

STRENGTHENING THE ROLE OF LINE MINISTRIES IN THE BUDGET PROCESS IN SOUTH-EAST EUROPE

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EXECUTIVE SUMMARY

This paper serves as a background material for future CEF activities aimed at line ministries. The paper is based on interviews with the finance directors of line ministries in three countries: Slovenia, Croatia and the Netherlands. It describes the typical organisation and task package of the Finance Directorate of a line ministry in Croatia and Slovenia on the one hand, and in the Netherlands on the other hand.

The picture that arises from these descriptions is that of a Finance Directorate of a line ministry as a financial administration in Slovenia and Croatia, and as a “concern controller” in the Netherlands. The stronger role, characteristic of the Netherlands, results from a stronger focus on internal fiscal policy coordination and budgetary discipline. Fiscal policy coordination must ensure that the budget can be easily adjusted to changing social and economic circumstances and political priorities. Budgetary discipline must ensure better compliance with budgetary ceilings.

In order to strengthen the role of the Finance Directorate of the line ministry as internal fiscal policy coordinator, it is important that (a) the budget preparation calendar is moved forward, (b) sectoral directorates are recognised as budget holders, and (c) a standard evaluation procedure is introduced. To strengthen the role of the Finance Directorate of the line minister as guardian of fiscal discipline, it is vital that (d) expenditures estimates of current policy (baselines) are regularly updated and approved by the Ministry of Finance, (e) rules of budgetary discipline are established, and (f) the line ministry works in close coordination with the Ministry of Finance.

The paper specifies the steps to be taken by the Ministry of Finance and the line ministries to implement these reforms. It also identifies some major challenges that the reforms pose for the countries in South-East Europe. Among other things, politicians and senior civil servants will have to agree on a stronger, neutral role of the finance director of a line ministry and on more autonomy for line ministers to put their stamp on sectoral policy.

INTRODUCTION

This paper serves as a background material for future CEF activities aimed at line ministries.¹ It addresses the current role of line ministries in the budget process, the opportunities for strengthening this role and the ensuing benefits, concrete steps that could be taken for this purpose, and challenges that such steps would pose in the context of regional circumstances.

There is relatively little comparative literature on the role of line ministries in the budget process in the countries of South-East Europe (SEE).² It is fair to say that in SEE the systematic investigation of the role of line ministries in the budget process started only with the “Fiscal Impact Assessment of Structural Reforms” project, which the CEF delivered in 2012-2013.³ This led to a book of case studies (CEF 2014) that has served as an important source of information for the current paper (along with the minutes of the conference that was devoted to this book and held on 23-24 October 2012). In addition, use was made of information provided orally or in writing by participants of two CEF courses in 2014 aimed at line ministries.

This paper is largely based on structured interviews with finance directors in three countries: the Netherlands, Slovenia and Croatia. For this purpose a question list was drafted⁴ and in each country one or two finance directors of line ministries were interviewed. The question list and the interviews focused on factual information about financial management in the line ministries.

The Netherlands was chosen because its model of cooperation between the Ministry of Finance and the line ministries can provide inspiration as to the role of line ministries. In particular, the problems of allocational rigidity, overspending and arrears, which according to the analysis in this paper are at least partly caused by the weak position of line ministries in the budget process, are in the Netherlands largely overcome.⁵ Slovenia and Croatia were chosen because they can be seen as countries that are relatively advanced in the area of budget reform within the region.⁶ This offers a certain assurance that conclusions drawn from comparison with the Dutch case have a wide relevance for other countries in the region.

The paper is structured as follows.

Section 1 describes the typical organization and task package of the Finance Directorate of a line ministry in Croatia and Slovenia. Naturally, there are marked differences between the two

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² The Public Expenditure and Financial Accountability (PEFA) surveys of the World Bank contain little information on the role of line ministries. The OECD Budget Reviews of the countries in the region (Kraan & Wehner 2004; Kraan et al. 2006; Kraan, Bergvall & Hawkesworth 2007; Kraan et al. 2010) pay some attention to the internal budget process in line ministries but on a quite general level (not more than half a page in each review). The IMF Fiscal Affairs Department has traditionally focused its country reports as well as some comparative papers on the role of the Ministry of Finance (see e.g. Olden et al. 2012).

³ The project was financed by the World Bank’s SAFE Trust Fund.

⁴ The question list is available upon request.

⁵ The role of line ministries in the budget process in the Netherlands is very similar to that of line ministries in Denmark, Sweden and Norway. In this light the Dutch model can be seen as representative for small North European countries.

⁶ In addition, the practical consideration that the CEF is in Ljubljana and close to Zagreb played a role.

countries and between the line ministries in each country. The description leaves these differences aside and focuses on the common denominators: the organisational features and task package that occur in each case. *The picture that arises from this description is that of the Finance Directorate as the financial administration of the line ministry.*

Section 2 focuses on a number of organisational features and task package of a Finance Directorate of a line ministry that are common in the Netherlands, but not in Croatia and Slovenia. *These features, which come in addition to those of a financial administration, characterise the Finance Directorate of a line ministry in the Netherlands as the “concern controller” of the ministry.*

Section 3 explains why the role of the concern controller is important to prevent allocational rigidity, overspending and arrears.

Section 4 concludes the paper and explains a number of next steps that could be taken by countries in the region to strengthen the position of their line ministries in public financial management. These steps do not involve major revisions of the Budget Code or other formal regulations, but rather pragmatic measures that can be implemented on a short notice, as soon as there is basic consensus among politicians and senior civil servants that strengthening the role of line ministries in public financial management is a worthwhile reform. This section also mentions the major challenges that SEE countries may have to face and overcome if they want to implement these reforms.

SECTION 1

THE CURRENT ROLE OF
THE FINANCE
DIRECTORATE OF LINE
MINISTRIES
IN CROATIA AND
SLOVENIA

The Finance Directorates in Croatia and Slovenia have 10 to 30 staff members; depending on the size of the budget of the line ministry and the nature of the policy instruments used by the ministry (for instance investments are more complicated than salaries). However, Finance Directorates sometimes include divisions that are connected to the specific task package of the ministry (for instance a division for EU funding of a ministry for infrastructure) or that in other countries are organised outside the Finance Directorate (for instance a procurement division). The staff that is responsible for budget preparation and execution inside the line ministry can be estimated at 15 employees at most.

