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OUTPUT MEASUREMENT IN THE SCOTTISH BUDGET

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Introduction

The publication of the new spending plans for Scotland (Scottish Executive 2004a) after the debate on Spending Review 2004 was greeted in journalistic and political circles as but the latest exercise in government spin. *The Herald*'s Scottish political correspondent (Gordon, 2004) inferred that the dropping of 138 targets was part of a Machiavellian exercise of control of information to cloud the process of accountability, and as greater transparency and efficiency in public spending was central to the rationale for targets, then clearly if correct, this was a major issue of public concern. The practice of target-setting by the Executive however, *requires* the reconsideration of targets in each Spending Review and their replacement as appropriate, whether by more relevant measures or to reflect new priorities. In this case, there was no presentational spin.

The New Labour version of performance measurement has its origins in the Clinton Administration adoption of the philosophy of governance advocated by Osborne and Gaebler (1993), known as 'Reinventing Government'. Performance information is now in widespread use in Europe and America, as "indispensable tools for improving management and accountability" (Forsythe, 2001), even though to date, there is greater evidence of the rhetoric of performance management than impact on resource allocation in reality. Performance information was first used in output budgeting reforms in the 1960s, and reinvented as part of the Conservative approach to value-for-money in the Financial Management Initiative of 1982, before being reformed again in New Labour's Public Service Agreements in 1998. The Treasury argument is that government should have transparent outcomes and targets, to relate inputs to the outputs and outcomes it seeks to achieve (Balls and O'Donnell, 2002).

It is perhaps worth pausing for a moment to clarify the difference between output measurement for budgetary purposes, from output measurement in the national accounts. The latter is mainly a tool of economic analysis which attempts to measure economic output. This is problematic for the public sector, as the conventional approach has been to equate the value of inputs with outputs. Put simply, government output is simply government expenditure.

The Atkinson Review (2004) has grappled with this convention, as it assumes there is no change in productivity, a particularly dubious assumption in a period of rapid technological change. This convention, particularly in conjunction with the practice of measuring growth of GDP in aggregate terms, (rather than per capita terms), makes the ongoing arguments about Scotland's poor relative economic performance of questionable value (MacLaren, 2003). As Atkinson notes, "the design of direct output measures needs considerable care" (p.10). Moreover, on crude output measures, decisions to improve the quality of services, e.g. reduced pupil/teacher ratios or patients per practice, will record lower output, which seems perverse if these lead to better outcomes.

Further, in part because of devolution, the new approach to measuring government output developed for the national accounts does not apply in Scotland, Wales and Northern Ireland. So with Government activity accounting for a large share of Scottish GDP, *any* comparisons on the current model will be open to challenge.

Atkinson has recognised that there are important differences of objectives in measuring output for budgetary purposes. Although there are similar problems of definition and measurement, measuring performance in government is a more complex task than measuring economic output and productivity, as spending programmes are concerned with effectiveness and equity as well as efficiency.

In Whitehall, Public Service Agreements (PSAs) formalised Labour's approach into a format of aims, objectives and targets for each department, but also for a number of cross-cutting programmes. Over the years, the number of targets has fallen, from 250 in 1998 to 110 in 2004, and have become increasingly outcome focussed. In the most recent White Paper (HM Treasury 2004), the Chancellor argues that PSAs combine clear national goals with unprecedented levels of transparency, and have shifted the debate so that:

> "we can measure how effectively resources are being used and whether services are delivering the outcomes that will really make a difference to peoples' lives……
>
> The PSAs in this document set out objectives and performance targets across government, explaining what departments plan to deliver in return for the continued investment in resources. The PSA is an integral part of a framework for increased clarity, devolution and accountability in the delivery of public services". (Foreword).

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The Spending Review Process in Scotland

The financial arrangements for the Scottish Executive are largely the continuation of the pre-devolution framework as adjusted by the Labour Government after 1997. This divides resources into the Departmental Expenditure Limit (DEL) which can be directly controlled rather than being demand-driven, and Annually Managed Expenditure (AME), which is negotiated annually.

