

**THE IMPLEMENTATION OF PERFORMANCE BUDGETING  
IN THE MALTESE PUBLIC SECTOR**

by

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## **Abstract**

This study considers the potential for the implementation of performance budgeting within the Maltese public sector, exploring the pressures which support and inhibit this reform, proposing a possible implementation approach and identifying the issues surrounding the implementation of changes to the budgetary system. The study also seeks to identify the recent reforms of the budgetary framework, which have occurred since the change in government in March 2013. Change is inevitable as the government is committed to meet specific targets for fiscal deficit and debt reduction, in line with its EU obligations.

The research follows a qualitative approach, using data gathered from documentary sources, corroborated with empirical evidence collected from in-depth, semi-structured interviews. Access has been obtained to discuss relevant issues with senior politicians from the government and the opposition, including former ministers and Prime Ministers.

The findings indicate that there are a number of macro-level and institutional pressures acting as triggers for the implementation of budgetary reform; at the same time, there are elements constituting resistance to change which have to be tackled should government intend to change the budgetary framework. A combined approach, with more emphasis on the bottom-up perspective, is recommended for the implementation of performance budgeting.

*To my family:*

*To Gabriel and Elisa, joy of my life and music of my soul, and especially...*

*With all my heart...to Kevin.*

*How incredibly blessed I am to have you!*

*All my love,*

*Lauren*

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## List of Abbreviations

CBM	Central Bank of Malta
CIPFA	Chartered Institute of Public Finance and Accountancy
CSR	Comprehensive Spending Review
DOI	Department of Information
EBU	Extra Budgetary Unit
EDP	Excessive Deficit Procedure
EPD	Economic and Policy Department
ESA	European System of Accounts
EU	European Union
Fitch	Fitch Ratings
GAAP	Generally Accepted Accounting Principles
GDP	Gross Domestic Product
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
IT	Information Technology
KPI	Key Performance Indicator
MFSA	Malta Financial Services Authority
MOF	Ministry for Finance
Moody's	Moody's Investors Service
MP	Member of Parliament
NAO	National Audit Office
NSO	National Statistics Office
OECD	The Organisation for Economic Co-operation and Development
OPM	Office of the Prime Minister
PB	Performance Budgeting
PI	Performance Information
PPP	Purchasing Power Parity
S&P	Standard & Poor's
UK	United Kingdom
US	United States



# **CHAPTER 1: INTRODUCTION**

## 1.1 Introduction

*“Performance budgeting refers to procedures or mechanisms intended to strengthen links between the funds provided to public sector entities and their outcomes and/or outputs through the use of formal performance information in resource allocation decision-making”* (Robinson and Brumby, 2005: 5).

Performance budgeting (PB) is an important theme of public financial management reforms, which is targeted at enhancing public sector performance, bettering the use of public funds, and increasing accountability to the public. In the past few years, Malta has faced fiscal deficit issues and high government debt. Being a member of the European Union (EU), Malta has to comply with the Union’s laws and regulations. The fiscal issues faced by the country could stimulate government’s efforts to introduce budgetary reforms, in order to secure fiscal sustainability. This study considers the potential for the implementation of PB in the Maltese public sector, exploring the pressures for and against the reform, proposing a possible implementation approach and identifying the issues surrounding the implementation of the changes to the budget system.

This chapter gives an introduction to the study. Section 1.2 provides some background information, whilst section 1.3 explains some key terms. This is followed by section 1.4, which gives an overview of the Maltese scenario by providing some insights of the environment in which the research is undertaken. Subsequently, the rationale for the study is explained in section 1.5 and the research objectives are set out in section 1.6. Section 1.7 describes the scope and limitations underlying the study, whilst the last section (1.8) provides a road map for the rest of the dissertation.

## 1.2 Background to the study

The “...*all-important thing in budgeting is the work or service to be accomplished and what that work or services will cost*” (Schick, 1971). This statement postulates the underlying objective of the various forms of budgeting that have been developed and implemented over the years. According to Martin et al (1995), budgets are more critical than financial statements in governments. This is because a budget represents a financial planning tool for matching limited public resources to the citizens’ needs; furthermore, the adoption of a budget constitutes legal authority for spending money. Conversely, a set of financial statements summarises historic financial activities undertaken by government in the past year.

Most academics concur that budget systems are multifunctional. Schick (1966) defined three competing budget functions: planning, management, and control. Campos and Pradhan (1997) stated that a budget system has three basic expenditure outcomes that need to be achieved: (a) to ensure aggregate fiscal discipline, (b) to facilitate strategic prioritization of expenditures across programmes and projects, and (c) to encourage technical efficiency in the use of budgeted resources. Wildavsky (1978: 501) claimed that: “*Budgeting is supposed to contribute to continuity (for planning), to change (for policy evaluation), to flexibility (for the economy) and to provide rigidity (for limiting spending)*”. Budgeting facilitates the two main elements of a management information system, namely decision-making and control (Zimmerman, 2003).

In the context of the public sector, the budgeting process assists decision makers within government departments in the allocation of scarce resources amongst various competing programmes. It also controls the behaviours of appointed public officials by limiting the waste or misuse of governmental resources (Smith and Cheng, 2006). The authors note that there are

similarities between budgeting practices in business and in government, in that both businesses and government allocate resources among competing programmes, and both are concerned with enhancing efficiency and effectiveness in these selected programmes.

The economic and financial crises have triggered huge pressures for expenditure cuts and public debt reduction (Anessi-Pessina et al, 2016). Constraints in government revenue, coupled with increased demands for services from the citizens, have led to the restructuring of the public budgeting systems in a number of countries. The traditional view of budget systems focused mainly on resource allocation and input control, with little follow-up action undertaken to assess the actual performance of spending departments (Diamond, 2003). The new budget system, referred to in this document as ‘performance budgeting’, aims to establish a more direct link between performance in achieving pre-determined objectives and resource allocation through the budget process (Diamond, 2003). Thus, budgetary reform can be seen as representing a move from an emphasis on inputs, to a focus on performance, outcomes or results.

All results-oriented budget reforms have the objective of making government more efficient and effective by introducing modern management and policy-making concepts into government (Sterck and Scheers, 2006). Governments today are especially trying to ascertain how well public organisations and programmes are doing in providing services and products to their citizenry (Young, 2003). King (1995) suggests a number of reasons for the employment of PB, including the following: (i) government must be driven by citizen desires and needs, not government rules and regulations; (ii) taxpayers will pay for results, not efforts; (iii) government must better communicate progress toward goals and objectives. Governments are asking: *“What kind and how many services are we getting from allocated dollars? Are these public services of good value? Are they making a difference in citizens’*

*lives?*” (Young, 2003: 12). The implementation of PB systems by public administrations is targeted at addressing these questions, and other similar ones.

### 1.3 Key terms and definitions

The table below sets out some key definitions pertinent to the study.

**Table 1: Key definitions**

Term	Definition
Performance budgeting	PB (also referred to as ‘performance-based budgeting’ in this document) has been defined by the OECD (2008: 2) as “ <i>budgeting that links the funds allocated to measurable results</i> ”. PB has been defined as the provision of information in the budget document which explains what the organisation or department has achieved or expects to do with the funds at its disposal (Jordan and Hackbart, 1999; Melkers and Willoughby, 1998).
Traditional / conventional / line-item budgeting	The line-item budget presents expenditures by inputs purchased and classifies expenditure items by operating and capital expenditures (Shah and Shen, 2007).
Performance measures	A performance measure has been defined as a “ <i>quantifiable expression of the amount, cost, or result of activities that indicate how much, how well, and at what level, products or services are provided to customers during a given time period</i> ” (Office of Financial Management, 2011: 1). Performance measures include output and outcome measures.
Inputs	“ <i>Inputs are those resources that contribute to production and delivery...Taking the medical sector as an example, inputs commonly include things such as labour, physical assets and IT systems (e.g. doctors, nurses, scanning equipment, etc.)</i> ” (OECD, 2007: 193).
Outputs	“ <i>Outputs are the final products, or goods and services, produced by the organisation for delivery to the customer (e.g. the number of effective medical treatments or operations that take place)</i> ” (OECD, 2007: 193).
Outcomes	“ <i>Outcomes are the impacts or consequences for the community or individual of government activities, and normally represent what the organisation is trying to achieve (e.g. longer life expectancy and better health)</i> ” (OECD, 2007: 193).

### 1.4 The Maltese scenario

Malta currently operates a traditional cash budgeting system. The annual government budget presents expenditures by inputs for each ministry and for the government departments and

agencies falling under that ministry. Focus is placed upon ensuring that the ministries do not spend in excess of the stipulated line item caps and no performance information is incorporated in the budget documents.

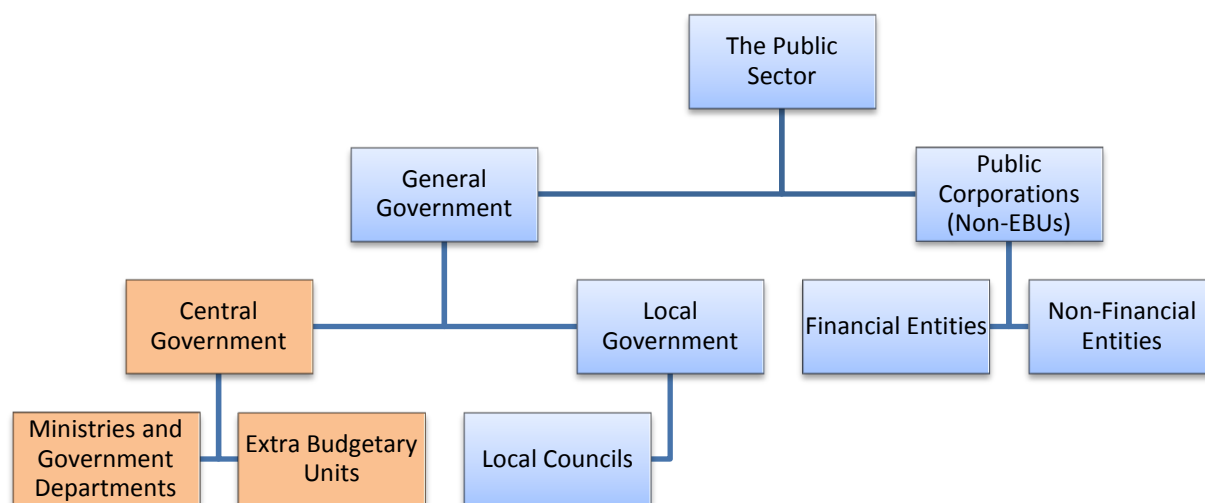
#### **1.4.1 Key facts and figures**

Malta is a European country situated in the Mediterranean sea. The island has a population of approximately 425,000 people (as per an estimate of 2013) and covers around 316 km<sup>2</sup>, which makes it one of the world's smallest and most densely populated countries (Malta Tourism Authority, 2015). Malta's gross domestic product (GDP) for 2014 was of €7.96 billion, which translated into a GDP per capita (PPP) for 2014 of about €18,700 (National Statistics Office, 2015a). The unemployment rate stood at 5.7% of the total labour force, in the first quarter of 2015 (Trading Economics website).

Malta joined the EU on 1 May 2004 and became part of the Eurozone on 1 January 2008. Malta has established itself as an international financial services centre. The country has sound wealth management, fund, insurance and banking sectors which have drawn investment from high net-worth individuals and leading financial institutions across the world (NexiaBT website). Malta has also been successful in attracting aircraft and ship registration and gaming businesses (Wikipedia, 2015). The hospitality industry is also a major contributor to the country's economy.

#### **1.4.2 The public sector in Malta**

The public sector in Malta is composed of the general government's entities and the public corporations, which are also referred to as non-EBUs (non-Extra Budgetary Units) – refer to Figure 1 below.

**Figure 1: Definition of Public Sector<sup>1</sup>**

The general government's administrative responsibility is divided between the central government and the local councils.

The central government comprises the Office of the President, the House of Representatives, the Office of the Prime Minister, fourteen ministries split into various government departments and agencies that fall under their direct responsibility, and a number of EBUs<sup>2</sup> (Extra Budgetary Units).

Malta's local government system, which has been in operation since 1993, holds responsibility for the general upkeep of the locality and performs general administration duties on behalf of central government. Local government consists of 68 local councils.

There are no intermediate levels between central government and local government.

<sup>1</sup> Different colour coding has been applied for the 'central government' component since this falls under the scope of the study.

<sup>2</sup> An EBU is an autonomous government body which depends on government's budget allocations for its financing. Conversely, a non-EBU, which is also autonomous from the government, does not depend on central funds for its financing requirements. As at 31 December 2014, there were 49 EBUs, including two tertiary education institutes, two hospitals, a waste management unit, a number of culture and sports entities, units in social protection and units dealing with the administration and regulation of services offered to the public (National Statistics Office, 2015a).

This study will focus on central government. Central government in Malta has a considerably broad scope, with most public functions falling under the responsibility of the central government. For example, the relevant ministries manage public schools and hospitals (including health clinics), and their employees are considered part of central government.

### **1.4.3 Politics**

Malta became a parliamentary democracy within the Commonwealth in 1964, having previously been under the sovereign reign of Queen Elizabeth II of the United Kingdom (UK). In 1974, Malta became a republic. The President of Malta holds executive authority; however, the Prime Minister of Malta, as head of government, is responsible for the overall direction of the Maltese government. The Parliament of Malta, which consists of the President and the House of Representatives, forms the legislative body of the country. The House of Representatives consists of 69 parliamentary members.

The main political parties are the Labour party, which is a social democratic party, and the Nationalist party, which is a Christian democratic party. The Labour Party is presently in government, having won the 2013 general election after nearly 25 years in opposition. The Prime Minister of Malta and leader of the Labour party is presently Dr. Joseph Muscat. The Nationalist Party is currently in opposition, led by Dr. Simon Busuttil. There are a few other small political parties, which do not have any parliamentary representation.

### **1.4.4 Government accounting**

The central government of Malta uses a cash-based accounting system for its government ministries and departments, supplemented by accrual based information.



The accrual accounting reform was originally launched by the Ministry for Finance (MOF) in 1999 (Department of Information, 2001) and it is to date still on-going. A decision has recently been taken by the public administration to adopt International Public Sector Accounting Standards (IPSAS), being the only recognised public sector accounting standards. Though the appropriate structures are now in place, government is still at the beginning of the implementation process. In this regard, the Treasury is aiming for 2019/2020 to have the first dry run, consisting of the compilation of consolidated accounts.

In the meantime, the cash-based accounting system is being supplemented by accrual-based data collected manually from the government departments which, however, does not meet IPSAS requirements (Camilleri, 2014). The gathering of accrual data is an unreliable process, because it is too dependent on the people compiling the information (Camilleri, 2014).

A report prepared by the UK Chartered Institute of Public Finance and Accountancy (CIPFA), dated November 2013, was commissioned by the Maltese authorities to provide a ‘gap analysis’ for moving to accrual accounting on the basis of IPSAS (Camilleri, 2014). The main conclusions of this report were categorised under five headings: Accounting, Systems, Processes, People and Programme Management. When tackling ‘Accounting’, this report commented on the choice of the accounting basis underlying financial reporting, on the one hand, and budgeting, on the other:

*“Budgeting on a cash basis and reporting on a full accrual basis will give rise to complexity, and raise questions about which figures people are accountable for. The full potential benefits of the move to accrual reporting can only be realised if the budget framework moves to a full accrual basis in the medium to longer-term.”*  
(Camilleri, 2014: 39)

### 1.4.5 EU influence on Malta's implementation of budgetary reform

As Malta is an EU Member State, it has to adhere to EU laws and regulations and meet the demands of such affiliation. Van Nispen and Posseth (2009) claim that fiscal stress is a key driver for budgetary reform, but it's not the only reason for such reform. There are other triggers for budgetary reform, such as the Maastricht criteria for qualification and participation in the Economic and Monetary Union (van Nispen and Posseth, 2009).

The Maastricht criteria specify, in two separate protocols, five conditions that need to be satisfied by EU member countries (Protocol on the excessive deficit procedure and Protocol on the convergence criteria) (European Union, 1992), as detailed in the following table:

**Table 2: Conditions of EU membership**

Conditions to be satisfied by EU member countries
a) The planned or actual government deficit should not exceed 3% of each country's GDP at market prices
b) The government debt is not to exceed 60% of GDP at market prices
c) The average rate of inflation, observed over a period of one year before the examination, does not exceed more than 1.5 percentage points of, at most, the three Member States with the lowest inflation rates
d) No exchange rate realignment for at least two years
e) Over a period of one year before the examination, the average nominal long-term interest rate does not exceed by more than 2 percentage points that of, at most, the three Member States with the lowest inflation rates.

*Source: Protocol on the excessive deficit procedure and Protocol on the convergence criteria (European Union, 1992)*

The first two criteria are targeted at reinforcing the stability of the euro, by protecting the EU from threats of inflation which may arise from government budget deficits (Afxentiou, 2000).

If a Member State does not satisfy these two criteria, the European Commission can open an excessive deficit procedure (EDP) for that country. Article 3 of the Protocol on the EDP

(European Union, 1992) states that “*The Member States shall ensure that national procedures in the budgetary area enable them to meet their obligations in this area.*” The last three criteria mentioned above are designed to ensure monetary stability by supporting a fixed exchange rate regime among member countries (Afxentiou, 2000).

With respect to the local scenario, in June 2013, the EU placed Malta under an EDP, since the fiscal deficit was observed at 3.3% of GDP at the end of 2012, above the EU's 3% of GDP reference value for government deficits. The EU called on Malta to take corrective actions and it set a deficit target of 3.4% of GDP for 2013 and 2.7% of GDP for 2014 (Malta Today, 2013a). The Maltese government was committed to reduce the country's deficit and targeted a 2.7% deficit by the end of 2013 (Xuereb, 2013). This target was nearly met, with Malta ending 2013 with a deficit of 2.8% of the GDP (Times of Malta, 2014a). By the end of 2014, the deficit was reduced to 2.1% of GDP and was forecast to remain at 3% of GDP in 2015 and 2016 (Times of Malta, 2015a) – as a result, the EDP against Malta was lifted in June 2015 (Times of Malta, 2015b). Nevertheless, the EU has made a number of recommendations (targeting health care, energy and pension reforms, amongst others) in order for Malta to ensure long term fiscal sustainability. Furthermore, the interview data collected for the purposes of the study showed that the deficit reduction has, to some extent, been attained, by sacrificing expenditure in certain areas, such as infrastructure.

The fiscal deficit issues that Malta has been facing could stimulate the country's efforts to introduce budgetary reforms in order to ensure that the Maastricht criteria for qualification and participation in the Eurozone are consistently adhered to.

In view of this background, the implementation of financial management reform in the Maltese public sector is fundamental in order to ensure that the public finance domain will

support macroeconomic stability and ensure smooth financing of government functions. In the absence of sustainable changes in public financial management, there is a risk that the government will face fiscal stress and unexpected surprises, which need to be resolved immediately. In these circumstances, quick-fix decisions will need to be made which would consider only the short-term impact, without taking into account the medium and long-term risks and impact.

#### **1.4.6 The traditional budgeting system**

The line-item cash budgeting system has been in operation within the Maltese public administration for several years. This relatively simple system potentially facilitates the control of public expenditure by stipulating the line-item cap in the fund allocation process to ensure that departments do not spend in excess of their ceiling (Shah and Shen, 2007). The resilience of traditional line-item budgeting has been the result of the strong advocacy by budget offices and ministries of finance for the control of public funds (Shah and Shen, 2007).

Notwithstanding its endurance, this system embodies certain limitations which impede the effective planning and decision-making processes vis-à-vis resource allocation, as well as limit performance-oriented accountability in the public sector (Shah and Shen, 2007). The line-item budget focuses on how much money is spent and on whether expense items have increased or declined in comparison with the previous year's budget, rather than on how efficiently resources have been used (Shah and Shen, 2007). As a result of its inherent characteristics, this budgeting system makes it difficult to assess the performance of government programmes and to appraise the level of service delivered by public officials. Moreover, it adopts a short term perspective for budgeting, focusing on year-on-year changes in expenditure levels; this may create planning problems for government.

### **1.4.7 Motivations for budgetary reform in the local context**

Budgetary reforms seek to remedy the deficiencies embedded in the traditional line-item budgeting system. By concentrating on the performance dimension in resource allocation decisions, PB is aimed at achieving operational efficiency and enhancing accountability for results attained (Shah and Shen, 2007).

An overview of the Maltese context, as illustrated above, reveals that the Maltese government is operating under tight financial conditions, facing fiscal deficit problems and high government debt. This fiscal stress coupled with the country's requirement to comply with EU laws and regulations, may act as triggers for budgetary reform.

The implementation of PB in the local scenario may prove to be a useful tool for making spending decisions based on the results achieved by programmes within the various government's ministries. In view of government's commitment to keep the fiscal deficit under control, PB may indicate which government programmes are ineffective or under-performing, such that decisions vis-à-vis budgetary cuts are taken after considering their full impact.

## **1.5 Rationale for the study**

As stated earlier, Malta's budgetary system is presently based on the conventional, line-item budgeting approach. Though this method still enjoys popularity in some countries due to its simplicity, it is considered by many developed countries' governments to be out-dated and has been replaced by budgeting systems which seek to link input resources to performance and results. A common budgetary reform which has been applied in a number of developed countries (including US, UK, Australia, Canada, New Zealand, Sweden, Netherlands and Denmark) is the implementation of a PB system.

To my knowledge, no study has been undertaken to date which explores the possibility of implementing PB within the Maltese central government. In this respect, my research could be valuable for Malta because it provides insights to government on the possible implementation of budgetary reform and the issues surrounding such implementation. The research also sheds light on the requirement to create capacities for the implementation of the reform.

The results emanating from my research could also be extended to other small EU countries which intend to implement PB within their central government. It is hoped that this study will make a contribution to performance-related issues surrounding the budgeting process in small countries. In this regard, the implementation approach proposed by the study, the identified issues underlying the implementation of PB and the means for successfully addressing such issues, could be applied to other small EU countries in the future. Furthermore, the application of institutional theory, radical change and policy implementation, in the context of the Maltese public sector, could be drawn upon by other small countries seeking to understand public financial management reforms.

## **1.6 Objectives of the study**

The basic research question endeavours to assess why and how the Maltese public administration might transition from the existing line-item budgeting system to a performance based system. The study will raise an understanding of the current reform situation with respect to the budgeting system.

The context of a small nation, within which the research is carried out, forms the underlying concept of the study. The research attempts to address the objectives set out below in respect of budgeting reforms in Malta.

1. Understand why the reforms in the budgetary system might be implemented in the local context. This will include a discussion of the pressures which support and inhibit the implementation of PB.
2. Identify the reforms of the budgetary framework which have occurred since the change of government in March 2013.
3. Ascertain the conceptual implications of including performance information in budget documents and holding public officials responsible for the actual performance of their department/programmes.
4. Propose a suitable implementation approach and determine the potential issues around the implementation of PB.

## **1.7 Scope and limitations**

This study is limited to central government, which comprises government ministries and departments and government bodies that depend on budget allocations for their financing.

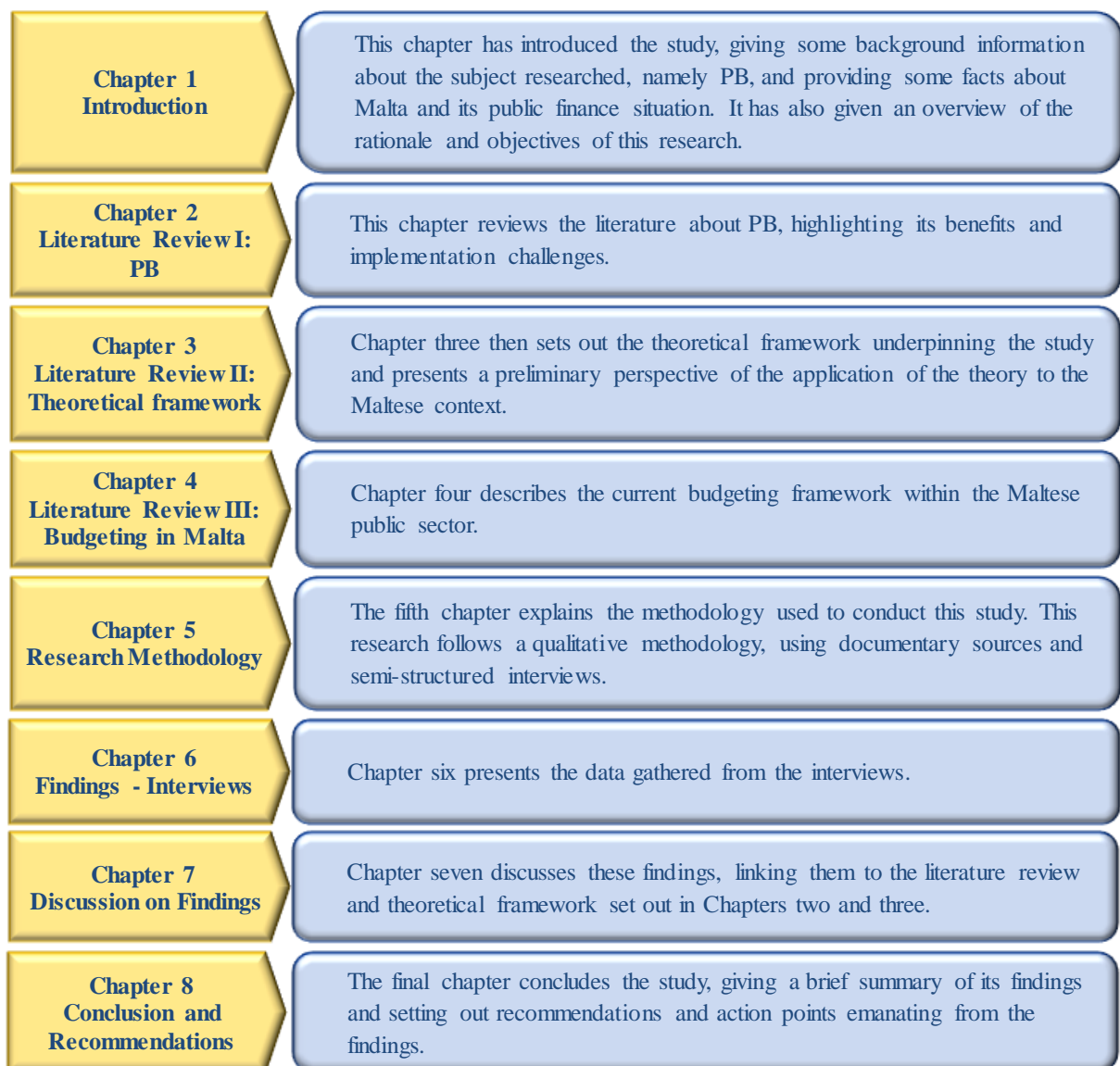
The research is based on empirical data collected during the period commencing August 2014 and ending April 2015. It is to be noted that the EDP against Malta was lifted by the EU in June 2015; thus, the empirical data was gathered during a period when the EDP was still in force.

Given that the study has been carried out within the context of a small country, the findings emanating from the research may not apply within the framework of a medium-sized or large country.

## 1.8 Overview of the document

This document is composed of eight chapters, as illustrated in the figure below:

**Figure 2: Dissertation overview**





**CHAPTER 2:**  
**LITERATURE REVIEW I**  
*PERFORMANCE*  
*BUDGETING*

## **2.1 Introduction**

This chapter gives an overview of the literature reviewed in relation to PB in the context of the public sector. Section 2.2 looks into some definitions put forward for PB. Sections 2.3 and 2.4, respectively, describe the objectives and advantages of a performance-based budgeting system. Next, the weaknesses of traditional line-item budgeting are highlighted in section 2.5. This is followed by section 2.6, which explains the challenges surrounding the implementation of a PB system. Subsequently, an explanation of performance measurement and an illustration of a PB system are presented in section 2.7. Section 2.8 then sets out a discussion of the accrual basis of accounting for historical financial reporting and budgeting, whilst the last section (2.9) gives a brief overview of the experiences of countries which have implemented PB.

## **2.2 What is performance budgeting?**

PB has been defined in various ways to refer to similar or various practices (Joyce and Sieg, 2000). Notwithstanding, there is agreement in the literature that performance is increasingly being incorporated in the budgeting practices of public organisations, though to different degrees and in different ways (e.g. Guthrie et al, 1999).

In the broadest possible context, PB has been defined as any reform that attempts to incorporate performance measures in the budget process (Kong, 2005). PB deals with the allocation of funds to achieve pre-determined goals – this requires measurement of work, efficiency and/or effectiveness (e.g. Robinson and Brumby, 2005; Young, 2003; Garsombke and Schrad, 1999). In this context, PB represents a budget in which an increase in resources is explicitly linked to an increase in the number of products or services delivered.

Mikesell (1999) states that performance budgets are basically the linking of inputs or costs to programme activities and goals. Joyce (1999: 598), while acknowledging that “*no standard definition*” of PB exists, states that it “*involves a sophisticated web of relations, from inputs to outputs, to outcomes... the connecting of resources to results for budgeting purposes*”. Similarly, Dawson (1995, cited in Young, 2003: 12) describes performance measurement and budgeting “*as general terms applied to systemic efforts to assess government activity and enhance accountability for progress and outcomes in achieving results*”.

In a report published in the US by the National Conference of State Legislatures in 1994, PB was defined as follows:

*“Performance budgets use statements of missions, goals and objectives to explain why the money is being spent...[It is a way to allocate] resources to achieve specific objectives based on programme goals and measured results...Performance budgeting differs from traditional approaches because it focuses on spending results rather than the money spent – on what the money buys rather than the amount that is made available”* (Carter, 1994: 2-3).

Van Reeth (2002) states that the concepts of ‘performance budgets’ and ‘performance budgeting’ have been used as the antithesis of traditional budget formats and budgeting procedures. Whereas PB involves making budgetary decisions on the basis of programme goals and measured results, in traditional systems budgetary choices are based on criteria at a macro-level, in the sense that budgetary increments are either granted across the board to minimise political conflict or budgetary cuts are made without considering their impact on programme performance (Van Reeth, 2002). Changing from traditional budgeting towards a budgetary process which is informed by performance requires the availability of performance information (PI) and the use of that information for decision-making “*at each stage of the budgeting cycle*” (Joyce, 2011: 357).

Young (2003) suggests that PB has four primary characteristics: first, it sets a goal, or a set of goals, to which monies are allocated; second, PB provides information and data on past performance and proceeds to allow for meaningful comparisons between ‘expected’ and ‘actual’ progress; third, adjustments to programmes are made either at this point or during a future budget preparation cycle to close any performance gaps that may exist; fourth, PB provides an opportunity for regular or ad hoc programme evaluations which give independent and verifiable information to budget decision makers.

OECD (2008) defines PB as budgeting that links the funds allocated to measurable results. This definition is close to that advanced by the US General Accounting Office where PB is defined as the process of linking budget levels to expected results, rather than to inputs or activities (General Accounting Office, 2005).

OECD (2007) has categorised PB into three types: presentational, performance-informed and direct. In presentational PB, the PI presented in budget documents does not play a role in decision-making and does not affect the way in which resources are allocated. PI is included as background information for the purposes of accountability and dialogue with legislators and citizens, on public policy issues and government direction. In performance-informed budgeting, the PI is important in the budget decision-making process, but does not determine the amount of resources allocated. Therefore, under this type of PB, past performance or proposed future performance impact resource allocation indirectly. Direct PB involves allocating resources based on results achieved. Appropriations are based on a formula/contract with specific performance or activity indicators, and funding is directly based on results achieved. The PB categories proposed by the OECD are summarised hereunder.

**Table 3: PB categories**

Performance budgeting categories		
Type	Linkage between performance information and funding	Main purpose in the budget process
Presentational	No link	Accountability
Performance-informed budgeting	Loose/indirect link	Planning and/or accountability
Direct performance budgeting	Tight/direct link	Resource allocation and accountability

Source: OECD (2007)

### 2.3 Objectives of performance budgeting

PI incorporated into budgets holds public officials accountable for service quality, cost-efficiency, and programme effectiveness (Young, 2003). If PB is used to hold public officials accountable for their actual performance, the implications are either to reward officials who meet or exceed performance expectations or to punish officials who perform poorly. Hou et al (2011) advise that the evaluation of performance must be linked to incentives, such as status, pay or promotion. OECD (2007) has mentioned a number of mechanisms that can be used to motivate performance, distinguishing between financial or non-financial incentives. As set out in the table below, these incentives have been categorised into: (1) financial rewards or sanctions; (2) increasing or decreasing financial and/or managerial flexibility; and (3) making the results public, i.e. naming and shaming poor performers and recognising good performers. Otley (1999) referred to the establishment of rewards/penalties as one of the issues to be addressed when developing a model for the management of organisational performance. Burgess and Ratto (2003) suggested that team-based rewards may be preferable to individual compensation schemes, especially where only aggregate performance measures are available and where cooperation is essential for the achievement of the organisation's goals.

**Table 4: Mechanisms to motivate performance**

Mechanism	Rewards	Sanctions
<b>Funding</b>	Increase funding to the agency	Reduce or restrict agency funding
	Maintain status quo on agency funding	Eliminate agency funding
	Provide management and/or employee bonuses	Cut the salary of management and/or employees
	Increase the staff budget	Cut the staff budget
<b>Flexibility</b>	Allow the agency to retain and carry over efficiency gains	Return all funding to the centre
	Allow flexibility to transfer funds between different programmes and/or operating expenditures	Restrict the ability to transfer funds
	Exempt the agency from certain reporting requirements	Increase the reporting requirements
		Order a management audit of the agency
<b>Public recognition</b>	Publicly recognise the agency's achievements	Publicly criticise the agency's performance

Source: OECD (2007)

According to Sterck (2007), PB initiatives have had two major objectives: improving allocation decisions and increasing operational efficiency; moreover, the budget is also a control instrument. Joyce (1999) also mentions improved decision-making and enhanced service delivery, as the two main aims that PB strives to fulfil. Firstly, for improved decision-making, public officials require qualitative, timely and comprehensive information. PB provides this through its various components, such as, the setting of goals and objectives, the prioritizing of these ends, and the measuring of performance levels (Young, 2003). Secondly, PB aids improved superior service delivery by establishing performance targets and simultaneously providing for some measuring device to monitor efficiency and effectiveness of service delivery efforts (Young, 2003).

Robinson and Brumby (2005) claim that the core objectives of PB are enhanced allocative and productive efficiency in public expenditure. According to Gilmour and Lewis (2006), the

most important reason for adopting PB is to determine which government programmes are delivering results and therefore, qualify for budget increases.

There is also an important link between PB and macro-level goals relating to the level of aggregate expenditure and to fiscal sustainability (Robinson and Brumby, 2005). If productive efficiency is enhanced such that a product or a service is delivered at the minimum cost without sacrificing on quality, overall public expenditure would be lower, other things being equal. This would translate either in the funding of new products and services or in reducing the citizens' tax burdens. Where the public administration is seeking to reduce government expenditure to narrow the fiscal deficit, improved expenditure prioritisation assumes fundamental importance. PB is a useful tool which assists governments to reduce expenditure on lower-priority or ineffective programmes, instead of making across-the-board expenditure cuts which might harm effective, value-for-money programmes. Governments are constantly challenged to provide effective public services and to do more with less, in view of the current economic and fiscal environment – thus, policy results, public service performance and budgeting are indivisible (Lu et al, 2015). In this regard, Lu et al (2015) believe that PB will remain important in public budgeting and governance.

## **2.4 Advantages of performance budgeting**

PB improves communication between public officials involved in budgeting and the citizens – through the identification of programme objectives and the establishment of targets for performance, it provides clear parameters for expected performance by government (Shah and Shen, 2007). Unlike the conventional line-item budget, a performance budget comprises PI on each government programme, thus facilitating the public officials' task of providing information to the public about the programmes being undertaken and obtaining the public's

support for government's activities (Shah and Shen, 2007). McGeough (2014) argued that PI plays a critical role in discharging accountability for performance, as the public administration attempts to justify the utilisation of public funds and to respond to criticisms of poor performance. Lack of performance reporting indicates weak accountability, since the assessment of the organisation's performance by users of annual reports will be rendered more difficult; this will result in less pressure for the improvement of performance by management (McGeough, 2014).

Whilst PB might not alter the political budgeting process, the availability of PI adds value to the discussions involved when deciding on the resources to be allocated (Shah and Shen, 2007; McGeough, 2014). PI could prove useful in fund allocation decisions relating to new proposed programmes or in justifying funding decreases or increases (Shah and Shen, 2007).

Conventional budgets, which are typically presented on the basis of line-item inputs, do not provide meaningful information as to how government programmes are performing (Shah and Shen, 2007). In contrast, a performance budget organises funds by programmes and sets out performance measures and indicators, making it easier for the citizens to understand government's achievement vis-à-vis the activities being pursued (Shah and Shen, 2007). As a result, the budget document provides the public and the legislative body, with a tool of transparency and accountability for the results achieved by public officials (Shah and Shen, 2007). Sinclair (1995) has identified five forms of accountability as follows: (i) *political accountability* links the public official with the civil servant heading the ministry (Permanent Secretary), who, in turn, has to respond to the minister or to the Cabinet, to Parliament and to the electors; (ii) *public accountability* involves dealing with public concerns about administrative activity; (iii) *managerial accountability* is concerned with holding managers in the public sector accountable for meeting their budget (fiscal accountability) and for



delivering expected results (outcome or programme accountability); (iv) *professional accountability* arises from the public officials' duty to adhere to the standards of professional groups to which they belong; and (v) *personal accountability* involves being faithful to one's moral and ethical values.

## **2.5 Conventional budgeting**

The conventional (line-item) budget presents expenditures by inputs or resources purchased. A salient feature of a conventional budget system is to stipulate the line item ceiling in the budget allocation process, ensuring that government departments do not spend in excess of these caps (Shah and Shen, 2007). The strengths of such a system rest on its relative simplicity and the potential control of public spending in view of the detailed specification of resource inputs (Shah and Shen, 2007).

### **2.5.1 An illustration of a line-item budget**

An example of a conventional line-item budget is demonstrated in the table below – the figures, which are being presented for illustration purposes only, have been extracted from the 2016 Financial Estimates, compiled by the Ministry for Finance (2015d) in Malta.

**Table 5: Recurrent expenditure - Ministry for Education and Employment**

Expenditure by Standard Item	Actual	Approved	
	Expenditure	Estimate	Estimate
	2014	2015	2016
	€'000	€'000	€'000
Personal Emoluments	3,716	4,050	4,243
Operational and Maintenance Expenses	1,612	1,112	1,864
Programmes and Initiatives	98,601	96,572	114,797
Contributions to Government Entities	101,838	111,239	121,460
<b>Total Ministry for Education and Employment</b>	<b>205,767</b>	<b>212,973</b>	<b>242,364</b>

Source: Ministry for Finance, *Financial Estimates 2016* [<https://mfin.gov.mt/en/The-Budget>]

### 2.5.2 Limitations of line-item budgeting

The line-item budget has a number of limitations, as explained in the table below.

**Table 6: Limitations of line-item budgeting**

The line-item budget suffers from a number of weaknesses as detailed below:	
Limitation	Explanation
Lack of quality assessment	This form of budgeting makes it difficult to assess the quality of the services delivered by the government (Murray and Efendioglu, 2011). The focus is not on whether an item of expenditure is appropriate or whether a particular programme is effective, but on how much the cost has gone up or down compared to last year's budget. Furthermore, because line-item budgeting focuses on expense categories, the associated reporting systems provide information on how much is spent rather than how efficiently or effectively it was spent (Shah & Shen, 2007).
Short-term focus	As a process, line-item budgeting concentrates on year-to-year changes by revenue and/or expense categories and penalises, rather than rewards, cost-saving decisions (Murray and Efendioglu, 2011). Consequently, if a public official delivers the product or service with fewer resources than allocated in the budget, then the department's budget is usually reduced for the following year. This may result in spending decisions which lead to sub-optimal resource utilisation. Moreover, there is no medium-term perspective for budgeting, which might lead to expenditure planning problems for government.
Changing economic conditions	Line-item budgeting is especially ineffective during times of fiscal turbulence (Murray and Efendioglu, 2011). During times of economic uncertainty or in the midst of a fiscal crisis, government might need to effect budgetary expenditure cuts in an attempt to keep the government deficit under control. Jogiste et al (2012) remark that when resources are going to be limited, equal across-the-board cuts could be imposed by government, rather than decreasing resource allocation for ineffective or inefficient programmes. Thus the cuts in services and programmes are made without any identified connection to their value for the citizens and the benefits they provide for the country (Murray and Efendioglu, 2011).

## 2.6 Challenges to performance budgeting

In contrast with conventional line-item budgeting, PB seeks to introduce an incentive mechanism in the budgetary process. According to Kong (2005), in view of the fact that

conventional budgeting focuses on control, it promotes destructive budget maximising competition among agencies and discourages cost-saving efforts. *“Public managers are penalised for identifying and implementing cost-saving techniques... [in that] departments that realise cost savings through process improvement or managerial reforms may have their budgets cut in the following fiscal year and resources transferred to organisations that met or exceeded their funding levels”* (McNab and Melese, 2003: 78). PB shifts the focus from inputs to results and outcomes, and thus restrains the culture of using all the department’s funding for fear of having the expenditure cut the following year.

There are, however, challenges in the application of PB in the public sector as explained in the following table.

**Table 7: Challenges to PB**

The application of PB in the public sector comes up against a number of challenges	
Challenge	Explanation
Effect on fund allocation	The allocation of resources is mainly driven by traditional budget practice, whilst PI is used to support internal management decisions on setting priorities and adjusting operations (OECD, 2002a). In this regard, PB initiatives have been successful in managing programmes, but have had little influence in affecting actual appropriations (Willoughby and Melkers, 2000; Broom and McGuire, 1995; Ho, 2011). Wildavsky (1961) noted that the principal purpose of budgetary reform is changing fund allocations, <i>“Otherwise, why bother?”</i>
Use of outcome information	According to Aristigueta and Justice (2006), an issue that arises is how outcome information is to be applied in the allocation of resources. If the PI indicates that a programme is effective, will the allocation of additional funds generate more valued outcomes, or should government cut the programme budget and still get the targeted results? On the other hand, where a programme is underperforming, should government allocate more money because the ineffectiveness is a sign of underfunding or should the programme be terminated to stop wasting public funds? (Aristigueta and Justice, 2006). On a similar note, Caiden (1998: 44) commented that <i>“If a programme is doing badly, and showing few results, does this mean it should be terminated, or provided with more resources to do a better job? Conversely, if a programme is doing well and achieving its objectives, should it be provided with more resources to do an even better job, or should it be cut back on the grounds that its purpose has been achieved and it is no longer needed?”</i>

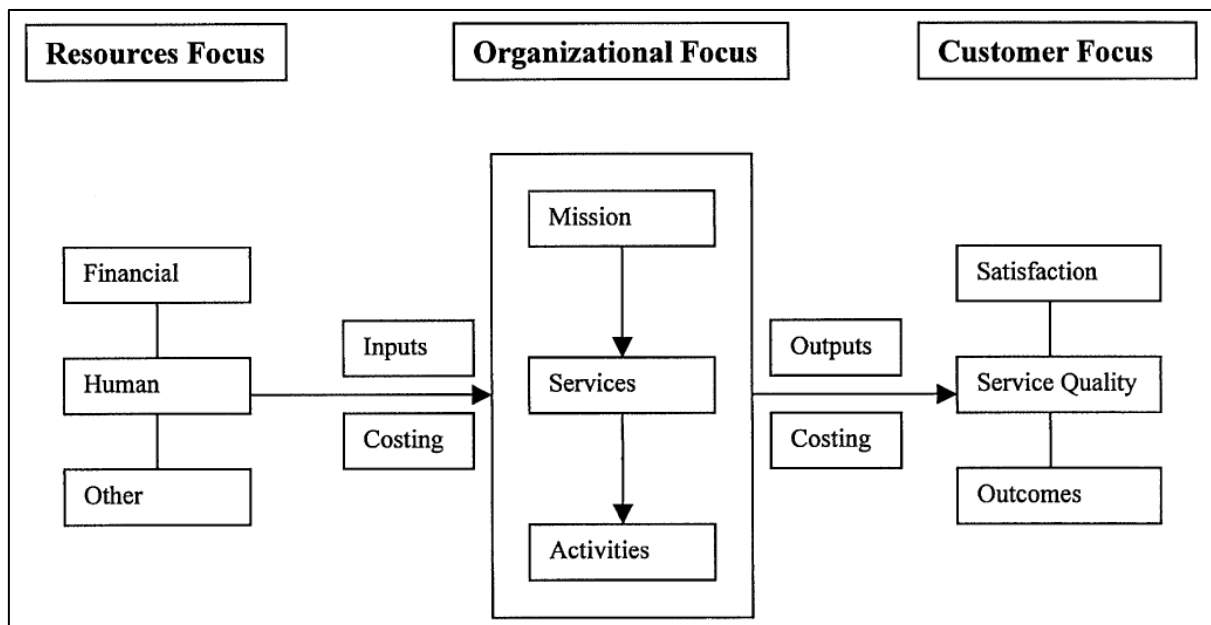
Target setting	In the political background surrounding public budgeting, setting up outcome targets which are agreed upon by various stakeholders is not a simple task. Furthermore, even if agreeable outcome targets are established, it will be difficult to determine who is responsible for the outcomes because of a multitude of factors including time lag and uncontrollability (Kong, 2005). The impact of some programmes may not be seen for years and this factor invalidates annual incentive systems whilst at the same time encourages public officials to aim for short-term outcomes (Kong, 2005). Additionally, some outcomes are not within the direct control of public officials (Stiefel et al., 1999). Under this scenario, it is inappropriate to provide rewards or impose penalties.
Cultural change required	PB is not universally used today by local governments (Murray and Efendioglu, 2011). Firstly, a shift from conventional to PB requires a culture change, which is both time-consuming and expensive (Murray and Efendioglu, 2011). Secondly, the main motivation for shifting to PB usually is the result of citizens' initiative, rather than legislation (Murray and Efendioglu, 2011). These initiatives are time-consuming and expensive and require significant effort by citizens to develop plans, determine targeted outcomes and monitor the process to ensure that the cultural change occurs (Willoughby and Melkers, 2005).
Leadership skills	The implementation of a reform in the public sector requires strong leadership. Good leadership provides a clear vision of the PB system with well-documented directives and it should bring in all stakeholders - policy makers, citizens, clients, budget analysts, outside consultants, department heads, managers and unions - throughout the whole planning and implementation process (Kong, 2005).
Adequate resources	A common issue in the implementation of new systems within government is that they are often launched without adequate financial and human resources (Kong, 2005). Kong (2005) also claims that many new systems fade away due to the lack of financial or human support. Apart from human and financial resources, " <i>budget process reform requires a significant investment in accounting and information systems</i> " (McNab and Melese, 2003: 80). Furthermore, a reasonable timeframe is critical for the successful implementation of the new system. The timeframe should take into account both the time required for the mechanics of the reform and also the time necessary for behavioural changes (Kong, 2005). A hurdle to creating and maintaining an effective PB system has been insufficient capacity to develop high quality mechanisms to track and report PI (Kopczynski and Lombardo, 1999).

## 2.7 A performance budgeting system

Public budgets increasingly contain information about outputs and outcomes in addition to the traditional information about the inputs and activities (OECD, 2002b).

The figure below identifies the main elements of a budgeting system, namely resource allocation, organisational management and customers. Traditional line-item budgeting focuses on the allocation of resources including funding, human resources, facilities and equipment (Kong, 2005). The early forms of PB were focused on organisational elements such as the mission statement, policy goals, services and activities (Kong, 2005). In later years, the focus of PB shifted to outcomes, service quality, and citizen/customer satisfaction (Kong, 2005).

**Figure 3: The focus of budgeting: conventional vs. performance-based (Source: Kong, 2005: 96)**



### 2.7.1 Performance measures

Robinson and Brumby (2005) note that the development of performance measures – including output and outcome measures – is a necessary precondition of PB and this is something which takes both time and serious effort. A performance measure is a “*quantifiable expression of the amount, cost, or result of activities that indicate how much, how well, and at what level, products or services are provided to customers during a given time period*” (Office of

Financial Management, 2011: 1). Performance measures provide a snapshot of current performance capabilities and track whether actual performance is getting better, staying the same, or getting worse over time (Office of Financial Management, 2011). Performance measurement facilitates accountability and attempts to gauge whether progress is being made towards achieving the targets.

Performance measures are linked to time-frames - annual, intermediate, and long-term. Annual measures are relevant for annual performance evaluation and budget appropriations; intermediate measures, mostly in a 3-5 year range, are designed to assess the early results of a programme and are useful when the objectives of the programme will not be achieved until years into the future (Tigue and Greene, 1994). The meaningful use of long-term, strategic measures (mostly in a 10 year range) is almost non-existent (Kong, 2005). The different types of measures are explained in the table hereunder.

**Table 8: Types of performance measures**

Performance measures	
Type	Description
Input measures	These measures, which have been the core of conventional budgeting, provide information as to the amount of resources required to offer a product or service (Kong, 2005). These measures show the total cost of providing a product or service, the mix of resources used to provide the service, and the amount of resources used for one service in relation to other services (Tigue and Greene, 1994).
Output measures	These measures, which are the most common measures of the earlier versions of PB, focus on the organisational activities required for the provision of a product or service. Workload measures, which are designed to show how staff time will be allocated to respond to service demand, are most commonly reported. Output measures can be a significant operational/managerial tool, but they may be of limited interest to elected officials and citizens (Tigue and Greene, 1994). Output measures are usually the easiest kind of data to obtain and are the least sensitive or threatening in an evaluation context (Poister and Streib, 1999).
Outcome measures	These are used to assess the quality of programmes and to evaluate whether a service/programme is meeting its predetermined objectives. Though outcome measures are of greatest interest to citizens and policy makers, they are the least utilised, partly, in view of the cost of gathering the information needed to produce the measures and also, due to the difficulty of ascertaining the relationship between the government programme and the needed outcome (Tigue and Greene, 1994).
Citizen satisfaction	This represents an external measure, focusing on customers. The measurement of citizen satisfaction can be problematic: <i>“It is unclear what criteria the citizens are using to evaluate effectiveness. Also questionable is how much accurate information citizens have on which to base their evaluations”</i> (Kelly and Swindell, 2002: 610). In addition, Vigoda (2002) claims that the users of ‘client/citizen satisfaction’ measures may run a risk that such measures may overestimate short-term considerations and popular decisions, and may not represent the true voice of the majority.
Cost measures	Cost measures provide information to evaluate cost-efficiency and cost-effectiveness. Cost efficiency refers to unit costs for output measures while cost-effectiveness refers to unit costs for outcome measures (Kong, 2005). Cost measures will be more important as indirect and overhead costs have become a much greater portion of total costs while labour cost as a percentage of total costs is decreasing (Brown et al., 1999).