Budget preparation proceeds mostly according to the calendar set out in the Budget Act. In Croatia there is only one budget circular. It sets ceilings to the expenditure envelopes of ministries and first-level budget users. Based on the Amendments to the Budget Act of January 2015, it should be sent out by August 15. However, the legal submission dates have not always been observed in the past.⁷ The envelopes (expenditure framework) are set by the Government on the basis of a proposal of the Ministry of Finance. The Amendments to the Budget Act set out for separate ceilings for current policy (expenditures arising from currently applicable regulations) and for new policy (expenditures arising from the introduction and implementation of new or changed programmes or activities). The decision on the framework is informed by the spring macroeconomic forecast and fiscal targets for the medium term. In the last few years these targets have aimed at the reduction of the budget deficit to the limits set by the EU. There is no systematic exploration of neither tax alternatives nor new spending or savings options prior to the decision on the expenditure framework.⁸

In principle, fiscal policy in Croatia is based on sectoral strategic planning of the ministry. The strategic plans are products of the sectoral directorates of the line ministries which are loosely coordinated by the Finance Directorate of each ministry. These plans are the basis of the “National Reform Program” and the “Convergence Program of the Republic of Croatia”. These documents are drafted by the Ministry of Regional Development and EU Funds and the Ministry of Finance, respectively. They are the main planning documents at the national level and serve simultaneously as Croatia’s submissions to the European Semester procedure of the European Union. The role of the sectoral plans in the setting of the ministerial ceilings is not transparent. It must be assumed that there is an informal negotiation process between the line ministers and the Minister of Finance and a role for the Government in the final decision, but this process is entirely political and informal and leaves no paper trail. Once the ceilings are set, they are inserted in the ICT system for budget preparation. Since the system does not accept budget proposals in excess of the ceilings, these proposals can only be put forward if first the ceilings are raised. However, it seems possible for the line ministries to negotiate a ceiling increase after the ceilings have initially been set.

In Slovenia the first budget circular should arrive by 15 May, but in the last few years it has arrived only in June or July. This may be due to changes of Government or fiscal emergencies related to the global financial crisis. The circular includes ceilings for expenditure envelopes of ministries and selective direct budget users⁹ (expenditure framework), decided by

⁷ In 2014 there was no circular, only a list of ceilings, which came in October.

⁸ However, following up on an EU recommendation, Croatia has started with a spending review procedure as of December 2014.

⁹ A selective group of direct budget users have their own ceilings, namely 38 (including 14 ministries) out of 168.

the Government on the proposal of the Minister of Finance. The ceilings are based on the spring macroeconomic forecast (produced by the Institute of Macroeconomic Analysis and Development, IMAD) and targets for deficit reduction. There is no systematic exploration of tax alternatives and spending or saving options prior to the Government decision on the ceilings.



Slovenia has also medium-term sectoral plans and a government-wide medium-term planning document “State Development Priorities and Investments”¹⁰, which in turn are based on a long-term (at least 7-year) Strategy of Development. These planning documents are inputs for the Government decision on the expenditure framework. Like in Croatia, the negotiation process prior to the setting of the ceilings is entirely political and informal. Budget submissions in reply to the first budget circular must comply with the ceilings at the moment they are confirmed. Before that moment they can exceed the ceilings (estimated by one finance director as 25% higher than the ceiling on average). However, the ceilings in the first budget circular are not definitive and negotiations in August or September may change them.

Normally the submission of proposals in accordance with the ceilings is a precondition for the start of the negotiations, which gives the Ministry of Finance a reversion level advantage in the negotiations. Negotiations proceed first at the level of civil servants, then at the level of ministers and the government, leading to a final decision on the ministerial ceilings and possibly on major programmes and sub-programmes in September. These final ceilings are communicated in the second circular to the line ministries. The line ministries have then to fill in the budget, while respecting the final ceilings.

Slovenia has a two-year budget, but an annual budget process. This implies that the budget proposal that the Government annually submits to the Parliament is formally the proposal to change the budget for the next year and to establish the budget for the subsequent year.¹¹

¹⁰ The State Development Priorities and Investments include the National Reform Programme, which aims to ensure the connection with the EU 2020 Strategy and the Stability and Growth Pact (CEF 2014).

¹¹ There is little difference between the policy relevance of the estimates for the second year of the Slovenian budget and that of the multi-annual estimates at line item level in other countries. However, apart from investment expenditures, Slovenia has no

In Croatia and Slovenia the Finance Directorates of the line ministries coordinate the internal budget process. However, the competence of the Finance Directorate is mostly limited to the ministry as a direct or first-level budget user. In all countries of the region central government ministries and agencies can be divided in direct or first-level and indirect or second-level budget users. Direct/first-level budget users have their own financial administration. During budget execution, they can incur commitments and order payments, subject to the approval of the Treasury. Although they may be formally subordinated to ministries, in practice they have substantial fiscal autonomy.

In Croatia and Slovenia there is a substantial number of direct/first-level budget users outside the line ministries (in Croatia there are 20 ministries and 27 other first-level budget users; in Slovenia there are 14 ministries and 154 other direct budget users). In Croatia all first-level budget users have their own expenditure ceiling and negotiate their ceiling directly with the Ministry of Finance. In Slovenia only the “proposers of financial plans” have their own ceiling which they negotiate directly with the Ministry of Finance. This includes 38 direct budget users, of which 14 ministries. Indirect/second-level budget users also have their own financial administration. They submit their budget requests to the line ministry and do not have their own ceilings. Their autonomy is limited to budget execution, in that they can make commitments and order payments, subject to the Treasury’s approval.

In Croatia and Slovenia the sectoral directorates of line ministries are not budget users. Although in practice the sectoral directorates are held responsible for their part of the ministerial budget, formally there is only one budget user in the ministry, namely the minister, and only one financial administration, namely the Finance Directorate of the line ministry. Sectoral directorates bring their wishes to the attention of the minister orally or by submitting notes. Competing wishes may be discussed in the Ministerial Board. Next to the minister, the Board typically consists of the deputy and assistant ministers, the sectoral directors, the permanent secretary, the legal advisor and the finance director. The role of the finance director is limited, because the sectoral directorates prefer to plead their causes directly with the minister. The minister ultimately decides on the submission of the request estimates to the Ministry of Finance (and, in Croatia’s case, on the proposal to the Ministry of Finance to increase the ceiling).

The main task of the Finance Directorate of line ministries in Croatia and Slovenia is the management and execution of the financial administration for the ministry. Both countries make use of an integrated ICT system for budget execution and accounting (SAP in Croatia, MFERAC in Slovenia). Incoming invoices are recorded and sent to the sectoral directorates to check whether the goods are delivered. After approval of the sectoral directorate, the invoices are sent to the Ministry of Finance for payment. The Ministry of Finance (in Croatia the Treasury, in Slovenia the Directorate for Public Accounting) conducts checks on the payment orders, including the availability of sufficient budget (cash control). Large payments require prior recording of commitments and approval by the Ministry of Finance (commitment control). Consolidation of accounts and financial reporting to the Parliament and international organisations is in both countries a task of the Ministry of Finance but the Finance Directorate of

medium-term estimates in the budget submitted to the Parliament. So, apart from investment expenditures, medium-term estimates for the second and third out-year are not included in the budget or the budget documentation.

line ministries can consult the ICT system at any moment to obtain information about the execution of their budget.