UK Spending Reviews take place every two years, but utilise a three-year planning cycle, in which the last year of the current cycle overlaps with the first year of the new cycle and which is reconsidered as part of the process. The Spending Review is essentially concerned with allocating the DELs. The Executive is only subject to Treasury control over the totals; financial management is a matter for decision in Scotland, with no requirement to follow the UK pattern of departmental allocations. Moreover, the Executive is *not* subject to a Public Service Agreement with the Treasury, although it makes use of the 'aims-objectives and targets' format *within* the Scottish Budget. The Scottish Spending Review is carried out by the Executive after its Departmental Expenditure Limit has been set by the UK Government in July.

In the initial post-devolution budgets, it was argued that there was a "lesser emphasis on a schematic structure of indicators" as "the Executive has not appeared to embrace detailed performance and output indicators as a tool of planning with the same enthusiasm as in Whitehall" (Parry, 2000, pp 3-4). It is certainly the case that practice was inconsistent across departments (Flynn, 2001), but a more recent study reported views from within the Executive that a greater focus on outcomes and outputs was the driving force in budgetary reform (McKay and Fitzgerald, 2002).

The appointment of a new Finance Minister in 2002 resulted in an overt commitment to push this process forward, and Spending Review 2002 (Scottish Executive 2002) was presented as an improved framework of financial and performance management which delivered more efficient, transparent public spending tightly targeted on priorities, and

> "this emphasis on making clear linkages between our spending and our priorities will become ever stronger, ensuring that our resources are focused more and more tightly on delivering positive change for the people of Scotland".
>
> (Scottish Executive 2002, p.12)

Whilst in practice this aspiration remained unfulfilled, and problems of linking *resources with results* and of *targeting priorities* were highlighted by the Finance Committee (2003), it is nevertheless fair to observe an improvement in the quality of financial and performance information in the budget. The key issue is the scope for integrating such data, for the state of the art elsewhere remains limited (Talbot and Johnson, 2003).

In 2004, a new *Annual Evaluation Report* (AER) now included a report on performance in meeting targets set in 2002; a statement of the new spending priorities; and a summary of current expenditure plans. It is then the subject of consultation over the proposed priorities with Parliament and public, who can submit comments to the Executive for consideration during the Scottish Spending Review process in the summer. The Draft Budget is delivered in the autumn, and contains the Executive's formal response to Parliament's budget recommendations.

The 2004 Spending Review in Scotland is the third such exercise carried out by the Scottish Executive since 1999. During this period, there has been continuous real growth in the Departmental Expenditure Limit (DEL), of around 4.5% per annum. Whilst SR 2004 reduces the rate of growth in real terms by around 1%, this nevertheless marks a continuation of the most sustained period of expenditure growth in modern history. The UK Government undertook a Comprehensive Spending Review in 1998, and the Scottish Office participated in that exercise. The format adopted by the Scottish Executive post-devolution has its roots in Whitehall's FMI initiative, which recommended the setting of departmental "aims, objectives and targets" (Likierman, 1987). Scottish Executive departments each produce a business plan with "a hierarchy of policy aims and programmes" and "output measures and other milestone indicators so that progress against the plans can be measured" (Audit Scotland 2002 p.20). The objectives of FMI are enshrined in the memorandum to accountable officers of April 2002, which, amongst other responsibilities, seeks

Æ to ensure that managers have a clear view of their objectives and means to measure performance, and

Æ to ensure managers have well-defined responsibilities for making the best use of resources.

The business plans form the basis of the budget documents, which include output measures and key performance targets (Audit Scotland 2002, p.21)

The Executive argues that the Spending Review process has a longer-term look within a strategic framework, which should facilitate better targeting of resources on priorities, and greater transparency in reporting performance against targets. The difficulties of linking resources with results in similar approaches used elsewhere are warning signals to reformers, but are not acknowledged in the official documentation. It also introduced *outcome* measures related to health status, educational achievement, poverty and crime.

The set of targets inherited from the Scottish Office was a mix of process and output-based measures, but few were outcome-based. Examples include "pay Revenue Support Grant on time and accurately throughout the year" (process); and "improve 100,000 houses suffering from dampness and condensation by 2003" (outputs). A study of the Scottish model in 2001 which sought to assess the extent to which outcome measures were in use, concluded this was inconsistent and linking resources to results remained problematic (Flynn, 2001).