An important consideration to make is that all types of measures are inter-linked. Although each type of measure has some value, it appears that more governments are inclined to use outcome measures and client/citizen satisfaction (Kong, 2005).



### **2.7.2 An illustration of performance budgeting**

By shifting the emphasis from inputs to results, the performance budget moves away from a discussion of detailed line items, focusing instead on the overall objectives and performance targets of government programmes – this leads to more informed decision-making in the budgetary context (Shah and Shen, 2007).

The table below provides an illustration of the application of PB within Australia’s Education Portfolio. The figures, which are provided for illustrative purposes only, have been extracted from the Portfolio Budget Statements for 2014–15 and relate to the ‘Child Care Benefit’ programme. The table shows that the budgeted expenditure allocated to this programme is being linked to the quantification of the deliverables expected to be achieved and the key performance indicators identified for the programme.

**Table 9: Australia's Child Care Benefit Programme**

<b>Programme 1.2 - Child Care Benefit</b>					
<b>Performance objectives:</b>					
Assists parents with the cost of approved and registered child care. The provision of this assistance means more families are able to access quality child care services.					
<b>Administered items:</b>					
The payment of Child Care Benefit (CCB) varies depending on family income, the number of children in care, the hours of care, and the type of child care used. Low income families receive the highest rate of Child Care Benefit.					
<b>Programme expenses:</b>					
	2013-14 Estimated actual \$'000	2014-15 Budget \$'000	2015-16 Forward Estimate \$'000	2016-17 Forward Estimate \$'000	2017-18 Forward Estimate \$'000
Total programme expenses	2,359,607	3,140,717	3,294,464	3,494,066	3,721,701
<b>Deliverables:</b>					
	2013-14 Revised Budget	2014-15 Budget	2015-16	2016-17	2017-18
Number of children using approved child care places	1,436,000	1,570,000	1,620,000	1,672,000	1,725,000
Number of families using approved child care services	998,000	1,091,000	1,125,000	1,161,000	1,199,000
Number of families using approved child care services and receiving a child care payment (percentage of families who use care and receive a payment)	978,000 -98%	1,069,000 -98%	1,103,000 -98%	1,138,000 -98%	1,175,000 -98%
Number of families receiving both CCB and Child Care Rebate	686,000	750,000	774,000	799,000	824,000
Number of families receiving only CCB	89,000	97,000	100,000	104,000	107,000
<b>Key performance indicators:</b>					
	2013-14 Revised Budget	2014-15 Budget	2015-16	2016-17	2017-18
Percentage of child care out-of-pocket expenses as a proportion of weekly disposable income after child care subsidies	8 to 12%	8 to 12%	8 to 12%	8 to 12%	8 to 12%

Source: Department of Education, Government of Australia, 2014

## **2.8 Accrual accounting and budgeting**

The purpose of this section is twofold: (i) to consider the use of the accrual basis for budgeting; and (ii) to ascertain whether the accrual basis is a prerequisite for the implementation of PB.

### **2.8.1 The accrual basis**

The adoption of accrual accounting and budgeting is controversial and has been extensively debated in the public sector accounting literature (Martí, 2006).

In terms of the International Public Sector Accounting Standards (IPSAS, 2009: 1513), accrual accounting is defined as “*a basis of accounting under which transactions and other events are recognized when they occur (and not only when cash or its equivalent is received or paid)*”. The objective of adopting the accruals basis for historical financial reporting is to make the real cost of government services more transparent; for example, when undertaking capital projects, these are incorporated into the annual operating expenditure through a depreciation charge, instead of having spikes in expenditure when capital projects are carried out (Blöndal, 2003). A further objective for adopting accruals is to improve decision-making in government by using this enhanced information (Blöndal, 2003). In 1992, New Zealand became the first country in the world to produce Whole of Government financial statements on a full accrual basis (Pallot, 2001).

### 2.8.2 Accrual budgeting

Cash and accruals<sup>3</sup> represent two extremes on a continuum of possible budgeting bases. Between these extremes, a number of variations have been applied by countries in practice. According to Robinson (2009: 3), accrual budgeting “*means that spending ministries are given budgets which are defined in terms of accrual concepts...the budget sets quantitative limits on the expenses which they incur rather than the cash payments they make.*” Accrual budgeting refers to the use of accrual accounting records and measures in the budgeting process (Lüder and Jones, 2003: 35). The main benefits of accrual budgeting include (1) the improvement in the effectiveness and efficiency of expenditure and (2) the improvement in decision-making with regard to assets (Robinson, 2009). Expenditure prioritisation is enhanced in view of the fact that budgetary decisions are made on the basis of the true costs of the inputs required to produce public goods or services (Robinson, 2009). Decisions related to the acquisition, disposal and maintenance of fixed assets, as well as those related to the management of stocks are enhanced; ministries are encouraged to sell surplus assets, thus reducing their depreciation charge and permitting increased spending on other types of expenses (Robinson 2009).

With regard to the implementation of accrual budgeting, Sterck and Scheers (2006) distinguish three groups: (a) countries that have adopted full accrual budgeting, (b) countries

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<sup>3</sup> Cash basis accounting is a method of bookkeeping that records financial events based on cash flows and cash position (Sterck, 2007). Revenue is recognised when cash is received and expense is recognised when cash is paid (Sterck, 2007). On the other hand, accrual basis accounting records financial events based on events that change your net worth (Sterck, 2007). Revenues are recorded in the period in which they are generated and expenses are recorded in the period in which they are incurred (Sterck, 2007). Even though cash is not received or paid in a credit transaction, they are recorded because they are consequential in the future income and cash flow of the organisation (Sterck, 2007). In fact, cash is an inherent feature of the accruals basis - accruals records transactions both on an accruals basis, as described above, and on a cash basis. The operating (profit and loss) statement presents the information on an accruals basis and the cash-flow statement presents the information on a cash basis (Blöndal, 2004).

that have partly implemented accrual budgeting, and (c) countries with a budget system based on cash and commitments.

According to Blöndal (2003), there is much greater acceptance of accruals for financial reporting than for budgeting purposes. The reasons for this are that, firstly, the accrual budget is believed to risk budget discipline because only cash provides a match between when money is spent and when it is reported in the budget; secondly, the accruals basis is believed to be extremely complex. With respect to the first issue mentioned, whilst accounting for current budgeted expenditure in accrual terms does not result in significant changes because accrual and cash measurement are almost the same, accrual budgeting delays cost recognition of capital expenditure compared with a cash-based budget (Martí, 2006). However, the problem with applying accruals only to financial reporting and not to budgeting is that there is a risk that the historical financial statements might become a purely technical accounting exercise. This is because the budget is the key management document in the public sector, and if it is on a cash basis, it will serve as the main basis on which politicians work (Blöndal, 2003).

### **2.8.3 Accrual basis – Financial statements versus budgets**

The table below lists some OECD countries and indicates the basis of accounting adopted by each country in the reporting of historic financial information and in the budgeting system. The information contained therein demonstrates that the majority of these countries are using accruals accounting in their historic financial statements and a number of countries are in transition to accruals. With respect to the budgeting system, very few countries have adopted or are in the process of switching to accrual budgeting.

**Table 10: Basis of accounting for financial statements and budgets**

Country	Financial statements	Budgets
Australia	Full accruals	Full accruals
Austria	Full accruals (Public Service Pensions excl.)	Full accruals (Public Service Pensions excl.)
Belgium	Full accruals (Public Service Pensions excl.)	Full accruals (Public Service Pensions excl.)
Brazil	Cash – Transitioning to Accruals	Full Cash
Canada	Full accruals	Full Cash
China	Cash – Transitioning to Accruals	Full Cash
Czech Republic	Full accruals (Public Service Pensions excl.)	Full Cash
Denmark	Full accruals (Public Service Pensions excl.)	Full accruals (Public Service Pensions excl.)
Estonia	Full accruals	Cash – Transitioning to Accruals
France	Full accruals (Public Service Pensions excl.)	Full Cash
Germany	Full Cash	Full Cash
Greece	Cash (Supplementary Accrual Information Provided)	Full Cash
Hungary	Full accruals	Full Cash
Iceland	Full accruals (No Capitalisation / Depreciation of Assets)	Full accruals (No Capitalisation / Depreciation of Assets)
Ireland	Cash (Supplementary Accrual Information Provided)	Full Cash
Italy	Cash (Supplementary Accrual Information Provided)	Cash (Supplemental Accrual Information Provided)
Japan	Cash (Accrual Basis Statements Also)	Full Cash
Korea	Full accruals	Full Cash
Latvia	Full accruals	Full Cash
Lithuania	Full accruals (Public Service Pensions excl.)	Full Cash
Luxembourg	Cash (Supplementary Accrual Information Provided)	Full Cash
<b>MALTA</b>	<b>Cash (Supplementary Accrual Information Provided)</b>	<b>Full Cash</b>
Mexico	Full Cash	Full Cash
Netherlands	Cash (Agency Reporting on Accruals)	Full Cash
New Zealand	Full accruals	Full accruals
Norway	Cash (Supplementary Accrual Information Provided)	Cash (Supplemental Accrual Information Provided)
Poland	Full accruals	Full Cash
Portugal	Cash (Agency Reporting on Accruals)	Full Cash
Slovak Republic	Full accruals (Public Service Pensions excl.)	Full Cash
Spain	Full accruals (Public Service Pensions excl.)	Full Cash
Sweden	Full accruals	Cash (Running Costs on Accruals)
Switzerland	Full accruals (Public Service Pensions excl.)	Full accruals (Public Service Pensions excl.)
UK	Full accruals	Full accruals
USA	Full accruals	Cash (Loan and Guarantee Programmes on Accruals)

Source: OECD (2015)

#### **2.8.4 Is the accrual basis required to implement performance budgeting?**

PB and the accrual basis are among the most prominent reforms on the budget agenda (Schick, 2007). In the context of public financial management reform, with its emphasis on performance, the need to introduce the accrual basis was identified in order “*to encompass accounting and reporting on the allocation and use of total economic resources (both cash and non-cash) at the disposal of managers*” (OECD 1993: 3). Mauro et al (2015) opine that the link between accrual accounting and PB is not fully explored, while Diamond (2002) rejects the assumption that PB requires accrual accounting. The experience of countries that have cash budgets, such as Canada, the US, Sweden and the Netherlands, demonstrates that accrual budgeting is not necessarily required for the purpose of implementing PB (Sterck, 2007). Diamond (2002) argues that the implementation of an accrual-based system for government accounting, given the costs involved, is perhaps only worthwhile in the context of an overall transformation of public sector management. In view of the fact that the introduction of accrual accounting is hardly a costless exercise, it is important to recognise that there may be intermediate solutions or alternative ways of gaining some of the benefits afforded by accrual accounting (Diamond, 2002). Furthermore, Diamond (2002) notes that in assessing the need for accrual accounting in the implementation of PB, the focus should be on why there is the need for the additional information obtained from an accrual accounting system.

Though not a prerequisite for implementing PB, accrual budgeting can add value to PB in various ways, including providing a measure of the full cost of outputs in the budgetary statements, measuring efficiency and cost-effectiveness of the services provided and basing expenditure prioritisation on the full costs of programmes within a medium and long-term expenditure framework (Martí, 2013).

## 2.9 Countries’ experiences with performance budgeting systems

A number of countries have been working on introducing PI into budgeting for various years (OECD, 2007). The major reform motivators are summarised as financial crisis pressure to reduce public expenditures, improve efficiency and reduce waste; and a change in political administration (OECD, 2007).

### 2.9.1 Implementation strategies

The OECD (2007) undertook a study on the PB reforms in eight OECD countries. The table below summarises the implementation strategies adopted in these countries.

**Table 11: Summary of country implementation strategies**

	Strategies		Coverage		Timescale	
	Top-down	Bottom-up	Comprehensive	Partial	Big bang	Incremental
Australia		√	√			√
Canada	√		√			√
Denmark		√		√		√
Korea	√			√	√	
Netherlands	√		√		√	
Sweden		√		√		√
UK	√		√			√
US	√		√			√

*Source: OECD (2007)*

As illustrated in the above table, OECD countries have adopted diverse implementation strategies for introducing PI into budgeting systems. This reflects the countries’ cognizance that there is no ‘best practice’ in the implementation of these reforms, but each country has to design and adapt such reforms to its own priorities, culture and national capacities.

One of the considerations that a country needs to make is whether the reform should be enacted in law - if the reforms are introduced through legislation, this ensures some form of



permanence because if there is a change in government, it might be easier for the reform to continue (OECD, 2007).

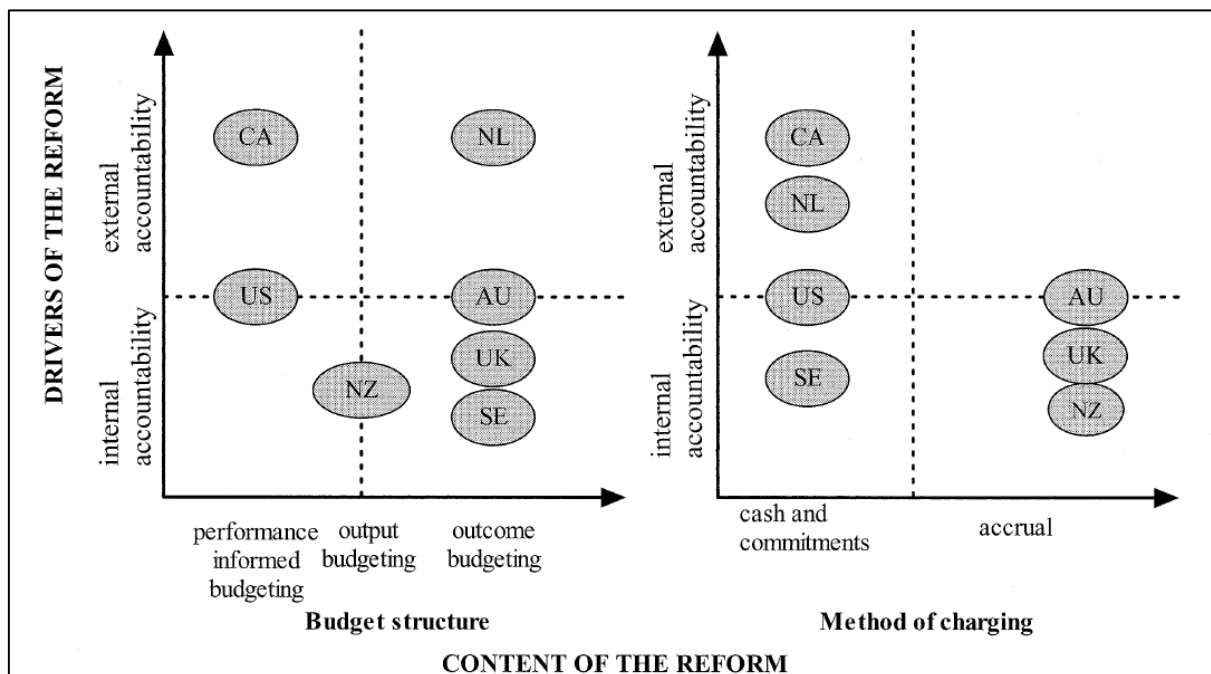
Another issue to be taken into account is whether to adopt a top-down versus a bottom-up implementation approach. In the top-down approach, the central government agency (the MOF, the Office of the Prime Minister (OPM) or the Cabinet office) has a primary role in developing, implementing and monitoring the reforms (OECD, 2007). With a bottom-up approach, the individual departments develop their own approaches and there is less enforcement from the top (OECD, 2007). There are risks involved in both extremes. A too centralised (top-down) approach can result in PB becoming a compliance exercise with the risk of turning into an expensive paper exercise (OECD, 2007). In contrast, with too little central involvement, the pressure for change is reduced and in addition, there can be lack of consistency in the presentation of PI such that comparisons across government departments would be difficult to make (OECD, 2007).

A further question to answer is whether to adopt a big bang versus an incremental implementation approach. An incremental approach (as adopted by Australia) implements change on a step-by-step basis, whilst a big bang approach (as adopted by Korea) introduces a number of sweeping reforms at the same time (OECD, 2007). A big bang approach is likely to be implemented in situations where the drivers for change are strong such as a change in government or an economic crisis (OECD, 2007). The drawback of this approach is that it requires a high level of political and financial commitment which might be difficult to achieve in many countries (OECD, 2007).

### 2.9.2 Different types of performance budgeting systems

Sterck and Scheers (2006) carried out a study covering seven OECD countries, which adopted different types of PB (Australia, Canada, New Zealand, Sweden, the Netherlands, the UK, and the US). Figure 4, below, gives an overview of the types of PB reforms implemented in these seven countries. On the x-axis the content of PB reforms is shown, whilst the y-axis shows the drivers of the budget reform.

**Figure 4: Drivers and content of PB reform (Source: Sterck and Scheers, 2006: 66)**



The study shows two major trends in public budget format change: (a) an evolution toward output and outcome budgeting, and (b) a tendency toward accrual budgeting. The most advanced budget formats are the accrual-based appropriation budgets that are structured along outcomes, which is the case in Australia and the UK. The Netherlands has taken the step toward an outcome budget, but the method of charging is still based on cash and commitments, except for the executive agencies. The Swedish government has also

introduced outcome budgeting. The New Zealand public administration has an accrual-based output budget in place and makes appropriations for outputs instead of outcomes, while explaining the connection between outcomes and outputs in supplementary documents. The study also revealed that other countries such as Canada and the US make appropriations for outcomes and outputs but use the output and outcome information only to inform the budgetary decision-making. The output and outcome information is then reported in the non-authorised part of the budget (explanatory memorandum) or in separate performance plans. The method of charging in these countries is based on cash and commitments.

The above analysis demonstrates that the implementation of PB does not require an accounting basis based on accruals. A number of countries have implemented PB but are still operating a budgeting system based on cash and commitments. This ties in with Diamond's (2002) conclusions which reject the assumption that PB requires accrual accounting.

Sterck (2007) carried out a study covering four countries which adopted different types of PB: Australia, Netherlands, Sweden and Canada. These countries were selected because they are forerunners in results-oriented financial management (Sterck and Scheers, 2006). The following diagram summarises the PB systems adopted in the countries subject to the study.

**Figure 5: Description of four cases (Source: Sterck, 2007: 193)**

	AUS	CA	NL	SE
Executive government	Majoritarian <sup>a</sup>	Majoritarian	Consensual	Intermediate
Output and outcome information	Outcome information in authorized Budget Bill	Output and outcome information in explanatory documents	Outcome information in authorized Budget Bill	Outcome information in authorized Budget Bill
Cash or accrual? <sup>b</sup>	Accrual budgeting	Modified accrual	Cash and commitments (except for agencies)	Cash and commitments

Note a: A majoritarian electoral system is one which is based on single member constituencies.

Note b: In cash basis accounting, financial events are recorded on the basis of cash flows and cash position; in accrual accounting, financial events are based on events that change the net worth.

### 2.9.3 Use of performance information – studies' results

In their study of PB reforms in the seven countries identified earlier on, Sterck and Scheers (2006) sought to assess the extent to which resource allocation depended on performance. Although an evolution toward output and outcome budgeting was observed among these countries, Sterck and Scheers (2006) concluded that PI is not extensively used in final allocation decisions.

In his study of PB systems in four countries (Australia, the Netherlands, Sweden and Canada), Sterck (2007) observed that though the PB reforms had the objective of increasing the transparency of the budget, the complexity of budgeting may increase. This complexity is augmented when outcome/output budgeting is combined with accrual budgeting. Sterck

(2007) suggests that in order to encourage Members of Parliament (MPs) to find the right information and to use it, there is the need for increased communication about reforms and rigorous training for MPs. The study concluded that the PB reforms, which were introduced with the aim to enhance accountability to Parliament, emphasise the alteration of the budget structure and the format of the budget documents, but do not seem very successful in changing the budget functions. In fact, Sterck (2007) found little evidence that PI in budgets and annual reports is directly used by MPs in their oversight function.

Empirical literature covering PI use in the public field has been increasing (Willoughby and Melkers, 2005; Pollitt, 2006; Askim, 2007; Moynihan and Pandey, 2010; Taylor, 2009 and 2011; Demaj and Summermatter, 2012; Hammerschmid et al 2013; Kroll, 2014).

There is supporting evidence showing that politicians are only moderately interested in PI (Willoughby and Melkers, 2005; TerBogt, 2006; Jansen, 2008; Montesinos et al, 2013; Mimba et al, 2013; Saliterer and Korac, 2013). Raudla's (2012) study indicated that members of the finance committee of the Estonian Parliament make only limited use of PI for budget decision-making; instead they rely on informal networks for collecting the data deemed necessary for budget negotiations. Furthermore, the interview data showed that PI is not discussed during the meetings of the finance committee and some members never read documents containing PI. The study revealed that the main reasons for the lack of use of PI by the Estonian finance committee were: documents comprising PI are too long; the budget process is constrained by a very limited time-frame; and the parliament's input for changing the budget is limited. In their research, Ter Bogt et al (2015) observed that, during Council and Council committee meetings, councillors of the province of Groningen (Netherlands) make very limited use of PI incorporated in the budget for their decision-making and control functions. Empirical data gathered through twenty-one interviews with Estonian civil servants

showed that in specific circumstances of cutbacks in budgets, PI plays a marginal role (Raudla and Savi, 2015). Kroll (2013) found that public managers favour non-routine PI, such as ad hoc, verbal and qualitative feedback over systematic and formal data set out in performance reports.

Contrary to this, Askim (2007) found that local councillors in Norway use PI actively. Similarly, Liguori et al (2012), who studied Italian municipalities, showed that PI played an important role in politicians' decision-making. A comparable situation was observed by Bjornholt and Houlberg (2013) in Danish municipalities; however, the authors also found that political actors are generally unable to link PI to budgetary decisions. A survey distributed to public sector executives from six European countries found that the *availability* of PI is mostly relevant in influencing the use of such information by public managers (Hammerschmid et al 2013). Demaj and Summermatter (2012: 93) suggest that PI is "*first and foremost meant to provide the basis for performance appraisals by politicians*".

The results of the OECD 2005 Questionnaire (Curristine, 2005) indicate that the primary objectives listed by responding countries for introducing performance measures in budgeting include the improvement of efficiency and effectiveness of government programmes and the provision of more concrete information to government on performance for decision-making purposes and for setting future targets and priorities. The secondary aims listed include helping to reduce expenditure, providing information to help reallocate resources between programmes and providing a mechanism for the MOF to monitor the activities of government organisations. There are, of course, challenges that need to be managed. The main challenges that the responding countries came across when introducing performance measures comprise difficulties in attributing outcomes to specific programmes, difficulties in designing measures for specific activities, insufficient political support, unclear objectives and poor quality data.

This research concludes that the majority of OECD countries have introduced performance-informed budgeting. These countries make use of performance measures in the budget process; however, the performance data is used to provide information but does not determine budget allocations.

A study comparing performance reporting between the UK and Ireland concluded that political drive is fundamental for stimulating the use of PI and the development of performance targets (McGeough, 2014). If PI is demanded by the political system, it will be provided and will then be used as the basis for dialogue between the civil service and the politicians (McGeough, 2014). Another element which enhances the value of PI and thus increases its use is the quality of such information (Ter Bogt et al, 2015).

The OECD 2011/2012 Performance Budgeting Survey (von Trapp, 2014), in which thirty-one OECD member countries and the Russian Federation participated, found that PB practices are widely used but vary considerably between countries. Furthermore, it was revealed that there is only a loose/indirect link between PI and funding decisions. In effect, it appears that PI is useful for accountability purposes, but not so much for resource allocation. As such, the resource allocation process remains a political procedure. The survey results also showed that the main institutions responsible for setting performance targets are the line ministries and agencies. In addition, there seems to be less reliance on PI in budget negotiations between the central budget authority and line ministries than revealed in past surveys; furthermore, in some cases PI is not being used.

According to the results of their study amongst US states, Jordan and Hackbart (1999) determine that using performance to impact budget allocations may be implied but is seldom used. Jordan and Hackbart (1999: 85) suggest that “*performance budgeting may impact*

*appearance and preparation of the budget document, but the outcome in terms of funding is not significantly (if at all) affected*". This reasoning mirrors the conclusions reached by Sterck (2007) as outlined above. A reason for the continued efforts at PB is the need for public accountability and taxpayer support of expenditures (King, 1995). Another study of state governments in the US (Melkers & Willoughby, 1998) also found little evidence of the use of PI to influence funding decisions. A survey carried out by Melkers et al (2002) on behalf of the Governmental Accounting Standards Board (GASB) found that only 7.5% of state budget offices considered performance measures as 'effective' or 'very effective' in changing budget allocations. Research carried out by Ho (2011) also confirmed that the role played by PB in determining final budget appropriations is limited; however, PB still adds value to budget discussions during the budgetary process. Ho (2011: 393) advised that "*modern conceptions of PBB [performance-based budgeting] have mostly abandoned any traditional notions that appropriation amounts should be solely based on performance*". Using an experimental approach to gain insight as to how PI is used, Moynihan (2016) concluded that resource allocation is influenced by more than performance data and depends on other variables such as the characteristics of the information, the communication skills of those providing the data and the context in which the information is presented.

#### **2.9.4 Lessons learnt**

A study covering six countries in emerging Europe, written by a World Bank team, highlights some potentially valuable lessons in the implementation of budget reforms, as detailed in the table below. The countries selected for the purposes of this study were Bulgaria, Croatia, Latvia, Poland, Slovakia and Turkey (Kąsek and Webber, 2009).



**Table 12: Lessons in the implementation of budget reforms**

Valuable lessons in the implementation of budget reforms	
Lesson learnt	Explanation
Duration of the reform process	Countries which undertake budget reforms should expect a long implementation process, involving a complex and challenging learning experience and requiring continuous enhancement in systems and procedures. To ensure systemic change, key stakeholders have to provide support to all concerned in solving the difficulties and obstacles encountered along the way (Kąsek and Webber, 2009).
Leadership	Strong leadership, supported by political commitment, are fundamental for undertaking successful budgetary reform (Ho, 2011). It is valuable to have key people in ministries who champion the change, both at the outset and for maintaining the drive for change. There should be general support for the reforms, on the basis that they are fundamentally important for public sector efficiency and modernisation. If the reforms are identified with one political party, there is the risk of abandonment should a different party be in public office (Kąsek and Webber, 2009).
Relevant skills and capacities	It is important to develop the necessary capacity and skills within the MOF and other entities, such that successful implementation of the budgetary reform could be achieved. Mimba et al (2013: 16) claim that “ <i>a low institutional capacity is a hindrance for the design and use of adequate accounting systems, including performance measurement systems</i> ”. Self development should be promoted amongst employees working within the public sector environment, in order to build the required budget management knowledge, which includes technical abilities, managerial capabilities and problem solving skills (Kąsek and Webber, 2009).

On a concluding note, a PB system can inform decision-making when such system is properly integrated into the budgeting process, its purpose is comprehended and the performance measures are reliable (Willoughby, 2011). Furthermore, Willoughby (2011) maintained that championing by key people and constant improvement to the system strengthen the effectiveness of a PB system.

**CHAPTER 3:**  
**LITERATURE REVIEW II**  
***THEORETICAL***  
***FRAMEWORK***

### **3.1 Background**

This chapter presents the theoretical framework underlying the study. Section 3.2 sets out the institutional concepts which explain *why* the Maltese public administration might transition from the existing line-item budgeting system to a performance based system. Subsequently, the policy implementation theory, explained in section 3.3, provides insights as to *how* PB should be implemented in Malta and identifies potential issues around implementation.

### **3.2 Institutional theory**

#### **3.2.1 Introduction**

Institutional theory is being employed to explain the budgeting system choice in the Maltese public sector. The existing conventional budgeting system is a strongly institutionalised procedure and has been deeply grounded in the Maltese public administration's practices. Institutional theory suggests that the Maltese government may eventually be inclined to implement a PB system to replace the current traditional budgeting system because of institutional pressures. The analysis draws on DiMaggio and Powell's (1983) concept of institutional isomorphism to explain these institutional pressures. Greenwood and Hinings' (1996) framework of organisational change is also being used to explain the type of organisational change that may be expected in the Maltese public sector to implement a PB system and move away from the currently embedded system.

The section below sets out an overview of the insights into institutional theory put forward by various academics and researchers. This is then followed by a review of the theoretical model for understanding change, proposed by Greenwood and Hinings (1996). Subsequently, a preliminary application of institutional theory to the Maltese scenario is presented, which

comprises a discussion of the institutional pressures for change within the local budgeting framework, using the concept of institutional isomorphism proposed by DiMaggio and Powell (1983); as well as an analysis of the potential expected change in the local budgeting system, based on Greenwood and Hinings' framework (1996).

### **3.2.2 Theoretical overview**

A generally used definition of 'institution' is: "*a way of thought or action of some prevalence and permanence, which is embedded in the habits of a group or the customs of a people.*" (Hamilton, 1932, cited in Burns and Scapens, 2000: 5).

Institutional theory is concerned with how organisations are influenced by forces outside their control (Hoffman, 1999) and is developed on the concept that institutional environments are constructed within a society (DiMaggio and Powell, 1983). Thus, the institutional environment and the participants therein influence and mould organisational systems and behaviours (Munir et al, 2011). From an institutional perspective, organisations are viewed as functioning within a framework of values, norms and taken-for-granted assumptions which define acceptable and appropriate behaviour (Oliver, 1997). Institutional theory presumes that organisations implement management practices and structures which are viewed as legitimate by other organisations practising in the same field, irrespective of their real usefulness (Carpenter and Feroz, 2001). It assumes that the structure of the organisation is primarily determined by the pressure applied by external and internal players on the organisation in order for it to follow a set of norms and thus, secure long term survival and access to resources and ultimately, achieve legitimacy (Brignall and Modell, 2000).

The principal works underpinning the new institutional theory are those of Meyer and Rowan (1977) and DiMaggio and Powell (1983). New institutionalism presumes that organisations

respond to pressures from their environment by adopting organisational procedures which are considered as appropriate and which are socially accepted (Carpenter and Feroz, 2001). Meyer and Rowan (1977: 344) claim that institutionalised techniques are not based on efficiency but are used “*to establish an organisation as appropriate, rational and modern. Their use displays responsibility and avoids claims of negligence.*”

Powell and DiMaggio (1991) describe ‘new institutionalism’, as focusing on the ways in which order and structured actions are facilitated by shared rules which, on the one hand, restrict the ability of groups to optimise and, on the other hand, favour some actors whose interests are guarded through existing sanctions and rewards.

Institutions are often regarded by social theorists as instruments which restrain, prohibit and control behaviour; however, it must be appreciated that institutions likewise provide support and give power to players and their activities (Scott, 2014). Jepperson (1991: 146) observes that “*institutions simultaneously empower and control*” and Fararo and Skvoretz (1986: 227) describe institutions as having “*a constraint/freedom duality*”. Constraints are laid down by institutions because they differentiate between appropriate and inappropriate behaviour, by delineating ‘legal, moral and cultural boundaries’; on the other hand, institutions make available resources and set out guidelines for the players within such institutions (Scott, 2014). Institutions can be passed on through generations (Zucker, 1977) and they can be somewhat resistant to change (Jepperson, 1991). Scott (2014) suggests that although institutions seek to offer order and stability, they go through change, which could be both revolutionary and incremental.

The sociological perspective of institutional theory is especially relevant when studying implementation because questions are raised about the degree to which human actions are

determined in a structural manner and emphasis is placed on organisational activities which are clearly pertinent when assessing implementation (Hill and Hupe, 2014). Institutional theory takes into account the conflicting interests and power relationships between the different stakeholders (Brignall and Modell, 2000).

An important influence on institutional theory was the work of Selznick (1957) who distinguished between ‘organisations’ and ‘institutions’ as follows:

*“The term ‘organisation’ ... suggests a certain bareness, a lean no-nonsense system of consciously coordinated activities. It refers to an expendable tool, a rational instrument engineered to do a job. An ‘institution’, on the other hand, is more nearly a natural product of social needs and pressures – a responsive adaptive organism.”*  
(Selznick, 1957: 5)

The distinction illustrated above highlights the fact that organisations function within a social domain and are influenced by the external environment surrounding them and the needs and networks of the people forming part of the organisations; these, in turn, mould the social structures that develop within organisations (Hill and Hupe, 2014).

Edelman (1992) and Dobbin and Sutton (1998) departed from the notion that organisations face common pressures and act in a relatively similar manner; rather, they argued that organisations respond to the law in complex and diverse ways and they noted that professionals within organisations influenced the drafting of regulations that constituted best practice in the area of employment rights and regulations (Powell, 2007). Powell (2007) draws on the ideas of DiMaggio (1988) who recognised the fact that institutionalism is a political process and that the shape and success of such a process is dependent on the power of the individuals who drive this process.

Meyer and Rowan (1977: 361) claim that:

*“Organisations which incorporate institutionalised myths are more legitimate, successful and likely to survive.”*

The formal structure of an organisation reflects the ‘myths’ of its institutional environment, rather than the exigencies of the organisation’s actual work activities (Meyer and Rowan, 1977). The formal structure, which incorporates an organisation’s blueprint and established rules and procedures, is distinct and separate from the informal aspect which reflects the organisation’s actual work activities (Meyer and Rowan, 1977). Meyer and Rowan (1977) argue that the inclusion of the ‘proper’ formal structures within organisations could enhance an organisation’s reputation and increase its success. For example, organisations which adopt external criteria that illustrate their value, are viewed positively by their stakeholders:

*“Ceremonial criteria of worth ... are useful to organisations: they legitimate organisations with internal participants, stockholders, the public and the state ... The incorporation of structures with high ceremonial value, such as those reflecting the latest expert thinking or those with the most prestige, makes the credit position of an organisation more favourable.” (Meyer and Rowan, 1977: 351)*

Therefore, the implication is that the success of an organisation is not solely dependent on the level of efficiency and effectiveness of its productive capabilities, but also on the incorporation of structures based on institutionalised rules (Meyer and Rowan, 1977). Though the implementation of certain rules may conflict with the sense of efficiency because of the additional costs involved for their operation, failure to include the ‘proper’ elements of structure may lead to negative consequences for the organisation (Meyer and Rowan, 1977).

It is argued that:

*“Organisations that incorporate societally legitimated rationalised elements in their formal structures maximise their legitimacy and increase their resources and survival capabilities.” (Meyer and Rowan, 1977: 352)*

Budget reforms have been explained by examining the shifts in budget formats, procedures and function (Van Reeth, 2002). In particular, performance oriented budgeting systems highlight the policy planning and decision-making functions. Van Reeth (2002) claims that in order for the budget reform to be ‘real’, the shift in the budgeting format and procedure has to be supported by a shift in the budget function which demonstrates the capacity to use the budget tool for better decision-making and policy formulation. In this regard, a study undertaken by Mimba et al (2013) covering local government agencies in Indonesia, found that managers in such agencies placed more focus on satisfying the formal requirements vis-à-vis the format and timely delivery of annual performance reports, rather than on the contents of such reports. Mimba et al (2013: 15) describe this as indicating “*a symbolic rather than functional use of performance information*”. Budget reforms are sometimes used as a means to establish legitimacy:

*“Shifts in the information-content of budget systems can therefore become part of strategies of administrative or political stakeholders to create meaning, exercise control or establish legitimacy.”* (Van Reeth, 2002: 2)

This is also pointed out by Miller (1991) who states that the development of budgeting processes has been shaped by political, administrative and societal players who have promoted the implementation of new budgeting systems in search of legitimacy.

Where the budgetary reform comprises performance oriented formats and procedures, but the actual decision-making by the public administration largely ignores performance criteria, “*the performance procedures and formats are used, at best, to rationalise and legitimise the decisions*” (Van Reeth, 2002: 12). DiMaggio and Powell (1983) claim that governments with unclear goals make use of legitimacy procedures to show economic and social robustness.



In their research, Carpenter and Feroz (2001) sought to explain the factors which influence the choice of the basis of accounting in the public sector. The research showed that the decision of governments to adopt generally accepted accounting principles (GAAP) for external financial reporting is highly influenced by the personal values of key people in the organisation, organisation culture, pressures to change which emanate from the providers of capital and from accounting education courses (Carpenter and Feroz, 2001).

Burns and Scapens (2000: 23) “*conceptualise management accounting as organisational rules and routines...[which have] the potential to become institutionalised*”. From an institutional perspective, management accounting change is viewed as a process, in line with Selznick’s (1957: 16) view of institutionalisation as something “*that happens to the organisation over time*”. They claim that the execution of management accounting change necessitates a deep understanding of the organisation’s current environment, in particular ‘its routines and institutions’. This requires understanding the formal systems, as well as obtaining knowledge about the routines and customs of members of the organisation (Burns and Scapens, 2000). Where the changes conflict with the existing ‘routines and institutions’, they might meet with resistance from the parties who will be affected by the changes (Burns and Scapens, 2000).

Burns and Scapens (2000: 17) describe three elements constituting resistance to change:

*“(1) formal and overt resistance due to competing interests; (2) resistance due to a lack of capability (knowledge and experience) to cope with such change; and (3) resistance due to a ‘mental allegiance’ to established ways of thinking and doing, embodied in existing routines and institutions.”*

DiMaggio and Powell (1983) propose the idea of institutional ‘isomorphism’ (similarity) to explain organisational change<sup>4</sup>. Isomorphism is “*a constraining process that forces one unit in a population to resemble other units that face the same set of environmental conditions*” (DiMaggio & Powell, 1983: 149). This concept explains why organisations operating in the same spheres are likely to exhibit similar traits. Di Maggio and Powell (1983) mention coercive, normative and mimetic processes to explain why organisations are developing into more ‘homogeneous’ groups. Coercive aspects relate to political pressures and the influence of the state who is entrusted with the provision of regulatory control and monitoring; normative forces emanate from the role of education and the significant impact of the professions; and mimetic factors refer to the expected reactions to situations of uncertainty (Powell, 2007). DiMaggio and Powell (1983) claim that organisations are compensated for being like other organisations in their area, because this similarity facilitates the recruitment of skilled and career-oriented people, the undertaking of transactions with other establishments, the qualification for grants and/or contracts and the building of their reputation.

DiMaggio and Powell (1983) maintain that when dissimilar organisations in the same occupation are organised into a tangible discipline, strong influences come into play which steer such organisations to resemble one another. The adoption of similar work practices by these organisations increases their legitimacy and enhances their social credibility, which in turn, leads to improved probability of survival and success (Meyer and Rowan, 1977). Isomorphism (or the process of becoming similar) acts as a constraint because it pressures one organisation to be similar to other organisations that are subject to the same environmental circumstances (Hawley, 1968, cited in DiMaggio and Powell, 1983). Though organisations

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<sup>4</sup> Organisational change refers to “change in formal structure, organisational culture, and goals, programme or mission.” (DiMaggio and Powell, 1983: 149)

try to effect changes on a continuous basis, the extent of diversity is diminished through the isomorphism effect and organisational players create an environment which restricts their aptitude to change further in the longer term (DiMaggio and Powell, 1983).

Scott (2014) has referred to three foundations underlying institutions, which he termed the ‘three pillars of institutions’, namely regulative systems, normative systems and cultural/cognitive systems.

*“Institutions comprise regulative, normative and cultural-cognitive elements, that together with associated activities and resources, provide stability and meaning to social life.”* (Scott, 2014: 56)

These pillars provide a distinctive basis for legitimacy, either because of legal sanctioning, moral obligation or cultural support (Powell, 2007). Each component is important; and although at times, one element may dominate, they often work together (Scott, 2014). The regulative pillar focuses on the setting of rules and sanctions, the normative aspect comprises an obligatory and binding expectation, and the cultural/cognitive element relates to taken-for-granted or shared understanding of concepts (Powell, 2007). The three components make up a continuum ranging *“from the conscious to the unconscious, from the legally enforced to the taken for granted”* (Hoffman, 1997: 36). Table 13 sets out the main dimensions for each pillar, whilst table 14 provides further explanation vis-à-vis the said pillars.

**Table 13: Three Pillars of Institutions**

	<b>Regulative</b>	<b>Normative</b>	<b>Cultural-Cognitive</b>
<b>Basis of compliance</b>	Expedience	Social obligation	Taken-for-grantedness; Shared understanding
<b>Basis of order</b>	Regulative rules	Binding expectations	Constitutive schema
<b>Mechanisms</b>	<i>Coercive</i>	<i>Normative</i>	<i>Mimetic</i>
<b>Logic</b>	Instrumentality	Appropriateness	Orthodoxy
<b>Indicators</b>	Rules; Laws; Sanctions	Certification; Accreditation	Common beliefs; Shared logics of action; Isomorphism
<b>Affect</b>	Fear Guilt / Innocence	Shame / Honour	Certainty / Confusion
<b>Basis of legitimacy</b>	Legally sanctioned	Morally governed	Comprehensible; Recognisable; Culturally supported

Source: Scott (2014: 60)

**Table 14: Explanation of Pillars of Institutions**

Pillars of Institutions	Description
Regulative	<p>This emphasises regulatory processes, namely rule-setting, monitoring and sanctioning activities (Scott, 2014). The logic underpinning the regulatory pillar is an instrumental logic – individuals create laws to further their interests and they abide to these laws to obtain the ensuing awards or to avoid punishments (Scott, 2014). Though regulation is perceived as constraining and repressing behaviour, various types of rules actually empower and confer benefits to some players, such as awarding licences to operate in the market (Scott, 2014). The primary mechanism of control, using DiMaggio and Powell’s (1983) categorisation, is coercion. Where laws are ambiguous and do not lay down clear directions for behaviour, law interpretation has to rely more on the normative and cognitive elements, than the coercive component for its effect (Suchman and Edelman, 1996). The principal features of the regulatory pillar are fear, force, sanctions and expedience; the stern effects of these components are mitigated by the existence of rules, both formal and informal, that justify using force (Scott, 2014).</p>
Normative	<p>Normative systems comprise values (conceptions of what is preferred and the setting of standard levels) and norms (how things should be done and values achieved); they define goals and objectives and specify appropriate ways to achieve them (Scott, 2014). Normative systems restrain social behaviour, but at the same time, they empower and enable social action, by granting rights and responsibilities, licenses and mandates, and privileges (Scott, 2014). The logic underlying the normative pillar revolves around ‘appropriateness’; rather than seeking self-interest as is the case with the instrumental logic, it searches for the appropriate behaviour to be carried out (Scott, 2014). The indicators for the existence of normative institutions comprise certifications and accreditations bestowed upon the organisation by professional associations. Infringement of norms causes feelings of shame or disgrace; on the other hand, exemplary behaviour evokes feelings of honour and respect – these emotions provide strong inducements to observe established norms (Scott, 2014).</p>
Cultural-cognitive	<p>The cultural-cognitive perspective of institutions has been given prominence by neo-institutionalists, who concentrate on the cognitive elements of human existence. “A <i>cultural-cognitive conception of institutions stresses the central role played by the socially mediated construction of a common framework of meaning</i>” (Scott, 2014: 70). This element emphasises that “<i>internal interpretive processes are shaped by external cultural frameworks</i>” (Scott, 2014: 67). Hofstede (1991: 4) suggests that culture provides “<i>the software of the mind</i>”, that is, it provides the mental programmes which shape the ways of thinking, feeling and acting. The underlying logic is orthodoxy, where actions are justified in view of their soundness and perceived correctness (Scott, 2014). The feelings evoked by this institutional pillar range from certitude and confidence to confusion and disorientation; compliance with established cultural beliefs lead to feelings of competence, whilst contradictory behaviour is regarded as bizarre (Scott, 2014).</p>

In some circumstances, one particular pillar will operate on its own to support the social order, and in other circumstances, a particular pillar will dominate (Scott, 2014). When the three pillars of institutions are aligned, the strength of their combined forces could be remarkable (Scott, 2014); conversely, misalignment between the pillars can lead to conflict and confusion which in turn, are likely to stimulate institutional change (Dacin et al, 2002).

Organisations require legitimacy – Scott et al (2000) claim that:

*“Organisations require more than material resources and technical information if they are to survive and thrive in their social environments. They also need social acceptability and credibility.”* Scott et al (2000: 237)

The concept of legitimacy is a basic element in institutional development. The importance of legitimacy becomes instantly apparent if lost, which suggests that legitimacy is a fundamental condition of social existence (Scott, 2014). Meyer and Rowan (1977) argue that organisations increase their legitimacy and survival potential if they adopt certain work practices, though these practices may not necessarily lead to improved performance or efficiency. Brignall and Modell (2000) observe that managers may be motivated to use PI within public sector performance measurement systems, for legitimacy purposes rather than to maximise efficiency. Each of the three institutional pillars puts forward a basis for legitimacy: the regulative pillar implies that legitimate organisations are those operating according to legal requirements; the normative view suggests that both intrinsic and extrinsic rewards provide the incentive to conform; the cultural-cognitive perspective rests on taken for granted, preconscious understandings (Scott, 2014).

With respect to the implementation of policy, the sociological work of Scott (2014) adopts a different perspective to that employed by political scientists; rather than focusing on how public policy develops, it is concerned with how organisations function and how the

responsibilities to implement public policy are held within organisations (Hill and Hupe, 2014). This outlook of the institutional theory sheds light on why organisations may not cooperate between themselves or may be unwilling to amend their processes and procedures (Aldrich, 1976).

March and Olsen's (1984) views of the institutional approach suggest that an analysis of a policy implementation process has to be undertaken in an organised framework, where "*there are established norms, values, relationships, power structures and standard operating procedures*" (Hill and Hupe, 2014: 37). The institutional perspective is explained by March and Olsen (1984) as follows:

*"Political democracy depends not only on economic and social conditions but also on the design of political institutions. The bureaucratic agency, the legislative committee, and the appellate court are arenas for contending social forces, but they are also collections of standard operating procedures and structures that define and defend interests. They are political actors in their own right."* (March and Olsen, 1984: 738)

In her book entitled 'How Institutions Think', Douglas (1986) notes that an institution is characterised by its enabling role in shaping the cognitive processes of individuals, rather than by its formal structure and authority. Douglas (1986: 8) seeks to clarify "*the extent to which [individual] thinking depends on institutions*". Douglas (1986) claims that individuals do not make decisions in isolation, but they draw upon shared knowledge and moral standards within their communities when making decisions. Societies develop legitimised social groupings (for example, family) or social processes (for example, ceremonies or games), on the basis of this shared knowledge and standards (Douglas, 1986). The author refers to such legitimised groups or processes as 'institutions'. In maintaining that institutions think, Douglas (1986) does not imply that institutions have 'minds' of their own, but the thinking is done by the individuals within their institutional commitments. Institutions encode information and as a

result, they provide individuals with a framework for making routine decisions, solving routine problems and doing a great deal of thinking on behalf of individuals (Douglas, 1986: 47). Thus, institutions act as machines for thinking and decision-making with “*the effect of turning individual thought over to an automatic pilot*” (Douglas, 1986: 63). This saves time and energy for individuals when resolving problems (Douglas, 1986).

The use of institutions in thinking may limit the capacity for independent thought, creating “*shadowed places*” in which nothing can be seen nor any questions asked (Douglas, 1986: 69). While institutions can save time and energy in decision-making, they also diminish an individual’s creativity in developing new and novel ways to address issues and restrain an individual’s ability to identify potential problems inherent in the solutions proposed by institutions (Douglas, 1986).

Young (1996) applied institutional thinking in her study on accounting reforms in the US, focusing on an FASB project on financial instruments. In her study, Young (1996) claimed that ‘financial accounting’ is an institution. Young (1996) notes how the number and types of financial instruments (for example, interest rate options, interest rate swaps and interest rate futures) have increased over the last two decades. This had consequences for accounting, in particular to ensure that financial statements represent fairly the transactions of an organisation. According to Young (1996), the FASB developed an accounting standard which highlighted the traditional tasks of disclosure, recognition and measurement, rather than developing accounting rules which emphasise the fundamental nature of these new financial instruments. Young (1996: 487) discusses how the development of the accounting standard was limited by institutional thinking, such that during the standard-setting process, only certain types of questions were asked and many important issues were ignored. In addition, Young (1996: 491) claims that questions which posed challenges to the existing accounting



framework were not asked. She argues that the reliance on the conceptual framework limited the search for appropriate solutions and although, time and effort were saved, these savings came at a cost because some pertinent issues were left unaddressed (Young, 1996: 491).

Another study applying institutional thinking is that undertaken by Potter (2002), who examined financial accounting reforms in the Australian public sector. In his study, Potter (2002) maintains that the ‘conceptual framework’ is an institution. Potter (2002) explains how accounting regulations were developed for the Australian public sector on the basis of the concepts outlined in the conceptual framework, which required public sector organisations to adopt commercial accounting rules. He claims that the regulations apply the traditional accounting concepts of accountability and performance, even though the main objectives of the organisations impacted are not financial (Potter, 2002). The study shows how the development of the accounting rules was limited by institutional thinking and thus, a number of issues related to the regulations were not tackled and only certain questions were asked (Potter, 2002). Potter (2002: 73) explains how the conceptual framework represents an automatic starting point for addressing issues and the possibility of resolving problems in other ways, perhaps non-financial, is rejected.

### **3.2.3 Greenwood and Hinings’ framework**

#### ***Reasons for using the Greenwood and Hinings’ model***

Various models have been put forward for describing reforms. In this respect, Argento and van Helden (2010) referred to the following theoretical frameworks for explaining reform processes: Hood (1995); Greenwood and Hinings (1996); Lüder (2002); and Pollitt and Bouckaert (2004). Other frameworks which have been used to conceptualise change processes

include Argento and van Helden (2009), which builds upon Greenwood and Hinings (1996), and Burns and Scapens (2000).