In both countries there is a Single Treasury Account. Cash management (ensuring sufficient cash balances on the accounts of all budget users and minimal volatility in cash buffers) is a task of the Ministry of Finance (in Croatia the Treasury, in Slovenia the Public Payments Administration). Cash management is mainly conducted on the basis of historical cash patterns, but the Finance Directorates of line ministries are required to announce demands for cash in quarterly and monthly cash plans.

SECTION 2

THE ROLE OF THE
FINANCE DIRECTORATE
OF A LINE MINISTRY IN
THE NETHERLANDS

Whereas financial administration is the core task of the Finance Directorate of line ministries in Croatia and Slovenia as well as in the Netherlands, in the latter country the Finance Directorate carries out a broader task which can be denoted as that of “concern controller”. This task consists of two additional components: (1) internal fiscal policy coordination, and (2) ensuring budgetary discipline. These require additional capacity. The Dutch Finance Directorates are larger than in Croatia and Slovenia not only because the budgets they manage are larger, but also because they carry out additional tasks. The size of the Finance Directorate in a line ministry in the Netherlands varies between 30 employees for small ministries to 100 for larger ones.

Internal fiscal policy coordination in the Netherlands

Internal fiscal policy coordination focuses on the internal trade-off between new policy initiatives of sectoral directorates, as well as on the trade-off between current policy and new policy initiatives. This coordination is required before and after the annual updating exercise of the ministerial ceilings.

Ceilings for ministerial envelopes are set for four years at the beginning of a cabinet period. However, although aggregate central government expenditure is fixed, reallocation between ministries, and between the ministries and the social security funds, is possible from year to year.¹² For this reason the annual budget process starts with an updating exercise of the ministerial ceilings. This leads to a decision of the Council of Ministers on the updated framework in May or June. This is not very different from the annual ceiling setting exercise in Croatia and Slovenia, apart from the fact that the aggregate central government ceiling in the Netherlands is fixed.

In the Netherlands there are only ceilings for budget chapters (basically ministries) and for the social security and health funds. All arm’s-length and independent agencies, regardless whether they have legal personality¹³, are financed by line ministries and their budgets are included under the ministerial ceilings. There are thirteen ministerial ceilings (one for each ministry) and two ceilings for the social security funds (one for social benefits and one for public health).

The Dutch ceilings are binding (formally and factually), so that the size of the ministerial envelopes is fixed after the decision on the ceilings. In the “single decision moment” of May or June all relevant trade-offs have to be made. To make this possible, the decision must be informed by the latest expenditure and revenue forecasts on the basis of current policy as well as by options for new expenditure and revenue policies. For this purpose the Ministry of Finance invites the finance director of line ministries to submit proposals for new policies in “policy letters” around February/March. The finance director coordinates these letters on the basis of contributions from sectoral directorates.

¹² In addition, European requirements concerning the EMU balance may lead to temporary downward adjustments of the aggregate ceiling.

¹³ Budgets of agencies with legal personality are included in the ministerial budget on a net basis. These agencies can have their own revenue that is not included in the budget.

After the ministerial ceilings have been set, Dutch line ministries are largely free to reallocate resources within their envelope as they see fit, as long as the ceilings are respected. Since, at the moment the ministerial ceilings are set, the sum of baseline estimates (reflecting current policy) is often close to the ceiling or even in excess of that, especially in the recent years of the global financial crisis, room for new policies has to be found by savings on



current policy. The finance director coordinates this process, consulting closely with sectoral directorates to learn about urgent needs and options for savings. The minister plays a crucial role in this process, since the finance director will only be able to find savings if the minister insists on the priority of new spending initiatives. This process ends with the submission of the final estimates at the line item level to the Ministry of Finance in July.

In order for the finance director to serve as the coordinator of internal fiscal policy and neutral advisor to the minister, it is important that the sectoral directorates be formally recognized as the financial managers or “budget holders” of the line ministry. In the Netherlands there is a “mandate decree” in every line ministry that identifies the budget holders (mostly directors-general of sectoral policy) and specifies their authority to delegate financial authority to lower levels in the administration. Each budget holder is in charge of one or more programmes, as specified in the budget law, and responsible for defining the objectives of the programme and collecting information about outputs and outcomes. Budget holders have a broad responsibility for operational management: not only financial management, but also human resources management, ICT management, etc. The budget holders can incur commitments and are ultimately responsible for their budgets. For that purpose they have their own financial administration, apart from the central ministerial administration. In this respect the budget holders resemble the direct/first-level budget users in Croatia and Slovenia. However, budget holders do not have their own ceilings and submit their budget requests to the line minister, not to the Minister of Finance. Since a few years, commitments no longer need the approval of the Finance Directorate.¹⁴ Incurring commitments is now the sole responsibility of the budget holder. Invoices are transmitted to the Finance Directorate, which orders payment. The financial administrations of sectoral directorates are sometimes merged in a shared service directorate of

¹⁴ This implies that the Netherlands is no longer a country with “decentralised commitment control” (Radev & Khemani 2009). It is rather a country with no commitment control. The abolition of commitment control was decided in view of the fact that in practice it never occurred that budget holders made commitments in excess of budget appropriations (current year) or commitment limits (future years).

operational management, inside the ministry but outside the Finance Directorate, or even in an inter-ministerial service centre outside the ministry.

In the Netherlands the incentive to produce good savings proposals to make room for new spending initiatives arises from the binding character of the ministerial ceilings. If in a country the ministerial ceilings/targets set at the start of the budget process are negotiable, the line ministry and its Finance Directorate tend to focus on the negotiation process with the Ministry of Finance in order to get the ceiling/target raised. *Any internal exploration of savings options will be avoided or conducted in high secrecy, because if it became known, it would fatally weaken the negotiation position vis-à-vis the Ministry of Finance.* If the negotiation process with the Ministry of Finance continues until shortly before the submission of the budget to the Parliament, the attention for internal savings options, and thus for new spending initiatives financed by such savings, almost disappears. This is to a large extent the case in Croatia and Slovenia. This mechanism explains the relative rigidity of the internal allocation of resources and the lack of policy innovation that is characteristic of Croatian and Slovenian line ministries.¹⁵

In the Netherlands policy evaluation is an important instrument of the line ministry to assess the quality of its policies and to provide a basis of reform. Policy evaluation focuses on fundamental questions beyond the day-to-day monitoring of outputs and outcomes,¹⁶ such as: Why is this programme a task of central government, rather than of the market or local government? What does each policy instrument in the programme cost? What alternative policy instruments could be used to achieve the programme objectives? What would happen if the policy instrument or the entire programme was abolished? What would be its effects on objectives and savings?