A major improvement to the model came with *Building a Better Scotland* (Scottish Executive 2002) which set cross-cutting targets for the first time – for promoting *equality* and *sustainability* – and also increased *outcome* measures

The Parliament's Finance Committee has been supportive in principle of developing outcome measures, even when expressing dissatisfaction with practice, and recommended that the Executive should rationalise and simplify the process in Spending Review 2004. It reported widespread concern with existing practice in evidence from Subject Committees. One witness, Professor Irvine Lapsley, advised that

> "it is difficult to set a target, identify a programme of expenditure, and establish how it impacts on the target" (para.60);

whilst Professor Peter Wood similarly observed that

> "the targets are not necessarily or clearly related to activities which represent the main elements of spending, or even the elements of spending which are being increased" (para.59),

and finally, Professor David Heald advised the Committee

> "not to put too much emphasis on targets" but "regard them as a useful benchmarking exercise, and not as a substitute for political and managerial judgement" (para.60).

The Committee's conclusion reflected this evidence, in noting that linking objectives, funding and targets was still problematic, and that the Executive should *set targets which its actions could influence*. It recommended dropping around one-third of the 153 targets which were process-based in 2004. (Scottish Parliament Official Report, pp. 14-17).

A recent study, carried out *prior to* Spending Review 2004, from an economic perspective, advocated greater use of cost-benefit analysis and monetary valuation of outputs rather than performance measurement (Crafts, 2004). This paper noted that socio-economic factors can influence performance against targets, and argued for better quality information. Crafts, however, appears to confuse the objectives of measuring performance and measuring productivity. Whilst cost-benefit analysis *is* in use for evaluating options within capital programmes, the limitations of the approach mean that they at best inform, and at worst simply legitimise, political judgements. Using cost-benefit analysis or comparison *across* programmes is not widespread, and fraught with difficulty.

Indeed, there is little evidence in the public domain that performance targets influence budget decisions, rather they are instruments of accountability. Parliament and the Executive are considering how best to improve performance reporting to strengthen the scrutiny process. In the most recent document, there is a greater incidence of output and outcome measures *Outputs* are more easily identified, recorded, and related to spending, whether in terms of staffing, buildings or technology. *Outcomes* remain problematic, because intervening variables influence results in terms of economic growth, health status, or educational achievement. Linking these outcomes directly to spending decisions is impossible. For example, health status has improved each year since the establishment of the NHS, but this reflects economic and social progress as well as medical practice, and also public spending on housing, education, etc. The Scottish experience is similar to Whitehall, where, in practice, negotiation over targets is an ongoing process of refinement between Treasury and Departments, and only a minority of targets are dependent on new resources from Spending Reviews.

The New Efficiency Targets

In June 2004, the Executive announced its intention to seek savings in the Scottish Budget – which would release resources for spending on priorities, in an initiative entitled 'Efficient Government'. The target was savings of £500m over the Spending Review period to 2007-08, rising to £1billion by 2010.

A few weeks later, the Chancellor announced a similar efficiency drive across Whitehall, on the basis of a report by Sir Peter Gershon (Gershon, 2004). The objective was also to release resources for use in front line services, with a target of £20billion by 2007-08, of which at least 60% (or £12billion) would be cash-releasing.

This report did not apply directly to the Scottish Executive, although the review team did share its proposals with the devolved administrations, and reported that the Executive was seeking annual efficiency gains 'as ambitious as those in England'. Moreover, the areas identified as appropriate for efficiency gains in Scotland are identical to Gershon, namely procurement; back-office reform; transactional services, productive time; and policy, funding and regulatory regimes. The Finance Minister stated the Scottish target would be achievable without job loss (Kerr, 2004); and the First Minister later asserted that Scotland would "go further" than Whitehall (Blitz and Nicholson, 2004). Mr. McConnell is also reported as saying that the savings will be 2% per annum, compared with 1.5% per annum in *cash* in Whitehall. This efficiency drive was viewed as a central plank of the refreshed *Framework for Economic Development in Scotland* (FEDS), as the mechanism for increasing public sector productivity. Ironically, of course, simply redistributing finance from administration to service delivery would increase output, but *not* be recorded as growth in the current national accounts model applying in Scotland.

The basis of this comparison, however, is unclear. Although the First Minister is reported as seeking 2% per annum, the Finance Minister's figure was 2% by 2007-8. Therefore, this would compare poorly with the 4.5% set for Whitehall. This led to persistent questioning of the Executive's plans by the press and Parliament, over both the scale of the targets and the implications for jobs. By December 2004, the Executive's target for 2007-8 was raised three times, to £650m, then £745m, and potentially to £900m.