For the purpose of the research, some of the frameworks mentioned above have been considered, but they were not adopted for the reasons discussed below.

- Lüder's (2002) model highlights reform drivers and promoters as factors which trigger a reform. It was considered difficult to populate some of the contextual, behavioural and instrumental variables incorporated in this framework, in view of the fact that the implementation of PB in the Maltese public sector is still a *proposed* reform. Furthermore, a recent study which delved into central government accounting reform in Malta (Jones and Caruana, 2014) has adopted Lüder's (2002) model – in the context of Malta which is a very small country, it is very likely that the reform drivers, political reform promoters and stakeholders would be the same individuals/groups for both the accrual accounting reform and the PB reform. Thus, the adoption of Lüder's (2002) model in this research would have potentially been largely repetitive of the Jones and Caruana (2014) study.
- Pollitt and Bouckaert's (2004) framework, which emphasises the elite group's perception of desired change, was not considered sufficient to explain the type and pace of change expected in the Maltese scenario.
- Burns and Scapens' (2000) institutional framework aims to describe analytical concepts that can be used for case studies of management accounting. Whilst this model recognises that there are both internal and external influences on management accounting change processes, it adopts a micro level of analysis, focusing on internal factors. For instance, issues of power have not been explored in this model, failing to consider that rules and

routines can also be kept in place by the use of power, rather than by taken-for-granted assumptions.

- In their research, Argento and van Helden (2009) have complemented institutional theory with network theory, focusing on collaboration and interactions between the various stakeholders as factors which influence the outcome of a change process. In view of the potential importance of a powerful decision maker (champion) in leading and pushing the successful implementation of the budgetary reform in the Maltese context (Willoughby, 2011), negotiations and discussions between the stakeholders were considered to be less influential in shaping PB reform in Malta.

The Greenwood and Hinings' (1996) model was deemed appropriate for explaining the type of organisational change expected in the Maltese budgetary framework (radical versus convergent and evolutionary versus revolutionary). It was considered essential to establish whether a radical change is possible in the Maltese context and to identify the factors that would enable or hinder such a change, with a view to addressing any constraining factors. Unless a radical change is envisaged, it might not be worth pursuing a reform which will potentially involve significant investment in time, effort and resources. Furthermore, it was deemed important to identify the pace by which such change is expected to happen, in order to allow for adequate planning to ensure successful adoption of the reform. This model also explores power relationships, which are viewed as key facilitators for the implementation of change.

### ***Explaining the Greenwood and Hinings' model***

Greenwood and Hinings (1996) proposed a framework for understanding organisational change from the perspective of neo-institutional theory, since this theory contains insights

which provide a model of change that links organisational context and intraorganisational dynamics (Greenwood and Hinings, 1996: 1023).

Greenwood and Hinings (1996) seek to explain why a radical change takes place and the incidence and pace by which such change occurs. In this respect, Greenwood and Hinings' model (1996) sheds some light as to why some organisations implement radical change whereas others do not, even though they all experience the same institutional pressures. The authors commence their discussion with a message which is fundamental in institutional theory – Greenwood and Hinings (1996) determine that a major source of organisational resistance to change originates from the premise that an organisation is normatively embedded in its institutional context. Subsequently, they suggest that the incidence and pace of radical change vary *across* institutional sectors because of differences in the structures of institutional sectors; they also vary *within* sectors because of differences in organisations' internal dynamics (Greenwood and Hinings, 1996: 1023). Therefore, these internal dynamics determine whether organisations undergo radical change and, if they do, how quickly (Greenwood and Hinings, 1996: 1024). Focus is placed by the authors upon four aspects of an organization's internal dynamics - interests, values, power dependencies and capacity for action.

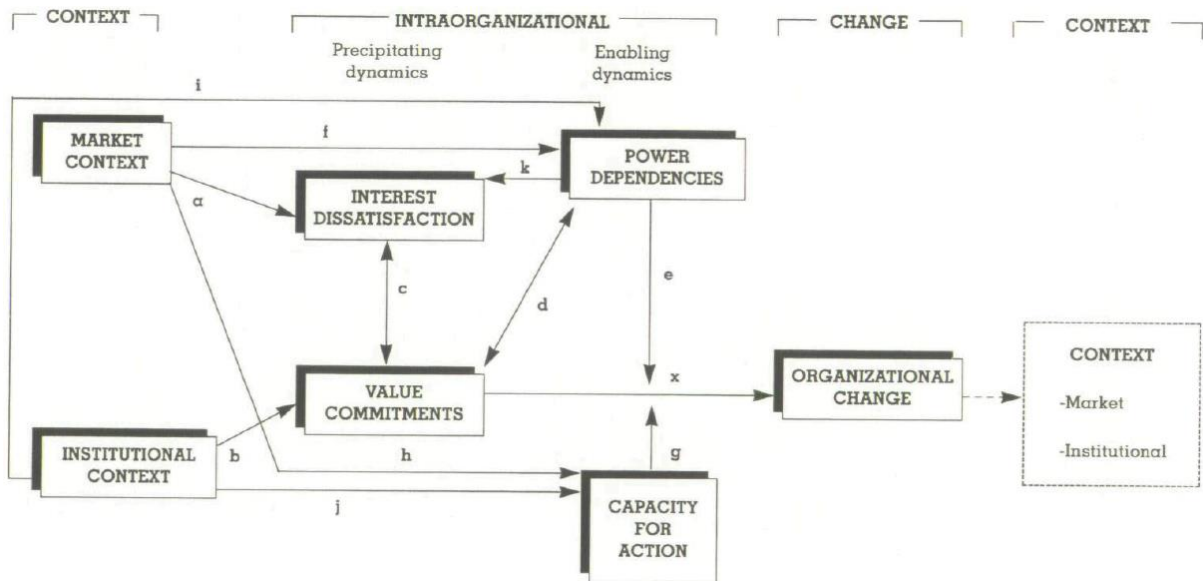
Greenwood and Hinings (1996) establish two aspects of organisational change: convergent versus radical change and revolutionary versus evolutionary change. Radical organisational change involves the transformation of the organisation, whilst convergent change refers to the fine tuning of the existing orientation; revolutionary change occurs quickly and impacts practically all parts of the organisation concurrently, whereas evolutionary change takes place slowly and gradually (Greenwood and Hinings, 1996: 1024).

Institutional theory emphasises convergence around institutionally prescribed templates, such that the nature of change is one of constant reinforcement of existing concepts and modes of thought, that is, change is convergent (Greenwood and Hinings, 1996: 1027). From this perspective, the authors claim that convergent change is the more normal occurrence and radical change is problematic because of the fact that an organisation is normatively embedded in its institutional context. Argento and van Helden (2010: 793) also observe that institutionalisation can be an obstacle to change because rules and practices in an organisation become part of the way things are, that is, they become deeply embedded in an organisation. However, should institutional change occur, it is more likely that such change will be revolutionary (fast pace of change and large scale change) rather than evolutionary (Greenwood and Hinings, 1996).

Powell and DiMaggio (1991: 29) pose the following question: *“If institutions exert such a powerful influence over the ways in which people can formulate their desires and work to attain them, then how does institutional change occur?”* Greenwood and Hinings (1996: 1032) attempt to explain that the response of the individual organisation to institutional pressures is a function of the organisation’s internal dynamics and therefore, the role of intraorganisational dynamics is critical in accepting or rejecting institutionalised practices.

The framework proposed for understanding organisational change is summarised in Figure 6.

**Figure 6: Model for understanding organisational change (Source: Greenwood and Hinings, 1996: 1034)<sup>5</sup>**



The model includes exogenous dynamics (market context and institutional context) and endogenous dynamics (interests, values, power dependencies and capacity for action). The outcome of the model is radical organisational change, which becomes the input to market and institutional contexts, demonstrating that successful practices are mimicked and institutionalised:

*“An organisation that adopted a new organisational form and achieved competitive success in the marketplace would produce pressures on other organisations to adopt the same organisational form.” (Greenwood and Hinings, 1996: 1033)*

<sup>5</sup>Letters a to x in the model represent the following: line a denotes that interest dissatisfaction can vary from one organisation to another, even if the market context is the same; line b represents the fact that the pattern of value commitments will vary between firms given their diverse locations within the institutional context; line c links interests and values in view of their potential to exert pressure for change; line d represents the reciprocal relationship between power dependencies and value commitments; line e indicates that power dependencies enable or hinder radical change; line f denotes the fact that changes in the market context may lead to changes in the power relationships within a firm; line g shows that radical change will occur if there is the capacity for action; line h demonstrates the link between capacity for action and market context; lines i and j indicate that the institutional context influences the power of groups within the organisation and the capacity for action respectively; line k shows that groups use favourable power dependencies to promote their interests; and line x shows that radical change will arise if interests are complemented with a competitive or reformative pattern of value commitment. (Greenwood and Hinings, 1996)

The authors classify the endogenous elements of the model into precipitating dynamics and enabling dynamics.

### Precipitating dynamics

Greenwood and Hinings (1996: 1033-1037) observe that pressures for change within an organisation derive from *interest dissatisfaction* and the *pattern of value commitments*.

Therefore, stakeholder dissatisfaction is a significant factor which gives rise to reform:

*“A potential pressure for change...is the extent to which groups are dissatisfied with how their interests are accommodated within an organisation.”* (Greenwood and Hinings, 1996: 1035)

*“Dissatisfaction, however, does not provide direction for change.”* (Greenwood and Hinings, 1996: 1035)

Therefore, dissatisfaction does not automatically provide an alternative template (Argento and van Helden, 2009). Dissatisfaction will only lead to radical change if the dissatisfied stakeholders link their position of disadvantage to the existing template (way of doing things), and there is the possibility of an alternative template (Greenwood and Hinings, 1996).

At this stage, the critical factor leading to the possibility of radical change and providing the direction for change is the pattern of value commitments within the organisation (Greenwood and Hinings, 1996). The authors identify four patterns of value commitments: status quo, indifferent, competitive and reformative.<sup>6</sup>

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<sup>6</sup> *Status quo* - all stakeholders are committed to the existing institutionalised template-in-use; *indifferent* - groups are neither committed nor opposed to the template-in-use; *competitive* - some groups support the template-in-use, others prefer an alternative template; and *reformative* - all stakeholders are opposed to the template-in-use and prefer an alternative. (Greenwood and Hinings, 1996)

Reform is thus only possible if stakeholder dissatisfaction is coupled with a competitive or reformative pattern of value commitments:

*“Radical change will only occur if interests become associated with a competitive or reformative pattern of value commitment (line x in figure 6) ... Otherwise, interest dissatisfaction will precipitate convergent change.”* (Greenwood and Hinings, 1996: 1036, 1037)

As regards the pace of change, Greenwood and Hinings (1996: 1037) claim that a reformative commitment triggers revolutionary change because of the lack of resistance, whilst a competitive commitment will lead to evolutionary change in view of the resistance encountered from certain groups.

#### Enabling dynamics

*“Radical change ... will occur only in conjunction with an appropriate capacity for action and supportive power dependencies.”* (Greenwood and Hinings, 1996: 1037)

The authors identify *capacity for action* and *power dependencies* as the enablers of radical change. These conditions are necessary for radical organisational change because they enable or constrain it, but, by themselves, they are not sufficient to lead to radical change (Greenwood and Hinings, 1996: 1041).

Power dependencies either enable or suppress radical change within an organisation – radical change takes place where the power dependencies are combined with a reformative or competitive pattern of value commitments (Greenwood and Hinings, 1996: 1039). Where the pattern of commitment is competitive (and therefore there are divergent views on the proposed change), radical change will only happen if the people in positions of power are in favour of the proposed change (Greenwood and Hinings, 1996: 1038).



The second enabler for a reform process is capacity for action, that is, the ability of making the transition from the existing template to an alternative template – this requires the organisation’s understanding of the new template, having the competencies to function with the new template and having the ability to manage the transition to the new destination (Greenwood and Hinings, 1996: 1040). The authors state that capacity for action requires leadership skills, which include the carrying out of charismatic, instrumental and institutional activities<sup>7</sup>. In the absence of capacity for action, radical change will not happen; furthermore, “*capacity for action [has to be] combined with either a reformative or competitive pattern of value commitments*” (Greenwood and Hinings, 1996: 1040). The authors further emphasise that a good understanding of the new template together with a clear road map to arrive at the new destination gives the organisation the sureness to change rapidly. The institutional context might impinge on the capacity for action because an organisation which is deeply embedded within its institutional context might encounter obstacles to develop the required competencies (Greenwood and Hinings, 1996: 1041).

Greenwood and Hinings (1996: 1047) acknowledge that their framework contains a number of concepts which are difficult to measure including power, interests and leadership; moreover, such concepts are very sensitive to context in their operation.

### **3.2.4 Preliminary perspective on Malta**

#### ***Overview***

Van Reeth (2002) observes that budget reforms are sometimes used to attain legitimacy rather than for enhancing policy formulation and decision-making. In a hypothetical scenario where

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<sup>7</sup> *Charismatic* - envisioning, energizing, enabling; *instrumental* - structuring, controlling, rewarding; *institutional* - ensuring changes stick.

the Maltese government adopts PB, but fails to use the PI to make budgetary allocation decisions, it would have implemented a PB system to achieve institutional legitimacy. This will be manifested if huge amounts of data are gathered and presented in budget documents, but in actual fact the information would have no relevance for planning and decision-making.

In terms of the institutional thinking perspective put forward by Douglas (1986), the traditional budgeting system could be viewed as an ‘institution’. Budgeting in the Maltese public sector follows the line-item approach which has been in operation for the past years. This deeply embedded system (‘institution’) may be restraining government’s ability to develop new and creative ways to address the limitations inherent in the traditional system, such as the lack of accountability and the failure to measure the performance achieved by the line ministries.

### ***Pressures for change***

The three areas of institutional isomorphic change – coercive, normative and mimetic – (DiMaggio and Powell, 1983) manifest themselves in the context of budgetary reform, as explained in Table 15 below. These pressures exert influence for promoting change to the new budgetary system.

**Table 15: Institutional isomorphic pressures**

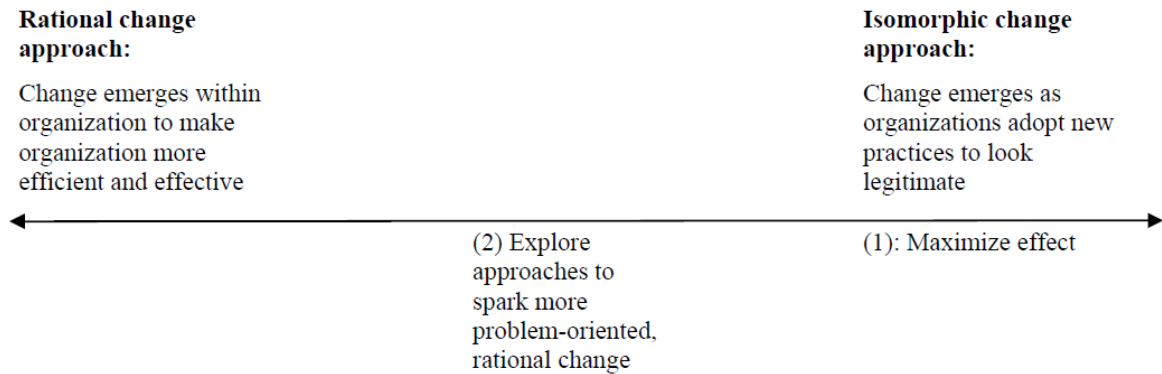
Institutional pressures	Budgetary reform in the Maltese context - Preliminary views
Coercive (legal and technical requirements)	<p>Malta's EU membership lays down conditions that must be satisfied by the country as a result of its affiliation and imposes demands for public financial management reform initiatives. The Maastricht criteria for qualification and participation in the Economic and Monetary Union specify conditions that need to be satisfied by EU member countries, including the requirement that government deficit should not exceed 3% of the country's GDP. Coercive pressures are constantly being exerted upon Malta in the form of demands by the EU for Malta to keep its deficit at or below the 3% threshold. The fiscal deficit issues faced by the country, coupled with the Maastricht criteria for qualification and participation in the Eurozone constitute key drivers for the introduction of budgetary reforms.</p> <p>Meyer and Scott (1982) suggest that organisations which provide resources to government entities, such as the credit markets, are in a position to exercise power over the government. In this respect, the EU provides funds to the Maltese government for the financing of certain projects, and can, therefore, exert coercive institutional pressures to implement budgetary reform. Carpenter and Feroz (2001) claim that coercive isomorphism may be the result of resource dependence, which in turn can influence the government's choice of systems and procedures.</p>
Normative (professional influence)	<p>Normative isomorphic change arises from professionalization; if key employees and management are <i>"filtered on a common set of attributes"</i>, they are likely to look at issues in the same manner and tackle decisions consistently (DiMaggio and Powell, 1983: 153). This ensures that organisations are led by professional <i>"people with similar values and beliefs about the purpose and design"</i> of an organisation (DiMaggio and Powell, 1983: 152). Normative pressures <i>"describe the effect of professional standards and the influence of professional communities on organisational characteristics"</i> (Ashworth et al, 2009: 167). As a result of normative isomorphism, organisations feel compelled to implement systems and processes which have been endorsed by dominant professional groups (Burns, 2000). This reflects the Maltese context, where government might feel obliged to implement the budgetary reform systems which have been advocated by other dominant countries.</p> <p>Andrews (2009) claims that professional persons are more cognisant of good practices, which results in enabling the transfer of 'best practice'; this, in turn, enriches the mimetic influences such that the good practices are adapted to the given local contexts.</p> <p>Ezzamel et al. (2007) describes how normative isomorphic change was weakened when applying accounting and budgetary reforms in the UK, in particular in relations to the politicians' role. They discovered that <i>"only a small number of politicians ... tended to have either accounting/finances background or extensive experience in the public sector..."</i> which constrained their understanding of new accounting and budget systems as well as their aptitude to apply these new procedures (Ezzamel et al., 2007: 29). Ezzamel et al. (2007) claimed that this lack of understanding acted as a stumbling block for effective change. This emphasises the importance of having the right professional people at the top of Maltese government departments and agencies, in order for the budgetary reform to be successfully implemented. Andrews (2009) confirms this when he argues that 'profession proficiency' promotes isomorphic change whilst 'profession deficiency' weakens isomorphic change by decreasing normative and mimetic pressures.</p> <p>In this regard, Greenwood et al (2002: 58) state that: <i>"Professional associations ... play an important role in theorizing change, endorsing local innovations and shaping their diffusion."</i></p>

Mimetic (modelled on good or best practice)	<p>DiMaggio and Powell (1983) observe that when organisations face uncertainty or have unclear goals, they tend to model themselves on other organisations which they believe to be more successful. Carpenter and Feroz (2001: 571) suggest that mimetic isomorphism is “<i>a response to organisational uncertainty in identifying the best course of action</i>”. Thus, “<i>models may be diffused unintentionally, indirectly through employee transfer or turnover, or explicitly by organisations such as consulting firms or industry trade associations</i>” (DiMaggio and Powell, 1983: 151). Mimetic pressures are also demonstrated when organisations attempt to replicate desirable practices, even though such practices may have been unsuccessful (Andrews, 2009).</p> <p>Andrews (2009) maintains that countries are often willing to reproduce reform plans that are considered to be 'good international practice'. PB is considered to be 'good practice' in a number of countries which have modelled their budgeting system on this basis. In implementing such budgetary reform, the Maltese public administration will be subject to mimetic pressures to model its budgeting system on that adopted by other countries. In this respect, the Minister of Finance has admitted that Malta's budgetary system needs to be reformed, because Malta's budget format is significantly out-dated when compared to that implemented by the majority of the other European countries (Malta Today, 2013b; Times of Malta, 2014b).</p>
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#### Further considerations on isomorphic influences

It has been argued by Andrews (2009) that the success of reforms might be limited, in view of the isomorphic characteristics of reform methods. These limits can, however, be counter-balanced by shifting towards a rational approach as encouraged by Ashworth et al (2007). This approach concentrates on actual problems in an organisation and promotes change as tackling such issues (Andrews, 2009). In this respect, budgetary reform in the local context should be purposely introduced to improve the allocation of limited public funds amongst competing government programmes and to enhance accountability in government spending, rather than as a result of institutional pressures. Figure 7 depicts a change continuum between rational and isomorphic – it shows that isomorphic change on its own can be limited, but if the focus is shifted on the real issues (increasing efficiency and effectiveness), then, the limitations will be mitigated (Andrews, 2009).

**Figure 7: A continuum of change approaches and challenges for development (Source: Andrews, 2009: 32)**



### Macro-level aspect

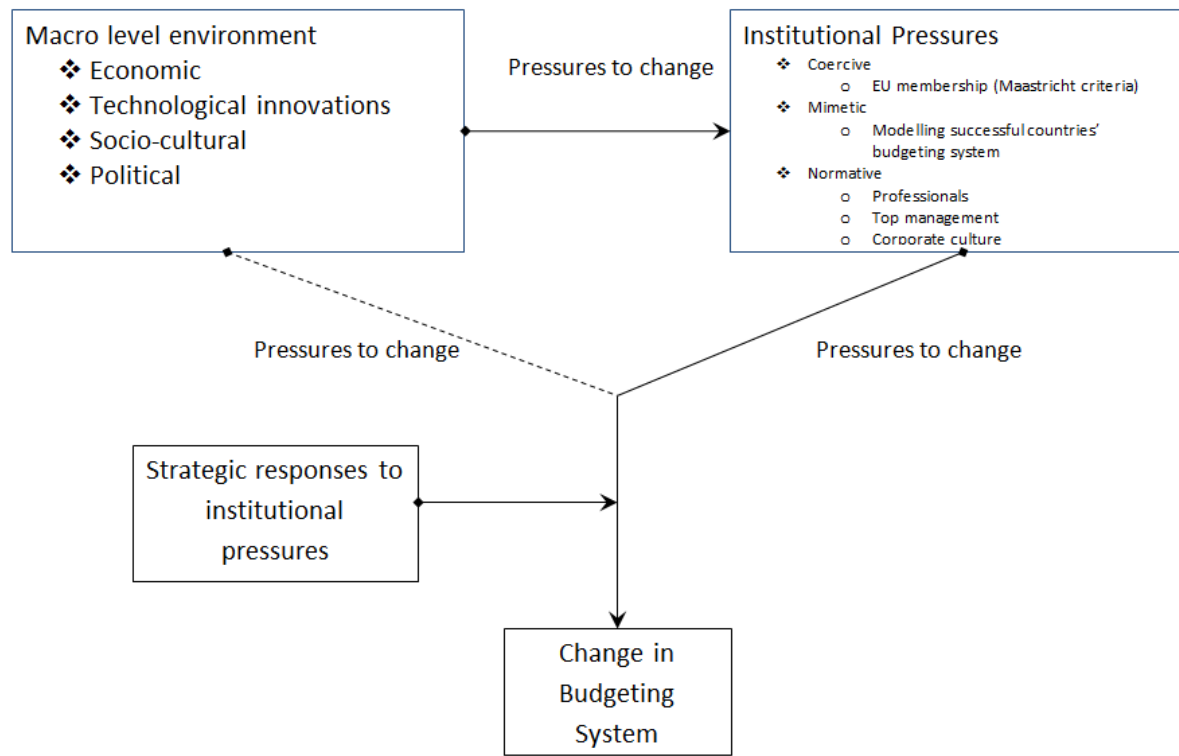
Munir et al (2011) proposed a framework to examine changes in performance management systems in banks, drawing from DiMaggio and Powell (1983) and Oliver (1991). This framework illustrates that banks may implement changes to their performance management systems as a result of coercive, mimetic and normative pressures, as well as due to pressures from factors in the macro-level environment, including economic conditions, technological innovations, socio-cultural and political influences (Munir et al, 2011).

In terms of the Maltese public administration, this framework implies that both the institutional factors and the macro-level aspect are significant catalysts in the change process involved to move from a traditional budgeting system to performance based budgeting. The adapted framework is shown in Figure 8. The institutional isomorphic pressures have been discussed above. With respect to the economic climate, the global financial crisis has significantly squeezed government revenues leading to deficit issues and high government debt. This necessitates tighter control over government spending and could act as a trigger for the implementation of PB, whereby funds are allocated to the programmes which deliver the desired results and outcomes. Technological improvements play an important role in the

advent of a new budgeting system because they facilitate the data gathering and analysis processes across the whole of government. As regards the socio-cultural and political aspects, citizens are demanding more accountability from government; this is especially important in the local context where the change in government has heightened the public's expectation that the new government will deliver what was promised and will ensure accountability and trust in its dealings and in the allocation of public funds. In this respect, immediately after being elected, the Prime Minister made the following statement: "*We will be restructuring how the secretariat [of the Prime Minister] works. It will be more business oriented and utilise concepts such as Key Performance Indicators*" (Malta Today, 2013b). The Prime Minister also stated that the KPIs will establish the level of performance that government departments must achieve, will determine communication standards and will enhance transparency in government's dealings (Malta Today, 2013b).

The above discussion suggests that the macro-level environment (economic, technological innovations, socio-cultural and political) (Munir et al, 2011) may also be a source of 'informal pressure' for the introduction of budgetary reform. Munir et al (2011: 103) argue that "*organisational responses to macro-level influences are often not spontaneous*" and the reactions to macro-level aspects may stem from coercive, mimetic and normative pressures.

**Figure 8: Analytical Framework for examining changes in performance measurement systems within the banking sector (Source: Munir et al, 2011: 98) (Adapted)**



### *Influences that might prohibit change*

Whilst coercive, normative and mimetic institutional influences together with macro-economic factors might exert pressure to promote the change to the new budgetary system, there could be other influences which act to hinder the reform. These potential issues will be delved into during the empirical data collection process.

### *Greenwood and Hinings' model*

Greenwood and Hinings' model is relevant for an understanding of the proposed transition from conventional input-based budgeting to PB because it sets out situations under which a radical versus a convergent organisational change could be expected.

The existing conventional budgeting system is a strongly institutionalised practice in the Maltese public administration. However, there is *dissatisfaction* with the current system, as acknowledged by the Minister for Finance (Malta Today, 2013c; Times of Malta, 2014b). Moreover, the budgetary reform is being prompted by institutional pressures which result from Malta's EU membership. The fiscal deficit issues faced by the country and the EU's demands to keep the deficit under control, together with the stipulated Maastricht criteria for qualification and participation in the Eurozone constitute coercive pressures for the implementation of budgetary reforms. Furthermore, other normative and mimetic institutional pressures are present including the need to reform the budgetary system and to model it on that operated by the majority of other European countries. In addition, macro-economic factors may also impose pressures for change to the current budgetary framework.

The implementation of PB is expected to constitute a radical change because it involves a completely new way of allocating funds to the various government ministries, departments and public entities – whilst the current system emphasises input performance (not exceeding the allocated budgets), the proposed system is mainly interested in outcomes and results. This radical change represents an *alternative for the current template* (Greenwood and Hinings, 1996).

With respect to dissatisfaction with the existing practices, there might be diverging views between stakeholders. On the one hand, some groups might be dissatisfied with the existing budgeting system and might have strong reform ambitions, in order to achieve enhanced decision-making, improved accountability and superior allocation decisions. In this respect, the Minister of Finance has publicly declared that Malta's budgetary system needs to be reformed. On the other hand, there might be groups including other ministries within



government and civil servants, who put up resistance against this change because they are used to the existing system (status quo) and might view the reform as threatening their current position since they have to be more accountable under the new system. This indicates a *competitive pattern of value commitments*. Greenwood and Hinings (1996: 1028) claim that resistance to change is a result of rigidity and a powerful embeddedness of an organisation within its institutional field.

The diverging views of the different stakeholders might act as a hindrance for a radical change to happen. Greenwood and Hinings (1996: 1039) observe that where there are divergent opinions on the proposed reform, radical change can only occur if the *people in positions of power* are committed to the proposed change.

The *capacity for making the transition* from the existing to the new budgeting system requires the possession of the necessary competencies and the aptitude to learn how to operate the proposed system – this depends on the skills of the human resource complement within the MOF, which will potentially manage the transition and implementation of the new system. The provision of the required training to staff involved in the budgeting process could facilitate the transition to the new system. If the reform is championed by a person in a high position of power, the process of mobilising the necessary resources (including human resources) would be facilitated.

Thus, although the diverging opinions of the different stakeholders might be problematic for a radical change to take place, the existence of a champion for the reform in a high ranking position of power might still stimulate a radical change in the budgeting system. The preliminary application of the Greenwood and Hinings' framework in the Maltese scenario indicates that there is dissatisfaction with the existing system, there is the possibility of an

alternative template, a competitive pattern of value commitments possibly exists, there are people in positions of power who are in favour of the reform, and the capacity to make the transition to the new system can be facilitated by the champion of the reform. These factors indicate that a radical change in the local budgeting system is possible.

### **3.3 Policy implementation theory**

#### **3.3.1 Introduction**

Policy implementation theory is being employed to identify a suitable implementation approach and to determine the potential issues around the implementation of PB in Malta.

The section below describes some key terms and definitions used in the implementation literature. This is then followed by an overview of the theoretical considerations underlying the top-down implementation approach, the bottom-up perspective and a combination of the two views. Subsequently, the implementation success factors are discussed, followed by the limitations inherent in the implementation literature. The final section sets out a preliminary view of the implementation approach that might be adopted for the operation of PB in Malta.

#### **3.3.2 Key terms and definitions**

The dictionary definition of implementation is: to carry out, accomplish, fulfil, produce or complete a given task. In this respect, what is being implemented is ‘policy’. Therefore, implementation in the context of public administration presupposes policy (Hill and Hupe, 2014).

Anderson (2011: 7) defines ‘policy’ as a *“purposive course of action followed by an actor or set of actors in dealing with a problem or matter of concern...Public policies are those*

*policies developed by governmental bodies and officials*”. A number of authors have compiled models setting out the stages of the policy process, claiming that the stages framework provides a systematic approach which captures the diversity of the real context. Anderson (2011: 4) puts forward the following policy process framework:

**Figure 9: The Policy Process (Source: Anderson, 2011: 4)** (As adapted from Anderson J.E., Brady, D.W. and Bullock, C. III, *Public Policy and Politics in the United States*, 2<sup>nd</sup> ed. Monterey, CA: Brooks/Cole 1984)

Policy Terminology	<b>Stage 1: Policy Agenda</b>	<b>Stage 2: Policy Formulation</b>	<b>Stage 3: Policy Adoption</b>	<b>Stage 4: Policy Implementation</b>	<b>Stage 5: Policy Evaluation</b>
Definition	Those problems, among many, that receive the serious attention of public officials	Development of pertinent and acceptable proposed courses of action for dealing with a public problem	Development of support for a specific proposal so that a policy can be legitimised or authorised	Application of the policy by the government's administrative machinery	Efforts by the government to determine whether the policy was effective and why or why not
Common sense	Getting the government to consider action on the problem	What is proposed to be done about the problem	Getting the government to accept a particular solution to the problem	Applying the government's policy to the problem	Did the policy work?

Hill and Hupe (2014) observe that the implementation of public policy (depicted as stage 4 in the above diagram) is the result of what has occurred in the earlier stages (stages 1 to 3) of the policy process. Anderson (2011) notes that the content of the policy and its effect on the parties impacted may be significantly modified during the stage of implementation.

Mazmanian and Sabatier (1983: 20-21) define ‘implementation’ as follows:

*“Implementation is the carrying out of a basic policy decision, usually incorporated in a statute but which can also take the form of important executive orders or court decisions. Ideally, that decision identifies the problem(s) to be addressed, stipulates*

*the objective(s) to be pursued, and in a variety of ways, ‘structures’ the implementation process. The process normally runs through a number of stages beginning with passage of the basic statute, followed by the policy outputs (decisions) of the implementing agencies, the compliance of target groups with those decisions, the actual impacts – both intended and unintended – of those outputs, the perceived impacts of agency decisions, and finally, important revisions (or attempted revisions) in the basic statute.”*

O’Toole (2000: 266) defines policy implementation as “*what develops between the establishment of an apparent intention on the part of government to do something, or stop doing something, and the ultimate impact in the world of action*”. Therefore, the main question when researching implementation is: “*what happens between the establishment of policy and its impact in the world of action?*” (O’Toole, 2000: 273). John (1998: 204) describes implementation as “*the stage in the policy process concerned with turning policy intentions into action*”. DeLeon (1999: 330) refers to implementation as “*little more than a comparison of the expected versus the achieved*”.

Linton (2002: 66) suggests that the “*implementation of a new process begins when an innovation has been adopted and ends when the innovation becomes routine or is abandoned*”. Klein and Sorra (1996: 1057) define implementation as “*the transition period during which targeted organisational members ideally become increasingly skilful, consistent, and committed in their use of an innovation. Implementation is the critical gateway between the decision to adopt the innovation and the routine use of the innovation within an organization*”.

When a comparison between what is achieved and what was expected is carried out (DeLeon, 1999), there is the possibility of observing an ‘implementation gap’ or an ‘implementation failure’ (Hill and Hupe, 2006). Parsons (1995) mentions a number of factors which might lead to implementation failure, including difficult human relations, poor information flows,

learning problems, labour/management conflict, cultural issues or problems with structures, amongst others.

On the other hand, Ingram and Schneider (1990) give a number of definitions for successful implementation: agencies comply with statutory prescriptions such that the desired outcomes are achieved; holding agencies accountable for reaching stipulated goals which ensures that the agencies will carry out their tasks correctly; achievement of local goals; or the political climate is improved as a result of the programme. Ripley and Franklin (1982: 200) define successful implementation as that which “*leads to desired performance and impacts*”.

The policy process illustrated in figure 9 above distinguishes between implementation and evaluation as two different stages. Parsons (1995: 461) observes that evaluation explores “*how public policy and the people who deliver it may be appraised, audited, valued and controlled*” whilst implementation is concerned with “*how policy is put into action and practice*”.

Policy implementation research led to the development of two schools of thought for studying and analysing implementation: the top-down perspective and the bottom-up perspective.

Matland (1995: 146) describes these two views as follows:

*“Top-down theorists see policy designers as the central actors and concentrate their attention on factors that can be manipulated at the central level. Bottom-up theorists emphasize target groups and service deliverers, arguing policy really is made at the local level.”*

A number of scholars have attempted to synthesize these two perspectives, arguing that some convergence between these two views is necessary to bring together the macrolevel variables considered by the top-down proponents and the microlevel variables of the bottom-up models (Matland, 1995: 146).

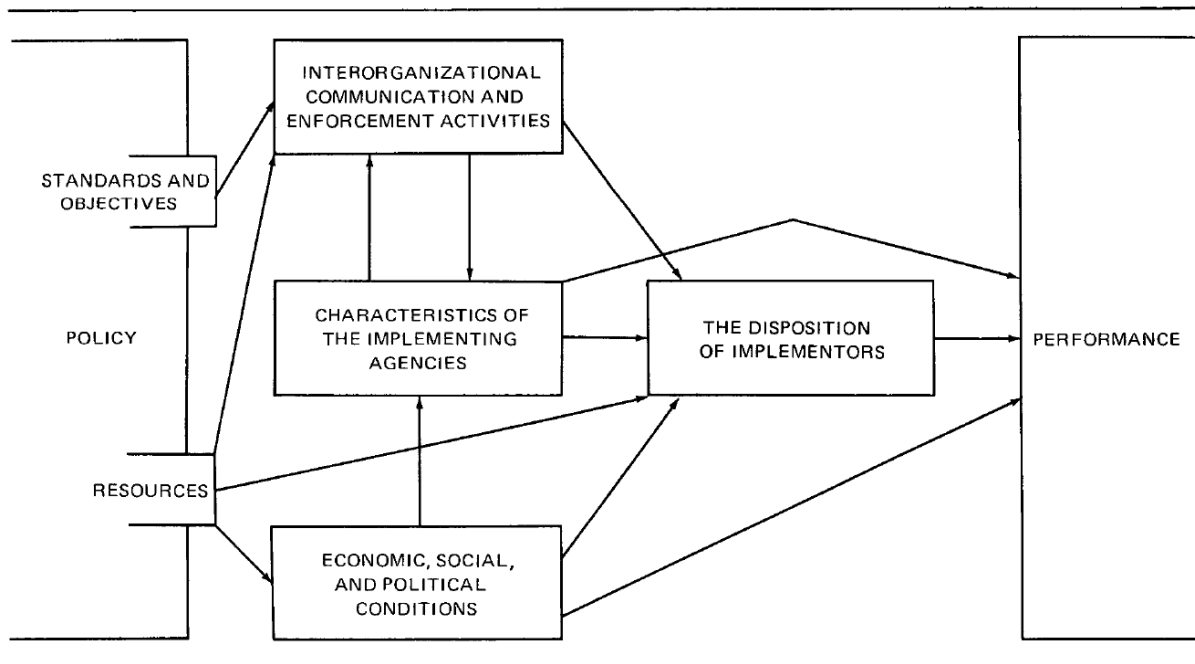
### 3.3.3 The top-down perspective

The founding fathers of implementation studies, Pressman and Wildavsky (1973) proposed a top-down approach and defined implementation in terms of a relationship to policy as laid down in official documents. They observe that “*policies normally contain both goals and the means for achieving them*” (Pressman and Wildavsky, 1984: xxi). The authors claim that successful implementation is dependent on close linkages and a high degree of cooperation between different organisations and departments; in the absence of such close links, an ‘implementation deficit’ will occur (Pressman and Wildavsky, 1973). Policy implementation is thus viewed as a process of interaction between setting of goals and actions to achieve them (Pressman and Wildavsky, 1984: xxi-xxiii).

Van Meter and Van Horn (1975) put forward a model for analysing the implementation process (refer to Figure 10 below) – their model contains six variables which are linked to the production of an outcome described in the model as ‘performance’. Implementation is viewed as a process which commences from a policy decision: “*policy implementation encompasses those actions by public and private individuals or groups that are directed at the achievement of objectives set forth in prior policy decisions*” (Van Meter and Van Horn, 1975: 447). The authors emphasise the importance of consensus and compliance over the goals and objectives of the policy, suggesting that successful implementation is achieved where goal consensus is high and only marginal changes are needed; furthermore, goal consensus is reached if ‘subordinates’ have participated in policy formation (Van Meter and Van Horn, 1975: 449). This argument contrasts with the bottom-up views because the authors are here proposing participation at the stage of policy formation. The implementation process set out in Figure 10

is depicted as a series of stages, with the arrows pointing forward or sideways (not back to the policy), indicating a top-down approach (Hill and Hupe, 2014).

**Figure 10: A Model of the Policy-Implementation Process (Source: Van Meter and Van Horn, 1975: 463)**

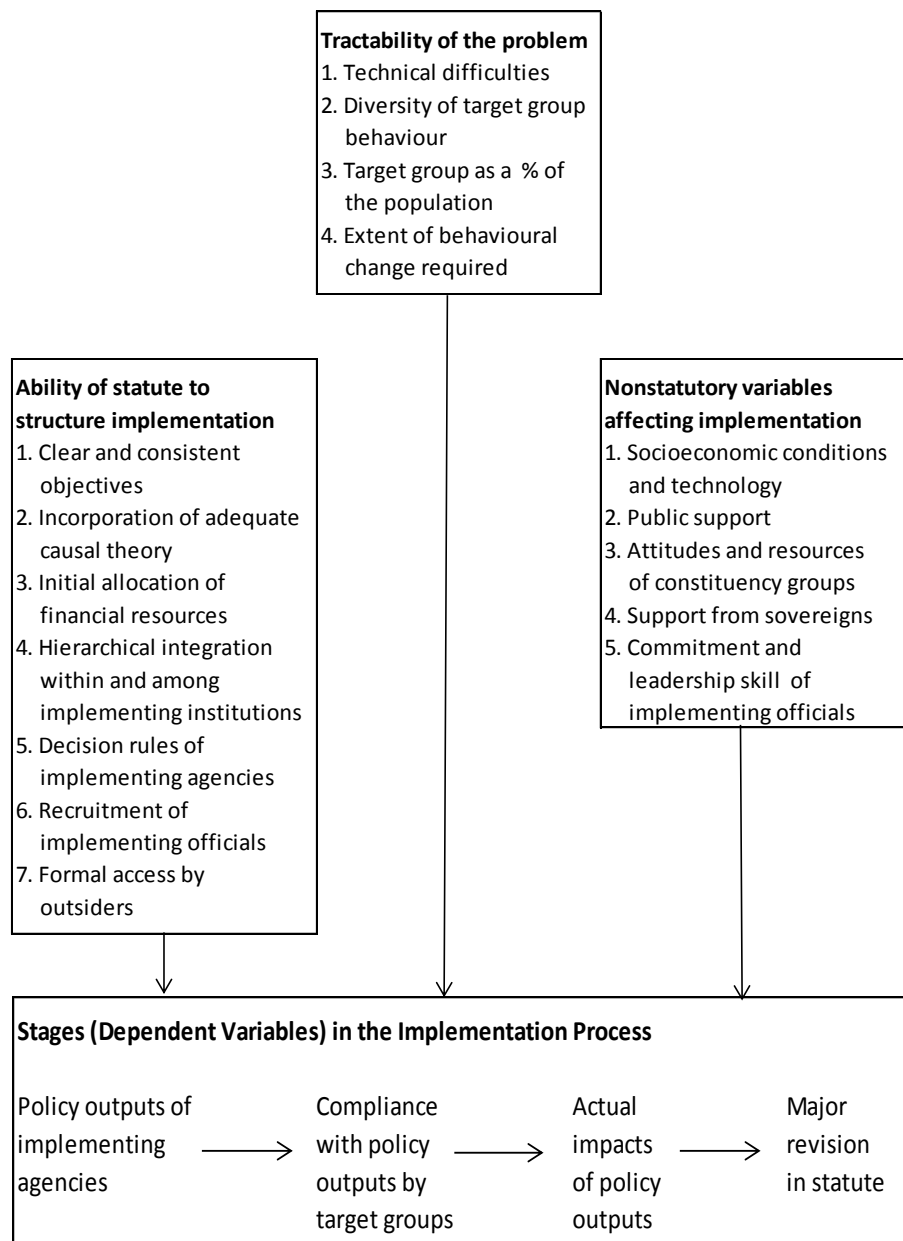


According to Mazmanian and Sabatier (1983), the starting point of policy implementation is the authoritative decision. This suggests centrally located actors, such as politicians and top-level bureaucrats, who are perceived as the most relevant in the achievement of the desired results (Paudel, 2009). The authors distinguish clearly between policy formation and policy implementation, recognising the role of the feedback process. The authors identify three types of variables which affect the implementation process, namely: tractability of the problem being addressed; nonstatutory variables affecting the implementation; and the ability of the statute to structure the implementation process. The first two types of variables constitute factors that will cause difficulties and the last type comprises factors that are crucial because

they may be controlled during the implementation process - recognition of such factors provides guidance to people at the top as to how to control implementation (Hill and Hupe, 2014).

The framework proposed by Mazmanian and Sabatier (1983) is set out in the diagram below:

**Figure 11: Variables involved in the Implementation Process (Source: Mazmanian and Sabatier, 1983: 22)**





Hogwood and Gunn (1984 cited in Hill and Hupe, 2014: 52) justify their top-down perspective on the basis that the people who design policies are elected in a democratic manner.

The top-down perspective is very prescriptive and seeks to generalise policy advice; it focuses on variables which could be controlled at a central level (Matland, 1995). The top-down view makes the following suggestions: the goals of the policy should be clear (Mazmanian and Sabatier, 1983; Van Meter and Van Horn, 1975); the degree of change should be limited (Van Meter and Van Horn, 1975); the number of players should be minimised (Pressman and Wildavsky, 1973); and the responsibility for implementation should be placed under an organisation which supports the goals of the policy (Van Meter and Van Horn, 1975; Sabatier, 1986).

Top-down models face their share of criticism. Firstly, the starting point of such models is the statutory language, without taking into account the actions taken earlier in the policy making process (Matland, 1995). Matland (1995) observes that if policy is taken as given without considering the initial stages of policy formation, the broader public objectives might be overlooked. Secondly, implementation has been regarded as an administrative process, disregarding the political issues surrounding it – in this respect, the emphasis on establishing clear goals is inconsistent with the ambiguous and contradictory goals inherent in the process of passing legislation (Matland, 1995). Lastly, the top-down view perceives the policy designers as key actors in the implementation process. However, it has been argued that service deliverers at a local level have the knowledge of the real problems and the expertise of dealing with them; further, service deliverers have great discretion, making it difficult for policy makers to control their actions (Matland, 1995). The top-down models view local

actors as impediments to successful implementation, requiring policy makers to control their behaviour (Paudel, 2009).

### **3.3.4 The bottom-up perspective**

The starting point of this perspective is a problem in society and in this regard, individuals and their behaviour represent the focal point in these models (Paudel, 2009). Lipsky (1980), who is considered by many theorists as the founding father of the bottom-up view, put forward a theory of ‘street-level bureaucracy’, where he analyses the behaviour of front-line people in policy delivery organisations. Lipsky (1980) considers street-level bureaucrats as having a better understanding of the customers’ needs because they are in direct contact with the people. Lipsky (1980) considers street-level bureaucrats to be the actual policy makers and to play a fundamental role in the implementation of public policies. Though the role of front-line staff is crucial for policy implementation, Lipsky (1980) argues that they are faced with huge time pressures to cater for the numerous needs of the public and as a result, these street-level bureaucrats develop techniques which deal with people in a stereotyped manner. The author claims that control from the top will result in street-level bureaucrats ignoring the needs of their customers and increasing their tendency to stereotype (Lipsky, 1980).

According to Berman (1978), policy implementation occurs at two levels – macro and micro. At macro-implementation level, centrally located planners design a government programme; at micro-implementation level, local agencies act in response to the macro-level plans by developing their own programmes and implementing them (Berman, 1978). Micro-level factors are only influenced indirectly by policy designers and the same implementation policy may be implemented differently at the local level (Matland, 1995). Palumbo et al (1984) argue that if local deliverers are not free to adapt the policy to local circumstances, the

programme would probably fail. Hjern (1982) observes that the success of a policy is largely dependent on the skill sets of people at the local level who can adjust the programme to suit the local circumstances; policy success depends only to a limited extent on central intervention.

Barrett and Fudge (1981, cited in Hill and Hupe, 2014) emphasise the political processes occurring during implementation and criticise the top-down view which tends to depoliticize the policy-action relationship, arguing that it is difficult to separate policy formation from implementation. Oosterwaal and Torenvlied (2012) investigate political conflict at policy formation stage, referring to it as ‘political divergence’ at the implementation phase.

Proponents of the bottom-up perspective therefore recommend a flexible strategy which allows for adaptation to local circumstances (Maynard-Moody et al, 1990).

Bottom-up models are also criticised. Firstly, it is argued that in a democratic society, policy control should be in the hands of individuals who are accountable to sovereign voters who have elected them democratically (Matland, 1995). In this respect, local service deliverers do not obtain their authority through a democratic election process. Secondly, the bottom-up view overemphasises the level of local autonomy – central policymakers can determine the required resources centrally and can significantly influence policy outcomes (Matland, 1995).

The table below sets out the main differences between top-down and bottom-up implementation approaches:

**Table 16: Differences between top-down and bottom-up approaches**

Variables	Top-down perspective	Bottom-up perspective
Policy decision-maker	Policymakers	Street-level bureaucrats
Starting point	Statutory language	Social problems
Structure	Formal	Both formal and informal
Process	Purely administrative	Networking, including administrative
Authority	Centralisation	Decentralisation
Output/Outcomes	Prescriptive	Descriptive
Discretion	Top-level bureaucrats	Bottom-level bureaucrats

*Source: Paudel (2009: 40)*

### 3.3.5 Combining the two perspectives

Clearly, the top-down and bottom-up views of the implementation approach present conflicting thoughts and each view tends to disregard the part of the implementation insights highlighted by the other. These two views are fundamentally in conflict with respect to what is success (consistency versus adaptation), how success is to be reached (clarity versus flexibility) and who should be the focal point for implementation (central versus local players) (Howard et al, 2010). In this regard, a number of researchers have attempted to synthesise the two perspectives, indicating whether the top-down versus the bottom-up approach is more appropriate under stipulated conditions.

Elmore (1979) attempted to combine the top-down and bottom-up views by proposing two approaches to implementation analysis - forward and backward mapping. Forward mapping consists of setting out clearly the policy objectives, it identifies specific steps which establish what is expected of implementers at each level and it specifies what a satisfactory outcome would be, in terms of the policy objectives originally stated and against which success or failure can be measured (Elmore, 1979: 602-603). Elmore (1979: 603) notes that the fundamental flaw of this approach is its assumption that policymakers control the

organizational, political and technological processes that affect implementation and thus, “reinforces the myth that implementation is controlled from the top”. Backward mapping presents an opposite view to forward mapping; it begins with a statement of the precise behaviour to be changed at the lowest level of the implementation process which gives rise to the need for a policy, it identifies a set of operations required to effect the change and moves up through the structure of implementing agencies until the central level is reached (Elmore, 1979: 604). Although Elmore’s approach is useful as a tool because it provides valuable suggestions for policy designers, as a theory, it lacks explanatory power (Matland, 1995).

Scharpf (1978: 347) employs network analysis in his study of implementation processes, emphasising that “it is unlikely, if not impossible, that public policy of any significance could result from the choice process of any single unified actor. Policy formulation and policy implementation are inevitably the result of interactions among a plurality of separate actors with separate interests, goals and strategies.” Scharpf (1978) notes that networks may be critical for addressing the ‘implementation deficit’ referred to by Pressman and Wildavsky. The policy network approach was also discussed by Klijn and Koppenjan (2000: 139) who stated that “policy is made in complex interaction processes between a large number of actors which takes place within networks of interdependent actors”. Cooperation is crucial to achieve the desired policy outcome; O’Toole (1988) observes that network management is aimed to improve cooperation between the actors. The government is regarded as an actor in policy networks, though it has a special role in view of its unique goals and resources (Hill and Hupe, 2006). The government can assume diverse roles in a network situation: it can choose to perform tasks in collaboration with private or other public actors; it can take the role of process manager, it can act as network builder or it can decide not to participate (Klijn and Koppenjan, 2000).