The finance director must see to it that all programmes of the ministry are regularly evaluated and make sure that the evaluation of programmes that run into problems (doubtful results, overspending) gets priority. It is sometimes said that evaluation cannot be critical if it is initiated and funded by the line ministry, since the line ministry has no interest in critical reports about its own programmes. This is true if evaluations are imposed by rigid regulations or by the Ministry of Finance. However, it is not true if evaluations are used by the line ministry itself to improve its policies and to make room for new policies.¹⁷ This does not mean that the Ministry of Finance should abstain from general rules about evaluation. On the contrary, these rules provide a quality guarantee that makes the instrument easier to use for the line ministry because it eliminates the need to invent such rules anew at each occasion an evaluation is initiated. If the evaluation is outsourced, the procurement process should comply

¹⁵ The same mechanism explains why it is so difficult to get good savings options on the table when the Dutch expenditure framework is established at the occasion of the cabinet formation. The Dutch “spending review” procedure was largely invented to get such savings options formulated and elaborated outside the regular budget process under the supervision of the Ministry of Finance.

¹⁶ Furthermore, it is now recognized in the Netherlands that for some programmes it is not possible to define sensible quantifiable indicators, and that such indicators, if they can be defined, may induce perverse effects if they are used for sanctioning of performance (Ministry of Finance 2011).

¹⁷ For this reason it is important to make a difference between evaluation and spending review. Evaluation has a broader objective than finding efficiency savings. Evaluation is a stage in the policy cycle that is aimed primarily at improving policy. It is essential that the line ministry has control over evaluation, both the selection of topics and the terms of reference. Spending review is a financial management tool of the Ministry of Finance to get saving proposals on the table, with or without the co-operation of the line ministry.

with criteria of objectivity. The supervisory committee should include external experts.¹⁸ Terms of reference and reports should be published, possibly together with a statement of the policy follow-up.

Ensuring fiscal discipline in the Netherlands

The second component of the task package of the Finance Directorate as “concern controller” regards budgetary discipline. In the Netherlands budgetary discipline is much stronger than in Croatia and Slovenia, and this difference is mostly due to the role of the Finance Directorate of line ministries.

The basis for the maintenance of budgetary discipline is the separation of expenditures for current policy and new policy. In the Netherlands the expenditure estimates at the line item level for current policy are included in the ICT system for budget preparation (IBOS).¹⁹ These “baseline” estimates for the current year, the upcoming budget year and five out-years, are updated regularly (7 or 8 times per year) in the light of cost developments (inflation, salaries, variation in the input mix) and demand for entitlement services (social benefits, education, health, etc.).²⁰ In addition, the baseline estimates are adjusted for new policies and savings. Each year, in the October update, the baseline estimates are extended with an additional last out-year ($t + 5$, t being the upcoming budget year).

Baseline updates regard primarily the upcoming and current budget year, but have repercussions on future years. Budget numbers are by nature changing continuously in reaction to external circumstances. Costs of programmes change, political preferences shift, project preparation accelerates or takes more time than expected. This regards in the first place the upcoming and current budget year. In the Netherlands these changes have to be registered in the IBOS system. Baseline updates after the start of the budget year have to be authorized in supplementary laws. Supplementary laws are submitted to the Parliament twice a year (in spring and autumn). There is no separate system for budget execution. Moreover, all changes in the upcoming and current budget year have consequences for future years, mostly through extrapolation. All these changes have to be inserted in the IBOS system and have to be approved by the Ministry of Finance. *As a consequence of regular updating, the Dutch authorities can avail, at any time, of a complete picture of the future costs of current policy as a basis for fiscal decision-making.*

In the Netherlands the Ministry of Finance has formulated an extensive set of “rules of budgetary discipline” which are updated and approved by the Council of Ministers at the start of each cabinet period. The essence of these rules can be summarized as follows.

- Ministers are responsible for avoiding overspending on ministerial ceilings, regardless of the cause of overspending.

¹⁸ The Dutch evaluation rules do not prescribe participation of the Ministry of Finance in the supervisory committee since this may have an adverse effect on the use of the instrument.

¹⁹ In the Netherlands there are relatively few line items: some 160 in the state budget as a whole and on average 12 per ministry. In Croatia and Slovenia there are more than 1,000 line items, but this difference does not preclude progress towards better recording of baseline estimates and better budgetary discipline.

²⁰ The budget and in-year reports to the Parliament contain estimates for four out-years. IBOS contains one more out-year.

- Changes of baseline estimates have to be marked in the IBOS system as either “autonomous” or “policy”. Autonomous changes occur without policy change as a consequence of cost developments, or a change in demand for entitlement services. The Minister of Finance can issue rules for autonomous changes (for instance, concerning inflation and wage costs). Policy changes occur as a consequence of the implementation of new policy instruments or the reform of existing policy instruments (often requiring a change of law or regulation).²¹ Upward adjustment of baseline estimates has to be compensated by policy measures (apart from those made possible by the annual revision of the ceilings), regardless of whether they arise from autonomous or policy changes (the so-called “specific compensation”). This implies, among other things, that overspending on entitlement benefits as a consequence of changes in demand is subject to specific compensation, either by change of the entitlement law or by measures on other programmes for which the Minister is responsible. Compensation applies to all years (the current year, the upcoming budget year and all out-years). This means, for instance, that a baseline increase in year $t + 2$ has to be compensated by measures that will impact the budget of year $t + 2$.
- Autonomous increases (set-backs) can be compensated with autonomous decreases (windfalls) but policy increases cannot be compensated with autonomous decreases. In other words: windfalls cannot be used to finance new policies; new policies must be financed by savings on existing policies.
- On the proposal of the Minister of Finance, the Council of Ministers can decide that an autonomous or policy increase is compensated by another ministry or a social security fund (“general compensation”).

The rules of budgetary discipline apply to budget preparation as well as to budget execution. Compensation has to be provided before and after the budget year has started at each update of the baselines. In this sense budgeting is a permanent process in which the distinction between budget preparation and budget execution has lost much of its relevance.²² The IBOS system is the central ICT system that is used permanently throughout budget preparation and execution.