The picture was further confused by the announcement in November by the new Finance Minister that the savings package would amount to £1.7 billion over the next three years (Barnes, 2004). This figure was inflated by counting the savings delivered in 2005-6 of £405m *three* times as these are recurring – giving a figure of £1,215m; a further £177m in 2006-7 counted again for 2007-8 thereby adding £354m; and a further £163m for 2007-8 making a cumulative total of £1,732m, which the Executive then converted to a percentage figure of 8.3% of 2004-5 spending – i.e. using three years savings as a percentage of a single year – which is arithmetically correct, but meaningless in terms of budget management. What matters is the percentage of recurrent funding available for redistribution in the budget, which is £745m or 2.9% of the 2007-8 Departmental Expenditure Limit.

On past experience, savings of 1% per annum should be deliverable. However, around £325m of this is attributed to local government which in the recent cuts exercises has made such savings through a combination of reductions and council tax increases.

In short, the Executive has set modest and deliverable efficiency targets, some of which would have materialised in the normal process of financial management - which will release limited but useful resources for service improvement. Good managers in the public sector would have been pursuing such efficiency gains – by improving the ratio of outputs to inputs – as part of their ongoing approach to budget management. In an era of post-ideological politics, politicians are keen to claim greater financial competence over their opponents.

The Executive has recently produced its efficiency technical notes but these are subject to review following advice from Audit Scotland. It has, however, produced a list of budget line items identifying broadly how the savings will materialise. This preliminary summary suggests that a wider range of efficiency savings is under consideration than the original categories defined as efficient government. Of these, *procurement* is the most prevalent, accounting for £207m of the £650m identified in the DEL. There are only a few examples of potential *back-office* savings. Of particular concern is the £67m identified as savings in the Supporting People programme and the Modernising Government and Efficient Government Funds. This will require careful appraisal to ensure these are *genuine* efficiency gains which improve the ratio of outputs to resource inputs, rather than simply programme underspends. Similarly, a number of items are simply called 'efficiency savings' with no indication of how these will be delivered. The politics of efficiency remain important in the tightly controlled public expenditure regime in Whitehall, particularly for the message the Executive's performance sends out to the Treasury.

Conclusion

The publication of the Scottish Budget in 2004 marked continuing progress in the development of performance reporting. The new targets are fewer in number, with a greater emphasis on output and outcome measures than previously. However, substantial problems of linking budgets to results remain.

The introduction of efficiency targets has potential to bring greater transparency to government spending, but exaggerating the targets led to some press, public and political scepticism over the process. Spending public money well is a key task of government, which requires serious consideration, particularly for Scotland, given the widespread scepticism elsewhere in the UK that the Barnett formula operates to our advantage. Technical problems of measuring performance and efficiency are such that whilst indicators can inform the process, in the final analysis, they simply assist political judgements. Performance management is not rocket science.

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Appendix I: Objectives and Targets Relating to Economic Growth

1. *Tourism, Culture and Sport Portfolio*

Objective: To generate jobs and wealth for Scotland by promoting and developing the creative industries.

Target: Year on year real terms increase of Scottish Creative Industries Gross Value Added (GVA) to end 2007.

2. *Enterprise and Lifelong Learning Portfolio*

Objective: To raise the long-term sustainable growth rate of the Scottish economy.

Targets:

- "Increase business investment in research and development compared to OECD competitors";
- Improve productivity levels in Scottish industry;
- Increase entrepreneurial activity in Scotland over time.

3. *Transport Portfolio*

To promote economic growth by building, enhancing, managing and maintaining transport services, infrastructure and networks to maximise their efficiency.

Targets:

- Increase passenger journeys on the Scottish Rail network by an average of 2% each year;
- Reduce the time taken to undertake trunk road journeys on congested or heavily trafficked sections of the network by 2008;
- Improve the condition of the trunk road network over a 10 year period against measurable milestones;
- Achieve key milestones each year on the delivery of the infrastructure projects set out in the long-term investment plan, subject to projects receiving the necessary public or parliamentary approval.

4. *Environmental and Rural Development Portfolio*

Objective: Promotion of sustainable growth in the rural economy and sustainable rural communities by supporting the agriculture, food and forestry sectors, pursuing land reform and improving rural services.