Berman (1980) states that the adoption of either the top-down or bottom-up approach for an implementation plan depends on a number of factors surrounding the policy context, including scope of change, goal conflict, technology and environmental stability. The author notes that these contextual factors cannot be influenced by the implementation designer. Berman (1980) suggests that the implementation plan should follow a top-down approach when change is incremental, goal conflict is low, technology is certain and a stable environment exists; on the other hand, a bottom-up approach is recommended when major policy changes are on the agenda, goal conflicts exist, the technology involved is uncertain and the environment is unstable.

Ripley and Franklin (1982: 9) describe implementation processes as follows, identifying five characteristics:

*“Implementation processes involve many important actors holding diffuse and competing goals who work within a context of an increasingly large and complex mix of government programmes that require participation from numerous layers and units of government and who are affected by powerful factors beyond their control.”*

The authors give particular attention to the political nature inherent in the implementation process and they also emphasise that the type of policy is relevant for the implementation process.

Sabatier (1986, 1991) moved away from the top-down approach, towards a combined view, accepting some of the strengths of the bottom-up perspective. According to Sabatier (1986), the way forward for viewing the policy process is to take an ‘advocacy coalition’ approach. Advocacy coalitions represent “*actors from various public and private organizations who share a set of beliefs and who seek to realise their common goals over time*” (Sabatier, 1986: 39). The ‘advocacy coalition’ approach adopts:

*“the bottom-uppers' unit of analysis – a whole variety of public and private actors involved with a policy problem – as well as their concerns with understanding the perspectives and strategies of all major categories of actors (not simply programme proponents). It then combines this starting point with top-downers' concerns with the manner in which socio-economic conditions and legal instruments constrain behaviour. It applies this synthesized perspective to the analysis of policy change over periods of a decade or more.”* (Sabatier, 1986: 39)

Sabatier's approach is closer to the bottom-up view because it includes actors from all levels (Hill and Hupe, 2014).

Lane (1987: 542) distinguishes between responsibility and trust, arguing that 'responsibility' issues concern the “*relationship between objectives and outcome*”, whilst 'trust' relates to “*the process of putting policies into effect*”. In this regard, the author notes that the top-down approach highlights the 'responsibility side' whilst the bottom-up view emphasises the 'trust side'. Lane (1987: 543) then claims that:

*“An implementation process is a combination of responsibility and trust...Without the notion of implementation as policy accomplishment there is no basis for evaluating policies and holding politicians, administrators and professionals accountable. On the other hand, implementation as policy execution rests upon trust or a certain amount of degrees of freedom for politicians and implementers to make choices about alternative means for the accomplishment of goals.”*

Goggin et al (1990) propose a 'communications model' for analysing implementation, which emphasises communication issues between layers of government (federal, state and local). The model includes elements from the top-down and bottom-up approaches. The authors identify three groups of variables which influence state implementation: inducements and constraints from the top (federal level); inducements and constraints from the bottom (state and local levels); and a state's decisional outcomes together with a state's capacity to act. The communications model acknowledges that distortions happen, signals are interpreted

differently and contextual circumstances can impact the perception of signals (Matland, 1995).

Rather than proposing a model which combines the top-down and bottom-up approaches, Matland (1995) developed a model – ‘the ambiguity/conflict model’ – which explains when the two approaches are most suitable. Matland (1995) noted that the implementation literature lacks theoretical structure and therefore, through his model, he sought to put forward a more theoretically based approach to implementation. The author observed that implementation studies have largely focused on presenting lists of variables which impact implementation, without explaining the theoretical relationships between them and without pointing to the conditions under which these variables are relevant (Matland, 1995: 153). For these reasons, it was considered useful to apply Matland’s theoretically based approach to the study, with a view to assess the robustness of this model and, if applicable, suggest improvements and refinements to the model that might come out of the empirical data gathering process.

The ambiguity/conflict model presents four implementation perspectives, based on a policy’s ambiguity and conflict level, as set out in the following diagram:



**Figure 12: Ambiguity-Conflict Matrix: Policy Implementation Processes (Source: Matland, 1995: 160)**

		CONFLICT	
		Low	High
AMBIGUITY	Low	<p><b>Administrative Implementation</b></p> <p>Resources</p>	<p><b>Political Implementation</b></p> <p>Power</p>
	High	<p><b>Experimental Implementation</b></p> <p>Contextual Conditions</p>	<p><b>Symbolic Implementation</b></p> <p>Coalition Strength</p>

Matland (1995: 156) claims that *policy conflict* in implementation arises when a number of organisations consider a policy as relevant to their interests and at the same time, these organisations have incompatible views either regarding the goals of the policy or the planned activities to implement such a policy. When conflict exists, a bargaining process ensues, focusing exclusively on achieving an agreement on actions, rather than agreeing on goals (Matland, 1995: 156). Whilst top-down proponents believe that a policy's level of conflict can be manipulated, bottom-up advocates claim that conflict cannot be manipulated (Berman, 1980). Matland (1995: 157) argues that certain types of conflict can be manipulated; conversely "*some policies are inevitably controversial and it is not possible to adjust them to avoid conflict*". The type of mechanisms employed to resolve conflict depend on whether the conflict level is high or low – at low conflict levels, persuasion or problem-solving are commonly used; at high conflict levels, bargaining and coercion are more common (Matland, 1995: 157).

With respect to *policy ambiguity*, the author identifies two aspects – ambiguity of goals and ambiguity of means. Top-down proponents argue that goal ambiguity is one of the reasons for implementation failure and therefore, the policy goals should be clearly stated. Matland (1995: 158) maintains that this suggestion ignores the positive effects of ambiguity, because goal ambiguity could be a way to limit conflict, allowing for different interpretations by diverse actors. Ambiguity of means mostly exists where the technology required to achieve the goals of a policy is still not available or where the environment is so complex that the choice of tools is not straightforward (Matland, 1995: 158). Though top-down approaches suggest that policy ambiguity should be eliminated, Matland (1995) notes that it is unclear whether ambiguity can be influenced in the policy design process.

The four implementation perspectives proposed by Matland (1995) are explained in the following table:

**Table 17: Implementation perspectives**

Policy implementation processes	
Process	Explanation
Administrative implementation	An <i>administrative implementation</i> is characterised by low ambiguity and low conflict, where goals are clear and the means (technology) for implementing the policy is known (Matland, 1995). In this type of implementation, if sufficient resources are allocated to the programme, then the expected outcome is assured (Matland, 1995). The problems that arise under conditions of low conflict and low ambiguity are of a technical nature and include lack of financial and time resources, poor coordination or an ineffective monitoring system to control deviant behaviour (Matland, 1995). The administrative implementation process largely reflects the views of a top-down perspective.
Political implementation	The author suggests that a <i>political implementation</i> typically exhibits low ambiguity and high conflict. In this type of implementation, goals are clearly defined, but incompatible; furthermore, “ <i>outcomes are decided by power</i> ” (Matland, 1995: 163). In this situation, resources which are required for the policy implementation are controlled by actors who are sceptical or opposed to the policy and therefore, if the implementation is to succeed, the implementer either needs to have the power to force his/her will on the other actors or has to have the resources to be in a position to bargain (using coercive and remunerative methods) for the purpose of reaching agreement on actions (Matland, 1995). Political implementation is captured by top-down models which highlight political factors as fundamental in achieving the desired results.
Experimental implementation	<i>Experimental implementation</i> is typical of a policy which displays high ambiguity and low conflict. This implementation process includes policies with both unclear goals and means, as well as policies with clear and supported goals but unclear means of implementation (Matland, 1995: 167). In experimental implementation, technology is uncertain and ambiguity is seen as an opportunity to learn (Matland, 1995). The bottom-up approach reflects more closely the circumstances described in this implementation process, since ambiguity is more acceptable in bottom-up models (Matland, 1995: 167).
Symbolic implementation	Policies exhibiting high levels of ambiguity and high levels of conflict are described by the author as <i>symbolic implementation</i> processes. Despite the fact that the policy is vague, this type of implementation exhibits high conflict. The strength of coalitions determines the outcomes under this process. Matland (1995) observes that for this type of implementation, both the top-down and the bottom-up approaches have some relevance.

Source: Matland (1995)

In relation to Matland’s model, Hill and Hupe (2006: 76-77) maintain that the model provides some valuable suggestions for implementation research; at the same time, they pose the following question: “*How easy is it to label policies in the way he does?*”

### 3.3.6 Measures of implementation success and success factors

Linton (2002) suggests that the benefits of an innovation will be achieved if implementation results in a positive outcome. To this effect, the author summarises the measures of implementation success (Linton, 2002: 67-69) and the factors that lead to implementation success (Linton, 2002: 69-72), as set out below:

**Table 18: Implementation success**

Measures of implementation success	Factors that lead to implementation success
<ul style="list-style-type: none"> <li>• Routinisation occurs when the implementation phase is completed</li> <li>• Incorporation measures whether an innovation is utilised to its full capacity</li> <li>• The time taken to implement an innovation is an indicator of the efficiency of the implementation process: if an innovation is implemented in a short time-frame, its benefits will be reaped sooner</li> <li>• Management satisfaction with the innovation</li> <li>• Goal achievement measures whether the innovation met its expectations</li> <li>• Payback calculation: the shorter the payback, the more desirable is the innovation</li> </ul>	<ul style="list-style-type: none"> <li>• Organisational structure: implementation success depends on organisational traits including structure, size and culture</li> <li>• Technology: the complexity of the technology affects the outcome of an implementation</li> <li>• Project management affects positively the success of an implementation if it is properly understood and effectively used by the implementer</li> <li>• Divisibility of a programme into smaller elements reduces the risk of an implementation</li> <li>• Social interactions including management buy-in, technology championing, communication between implementers and other involved individuals, personnel training and interactions with suppliers and consultants, are factors which positively influence the success of the implementation process</li> </ul>

Source: Linton (2002)

### 3.3.7 Limitations of the implementation literature

A number of scholars have commented on the shortcomings of the existing implementation literature. Goggin et al (1990) observed that implementation, as a separate field of study, is still in its infancy. Rothstein (1988 cited in Hill and Hupe, 2006: 79-80) describes implementation research as “*to a great extent...misery research*”; the author identifies three issues with implementation research: firstly, the research is largely focused on programmes which failed; secondly, programmes with high complexities and ambitions are focused upon; and finally, the research took an extremely rationalistic and mechanistic view of the implementation process. Matland (1995) claimed that the implementation literature lacks theoretical structure, largely focusing on providing lists of variables affecting implementation. Similarly, Hill and Hupe (2006: 80) maintain that the result of the implementation research has been the “*accumulation of checklists of factors that may affect success in the implementation process*”. Paudel (2009: 50) states that the implementation literature “*is dominated by the top-down and bottom-up perspectives and their synthesis*”; however “*the concrete theory of policy implementation is still lacking*”. Linton (2002) notes that there is still the need for theory building in the area of implementation research.

### 3.3.8 The implementation of performance budgeting in Malta

As discussed earlier, the top-down approach involves a more centralised and systematic approach for the implementation of budgetary reforms. With this approach, the principal responsibility for developing, implementing and monitoring PB initiatives would rest with a central governmental agency, possibly the MOF or the OPM (OECD, 2007). The central agency is also responsible for issuing rules and guidelines to all ministries and departments.

In a bottom-up approach, there is less enforcement from the top and the individual agencies are allowed to develop their own systems and methods (OECD, 2007). Their participation may be on a voluntary basis. The individual ministries and departments are the key players in the reform process and central intervention is minimal. This approach is considered to be more ad hoc than systematic, because of the lack of central enforcement and its voluntary characteristic (OECD, 2007).

In most OECD countries, the MOF is mainly responsible for the PB reforms, but it is usually supported by the OPM (OECD, 2007). The role played by the MOF in developing and implementing PB varies across countries: there are countries, such as the UK, which operate a centralised top-down approach where the MOF is highly involved in the development and implementation of the budgetary reforms; on the other hand, there are countries, such as Denmark and Iceland, which have adopted a decentralised bottom-up approach where the individual ministries are responsible for the implementation of the reforms and the involvement of the MOF is minimal and limited to issuing advice and guidelines (OECD, 2007). Other countries adopt an approach which lies between these two extremes.

In their study, the OECD (2007) have identified the benefits and risks involved in a top-down versus a bottom-up implementation approach, as illustrated in the table below:

**Table 19: Potential benefits and risks of top-down and bottom-up implementation approaches**

	Benefits	Risks
<b>Top-down approach</b>	Stronger pressure for reform	Limiting flexibility to achieve results
	Uniformity in approach and framework across government	Too rule-bound, and performance becomes mere compliance
	More information at the centre to make decisions	Creating too many reporting requirements and becoming an expensive paper exercise
	Better coordination and monitoring	Failing to gain the support of agencies
		Creating perverse incentives and distorting behaviour
<b>Bottom-up approach</b>	Greater flexibility	Inertia due to lack of pressure to reform
	Capacity to tailor reforms to agencies' needs	Being more difficult and time-consuming to implement
	Enables greater responsiveness to clients and local communities	Lack of coordination of reforms
	Encourages ownership of reforms by agencies	Lack of information at the centre to make decisions
		Lack of consistency in reform efforts and presentation of data

*Source: OECD (2007: 34)*

With the current line-item budgeting system operated in Malta, the individual ministries submit their requests for funding to the MOF; this is then followed by rounds of discussions between the individual ministries and the MOF. The final decision with respect to the funds to be allocated to each ministry is made by the MOF upon recommendations from the OPM.

If PB is introduced, the individual ministries ('street-level bureaucrats') would potentially be involved in developing performance measures and setting performance targets; however, the MOF would still potentially play an active role in the implementation of this budgetary reform, holding responsibility for the approval of the final performance measures and targets following a negotiation process with the individual ministries. The benefit of involving the individual ministries in the development of performance measures and targets is that these implementers would feel ownership of the budgetary reforms and would be motivated to deliver the results. Cooperation between the parties involved and development of

collaborative networks increases the likelihood of successful implementation (Scharpf, 1978). Moreover, as has been argued by Lipsky (1980), street-level bureaucrats play an important role in implementing policies because of their direct contact and better understanding of the needs of the people. This knowledge and experience held by the local implementers will translate in the development of performance targets which better reflect the needs of the citizens. The top-down models consider street-level implementers as providing obstacles to successful implementation (Paudel, 2009) – in the Maltese context, the local implementers should be regarded as contributors to the implementation process, rather than as impediments.

However, central involvement is still required – lack of central involvement might lead to non-implementation of the reforms at a departmental level. Furthermore, the involvement of the MOF ensures uniformity in the presentation of information which makes possible the comparison of performance across ministries and across the whole of government. The MOF would also be responsible for providing formal and/or informal rules, guidelines and procedures which have to be followed by the individual ministries and departments in the operation of the new budgeting system.

In summary, the above preliminary analysis indicates that the approach which should be adopted for the implementation of PB in Malta is a combined approach, with greater emphasis on the bottom-up perspective. In this regard, central involvement is considered to be extremely important to ensure consistency in the generation of PI and successful implementation of the reform across the whole of government.



**CHAPTER 4:**  
**LITERATURE REVIEW III**  
***BUDGETING IN MALTA***

## 4.1 Introduction

This chapter starts off by providing an overview of the trends in Malta's key economic indicators over the last few years. A summary of the main events which affected the country's credit rating in recent years is then provided. Next, the functions of the Budget Office and the Economic Policy Department (EPD), two units that fall under the portfolio of the MOF, are described. This is followed by an outline of Malta's existing budgetary process and a description of the budget documents being currently compiled. Subsequently, highlights from the Fiscal Responsibility Act recently enacted in Malta, are given. The last section then presents an analysis of actual and budgeted expenditure in the health and education sectors.

Based on documentary sources, this chapter seeks to describe the Maltese economic environment and the current budgetary framework, paving the way for a better understanding of the context in which PB might be implemented and for facilitating the identification of recent budgetary reforms, in support of the first and second research objectives respectively<sup>8</sup>. An illustration of the budget positions of the education and health ministries is also provided, in view of the fact that representatives from these ministries were selected to participate in the empirical data collection, for the purpose of obtaining the line ministries' viewpoints.

## 4.2 Economic trends

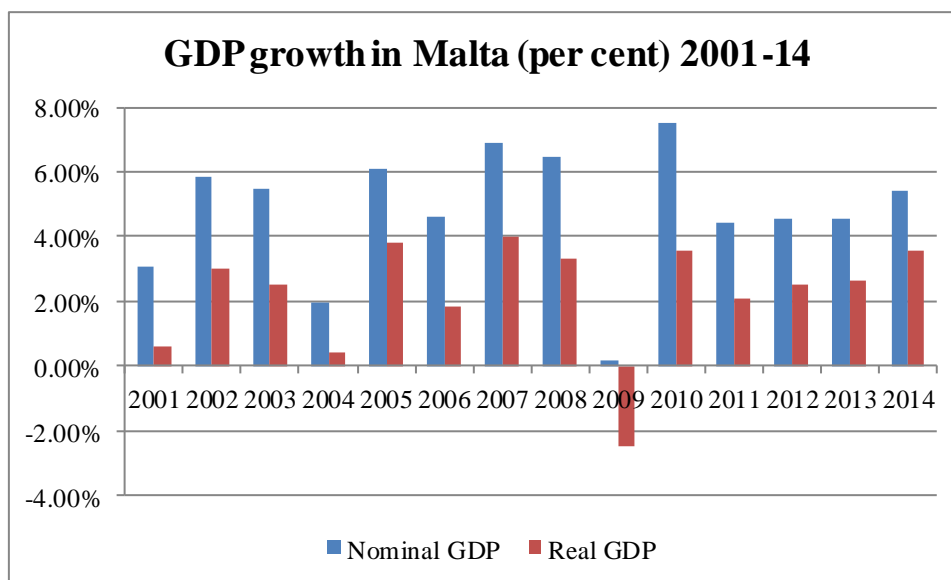
This section highlights Malta's economic performance over the period from 2001 to 2014, as depicted by trends in key economic variables analysed on an annual basis (illustrated in Figures 13 to 18 below).

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<sup>8</sup> Vide section 1.6

Malta's key strengths are its limestone, a favourable geographic location and a productive labour force. The economy is highly dependent on tourism, financial services, foreign trade and manufacturing (mainly pharmaceuticals and electronics). Malta's main trading partners are Europe and Asia, though a substantial amount of goods are exported to the African market with the majority bound for Libya (KPMG, 2013).

Looking forward, Malta must continue to invest in its human resources and in its knowledge based industries in order to increase its competitiveness (KPMG, 2013). Malta's low labour participation rate could be perceived as an impediment to higher economic growth. As a result, government is introducing measures and incentives to encourage older workers to remain longer in the work force and to encourage females to enter the labour market (Central Bank of Malta (CBM), 2007). Furthermore, in order to enhance its growth potential, Malta must adopt further policies for safeguarding fiscal sustainability and maintaining macroeconomic and financial stability, as suggested in the IMF country report (Malta Financial Services Authority, 2013).

**Figure 13: Growth in Gross Domestic Product in Malta, 2001 to 2014**

Source: National Statistics Office, Central Bank of Malta

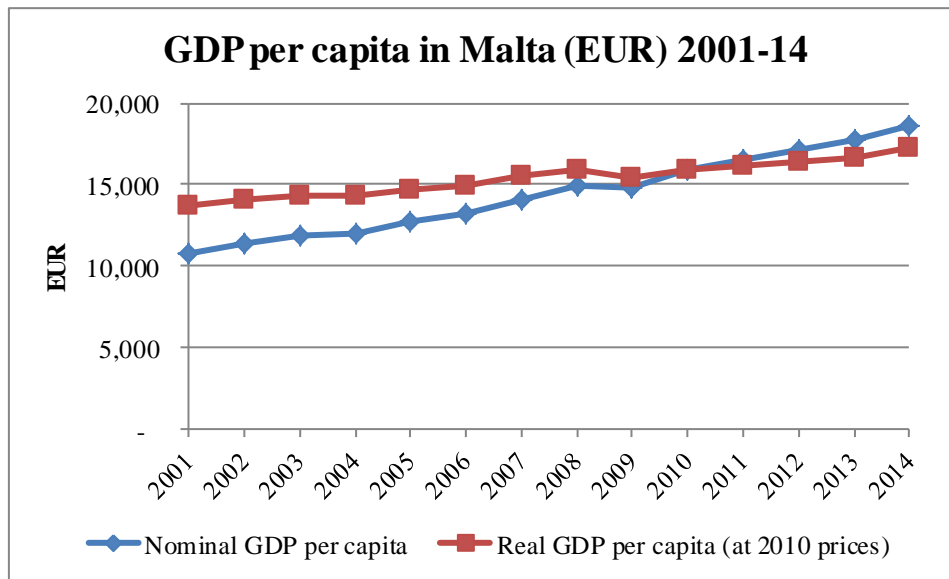
*Notes:*

Over the last 14 years, annual GDP growth in nominal terms averaged around 4.8%, with real GDP growth (at 2010 prices) averaging around 2.2% per annum.

After a few years of low growth between 2001 and 2004, which was largely underpinned by a slowdown in the tourism and electronics industries, real GDP growth recovered in the years between 2005 and 2008, averaging about 3.2% per annum. The recovery in 2005 was mainly attributable to improved productivity levels, according to a study compiled by the European Commission (CBM, 2007).

In 2009, Malta's economy slipped into recession and real GDP contracted. The country's high dependency on food and energy imports and on the tourism industry, make the economy particularly vulnerable to swings in other countries' economies. As tourism declined in 2009 in view of neighbouring countries' economic difficulties, Malta's economy was negatively affected and registered negative growth.

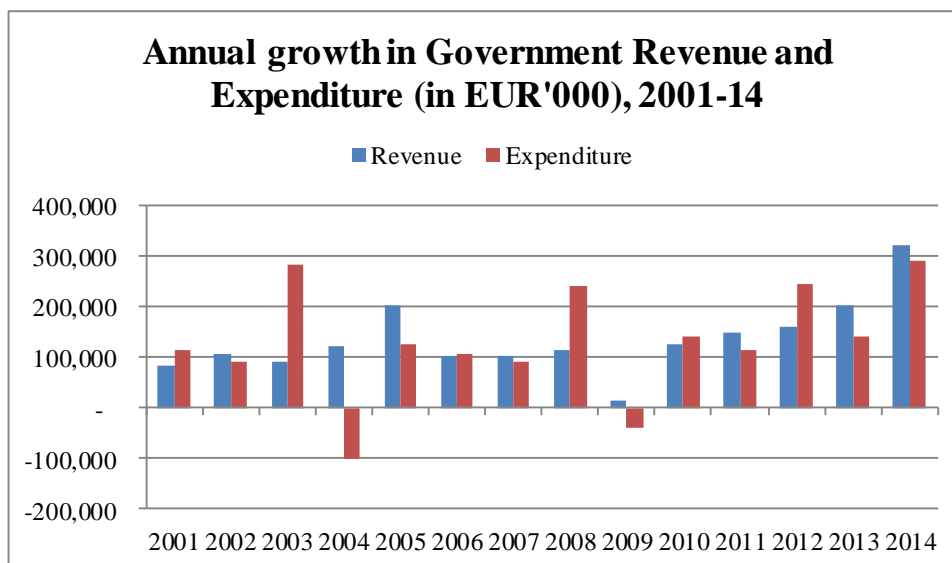
During 2010, the country's nominal GDP grew by about 7.5% over the previous year whilst real GDP registered an increase of 3.5%. Malta's GDP grew further in the following two years, reaching an average real GDP growth of around 2.3% per annum. This expansion in the economy was driven by significant growth emanating mainly from the financial services and Information Technology industries, as well as from other service activities (KPMG, 2013). Economic activity in Malta continued to grow during 2013 and 2014, with real GDP growth reaching 2.6% in 2013 and rising to 3.5% for 2014. This growth was mainly driven by domestic demand, with the largest contributor to the increased economic activity being investment (CBM, 2015).

**Figure 14: Gross Domestic Product per Capita in Malta, 2001 to 2014**

Source: National Statistics Office, Central Bank of Malta

*Notes:*

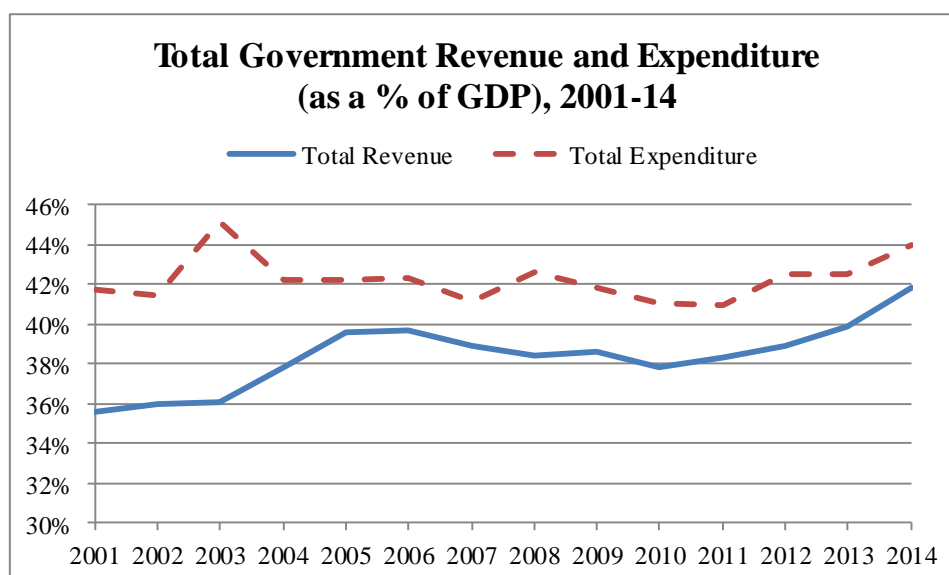
GDP per capita in nominal terms has increased steadily during the period under consideration, from €10,800 in 2001 to €18,700 in 2014. In real terms (at 2010 prices), the growth in GDP per capita over 2001 to 2014 averaged around 1.5% per annum.

**Figure 15: Annual Growth in Government Revenue and Expenditure, 2001 to 2014**

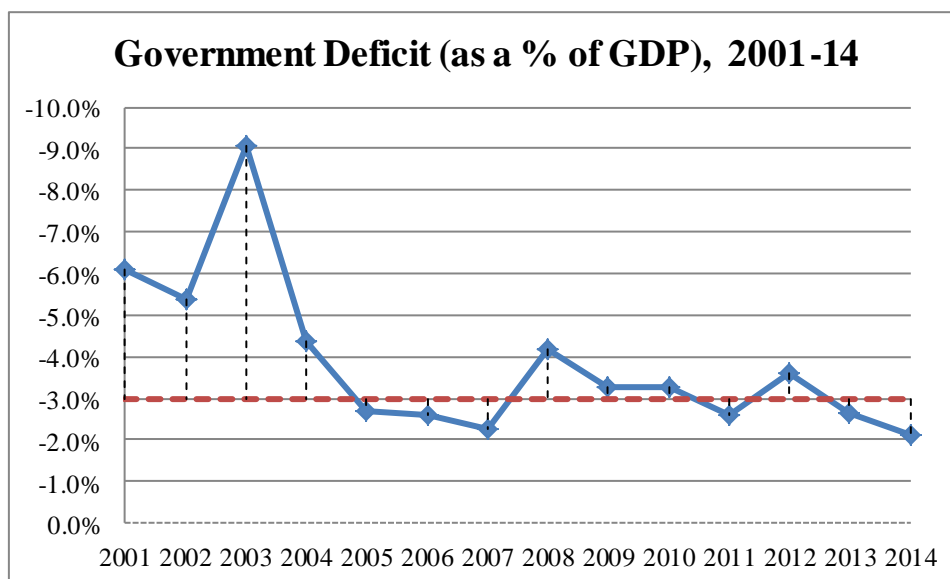
Source: Central Bank of Malta

*Notes:*

Total government revenue and expenditure have grown by an average of around 6.2% and 5.5% respectively over the period from 2001 to 2014. During 2014, general government revenue grew by 10.6%, reflecting higher tax revenue, arising from fiscal measures as well as positive economic developments (CBM, 2015). At the same time, expenditure rose by 9.0% in 2014, mainly reflecting higher spending on social assistance and retirement pensions, and increased expenditure in the education and health sectors (CBM, 2015).

**Figure 16: Government Revenue and Expenditure as a percentage of Gross Domestic Product, 2001 to 2014**

Source: National Statistics Office, Central Bank of Malta

**Figure 17: Government Deficit as a percentage of Gross Domestic Product, 2001 to 2014**

Source: National Statistics Office, Central Bank of Malta

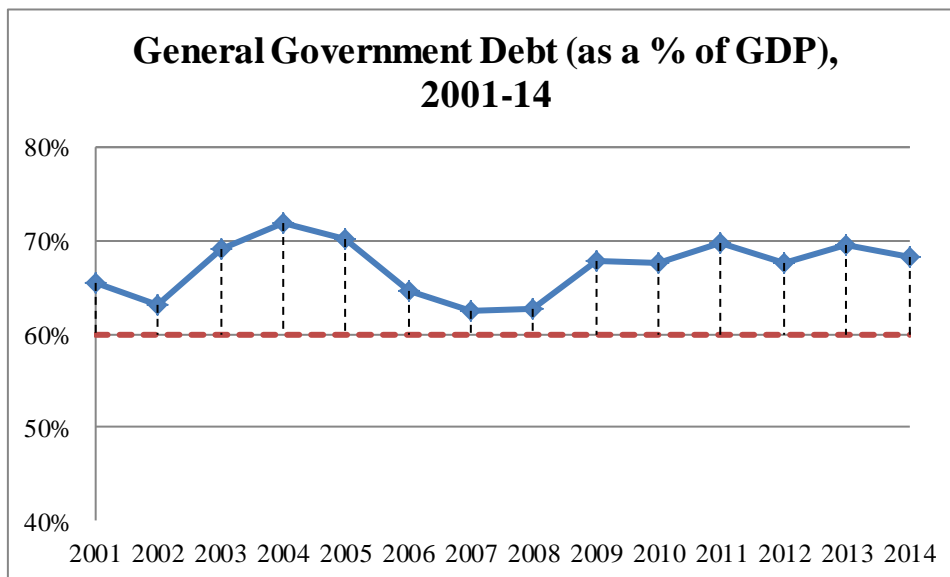
*Notes:*

Malta's budget has been in deficit throughout the period under consideration.

During the period under consideration, government deficit as a percentage of GDP peaked at just above 9% in 2003, declined steadily beyond 2003 until 2007 (reaching a level of 2.3%) and went up again to around 4.2% in 2008. Subsequent to 2008, it decreased again, falling below the 3% benchmark during 2011. (The Maastricht criteria for qualification and participation in the Economic and Monetary Union specify that the planned or actual government deficit should not exceed 3% of each country's GDP at market prices.) However at the end of 2012, the deficit was observed at above the 3% of GDP threshold. As a result of this, in June 2013, the EU placed Malta under an excessive deficit procedure. Subsequently, Malta ended 2013 with a deficit of 2.8% of the GDP and in 2014, the deficit declined further to 2.1% of GDP. This led to the closure of the excessive deficit procedure which had been opened against Malta.

The Maltese government has so far avoided the implementation of any austerity measures by the EU, mainly because no extraordinary intervention, such as bailouts to the financial sector, was needed to deal with the consequences of the European recession (KPMG, 2013). Government's favoured strategy seems to be attracting foreign investment to the country which would result in reducing the deficit through higher tax revenue rather than through significant cuts in expenditure (KPMG, 2013). Notwithstanding, government may have to complement the increase in revenue with a reduction in spending in order to keep the deficit below the required threshold.

**Figure 18: General Government Debt as a percentage of Gross Domestic Product, 2001 to 2014**



Source: National Statistics Office, Central Bank of Malta

*Notes:*

All EU member states, including Malta, accumulated debt throughout the years, diverging from the 60% benchmark. (The Maastricht criteria stipulate that the government debt is not to exceed 60% of GDP at market prices.) As shown below, at the end of 2014, Malta's General Government Debt expressed as a percentage of GDP stood at around 68%. The international credit rating agencies consistently refer to the Maltese government's high national debt as a constraint to economic growth, with debt reduction being one of the main challenges of the government in Malta.

As an upside, public debt in Malta is primarily composed of locally subscribed debt. In fact, as at the end of 2014, over 90% of the total government debt was in the form of Malta Government Stocks which are mainly held by Maltese residents and businesses.

The simplest measure to control further growth of government debt is to raise taxation and cut government spending (KPMG, 2012). However, these direct measures can have a negative effect on economic growth, especially if cuts in government expenditure are directed towards activities which promote investment and innovation, such as research and development and if the imposition of higher taxation acts as an impediment for investment initiatives (KPMG, 2012).

### 4.3 Malta's credit ratings

The fiscal deficit issues and high government debt, which Malta has faced in recent years (refer to Figures 17 and 18 above), have led to a series of downgrades in its sovereign rating



by credit rating agencies. The table below highlights the main events which affected the country's credit rating in recent years.

**Table 20: Changes in credit rating**

Date	Malta's deficit issues and credit rating
Nov-11	Malta at risk of not meeting its target for deficit reduction to below 3% of GDP by end 2011 – Government's 2012 Budget projects deficit to 2.8% of GDP by end 2011 and to 2.3% in 2012
Jan-12	Government commits to reduce spending by a further €40m
Jan-12	S&P's lowers Malta's credit rating a notch to A-
Feb-12	Malta received one-notch downgrades from Moody's; negative outlook maintained; downgrade of the foreign- and local-currency debt ratings of Malta Freeport from A2 to A3
Sep-12	Moody's affirms Malta's A3 rating and negative outlook
Jan-13	S&P's downgrades Malta's LT sovereign credit rating to BBB+; ST sovereign credit rating kept at A-2; stable long-term outlook maintained (Government's debt burden highlighted, referring esp. to Enemalta)
Mar-13	S&P's gives Enemalta a negative outlook: projected to remain loss-making till 2016
May-13	EU projects deficit at 3.7% of GDP by end of 2013 – Government commits to keep the deficit at 2.7%
Jun-13	EU placed Malta under an excessive deficit procedure - fiscal deficit observed at 3.3% of GDP end 2012; Maltese government remains committed to a targeted deficit of 2.7% by end of 2013
Jul-13	S&P's affirmed Malta's sovereign credit rating at BBB+/A-2 with a stable outlook
Sep-13	Fitch Ratings downgrades Malta's LT foreign and local currency issuer default ratings from A+ to A (stable outlook): downgrade reflects fiscal slippage and Malta's EDP issues
Oct-13	Moody's affirmed Malta's A3 government bond rating and changed the outlook to stable from negative
Feb-14	S&P's has revised its outlook for Enemalta to stable from negative: government's restructuring plan and near finalisation of transaction with Chinese company for equity injection
Mar-14	Fitch affirms Malta at 'A' rating; outlook stable acknowledging that the Maltese economy is on the road to recovery
Apr-14	Figures published by Eurostat indicated that Malta ended 2013 with a deficit of 2.8% of the GDP, down from 3.3% at the end of 2012
Jul-14	S&P reaffirms Malta's credit rating at 'BBB+/A-2', with a stable outlook
Sep-14	Fitch affirmed its 'A' ratings for Malta and the stable outlook, warning of expenditure slippages
Oct-14	Moody's reconfirmed Malta's A3 rating with a stable outlook, highlighting the national debt as government's main challenge
Jan-15	S&P's 'BBB+' rating, with a stable outlook, reaffirmed
Feb-15	Fitch Ratings has affirmed Malta's long-term foreign and local currency issuer default rating (IDRs) at 'A'; the outlooks are stable
Jun-15	The European Commission lifts the excessive deficit procedure against Malta, in view of the deficit standing at 2.1% at the end of 2014
Jul-15	S&P upgraded the country's outlook from stable to positive, affirming the BBB+ rating, based on the Maltese economy's growth prospects
Aug-15	Fitch has affirmed Malta's 'A' rating, with a stable outlook in August 2015
Jan-16	S&P's has affirmed Malta's ratings at BBB+/A-2 and said the outlook remained positive

Source: *Times of Malta; Malta Today*

As illustrated in the above table, at the beginning of 2014, the credit ratings started to show some improvements, reflecting the fact that Malta ended 2013 with a deficit of 2.8% of GDP (below the 3% threshold) and acknowledging that the country's economy was on the road to recovery. These improvements subsequently led to the closure of the EDP in 2015.

The table below sets out the current sovereign ratings assigned to Malta by credit-rating agencies:

**Table 21: Malta's current sovereign ratings**

Malta Sovereign Credit Ratings				
Rating Agency	Long-term	Short-term	Outlook	Date of Latest Update
Fitch	A	F1	Stable	21/08/2015
Moody's	A3	n/a	Stable	28/10/2014
Standard & Poor's	BBB+	A-2	Positive	08/01/2016

*Source: Ministry for Finance (2016)*

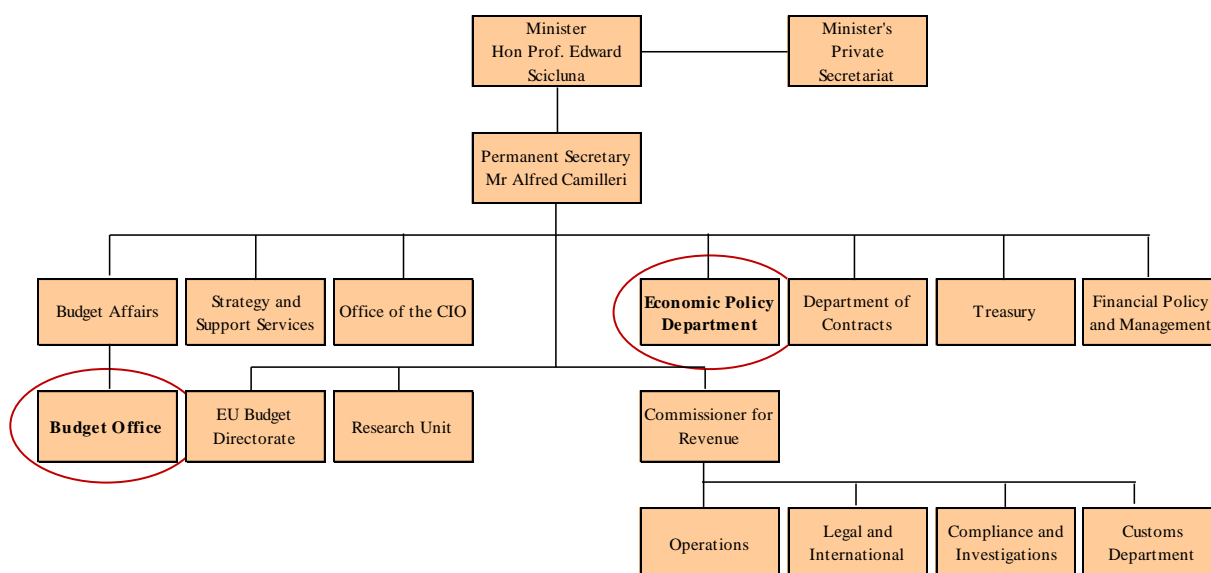
Notwithstanding the recent growth in the country's economy and the lifting of the EDP, the rating agencies warned that government's high debt burden was considered as a constraint and that government is expected to deal with issues such as health care, energy sector and pension reforms in order to avoid slippages in public expenditure. In this context, the implementation of PB may assist in directing public funds to programmes which are delivering results and in eliminating ineffective expenditure, such that the fiscal deficit will be controlled and the debt burden reduced.

#### 4.4 MOF divisions involved in budgeting

The Public Administration is the fundamental body within Government which is responsible for the management of public programmes. There are fourteen ministries under the current administration, including the MOF (Government of Malta website).

The organisation chart for the MOF is depicted below. Both the Budget Office and the EPD form part of the MOF's portfolio and are heavily involved in the budgetary process.

**Figure 19: Organisation Chart, MOF (Source: [www.http://mfin.gov.mt](http://mfin.gov.mt))**



The Budget Office is responsible for the publication of the financial estimates for the next fiscal year, as part of the annual budget process. The budgetary process incorporates ministries, departments and public entities. The principal functions of the Budget Office include the provision of advice to government on the apportionment of the government's financial resources in reflection of set priorities, as well as the compilation of draft annual and medium-term expenditure and revenue projections for ministries, departments and public entities. The Office also provides recommendations for the application of corrective measures,

where issues of expenditure over-runs or revenue shortfalls are expected, as the financial year progresses (MOF website).

The EPD provides government with advice in designing economic policy, managing economic activity and formulating international trade policy, for the purpose of achieving the country's targeted economic growth (MOF website). As part of the budgetary process, this department is responsible for economic planning and for estimating the macro-economic variables, which then feed into the budget compiled by the Budget Office.

## **4.5 Budgetary framework**

### **4.5.1 Current budgetary process**

Malta currently operates a traditional budgeting system. Expenditures are forecasted for the following fiscal year and they are presented in two budgets, one comprising government's recurrent operations by expenditure categories and the other one setting out capital expenditures. Operating expenses include costs for the day-to-day operations such as personnel, travel, maintenance, office supplies and utility costs. The capital outlays comprise the acquisition of long-lived assets such as land, buildings, equipment and vehicles.

As part of the budget process, the financial planning process covering the subsequent fiscal year is launched in April/May of the current year, by means of a circular issued by the Permanent Secretary within the MOF to Permanent Secretaries, Directors General and Directors. Ministries are required to submit their budget requirements for the upcoming year. Following these submissions, the MOF holds inter-ministerial discussions in two stages. A first round of meetings is held between the MOF and the respective Ministry individually, at Permanent Secretary level, for the purpose of discussing the submissions received. A second

round of meetings is subsequently held at Ministerial level, focusing on national priorities (MOF website). At the end of the budgetary process, the Budget is approved by a majority vote in Parliament.

In recent years, Government's policy was targeted at ensuring reductions in the yearly fiscal deficit. For instance, in compiling the financial plans for 2013, government ministries, departments and entities were requested to seek expenditure efficiencies. The MOF informed the ministries, departments and entities that the assumption to be applied for both recurrent and capital expenditure, was that the budgets for the following year would be equivalent to the approved budgetary allocations included in the preceding year's financial estimates. Ministries, departments and entities were instructed to keep requests for additional funding (vis-à-vis the previous year's allocations) at an absolute minimum, and limited to instances where non-provision of funds above the previous year's allocations would adversely affect the core workings of the ministry, department or entity (MOF website).

The 2014 Financial Estimates which were presented to Parliament in November 2013 as part of the budget process, incorporated, for the first time, three-year revenue and expenditure projections for 2014 to 2016, at line ministry level.

As part of the financial planning process for 2015, the MOF instructed line ministries to refer to the 2015 projections (which were published as part of three-year projections incorporated in the 2014 Financial Estimates), and to ensure that in the 2015 financial plans submitted to the MOF, revenue does not fall below, and expenditure does not exceed, the published projections on a ministry basis (MOF website).

The implementation of PB in the Maltese public administration may provide a useful tool to link government spending in various sectors with the targeted results and outcomes. In a

situation where government is committed to control the fiscal deficit and reduce the debt burden, PB potentially assists in making budgetary decisions on the basis of programme goals and measured results, as opposed to basing the following year’s financial projections on the previous year’s budgetary allocations or making budgetary cuts across the board without taking into consideration their impact on programme goals and performance (as is the practice in the local scenario where a line-item budgeting system is in operation).

#### 4.5.2 Budget documents

The most recent annual budget was presented by the MOF during October 2015 and related to budget allocations for 2016. The budget documents published as part of the 2016 Budget are described in the following table:

**Table 22: 2016 Budget Documents**

2016 Budget Documents	
Document	Contents
Budget Speech 2016	Sets out the speech delivered by the Minister for Finance when presenting the budget to the public (MOF, 2015b).
Budget Document 2016	Provides a macroeconomic review and outlook, together with a fiscal review and outlook; and highlights the main budget 2016 measures (MOF, 2015a).
Financial Estimates 2016	Incorporate three-year revenue and expenditure projections for 2016 - 2018, at line ministry level, as well as budget allocations for 2016 for each ministry, on a line-item basis, covering both recurrent and capital expenditures (MOF, 2015d).
Economic Survey 2015	Sets out details about the economic and financial situation in Malta (MOF, 2015c).
Budget 2015 Implementation	Published for the first time in 2014, the aim of this document is to report on the implementation of the previous year’s budget measures (Office of the Prime Minister, 2015). Each 2015 budget measure is listed in the report under the ministry which is responsible for its implementation and is then analysed on a quarterly basis in respect of its implementation status.

## 4.6 Fiscal responsibility

On 8 August 2014, by virtue of Act XXVII of 2014, the Maltese government enacted a Fiscal Responsibility Act (referred to below as ‘the Act’), with the aim of ensuring sustainable public finances and enhancing accountability and transparency in the conduct of its financial undertakings. In this respect, the Minister for Finance stated that “*this law will provide deeper control on government spending, increase efficiency, monitor expenditure ceilings and give taxpayers the comfort that the government and entities must control their expenditure*” (Malta Today, 2014). In line with EU requirements, the Act establishes fiscal rules, an independent fiscal council, a medium-term budgetary framework, a fiscal risk statement and a contingency reserve (International Monetary Fund, 2014). The enactment of this Act fulfils the requirements of Directive 85/2011/EU on budgetary frameworks.

The Fiscal Responsibility Act lays down the principles of fiscal responsibility, as detailed in the following table:

**Table 23: Principles of fiscal responsibility**

Principles of fiscal responsibility	
Principles	Explanation
Principle of transparency	In carrying out fiscal and budgetary policies, Government is obliged to publish all the necessary information to allow assessment of the implementation of such policies and of the position of central and local finances.
Principle of stability	Government is to carry out its fiscal and budgetary policy in a manner that ensures medium-term predictability and macro-economic stability.
Principle of fiscal responsibility	Government is to carry out its fiscal and budgetary policy and manage budgetary resources in a manner that ensures the sustainability of the fiscal position in the medium and long term. This avoids the need to introduce destabilising expenditure or revenue adjustments, in order to manage unforeseen events in future periods.
Principle of equity	In conducting its budgetary and fiscal policies, Government shall consider the financial impact on current and future generations, as well as the impact on medium and long term economic development.
Principle of efficiency	Government's fiscal and budgetary policies should be aimed at achieving an efficient use of scarce public resources.
Effective management of personnel spending	Public sector employment and pay policies shall be consistent with the fiscal and budgetary targets contained in the fiscal strategy.
Principle of effective financial and asset management	Government is to implement its fiscal and budgetary policies in accordance with the best practices for effective financial and asset management.

Source: *Fiscal Responsibility Act, 2014: s.3*

Some of the salient provisions of this Act, which are pertinent to the budgetary process, are highlighted below.

#### 4.6.1 Fiscal rules

The budgetary rule is that for each year either the budget condition or the adjustment path condition is satisfied. The budget condition is that either the budgetary position of the general government is in balance or in surplus; or if this is not met, fiscal sustainability is not jeopardised in the medium term and the reason for not meeting such requirement is the result of exceptional circumstances. The adjustment path condition is that either the annual structural balance of the general government is converging towards the medium term budgetary objective; or if this is not met, fiscal sustainability is not endangered in the medium



term and the reason for not meeting such requirement is the result of exceptional circumstances (Fiscal Responsibility Act, 2014: s.8).

As regards the ratio of general government debt to GDP, the target ratio is of 60%; if this ratio exceeds 60%, it must be reduced (Fiscal Responsibility Act, 2014: s.9).

If the EU addresses a warning to Malta under Article 6(2) of the Council Regulation (EC) No. 1466/97 (in view of significant divergence of the budgetary position from the medium term budgetary objective or the adjustment path towards it) or if the government considers that the budgetary rule was not adhered to, the government shall lay a plan of what has to be done to secure compliance with the budgetary rule, before the House of Representatives (Fiscal Responsibility Act, 2014: s.11).

#### **4.6.2 Budgetary process**

##### ***Business and financial plans***

Every ministry, department and entity which is in receipt of a government subvention is required to prepare a three-year rolling business and financial plan, as prescribed, from time to time, by the Minister for Finance. The business and financial plans have to be submitted to the MOF and they are to be based on the most recently announced Medium Term Fiscal Strategy (Fiscal Responsibility Act, 2014: s.14).

##### ***Medium term fiscal strategy***

In every financial year, the government shall present to the House of Representatives, the Medium Term Fiscal Policy Statement and the Fiscal Policy Strategy. These documents will comprise government's fiscal objectives, strategic priorities and a three-year rolling target for fiscal management. Amongst a number of items specified in the Act, the macroeconomic

framework underlying the Medium Term Fiscal Policy Statement will contain information on the macroeconomic situation and forecasts for the current budget year and at least the next three financial years and actual out-turns for the two previous budget years. The Medium Term Fiscal Policy Strategy will set out an aggregated level of the government's spending plans for the forthcoming budget year, the three subsequent years, estimated actual results for the current year and actual results for the two previous years. The macroeconomic and fiscal forecasts have to be endorsed by the Fiscal Council and made public (Fiscal Responsibility Act, 2014: s15).

#### ***Annual draft budget***

The MOF will compile a Draft Budgetary Plan for the forthcoming year, based on the Medium Term Fiscal Plan projections. The Draft Budgetary Plan will be submitted to the Fiscal Council for endorsement and will thereafter be made public. It will also be submitted by the Minister for Finance to Cabinet, where deliberations will be made which shall constitute the basis for the presentation of the budget (Fiscal Responsibility Act, 2014: s16).

#### ***Annual budget***

An annual budget, which is consistent with the fiscal responsibility principles, the fiscal rules, the fiscal strategy and any other requirements in the Act, shall be presented by government to the House of Representatives. Allocations of budget funding to a ministry or sector can only be made through the annual budget process (Fiscal Responsibility Act, 2014: s17).

In the presentation of the annual budget, the MOF is required to publish a detailed annual programme for revenue collection, including quarterly targets for revenue collection in respect of each revenue source, quarterly targets for recovering revenue arrears and planned measures to combat tax evasion and tax fraud (Fiscal Responsibility Act, 2014: s29).

The submission to the MOF of programme initiatives which involve new or increased public expenditure have to be accompanied by a detailed description of the proposed project, its objectives and likely outcomes, together with a detailed financial statement including underlying assumptions. Unless expressly approved by the Minister for Finance, in the course of the budget year, no new or additional expenditures can be made or committed to in excess of the relevant budgetary allocation (Fiscal Responsibility Act, 2014: s.18).