At each occasion of baseline updating the Inspectorate of Finance (Expenditure Division) of the Ministry of Finance has to approve the changes in the baseline estimates. The proposed changes are inserted by the Finance Directorates of the line ministries in the IBOS system at the line item level. Each new line item level estimate for each year (current year, upcoming budget year, out-years $t + 1$, $t + 2$, $t + 3$, $t + 4$ and $t + 5$) has to be approved by the responsible inspector (the budget analyst in the Expenditure Division responsible for the expenditure programme).

The inspector checks:

- Whether the change is reasonable, given the underlying cause of the autonomous change or the new policy measures put in place; in case of a policy change, also whether the estimates

²¹ Not all policy instruments require a legal change for their implementation. For instance, an investment in road construction project generally does not require a law or regulation.

²² In fact, the baselines tend to change more before the start of the budget year (during “budget preparation”) than after that moment (during “budget execution”). It can therefore be said that the rules of budgetary discipline are more relevant for budget preparation than for budget execution. Once the budget year has started, changes of baselines become rarer and have to be approved by the Parliament in supplementary budgets.

are consistent with the information about fiscal consequences provided when the substantive policy was decided.

- Whether the change is correctly marked as “autonomous” or “policy”.
- Whether in case of upward changes sufficient specific compensation is proposed to fully compensate the increases (apart from any increase made possible by the annual revision of the ceilings).
- Whether the proposed changes comply with the rule that windfalls are only used to compensate for set-backs, not to finance new policy.

In case that a change is not approved, the matter is referred to higher levels in the hierarchy, up to the ministers.

The finance director is responsible for budgetary discipline and has to make sure that the updates of the baselines are accepted by the Ministry of Finance and do not lead to escalating conflicts. For this purpose it is important that the finance director follows closely the development of the sectoral budgets and consults timely with sectoral directors in case of any adverse developments. Once the budget year has started, the finance director follows the execution process and consults with the sectoral directors as soon as any threat of overspending appears. In the first months of the budget year it is often still possible to take corrective measures in a programme that spends too fast, or to implement savings measures in other programmes to offer compensation.

Maintenance of budgetary discipline is a much broader task than expenditure control (checking whether there is sufficient budget for a commitment or a payment). In the Netherlands commitments were subject to approval by the Finance Directorate until a few years ago. Currently the responsibility for incurring commitment rests exclusively with the budget holder. Invoices are sent to the Finance Directorate, which checks with the budget holder whether the goods are delivered. The Finance Directorate is responsible for timely payment. This procedure implies that there is a formal check on the availability of budget when a commitment is paid (not when it is incurred), but this is not at all the most important instrument of expenditure control. In fact, it never occurs that a budget holder makes a commitment for which there is no budget.²³ *The essence of budgetary discipline is rather the timely correction of policies that otherwise would lead to overspending and the finding of compensatory savings in case that policies cannot be corrected anymore or are seen as spending priorities in spite of lacking budgets by the political leadership.* For several ministries (social security, public health, education) this task mostly comes down to the management of major entitlement programmes in close consultation with the sectoral directorates.

In the Netherlands, the Parliament not only authorizes cash expenditures for the upcoming budget year, but also limits of commitments to be incurred in the budget year for out-years. These limits are specified at line item level. This means that budget holders, while making commitments for future years, have to comply with the commitment limits of the budget law. In Croatia and Slovenia, similar constraints on commitment for future years are in place (Art. 51 of the Public Finance Act of Slovenia and Art. 44 of the State Budget Act of Croatia). However, in

²³ Committing without budget is a criminal offense like in Croatia and Slovenia.

several other countries in South-East Europe there are no commitment limits for out-years in the annual budget law. This makes it impossible to check commitments for out-years against parliamentary authorizations, both for budget holders and for the Finance Directorate. This hole in the legislation should urgently be remedied in the countries concerned.

An additional advantage of decentralised expenditure control is that it avoids duplication and is more efficient. In the Netherlands, the state of budget execution is reported every month (12 times per year) to the Government's Bookkeeping Bureau (Rijkshoofdboekhouding) in the Ministry of Finance. Incurred commitments for out-years are reported once at the end of the budget year. Individual invoices are not seen by the Ministry of Finance and payment orders go directly from the Finance Directorate of the line ministry to the bank.²⁴ This applies as well to payment orders on the basis of permanent contracts such as salaries and public utility bills. Apart from the logic that expenditure control should be imbedded in the toolkit of the Finance Directorate as the main guardian of budgetary discipline (albeit as a relatively unimportant instrument; see paragraph '*Maintenance of budgetary discipline...*' on page 16), this procedure has the obvious advantage that it avoids double cash control (first by the Finance Directorate, second by the Treasury). Since the abolition of commitment control in the Netherlands, individual commitments are seen neither by the Ministry of Finance nor by the Finance Directorate of the line ministry, so that costs of commitment control are avoided entirely.

²⁴ In the Netherlands the Treasury Single Account is outsourced to a number of commercial banks. The balances are swept back daily into the account of the Treasury with the Central Bank. Negative balances are forwarded by the commercial banks (with interest). The Debt Agency of the Ministry of Finance is responsible for a sufficient balance on the Treasury Single Account with the Central Bank for the daily liquidation of all positive and negative balances on the accounts with the commercial banks. For this purpose payment orders of more than 20 million euro, that have not been announced in the cash plans, must be announced to the Ministry of Finance some days in advance of the payment order to the bank.

SECTION 3

WHY STRENGTHENING THE ROLE OF LINE MINISTRIES SHOULD BE A PRIORITY OF INSTITUTIONAL REFORM

Strengthening the role of line ministries in the budget process (becoming a “concern controller”) may yield benefits in two areas: **more flexibility and better budgetary discipline.** In order to react rapidly to changing social and economic circumstances without jeopardising deficit and debt objectives, it is necessary that line ministries avail of the tools to free up resources in existing programmes and steer them in the direction of new policy initiatives. In order to ensure budgetary discipline, it is necessary that line ministries avail of the tools to control the expenditures of existing programmes, including allegedly “inflexible” entitlement programmes and programmes under the authority of “direct/first-level budget users”.

Strengthening the role of line ministries requires better tools, not better efforts or expertise. Budgetary rigidity and lack of budgetary discipline, which are characteristic for a number of countries in South-East Europe, cannot be attributed to a lack of effort or expertise on the part of line ministries. There is no reason to presume that in general there is something wrong with the quality of human resources in line ministries or in the Finance Directorate of line ministries. Of course, upgrading human resources through training can in many cases contribute to better results, but this is equally true for the Ministry of Finance. What is needed in the first place is improvement of tools: in particular changes in procedures and organization. These changes can only come about with the support of the Ministry of Finance and the government. Even if it concerns changes that the line ministry can decide for itself, the effects will be dependent on government cooperation.