Targets:

- Maintaining at least 95% of agricultural land in the Scottish LFA in productive use over the Spending Review period, except where that land is converted to other sustainable uses;
- By March 2008, improve service delivery in rural areas so that agreed improvements in accessibility and quality are achieved for key services in remote and disadvantaged areas.

Appendix II: Efficient Government Cash-Releasing Projects by Portfolio

	Portfolio	Amount (£m)
	Communities	
C/C1	Reducing unit costs in Communities Scotland Development Programme	9
	Total	*9*
	Crown Office and Procurator Fiscal Service	
COPFS/C1	Alternatives to prosecution	1.1
COPFS/C2	Case related costs/rationalisation of estate	0.5
COPFS/C3	Increase Sheriffs solemn sentencing power to 5 years	0.4
COPFS/C4	Staff savings from introduction of new IT system in COPFS	0.8
	Total	*2.8*
	Education and Young People	
CYP/C1	SQA efficiency gains	1
EYP/C2	Care Commission Efficiency Savings	1
	Education and Young People Portfolio Efficiency Saving	9.8
EYP/C3	NED Broadband	0.8
EYP/C4	Pupil Support and Inclusion	0.2
EYP/C5	Additional Support Needs	1.4
EYP/C6	Children and Families	3.4
EYP/C7	Youth Crime	3.1
EYP/C8	Looked After Children and Youth	0.5
EYP/C9	Information and Analysis	0.1
EYP/C10	Gaelic	0.2
EYP/C11	Other	0.1
	Total	*11.8*
	Enterprise and Lifelong Learning	
ELL/C1	Scottish Enterprise savings	5.3
	Total	*5.3*
	Environment and Rural Development	
ERD/C1	Efficiency savings in Forestry Commission (Scotland)	1
ERD/C2	Savings in SEPA	4
ERD/C3	Savings in SNH	
	Total	*5*
	Finance and Public Services Reform	
	Central Government	
	Miscellaneous Others	0.1
FPSR-C/C1	Standards Commission	0.016
FPSR-C/C2	Inspectorate of Prosecution	0.08
FPSR-C/C3	Internal efficiency savings in SPPA	0.635
	Total	*0.735*
	Local Government	
FPSR-LG/C1	Assumed Local Government Efficiency Savings	168.3
FPSR-LG/C2	Fire Service Reform	1.5
FPSR-LG/C3	Common Police Services	8
FPSR-LG/C4	Efficiencies in Supporting People programme	27
FPSR-LG/C5	Modernising Government and Efficient Government Fund Efficiency Savings	40
	Total	*244.8*

	Health	
H/C1	NHS Procurement	50
H/C2	NHS Support Service Reform	10
H/C3	NHS Logistics Reform	10
H/C4	Improved prescribing of drugs	20
H/C5	Preventing inappropriate hospital admissions	25
H/C6	National benchmarking exercise on use of staff	10
H/C7	NHS Efficiency savings	40
H/C8	Estate and facilities management	1
	Total	*166*
	Justice	
J/C1	Fire Central Government	0.1
J/C2	Community Justice Services	4
J/C3	Scottish Court Service	3
J/C4	Legal Aid – changes in rules and increased efficiency	12
J/C5	Efficiency savings in SPS	10
J/C6	Accountant in Bankruptcy – take more cases in house	1
	Total	*30.1*
	Tourism, Culture and Sport	
TCS/C1	Efficiency savings from Tourism, Culture and Sport NDPBs	1.75
	Total	*1.75*
	Transport	
T/C1	Rail Franchise - Procurement	5
T/C2	Concessionary Fares	5
T/C3	Rail Franchise - Introduction of ticket machines	1.5
T/C4	Traveline/Transport Direct	1
T/C5	Highlands and Islands Airport Limited	0.5
T/C6	Caledonian MacBrayne	0.5
	Total	*13.5*
	Administration*	
A/C1	CAP Reform	2.4
A/C2	Procurement	2.4
A/C3	e-HR	0.5
A/C4	eRDM	0.5
A/C5	Savings from non-staff costs/better staff deployment	2
	Total	*8.4*
	Other	
O/C1	Procurement	150
O/C2	Scottish Water savings	95
	Total	*245*
	Overall Total	744.185

Author's Note:

***Totals do not add up to £8.4m.**

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