### ***Monitoring of budget execution***

In the course of the budget execution, the MOF shall monitor and evaluate regularly the implementation of the approved budget. The MOF will publish monthly schedules of revenues and expenditures, desegregated by source and economic function. The ministries, departments and government entities are responsible for keeping proper books of accounts, they are to follow accounting policies and methodologies as prescribed by the MOF, and they have to ensure the reliability and timeliness in reporting financial data to the MOF, the Treasury and the National Statistics Office (Fiscal Responsibility Act, 2014: s.39).

In July of each year, the Minister for Finance will present to the House of Representatives a half-yearly report on the economic and budgetary situation (Fiscal Responsibility Act, 2014: s.39).

### ***Government annual report***

By the end of June of each year, the Minister for Finance is required to compile and make public an annual report on the previous fiscal year. The annual report will provide information on the execution of the previous budget, comparing its outcome with the strategic objectives in the fiscal strategy and the fiscal targets announced in the previous annual budget (Fiscal Responsibility Act, 2014: s.41).

### **4.6.3 Fiscal Council**

The Fiscal Council is responsible for examining government's decisions and endorsing every report required in accordance with the Fiscal Responsibility Act. Amongst its numerous obligations, the Fiscal Council will “*endorse, as it considers appropriate, the macroeconomic and fiscal forecasts prepared by the Ministry for Finance and provide an assessment of the official forecasts; ... assess the Government's budgetary performance against the fiscal targets and policies specified in the fiscal strategy ....; analyse and issue an opinion and any recommendations pursuant to the Government's publication of the half-yearly and the annual report on the execution of the budget*” (Fiscal Responsibility Act, 2014: s.13 (3)).

The Fiscal Council will be composed of three members and may appoint persons to be members of the staff of the Fiscal Council. The Fiscal Council is required to prepare a report of its activities after the end of each year (Fiscal Responsibility Act, 2014: s.47,52,58).

The Chairperson of the Fiscal Council shall give evidence in relation to matters affecting the Fiscal Council and its operations, to the Public Accounts Committee, when requested to do so by the Chairperson of the Public Accounts Committee (Fiscal Responsibility Act, 2014: s.57).

## **4.7 Public expenditure in the Education and Health sectors**

To obtain the viewpoint of the line ministries for the purpose of this study, focus is being placed upon the education and health sectors, which constitute two very significant elements of government spending within the Maltese budgetary framework. Education and health are the two largest spenders in the Maltese economy – the investment in education is of extreme importance because Malta does not have any natural resources and its economy growth is

largely dependent on the quality and skills of its human resources, whilst health spending is continuously growing in view of Malta's ageing population.

The following table sets out an analysis of capital expenditure within the public sector, by Ministry. The figures shown represent the actual expenditure for 2014, the revised estimated expenditure for 2015 and the budgetary estimate for 2016.

**Table 24: Capital Expenditure by Ministry, 2014 to 2016**

Capital expenditure	Actual	Revised	Estimate	2014	2015	2016
	Expenditure	Estimate				
	2014	2015	2016	2014	2015	2016
	€'000	€'000	€'000	%	%	%
Office of the President	188	122	217	0.00	0.0%	0.1%
Office of the Prime Minister	12,412	15,646	10,945	2.8%	2.9%	2.8%
Ministry for European Affairs & Implementation of the Electoral Manifesto	23,481	39,634	70,551	0.05	7.3%	18.0%
Ministry for Foreign Affairs	1,291	3,276	1,582	0.3%	0.6%	0.4%
Ministry for Tourism	17,797	1,656	6,707	4.0%	0.3%	1.7%
<b>Ministry for Education and Employment</b>	<b>68,283</b>	<b>61,640</b>	<b>33,051</b>	<b>15.2%</b>	<b>11.3%</b>	<b>8.4%</b>
Ministry for Sustainable Development, the Environment and Climate Change	47,046	78,732	40,722	10.5%	14.4%	10.4%
Ministry for Transport and Infrastructure	83,921	87,351	75,335	18.7%	16.0%	19.3%
Ministry for Gozo	9,552	15,308	6,364	2.1%	2.8%	1.6%
Ministry for Social Dialogue, Consumer Affairs and Civil Liberties	2,326	2,451	1,671	0.01	0.4%	0.4%
Ministry for the Economy, Investment and Small Business	46,839	46,377	32,579	10.4%	8.5%	8.3%
Ministry for the Family and Social Solidarity	4,689	5,868	5,358	1.0%	1.1%	1.4%
Ministry for Justice, Culture and Local Government	-	17,806	10,162	-	0.03	2.6%
Ministry for Home Affairs and National Security	11,933	23,252	23,540	2.7%	4.3%	6.0%
Ministry for Finance	53,221	65,833	44,392	11.9%	12.1%	11.3%
Ministry for Energy and the Conservation of Water	24,931	-	-	5.6%	0.0%	-
Ministry for Health	<b>41,192</b>	-	-	<b>9.2%</b>	<b>0.0%</b>	<b>-</b>
<b>Ministry for Energy and Health</b>	<b>-</b>	<b>80,241</b>	<b>28,164</b>	<b>-</b>	<b>14.7%</b>	<b>7.2%</b>
	449,104	545,193	391,340	100.0%	100.0%	100.0%

*Source:* Ministry for Finance, Financial Estimates 2016. [<https://mfjn.gov.mt/en/The-Budget>]

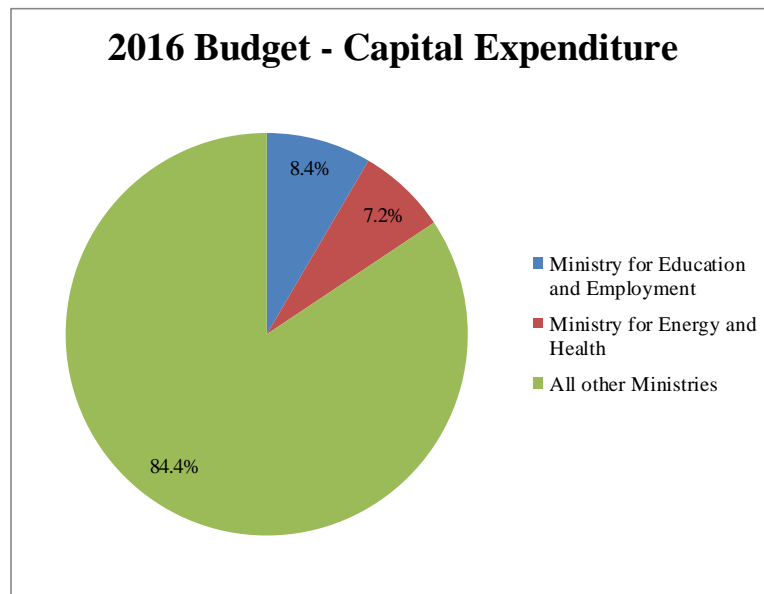
*Note 1:* The Ministry for Health has recently been amalgamated with the Ministry for Energy and the Conservation of Water, becoming the Ministry for Energy and Health.

*Note 2:* The reduction in estimated capital expenditure between 2015 and 2016 is mainly a result of lower EU fund allocations.

The above analysis shows that the estimated capital expenditure in the education sector for 2016 represents circa 8.4% of total estimated public capital expenditure (15.2% in 2014 and 11.3% in 2015). In the health (and energy) sector, the estimated capital expenditure in 2016

comprises circa 7.2% of total estimated capital expenditure (Health: 9.2% in 2014 and Health and energy: 14.7% in 2015). (Refer to figure below).

**Figure 20: Budgeted Capital Expenditure for 2016**



*Source: Analysis based on Information from Ministry for Finance, Financial Estimates 2016.  
[<https://mfin.gov.mt/en/The-Budget>]*

An analysis of public sector recurrent expenditure, by Ministry, is set out in the table below. The figures show the actual recurrent expenditure for 2014, the revised estimated expenditure for 2015, the budgetary estimate for 2016 and projections for 2017 and 2018.

**Table 25: Recurrent Expenditure by Ministry, 2014 to 2018**

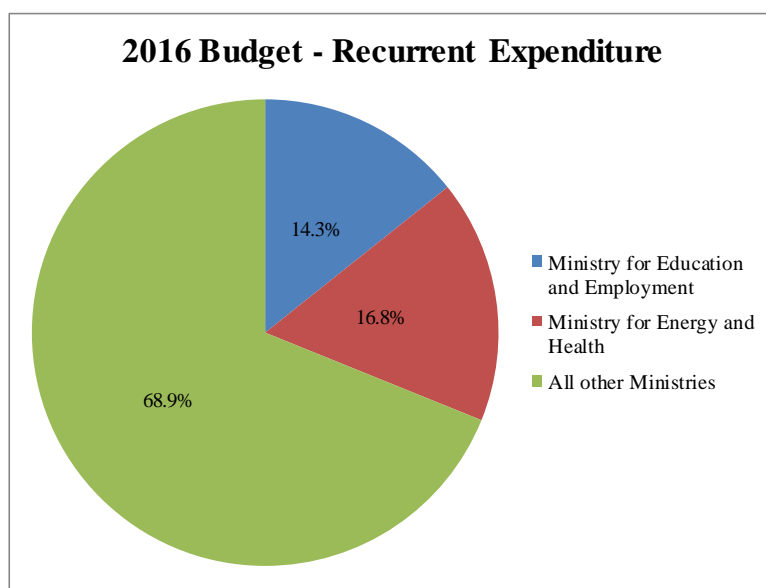
Recurrent expenditure	Actual	Revised		Projections						
	Expenditure	Estimate	Estimate	Projections	Projections	2014	2015	2016	2017	2018
	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018
	€'000	€'000	€'000	€'000	€'000	%	%	%	%	%
Office of the President	3,388	3,880	3,868	4,008	4,115	0.1%	0.1%	0.1%	0.1%	0.1%
Office of the Prime Minister	47,861	49,893	38,040	36,090	41,639	1.7%	1.6%	1.2%	1.1%	1.2%
Ministry for European Affairs & Implementation of the Electoral Manifesto	10,575	12,946	32,867	32,978	13,209	0.00	0.4%	1.0%	1.0%	0.4%
Ministry for Foreign Affairs	22,699	25,966	30,326	31,687	33,032	0.8%	0.8%	0.9%	1.0%	1.0%
Ministry for Tourism	66,068	48,738	50,791	51,843	52,915	2.3%	1.6%	1.6%	1.6%	1.5%
<b>Ministry for Education and Employment</b>	<b>400,655</b>	<b>428,243</b>	<b>458,423</b>	<b>477,908</b>	<b>496,991</b>	<b>14.0%</b>	<b>14.0%</b>	<b>14.3%</b>	<b>14.4%</b>	<b>14.5%</b>
Ministry for Sustainable Development, the Environment and Climate Change	47,214	50,255	66,303	59,074	60,990	1.7%	1.6%	2.1%	1.8%	1.8%
Ministry for Transport and Infrastructure	90,604	87,826	95,149	96,164	97,714	3.2%	2.9%	3.0%	2.9%	2.9%
Ministry for Gozo	27,186	27,892	29,759	30,295	30,901	1.0%	0.9%	0.9%	0.9%	0.9%
Ministry for Social Dialogue, Consumer Affairs and Civil Liberties	10,943	14,855	13,462	13,747	13,991	0.4%	0.5%	0.4%	0.4%	0.4%
Ministry for the Economy, Investment and Small Business	33,420	39,061	36,449	35,584	35,561	1.2%	1.3%	1.1%	1.1%	1.0%
Ministry for the Family and Social Solidarity	1,217,211	1,274,105	1,317,699	1,369,912	1,428,786	42.6%	41.7%	41.0%	41.4%	41.8%
Ministry for Justice, Culture and Local Government	50,092	79,844	92,148	93,960	96,504	1.8%	2.6%	2.9%	2.8%	2.8%
Ministry for Home Affairs and National Security	142,087	138,436	139,502	140,860	143,146	5.0%	4.5%	4.3%	4.3%	4.2%
Ministry for Finance	218,628	258,767	251,550	256,334	264,493	7.7%	8.5%	7.8%	7.7%	7.7%
<b>Ministry for Energy and Health</b>	<b>460,887</b>	<b>508,600</b>	<b>540,643</b>	<b>567,222</b>	<b>593,760</b>	<b>16.1%</b>	<b>16.6%</b>	<b>16.8%</b>	<b>17.1%</b>	<b>17.4%</b>
House of Representatives, Office of the Ombudsman, NAO	7,533	9,211	13,119	13,392	13,651	0.3%	0.3%	0.4%	0.4%	0.4%
	2,857,050	3,058,518	3,210,098	3,311,058	3,421,398	100.0%	100.0%	100.0%	100.0%	100.0%

*Source:* Ministry for Finance, *Financial Estimates 2016*. [<https://mfim.gov.mt/en/The-Budget>]

*Note 1:* The Ministry for Health has recently been amalgamated with the Ministry for Energy and the Conservation of Water, becoming the Ministry for Energy and Health.

*Note 2:* The expenditure within the Ministry for the Family and Social Solidarity includes social security benefits. These make up around 90% of total expenditure within this Ministry during the period under consideration.

The estimated 2016 recurrent expenditure in the education sector makes up 14.3% of the total estimated public recurrent expenditure (14.0% for both 2014 and 2015). The proportion of total recurrent expenditure voted for the education sector for 2017 and 2018 is expected to remain approximately at the 2016 level (14.4% in 2017 and 14.5% in 2018). In the health sector, the estimated recurrent expenditure for 2016 represents 16.8% of total recurrent expenditure (16.1% in 2014 and 16.6% in 2015). Going forward, it is projected that the proportion of total recurrent expenditure allocated to the health sector for 2017 and 2018 will be of 17.1% and 17.4% respectively. The figure below shows the significance of the 2016 budgeted recurrent expenditure in education and health.

**Figure 21: Budgeted Recurrent Expenditure for 2016**

*Source: Analysis based on Information from Ministry for Finance, Financial Estimates 2016.  
[<https://mfin.gov.mt/en/The-Budget>]*

The recurrent expenditure table illustrated above shows that the largest portion of recurrent expenditure relates to the Ministry for the Family and Social Solidarity (41.0% of total recurrent expenditure in 2016). These expenditure figures comprise government spending on social security, which represents around 36% of total estimated recurrent expenditure in 2016. If spending on social security is excluded from total recurrent expenditure (refer to table and figure below), estimated recurrent expenditure on education and health in 2016 make up 22.5% and 26.5% of total recurrent expenditure respectively. These figures indicate that these two sectors are highly significant within the Maltese public administration.

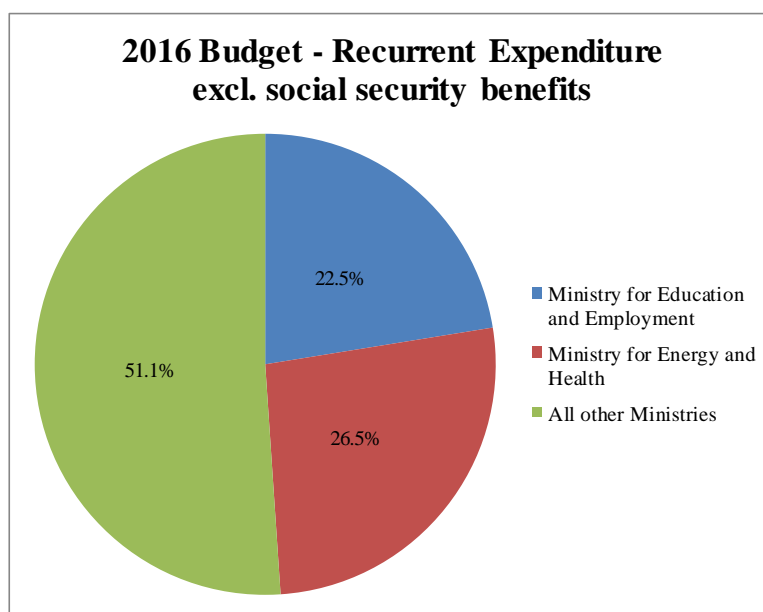


**Table 26: Recurrent Expenditure excluding social security benefits, 2014 to 2018**

Recurrent expenditure - excluding social security benefits from the Ministry for the Family and Social Solidarity	Actual Expenditure	Revised Estimate	Estimate	Projections	Projections					
	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018
	€'000	€'000	€'000	€'000	€'000	%	%	%	%	%
Office of the President	3,388	3,880	3,868	4,008	4,115	0.2%	0.2%	0.2%	0.2%	0.2%
Office of the Prime Minister	47,861	49,893	38,040	36,090	41,639	2.7%	2.6%	1.9%	1.7%	1.9%
Ministry for European Affairs & Implementation of the Electoral Manifesto	10,575	12,946	32,867	32,978	13,209	0.6%	0.7%	1.6%	1.6%	0.6%
Ministry for Foreign Affairs	22,699	25,966	30,326	31,687	33,032	1.3%	1.3%	1.5%	1.5%	1.5%
Ministry for Tourism	66,068	48,738	50,791	51,843	52,915	3.7%	2.5%	2.5%	2.5%	2.5%
<b>Ministry for Education and Employment</b>	<b>400,655</b>	<b>428,243</b>	<b>458,423</b>	<b>477,908</b>	<b>496,991</b>	<b>22.7%</b>	<b>22.2%</b>	<b>22.5%</b>	<b>22.8%</b>	<b>23.1%</b>
Ministry for Sustainable Development, the Environment and Climate Change	47,214	50,255	66,303	59,074	60,990	2.7%	2.6%	3.2%	2.8%	2.8%
Ministry for Transport and Infrastructure	90,604	87,826	95,149	96,164	97,714	5.1%	4.5%	4.7%	4.6%	4.5%
Ministry for Gozo	27,186	27,892	29,759	30,295	30,901	1.5%	1.4%	1.5%	1.4%	1.4%
Ministry for Social Dialogue, Consumer Affairs and Civil Liberties	10,943	14,855	13,462	13,747	13,991	0.6%	0.8%	0.7%	0.7%	0.6%
Ministry for the Economy, Investment and Small Business	33,420	39,061	36,449	35,584	35,561	1.9%	2.0%	1.8%	1.7%	1.7%
Ministry for the Family and Social Solidarity	125,224	147,478	149,174	155,085	161,750	7.1%	7.6%	7.3%	7.4%	7.5%
Ministry for Justice, Culture and Local Government	50,092	79,844	92,148	93,960	96,504	2.8%	4.1%	4.5%	4.5%	4.5%
Ministry for Home Affairs and National Security	142,087	138,436	139,502	140,860	143,146	8.0%	7.2%	6.8%	6.7%	6.6%
Ministry for Finance	218,628	258,767	251,550	256,334	264,493	12.4%	13.4%	12.3%	12.2%	12.3%
<b>Ministry for Energy and Health</b>	<b>460,887</b>	<b>508,600</b>	<b>540,643</b>	<b>567,222</b>	<b>593,760</b>	<b>26.1%</b>	<b>26.3%</b>	<b>26.5%</b>	<b>27.1%</b>	<b>27.6%</b>
House of Representatives, Office of the Ombudsman, NAO	7,533	9,211	13,119	13,392	13,651	0.4%	0.5%	0.6%	0.6%	0.6%
	1,765,062	1,931,891	2,041,573	2,096,231	2,154,362	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Ministry for Finance, Financial Estimates 2016. [<https://mfjn.gov.mt/en/The-Budget>]

Note: Social security benefits amounting to €1,091,988k, €1,126,627k, €1,168,525k, €1,214,827k and €1,267,036k during 2014, 2015, 2016, 2017 and 2018 respectively, have been excluded from this analysis.

**Figure 22: Budgeted Recurrent Expenditure excluding social security benefits for 2016**

Source: Analysis based on Information from Ministry for Finance, Financial Estimates 2016.

[<https://mfjn.gov.mt/en/The-Budget>]

### *Line-item budgeting – Citing Education and Health*

As mentioned above, the existing budgetary system is based on line-item budgeting which presents estimated expenditures by inputs or resources purchased. Two budgets are presented for every ministry, one setting out estimated recurrent expenditures and the other incorporating estimated capital expenditures.

The following table displays extracts from the 2016 budgetary estimates (recurrent and capital) for the education and health sectors, analysed by line-item expenditure.

**Table 27: 2016 Budgetary estimates – Education and Health**

Ministry for Energy and Health - RECURRENT	Estimate	Ministry for Education and Employment - RECURRENT	Estimate
	<b>2016</b>		<b>2016</b>
	<b>€'000</b>		<b>€'000</b>
<b>Ministry for Energy and Health (Vote 31)</b>		<b>Ministry for Education and Employment (Vote 13)</b>	
Personal Emoluments	3,134	Personal Emoluments	4,243
Operational and Maintenance Expenses	775	Operational and Maintenance Expenses	1,864
Programmes and Initiatives	40,695	Programmes and Initiatives	114,797
Contribution to Government Entities	29,150	Contribution to Government Entities	121,460
<i>Total Vote</i>	73,754	<i>Total Vote</i>	242,364
<b>Health (Vote 32)</b>		<b>Education (Vote 14)</b>	
Personal Emoluments	235,892	Personal Emoluments	196,080
Operational and Maintenance Expenses	57,788	Operational and Maintenance Expenses	16,973
Programmes and Initiatives	125,322	Programmes and Initiatives	3,006
Contribution to Government Entities	47,887	Contribution to Government Entities	-
<i>Total Vote</i>	466,889	<i>Total Vote</i>	216,059
<b>Total Recurrent Expenditure - Ministry for Energy and Health</b>	<b>540,643</b>	<b>Total Recurrent Expenditure - Ministry for Education and Employment</b>	<b>458,423</b>

Source: Ministry for Finance, Financial Estimates 2016. [<https://mfin.gov.mt>]

Source: Ministry for Finance, Financial Estimates 2016. [<https://mfin.gov.mt>]

Ministry for Energy and Health - CAPITAL	Estimate	Ministry for Education and Employment - CAPITAL	Estimate
	<b>2016</b>		<b>2016</b>
	<b>€'000</b>		<b>€'000</b>
<b>Ministry for Energy and Health (Vote XII)</b>		<b>Ministry for Education and Employment (Vote V)</b>	
ICT	3,826	ICT	1,200
EU Structural Funds 2007-2013 Malta funds	2,350	e-Learning	900
EU Cohesion Funds 2007-2013 Malta funds	3,000	EU Structural Funds 2007-2013 Malta funds	5,700
Intelligent Energy Europe	53	EU Structural Funds 2014-2020 EU funds	1,040
Directly Managed Funds	20	EU Structural Funds 2014-2020 Malta funds	260
EEA/Norwegian Financial Mechanisms 2009-2014	1,768	Improvements to buildings	30
7th Framework Programme - EU funds	119	University of Malta and Junior College	7,000
Improvements to property & Regeneration works	2,350	Malta College of Arts, Science and Technology	400
Drainage - Gozo	200	Examinations Department	5
Integrated Health Information System	5,000	Foundation for Tomorrow's Schools - Capital Program	10,431
Pharmacy of Your Choice	60	Malta Council for Science and Technology	1,000
Infectious Disease Units	200	Malta Libraries	50
Permanent Secretary's Office - refurbishment	10	National Archives	120
Central Procurement & Supplies Unit	500	Sport	2,870
		<b>Total Vote</b>	<b>31,006</b>
<i>Institutional Health Care - Malta</i>		<b>Education (Vote V)</b>	
Mater Dei Hospital - works and equipment	3,300	Equipment for Government Schools - Malta	400
Equipment at Mater Dei Hospital re ERDF 314	1,600	IT in Government Schools - Malta	1,470
Mount Carmel Hospital - upgrading works	300	Equipment for Education Support Services - Malta	25
National Blood Transfusion Centre	200	Equipment for Government Schools - Gozo	50
Oncology Hospital	2,718	Construction and maintenance works in schools - Gozo	100
		<b>Total Vote</b>	<b>2,045</b>
<i>Primary Health Care</i>		<b>Total Capital Expenditure - Ministry for Education and Employment</b>	<b>33,051</b>
Improvements at Health Care Centres	500		
Public Health	80		
Public Health Regulation	10		
<b>Total Capital Expenditure - Ministry for Energy and Health</b>	<b>28,164</b>		

Source: Ministry for Finance, Financial Estimates 2016. [<https://mfim.gov.mt>]

Source: Ministry for Finance, Financial Estimates 2016. [<https://mfim.gov.mt>]

As clearly illustrated in the above table, the budgetary estimates presented by the Maltese government do not include any pre-established targets, performance information or output or outcome expectations, but are solely based on expected input consumption. The main objective for each individual ministry is to operate within the expenditure limit set in the budget, rather than to achieve some pre-determined results, outputs or outcomes.

This section has demonstrated the significance of the budgetary allocations directed towards the education and health sectors, seeking to justify why representatives from these two sectors were targeted for the empirical data collection.

**CHAPTER 5:  
RESEARCH  
METHODOLOGY**

## 5.1 Introduction

This chapter explains the research methodology adopted for the purpose of achieving the objectives of the study. The next section refers to the initial contacts made for the purpose of the research. Section 5.3 then presents the data collection methods selected, whilst section 5.4 looks into the research instrument used. This is followed by section 5.5, which focuses on the research participants selected for the study. The analytical approach used is then explained in section 5.6. Subsequently, section 5.7 discusses the limitations encountered and section 5.8 concludes the chapter.

The methodology was specifically designed for addressing the research objectives<sup>9</sup> underpinning the study. Data was gathered using documentary sources and interviews. Documentary sources provided the background information necessary for obtaining an in-depth understanding of the topic under consideration. Documentary research was fundamental for ascertaining the economic environment prevailing in Malta and the country's existing budgetary framework, in support of the first and second research objectives, which involve gaining an understanding of why budgetary reforms might be implemented in Malta and identifying the recent reforms in the budgetary framework. To address the first and second objectives, the collection of empirical evidence from interviews complemented the documentary research. Interviews were also used to tackle the third and fourth objectives, namely, assessing the implications of including PI in budget documents and of holding public officials responsible for their performance, and suggesting a suitable implementation approach for PB.

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<sup>9</sup> Vide section 1.6

## 5.2 Making initial contacts

Prior to embarking on the study, a meeting was held with an economist and academic (in February 2012) for the purpose of discussing the feasibility of the topic selected and the need for the study in the Maltese context. In preparation for this meeting, an initial literature review was carried out and a short document, setting out an overview of the topic proposed, was compiled.

Subsequently, a meeting was held with the supervisors during October 2012 in order to discuss the research proposal. This discussion led to the narrowing down of the focus of the research topic to specific research objectives.

In April 2013, a month after the general election and the change in government, an email was sent to the newly elected Prime Minister, in order to inform him of the study being carried out and to ask his opinion as to whether the research project would be useful and beneficial for Malta. A very positive reply was received, encouraging the conduct of the research and proposing a meeting at the OPM to further discuss the study.

This was followed by a meeting with the Principal Permanent Secretary within the OPM, held during May 2013. During this meeting, a presentation was delivered giving background information on the topic being studied and highlighting the main objectives of the research. The Principal Permanent Secretary's response was very positive, and he promised his support for the study, if needed.

Another preliminary meeting was held with the Permanent Secretary within the MOF during July 2013, with the purpose of obtaining an understanding of the current budgetary system and the main players involved in the budget process. Following this meeting, an initial list of

the potential interviewees was compiled. The possibility of subsequently modifying this list was envisaged, since it was expected that during the conduct of the interviews, respondents would suggest other potential participants.

For the purpose of conducting the interviews, it was considered important to target senior politicians, being policy makers, as well as senior civil servants who influence the policy makers and are responsible for implementing policies. These interviewees can be termed an ‘elite population’, in view of their closeness to power and policy making (Lilleker, 2003). Policy implementation is being addressed in the first and fourth research objectives<sup>10</sup>.

### 5.3 Data collection

A detailed analysis of the topic under study was made possible by gathering data from both secondary and primary sources, as explained in sub-sections 5.3.1 and 5.3.2.

The research follows a qualitative approach, using data gathered from documentary sources (secondary data), corroborated with empirical evidence collected from in-depth, semi-structured interviews (primary data). The triangulation of documentary sources against oral sources provides a more reliable account of an event or situation (Gidley, 2004), since the use of multiple independent sources of data collection provides corroborative evidence for the research findings (Saunders et al, 2009). Furthermore, “*all methods have inherent biases and limitations, so use of only one method to assess a given phenomenon will inevitably yield biased and limited results*” (Greene et al, 1989: 256). Qualitative research attempts to understand the behaviour, viewpoints and interactions of the subjects involved in the study (Flick, 2009). Spicer (2004) mentions that qualitative methods can capture complexity,

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<sup>10</sup> Vide section 1.6

diversity and contradiction in the social and human world. The qualitative approach is embedded in an ‘interpretivist’ research philosophy, since it seeks to delve into how the social context is understood, experienced and interpreted (Mason, 2002).

### 5.3.1 Collection of secondary data

The review of existing literature was considered necessary for obtaining a detailed understanding of the subject matter being tackled and for guiding the compilation of the contents of the research instrument used to gather primary data. Furthermore, secondary data collection facilitated the formulation of the theoretical framework underpinning the study.

As mentioned above, secondary data was mainly obtained from documentary sources, as detailed in the table below:

**Table 28: Documentary sources used for research**

Documentary source	Purpose
Academic and professional journals; research papers and books	To gain in-depth knowledge of the current thinking and theoretical underpinnings of the subject being researched
EU law: Treaty on European Union (Maastricht Treaty)	To review fiscal deficit and debt provisions
Publications and reports by international organisations (e.g. OECD, World Bank and EU) and by the Big 4 accounting firms	To identify budgetary reform experiences across a number of countries
Websites of foreign governments (including Australia, Canada, US and UK)	To obtain documents containing performance budgets and reports of the respective government
Maltese government website	<ul style="list-style-type: none"> <li>- To gather information on the structure and functions of the Finance Ministry, in particular the Budget Office</li> <li>- To obtain circulars issued by the Finance Ministry regarding financial plans and the budget process</li> <li>- To download the latest budget documents and financial estimates</li> </ul>
Maltese law	To obtain an understanding of the relevant legal provisions
Central Bank of Malta and National Statistics Office websites	To obtain historical financial and statistical data for the purpose of identifying trends in government’s fiscal deficit and debt position
Newspaper articles	To gather information on the Maltese economic and fiscal climate, as reported by major credit rating agencies (Standard & Poor’s, Fitch Ratings and Moody’s)



Webb et al (1984) mention that an advantage in using documentary data is its ‘non-reactivity’, which means that the researcher is not in a position to bias records and subjects. Another benefit is that the researcher can collect the data without being present during the data collection process (Appleton and Cowley, 1997). Furthermore, Gidley (2004) claims that documentary sources may be the only means to access the data relating to the research question.

Despite the strengths of documentary sources, there are limits to the usability of data collected by someone else, because the researcher’s background would differ from that of the fieldworker who interprets the data on the basis of first-hand experience, as pointed out by Hammersley (1997). In addition, Denscombe (1998) notes that when relying on documentary sources, researchers use data which has been manufactured for purposes other than the aims of their study. Furthermore, the researcher can be biased in choosing particular documents (Denscombe, 1998). These weaknesses highlight the importance of complementing the documentary data with the collection of empirical evidence specifically tailored to addressing the research objectives.

### **5.3.2 Collection of primary data**

Primary data was gathered using semi-structured in-depth interviews, carried out on a face-to-face basis. The use of interviews facilitated the collection of data that was relevant to the research objectives. In this respect, a list of themes and questions supporting the research objectives and taking into account the literature and theory reviewed, was developed for use during the interviews. Qualitative interviews were considered appropriate for the research in order to seek to understand the reasons underlying the participants’ opinions and attitudes (Saunders et al, 2009). The interviews were conducted as a set of open-ended questions,

providing the participants with the opportunity to discuss the subject matter according to their knowledge and interests.

Interviews were carried out with twenty-eight respondents, who were categorised into five groups – senior politicians and economists; MOF representatives; Ministries for Education and Health representatives; stakeholders; and reform promoters. A detailed breakdown of the categories of interviewees is presented in Figure 24 (vide section 5.5.1). The selection of the research participants was made on the basis of their present or past involvement in the annual budgetary process and/or on the basis of their experience in public financial management. As mentioned earlier, an initial list of interview participants was compiled following a preliminary meeting with the MOF Permanent Secretary, which meeting was held to obtain an understanding of the current budgetary process. This list was slightly augmented during the empirical data gathering process, whereby a few initial respondents suggested other potential participants for the research, a technique referred to as ‘snowball sampling’ (Saunders et al, 2009).

Access has been obtained to discuss relevant issues with senior politicians from the government and the opposition, including former ministers and Prime Ministers. In line with the definitions proposed by Lilleker (2003) and Mikecz (2012), the participants represent an ‘elite’ population, since they occupy positions of power and can potentially influence policy making. Lilleker (2003: 207) observed that “*elites can be loosely defined as those with close proximity to power or policy making*”, whilst more recently, Mikecz (2012) referred to an elite population as authority-bearing persons holding positions of power.

## 5.4 Research instrument

This section deals with the research instrument used for gathering empirical evidence, explaining the rationale for the use of semi-structured interviews, outlining the design of the interview schedule and describing how the research instrument was applied.

### 5.4.1 Semi-structured interviews

The research objectives listed in Chapter 1<sup>11</sup> were principally achieved through the conduct of qualitative semi-structured interviews. This technique is appropriate when the study is explanatory in nature and the data gathered is used to test theories (Saunders et al, 2009). Semi-structured, in-depth interviews are also valuable for conducting exploratory research, where the researcher wishes to discover what is happening and to pursue new insights (Robson, 2011).

An interview guide comprising themes and open-ended questions was developed in order to ensure that all the topics relevant to the research objectives would be covered; however the wording and the order of the questions were often modified during the interview, depending on the flow of the conversation (Robson, 2011). Furthermore, through the use of the semi-structured approach, additional unplanned questions were at times asked to follow up on what the respondent said (Robson, 2011), whilst some questions were occasionally omitted (Saunders et al, 2009) if it was felt that the interviewees were either uneasy or lacked knowledge in respect of a particular topic.

As suggested by Saunders et al (2009), the use of semi-structured interviews provides the possibility to ‘probe’ responses, where the researcher wishes that the respondent explains in

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<sup>11</sup> Vide section 1.6

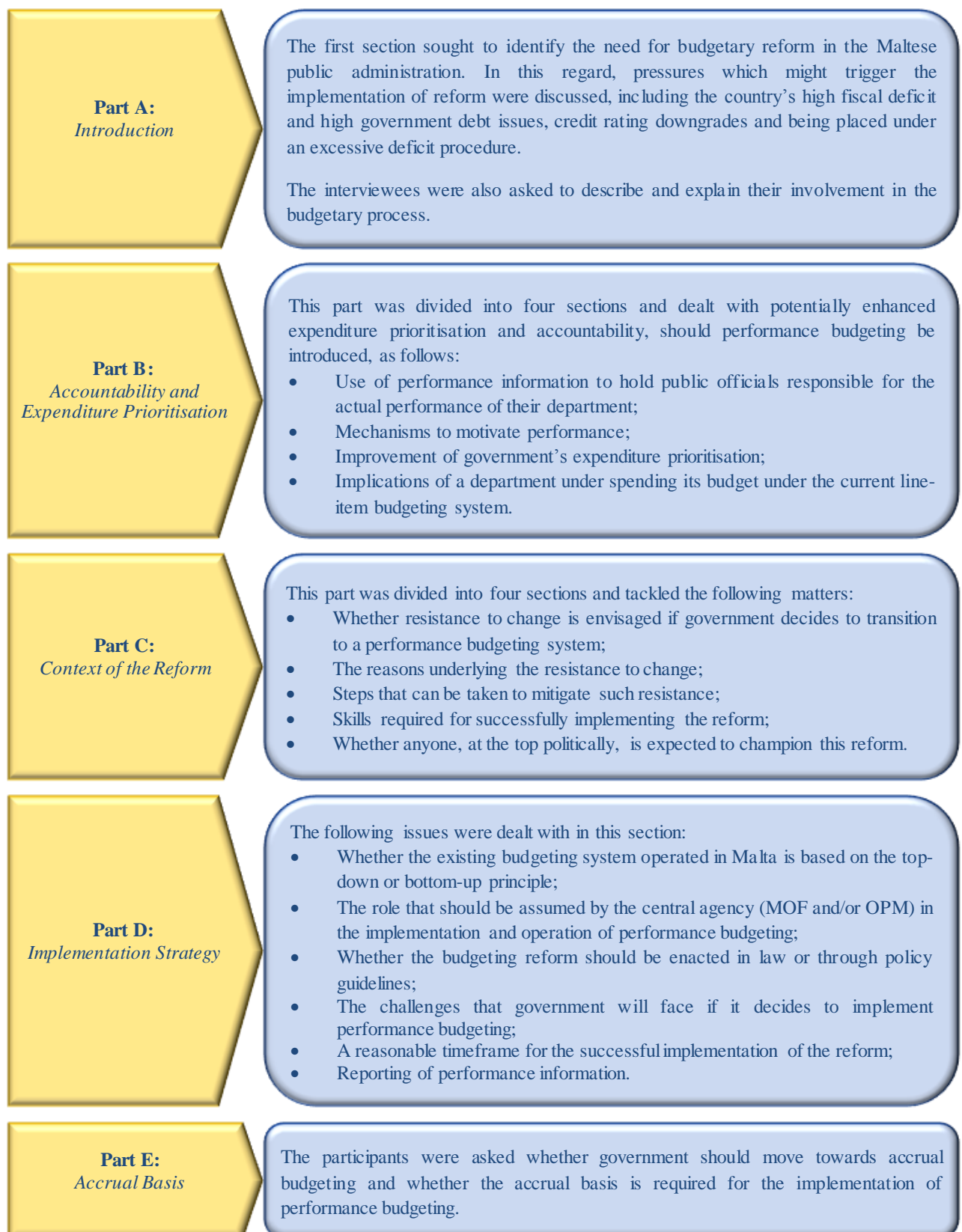
further detail or builds upon his/her answers. For instance, where a particular topic of interest was being discussed and the researcher felt that an example could enrich the interviewee's explanation, the respondent was asked to illustrate his/her point further by citing an example. Through the use of in-depth interviews, the researcher was also provided with the opportunity to discuss areas which had not previously been considered, but which then enhanced the researcher's understanding of relevant issues that were important for tackling the research objectives or for formulating a further objective (Saunders et al, 2009). Indeed, the second research objective, which relates to the identification of reforms in the budgetary framework that occurred since the change in government in March 2013, was formulated as a result of the interviewing process.

In view of the high profile of the research participants selected, the use of personal, face-to-face interviews was considered important for achieving a high response rate (twenty-eight out of thirty people contacted agreed to participate in the study). This is because respondents might feel more comfortable providing confidential information in a face-to-face meeting; they might want to ensure that the information will be used appropriately and solely for the purpose of the research; and given their very busy schedules, they might be reluctant to spend time providing written answers (Saunders et al, 2009). Furthermore, the only possible way to get the undivided attention of a very busy person is to set up a face-to-face meeting for a specific date and time.

#### **5.4.2 Design of the interview schedule**

Following the conduct of the documentary research and the thorough review of the literature and theory underpinning the study, an interview schedule was prepared in line with the

research objectives. This comprised five sections, as summarised in Figure 23 below. The questions formulated were all open-ended.

**Figure 23: Summary of the format and content of the research instrument**

### 5.4.3 Conducting the interviews

The draft interview schedule was thoroughly reviewed by the supervisors, whereby suggestions for improvements were made and some rewording was carried out to ensure that leading questions would be avoided in order to prevent bias.

The first five interviews were deliberately targeted to initially avoid dealing with elite people in current posts. This was considered sensible in order to obtain personal confidence as an interviewer and to ensure that the questions were understandable, clear and unambiguous. Following the first five interviews, a few minor amendments were made to the interview questions. This process also helped to assess the approximate length of time taken to conduct the interview and to identify any questions which the interviewees felt uncomfortable answering or lacked knowledge about. This latter issue helped the researcher to be sensitive when asking these particular questions to the other respondents.

The interviews were held between August 2014 and April 2015, at the offices of the participants. The interviews varied in length from half an hour to two hours. This is because the interviews followed a semi-structured approach and comprised open-ended questions, whereby interviewees were encouraged to talk about a particular topic or issue, depending on their individual expertise and experience.

Mikecz (2012: 482) suggests that *“the success of interviewing elites hinges on the researcher’s knowledgeability of the interviewee’s life history and background”*. Because of the researcher’s knowledge of Malta and of the elites participating in the study, there was no need to carry out detailed research on the background of the respondents before conducting the interviews.

Prior to the interviews, some of the participants were sent a copy of the interview questions. In the case of a few interviewees, namely, the Ministers currently in office, it was considered unwise to send them a copy of the questions in advance, because given their tight time schedules, it was highly probable that they would either not consult the questions prior to the interview or they would opt out of the meeting because they might consider the number of questions to be excessive.

At the start of the interview, the participants were asked to sign and date a prepared consent form. Before commencing, the participants were advised that should they feel uncomfortable answering certain questions, such questions would be skipped. Furthermore, depending on the expertise and experience of the person being interviewed, some questions were delved into more deeply whilst others were tackled more generally.

Permission was asked to voice-record the interviews. This allowed the interviewer to engage more actively with the participants during the interview. Furthermore, the audio recording provided an accurate and full record of the interview which could be referred to later on. All the participants, except one, accepted to be recorded. In the case of the interviewee who asked not to be recorded, manual notes were taken during the interview.

The interviews which were digitally recorded, were then carefully transcribed. The interviews were mainly conducted in English; however, where the Maltese language was used in a few instances, careful translation and, then, transcription was done. Riessman (1993: 56-58) emphasises the importance of taping and transcribing interviews and observes that “...*By transcribing at this level, interpretive categories emerge, ambiguities in language are heard on the tape, and the oral record – the way the story is told – provides clues about meaning.*” Though transcribing is an extremely time-consuming task, the researcher did not delegate the



transcription process, in order to ensure that all key moments in the interview were captured in the transcript and also to ensure the security and anonymity of the interviewees, especially in the case of very senior politicians and civil servants.

Five respondents, including the Prime Minister, the Minister for Finance, the Minister for Education, the Permanent Secretary for Education and the Accountant General, are identifiable in the dissertation findings and analysis. It was considered important to identify these interviewees in view of their influence in policy making. In this respect, a copy of the text in which their position in office appears in the dissertation was sent to them for their review (even though all these respondents had consented to the use of the interview data in the research project and had waived their right to remain anonymous). Another interviewee was selected to remain identifiable in the dissertation, but he insisted that the interview could be used for research but not for publication purposes; thus, reference to his position was removed from the thesis.

## **5.5 Research participants**

As mentioned earlier, the empirical evidence has been collected from interviews conducted with twenty-eight participants, during the period from August 2014 to April 2015. The interviews were held with politicians, senior public officials and economists who are active in the public sector. In addition, two preliminary meetings were organised: one was held with the Principal Permanent Secretary within the OPM during May 2013 and the second one was held with the Permanent Secretary within the MOF during July 2013.

Another two potential participants, a politician and a senior civil servant, were contacted but they did not participate in the study.

### **5.5.1 Profile of participants**

The research participants selected (excluding the two preliminary meetings) were sub-divided into five categories, as detailed in Figure 24: (i) senior politicians (including former Prime Ministers and former Ministers for Finance) and economists, (ii) representatives from the MOF, (iii) representatives from the Education and Health Ministries, (iv) stakeholders which may affect the reform process and (v) potential reform promoters. A detailed description of these categories is set out in the table below.

**Table 29: Categorisation of research participants**

Categories of participants	Commentary
First category included two former Prime Ministers, two former Ministers for Finance, two economists and a former Director General at the Budget Office	<p>During their term in office, both former Prime Ministers had taken the MOF under their responsibility for a period of time, because it was felt at the time that public finances were under considerable strain and had to be overseen by the Prime Minister himself.</p> <p>The two former Ministers for Finance were responsible for the implementation of a number of reforms in the Maltese public financial management scene, including the introduction of the VAT system in Malta, the initiation of the accrual accounting reform and entry into the Eurozone.</p> <p>The two economists have a very high profile in Malta and they are frequently invited to discuss economic, financial and political matters in the local media. They both lead consultancy businesses in the local market. One of these economists is also an academic who lectures at the University of Malta and the second one is an advisor to government.</p> <p>The participants within this category are considered to be very experienced and knowledgeable in matters relating to the Maltese public administration, through their involvement in the country's financial management including the budgetary framework.</p>
Second category consisted of representatives from the MOF	This category included the Minister for Finance, top public officials who are involved in the budgetary process and a Professor of Public Policy who is advising the MOF and who is currently carrying out spending reviews across all the ministries.
Third category comprised representatives from the Education and Health Ministries	<p>Whilst the views of the central agency were obtained through interviews with politicians and senior public officials within the OPM and within the MOF, it was considered important to also take into account the perspectives of the line ministries. This was achieved through discussions with top civil servants and a politician from the Education and Health Ministries. These ministries were chosen because they represent the two largest spenders in the Maltese economy and spending within such ministries is expected to keep growing. The investment in education is of extreme importance because Malta does not have any natural resources and its economy growth is largely dependent on the quality and skills of its human resources; whilst health spending is continuously growing in view of Malta's ageing population.</p>
Fourth category represented stakeholders who may potentially affect the budgetary reform process	This category was made up of representatives from the National Audit Office, the National Statistics Office and the Central Bank of Malta; a public official who was heavily involved in the Comprehensive Spending Review process carried out by the MOF in parallel with the 2015 budget preparation process; and a public official who lectures at the University of Malta in 'Public Sector Performance Measurement'.
Fifth category included the Prime Minister of Malta and the Permanent Secretary within the OPM	These participants are considered to have the power to initiate, implement and enforce the reform. The Minister for Finance, who was included under the second category described above, could also be considered as a potential reform promoter.

**Figure 24: The Research Participants**

### **5.5.2 Establishing contact with the participants**

Gaining access to elites can be challenging and time-consuming (Mikecz, 2012).

The email addresses of politicians currently in office and of public officials were readily available from the Government of Malta's website. These participants were contacted by email and were sent a participant information sheet.

Contact information of two of the former Prime Ministers and a former Minister for Finance was not readily available on the internet. The two former Prime Ministers were located on an online social networking medium and messages were sent to them, informing them of the study being carried out and asking them to provide the researcher with their email addresses. Both former Prime Ministers replied within a few days, providing their email addresses. They were subsequently sent an email attaching a participant information sheet. One of the former Prime Ministers replied to the email, giving his mobile number and asking the researcher to contact him. During the phone call which followed, an interview meeting was scheduled. The other former Prime Minister replied to the email, suggesting a date and time for the interview, which was accepted by the researcher. The email address of the former Minister for Finance was obtained through a friend of the researcher, who is also a relative of the former Minister. An email was sent to the potential participant, to which a reply was received asking the researcher to call, in order to set up an appointment for an interview.

Given that the two economists interviewed lead consultancy firms in Malta, their contact details were obtained from their businesses' websites. They were both contacted by email, attaching the participant information sheet. One of the participants replied to the email, asking the researcher to contact him on his mobile phone. During the telephone conversation which followed, the participant sought further information on the scope of the interview, in order to

better understand how he can contribute to the study. The other participant replied to the email, suggesting a date and time for the interview, which was accepted by the researcher.

The former Director General at the Budget Office and the Professor of Public Policy who is advising the Maltese Finance Ministry were contacted by email, on behalf of the researcher, by a representative of the National Audit Office, who had been previously interviewed by the researcher. Both participants accepted the invitation to participate in the study and suggested a tentative date for a meeting, which was accepted by the researcher. The Director General at the Central Bank of Malta was contacted, on behalf of the researcher, by the Head of the Department of Accountancy at the University of Malta. This initial contact was followed by a phone call from the researcher and a meeting was scheduled accordingly.

### **5.5.3 Challenges encountered**

Obtaining access to some of the participants proved to be quite challenging, in view of their high profile. This issue was, to some extent, mitigated by the fact that Malta is a very small country where everybody knows everyone else. As a result of this, when the researcher was unable to obtain the contact details of a potential participant, assistance was sought from someone who knew or had a professional relationship with the potential participant. The small country size factor proved also useful in reaching and meeting face-to-face all the participants who could possibly contribute to the study.

Another difficulty that the researcher came across as a result of some of the participants' high position was the limited time allowed by the participant for the conduct of the interview. This limitation was mainly encountered in the case of interviews held with Ministers (including the Prime Minister) who are currently in office. To address this limitation, prior to the interviews, the researcher highlighted the most important questions to be asked, in order to ensure that if

time runs out during the interview, the critical topics would have been covered. Furthermore, the researcher was very well conversant with the questions comprised in the interview schedule, such that the questions could be posed to the interviewee without the researcher having to consult the papers in front of her. The interviews with the Ministers currently in office were held towards the end of the interviewing process; this explains the familiarity of the researcher with the interview schedule. Prior to entering the meetings with the said participants, the researcher was advised by the Ministers' secretaries of the time slot allotted – this enabled the researcher to assess the approximate number of questions that could be discussed in the time frame available. In view of this, it was important for the researcher to be totally focused in order to obtain as much data and information as possible and to make the most of the opportunity granted, during the allocated time slot. Audio recording was fundamental in these circumstances, in order for the researcher to keep concentrated on what was being said during the interview and to avoid wasting time taking written notes.

A further challenge encountered, as a result of the elite interviewees selected, was the postponement of meeting dates, due to the participants' busy and tight schedules. Some of the meetings were postponed more than once and up to four times. In one circumstance, a few minutes after the interview commenced, the researcher got the feeling that the participant was not focused and seemed distracted. At that point, the researcher asked the participant whether she would prefer to postpone the meeting; the interviewee was relieved and extremely grateful, explaining that something urgent had cropped up unexpectedly. As a result, the interview was postponed and held at a future date.

Given the profile of the participants selected for gathering empirical evidence and their consequent tight schedules, it was important for the researcher to make herself available for

interviews, when and as requested. This called for total flexibility and commitment from the researcher during the period when the interviews were being conducted.

It was fundamental for the researcher to thoroughly plan the interview beforehand, since it was considered very difficult, if not impossible, to be granted a second interview, given the elites involved in the research. Furthermore, the researcher made it a point to arrive early for the interviews, in order not to feel rushed and not to lose out on the allocated time. To ensure this, the researcher visited the address given for the interview beforehand, in order to be familiar with the place and avoid getting lost and arriving late on the day of the interview.