More flexibility

It has often been observed that the allocation of resources in public budgets is quite resistant to change.²⁵ The stakeholders of each programme will try to extend their budget, and will not give up on any increase that they have ever obtained. The stakeholders include the iron triangle of (1) the budget holder, (2) the clients of the programme and their pressure groups, and (3) parliamentarians with grassroots support among clients. If there are no new resources for a ministry and savings on current policies are effectively blocked, new policies cannot be funded and become less likely. However, as argued above, the presence of binding ceilings for the ministerial envelope is conducive to the implementation of savings measures. So is the prevalence of a culture of policy evaluation. If the conditions in these areas are met, the efforts of the Finance Directorate determine to a large extent whether change will actually occur.

The finance director has a unique perspective on the priorities of the minister and the possibilities for savings. The finance director knows in which programmes there is room for cuts without dramatic consequences and which programmes have doubtful results that require critical evaluation. Next to binding ceilings and more emphasis on evaluation, the capacity of the Finance Directorate of the line ministries is a critical factor for the flexibility of the budget, namely the extent to which it can rapidly be adjusted to changes in social and economic circumstances through policy reform.

²⁵ Wildavski (1964) based his theory of budgetary incrementalism largely on this observation.

Better budgetary discipline

Many countries in the region, including Croatia and Slovenia, have been struggling with high budget deficits. Permanent high deficits in turn lead to high public debt. High deficits can have several causes, including too optimistic revenue forecasts and too lax deficit targets. However, other causes being equal, the Finance Directorate of the line ministry can make a difference. In particular the finance director can make sure that the costs of current policy are estimated in a realistic way, namely not too low, thus triggering savings measures if ceilings are exceeded. Of course, it is the minister who ultimately decides, but it is the task of the finance director, as a neutral expert, to explain the risks of too low cost estimates. Furthermore, the finance director can contribute to budgetary discipline under changing economic and social circumstances, timely proposing corrections to policies that cost too much and finding savings in low priority areas to compensate for overspending on high priorities.



Another recurrent problem in the area of budgetary discipline is that of arrears.²⁶ Arrears can have five causes: (1) deficient cash or debt planning; (2) lack of commitment constraints, especially for out-years; (3) insufficient funding of entitlement programmes (health, education, social benefits) and permanent contracts (utilities, salaries); (4) in-year downward budget revisions; and (5) delays or deliberate deferrals in processing payments.²⁷ Cause (1) concern failures of the Ministry of Finance and must be remedied by reforms in that ministry. Cause (2) is mostly relevant for countries that lack commitment limits for out-years in the annual budget

²⁶ The problem is largely overcome, although not entirely, in Croatia and Slovenia, but still very common in other countries in the region.

²⁷ The IMF uses a slightly different typology of causes (Flynn & Pessoa 2014), which includes “formulation of unrealistic budgets” and “inadequate sanctions” (against officials who fail to comply with the law). However, the latter causes are of a somewhat different order than the other causes (they cannot lead to arrears independently from the other causes).

law and should be remedied by introducing such limits.²⁸ This too is a responsibility of the Ministry of Finance. **As to the other causes of arrears, the finance director of the line ministry has a crucial preventive role. As to cause (3) of arrears (insufficient funding of entitlement programmes and permanent contracts), finance directors must see to it that all commitments are adequately covered by the budget.** Sectoral directors have a tendency to underestimate the costs of entitlement programmes (social security, health, education) in order to avoid triggering savings measures. The same is true for permanent contracts (salaries, utility services). It is a task of the finance director to counter this tendency and insist on realistic estimates, even if this triggers compensation measures.

As to cause (4) of arrears (in-year downwards budget revisions), finance directors have to ensure that savings are distributed over the programmes of the ministry in such a way that commitments that have already been incurred are not affected. Naturally in-year budget revisions driven by fiscal policy, especially to compensate for tax revenue set-backs, must be avoided in the first place. This is a task of the Ministry of Finance that should use conservative economic forecast or apply a prudence margin of 1 or 2 percentage point GDP, and choose an ambitious deficit target (preferably a surplus target) in order to avoid the need for any in-year adjustments. However, if this is not done to a sufficient extent, and in-year adjustments become necessary anyway, then finance directors must ensure that existing commitments are not affected to avoid a lack of funds for the payment of invoices.

As to cause (5) of arrears (delays or deliberate deferrals in processing payments), finance directors must avoid such delays. For this purpose it is important that all incoming invoices are provided by the internal post unit of the ministry with a date stamp and directly transferred to the Finance Directorate (regardless whether the invoice is addressed to somebody else, for instance to the sectoral directorate). This is automatically ensured if a line ministry moves to e-invoicing. The Finance Directorate should handle payment of invoices and permanent contracts according to a standardized procedure with fixed dates for each step in the procedure.²⁹

²⁸ Commitments may lead to arrears if they are not covered by the budget. This may have two causes: no commitment limits for out-years in the budget, and no preventive check of commitments with the budget for the current year and with commitment limits for out-years. In the countries of South-East Europe the first cause is more important than the second.

²⁹ See Flynn & Pessoa (2014) for an overview of ultimate payments dates for different kinds of liabilities.

SECTION 4

STRENGTHENING
THE ROLE OF LINE
MINISTRIES:
NEXT STEPS

In order for the Finance Directorate of a line ministry to evolve as a concern controller a number of reforms are necessary. Some of these reforms require minor legislative change, in particular of the Budget Code and its by-laws. Others require measures or guidance from the Ministry of Finance, and still others can be undertaken by the line ministries themselves. To strengthen the role of the Finance Directorate of the line ministry as internal fiscal policy coordinator, it is important that (a) the budget preparation calendar is moved forward, (b) sectoral directorates are recognised as budget holders, and (c) a standard evaluation procedure is introduced. To strengthen the role of the Finance Directorate of the line minister as guardian of fiscal discipline, it is important that (d) expenditures estimates of current policy (baselines) are regularly updated and approved by the Ministry of Finance, (e) rules of budgetary discipline are established, and (f) the line ministry works in close coordination with the Ministry of Finance.

Moving the budget calendar forward

Ceilings can only acquire a binding character if the entire budget preparation process is moved forwards. Ceilings do not become binding by simply declaring that they cannot be changed. Line ministries rightly demand that budget preparation procedures allow them to negotiate their requests with the Ministry of Finance. It is not realistic to conceive “top-down budgeting” as just imposing ceilings, while denying line ministries the opportunity to plead for new policies with the Ministry of Finance.

