning resources, including those outside the Commonwealth, be consulted as the curriculum is fashioned.

2. *The performance based budgeting pilot program should be substantive enough to move the Commonwealth toward a successful implementation of performance based budgeting that integrates strategic planning with the budget process.*

The development of a performance based budgeting pilot program is no small task. Not only do the designers need a firm understanding of the mechanics of performance based budgeting and strategic planning, they also need to understand that the success of performance based budgeting hinges on a strong pilot program. It is incumbent upon the designers to ensure that the pilot program is structured in a way to develop a mechanism for using consistently and comprehensively developed performance information during the budget process. The designers of the pilot program can do this by researching other states that have successfully implemented performance based budgeting.

During our preliminary research, we found examples of states that have implemented performance based budgeting. Some states we researched develop performance information as part of a strategic planning process and report this information as part of the Governor's budget request. For example, the state of Louisiana pulls program descriptions and key objectives and performance indicators from strategic plans for inclusion in the Governor's budget request and the Appropriations Act. The performance information often measures the performance and effectiveness of programs and subprograms within budget units.

The State of Texas takes the concept of performance based budgeting further; its appropriations are based on strategies (*strategy* is often used as another term for objective). For example, the budget of the Texas Department of Agriculture lists various strategies, which receive individual appropriations. The General Appropriations Act for the 2000-2001 biennium lists nine strategies receiving appropriations for the Department of Agriculture.

One such strategy receiving an appropriation is *Generate marketing opportunities for Texas farmers, ranchers and agribusinesses*. This strategy received appropriations of \$7,935,762 and \$6,938,780 for years ending 8/31/00 and 8/31/01 respectively. Performance indicators such as *number of companies enrolled in TDA marketing programs and businesses developed as expansion/recruitment prospects in rural Texas* are also included in the Act.

We acknowledge and applaud the steps the Office of State Budget Director is taking to facilitate strategic planning training and choose the best possible design for the performance based budgeting pilot project. However, we also want to stress the importance of consulting with a variety of states that have had success in integrating performance information as part of a strategic plan with the budget process.

3. *GOT should ensure that the uniform electronic strategic plan database includes a tracking system to generate quarterly reports to illustrate how well agencies are meeting their targets.*

As mentioned previously, HB 502 requires GOT to develop a uniform electronic strategic plan submission form as well as a procedure that allows the plans to be entered into a searchable electronic database. We agree this is an important first step to ensure the consistent submission, storage, and accessing of performance information. However, we also believe GOT should include a tracking system that generates quarterly reports to show how well agencies are meeting their targets. In states we consulted, quarterly reporting allows internal and external review of performance information by various interested parties.

States like Louisiana and Texas use tracking systems to provide reports to the Governor's office, legislative oversight entities, legislators, and program managers. This information allows these parties to monitor and influence the progress agencies are making toward their targets during the interim. The Commonwealth should likewise ensure that such information is submitted and stored in a manner accessible by interested parties.

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## **Conclusion**

The Commonwealth is poised to take advantage of a legislative framework established during the 2000 Regular Session. The principals identified in the Appropriations Act, as major contributors to this effort, are clearly important participants. It is incumbent upon them to ensure that the building blocks are developed so performance based budgeting will succeed. Then, the funding of programs and subprograms will be based on performance and effectiveness, which will provide government accountability to the taxpayers of the Commonwealth.