## **5.6 Data analysis**

Data analysis was carried out using a thematic approach. Whilst undertaking the activity of analysing qualitative data, the researcher brings to data the inherent skills of critical thinking (Bazeley, 2013). According to Fetterman (1998, cited in Robson 2011), analysis involves processing information in a useful and meaningful way. Bazeley (2013: 3) further observes that qualitative analysis is “*potentially productive of fresh insights and deep understanding*”. By understanding the complexities surrounding human behaviour, the qualitative researcher moves beyond description to theory building (Harper, 1992 cited in Bazeley, 2013).

The first phase of the thematic analysis undertaken was to develop familiarity with the data. In this regard, ‘analysis’ has been referred to as developing a close engagement with the data gathered (Bazeley, 2013). The fact that the interviews were transcribed by the researcher herself facilitated the attainment of this familiarity. Upon completion of the transcription process, the documented text was read repeatedly and thoroughly, in order for the researcher



to immerse herself in the data. During this process, the initial thoughts and ideas about codes and themes were noted and recorded.

The next phase involved generating initial codes for the purpose of categorising the data comprised in the transcripts. Subsequently themes were identified. Bazeley (2013: 191) advises that “*the development of themes depends on data having been coded already*”. The themes identified were both ‘theory-driven’ and ‘data-driven’. The ‘umbrella’ themes, which encapsulate the main points in the data set, were determined on the basis of the research questions and the theoretical underpinnings. However, the sub-themes emerged from a review of the data gathered. The entire data was then reread, in order to ascertain whether the themes capture appropriately what is in the data and to assess the need for re-coding some data extracts, where necessary.

This was then followed by an exploration of the themes, in order to interpret the data and understand what is being revealed. The analysis sought to integrate the empirical data with the theoretical framework proposed and the literature reviewed at the start of the study (Wertz et al, 2011). This helped to determine what is significant about the study and what new contributions the study makes towards the existing literature. In this respect, Wertz et al (2011: 255) suggest that “*at the end of the study, the researcher returns to the literature review prior to data collection and reevaluates prior research in light of the study’s findings*”.

## **5.7 Limitations**

A limitation encountered was the issue of being unable to widen the population selected for empirical evidence collection, to embrace public officials at lower levels in government’s employment hierarchy. The reason for this was the lack of knowledge held by lower level

civil servants in the subject matter being explored. It was considered appropriate to stop at the level of Director, Corporate Services since this person is responsible for overseeing the finance function within the ministries, which includes aggregating the individual budget proposals of the departments into one ministerial budget submission.

As mentioned earlier, some of the participants were provided with a copy of the interview questions prior to the interview. The majority of these respondents were thoroughly prepared and had notes written down next to the questions. However, a few of the interviewees did not prepare their responses beforehand; though this could have impacted the accuracy and level of detail of the responses provided, it is believed that this lack of preparation was considerably mitigated in view of the wide experience and knowledge of the people interviewed.

As maintained by Mikecz (2012: 484), *“elites are used to being in charge and being asked about their opinion; they have the ability to converse easily, ‘just talk’ and get into monologues instead of answering the hard questions...It is not uncommon for researchers to hear the ‘public relations’ version of events instead of their personal account of events”*.

Given the elite population targeted for the interviews, the researcher prepared herself in advance to ensure that this issue would be dealt with effectively. The best tool for dealing with this challenge was to be fully conversant and comfortable with the interview questions. In addition, in the first few minutes of the interview, the researcher sought to put the respondents at ease by giving them the option to skip any questions that they might feel uncomfortable with. At the same time, the researcher emphasised the value of their contribution to the study in order for them to feel flattered – this tended to have the effect of the interviewees opening up. Furthermore, the interview schedule proved to be a very useful guide for ensuring that the conversation remained focused on the research and on the objectives underlying the study – thus, where the researcher felt that the interviewee was

going off at a tangent, intervention was made to bring the discussion back to the subject under study.

A further limitation relates to the timing of the study, which is such that one cannot comment on the effectiveness of PB introduction, because such reform has not yet been implemented.

## **5.8 Conclusion**

This chapter has described the research methodology adopted for the purposes of the study. The findings emanating from the empirical data collection are set out in chapter six and analysed in chapter seven.

**CHAPTER 6:  
FINDINGS -  
INTERVIEWS**

## 6.1 Introduction

This chapter presents the empirical evidence collected from in-depth, semi-structured interviews, conducted with twenty-eight participants, during the period from August 2014 to April 2015.

The research findings are presented in nine further sections. These sections set out the views of the interviewees on the subjects presented. Section 6.2 provides some background information on the involvement of a number of units/entities in the budgetary process. Section 6.3 looks into the need for budgetary reform in the Maltese public sector, exploring some of the pressures which might support the implementation of performance budgeting (PB). Next, a review of the recent reforms of the budgetary framework which have occurred since the change in government, in March 2013, is presented in section 6.4. The chapter proceeds with a discussion in section 6.5, of whether the compilation and publication of performance information (PI) would increase public officials' accountability and enhance government's expenditure prioritisation. Subsequently, section 6.6 investigates the pressures which might inhibit the implementation of PB. This is followed by section 6.7, which studies the implementation strategy for the introduction of PB in the local context. Afterwards, the accrual basis of accounting, in the context of budgeting, is discussed in section 6.8. This is followed by section 6.9 which sets out an overview of the key performance indicators for the education and health sectors, as proposed by the respondents. Section 6.10 then concludes this chapter.

The findings seek to address the research objectives<sup>12</sup> underpinning the study. The first research objective, which involves an analysis of the pressures supporting and inhibiting the

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<sup>12</sup> Vide section 1.6

implementation of PB, is tackled in sections 6.3 and 6.6 respectively. The second objective relates to the identification of reforms in the budgetary framework which have occurred since the change in government in March 2013 and is addressed in section 6.4. A third objective of the study is to ascertain the implications of including PI in budget documents and holding public officials responsible for their actual performance – this is dealt with in section 6.5. The last research objective, which is concerned with the implementation approach to be adopted for PB, is addressed in section 6.7. The remaining sections (6.2, 6.8 and 6.9) set out further data gathered from the interviewing process and seek to complement the findings relating to the main research objectives.

## **6.2 Contributors to the budgetary process**

The MOF, in particular the Budget Office<sup>13</sup>, has the main responsibility for the budget preparation process and for monitoring actual expenditure against the budget on a monthly basis. There are, however, other units which contribute significantly to the budgetary process, as discussed hereunder. The information set out in this section has been extracted from interview data.

### ***The Economic Policy Department (EPD)<sup>14</sup> – within the MOF***

The EPD, which is a department under the MOF, focuses on economic planning and on the estimation of the macro-economic variables, which underpin the annual budget (fiscal projections) prepared by the Budget Office. The main responsibility of the EPD is to prepare the macro-economic forecast and to ensure that the fiscal projections are consistent with the macro-economic variables.

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<sup>13</sup> Vide section 4.4

<sup>14</sup> Vide section 4.4

The EPD's process for macro-economic forecasting starts off with discussions with other institutions, including the EU Commission and the Central Bank of Malta, who both compile their own forecast. The Central Bank's involvement in the budget process is limited to a comparison of their macro-economic forecast with the EPD's forecast. Where the Central Bank has further insights or information than the EPD has, the latter will update its forecast accordingly.

The EPD compiles forecasts for the main components of government's revenue, including VAT, income tax, national insurance, customs and licences. As regards expenditure, the EPD is mainly involved in the area of pensions and social security, as well as in the salaries' projection.

The process for ensuring consistency between the macro-economic forecast and the fiscal projections is as follows: the Budget Office and the EPD each compile their own projections independently, covering the items identified above. Representatives from the two departments then meet up to discuss the differences between the two sets of projections. The main differences usually emanate from the different methodologies used – the EPD works at a macro-level, whilst the Budget Office relies on micro data. For example, for projecting the expected income from VAT, the EPD looks at expected consumption and spending by tourists, amongst other things; whilst the Budget Office reviews the data available within the VAT department. The differences between the two sets of projections are then analysed in the light of information held by the two departments, ensuring that all relevant information is reflected. This process is quite long and time-consuming, involving a lot of going to and fro between the two departments. It is, however, doable in view of the small country size, where holding physical meetings between the two departments is very easy. There is also the added complication that the EPD works with ESA10 data which is based on accruals, whilst the

Budget Office's main variables are based on cash. In this respect, the National Statistics Office (NSO) supports the process, by converting the cash figures to ESA compliant figures.

### *The National Audit Office (NAO)*

During the budget compilation process, the NAO's role is to endorse the macro-economic forecasts/assumptions underlying government's budget which would have been formulated by the EPD, and to issue an independent opinion on their reasonableness. This endorsement is required by EU legislation and by the Maltese Fiscal Responsibility Act, and has been carried out since 2013. The NAO is also currently responsible for endorsing the fiscal projections, as mandated by the Fiscal Responsibility Act. Though the NAO cannot question government's policies and budgetary measures, it can look into and comment upon the inputs underlying the policies and their potential economic and social effects. These roles are expected to be taken up by the Fiscal Council<sup>15</sup>.

Subsequently, when expenditure is incurred, the NAO looks into the records kept by the ministries/departments, in order to assess whether the expenditure made is justified and under control. This expenditure audit is carried out on a rotational basis, such that over a number of years, all departments would have been subject to an audit. In addition, in the case of sensitive issues, the NAO is requested by the Public Accounts Committee to investigate specific aspects of certain transactions – this work is performed by the Special Audits and Investigation Unit within the NAO.

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<sup>15</sup> Vide section 4.6.3



### ***The National Statistics Office (NSO)***

The NSO is responsible for compiling, on a historical basis, the country's debt and deficit figures, together with the indicators relating to government's operations. The data reported on a historical basis is then used as a starting point for the estimation of the macro-economic forecasts by the EPD, including the projection of economic growth and GDP figures.

The NSO is also responsible for converting government's annual budget figures in order to ensure compliance with the ESA10 methodology, for onward submission to the EU Commission. Thus, once the budget allocations are completed from the Budget Office's end, the figures are passed on to the NSO, in order to be presented in the format requested by the EU.

### **6.3 The need for budgetary reform**

Reference was made by the researcher to some of the issues faced by Malta in the last couple of years, namely, fiscal deficit issues, high government debt, credit rating downgrades and being placed under an excessive deficit procedure (EDP)<sup>16</sup>. The participants were asked whether these issues, coupled with the country's requirement to satisfy the Maastricht criteria for qualification and participation in the Eurozone, could trigger government's response for the implementation of budgetary reform. The majority of the participants opined that the existing budgetary system/process needs to be reinvented. There were, however, diverging views as to whether the desired reforms are necessarily prompted by the issues mentioned above.

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<sup>16</sup> On the 19<sup>th</sup> June 2015, the Economic and Financial Affairs Council of the European Commission approved the lifting of the EDP opened against Malta (Times of Malta, 2015b). In view of the fact that the interviews were carried out during the period August 2014 to April 2015 when Malta was still under an EDP, the participants have referred to such EDP that the country was subject to during this period.

The table below highlights some of the issues mentioned by the research participants, which give rise to the need for a budgetary reform. These matters are then discussed in further detail in this section.

**Table 30: Need for budgetary reform**

Need for budgetary reform
<b>The existing budgetary system/process needs to be reinvented as detailed below:</b>
The deficit issues (including the requirement to meet the 3% of GDP deficit target) faced by Malta are triggers for reform - in these circumstances, performance becomes very important.
Malta is behind some other countries with respect to the budget process.
Value for money concepts are not taken into consideration in the budget, because the budgeting is input-based and no analysis is carried out vis-à-vis the expected outcomes.
The line ministries make requests for funds which are exaggerated - thus, the MOF has to limit the budget allocation by going through each line item and adjusting some of them downwards.
The process to request a budget for a particular programme and to get the budget allocation is quite arbitrary.
There is scope for budgetary reform to ensure that priority is given to those expenditures which are really needed.
The budget is compiled by looking at the previous year's expenditure and adding on a percentage in order to arrive at the following year's allocation.
The current system of compiling the budget and of, subsequently, analysing budgetary measures implemented in the previous year, is not good enough to act as a tool for decision makers to enable them to design the right policies.
Modernising the budgetary system would potentially lead to better informed decision-making vis-à-vis required expenditure cuts.
The strategic decisions underlying the budget should be taken by the OPM rather than by the MOF, to ensure that a more holistic view is taken vis-à-vis the various policies adopted in the different sectors.
It is questionable whether government has control over the figures included in the budget; it was found that the civil service has a huge influence on the budget allocations.
The MOF makes decisions on the budget allocations without consulting the Heads of departments who would have worked hard to compile their business plans, in order to furnish the requested information to the MOF.
There is not enough time and resources to permit a detailed analysis by the MOF of the reports and business plans submitted by the line ministries.
The line ministries would only know what funds have been allocated to their ministries, a few days before the budget is presented to the public.
A reform is required in terms of continuous monitoring of the government departments with regard to how the budget is being executed.
Ministries approach the MOF on a regular basis during the year to ask for additional funds, claiming that they do not have enough money to continue with a particular project.

*Source: Interview data collected between August 2014 and April 2015*

An academic and advisor to the MOF (who has recently been involved in carrying out Comprehensive Spending Reviews within the ministries), argued that:

*“The deficit issues and the EDP that the country is subject to at the moment, are triggers for reform... in these circumstances, performance becomes very important. The compilation of PI would enable the ministries to review their performance and to identify ways on how to achieve better results with the available funds. It is difficult to accept the ministries’ claims that every Euro allocated to them has been perfectly spent and that there is no room for improvement. The reason for these claims is that there is a vested interest to hold on to the previous year’s budget and to ask for more.”*

The Accountant General observed that Malta is still behind other countries in so far as the budgetary process is concerned, adding that the EDP and the requirement to meet the 3% deficit target, are definitely triggers for reform.

It was mentioned by the respondent that the Fiscal Responsibility Act which has been recently approved by Parliament, forms part of the overall fiscal reform and fiscal discipline process being carried out by the public administration. Furthermore, there are other aspects which are being worked upon, including the accrual accounting reform; in this respect, the interviewee pointed out that a reform in accounting without a budgetary reform could, however, be an issue. The participant believes that a total reform is required in terms of budgeting and the budgetary process, as well as in respect of budgetary execution. As regards budgeting, value for money concepts are often not taken into consideration because the budgeting is regarded by many as being an input-based exercise; thus no analysis is carried out as to why funds are being spent on particular items and on what the expected outcomes are. It would be beneficial to assess what an activity/programme is costing, in order to try to improve the performance of that particular activity. The interviewee does not think that these types of assessments are being carried out (especially at ministry/departmental levels); if they are performed, they are only done centrally (by the MOF) without the ministries being aware of them.

In the opinion of an economist and advisor to government, government feels the need for budgetary reform, independently of the fiscal deficit issues and of pressures exerted by the EU

to meet the fiscal targets, because there is wide consensus (it has been experienced by the party which was in government in the recent past and by the present administration) that the way the budget is handled, which is line-item, expenditure based, is colonial and out-dated.

The interviewee claimed that:

*“There is no measure of efficiency and furthermore, there is no time for such considerations because the budget is prepared and finalised in a short timeframe. Moreover, it is doubtful whether the budget is prepared by government or by the civil servants – though the strategic policies are set by government, beyond these policies, it is questionable whether government has control over the figures which are ultimately included in the budget. Very close to the budget date, the civil service first allocates the required resources for the implementation of government’s policies and priorities and then, the remaining funds are spread between the ministries (giving them a small portion of what was initially requested by them) – the latter allocation is done irrespective of value for money concepts.”*

The interviewee explained that the MOF makes the decisions on the budget allocations in the last week before the budget, without consulting with the Heads of the departments who would have worked on their business plans for weeks, in order to furnish the requested information to the MOF. Furthermore, the Ministers, who would have held discussions with the MOF Permanent Secretary and delivered presentations on their proposals, thinking that they made their case for obtaining the requested funds, would only know what funds have actually been allocated to their ministries, a few days before the budget presentation to the public. Following this process, the budget is then subject to approval by Parliament, by means of a majority vote.

The respondent expressed his wish to see a different approach to the budget process – ideally, the budget should pass through Cabinet very early on in the year (during the first quarter of the year); the Cabinet makes the required decisions; then, within that framework of decision-making, the civil service would implement Cabinet’s decisions and incorporate them within the budget (rather than having the civil service implementing mathematical decisions). The

involvement of the Ministers at an early stage in the budget process would ensure that they understand the nature of government's constraints, refraining from making unrealistic demands for funds. Furthermore, it was mentioned that an IMF delegation has visited Malta during 2014, giving their opinion on how the budgetary process could be changed. The interviewee observed that the IMF did not state anything that was not known by the Maltese MOF, but the fact that the statement came from the IMF could perhaps have a stronger influence on the civil service. According to the interviewee, there is a commitment from government for the politicians and the civil service to look at what could be implemented following this IMF process.

An economist and academic observed that, as regards Malta's deficit and credit rating issues, high government debt and being under an EDP, the country's problems are not worse than those of other countries, from a short-term perspective. However, from a long-run outlook, the country will be worse off in view of its ageing population and the fact that this issue is not being addressed. According to the respondent, there is no efficiency motive in the public sector, in contrast with the private sector; thus, management systems are created within the former sector to operate the price mechanism. The implementation of PB would be a tool for informing budget and fiscal performance, in the context of the objectives and targets of the public sector. The respondent declared that he strongly believes in long-term forecasting (rolling budgets) and ring fencing (hard budget constraint) – the implementation of these two strategic approaches can be better achieved through such a management system.

A former Prime Minister opined that:

*“The current system of compiling the budget and of subsequently, monitoring and analysing budgetary measures which have been implemented in the previous year and the results and outcomes (economic, social and political) of those decisions, is not good enough to act as a tool for decision makers to enable them to design the right*

*policies. A radical change in Malta's budgetary system is required, because the process of how Parliament approves the budget is not efficient and it does not function properly. Thus, a transition to a performance based budgeting system is required, though this has to be complemented by a radical change in culture which is not an easy task."*

The interviewee explained that with the current system, the MOF takes the lead in the design of the budget and the allocation decisions to the respective ministries, though it has a clear direction from the OPM. The Minister for Finance meets the individual ministers, takes on board their feedback on the previous year's performance, listens to their initiatives, programmes and priorities and then allocates funds (usually a fraction of what they would have requested). The respondent compared the current negotiation process with "*haggling in a bazaar or market*". It was also mentioned that there is not enough time and resources to permit a detailed analysis by the MOF of the reports and business plans submitted by the line ministries. According to the interviewee, if the strategic decisions are taken by the OPM, rather than by the MOF, a more holistic view would be taken, embracing policies relating to health, education, competition, investment, social policy and the overall performance of the economy.

A Permanent Secretary argued that there is scope for budgetary reform, such that priority would be given to those expenditures that are really needed, rather than carrying out expenditures simply because they have been done in the past. It was stated that expenditures which have been budgeted for in the past are not questioned. According to the respondent, the process to request the budget and to get a budget allocation is quite arbitrary and not at all scientific. Innovation is lacking, because the current system does not encourage public officials to be creative. The Permanent Secretary believes that if PI is incorporated in budgets, better allocation decisions could be made.

Another Permanent Secretary claimed that “*the existing budget needs to be reinvented*”, in order to give a clearer picture of the country’s financial performance and position. Currently, government focuses on the budget expenditure, without providing information on the results achieved with the public funds spent. The participant mentioned the statistics for 2014, which registered a large increase in government employment, with a corresponding increase in payroll spending by government. In this respect, it was stated that one should not look at what is being inputted into the system, but rather on the expected productivity/output of these employees. Contrary to politicians, the Permanent Secretary, as an administrator, is more concerned with the input-output relationship and the objectives being reached through the budget allocations. By way of an example, the interviewee referred to the capital outlays being expended by government for building new schools; whilst politicians publicise these investments to gain political points, administrators look beyond and ask: “*if the country’s birth rate is on the decline, why are we building more schools which would eventually lead to higher maintenance costs?*”

A representative from the NAO declared that he is in favour of the implementation of PB in the local context; however, he qualified his statement stating that the introduction of PB by itself, without the application of fiscal discipline, will not improve the country’s financial situation and bring the deficit down. The participant believes that there is the need for fiscal discipline in two main areas: spending and revenue generation. As regards spending, the MOF is currently carrying out spending reviews to identify measures for cost cutting. The other area that should be emphasised further is the revenue side of the equation, because in the respondent’s view, government is not getting its dues in terms of taxes. The participant stated that the implementation of PB had already featured in government’s agenda, a few years back – Malta had committed to introduce PB in the IMF Report of 2008: “*The authorities are*



*reinforcing the fiscal framework with a medium-term orientation. They are pursuing more structured multiyear fiscal planning and the introduction of performance budgeting methods”* (IMF, 2008: 12). The interviewee observed that planning is one thing, but implementing is another!

A public official from the EPD explained that Malta’s economy grows at roughly 4.5% in nominal terms; in revenue terms, if elasticity is assumed at 1.2, the increase would be of 5.4%. The majority of the large public expenditure such as social benefits, health and education grow at this rate; however if all expenditure increases at this rate, it would mean that the deficit will never be reduced. Therefore, to reduce the deficit, the other expenses (which are not related to health, education, pensions and other social benefits) cannot increase by more than the inflation rate of roughly 2%. Notwithstanding this, many of the expenses involved, such as salaries, increase by more than inflation. Thus, it is not easy to reach the established deficit target, unless efficiency gains are achieved. The respondent claimed that Malta needs to target a balanced budget in structural terms, which is no easy feat; thus emphasising the need for budgetary reform.

A former Minister for Finance stated that this budgetary reform is very important, because the way the budget process is carried out, is not very efficient. The current process puts a lot of onus on what to allocate, on the MOF. In his experience, the interviewee claimed that the line ministries come forward with their plans which are not measured in terms of the objectives they are trying to achieve. The fundamental problem with the current budgetary system is that the civil service does not look at what the actual funding needs are, but rather on how to extort additional funds from the MOF. The respondent claimed that if a PB system is implemented, then the funding requested would have to be justified in terms of quantifiable outputs. In the absence of PB, the ‘haggling’ that currently takes place during the budget preparation process,

will persist, with the MOF having to go through the budget line items of each line ministry and to adjust some of them downwards.

Another former Minister for Finance declared that he is absolutely in favour of the implementation of PB in the local context, adding that every form of financial management, fiscal discipline and accountability structure, is desirable. The respondent mentioned that during his term as Minister for Finance, the budget used to be compiled by looking at the previous year's expenditure and adding on a percentage in order to arrive at the following year's allocated expenditure. This is still, more or less, the practice currently adopted during the budget compilation process. The interviewee explained how he tried to change this practice during his two-year term within a particular ministry. At that time, this ministry prepared a budget based on deliverables for the first time – the services that were being offered were costed and then priority listings were made. The interviewee noted that the budget compilation took around six months. However, it was well worth the effort, because when the MOF and the Prime Minister in office at the time, were pushing for a budget reduction for the said ministry, the participant asked them to review the priority listings and identify the services which will not be offered to the public; in truth, no services were eliminated and the ministry was awarded the requested budget in full. The interviewee emphasised that this would only be possible when PI and targets are presented in the budget documents. Unfortunately, the budget process that he had introduced when he was politically responsible for this particular ministry, was discontinued after his term as Minister ended.

The Minister for Finance mentioned that the business plans presented by the line ministries do not contain any output indicators, to back up their requests for funds. It was confirmed by the Minister that the budget is currently compiled on an incremental basis, such that from one year to the next, a percentage increase in non-discretionary expenditure is effected. The

Minister mentioned instances where the ministries request a 15% increase over the previous year's allocation, knowing well that the increase cannot exceed, say, 5%. In view of this, the MOF would have to limit the budget allocation – this is usually not done in the line ministers' presence, but after they leave the negotiation table, in order to avoid clashes between the MOF and the line ministries. As a result, the line ministries would not know whether the item requested has been voted for; they would usually be informed of their budget allocation a few days before the budget is presented to the public. Notwithstanding the MOF's effort to limit the ministries' fund allocations at budget preparation stage (in order to reach the deficit reduction target), ministries approach the MOF on a regular basis during the year to ask for additional funds, claiming that they do not have enough money to continue with a particular project. The ministries argue that even though allocated funds have been limited by the MOF, the line ministry is still politically committed to the people and it cannot go back on its word. Thus, the line ministry would make pressure on the MOF, stating that if the latter will not allocate additional funds to a particular capital project, the line ministry would have to tell the public that Finance did not provide the required funds and thus, the project has to be abandoned. The Minister pointed out that this also happens with recurrent expenditure. For example in the case of the free breakfast scheme for schoolchildren in government schools and the free child care initiative, the responsible ministry approached the MOF for additional funds; when the MOF queried why the actual cost shot up compared to the budgeted figures, the responsible ministry replied that this was the result of the initiatives' success. The MOF had to shift funds from other programmes to cover the additional costs of these initiatives. The Minister for Finance argued that the line ministries should be responsible for their budget and they should stick to what has been provided for in the budget, unless exceptional or unexpected expenditures crop up during the year.

When asked whether there is the need for reform in the budgetary process, a public official from the Budget Office stated that there *have* been budget reforms recently – not a huge reform, but small improvements. As an example, the respondent referred to the enactment of the Fiscal Responsibility Act, which lays down a number of responsibilities on the MOF and on the other ministries and departments.

In contrast with the majority of the respondents, a senior civil servant within the MOF claimed that the reform required is not within the budgetary framework, but in the policies being employed in the various sectors which constitute the real drivers of government expenditure. The respondent explained that the government's budget is, in the main, consumed by social welfare (including pensions), education, health and the care of old people. When these sectors are factored out of recurrent expenditure, the remaining items are insignificant. Therefore, according to the respondent:

*“It is not the way the budget process is carried out which is driving the expenditure; it is the policies that government is employing in these policy areas which are affecting the spending. The issue is that in these sectors, as long as the same policy stances remain, there is not much latitude for expenditure cutting, because the pensions, social benefits and salaries have to be paid, and free healthcare and education have to be provided.”*

The senior civil servant added that if, for instance, the issues in the social welfare and the dependencies that have been created are not tackled, or if the pension system is not reformed, government spending in this area will continue to rise. As regards education, one of the issues which is driving costs is the lack of economies of scale and the inefficient use of resources, whereby there are a number of nearly empty schools in the country with complements of teachers teaching a handful of students. Unless there is a policy change whereby these schools would be closed down and consolidation takes place, costs will not decline, because the school infrastructure will have to be maintained and the teachers' salaries will have to be paid.

The respondent also mentioned the provision of free healthcare which is creating a huge strain on the budget. Unfortunately, nobody wants to make tough decisions because of the risk of political fallout. The interviewee mentioned that the expenditure increase, year on year, in the above-mentioned high spending sectors is consuming and sometimes, even exceeding, the increase in revenue generation. As a result, other much needed expenditure, such as expenditure on aspects of infrastructure, is being crowded out. Thus, unless alternative policy stances are taken to address the challenges, changing the budgetary process will not solve the fundamental problems in the Maltese public finance, according to the respondent.

## **6.4 Recent reforms in the budgetary framework**

This section highlights the research findings relating to the changes that have taken place in the budgetary framework, in the past couple of years since the change in the public administration which occurred in March 2013.

### **6.4.1 Comprehensive spending review (CSR)**

In parallel with the process for compiling the 2015 budget, the MOF has, during 2014, launched a Comprehensive Spending Review (CSR) exercise to review expenditure on budget line items. The review exercise was carried out in relation to recurrent expenditure on ‘programmes and initiatives’ under each ministry, which had been included in the 2014 financial estimates. (Expenditure on personal emoluments and operational and maintenance expenses were excluded from the scope of the CSR).

The line ministries were asked to provide information on the budget line items included under ‘programmes and initiatives’, within recurrent expenditure. Some of the questions comprised in the template that each line ministry had to fill in, are listed in the table below:

**Table 31: Questions included in the CSR template**

CSR Questions
Information on the present outputs for each line item was requested. In this respect, the ministries had to specify what is being achieved, in terms of the improvement to the quality of life, as a result of the said line item expenditure. Furthermore, explanations as to what is currently being done with the said expenditure were required.
The ministries had to reflect and provide information as to whether the line item expenditure has brought about improvements to the service in the last three years (2012, 2013 and 2014).
The CSR required management in the ministries to consider a number of hypothetical scenarios with respect to budget allocation and ascertain the impact of such scenarios on the results achieved and on the people benefitting from the service. Amongst other things, the ministries had to consider the consequences of the following: funds being discontinued, a budget reduction of 5% and no change in the budget allocation vis-à-vis the previous year.
The ministries were asked whether there are any line items that can be consolidated through the discontinuity of another line item. They were also asked to consider whether there are any services which may be discontinued, in order to reallocate the respective funds to other initiatives.
The MOF also sought an explanation of the growth of each line item from 2012 to 2014. Ministries were encouraged to reflect as to whether the service has developed or not, as to whether the line item is a product of history and as to whether the service is still relevant to today's requirements.

The academic and advisor to the MOF, who led the CSR process, explained that the CSR involves reviewing line items in public spending, determining what output is being produced for a line item and assessing whether the line item is still relevant, such that resources within public spending can then be reprioritised without increasing public spending and without increasing taxes.

The interviewee mentioned that the concept of the CSR was launched in England during 1997, adding that he had been involved in such a process. According to the interviewee, the CSR was a huge success in England and led to a significant reduction in the country's deficit and to a release of resources which could then be spent on government's priorities. The Maltese MOF, with the respondent's support and advice, is seeking to replicate the CSR approach in Malta's public spending, in its attempt to reduce the deficit.

Though all ministries were covered in the CSR process and they were all required to provide the information referred to above, during the first CSR exercise (carried out in 2014), focus was placed on social security benefits, where a complete reform was proposed which eventually featured in the 2015 budget. The expenditure review covering social security was triggered following the issue of a damning report by the Auditor General (National Audit Office, 2014), highlighting the abuses in social security benefits. Measures included in the 2015 budget sought to address the existing social fraud, by changing policies with the aim of encouraging employment and ensuring that the social benefits are given to the deserving.

With the exception of social security, the results of the CSR exercise were not fed into the 2015 budget. This was also confirmed by a Permanent Secretary, who stated that:

*“The results emanating from the CSR exercise were not given enough consideration in the 2015 budgetary allocation – this could be due to the country’s fiscal situation where government cannot afford to lose control over its expenditure, where the resources have to be allocated carefully and where focus has to be placed on the areas of priority.”*

The Prime Minister observed that the CSR exercise being carried out by the MOF will take quite some time to be introduced from an operational aspect; but at least the public officials’ mind set will start to change. In truth, the majority of politicians, especially those who are lawyers or doctors by profession (with no accounting/finance background), would never have been involved in these types of processes and systems.

### ***The Education Ministry’s perspective***

#### Calculation of unit cost per student

As a starting point to the CSR process, the ministry was requested to calculate the annual cost of a student in education. This was estimated for scholastic year 2012/2013, in relation to all

schools, from kindergarten to higher education. In commencing the exercise for the calculation of the annual unit cost per student, a Director within the Education Ministry obtained a list of all the schools and colleges in Malta and Gozo and started identifying the expenses attributable to each school/college. The Director remarked that the resulting unit cost per student was not an accurate figure since the exercise required a number of approximations, including transport and textbook cost allocations.

### Comprehensive Spending Review

The Director was of the view that the MOF was not fully satisfied with the outcome of the CSR process. This viewpoint was shared by some other respondents. Firstly, the public officials in the Education Ministry had never been exposed to such a process and secondly, it was seen as a waste of time by some civil servants, especially since year after year, planning is undertaken but then the funds requested are not given in full because of lack of available funds. As mentioned earlier, the CSR exercise involved three questions: what would be the outcome of a zero budget, what would be the outcome of a 5% budget reduction and what happens if there is no change in budget allocation. For the ‘zero budget’ scenario, the civil servants involved in the exercise stated that “*they would close the door and go home*”. The MOF had hoped that the scenarios would be studied in depth by the civil servants, in order to come up with ideas of what could be done in such circumstances. The Director stated that, prior to the launch of the CSR, the MOF tried to convince education officials that less should be spent on education, mentioning in particular salary costs, in order to reduce the deficit. Though government’s motto has become to ‘do more with less’, the Director claimed that it is not always possible to achieve this objective.



As regards salary costs, there is disagreement between the MOF and the Education Ministry, with the MOF claiming that the academic staff complement in schools is excessive and the Education Ministry arguing that there is no scope for reduction in the number of teachers and Learning Support Assistants. In this respect, the academic and advisor to the MOF commented that there is a paradox in Malta: a calculation of the pupil-teacher ratio for Malta indicates that it is the lowest when compared to the rest of Europe; yet the failure rate of students is one of the highest in Europe. According to the Permanent Secretary for the Education Ministry, given that the salary bill represents the greatest portion in the budget allocation for education, there is little flexibility for cost cutting. Furthermore, a number of expenditure items within the Education Ministry are structured and subject to a collective agreement which comprises stipulated allowances.

The Director, Corporate Services stated that during the preparation of the 2015 budget, the Education Ministry tried to take into account what was learnt from the CSR exercise. In this respect, the Directors of each section were asked to identify the outcomes and performance indicators for budgeted line items under ‘programmes and initiatives’. For example, in respect of the ‘tablets project’ (provision of free tablets to every student in primary school from Year 4 onwards), the ministry tried to ascertain the number of students that will be benefitting from the programme, together with the learning outcomes from the project. (This project is currently being pilot tested).

### ***The Health Ministry’s views***

Referring to the CSR exercise carried out in 2014, a Director within the Health Ministry explained that for each programme and initiative comprised in the 2014 financial estimates, the Health Ministry had to identify the need for the project and the consequences/damages

should the project not be carried out. The interviewee acknowledged that it was not easy to fill in the template provided by the MOF, because it was not always possible to identify the requested information.

#### **6.4.2 Three-year projections**

An initiative taken by the new public administration was the preparation of a three-year financial plan, covering the fourteen government ministries. The three-year revenue and expenditure projections were presented for the first time in the 2014 Financial Estimates. The first year of the plan represents the budget year, with the following two years comprising forward estimates of revenue and capital and recurrent expenditure, per line ministry. Subsequent to the introduction of this practice, the requirement for the preparation of three-year projections was mandated by the Fiscal Responsibility Act (enacted in August 2014).

A Director within the Education Ministry opined that the education sector is so dynamic that one can only plan ahead for a year because keeping flexibility is important. It was mentioned that the MOF are pushing for the compilation of three-year plans, but the Education Ministry believe that the compilation of projected information is only feasible for one year. These comments indicate that the revenue and expenditure projections for the two years following the budget year, have been prepared centrally, by the MOF. This was confirmed by the Permanent Secretary within the Education Ministry.

A former Prime Minister mentioned that when he was Deputy Prime Minister, there was a system in place, whereby each ministry had to submit a three-year business plan – this encouraged civil servants to think on a long term basis. Unfortunately, this practice was discontinued in 2004. Notwithstanding this, the interviewee believes that planning ahead for a

minimum of three years, is of utmost importance. Medium-term financial planning would potentially result in achieving more effective results with the allocated funds.

### **6.4.3 Implementation of the Electoral Manifesto**

Another initiative undertaken by the new public administration was to appoint a ‘Minister for European Affairs and *the Implementation of the Electoral Manifesto*’. In this respect, the Minister for Education explained that government is using a system whereby the electoral manifesto and the commitments made therein, on which it was elected in government, have been translated into a five-year strategy, setting out when the measures will be implemented year by year. The Minister added that the yearly budget would, in turn, reflect the priorities and needs listed in government’s strategy. According to the Education Minister, the publication of this document keeps ministries ‘on their toes’, such that what is requested by the line ministries would be in line with the electoral mandate. When implementing new initiatives, the question that should be asked is whether there are available resources for such initiatives, and whether the said initiatives are according to government’s priorities. The Education Minister commented that, in his opinion, this process is very healthy.

When launching the budget process for 2014 and 2015, guidelines were issued by the Principal Permanent Secretary to the Permanent Secretaries responsible for the respective ministries, stating that there should be a strong effort to ensure that the outcomes/indicators targeted in the budget would be linked to the promises contained in the electoral manifesto. As a result, during the budget compilation exercise, the line ministries had to analyse budget line items and the corresponding expected outcomes in terms of what is stipulated in the manifesto about the respective item.

This was confirmed by a Director within the Education Ministry, who pointed out that during the preliminary meetings leading to the budget preparation process, the interviewee and the Director General briefed the Directors of the respective cost centres, explaining that the budget plans had to be in line with the electoral manifesto. It was emphasised that if a project in the cost centres' budget plan was not linked to an objective of the manifesto, there was the risk that funds would not be allocated for such project.

#### **6.4.4 Publication of the 'Implementation of the Budget' document**

In November 2014, government has published, for the first time, a document entitled 'The Implementation of the Budget' (Office of the Prime Minister, 2014), setting out the implementation status of the budgetary measures which had been included in the previous year's budget (for 2014). This document details, on a quarterly basis, how the government ministries are implementing each budgetary measure and indicates whether the measure has been completed as at the date of publication of the document or whether it is still in the process of being undertaken.

The Prime Minister of Malta affirmed that the purpose of compiling a report detailing the implementation of budgetary measures, is to enhance transparency and to introduce the idea of comparing budgets with actual results. The respondent explained that:

*“Government is taking a benchmark, being the electoral manifesto of the party which has been elected to government, and then measuring the progress for each objective in the manifesto on a quarterly basis. This is a way of measuring government's success, with success referring to the implementation of the electoral promises. A drawback of this practice is that it is not necessarily measuring the correct implementation of government's objectives; but at least, there is a programme of work to be done, there are milestones to be reached and if such milestones are achieved, government would be considered as performing.”*

A Director General from the Central Bank of Malta also opined that this document is a powerful tool of accountability and transparency, which exerts more pressure to implement the budgetary measures.

#### **6.4.5 Performance appraisals**

A further change initiated by government during 2014 was to establish clear and specific indicators against which the Permanent Secretaries responsible for each ministry were appraised, for the purpose of awarding performance bonuses. These performance indicators comprised the implementation of budgetary measures, simplification of procedures and other subjective measures such as team work, leadership and communication skills.

The performance appraisals of the Permanent Secretaries are being carried out by the Principal Permanent Secretary, whilst the latter is, in turn, being appraised by the Prime Minister. Performance assessments are being done twice a year, in June and in December; the June assessment helps to identify situations where performance is not on track, such that adjustments could then be made in time to ensure that the targeted deliverables are reached by year end.

As from 2015, this performance appraisal system will be cascaded down to Directors General and Directors, who will be appraised by Permanent Secretaries. A Permanent Secretary explained that once the budget is approved by Parliament and the planned initiatives and projects would be known, every ministry will receive a template setting out the expected deliverables for each ministry. The respective ministry would then plan the implementation of the initiatives and the responsibility for the implementation would be cascaded downwards. Thus, if a Director General is responsible for one of the deliverables, such measure would be included in his/her performance record.

This initiative emanates from government's pledge to enhance accountability of its public officers. The Prime Minister observed that:

*“Though there were already some practices which were performance related within the public sector, including the award of performance bonuses to certain civil servants, in reality the performance bonus has been regarded as a supplement or as part of the basic salary.”*

The Prime Minister claimed that, when launching this new initiative in 2014, it was made clear to the Permanent Secretaries, that it will be very difficult for a person to be awarded the full bonus allowance. The Prime Minister remarked that a number of people did not take this very well, adding that he did not even give the full bonus to his Principal Permanent Secretary, for 2014. According to the Prime Minister, this is the beginning of a new culture, mentioning that in his opinion, the existing system is ingrained in secrecy and it assumes that not all the checks and balances are in place, not necessarily with the intention of wrong-doing, but for the purpose of not disclosing information.

#### **6.4.6 Enactment of the Fiscal Responsibility Act**

In fulfilment of Directive 85/2011/EU on budgetary frameworks, a Fiscal Responsibility Act was enacted by the Maltese government in 2014, to ensure sustainable public finances and to enhance accountability and transparency in conducting financial activities. The Act was unanimously approved by Parliament; thus, from a political viewpoint, this reform has been endorsed.

The law provides for the establishment of a Fiscal Council, with the responsibility to carry out oversight duties. One of the functions of the Fiscal Council is to review the macro-economic forecasts published by government biannually (in April and October) and to give its views on their reasonableness; prior to the setup of the Fiscal Council, this role was carried out by the

NAO. In addition, the Fiscal Council is responsible for monitoring what government is doing and for providing recommendations in relation to areas where government is not on track. In particular, the Council will assess whether government will reach its financial targets vis-à-vis deficit and government borrowing thresholds.

In terms of the law, the Fiscal Council is a functionally independent institution – it cannot receive instructions; recruitment has to take place independently; and its budget is fixed by the Act and indexed to inflation. A former Finance Minister explained that the Chairman of the Council is appointed by the Minister for Finance, following consultation with the Shadow Minister for Finance. Then, the Chairman, in consultation with the Minister for Finance and the Shadow Minister, appoints the other two members of the Council. The Fiscal Council is composed of economists or experts in fiscal matters.

A Director from the EPD, who was involved in the drafting of the Fiscal Responsibility Act, mentioned that the law was based on the Irish Act, with respect to the provisions required to satisfy EU requirements, mainly the fiscal rules and the Fiscal Council set up. The reasons for adopting the Irish model were the following: Ireland is a small country as is Malta; it has an open economy and it has English traditions like Malta; it was going through a crisis and was therefore setting up strong institutions with the help of the IMF and Troika; and it is a model which has been accepted by the EU Commission.

According to the interviewee from the EPD, the Maltese Act went beyond the Irish Act and also beyond EU requirements. Firstly, unlike the Irish Act, the Maltese law starts by laying down the principles of fiscal responsibility<sup>17</sup>, which help in the interpretation of the Act. Secondly, in view of the fact that financial sophistication in Malta is lower than that of

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<sup>17</sup> Vide section 4.6

Ireland, a provision has been included in the Maltese Act which requires the Fiscal Council to explain the budgetary fiscal process in a way which is accessible to everyone including non-experts. Thirdly, as regards medium term budgeting, EU obligations stipulate that a medium term budget framework is required, without providing further guidance. The EPD believes that it is useless having fiscal rules and a fiscal institution, and then having a weak MOF. Thus, provisions have been included in the law to strengthen the powers of the MOF; such provisions relate to the establishment of spending ceilings and ensure that the ceilings are consistent with the fiscal rules.

The Act has given certain powers and commensurate responsibilities for expenditure, with the purpose of strengthening the MOF. Thus, if a public official exceeds the budget allocated by the MOF, without the approval of the Finance Minister, he/she could be personally liable. This obligation does not come out of the EU framework. For example, collective agreements need the MOF's approval, in contrast to what used to happen before the passing of this legislation; if the Ministry's approval is not obtained, such agreements could be declared null and void for the purposes of the law.

The EPD official believes that:

*“The reform has been carried out on paper and in a strong way. The Act incorporates reporting requirements which are sufficiently onerous to satisfy the reporting needs for a country which is constantly under an EDP – amongst others, there are requirements for the preparation of a mid-year report and a full-year report; every report has to be endorsed by the Fiscal Council; the medium term plan has to be endorsed; and every institution which plays a role in government's revenue has to compile its forecast. The issue is how ministries and departments will manage all these reporting requirements.”*

According to a Central Bank representative, the budget process will be much more under scrutiny, as a result of this law. According to the respondent:



*“Until recently, the budget was viewed as an annual exercise where the same issues were discussed year after year, including the cost of living increase, the prices of petrol and cigarettes and similar matters. However, with the enactment of this law, the type of analysis required has to go beyond what was being done in the past – the sustainability of the debt has to be ascertained, the impact of the deficit has to be considered and the identification of measures to address any structural deficiencies is required.”*

During an interview held in April 2015, a senior civil servant within the MOF was asked whether this law has led to any improvement since its enactment in August of the previous year. The respondent replied that to date, nothing has changed because whoever used to try to exceed the budget allocations, is still trying to do so. The interviewee added that *“we still have the same challenges – cultures cannot be legislated and they cannot be changed overnight.”*

## **6.5 Accountability and expenditure prioritisation**

The research participants were asked whether PI should be incorporated in budget documents and whether such information could be used by government to hold public officials responsible for the actual performance of their department/programmes. Some of the respondents also expressed their opinion on the mechanisms that could be applied to motivate performance.

Reference was then made to the current line-item budgeting system which promotes across-the-board expenditure cuts, in situations where government seeks to reduce its expenditure. Such practice could harm effective, value-for-money programmes. In this respect, the participants were invited to give their views as to whether PB could improve government’s expenditure prioritisation. The discussion then turned to the implications of a department underspending its budget, under the current line-item budgeting system.

### 6.5.1 Inclusion of performance information in budgets

The majority of the respondents claimed that PI should be included in budget documents, but were cautious when giving their views as to whether such information could be used to hold public officials responsible for their performance. A number of suggestions were put forward as regards the use of mechanisms to motivate performance, with the most commonly mentioned being the award of a performance bonus and the adjustment of the department's budget allocation for the following year.

An economist and academic believes that:

*“The inclusion of PI in budgets would be useful, provided it is used in the proper way to allow for better performance in the future, rather than to blindly find scapegoats for past underperformance. If the target was not reached, should the budget be increased to achieve it or should the budget be decreased because there was inefficiency? Moreover, if the target was not reached, was the target appropriately set in the first place or were there other factors which influenced the attainment of the target irrespective of efficiency levels?”*

The interviewee advised that the perspective that should be adopted is that public officials are to be accountable for the public money being spent; however, emphasis should be put on analysing why a target was not reached and deriving corrective action for the future, rather than looking at the past and taking automatic decisions which could perhaps be based on lack of information. The interviewee suggested that rewards and sanctions for the achievement and non-achievement of performance targets respectively should be applied as a last resort, reiterating that focus should rather be placed on what could be done better in the future.

An academic and advisor to the MOF agrees with the incorporation of PI in budget documents; however, in his opinion, rewards and sanctions should not be applied in relation to performance, because these mechanisms could result in the manipulation of data by civil

servants. Instead, a report should be compiled which shows whether ministries/departments are meeting their performance indicators.

A Director within the Education Ministry is of the opinion that rewards and sanctions should not be linked to performance indicators, since there are a number of factors which affect the achievement of performance that are beyond the public officials' control. An example mentioned related to the number of 'early school leavers', where government is aiming to reduce this figure. In this respect, if the student does not have the aptitude to continue studying (perhaps because of his/her home environment), is it just the teacher in the classroom who is responsible? The respondent claimed that the deficit cannot be viewed solely from a monetary point of view because the social aspect is fundamental in education. It was mentioned that the Education Ministry is pushing for the increase in staff complement for the provision of psycho-social services, in view of the high demand for such services arising from the increasing number of broken families in Malta. Though the additional expenditure on these salaries might not result in better academic results, there is a moral obligation to support students passing through family or other problems. Another point noted related to the low pupil-teacher ratio in the Maltese education system. Though this ratio has to be considered, the respondent claimed that when the system is based on inclusive education as is the case in Malta, no child can be ignored in class and Learning Support Assistants are brought in to support children with learning difficulties. The interviewee acknowledged that, at the same time, attainment of examination results cannot be ignored because, if achievement in a school deteriorates, the school would end up in the newspapers.

A Permanent Secretary expressed agreement with the inclusion of PI in the budget, given that public officials are dealing with public funds, and thus they are not just accountable to their employer but also to the citizens. However, holding public officials responsible on the basis

of PI could be problematic, in view of the fact that some matters might be beyond the control of a public official because of political interference.

The incorporation of PI in budgets clearly makes sense from a sustainability point of view, according to a Director within the Health Ministry. As regards linking the PI to rewards and sanctions, the respondent opined that rewards should be set at entity level, rather than at a personal level. A suggestion made was to allow the savings made by a department/ministry during a particular year to be carried forward to the next year for use on a specific project which would have been approved centrally. According to the respondent:

*“Giving rewards at a personal level could be risky, because monetary rewards could lead to lack of social responsibility and to greedy behaviour. This could, in turn, lead to irresponsible decisions that give quick gains at the expense of longer term benefits. Going for personal gain is especially dangerous in the health sector. Where monetary rewards are at stake, there is a higher probability of manipulation of figures.”*

Currently, public accountability is based on expenditure, rather than on production, according to an economist and advisor to government. In this respect, more information should be available to provide accountability on the funds voted and on what deliverables were achieved. The respondent suggested that the best reward or sanction that could be used would be the adjustment of the following year’s budget, that is, if a ministry/department did well, it could be rewarded by the allocation of a higher budget in the subsequent year.

A former Minister for Finance explained that the contracts covering government’s management structure are renewable every three years; thus it was suggested that should the pre-established targets not be reached by a public official during the said three years, consideration for terminating his/her contract should be made.

A former Prime Minister and a former Minister for Finance mentioned that there is already a performance bonus system in place. The former Prime Minister suggested that:

*“If the mechanism adopted to motivate performance in a PB system is tied to the performance bonus awarded to public officials, it should be ensured that the assessment as to whether a civil servant achieved the established targets or otherwise, would not be taken by that civil servant’s direct superior, but by an independent unit which can make an objective assessment. Currently, there are two main issues with the performance bonus system; firstly civil servants consider the bonus as an extension of the basic salary rather than a reflection of their performance; and secondly, the bonus amount is established by the superior of the public official being appraised, which creates difficulties in view of the human element involved, with the superior wanting to maintain a good relationship with his subordinate and therefore awarding a higher bonus than possibly deserved.”*

The Accountant General agrees that PI could definitely be used to hold public officials responsible for their actual performance. It was explained that actual outcomes might be beyond the control of the civil servants in view of unexpected expenditures which crop up during the year and which have to be provided for, or due to deteriorating economic conditions which may result in government going off-target in its revenue and expenditure figures. Nevertheless, as long as there are reasons and justifications as to why certain outputs and outcomes were not reached, there should not be any issue in gauging performance.

The Education Ministry Permanent Secretary agreed that accountability should be linked to results obtained by the public officials. In this respect, monetary awards such as bonuses could be awarded to civil servants, in order to motivate performance. Other mechanisms that could be considered by the public administration for encouraging the achievement of performance targets relate to a person’s career development opportunities.