The introduction of binding ceilings must rather be conceived as moving the budget calendar so far forward that meaningful budget negotiations can take place before the decision on the ceilings is taken. This requires that:

- The annual budget preparation process starts with an invitation to the line ministries to put forward their proposals for new policy initiatives with detailed cost estimates in a policy letter around March.
- The line ministries have an opportunity to discuss their proposals with the Ministry of Finance in April and May.
- The decision on the ceilings is taken in June by the Council of Minister on the proposal of the Ministry of Finance.
- The decision on the ceilings is informed by all required sets of data in a transparent way so that line ministers have a fair opportunity to discuss all possible trade-offs; next to the proposals for new policies, the sets of data must include the latest tax revenue forecasts, the latest updates of current policy estimates, savings options and tax options, and the deficit targets for the budget year and out-years.³⁰
- The Ministry of Finance makes it absolutely clear that it will not allow any adjustment of the ceilings after they have been decided; the ICT system should prop up this commitment by not allowing the insertion of budget estimates that exceed the ceilings in July or later.

³⁰ As long as the ceilings are not set, savings options usually have to come from the Ministry of Finance, because line ministries have little incentives to put forward good savings options before the decision on the ceiling is made. Spending reviews are a good instrument for the Ministry of Finance to develop savings options with inputs from line ministries, but without line ministries dominating the process.

Moving forward the budget calendar is not an easy reform, since politicians tend to postpone difficult decisions. However, this reform is increasingly supported by European regulations, including those connected to the European semester, which require reporting about the main outlines of the budget before the summer. These regulations are formally binding only for EU members, but since all countries in the region aspire to EU membership, they are still conducive to this reform.

Recognizing sectoral directorates as budget holders

For the Finance Directorate to play its role as a neutral fiscal policy coordinator it is important that sectoral directorates (or directorates-general) are recognised as budget holders. In practice directorates may already be responsible for the management of their budgets, but this is in many countries not formalized in any legal provision. Instead, the Budget Code often makes a distinction between direct/first-level and indirect/second-level budget users, and the ministry as a whole is defined as a single direct/first-level budget user, whereas certain arm's-length and independent agencies under the umbrella of the ministry are equally defined as direct/first-level budget users. For the Finance Directorate to play its coordinating role it is important that the responsibility of sectoral directorates for their budgets is formalized in a ministerial mandate decree.



Budget holders can make use of the Finance Directorate for their financial administration, but are entitled to incur commitments on their own authority and are responsible for managing their own budget.³¹ Mandate decrees can also specify that authority to incur commitments is delegated to certain officials inside the sectoral directorates.

Similarly, it is important that the ministerial ceiling covers all arm's-length and independent agencies under the umbrella of the line ministry and that these agencies are defined in the mandate decree as ordinary budget holders. This implies that they cannot have their own ceilings and cannot be allowed to negotiate their budgets directly with the Ministry of Finance. In practice this will come down to limitation of the number of budget users with their own ceilings (first level budget users in Croatia, direct budget users that propose financial plans in Slovenia) to the ministries. This is a major change in countries such as Croatia and Slovenia with large numbers of direct/first-level budget users outside the ministries.

³¹ Large budget holders can have their own financial administration.

Establishing an evaluation procedure

Evaluation is an important tool for the Finance Directorate in its role of internal fiscal coordinator. The Finance Directorate has to ensure that all sectoral programmes are regularly evaluated. In close coordination with the sectoral directorates it has to put up a planning schedule that indicates in which year each programme will be evaluated. Planning of evaluations should take into account the urgency of policy reform in view of changing social or economic conditions. Evaluations should be critical and provide input for policy reforms aimed at better results and savings through improved effectiveness and efficiency. It is a task of the Ministry of Finance to establish a regulation for evaluation that ensures quality (see paragraph ‘*In the Netherlands policy evaluation...*’ on page 13).

Updating baselines

In most countries of South-East Europe the inter-ministerial ICT system for budget preparation already includes the line item estimates for the current year, the upcoming budget year (t) and the out-years (t + 1, t + 2 and sometimes t + 3). However these estimates are not regularly updated and not maintained after the submission of the budget to the Parliament. What is essential for budgetary discipline is regular updating and maintaining the estimates on a permanent basis, while adding a new out-year at the start of every budget cycle. This will require certain adjustments to the ICT system, but not very large ones, since the systems already include the multi-annual estimates at the line item level. It is the task of the Ministry of Finance to adjust the ICT system. Moreover, the Finance Directorate of the line ministry has to reserve capacity to insert the regular updates in the system and the Ministry of Finance has to reserve capacity in its expenditure division to approve the updates. Updates have to take place at least three times per year:³² before the decision on the ceilings (in February), when the budget estimates are submitted to the Ministry of Finance (in June) and before the submission of the budget to the Parliament (in September).

Establishing rules of budgetary discipline

At the proposal of the Ministry of Finance, the Government should establish rules of budgetary discipline. These rules should make a distinction between expenditure estimates related to current policy and estimates related to new policy. Current policy estimates are subject to the prevailing updating procedures and need the approval of the Ministry of Finance at every update. Estimates related to new policy have to refer to a substantive policy change and, if applicable, to the law or by-law by which this change was implemented. The fiscal consequences of legislative proposals have to be specified in a standard form when the proposal is submitted for Government consideration, regardless at which moment of the budgetary cycle this occurs.³³

³² In the Netherlands they take place at least seven times per year, including once after the submission of the budget to the Parliament in connection with the second annual supplementary law (in November).

³³ In many governments, both in South-East Europe and in the OECD area, there have been attempts to co-ordinate proposals for new policy with the budget process. These attempts have mostly failed. The budget cycle does not coincide with the policy cycle, and the timing of decision-making on policy revision is determined by the urgency of reform and cannot be forced into the rigid annual budget cycle.

The estimates have to be assessed by the Ministry of Finance before the proposal is tabled for Government consideration. It is good practice that the fiscal consequences of large policy initiatives (changes in entitlement laws, infrastructural projects) are also assessed by the fiscal forecasting unit. The information provided should make clear how the proposal can be fitted under the prevailing ceilings for the first year of its implementation and all future years. If there is not enough room under the ceiling of any year after its implementation³⁴, the information should make clear which savings measures will be taken to compensate for the new spending. The only occasion when new policies can be proposed without reference to the existing ceiling is at the occasion of the policy letter in March, when proposals for new spending are an input to the decision on the ceilings.

Cooperation with the Ministry of Finance

The Finance Directorate can only fulfil its role as guardians of budgetary discipline if it works in close cooperation with the Ministry of Finance. This cooperation is the central axis of an effective budget process. While recognising the position of the finance director as an official of the line ministry and subordinate to its minister, it is essential for the Ministry of Finance to build trust with all finance directors and to make sure that no information which is important to them is withheld. An effective way to build such trust is to organise a periodical meeting with all finance directors, in which the Ministry of Finance provides oral information about the latest insights concerning the current budget year, including tax revenue and deficit projections, and about the upcoming budget year, including the latest ideas about the new ceilings in the light of macroeconomic forecasts, balance targets and tax options. The meeting can also be used to discuss process changes and to provide guidance (for instance on EU requirements for grants or loans).