The Minister for Education advised that performance targets should be realistic and achievable, and at the same time, they should be ambitious and challenging. If the targets are then not reached, one would still have the satisfaction of saying that everything possible was done to achieve them. The respondent cautioned that:

*“Though performance measures are a very useful tool, one has to keep in mind that behind the statistics, there are people, and thus, the KPIs should be used to achieve the ultimate objective, mainly to better the lives of humans. For example, if the Education Ministry aims that in a few years’ time, the number of youths aged between 18 and 24 would have achieved some basic skills, government would be pleased to report to the EU that the early school leaving rate has decreased; however, the number in itself or satisfying the EU is much less important than the persons themselves, who might become dependent should they fail to achieve some basic academic skills.”*

## **6.5.2 The current line-item budgeting system**

### ***Expenditure prioritisation***

The majority of the respondents confirmed that currently, if government needs to effect a cut in its expenditure during the year, such cut would be carried out across all ministries. Furthermore, the majority of the interviewees agreed that the introduction of PB would enhance government’s expenditure prioritisation, such that expenditure on ineffective programmes is reduced and the taxpayers’ money is directed towards initiatives which lead to tangible results.

Confirming that presently, when government needs to carry out expenditure cuts, they are effected across the board, a Permanent Secretary claimed that PB could certainly improve government’s expenditure prioritisation. However, certain government programmes have to be continued irrespective of their effectiveness, because of social and political considerations. It was argued that comparison with the private sector can only be done up to a certain extent, because the private sector is after profits and when profits decline, drastic measures are taken, whilst in the public sector, other factors come into the equation.

Another Permanent Secretary stated that: *“expenditure cuts during the year are carried out, in the main, in an arbitrary manner”*. The respondent is of the view that the implementation of

PB would serve two purposes; firstly, the MOF would be in a better position to take decisions which would not be potentially harmful, whilst, at the same time, effecting the required budget cuts; and secondly, the line ministries would be able to make a case for additional funding towards programmes which are delivering results.

A Director, Corporate Services, within a line ministry, stated that “*budget cuts by the MOF during the year, are a regular occurrence*”. The interviewee explained that when government comes across an issue during the year which requires funding that was not planned for in the budget estimates, such as problems with the public transport system, the MOF cuts expenditure across the board to provide for the additional funding required.

An NAO representative claimed that when expenditure cuts are carried out across the board, it could be counter-productive because a one-size-fits-all solution may not be the most appropriate. For instance, in certain departments, additional funds might be needed to enhance their effectiveness, whilst in others, expenditure cuts could be appropriate to eliminate waste of resources. The interviewee opined that there is such an intimate relationship between public funds and the economy that government has to be very careful as to how to make expenditure cuts, because such reductions could impact the economy negatively.

In contrast, a representative from the Budget Office stated that when government needs to effect an expenditure cut during the year, the MOF looks at the expenditure that has been made by each ministry till that month (by line item), reviews the commitments till the end of the year and targets those areas where an expenditure reduction would not adversely affect the departments’ operations as regards the delivery of public services. Nevertheless, the respondent acknowledged that when a ministry/department has its funds reduced during the year, its plans could be disrupted, especially where the public officials within such department

were diligent and cautious on spending at the beginning of the year, in order to save for a particular activity or to transfer funds to another line item (because of a shortfall).

A senior civil servant within the MOF argued that a budget cut across the board is totally illogical and it is, therefore, not done. He explained that the MOF monitors very closely what is happening in each area; it would know which funds are being used and for what; and it would be aware of the sensitivities in the different sectors. Moreover, the MOF keeps a history of virements (shifting of funds by ministries between line items), noting that a pattern can usually be observed in these virements – this implies that in some line items, there is an amount of funds which can be liberally reallocated. It follows that if the funds attributable to such line items can be reallocated, they can be equally cut since the programme attached to the line items will not be affected. Thus, for the purpose of budget cuts, the MOF targets line items which are the least sensitive and which, according to the MOF, contain an element of excess allocated funds. In contrast with the comments made by some of the interview participants, the respondent stated that budget cuts in salaries, education, health, social welfare and the ageing sector are never effected during the year.

A Director within the Health Ministry agreed that PB would improve government's expenditure prioritisation by highlighting programmes which are not delivering the desired results. However, the interviewee cautioned that the areas which are not giving the expected results would still require a discretionary look, because the under-achievement could mean one of two things – either that not enough resources were dedicated for the capital investment required to start reaping benefits from the programme or that the programme is a non-starter which is not having the expected effect. The point made is that lower achievement does not necessarily equate to a cut in expenditure; there has to be context analysis such that lower achievement could require either a cut in expenditure or further investment. Furthermore, the



respondent advised that one has to be careful with regard to the selection of performance indicators for the health sector, ensuring that the targets specified would not cause more harm than benefit. In this respect, the interviewee mentioned an example where one of the key performance indicators that the UK National Health Service had introduced was that the patient should not take more than a pre-determined number of hours from registration at the Accident and Emergency Unit till he/she is visited by a doctor – some managers within hospitals circumvented this indicator by asking the ambulance driver to keep driving round the block.

A Health Ministry official (within Finance and Administration) also mentioned the importance of a prioritisation exercise in respect of government expenditure, which is presently lacking. Though a budget is passed by government before the commencement of the year, the respondent spoke of his experience where throughout the year, civil servants make additional requests for funding. The respondent mentioned that unfortunately, such requests are often triggered by the politicians who ‘dream’ of new initiatives during the year. The interviewee claimed that:

*“The way resources are being allocated to the different sectors and the way the prioritisation of the budget is determined, are inefficient and ineffective. These issues stem from problems related to the current budgeting system, problems arising from the lack of an accrual accounting system and other problems including behavioural issues. There is no protocol on what one should do and on how one should act.”*

Another problem mentioned by the Health Ministry official is the fact that new programmes are introduced in the ministries’ budget under ‘programmes and initiatives’ (within recurrent expenditure); however, the old programmes are not terminated. Though expenditure reduction is a must for the Maltese government, in order to reduce the deficit, yet there is no discipline

or no political guts to terminate certain programmes. This then results in expenditure cuts being effected across the board.

When asked about this, the senior civil servant within the MOF explained that when the MOF tries to decrease the allocation attributable to a line item or when it tries to remove a line item (because it is an ‘old’ programme and initiative), some of the politicians do not accept this because of the public perception that the line item has been reduced or removed, even in cases where the funds are allocated to another line item.

The Prime Minister confirmed that:

*“Expenditure cuts are done during the year and they are carried out across the board. In truth, everyone has delivered, notwithstanding the expenditure cuts, which implies that there is a lot of ‘fat’ or waste in the system.”*

### ***Implications of underspending the budget***

All participants agreed that, currently, if a department/ministry underspends its budget, the assumption is that less funds were required than those allocated and thus, the excess funds are clawed back by the MOF. The majority of the interviewees were of the opinion that this practice is wrong because it does not incentivise line ministries to implement cost savings. In contrast, some interviewees who were/are involved in the MOF stated that it is only logical that if a department/ministry needs an amount of funds which is less than was allocated through the budget process, then the excess funds should be returned to the MOF to be used where required.

From his experience as Prime Minister, an interview participant noted that:

*“Where a department underspent its budget, the approach taken was to use the remaining funds quickly, such that the allocated budget for the following year would not be reduced. Where there is underspending on certain budget line items during the*

*year, that underspending is not reported but kept in mind to compensate overspending on items, later on during the year.”*

A Permanent Secretary mentioned that the ministries are not allowed to carry forward the balance of unspent funds from the previous year. As a result, in October/November of each year, the country goes through a ‘shopping spree’, where each ministry spends the remaining funds which would have been allocated as part of the budget process. The respondent advised that if a ministry would be allowed to carry forward to the following year a certain percentage of the unspent funds, to be used in a flexible manner by the said ministry, public officials would naturally be more inclined to spend wisely and save on expenditure. According to the interviewee:

*“The current system is penalising public officials who carry out cost savings. Furthermore, with the present system, ministries are ‘encouraged’ to spend all the allocated funds, firstly, in order not to lose the current year’s allocation and, secondly, not to have the following year’s budget reduced. This system could thus be leading to suboptimal spending decisions.”*

Another Permanent Secretary agreed that the practice of clawing back the savings made by ministries through the implementation of efficiency measures, is demotivating. It was confirmed that this system is leading to last minute spending sprees, where the expenditure might perhaps have been postponed since spending may not always be on items representing priorities. The respondent advised that savings on the previous year’s budget allocation arising from efficiencies (rather than from work not carried out) should be incentivised, with the savings being carried forward to the following year, for use by the ministry in question.

A Director, Corporate Services, within a line ministry confirmed that towards the end of the year, an exercise is undertaken to ascertain how unspent funds under certain line items are going to be spent, in order not to have the budget allocation for the following year reduced.

The respondent pointed out that unspent funds are not spent carelessly, but they are channelled towards programmes which are short of funds.

The Director from the Health Ministry also stated that the current practice whereby funds ‘expire’ at the end of the year is counter-productive. According to the respondent, the general opinion is the following: *“Why should I work so hard and improve efficiency if this would result in a lower budget for next year where I would have to deliver with less funds and at the same time I would be expected to reduce spending further?”* The respondent claimed that this practice is also applied in the case where the funds relate to strategic projects which span over a longer time-frame, say five or seven years. It was stated that it is unfortunate that the funds not spent in a particular year in respect of such projects, are lost. The respondent stated that although the framework for asking the MOF’s approval to carry forward the unspent funds, exists, the success rate of such discussions is close to zero.

Though there are instances of underspending in certain areas within the health sector, according to the respondent, this is not the case in the big health budgets, where in some cases, departments/entities start running into funding problems even by mid-year. With an ageing population and with a market which is pushing towards very expensive drugs in particular in relation to cancer treatment, the country has chronic under-funding situations in healthcare, where even if waste is reduced, the gap between what the Health Ministry requests by way of funding and what it is actually given, is huge.

A former Finance Minister stated that:

*“If a ministry underspends its budget, not only does it have to return the unspent funds to the central agency, but the following year’s allocated funds would be reduced accordingly. As a result, all ministries spend the excess funds carelessly, in order to ensure that all funds are used – this leads to an exorbitant waste of public money. This*

*practice is completely wrong – unspent funds should be carried forward to the following year.”*

A representative from the NAO also agreed that:

*“As things stand, a department which underspends its budget is penalised twice – it loses the saved funds in the current year and in all probability, the allocation for the following year would also be decreased. In the past, there have been discussions for considering the carrying forward of a proportion of the unspent funds in order to motivate departments to save on expenditure, but follow-up action never materialised.”*

The Permanent Secretary within the Education Ministry mentioned that this practice is also affecting negatively revenue generation, since some departments argue that it is not worth coming up with ideas to generate revenue because this income will go to Finance. This emphasises the need for PI, in order to decrease the dependence on the inputs and focus more on outputs and outcomes.

In agreement, an academic and advisor to the MOF stated that some ministries have got real potential for income generation, but they are reluctant to do it, because if they generate income/savings, such income would go to the MOF. The respondent suggested that if ministries underspend their budget allocation, they should be able to carry forward the unspent funds to the following year. Nevertheless, the respondent stated that this cannot be done at the moment, because Malta is under an EDP; thus, in view of this external constraint, if there are savings within the line ministries, they have to be clawed back by the MOF since government's focus is presently the deficit reduction. According to the respondent, government wants to move towards the concept of envelope budgeting (instead of going into every line item), whereby each ministry is allocated an amount of funds (according to its requirements) to be used as determined by the said ministry, provided the funds voted are not exceeded. For this concept to operate successfully, there has to be a commensurate element of

scrutiny of the results achieved; such accountability could be facilitated through the implementation of PB. At present, it is difficult to make budget allocations on this basis, because of the lack of capacity and financial expertise within the ministries, coupled with the existing deficit situation where tight control over spending has to be exercised by the MOF.

On the system of envelope budgeting, the senior civil servant within the MOF had somewhat different views. He argued that if the MOF had to give the line ministries an envelope and then leave fund allocation amongst the various line items in their hands without exerting control, the MOF would have an enormous unpleasant surprise within three months from the commencement of the year.

With respect to envelope budgeting, the Permanent Secretary for Education opined that this model could be a double-edged sword. As things currently stand, if the funds allocated for, say, salaries did not suffice, the line ministry would request the MOF to cover the additional expenditure; with a system of envelope budgeting, asking for additional funds would be more difficult because each ministry would be responsible for allocating the funds to its different requirements, provided that the allocated budget is not exceeded.

A former Prime Minister believes that the current practice of taking back unspent funds could be penalising those ministries which have been effective. The respondent recalled a case of rampant abuse in the social benefit system, way back in 1999-2000. The interviewee had introduced a computerised system whereby the ministry could connect with the banking system and verify whether a person held a bank account. It was found that 25% of the people who were benefitting from the children's allowance scheme (which was means tested), were abusing the system. The curbing of this abuse resulted in savings in government spending, running into millions of Euros. The respondent told the then Finance Minister that he

expected to have those savings allocated to his ministry for investment in other projects including the building of social housing, pointing out that the control he was going to implement was going to make him a large number of enemies which would cost him votes in the election. After lengthy negotiations, the then Finance Minister agreed to vote half of those funds to be invested in social policy initiatives. The experience recounted by the respondent implies that although the MOF has never practised the policy of allowing ministries to carry forward the amount saved in a given year or a percentage thereof, it can still happen in an informal way.

In agreement with the above comments, the Prime Minister stated that:

*“The present practice of clawing back unspent funds by the MOF, is one of the things that the government wishes to change, because savings should be encouraged rather than discouraged. The current practice is rewarding expenditure rather than savings. An output driven system, such as PB, would help in this regard, because at the end of the day, the most important thing is to achieve the output by year end, rather than to save funds at the expense of deliverables.”*

In contrast, a former Finance Minister stated that from his experience, underspending by a department/ministry is not a common occurrence, adding that if a particular amount of funds is allocated to an entity, such entity would spend the entire amount and probably, a bit more.

A representative from the Budget Office agreed that the budget allocated to departments is so tight, that nearly all the funds are necessarily spent by the departments. The respondent clarified that sometimes line ministries transfer unspent funds relating to a line item onto another item with a shortfall. Having said this, the interviewee is aware of the end of year ‘spending sprees’ by ministries, but it was stated that the MOF tries to identify such issues in order to claw back the funds before they are wasted. The respondent remarked that the

carrying forward of unspent funds by the ministries to the following year, “*is discouraged by the MOF*”.

In line with what was stated by the Budget Office official, the senior civil servant within the MOF confirmed that Finance monitors very carefully what is being spent and on what during the last three to four months of the year. Where the MOF realises that a department/ministry is trying to use unspent funds recklessly, Finance intervenes to control the situation. Having said this, the respondent noted that the majority of the allocations do not contain much waste, because a number of line items have been kept constant for a number of years, irrespective of inflationary pressures, which means that the funds allocated are being reduced in real terms. It was emphasised that should an expenditure review be carried out, only a few millions of Euros would be saved, since the majority of the budget is consumed by health, education, social welfare and the care of old people, as well as salaries. The respondent added that though a few millions could be substantial for a department, in the context of a national budget, it is a small amount and it will not solve anything.

A former Budget Office official likened the budget allocation given to line ministries to a loan facility, stating that if the allocated funds are not fully used by a line ministry, then the ministry would have ‘borrowed’ a lower amount from the MOF. The respondent argued that the budget comprises *forecasted* figures and thus, underspending is a result of the fact that the MOF cannot determine precisely what amount of funds would be needed for a particular ministry’s operations. In the event that the funds used are less than the budget allocation, returning the excess funds to the MOF should not be considered a punishment; it represents shifting unused funds of one ministry onto another ministry which genuinely requires additional funds to those allocated through the budget process. This is important in order not to upset the target deficit.



## **6.6 Pressures which inhibit the implementation of performance budgeting**

During the empirical data gathering process, a number of factors which might prohibit the change from the current budgeting system to a performance based system, were identified, as discussed below.

Former Prime Minister Alfred Sant concluded that the difficulties of modernising the public administration in Malta have persisted. *“Overmanning, structural imbalances in the technical competence of staff, weak leadership, excessive red tape, political interference...remain phenomena which it would be ill-advised to ignore in any worthwhile overview of the challenges facing the civil service today”* (Sant, 2012: 109-110).

### **6.6.1 Resistance to change**

All the research participants, without exception, envisage resistance to change from public officials, should government decide to transition to a PB system.

During an interview with former Prime Minister Dr Sant, it was claimed that change is not admired in the public sector, adding that even if there is the political will to effect change, bureaucracy might impede the process. The interviewee opined that fire fighting is usually done, with strategic change lagging behind.

According to another former Prime Minister, a PB system would highlight weaknesses in the performance of public officials and thus, implementation of such a system would be strongly resisted.

A former Finance Minister believes that should government decide to implement PB, resistance to change would be encountered “*from the first minute to the last*”.

Another former Finance Minister agreed that the reform would be resisted, stating that life for the ministries is far easier with the status quo, where money can be spent without anyone pinpointing that a particular measure has not been reached. PB would serve as a control system, highlighting weaknesses in the performance of ministries/departments; and “*nobody likes to be controlled*”.

The Minister for Education believes that resistance is unavoidable, because one would be going against a culture of inertia<sup>18</sup>.

An economist and advisor to government observed that resistance is to be expected, explaining that there is a hidden conflict between the politician and the civil service. Civil servants are sceptical of the politicians and resist changes to the systems, because from the perspective of civil servants, politicians would be in office for a limited period of time whereas the civil servants will be in office for a long time. Furthermore, when the general election is approaching, the politicians concentrate their efforts on getting elected, leaving the civil servants to carry on with the public administration duties. Civil servants are also concerned that if change is effected, it would be questionable whether they could keep the same control which they have on the present system.

A Permanent Secretary stated that from experience with previous reforms, resistance stems from a number of reasons including the following:

*“...people do not understand the new system; they are kept in the dark as to what the system involves and they have to accept a fait accompli situation with no previous*

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<sup>18</sup> Vide section 6.6.2

*consultation; and lastly, people are already working to tight schedules and view the changes as an additional burden.”*

The Accountant General claimed that resistance to change is to be expected within a large organisation such as government – the reform will bring about a change in the processes, a change in people’s mind-set, a change in legislation and a change in controls; naturally no one will be too willing to embrace these changes.

According to a Director from the Education Ministry, resistance could stem from the potential consequences of not reaching the pre-established performance targets, especially if the reason for not achieving the targets was of an economic or political nature and thus it was beyond the public official’s control.

The senior civil servant within the MOF remarked that *“there would be resistance from stakeholders because statistics could threaten certain segments”*. For example, if the indicators on absenteeism in schools were published, negative performance could be a reflection of the school management and of the country’s educational system.

### ***Mitigating resistance to change***

The need to provide training to civil servants and to have an effective communication strategy in place were identified as ways to limit the resistance to the implementation of budgetary reform, by the majority of the interviewees. Bringing in external consultants to facilitate the process, to design the system and to assist in its implementation, was also a common suggestion made by a number of respondents.

A former Prime Minister claimed that the provision of training to public officials as well as introducing new blood is important for the implementation of change. He further commented that organisational change has to be managed through people and in his opinion, consultants

should be brought in to assist in the reform process, emphasising that the consultants have to be part of the team and the change process.

Another former Prime Minister advised that the system should be designed in such a way that the weaknesses and underperformance are highlighted earlier on in the year, such that corrective action could be taken in good time.

According to a Permanent Secretary and an economist and advisor to government, to achieve change, political leadership is needed. These political leaders should take the civil servants into their confidence and propose to implement the change together, because the politicians cannot do it on their own and the civil servants have no interest to change since they are comfortable with the status quo. Although the politician can have good intentions, ultimately the implementation is in the hands of the civil servants who are very resistant to change; and thus, unless the politician ‘carries’ them with him/her, the policies will be shelved.

A representative from the NAO agreed that an effective communication strategy is fundamental, adding that the provision of training is also crucial. The citizen is in favour of enhanced accountability – knowing how taxpayers’ money is being spent. Thus, if the public administration emphasises that through the introduction of PB, accountability and public resources management will be improved, this reform would enjoy the support of the general public.

A Director from the Education Ministry stated that:

*“One way to mitigate resistance is to have the possibility of revising the goals during the course of the year, should circumstances change. For example, if a budget cut is effected by the MOF during the year, the performance targets would need to be revised downwards accordingly.”*

According to a Budget Office representative, though resistance to change is inevitable in the public sector, if the departments appreciate the usefulness of the new budgeting system, they would show more willingness to implement it. If civil servants perceive the system as being in their interest, it might be ‘sold’ to them; otherwise, there will be resistance as the system would be viewed as an additional control and as a tool to increase accountability for their performance.

A former Finance Minister believes that notwithstanding the resistance, the implementation of PB is possible, if government decides to implement it and dedicates the necessary resources for its implementation, including recruiting the right people in the ministries. The respondent mentioned that when government had decided to modernise its IT system, it had placed an IT chief officer in each ministry. In the same way, in order to carry out the budgetary reform, there should be a chief accountant with the appropriate competences in each ministry, responsible for the implementation and on-going operation of the system. It was also mentioned that, realistically, external consultants would have to be involved for the implementation of PB – ideally, these consultants would have implemented the system and seen it working somewhere else, thus having the required experience to design the Maltese budgetary reform.

The Prime Minister’s view is that:

*“Resistance could be addressed if there are rewards which are linked to the achievement of targets (carrot and stick approach). Furthermore, if the implementation of the budgetary reform is to succeed, people have to be convinced that the gauge being used to measure an individual’s performance is just. If the system is to be accepted, civil servants have to be comfortable that the system is fair and the performance targets established are realistic.”*

According to another former Finance Minister:

*“There is no way to mitigate such resistance; in order for this fiscal discipline tool to be introduced, there have to be powerful people at the top who impose the new system. It is important to understand that when these types of processes are introduced, one would be introducing control points throughout, including control over the line ministers; and not everyone appreciates controls. Thus, the implementation of PB requires strong political commitment from the top such that the system would be imposed on the politicians and on the civil servants. These two groups of people will resist these types of controls because everyone prefers to have a free hand in spending, with absolutely no accountability. This reform is definitely needed and should be implemented in the local context; however, if it is to happen, there has to be the will to ‘bulldoze’ over people.”*

## **6.6.2 Personnel issues and organisational structures**

### ***People***

There was general agreement amongst the respondents that there is a lack of suitably qualified civil servants within the ministries. It was claimed that unless government employs more qualified staff, including accountants and economists, it would be difficult to embark on a budgetary reform.

#### Human resource capability

A Permanent Secretary claimed that government lacks the human resource capability, unlike the private sector which can recruit the best people to get the required results.

A former Minister for Finance opined that the biggest challenge for the implementation of PB is not the availability of an accounting and IT system (as the general opinion seems to be, in the respondent’s view), because this can be procured and implemented; but it is the people – the knowledge and the culture. As regards knowledge, the ‘accountant’ in the ministries/departments, who is referred to as the Director, Corporate Services, does not necessarily have an accounting qualification. Though, by time, these people would acquire the experience, they would still lack the theoretical foundation. The participant opined that the

Director, Corporate Services should be a qualified accountant, mentioning that when he had made this proposition (when he was in office), he had always found resistance from the civil servants and from those around him. In reality, it is very difficult for government to attract accountants; though in the previous legislature, government reformed the salary structures such that accountants would get a better remuneration package, it is still impossible to compete with the private sector, even because in Malta, there is already a shortage of accountants in the private sector. The interviewee claimed that if “*one pays peanuts, then one cannot expect to employ high calibre people*”. Unfortunately, there are union issues, such that if the disparity between civil servants’ salaries is substantial, pressure would be exerted upon government, by the unions, to increase salaries throughout, creating a ripple effect on government salaries. Thus, in the interviewee’s opinion, the lack of knowledge has always hampered the possibility of introducing PB.

In agreement, the Budget Office official stated that the main challenge for augmenting the staff complement and enhancing the accounting expertise within government is the fact that people, especially accountants, are paid more attractive salaries in the private sector.

The senior civil servant within the MOF stated that though every ministry has a Director, Corporate Services who oversees the finance function, this function is not very strong within some of the ministries. However, according to the respondent, even if government employs the best people and the best accountants, though there will be improvement, there will not be structural changes in the makeup of the national budget, because structural changes in the budget will only happen if policy stances in the high spending sectors are changed.

### Embedded culture

A Permanent Secretary mentioned that given that the people in the Budget Office have been in the division for a long time, it would be more difficult to change the embedded culture and implement changes.

According to a former Finance Minister, the cultural aspect might inhibit change because people, naturally, do not like to have their performance measured. Therefore, a huge political commitment is required in order to overcome the various excuses put forward by civil servants, as to why budgetary reform should not be undertaken.

In this respect, an academic and advisor to the MOF commented that it will take time for people to accept a new way of doing things. With the current budgeting system, an incremental approach is adopted, such that if a ministry was given an amount in a particular year, they would expect the same amount plus something extra to cover for inflation in the following year. According to the participant, the incremental approach assumes that everything is perfect and it does not allow for review or measurement of performance.

The Director within the Ministry for Education noted that when attempts to introduce some changes are made, there would be civil servants who ‘accuse’ the change implementer that he/she does not know what he/she is doing, given that a particular practice had been in place for a number of years, adding that if a change is effected, there could be negative consequences. The interviewee mentioned how difficult it is to get people to attend courses, even if such courses are organised during office hours and they are free of charge for the employees. This was confirmed by another Director, Corporate Services within another ministry who also mentioned the lack of interest and motivation on the part of certain civil



servants, adding that the attendance at certain courses should be linked to the career progression of the individual.

A Health Ministry official spoke about certain cultures being strongly ingrained, mentioning healthcare professionals who are not used to measuring outputs. This was also confirmed by the Director from the Health Ministry, who stated that the culture of data capture or record keeping is not always in place, in the case of a healthcare professional because for him/her, if, for example, a patient needs to be vaccinated and a form to this effect has to be filled in, the vaccination will get priority and not the form filling. Many times, the healthcare professional does not realise that if the form is not filled in, it may appear that the work was not carried out, or in a worse scenario, if the vaccination given is not captured and the patient gets another one, there may be serious repercussions.

#### Low salaries for top civil servants

The academic and advisor to the MOF spoke about the issue of low salaries for top civil servants in Malta, drawing comparisons with salaries paid in the UK and with the salaries paid within the Maltese private sector. The Permanent Secretary in Malta, who is the highest ranking civil servant, is paid a salary of about €42k<sup>19</sup>; in the UK, the Permanent Secretaries receive a salary of about £180k (equivalent to around €250k). In addition, whilst people at a lower salary level (in the private sector) have comparable salaries with employees in the public sector in Malta, there are huge divergences in salaries in the case of people in high ranks. This makes it very difficult to recruit the best people for top positions in the civil service.

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<sup>19</sup> In this regard, the average annual basic salary of employees for the second quarter of 2015 was estimated at €16,406 in Malta. This amount refers to the annual basic salary and excludes extra payments such as overtime, bonuses and allowances (National Statistics Office, 2015b).

A Permanent Secretary also mentioned the tension between the private sector and the public sector vis-à-vis the employment of accountants and financial controllers, referring to the fact that the package offered by the private sector is very high compared with that offered by the public sector. It was explained that the public administration has looked at innovative ways which avoid skewing government salaries. For example, the Health Ministry had found a way out by recruiting financial controllers through the Foundation for Medical Services (which is a public entity responsible for delivering healthcare infrastructure) and then placing such people within the ministry's other entities. As a result, the Health Ministry has a network of financial controllers who receive a package that is more generous than that paid to accountants employed directly by government. The interviewee opined that if this was the way to try to make healthcare more sustainable, then it was worth the investment. Unfortunately, it was stated that there is a high turnover of these people.

#### Career prospects and training in the public sector

Former Prime Minister Dr Sant refers to career development issues for employees in the public sector. He states that *“it is difficult to find an ex-colonial country anywhere in the world with a consistent record of meritocracy in its public sector recruitment and promotion. The public sector provides the scope for a spoils system that helps parties to cement their political ties with supporters”* (Sant, 2012: 112). Furthermore, he observes that *“advancement in the ranks of the public service, even when meritocratic criteria are observed, has been extremely traditional in scope. To achieve a relatively high executive position in the service, one must expect to be much older than for comparable posts of responsibility in the private sector”* (Sant, 2012: 113). These issues highlight the challenge of finding the right people with the right skills and expertise to spearhead the budgetary reform.

The Minister for Education observed that training to people in different ranks within the civil service has not been adequately provided. He stated that though some civil servants have been exposed to some form of training in management, leadership and administration, such training has not been continuous and there are a lot of self-taught elements. For example, in the education sector, a person could be a good teacher or a good Head of School, but then when he/she moves up the ranks, he/she would come across tasks that are not strictly of an educational nature, but which constitute administrative, managerial, leadership or financial administration tasks. The Minister observed that in the education sector, the country has not invested in education planners or in education administrators. The Minister pointed out that this does not mean that there are not competent civil servants, but such people are competent “*not because of the system, but in spite of the system*”. It was also stated that these constraints are a common issue for all small countries, where people have to wear different hats. Notwithstanding, the Minister believes that there should be a better plan for human resource development.

### ***Structures***

According to the Accountant General, when it comes to budgeting and budget execution, the proper set-up is lacking, both within the MOF and also within the individual ministries. Referring to accounting, the respondent remarked that some of the line ministries do not even have a proper finance set-up – they are too much inclined to push projects, but in respect of the finance side, planning is lacking and reliance is made on the central agency. It was also mentioned that a number of ministries do not employ a single accountant! Thus, unless the public administration acknowledges this issue and strengthens the finance function within the line ministries and centrally, it would be very difficult to implement the desired reform.

In agreement with the above comments, the academic and advisor to the MOF mentioned that a number of line ministries do not even have a finance officer or a budget team, thus the budget process is very much centralised because the MOF is the strongest ministry in respect of financial expertise. The respondent also remarked that unless there is a budget team within each line ministry whose members talk in an integrated way to each other, each department/division within the ministry would look after its interest, making a demand for a higher budget allocation. As a result, each Permanent Secretary would then aggregate all the requests and send the business plan to the MOF, who would then have to make the necessary downward adjustments to the figures requested.

### **6.6.3 Lack of resources (IT systems, time and financial resources) and bureaucracy**

The Accountant General remarked that the implementation of reform takes a lot of time and resources; considering that government is currently in the process of moving towards accrual accounting, implementing budgetary reform on top of that, could be difficult.

Investment in an accounting and IT system is required if government decides to transition to a performance based budgeting system, according to a Finance and Administration official within the Health Ministry. The respondent explained that different entities within health use different accounting systems (such as Access Dimensions and Shireburn), leading to problems of interfacing. Some of the departments within health still rely on Excel, even for producing reports, which is rudimentary, in the interviewee's opinion. In agreement, a former Finance Minister stated that the existing accounting and information system, which is a modified version of SAGE, is not adequate to support a move towards PB. A Permanent Secretary remarked that the existing accounting system is an old system, which is not user-friendly,

which does not produce enough reports and which makes it difficult to manipulate information for the purpose of producing ad hoc reports as required. It was noted that there are, however, plans under way to change the current system.

Coming from the private sector, the Health Ministry respondent noted that one of the odd things that he has witnessed within government is the slowness of the pace to move in terms of decision-making, claiming that things move at a much faster pace in the private sector, once approval from the Board of Directors is obtained. One of the reasons for this could be that a number of roles are spread across diverse departments, and thus decision-making inevitably takes longer.

#### **6.6.4 Political factors**

According to a Permanent Secretary, using PI to hold public officials responsible for the actual performance of their department, could be an issue, in view of inherent political forces.

The interviewee argued that:

*“A public officer cannot be held completely responsible, because in order to hold someone responsible, he/she needs to have everything in his/her control. For example, does a public officer have a free hand to transfer people around if he/she believes that better results could be obtained from such a transfer? Or are there other forces which disallow the transfer of people around to improve performance?”*

An Education Ministry representative mentioned the frustration felt when after spending a number of months compiling tables and figures as part of the annual budget process, this work is overridden by a political decision. An example mentioned was the summer school initiative launched by the Education Ministry, where it was decided to open 29 centres till 5pm for five days a week – because of the huge demand for such services from the public, this decision gave rise to a substantial increase in salary bills and a significant investment in resources

required to occupy the kids during the summer months. Once the expenditure is committed, the finance section would then have to find the funds by decreasing expenditure on another item.

An NAO representative observed that in Malta, it is difficult to cut the staff complement within government because the unions would turn against government, and therefore, the politicians have their hands tied. This issue was also mentioned by a Health Ministry representative who stated that there is a strongly unionised environment within the Health Ministry, including doctors' union and midwives' and nurses' union. The same problem was referred to by the Director within the Education Ministry, who mentioned the issue of the extremely low pupil-teacher ratio in Malta and argued that there is not much that one can do in the public sector, if there is surplus or untrained staff. The pressure exerted by the Malta Union of Teachers is tremendous, with the union getting involved even if the ministry takes too long to pay a person, let alone if that person is made redundant.

The Permanent Secretary within the Ministry for Education noted that personal emoluments make up the largest percentage of recurrent expenditure in the Education Ministry. Unfortunately, politicians are hesitant to change certain practices because of potential political damage; such practices could be costing government a substantial amount of yearly expenditure. The interviewee claimed that unless there is a plan on how to utilise human resources more effectively, the expenditure cuts that can be carried out are very limited.

Former Prime Minister Dr Sant (2012: 112) confirmed that at times, instead of shedding its excess load of personnel, the state “*retained its former load of personnel and financial obligations, while assuming additional ones to cope with the tasks of supervision and regulation*”.

Another former Prime Minister argued that there could be huge political issues, should government decide to publish the actual results or outcomes achieved. If the actual performance is good when compared to the budgeted targets, then no issue arises; however, if the funds being voted for the various programmes are not giving the best possible results, then government's effectiveness might be put into question. In the respondent's opinion, a massive culture and mentality change is required if performance budgets are to be introduced. Furthermore, there is the issue of the use of this PI by the Opposition party. Though, in principle, one could argue that government should not shy away from a performance based report because such report could pinpoint where corrective action is required, in reality, this tool could serve as a very powerful tool in the hands of the political adversary for criticising government. The interviewee mentioned that in spite of Malta having made significant political and economic progress, issues are still very much politicised. Thus, though from a purely technical point of view, there is no doubt that the best budgeting system is one which is performance based, from a political perspective, if the potential negative political fall-out is not addressed, the reform will not go through. It was suggested that parts of the reports could remain internal and not be published, though it is difficult to withhold information, especially in a small island like Malta, where everyone knows everybody else.

A Permanent Secretary agreed that there is an element of political sensitivity and risk, should actual PI be made public. However, she referred to the present government's commitment to enhance transparency in government's financial undertakings and to ensure that things are being delivered. If government publishes information on performance targets, which are then not achieved, and an explanation is given as to why the pre-established targets were not reached, there is no shame in that. The Permanent Secretary added that the public administration would surely appreciate having its efforts acknowledged, through the

publication of PI. Above all, government is using public funds, and accountability and transparency are the salient principles in public expenditure.

### **6.6.5 Other issues**

#### ***Why has performance budgeting not been implemented?***

In view of the fact that both a former Finance Minister and a former Prime Minister pronounced themselves in favour of the implementation of PB during the respective interviews, they were asked why this system had not been implemented during their term in office.

The interviewees replied that during one of the legislatures, the primary project was the adoption of the Euro, which necessitated meeting the fiscal targets stipulated by the EU. This was a huge project and absorbed all the energy of the MOF. Thus, it was definitely not the right time to reform the budgetary system. In 2008, the financial crisis hit the world and the MOF had to focus on mitigating the effects of the global crisis. The financial and economic crisis brought about huge risks, including risks that some of the factories in Malta might close down. At that point, the circumstances did not allow government to experiment with a new budgeting system, when the country was trying to adjust to the adoption of the Euro; it was trying to adjust to the fact that the Eurozone was in crisis; and it was adjusting for the liberalisation and reform issues in various sectors.

The former Finance Minister also mentioned that the staff complement within the MOF at the time, required a drastic change. Though the Permanent Secretary within the MOF had started to change some people and recruit new staff, at the time, government was not seeing the urgency to reform the budgetary system. The respondent observed that to implement PB, there



is the need for will power and having key people in place; it was implied that government at the time was not willing to recruit a chief finance officer in each ministry and thus, the reform could not have happened.

***Should a budgeting system which has served the country for years be changed?***

It was stated by the Prime Minister that the current budgeting system, with all its inherent weaknesses, works; thus, one of the greatest fears of changing the system is that something which has served the country for years, is destroyed. The argument of those who want to maintain the existing system is that with the current system, the people in charge of the process know exactly how to pull the ‘right strings’ if immediate action is needed. These people argue that if a new budgeting system is introduced, it might be more difficult to take immediate corrective action if an unexpected event crops up.

The Prime Minister explained that:

*“The existing system is totally people centred, in the sense that there is a very small hard core group of people (not more than ten public officials) spread across the ministries, who know the system inside out and who are capable of manoeuvring it. This knowledge and experience has saved the situation a number of times, both within the present government and also in the previous administration. The current system is flexible and can adapt without involving a lot of people. Through their long-standing experience in the budgeting process, this group of people would know which ministries are asking for more funds than required and would take action accordingly.*

*On the downside, this also means that the existing system is extremely vulnerable, because it is not a system, but it is a group of people. Thus, if something happens to this group of people, the system will collapse, because the system does not exist.”*

## **6.7 Implementation strategy for performance budgeting**

This section starts off by considering whether the existing line-item budgeting system follows the top-down or the bottom-up approach, from the viewpoint of the interview respondents. Subsequently, it sets out the opinions of the research participants regarding the

implementation approach to be adopted for PB in the local context. Next, it seeks to highlight the potential salient issues surrounding the implementation of PB in Malta.

For the purpose of this discussion, the ‘top’ represents the central agency, namely the OPM and the MOF; whilst the ‘bottom’ consists of the line ministries including the departments and agencies falling under their responsibility.

### **6.7.1 Is the *existing* budgeting system top-down or bottom-up?**

When asked whether they consider the existing line-item budgeting system to be based on the top-down or on the bottom-up principle, different views were put forward by the respondents (as detailed in Table 32). The majority of the respondents stated that the existing system is based on the top-down approach, with priorities being politically set from the top and fund allocation being determined centrally. A number of interviewees tended to disagree, opining that the system embraces both the bottom-up and the top-down perspectives. In contrast, a couple of participants view the current system as being based on the bottom-up approach.

**Table 32: Respondents’ views on the existing implementation approach**

Top-down views
<p>According to a Permanent Secretary, the current budgeting process largely follows a top-down approach. In agreement, the Accountant General observed that the budget process starts off with the ministries/departments submitting their business and financial plans along with budgetary estimates based on their ministry’s programme. This is then followed by discussions between the MOF and the line ministries, in order to determine the priorities for the listed initiatives. The budget allocation is, in the end, determined by the MOF taking into consideration the overall fiscal targets. Another Permanent Secretary added that <i>“finally, the decisions are taken centrally and the line ministries do not really have a say in the budget allocation ”</i>.</p>
<p>A representative from the NAO stated that though there are bottom-up inputs (the line ministries providing their suggested figures), at the end of the day, the budget process is basically top-down, as it should be, with the final allocation decisions lying with the MOF. It is imperative that the MOF prioritises the ministries’ expenditure; otherwise the fiscal deficit would shoot up.</p>
<p>In the opinion of the Director at the EPD, the current budgeting process follows a top-down approach, with a spending ceiling being stipulated. The Fiscal Responsibility Act mandated this fiscal discipline tool, laying down consequences where a ceiling set by the MOF is exceeded by the line ministries.</p>
<p>According to a former Prime Minister, the adoption of the top-down approach could be a result of the country’s EU membership, whereby government has to operate within the parameters laid down by the EU, including the targets stipulated for the fiscal deficit. The <i>“tug of war”</i> between the line ministries for obtaining additional funds necessitates the involvement of the central agency such that an optimal decision on programme prioritisation would be arrived at.</p>
<p>A representative from the Health Ministry explained that in view of the fact that the country’s budget is subject to the EU Commission’s scrutiny, central intervention becomes fundamental to ensure that the country’s priorities are being addressed.</p>
<p>Another public official from the Health Ministry observed that although the line ministries compile their own financial plans, the decisions are ultimately taken centrally. It was claimed that much of the results of the bottom-up process are rejected. According to the respondent, this approach is necessitated by the requirement for meeting the fiscal deficit threshold.</p>
<p>The Permanent Secretary for the Education Ministry remarked that the budget compilation is a two-way process; however, at the end of the day, the decisions are taken at the top. The respondent understands the circumstances and constraints faced by the MOF, adding that at the end of the day, someone has to decide for the whole country. It was claimed that sometimes the proposals made by a line ministry might not make sense and thus, the central agency has to adjust the figures.</p>

### Bottom-up views

In the opinion of an economist and advisor to government, the existing budgeting system is “*completely bottom-up*” and it should be top-down, because the government has been democratically elected, it has a programme to accomplish, it is accountable to the electorate, and the budget is one of the major measures for the implementation of the pledges made to the electorate.

Agreeing with this view, a former Finance Minister stated that although the final decision on the budget allocation is centralised, the individual amounts expected to be spent by each ministry/department are determined by the line ministries, whose focus is on what funds could be obtained for their spending, rather than on what results will be delivered through the expenditure made. Within this scenario, the MOF then negotiates with each line ministry the actual percentage increases over the previous year’s budget that will be assigned to the respective ministry.

According to an academic and advisor to the MOF, the current budgeting system is incremental and bottom-up, with the line ministers requesting the same budget allocation as was given the previous year, plus something extra to cover for inflation.

### Combined perspectives

The senior civil servant within the MOF considers the current budgeting system to be based on a mix of the top-down and bottom-up approaches, whereby the line ministries compile their business plans and the MOF establishes the spending ceiling. Having said that, when the MOF detects situations of misallocation of funds by the ministries, it intervenes, in order to avoid the risk of having the ministries shifting funds allocated to salaries onto other programmes and then requesting additional funds from the MOF to cover the salaries, which have to be paid in any case.

The Director within the Education Ministry opined that, to a certain extent, the line ministries have some decision-making roles in the budget process, because the financial plans submitted by the ministries are taken into account by the Budget Office, when making the budget allocations. The process is as follows: the line ministry requests an amount of funds and submits the plans of how that money would be utilised; then the MOF would usually allocate a portion of the requested amount. The respondent emphasised that the final decision on the fund allocation rests with the MOF. However, it was stated that where the funding allocated was too tight for implementing a particular programme, the Education Ministry had the opportunity to highlight this issue and the MOF did listen to them.

Referring to the 2015 budget compilation process, the Education Minister stated that he felt it was more of a partnership between the Education Ministry and the MOF. The Minister mentioned his involvement in a number of meetings and discussions and stated that a week before the budget was publicly presented, he was given a draft of the budget allocation earmarked for his ministry, which remained unchanged in the final version of the budget.

In the Prime Minister’s view, the system combines both the top-down and bottom-up approaches: the MOF is fed the requests for funds from the line ministries, but then, at the end of the day, if there is the need to cut expenditure, the decision lies with the central agency.

*Source: Interview data collected between August 2014 and April 2015*

***Further observation***

An interviewee, who used to work in the Budget Office for a number of years and who used to be present during the budget negotiation meetings between the Minister for Finance and the respective line ministers, recounted his experience, stating that when the MOF is allocating funds to the respective ministers, the human factor plays a very important role. Whilst some of the line ministers would accept their share of the budget allocation without further discussion, there were cases where a lot of friction and tension was felt during the negotiations, with ministers walking out of the meeting with the MOF. The respondent mentioned a former minister (who practised the profession of a lawyer) who used to be very well-prepared for the budget meetings and who could make a case for additional funding even if in reality his arguments were inadequate. The interviewee, who has worked under the responsibility of four former Finance Ministers, added that the personality of the Minister for Finance also plays an important role – when the Finance Minister has a strong character, it is easier to put his foot down when additional funding is requested by the line ministers.

**6.7.2 Top-down versus bottom-up approach for performance budgeting**

The respondents were asked whether they advocate a top-down or a bottom-up approach for the implementation of PB in the local scenario. In the main, respondents were of the view that the implementation approach should embrace a mix of both perspectives, perhaps tending towards the bottom-up approach. It was, however, noted that central involvement is still required, especially within the existing cultural framework of the country.

The economist and advisor to government opined that the implementation approach for PB should embrace both the top-down and bottom-up perspectives. From a top-down view, the budgetary framework should be approved by a Cabinet decision which would then be

cascaded down to the MOF and to the line ministries, providing a framework within which financial plans would be subsequently developed. The line ministers would then develop performance targets and measures for their ministries/departments (bottom-up). In turn, the MOF has to be armed with sufficient information, in the form of international benchmarks and sources, in order to be in a position to challenge certain assumptions made by the line ministries.

Agreeing with a combined approach for the implementation of PB, the Budget Office representative maintained that the ministries/departments should be responsible for compiling their business plans and for developing their performance measures and targets, in order to ensure ownership from their end. Subsequently, the central agency would assess whether the targets are reasonable, giving its approval or proposing adjustments.

A representative from the EPD added that whilst the top-down view is fundamentally important because the spending ceiling has to remain, the bottom-up perspective (at the line ministry level) ensures that the established spending ceiling is credible and realistic. Thus, if after implementing all possible efficiency gains, the spending ceiling is exceeded, this would indicate that there is a problem which has to be financed, either through a revenue measure, an expenditure measure or through the reduction of spending by another ministry.

According to a former Prime Minister, the ideas should emanate at the level of the line ministry (bottom-up). For example, in social policy, it is the social workers who can indicate to their superiors what the social priorities are. In turn, the top public officials will design programmes which embrace the social priorities identified. Such programmes are then translated into financial plans and performance measures and submitted to the minister in charge. The minister (with a packet of initiatives which is expected to cost, say, €100 million,

but with only €50 million available for spending) would have to prioritise the programmes – these decisions should then be made hand in hand with the Finance Minister and the OPM. The involvement of the latter would ensure that the decisions taken are based on government's priorities.

According to the Accountant General, if PB is to be implemented, the existing top-down approach would have to change. The MOF would have to engage more with the line ministries. It should perhaps allow line ministries to manage their budgets but be in a position to apply sanctions if the pre-established performance targets are not reached (unless there is justification for not delivering what was expected). The MOF should determine the amount of funds to be allocated to each line ministry and then the ministries would use their discretion for distributing the money amongst the projects, ensuring that the envelope given is not exceeded. The role of the central agency should be focused on issuing budget guidelines and monitoring what the ministries are doing, rather than going into detailed analysis of every line item in the budget.

According to a former Finance Minister, the proposed PB system has to follow the bottom-up approach, because, ultimately, the budgets and performance targets have to be compiled by the respective department/ministry (as is the practice in the private sector) and then consolidated into one overall budget. The respondent clarified that the policies and projects would still be determined centrally. An academic and advisor to the MOF added that the ministries will subsequently be judged by the central agency on the attainment of the performance measures that they would originally have come up with.

A representative from the NAO cautioned that given the culture in the local context, the implementation of a PB system would still require central intervention. Though the ministries

would be responsible for compiling both the draft financial plans and the performance targets, the MOF should have the final say in budget allocation. Another NAO official referred to a process of decentralisation which was undertaken in the past, whereby line ministries were allowed to shift funds between certain line items without getting approval from the central agency. The respondent claimed that the result was not very positive, because decentralisation was implemented without a corresponding amount of accountability. Another issue raised was that given the fiscal deficit problems faced by the country, the top-down approach could be more appropriate for exerting control. A third representative from the NAO mentioned that, in the past, there have been attempts to move the recruitment away from the control of the OPM; however, when the central agency relaxed its control, the departments/ministries got carried away and then, once new recruits were employed, they remained on the government's payroll. The respondent claimed that if there is a move towards decentralisation, proper structures would have to be created in order to regulate and to monitor; otherwise, chaos will reign.

In conclusion, with the implementation of a performance based system and the corresponding inclusion of PI in budgets, the shift from the current top-down approach to a combined approach (tending towards the bottom-up view) appears to be possible. This is because if pre-established performance targets are set, which are then compared to actual PI, it would be easier for the central agency to exert control and to ensure increased accountability on the part of the ministries and departments.

### **6.7.3 Championing and project leadership**

The interview participants were asked whether they expect anyone, at the top politically, to champion this reform. A further question posed sought to identify who should act as project manager/leader for PB implementation.



As regards championing of the reform, there was general agreement between the respondents that it is fundamentally important to have the people at the top supporting the vision to move towards PB. It was claimed that political ownership will push the reform to happen and will ensure that it is carried out faster from a timing point of view. The majority of the respondents stated that if the reform is to happen, the Prime Minister has to act as champion for it. In this respect, a former Prime Minister stated that from his experience, when an initiative is backed by the OPM, the line ministries will cooperate much more. As an example, during the period between 2004 and 2008, government was striving to meet the Eurozone targets and it was decided that the Prime Minister should take up the role as Minister for Finance. This resulted in much more coordination and cooperation from the line ministries and departments. At the end of the day, the OPM has the power to nominate or remove a person from a ministerial role and thus, when instructions are issued from the OPM, they are followed more diligently.

Another view put forward was that the MOF should champion the reform, but with clear and full support from the Prime Minister.

With respect to project leadership for the implementation of the budgetary reform, the MOF was identified by all respondents as the most appropriate candidate to manage the transition. This is because the MOF is responsible for the budget preparation, with the budget being the main reason why the MOF exists. Furthermore, the MOF has the experience, expertise and institutional knowledge of the ministries and the budget process. It was mentioned that the MOF should have the overall management role, and then there should be a project leader within each ministry to coordinate with the central agency. At ministerial level, the project leaders should be the Permanent Secretaries, guided by a technical person (an accountant) and then, at a lower level, the Heads of the Departments should also be involved in the project management for the system implementation. It was, however, stressed that unless there is the

strategic backing and drive from the OPM, the reform will not work. Clear support is also required from Cabinet, in view of the many competing claims for funds between the ministries.