Once such a practice of periodical meetings is established, budget circulars will never come as a surprise to the line ministries. The meetings could also be used by the Ministry of Finance to explain its policies and by the line ministries to bring suggestions to the attention of the Ministry of Finance. The meetings can be chaired by the budget director of the Ministry of Finance. The budget director should see to it that the meetings are used to exchange information. The aim is not to negotiate about budgets. Budget negotiations should take place bilaterally between the Ministry of Finance and the line ministry, first on the level of budget officials and eventually on a political level, not in the periodical meetings of the finance directors.

³⁴ The ceiling may already include a reservation for the new policy.

Summarizing, the next steps for the strengthening of the role of line ministries in South-East European countries, are the following.

For the Ministry of Finance

- Moving forward the calendar for budget preparation so that the ceilings for the ministerial envelopes are decided in June (possibly by adjusting the Budget Code for that purpose), while allowing an opportunity for meaningful bilateral negotiations with line ministries in April and May.
- Introducing a regulation for policy evaluation, ensuring that quality requirements are met.
- Adjusting the ICT system for budget preparation, allowing the regular updating of baseline estimates at line item level and ensuring that baselines are maintained on a permanent basis (not removed at the start of the next budget cycle).
- Reserving capacity in the expenditure division for approving baseline updates.
- Establishing rules of budgetary discipline, requiring that all upward baseline updates (apart from those made possible by the annual revision of the ceilings) are compensated and prohibiting financing of new policies with expenditure windfalls.
- Attributing the responsibility for cash control exclusively to the finance director of the line ministry (possibly by adjusting the Budget Code for that purpose).
- Organizing periodical meetings with the finance directors of line ministries to exchange relevant information and build trust.

For the line ministries

- Establishing mandate decrees that define the sectoral directorates as well as arm's-length and independent agencies, currently known as direct/first-level budget users, as budget holders that are responsible for their own budget and that are authorized to incur commitments.
- Tasking the finance director with regular evaluation of all ministerial programmes as a tool to stimulate policy innovation and savings.
- Reserving capacity in the finance directorates for regular updating of baselines in close coordination with the budget holders, including the identification of savings that can be used to compensate for upward adjustments.

The measures outlined in the previous paragraph do not require major legislative reforms. Most are relatively easy to implement and take relatively little time to prepare. The only exception is the moving forward of the budget calendar, which in most countries will become easier if it is supported by legislative change.³⁵ However, in spite of the relative simplicity of the separate steps to be taken, the policy package as a whole will in many countries be seen as a

³⁵ Change of the Budget Code may not be strictly required, since the dates in the Code are usually ultimate dates, so that moving completion dates forward is not prohibited.

major institutional reform. In this light it is essential that policy makers, both politicians and permanent officials, thoroughly discuss the merits of the reform as a whole and reach agreement on its implementation before any separate steps are taken. For this purpose it is also useful to start a policy dialogue in each country, as well as in regional fora, about the pros and cons of this reform.

The most important challenge that the reform may pose for a number of countries is that it changes the position of the finance director. The finance director remains an official of the line ministry but moves closer to the Ministry of Finance. Her/his position becomes more that of a mediator between the Ministry of Finance and the line ministry.³⁶ Some officials in the line ministry may start to perceive the finance director as a (secret) agent of the Ministry of Finance. Of course the finance director also needs the confidence of the line minister, but this confidence needs to be based on technical expertise and inside knowledge about current thinking in the Ministry of Finance, not on her/his political loyalty or support in the fight against the Ministry of Finance. This may be perceived as a profound change in some countries. Moreover, it is incompatible with the political appointment of the finance director. The finance director needs to be a permanent civil servant, selected on the basis of knowledge and experience and able to serve ministers of different political orientation. This consequence of the strengthening of the position of line ministries in the budget process has to be discussed before countries decide to embark on this reform.

Another challenge, which countries may have to face and overcome if they want to strengthen the position of the line ministries, is possible resistance in the line ministries themselves. Ministers and the top management of line ministries may pose the question what is in this reform for them. What do they gain by it? They may hesitate taking on them the responsibility for budgetary discipline in regard to the entire budget of the ministry if they feel that major entitlement programmes or autonomous direct/first-level budget users under the umbrella of the ministry cannot in fact be controlled by them. The reply to these hesitations is twofold. First the Ministry of Finance has to provide the finance directors with better tools to control the ministerial budget. Second, given that these tools are provided, the line ministry can also gain. In particular increased flexibility of the line ministry's budget will make it possible to implement more new policies. It will also make it easier for line ministries to implement structural policy reforms (reforms with major impact on the economy). *Since every minister and senior civil servant wants to put his/her stamp on policy, this must be seen as a big advantage.* In addition, better budgetary discipline will protect the ministry against criticism by other ministries, parliamentarians and the public about its management of the tax payers' money, regardless how justified such criticism is. This, too, must be seen as a substantial advantage by every minister of senior civil servant of a line ministry.

³⁶ In the Netherlands the appointment of the finance director of the line ministry needs the approval of the Minister of Finance. In fact, many finance directors have worked previously in the Ministry of Finance.

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ABOUT THE CEF

The CEF supports capacity development in public financial management and central banking topics for individuals and institutions. We do this by designing high-quality, practical and learning-centred specialization programmes and training events; by promoting networks of professionals; and by stimulating regional cooperation. We partner with multilateral and bilateral agencies, knowledge institutions, and peer organizations, and we tap the expertise of a broad range of individual experts.

The CEF's main beneficiaries are central banks and ministries of finance in South-East Europe. Upon their initiative, we have been extending our efforts to also strengthen capacities of budget officials at line ministries. In 2012, we cooperated with experts from the region in the Fiscal Impact of Structural Reforms project to better understand line ministries' role in countries' annual processes of budget preparation and medium-term fiscal programming, and how costs of structural reforms are incorporated. The project was financed by the SAFE Trust Fund of the World Bank; its outcomes have been published.

We have addressed the capacity development needs through a series of learning and networking activities within our project on Strategic Planning and Budgeting, which is EU-funded. For example, we developed new courses on the Integration of Structural Reforms into Fiscal Programming, and Budget Submissions of Line Ministries. Also, we integrate line ministries' needs in our budget preparation and execution course programme, and involve budget officials of line ministries in joint activities with counterparts from ministries of finance. We are further intensifying our efforts in this regard.

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