#### **6.7.4 Reporting**

##### ***Budgeted versus actual performance information***

The responsibility for carrying out a comparison of the actual results with the budgeted PI and for checking whether the performance targets have been reached, should vest within every ministry, according to the interviewees. Following that, the MOF would then request such information from the ministries in order to analyse whether the allocated expenditure is delivering value. It was suggested that the reporting of the actual performance targets reached should be disclosed with the following year's financial estimates.

##### ***Performance audit reports***

In the main, respondents opined that the carrying out of performance audits in relation to the quality and coverage of PI should be under the responsibility of the NAO, which is an independent body and which is the external auditor of the civil service. Alternatively, a Quality Assurance Unit could be set up, possibly under the NAO's remit, to oversee this process. It was proposed that each ministry would be reviewed, say, every four years. With fourteen ministries, three or four ministries would be audited every year. To facilitate the audit process, it is important for the ministries to have good documentation on performance and to fill in various forms, which are then submitted to the NAO for its scrutiny. This body could also provide guidelines to the ministries on how they will be inspected in order to ensure transparency.

A respondent was of the view that the NAO's oversight will not suffice for exerting control on a regular basis. In this regard, it was suggested that each ministry should have an internal audit function (currently, the only internal audit function is within the OPM and it is more related to EU fund issues) for compiling performance audit reports and for reporting on other matters including risk factors surrounding the department and its internal control systems. The internal audit function within each ministry should ultimately be responsible to the MOF, rather than to the respective minister (as is the case in a private company where internal audit is responsible to the Board of Directors and not to management).

An alternative idea put forward by another interviewee was that the review should take the form of a management audit (assessing whether the procedures in place are leading to the achievement of the deliverables) and it should be carried out by the MOF or the OPM. According to this respondent, the NAO, which is responsible for scrutinising governance, is to be kept separate from this.

Some respondents suggested that another body which could take up this audit role is the Fiscal Council.

### **6.7.5 Other matters**

#### ***Type of performance budgeting***

When asked about the type of PB which is most appropriate for the local context (presentational, performance-informed or direct), the majority of the participants claimed that it is best to start off with presentational PB. Given that the introduction of PB necessitates a culture change in the way public officials think and operate, government should start with the first level of PB in order for the civil service to transition to this system in an incremental

manner, and then build up confidence and cooperation before implementing performance-informed budgeting. The interviewees observed that the presentation of more information in budget documents is always better than providing less information, as long as it is good and non-biased information. Furthermore, from a political perspective, the presentation of performance and outcome information justifies government's expenditure and informs the public as to what has been achieved with the taxpayers' money.

Another argument put forward for adopting presentational PB was that there should not be a tight link between performance and allocations, because if a department sets a target which is then not reached, it does not follow that the budget for that department should be reduced, in view of the fact that the said function could still be an important public service and a priority for government. It was also argued that quality should not be sacrificed, in order to achieve the targets/measures.

### ***Reform enacted in law or through policy guidelines***

There were diverging views from the respondents with respect to whether the budgetary reform should be enacted in law or by means of policy guidelines issued by the central agency.

A few respondents were of the opinion that the reform should be enacted in law, stating that though there is no difference between enactment in law and through policy guidelines as regards the operational aspect of the system, the difference becomes important when it comes to monitoring and the consequences if the law/policy is not adhered to. The deterrent of the consequences if one breaks a law rather than a policy is stronger; thus, the probability is that if the reform is enacted in law, a better result will be achieved with less monitoring.

The other viewpoint which was supported by the majority of the interviewees was that it is not necessary to legislate in respect of the budgetary reform. Instead, the reform should be implemented through policy guidelines issued by the MOF. A respondent added that:

*“Things are not changed by simply legislating and it is mistaken to assume that because the law has been changed, the reforms will be implemented. In truth, it is the people and the policies, and the people implementing those policies who can bring about the real change.”*

In agreement, another interviewee stated that:

*“The reform will not succeed just because it is enforced in law, but it will only succeed if government believes in the system, if there is cooperation at line ministry level, if the reporting is genuine and if there is objectivity – these fundamental elements for the success of the system will not come about if there is a law, but if a cultural change happens.”*

According to another interview participant, the main challenge for implementing PB is in terms of resources, because the majority of the ministries do not have the expertise required for the operation of this system – this is possibly why it is taking time for this reform to materialise. Thus, it would be premature to legislate at this stage, because the worst thing that could happen is to legislate when the required resources are not available since this would undermine the whole process.

Asked whether legislating would ensure permanence of the budgetary reform, it was claimed that if there is a change in government and the new administration sees that the system is working, there would be no benefit in dismantling it. The new politician would change the priorities, but within the existing tool.

### *Timeframe for implementation*

The views of the interview participants were sought with respect to the suggestion of a reasonable timeframe for the successful implementation of PB across central government. There were mainly two views in this respect; some respondents suggested that a long timeframe, in the region of ten to fifteen years, is required, whilst other interviewees mentioned that implementation is possible within a three to five year timeframe.

A number of respondents opined that the implementation could take a considerable number of years (possibly 10 to 15 years), because substantial effort is needed prior to implementation in order to prepare the system and then, more importantly, to educate and train the people involved. This suggested long timeframe stems from the fact that the reform will affect all government ministries and departments and furthermore, ministerial portfolios and people change over time making implementation more complicated. In agreement with this, the Accountant General compared a possible budgetary reform with the current accrual accounting reform, which is still on-going<sup>20</sup>. Thus, using the same measure, the implementation of PB might take decades, according to the Accountant General.

In contrast, some respondents mentioned that a three to five year period could be reasonable for the implementation of PB. It was stated that if government is serious about the reform, it should not take longer than this to implement; otherwise complacency will set in, with the people being satisfied with what has been accomplished up to a certain point and failing to put in extra effort to achieve the next milestone. Furthermore, if the momentum is not kept, people's morale would suffer and there would be changes in the ministries and their

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<sup>20</sup> The Accountant General stated that government had voiced its intention to implement the accrual accounting system way back in the 1990s; presently, the Treasury Department has arrived at a point where it has a very clear vision as to the way forward, but it is still at the beginning of the implementation process and it is aiming to have the first dry run (compilation of consolidated accounts) in 2019 or 2020.

portfolios, making the whole project more complex. Thus, it is important to have a project with a clear road map and clear timelines for implementation. Another point mentioned was that the timeline of the project would also depend on the quality of the people involved in the implementation.

In agreement with this, an interviewee suggested that government has to start the budgetary reform implementation at the beginning of its legislature, such that the peak is reached by the fourth year of a legislature. In the opinion of the respondent, the reform cannot be commenced in the middle of a legislature because, politically, this change could be a ‘minefield’. The interviewee opined that a period of five years is required, as a minimum, because there are logistics issues, including the need to recruit a number of accountants who are willing to work in the public sector.

### ***Changes to the legislative framework***

Information was sought during the interviews regarding the changes required to the legislative framework for the implementation of the budgetary reform.

A former Finance Minister stated that the current Financial Administration and Audit Act would have to be amended in order to provide for the required checks and balances in the law, reflecting the consequences of not reaching the pre-established targets and measures. The law should also give administrative power to the people involved in the process.

It was also suggested that a manual containing guidelines be developed and issued by the MOF – such manual would then be amended from time to time to take into account new developments.

### ***Parties involved at policy formation stage***

There was consensus amongst the respondents that the key stakeholders who should be involved at policy formation stage are the OPM, the line ministers, the Permanent Secretaries and the top civil servants (Heads of government departments).

It was also stated that consensus from the opposition party is also desirable, though according to the interviewees, this should not be a problem given the importance of the reform for the country. The implementation of this system has to result from an unanimous effort/commitment in the country, because the implementation would probably have to go through different legislatures (the government which will commence the development of this system will probably not be the one to launch its operation).

### ***Implementation challenges***

The challenges that government will potentially face if it decides to implement PB have been summed up by one of the respondents as follows:

*“A number of public officials will not understand what the system entails; some people would question why another change is necessary; some are comfortable with the status quo; others will be retiring shortly and will not want to face any new challenges; and financial resources, including IT support and training, have to be dedicated for the implementation.”*

Furthermore, another respondent mentioned that good political leadership is fundamental, such that there is consensus amongst all the ministers to make the transition. It is also important for government to have the civil servants on its side. However, to have the ministers on board and to obtain the civil servants’ support is no small task.



Given that the reform is necessarily a long process, there is the risk that people will lose interest along the way – thus, it is important to have a team which is driving the reform and keeping the momentum.

Another challenge is the limited human resources available, both as regards quantity and also quality (in terms of skills).

An interviewee observed that:

*“For the implementation of PB, there is the need for a mind-set to quantify what is to be achieved; there is the need of having the required technical competence to quantify; and finally, there is the need of having the competence and capacity to deliver.”*

## **6.8 Accrual basis**

As mentioned earlier, the Maltese central government uses a cash-based accounting system for its government ministries and departments. The cash-based system is then supplemented by accrual-based data collected manually from the government departments – this is mainly done to satisfy Eurostat reporting requirements.<sup>21</sup>

As regards budgeting, Malta also operates a cash-based system.

### **6.8.1 Budgeting**

A further question sought to obtain the respondents’ opinion as to whether the accrual basis should also be extended to budgeting.

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<sup>21</sup> The public administration has decided to adopt IPSAS, being the only recognised public sector accounting standards. According to the Accountant General, government is still at the beginning of this implementation process. The Treasury is aiming for 2019/2020 to have the first dry run, consisting of the compilation of consolidated accounts.

Whilst some participants were of the view that the accrual basis should also be adopted for budgeting, other interviewees were unsure as to the benefits that could be gained from the effort that has to be made to budget on an accruals basis.

According to the Accountant General, it is premature to introduce accrual budgeting in the local scenario and there are currently no plans for its adoption, since government is concentrating its efforts on implementing accrual accounting for historical reporting. It was mentioned that in many countries which make use of accrual budgeting, they had first adopted accrual accounting for historical purposes and then eventually moved towards accrual based budgeting. Thus, accrual budgeting might be introduced in the future, but, first, public officials have to get used to accrual accounting for historical reporting (which is still in the process of being implemented). Another issue highlighted was that it would be very difficult for the decision makers (including politicians) to grasp and use accrual based budgeting and to vote funds on that basis. If government decided to adopt accrual budgeting, a cash budget would invariably have to be prepared, alongside the accrual based budget.

### **6.8.2 Is accrual budgeting required for implementing performance budgeting?**

A number of interviewees argued that in order to implement PB, an accrual accounting system is essential. According to a former Finance Minister, if government does not have a real reading of what the actual costs are (expenditure is hidden between one year and the next), PB will not work. Therefore, a good accounting system is the basis for the implementation of PB. This view was shared by a number of participants, including a former Prime Minister.

Conversely, some interviewees argued that accrual budgeting is not necessary for the implementation of PB. An economist and academic stated that the school of thought which states that accrual accounting is a prerequisite for PB, emanates from the premise that accrual

accounting is the correct way to present financial information, and therefore, from this perspective, PB would be of no use if there is not a correct way of presenting information. However, according to the respondent, accrual accounting is not necessarily the correct way of presenting information. It was mentioned that in 2009/10, most of the governments were in financial crisis, with the problem being a liquidity issue rather than a solvency issue. In that scenario, the cash based system was more indicative of the true financial position, according to the interviewee.

## **6.9 Education and health KPIs**

The opinion of the interview participants was sought with regard to the key performance indicators (KPIs) in the local health and education sectors. According to the respondents, health is a delicate sector – if anything goes wrong, it is not just a question of underperformance, because people’s lives are at stake. Thus, the KPIs should show that the health and quality of life of people are improving. In education, the country has to think of the future of the children; thus, the outcomes have to be linked to the success of the children which, in turn, is the result of the educational system in operation.

### **6.9.1 Education**

The following table sets out the KPIs that have been listed by the respondents in respect of the education sector:

**Table 33: Education KPIs**

KPIs - Education sector
Number of ‘early school leavers’ – ‘early school leavers’ refer to young people who finish school at the age of 16 without a proper school leaving certificate which would allow them to continue with their studies. Decreasing this indicator is important such that more people would continue with their development in order to increase their employability.
Lifelong learning (from the cradle to the grave)
Attendance and absenteeism
Pupil-teacher ratio
Time taken to find employment after leaving the education system
Achievement in academic results
Number of courses offered
Measures of attainment, such as the number of students who entered into the tertiary education system or the number of students who found employment
Measurement of the success of programmes (For example, the present government has introduced free childcare – has an improved female participation rate been registered in the labour market?)

*Source: Interview data collected between August 2014 and April 2015*

### ***Further comments***

According to a former Prime Minister, the country is completely off track in the education sector: there is the government school system, the church school system (whereby government is funding the teachers’ salaries) and the private school system (whereby government is giving tax deductions on school fees). Through this education set up, the country is losing out on economies of scale. Though this structure does not make sense, it is still being publicly funded. In the respondent’s opinion, the starting point would be to merge these three systems; however, this is impossible from a political perspective. Unless this is done, the performance targets are going to be sub-optimal, in any case. The interviewee also referred to the stipends paid by government to students. Though the spending per capita on the education system is at the same level as that of other European countries, when the expenditure dedicated to stipends is factored out, the figures plummet. Thus, government prefers to subsidise the living costs of students at the expense of the advancement of the

country's education system. But any government who brings up this issue would be “*shot down politically*”. Unfortunately, when one looks at performance on sciences, literacy and duration at school, amongst other things, it is abysmally down the line compared to other EU countries. Thus, notwithstanding all the spending on education, the outcomes are not very promising. Furthermore, though a number of students achieve high performance levels, there are 30-40% of the students who lag behind.

An economist and advisor to government stated that the budget dedicated to the education sector should reflect the fact that the number of school children is reducing. Thus, decisions should be taken to close off primary schools in certain villages, centralise and build new schools which are modern and appropriate for today's realities. Centralisation would, in turn, lead to a decline in the cost per student. Government would also have vacant properties in villages which could then be used for other purposes. In agreement, the Finance Minister argued in favour of amalgamating schools, stating that this will not affect the services provided to students. The Minister added that this waste is not contributing to better results because the academic achievement of Maltese students is inferior in comparison with other EU countries. Thus, the focus should be on achieving better results.

Following the completion of the interviews, a performance audit was undertaken by the NAO in June 2015, having the objective of assessing whether there is cost efficiency in the use of resources for the operation of state primary schools. The report concluded that (National Audit Office, 2015: 42):

- The decrease in the student population, together with the expected decline in child birth, questions the need for a primary school in almost every locality in the country. The

additional resources being utilised by small schools could be dedicated to other pressing needs within the education sector.

- The financial feasibility of class sizes with a relatively small number of students is being questioned. It is stated that “*maintaining primary schools with a significantly low student population is an uneconomic endeavour, particularly since a number of reputable studies conclude that there are no advantages to be reaped in terms of social and academic development from small class sizes*”.

The Minister for Finance referred to the ratio of teachers and Learning Support Assistants to students, stating that it is unbelievably low in Malta compared to other EU countries, which highlights the excessive waste in the education system. The respondent suggested that the number of teachers should be reduced through attrition (non-replacement of leavers and retirees). Unfortunately, there is a commitment from government to employ all the graduate teachers. However, if people are employed for political reasons and not because they are needed, then government has a ‘problem’ which has to be financed.

### **6.9.2 Health**

As regards health, the KPIs identified were the following:

**Table 34: Health KPIs**

KPIs - Health sector
Waiting lists
Waiting time in hospital and in healthcare centres
Number of operations carried out in the different areas
Number of medicines which are out of stock in the hospital
Appropriate use of the stock of medicines including shelf life
Turnaround of patients in hospital
Measurement of the success of government's investment in preventive campaigns (For example, as regards a campaign against smoking, did the number of people who required medical attention for respiratory reasons decrease? Or did the government collect more revenue from cigarettes? If the latter case has materialised, then, the campaign is a waste of public funds).

*Source: Interview data collected between August 2014 and April 2015*

It was mentioned that the following three pillars – access, quality and sustainability – have to be reflected in any indicator data set used for monitoring a health system.

### ***Further comments***

A representative from the Health Ministry noted that one has to be careful when establishing KPIs and subsequently, when interpreting the statistics. For example, waiting time beyond a certain extent is clearly wrong, but if waiting time falls below a certain threshold, it could actually mean that there is an oversupply of doctors and nurses, resulting in an element of idle time. A further example relates to the case of a disease which was previously not being detected. If the number of persons suffering from the disease, subsequently, increases, it would actually be a good sign because it means that the capturing systems have improved.

A former Prime Minister remarked that during the 1990s and 2000s, the public investment figures on health were quite high, reflecting the development of the new public hospital. Although it boasts of state-of-the-art technology, the cost over-runs on this hospital have absorbed so many funds, that in the meantime, growing problems such as dementia, mental

illness and old age problems, have not been addressed. Though performance in certain areas (such as cancer) is good, in certain other areas, such as primary health care, the country is lagging because of lack of funding.

According to an economist and advisor to government, in reality, no one knows where to start off from, in the local health sector. The expenditure is going up, the technology is advancing (requiring further investment) and people's expectations are growing. The higher the success, the higher the expenditure and the more pressure on the budget, because when a person's life is extended, his/her demands for healthcare will increase with every year extended. In the interviewee's opinion, there should not be free healthcare for all, but only for those who cannot pay. The respondent claimed that the provision of free healthcare for all is unsustainable, especially in view of the fact that numbers are increasing given the country's ageing population. Thus, costs are increasing whilst resources are limited – these two issues are brought together by rationing, resulting in issues such as long waiting lists, overcrowding and bed shortage. A system of rationing is very unsocial, because the lower level of society do not have contacts so they are last in the queue; the top end of society have contacts so they go first in the queue. Therefore, according to the respondent, although free healthcare is aimed at providing fair and equitable healthcare to all, this purpose is not being served.

In agreement, the senior civil servant within the MOF stated that the purpose of free healthcare is to ensure accessibility and equity. In view of the fact that resources are limited which is giving rise to long waiting lists, this 'free' system is creating obstacles for accessibility to those persons who need healthcare. This is because healthcare is accessible to whoever has contacts or money (because if a person is financially comfortable, he/she could use private services), but inaccessible to those who do not have contacts or money.



In contrast, another former Prime Minister disagrees with the statement that free healthcare is not sustainable, claiming that if government is careful with its expenditure, then it can continue to sustain the existing health system. According to the respondent, the claim that healthcare is totally free in Malta is false, because primary healthcare includes a system of family doctors for which the public pays. Therefore, the most significant part of healthcare services is against payment, whatever the financial situation of the individual using this service. The remaining issue is then the public hospital. The interviewee noted that investment has to be made by government in health clinics, to encourage people who do not need to go to hospital to avoid going there. It was mentioned that whilst other countries allocate 10-15% of their budget to military services (armies of soldiers, weapons, bombs and planes), Malta does not incur such expenditure since the country's army is only used to take care of illegal immigrants. In fact, the percentage budget allocation for this purpose is insignificant. Therefore, Malta has an advantage over other countries in this respect, and as such, government can make decisions to offer the best possible health service. The million dollar question which has remained unsolved by the former Prime Minister is the following: how can government integrate private health insurance policies with the free healthcare system? In Malta, a person takes a private health policy; then if the need arises, the insurance company advises the individual to use the public hospital (because it's free) and then he/she will get a sum of money in cash from the insurance company. If this issue is solved and government manages to obtain the insurance companies' cooperation, such that people are incentivised to pay for private health insurance and then use private health services when the need arises, then the issue of public healthcare sustainability will be alleviated. There is another thing that could be done: today people pay national insurance of 10% of their salaries – this covers pensions, health and other benefits. This 10% is capped and the reason for the capping is

because the pension is capped; however, health services are not capped. Therefore, the respondent suggested that the 10% should be split, such that 8% [say] of the salary would cover the pension and would be capped (because the pension is capped) and the other 2% would cover health, but it should not be capped because there is no capping on health services. Theoretically, if the national insurance covering health is capped, health services offered should also be capped.

## 6.10 Concluding remarks

In conclusion, all the interview participants were in favour of the implementation of PB in the local scenario. It was stated that PB enhances accountability and increases the information available to the public, giving explanations of the purpose of the budget allocations.

When asked whether, in their opinion, this budgetary reform should be introduced, some respondents replied as follows: *“Yes, absolutely”*; *“PB is the only way forward, even because the EU Commission is pressing us to go that way”*; *“this is a vital tool for the country”*; *“yes, an unqualified yes”*; *“at the end of the day, it is not the amount invested, but the results obtained that count”*.

There were, however, some reservations with respect to the timing for the implementation of this reform. A respondent opined that *“this reform is way down the line”*. In agreement, another interviewee stated that *“we are a bit far away from the implementation of PB; first, the accrual accounting reform has to be implemented.”*

When asked whether PB should be implemented, the senior civil servant within the MOF replied:

*“Yes, why not! As long as it is complemented with good policies! On its own, PB will improve the public finance situation slightly, but there won’t be a revolutionary change or a radical transformation. In public finance, the real issues are not the lack of PB; the real issues are not weak structures here and there; the real issues are not accrual accounting; the real issues are not multi-year budgeting – in public finance the real issues are the structural problems we have in the different policy areas which need addressing in order to improve sustainability. Unless we do that, we are skirting the problem – we’ve been doing it for quite a number of years and we’re still at it.”*

According to the Minister for Education:

*“PB is important for the credibility of politics and public institutions. The people in public service (including the politicians) are using the taxpayers’ money for their work; and the citizens make a lot of sacrifices to earn their wage, part of which is paid as taxes to government. Therefore, the government has the obligation to use the resources efficiently, to curb theft, corruption and bad leadership, such that the money is used to better people’s quality of life and to improve society”.*

**CHAPTER 7:  
DISCUSSION ON  
FINDINGS**

## **7.1 Introduction**

This chapter discusses the main findings which were documented in the previous chapter.

This chapter presents the discussion in eleven further sections. Section 7.2 analyses the pressures which support the implementation of performance budgeting (PB) in Malta. Next, section 7.3 sets out a critical analysis of the current line-item budgeting system, while section 7.4 delves into the inclusion of performance information (PI) in the budget for accountability and expenditure prioritisation purposes. This is followed by section 7.5 which discusses the pressures inhibiting the implementation of budgetary reform. Subsequently, section 7.6 explores the type of organisational change expected in the Maltese scenario vis-à-vis budgetary reform, drawing upon Greenwood and Hinings' (1996) model. Section 7.7 then discusses implementation strategies and surrounding issues. Section 7.8 integrates institutional theory, change theory and policy implementation theory, seeking to address gaps identified in the individual theoretical frameworks. Section 7.9 considers whether the accrual basis is a requisite for the operation of PB and explores other institutional reforms needed in the Maltese public sector. Section 7.10 then provides some further reflections on the education and health sectors, whilst section 7.11 explores whether the concept of small country size impacts the budgetary reform. Section 7.12 concludes the chapter.

## **7.2 Pressures for change in the budgetary framework**

### **7.2.1 Institutional pressures**

The current line-item budgeting system could be viewed as a set of 'organisational rules and routines' which have become institutionalised (Burns and Scapens, 2000). The institutional thinking approach proposed by Douglas (1986) also suggests that the current system is an

‘institution’. This budgeting system has served the country for years and has become deeply embedded in the country’s processes. This thinking was confirmed by the Prime Minister, who voiced the concern of those people or groups who are frightened of changing a system which has worked for a number of years, notwithstanding its weaknesses<sup>22</sup>. Likewise, a Director within the Education Ministry mentioned how civil servants fear negative consequences where a practice which has been in place for several years, is changed.<sup>23</sup> In line with Douglas’ (1986) viewpoint, the existing system saves time in decision-making, particularly in circumstances where immediate action is needed to address unexpected events which crop up from time to time, as mentioned by the Prime Minister. However, the creativity in developing new ways/solutions to deal with arising matters may be limited by institutional thinking, such that important issues might be ignored and certain types of questions might not be asked (as found by the studies carried out by Young, 1996 and Potter, 2002). In this respect, the outputs and outcomes being delivered as a result of the budget allocations to the Maltese ministries and departments are neither being assessed nor questioned, as revealed by the interviews.

For instance, a Permanent Secretary mentioned the large increase in government employment in 2014 and emphasised the need to look at the expected productivity of these employees rather than focusing on the inputs, as is being presently done.<sup>24</sup> The Accountant General also expressed concern on the fact that value for money concepts are not being considered during the budgeting process because the budgeting is input-based and does not analyse the outcomes expected from the funds dedicated to activities/programmes. Similarly, a former Minister for Finance referred to the fact that the funding requested by line ministries is not

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<sup>22</sup> Vide section 6.6.5

<sup>23</sup> Vide section 6.6.2

<sup>24</sup> Vide section 6.3

justified in terms of quantifiable outputs, an observation which was also confirmed by the Minister for Finance presently in office.<sup>25</sup>

A very contentious issue which was mentioned by a number of interview participants and which demonstrates a situation where certain questions are not being asked as suggested by Young (1996) and Potter's (2002) analyses, relates to the concerns in the education sector, where the birth rate in Malta is decreasing and yet, the number of schools and teaching staff is on the increase. Having said this, institutional thinking explains only one aspect of this situation, because there are huge political considerations which are hindering government from taking corrective action in this respect, as shall be discussed later on in this chapter.

Notwithstanding the deep embeddedness of the existing system, institutional pressures come into play (DiMaggio and Powell, 1983) which drive and trigger change to the existing 'routines and institutions' (Burns and Scapens, 2000). As discussed below, the three areas of institutional isomorphic pressures proposed by DiMaggio and Powell (1983), namely coercive, mimetic and normative influences, manifest themselves in the proposed budgetary reform which, according to the majority of the interview respondents, is greatly needed in the Maltese context<sup>26</sup>.

### ***Coercive isomorphism***

A key driver for the implementation of budgetary reform consists of coercive pressure being exerted upon Malta by the **IMF**. In this respect, an interviewee mentioned that an IMF delegation visited Malta during 2014, advising on how the budgetary process could be changed. As observed by the respondent, suggestions and recommendations coming from the

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<sup>25</sup> Vide section 6.3

<sup>26</sup> Vide section 6.3

IMF have a stronger possibility of being taken seriously and implemented by the civil service.<sup>27</sup>

A further aspect of coercive influence for the introduction of budgetary reform stems from Malta's affiliation with the EU, in particular its **Eurozone membership**. Though the EU has not 'forced' Malta to reform its budgetary framework, compliance with the Eurozone rules implies a need to introduce changes to the country's budgeting system, as explained below.

Malta has to comply with the Maastricht criteria for qualification and participation in the Economic and Monetary Union, which stipulate a number of conditions that have to be met by member countries, including the requirement that government's fiscal deficit should not exceed 3% of the country's GDP and government debt should not exceed 60% of GDP. Non-compliance with these criteria leads to consequences and sanctions instituted by the EU against the country which is in breach of the stipulated conditions, in line with the regulative pillar proposed by Scott (2014). In this regard, Malta was placed under an EDP during the period from June 2013 to June 2015, in view of the fact that the deficit was above the 3% threshold. During this period, the public administration took a number of corrective actions in order to exit the EDP; however, some of the actions might have constituted quick-fix decisions which did not consider the medium and long-term implications. For example, the MOF's practice of carrying out expenditure cuts across the line ministries during the year, in order to reach the deficit target<sup>28</sup>, could be considered as a temporary solution which is leading to under-investment in certain areas (such as in aspects of infrastructure) and to interruption of certain programmes where allocated funds are subsequently reduced or withdrawn.

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<sup>27</sup> Vide section 6.3

<sup>28</sup> Vide section 6.5.2



Notwithstanding the closure of the EDP in June 2015, Malta still has to exert tight control over government spending in order to ensure that the deficit remains under the 3% threshold. Prior to being placed under an EDP, Malta had received warnings from the European Commission to take measures to correct its deficit. In this respect, the EU had emphasised the need for ensuring sustainable public finances and for implementing corrective measures in the areas of healthcare, energy and pensions, amongst others. Government is still in the process of undertaking such reforms.

The fiscal deficit issues recently faced by Malta and the demands imposed by the EU for corrective action are triggers/pressures for budgetary reform, according to some of the interview respondents.<sup>29</sup>

This view was put forward by a Permanent Secretary and an academic and advisor to the MOF. The latter added that budgetary reform should emphasise performance, which assumes fundamental importance in circumstances of fiscal deficit issues. The interviewee explained that the compilation of PI by line ministries helps to identify ways of achieving better results with the funds available.

The Accountant General also referred to the coercive influence for introducing budgetary reform:

*“The fact that the country is under an EDP<sup>30</sup>, the pressures being exerted by the European Commission for fiscal consolidation and the requirement to meet the 3% deficit target, are definitely triggers for reform.”*

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<sup>29</sup> Vide section 6.3

<sup>30</sup> The EDP against Malta was initiated in June 2013 and was closed in June 2015. However the interviews were carried out during the period August 2014 to April 2015 when Malta was still under an EDP, and therefore, the participants have referred to such EDP that the country was subject to during that period.

Eurozone membership, therefore, represents a strong form of coercive isomorphic pressure. In this respect, it is pertinent to note that prior to Malta's entry into the Eurozone, the deficit was considerably higher than 3% of GDP. It was just under 10% in 2003 and was brought down to 3% at the end of 2007 to qualify for entry in the Eurozone on 1 January 2008<sup>31</sup>.

It is to be noted that an EU Council Recommendation delivered to Cyprus following an examination of the country's 2012 national reform programme and stability programme advised Cyprus to take additional measures to achieve a durable correction of its excessive deficit. In this regard, one of the recommendations proposed was to "*take measures to keep tight control over expenditure and implement programme and performance budgeting as soon as possible*" (European Commission, 2012).

Coercive pressure for the introduction of reforms also arises from the pressures applied by credit rating agencies, through the **downgrades** effected in Malta's sovereign rating<sup>32</sup>. Similar to the EU, these agencies highlighted the requirement for fiscal consolidation, referring to government's requirement to implement a reform programme in order to boost growth and at the same time avoid fiscal deficit slippages and avoid increasing further its debt burden.

### ***Mimetic isomorphism***

The introduction of budgetary reform is also driven by mimetic pressure placed upon the public administration to strive for the effectiveness levels reached by private organisations. PB, with its focus on performance measurement, seeks to enhance effectiveness and efficiency in the allocation of public funds by directing such allocation to programmes which are delivering the desired outputs and outcomes.

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<sup>31</sup> Vide section 4.2

<sup>32</sup> Vide section 4.3

However, reaching the effectiveness levels achieved in the private sector could be problematic in the Maltese scenario for a number of reasons. A Permanent Secretary remarked that whilst the private sector can take drastic measures should profits decline, this might not be possible within government since other social and political factors come into play.<sup>33</sup> Another issue mentioned by a few respondents is the fact that private organisations, unlike government, can recruit the best people to achieve the desired results, by offering remuneration packages commensurate with the employees' responsibilities.<sup>34</sup> A Health Ministry representative mentioned that the decision-making process is slow within government, in comparison with the private sector<sup>35</sup> – this might lead to complacency and failure to get things done on time in the public sector. Furthermore, according to an economist and academic, there is the perception, worldwide, that government borrows carelessly, unlike private organisations which are more diligent when it comes to gearing up their companies. This presumption is, in fact, supported by the Maastricht criteria, which, according to the interviewee, have been introduced to control governments' actions.

Mimetic isomorphism is also manifested if the Maltese government is willing to follow 'good international practice', modelling the new budgeting system on that adopted by other countries (Burns, 2000). Following best practice ensures that actions are justified in view of their perceived soundness, as suggested by the cultural-cognitive pillar (Scott, 2014). In this regard, the Minister for Finance has opined that the existing budgeting system is out-dated when compared to that adopted by other European countries, and it needs to be reformed (Malta Today, 2013c), implying that the willingness by the current public administration to implement budgetary reform, exists.

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<sup>33</sup> Vide section 6.5.2

<sup>34</sup> Vide section 6.6.2

<sup>35</sup> Vide section 6.6.3

### *Normative isomorphism*

The introduction by the Maltese government of an appropriate and exemplary budget system which observes norms established by dominant countries supports the normative pillar put forward by Scott (2014).

Referring to accounting and budgetary reforms in the UK, Ezzamel et al (2007) claimed that normative isomorphic change was weakened where politicians lacked accounting and finance experience. In this respect, the Prime Minister noted that the majority of Maltese politicians have no accounting or finance background and would never have been involved in management accounting systems and processes.<sup>36</sup> This ‘profession deficiency’ weakens change by decreasing normative pressures (Andrews, 2009) and might act as a stumbling block for the introduction of PB.

Furthermore, a number of interviewees questioned the human resource capability within the public sector.<sup>37</sup> It was mentioned that the finance function within some line ministries is weak, with the Director, Corporate Services (who is in charge of the accounting/budgeting of the ministry) not necessarily having an accounting qualification. This financial illiteracy could seriously weaken isomorphic change. A number of reasons have been cited by the respondents for this situation, including the shortage of accountants in Malta, the unattractive remuneration packages for accountants and top civil servants in government employment and the dismal career prospects in the public sector. ‘Profession proficiency’ is important for promoting normative isomorphic change (Andrews, 2009) and thus to take forward the budgetary reform, the recruitment of experienced staff with an accounting/finance background in every ministry, assumes significant importance.

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<sup>36</sup> Vide section 6.4.1

<sup>37</sup> Vide section 6.6.2

### 7.2.2 Macro-level factors

The implementation of PB is also being driven by forces in the macro-level environment (Oliver, 1991 and Munir et al, 2011), as shown by the research findings.

From an **economic** perspective, the budgetary reform seems to be critically required in the Maltese context<sup>38</sup>. In this respect, an economist and advisor to government commented that the budget process is not embracing efficiency measurement. An economist and academic voiced his concern that in the long term, Malta will be economically worse off compared to other countries, because of the country's ageing population and the fact that this problem has not been tackled. A former Prime Minister remarked that a radical change in the budgetary system is needed, since the current system is not good enough to act as a tool for decision makers to enable them to design the right economic and social policies. A representative from the EPD opined that the budgetary reform is necessary in view of Malta's requirement to target a balanced budget in structural terms. He added that:

*“When there are pressures to increase certain expenditures at the same rate as revenue, to increase other expenditure items (including salaries) by more than inflation and at the same time, reduce the deficit, it is very obvious that there is the need to move towards PB.”*

There are also strong **political** pressures for implementing the budgetary reform, as indicated by the commentary below. The findings reveal that the final decisions on the budget allocations are made by the MOF, possibly by civil servants, without consultation with the line ministries, notwithstanding the effort made by the latter to compile their business plans<sup>39</sup>.

An economist and advisor to government remarked that:

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<sup>38</sup> Vide section 6.3

<sup>39</sup> Vide section 6.3

*“Given that the budget is such a serious matter, with huge political ramifications, the control of the final decisions should be in the hands of government who is ultimately responsible for the budget.”*

A former Prime Minister advised that when the final allocation decisions are determined by the MOF, there is the risk of failing to embrace a holistic view of the diverse sectors and to make sub-optimal decisions which do not properly address the needs of the country.

Though the budget is subject to approval by Parliament, it appears that this is just a routine procedure, which is not functioning properly since the decisions being taken by the MOF with respect to budget allocations, are considered final<sup>40</sup>. According to Raudla (2012), Parliament’s limited input for changing the budget is one of the reasons for the lack of use of PI. These findings imply that the MOF have greater influence than the OPM or the legislature in the determination of the budget allocations.

It appears that one of the fundamental problems of the current budgetary system is that the line ministries focus on extorting the maximum amount of funds possible from the MOF during the budget process, without analysing carefully their actual funding needs<sup>41</sup>. This viewpoint was shared by a number of respondents who are or have, in the past, been part of the MOF. In this regard, there are pressures, from a **socio-cultural** perspective, to reform the current system, such that a culture of delivery and reaching performance targets is instilled in the civil service. A culture change is not an easy task, as mentioned by some interviewees, and it takes time and perseverance, together with championing from the top, possibly the OPM.

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<sup>40</sup> It is pertinent to mention that in December 2012, the 2013 budget was rejected by Parliament causing the collapse of the previous government, as one member of the government (who was not part of Cabinet) had voted with the then Opposition party, against the budget (Malta Independent, 2012). In spite of this, the rejection of the budget was not directly related to problems with the ministries’ budget allocations, but rather to wider policy stances of the government in office and disagreement with such policies by the member of the government who voted against the budget.

<sup>41</sup> Vide section 6.3

### 7.2.3 Were the recent reforms in the budgetary framework a result of isomorphic pressures?

As detailed in the previous chapter<sup>42</sup> and as summarised in Figure 25, the new government, which was elected to power in March 2013, introduced a number of changes to the budgetary framework.

**Figure 25: Recent reforms of the budgetary framework**



<sup>42</sup> Vide section 6.4

Three months after the new public administration came into office (in June 2013), Malta was placed under an EDP by the EU, since the fiscal deficit was observed at 3.3% of GDP at the end of 2012 (MaltaToday, 2013a). This followed previous warnings by the EU for Malta to regularise its deficit position, as well as downgrades in the country's sovereign rating effected by a number of credit rating agencies<sup>43</sup>. As a result, the new public administration was 'forced' to take corrective action, which included the introduction of reforms to the budgetary framework, as revealed during the interviews (summarised in Figure 25).

An analysis of the recent reforms introduced (refer to Table 35 below) shows that isomorphic influences were manifested in the case of the launch of the *Comprehensive Spending Review* (CSR) exercise, the decision to start preparing *Three-year Projections* and the enactment of the *Fiscal Responsibility Act*.

With regard to the other reforms (*Publication of 'Implementation of the Budget' document, linking the Annual Budget to the Electoral Manifesto and carrying out Performance Appraisals for Permanent Secretaries*), it could be argued that the newly elected government sought to communicate the message, both to the civil service and to the public in general, that transparency and delivery of promises made, are being prioritised by the new administration. Moreover, managerial, public and political accountability, as proposed by Sinclair (1995), are being emphasised in these three reform initiatives (discussed in Table 35).

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<sup>43</sup> Vide section 4.3



**Table 35: Analysis of the recent budgetary reforms**

Reform	Commentary
Comprehensive spending review (CSR)	<p>The initiation of the CSR exercise (note a) was primarily a result of coercive isomorphic pressure, since the main objective of this process was to decrease the fiscal deficit and exit the EDP which the country was subject to, in order to comply with the Eurozone’s requirements. The CSR approach was also driven by mimetic and normative forces, where the Maltese MOF is seeking to replicate a process which had been successfully undertaken in the UK and which had led to a significant reduction in the deficit.</p> <p>The exercise embarked on by the Maltese MOF involved the review of expenditure on selected budget line items included in the 2014 Financial Estimates, in order to identify areas of expenditure which could be reduced or eliminated.</p> <p>It is unfortunate that with the exception of social security spending, the results of the CSR exercise “<i>were not given enough consideration in the 2015 budgetary allocation</i>”, as mentioned by a Permanent Secretary. There could be a number of reasons for this, including the fact that the CSR exercise carried out in 2014 was the first trial which served as an opportunity for civil servants to familiarise themselves with the process. Another reason could have been the limited time available from the conclusion of the CSR exercise till the date established for finalising the annual budget. The findings reveal that the CSR exercise was not taken as seriously by the line ministries as it was hoped for, and thus, the MOF might have decided to incorporate only limited aspects of the CSR process in the 2015 budget. In this respect, an interviewee from the Education Ministry showed considerable scepticism regarding the CSR, stating that the education civil servants were not, in any way, convinced that there is scope for reducing spending on education. There might also have been an issue of lack of capable human resources within the line ministries for taking responsibility for the exercise – in effect, the lack of knowledge within a number of line ministries was highlighted by a number of interview respondents. The Prime Minister also confirmed that it may take some time to incorporate the CSR process into the budgetary process, since this might require a change in culture and in public officials’ mind-set. The lack of accounting and finance background of the majority of the Maltese politicians was also highlighted.</p> <p>Notwithstanding the above-mentioned obstacles, coercive pressures to implement the CSR reform are very strong since government is obliged to meet the EU requirements for fiscal deficit control, if it is to avoid sanctioning (Scott, 2014). In fact, the findings revealed that the CSR process will be repeated and its scope will be widened to cover other spending areas. Mimetic and normative isomorphic influences might be weakened if the CSR exercise is not taken seriously and where lack of knowledge, referred to as ‘profession deficiency’ by Andrews (2009), prevails.</p>

Three-year projections	<p>As stated in the previous chapter, three-year revenue and expenditure projections (note b), covering all ministries, were first presented in the 2014 Financial Estimates (published in 2013). The preparation of three-year projections was subsequently mandated by the Fiscal Responsibility Act, which came into force in 2014. It could be argued that government took this initiative in 2013, in anticipation of the obligations that were to be imposed by the new law a few months down the line. Thus, this reform could have been driven by coercive influences arising from legally enforced requirements.</p> <p>The findings show that projections for the two years following the budget year, are being prepared by the MOF, rather than by the respective line ministries. In this respect, a public official from the Education Ministry stated that it is only possible to plan ahead for one year because the education sector is very dynamic. This line of thought could be the reason why the MOF had to shoulder responsibility for the compilation of forward estimates. Unfortunately, this central involvement could weaken the effectiveness of these forward estimates, since the line ministries do not feel ownership for such financial plans and thus, commitment to adhere to these plans is weak. During an interview with the Minister for Finance, it was evident that a feeling of frustration is felt where line ministries, which should be responsible for their budget, exceed their budget allocations. The preparation of forward estimates by the central agency augments this problem, since line ministries may not feel any responsibility for sticking to financial plans which were not prepared by them.</p>
Fiscal Responsibility Act (FRA)	<p>The enactment of the FRA in August 2014 (note c) is clearly driven by coercive isomorphic pressures, due to the fact that the law was passed to fulfil the EU directive on budgetary frameworks. Mimetic and normative influences are also manifested in this reform. As a result of mimetic forces, the law was largely modelled on the Irish Act, according to a Director from the EPD, in view of the similarities between Malta and Ireland. The setting up of institutions in Ireland, following its economic and banking crisis, was influenced by dominant institutions, including the IMF and Troika; furthermore, the Irish Act was accepted by the EU Commission. The influence of these professional and dominant organisations constitutes normative pressure for the implementation of this reform in Malta.</p> <p>The EPD official has mentioned that “<i>the reform has been carried out on paper and in a strong way</i>”, in view of the law’s onerous reporting requirements. Similarly, a Central Bank representative mentioned the increased and in-depth scrutiny required vis-a-vis the budget process, as a result of the Act. In contrast, a few months after the enactment of the law, the senior civil servant within the MOF maintained that he has not seen any tangible changes/improvements as regards fiscal discipline and sticking to the budget allocations by the line ministries. This leads one to ask whether this reform has been carried out 'on paper' only, for the purpose of meeting the EU obligations, or whether the interviewee is being overly pessimistic. Alternatively, it could be argued that it is still early days to assess the impact of this reform.</p>

Publication of the 'Implementation of the Budget' document	The publication of the document which sets out the implementation status of the previous year's budgetary measures (note d), seeks to ensure that each ministry is being transparent and accountable to the public, vis-à-vis the allocation of public funds for the various programmes and activities included in the previous year's budget plans. This document serves to publicly recognise or criticise the ministries' performance. During the interview, the Prime Minister explained that the electoral manifesto is being used as a benchmark for gauging government's performance – if the electoral programme is being implemented, then government is considered to be achieving the desired results. Though presently this document does not contain cost information or performance measures, it could eventually pave the way for PB by being adapted to incorporate a comparison between performance targets and actual results.
Implementation of the Electoral Manifesto	The requirement to ensure that the yearly budget is reflecting the promises set out in the electoral manifesto (note e) is an attempt by government to deliver on the promises made to the electorate prior to the general election – by placing the responsibility for the implementation of the electoral manifesto directly under a Minister, government is conveying a message to the public that it is taking promise delivery seriously. As remarked by the Education Minister, the process of linking the annual budget to the electoral manifesto ensures that the funds requested by the line ministries are directed towards government's priorities, rather than running the risk of having ministries going off at a tangent and undertaking programmes that may not be fundamentally required.
Performance appraisals	The establishment of specific guidelines against which to appraise Permanent Secretaries for the purpose of awarding performance bonuses (note f) appears to show government's commitment to enhance political and managerial accountability (Sinclair, 1995). At the same time, this initiative seeks to ensure that the top civil servants responsible for the line ministries are working hard to achieve results and to deliver the services expected by the citizens. This reform was referred to by the Prime Minister as an attempt to " <i>begin a new culture</i> " which encourages the disclosure of information and " <i>to have checks and balances in place</i> ". The practice of carrying out these evaluations twice yearly is healthy, since the mid-year assessment serves to check whether the targeted performance is expected to be reached by end of year and to take corrective action where necessary – this gives confidence and peace of mind to the appraisees, that the system is fair and just and is aimed at motivating performance rather than at punishing non-achievement.

Note (a): Vide section 6.4.1

Note (b): Vide section 6.4.2

Note (c): Vide section 6.4.6

Note (d): Vide section 6.4.4

Note (e): Vide section 6.4.3

Note (f): Vide section 6.4.5

***Did macro-economic forces play a role in the launch of the recent reforms?***

Some of the recent reforms discussed above have been driven by forces other than isomorphic pressures. The influence of factors in the macro-level environment (Oliver, 1991 and Munir et al, 2011) may have played a significant role in triggering a few of these reforms.

The publication of the ‘Implementation of the Budget’ document and the initiative of linking the annual budget to the electoral manifesto could have been driven by political factors. Government, following its election to power, wanted to prove its effectiveness and to demonstrate its enthusiasm and commitment to effect changes in public financial management, with the purpose of enhancing accountability, transparency and delivering on what was promised. As remarked by the Prime Minister, if it is shown that the previous year’s budgetary measures were achieved, “*government would be considered as performing*”<sup>44</sup>. Having said that, this practice does not necessarily measure the *correct* implementation of government’s objectives. By operationalising the strategies included in the electoral manifesto through the annual budget, government is attempting to ‘guarantee’ delivery of its electoral plans. If the electoral promises are delivered within the current five-year legislature, this attainment would be a powerful political tool in government’s hands which would probably be used as propaganda in the next general election’s campaign.

Socio-cultural influences can also be observed – the specification of guidelines for appraising the Permanent Secretaries’ performance could be an attempt by the public administration to change the attitudes and behaviours of civil servants, in order to instil a culture of accountability. It is planned that this practice will be extended to other civil servants. The findings show that, presently, there is lack of accountability for the public funds allocated to

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<sup>44</sup> Vide section 6.4.4

the government departments. It was stated by the Prime Minister that the existing system is ingrained in secrecy, and lacks checks and balances<sup>45</sup>. Moreover the Minister for Finance mentioned how line ministries approach the MOF for additional funds during the year, because the funds allocated through the budget would not have sufficed<sup>46</sup> – this shows lack of cooperation by the line ministries especially in view of the country’s fiscal deficit situation and government’s attempt to bring down the deficit.

As discussed above, institutional pressures were a key element in the launch of the CSR exercise. Economic and socio-cultural pressures are, however, also evident in the initiation of this process. From an economic perspective, the findings show that there are issues of wasteful spending in certain areas and at the same time, there is the problem of the country’s fiscal sustainability. The ‘waste of public money’ which is prevalent in the current system was referred to by the Prime Minister, the Minister for Finance, an academic and advisor to the MOF, and a former Minister for Finance. The need to tackle fiscal sustainability and reduce the deficit was mentioned by the majority of the interview respondents. Some of the interviewees expressed their concern over the lack of investment in certain areas, such as infrastructure, in order to make ends meet and to avoid increasing the deficit and the debt. The reduction of waste, which is one of the objectives of the CSR, is expected to help government to direct funds to its priorities, without augmenting the deficit issue or increasing taxes. The socio-cultural element is manifested, since the launch of the CSR is also aimed at starting a process of changing the public officials’ mind-set, as expressed by the Prime Minister. It is hoped that civil servants would start thinking on the outputs/outcomes being delivered through public funds and would identify circumstances where spending patterns could be improved and waste controlled.

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<sup>45</sup> Vide section 6.4.5

<sup>46</sup> Vide section 6.3

#### 7.2.4 Legitimisation

Institutional theory suggests that organisations respond to pressures from their environment by adopting procedures and systems which are considered as appropriate (Carpenter and Feroz, 2001), thus securing the organisations' long term survival and ultimately, achieving legitimacy (Meyer and Rowan, 1977; Brignall and Modell, 2000). Budget reforms are sometimes used to establish legitimacy (Van Reeth, 2002). Mimba et al's (2013) study indicated a symbolic rather than functional use of PI, in view of the focus placed on the format of performance reports rather than on their contents.

Will a transition by the Maltese government to a performance based system be used as an attempt to attain legitimacy, rather than for bettering budgetary allocation decisions? The implementation of PB will potentially take a lot of time and resources, as remarked by a number of respondents. The risk that the PI gathered will not be used for planning and decision-making (Van Reeth, 2002) exists; however, if the right effort and resources (including training) are dedicated to the development of the system, the line ministries are involved in such development, the establishment of performance targets and their subsequent attainment is linked to rewards and sanctions and the reform is championed by the OPM, the civil service will get used to the system and will appreciate its benefits for enhancing allocative efficiency in public expenditure. Through the operation of a performance based system, line ministries can even increase their budget on certain programmes/activities if outputs and outcomes justify such expenditure.

With respect to the introduction of some of the recent reforms in the budgetary framework, legitimacy purposes may have been taken into consideration. With reference to the enactment of the Fiscal Responsibility Act, which was aimed at ensuring sustainable public finances and

enhancing public accountability and transparency in government's financial dealings, the MOF senior civil servant claimed that this law has, so far, not led to any improvements in the budgetary framework. As regards the compilation of a three-year financial plan, the findings show that the projections for the two years following the budget year are being prepared by the MOF. The issue of lack of ownership of such figures by the line ministries is exacerbated by the attitude of civil servants who believe that projections beyond one year are unfeasible, as indicated during the interviews. The findings also show that the MOF was not totally satisfied with the results emanating from the CSR process, in view of the scepticism shown and the lack of in-depth analysis undertaken by some of the line ministries. Are these issues teething problems or have these reforms been carried out only on paper, in order to establish legitimacy through the introduction of acceptable work practices (Meyer and Rowan, 1977)? It is difficult to answer this question at this stage; however, it could be argued that it will take some time before the civil service gets used to these practices, firstly, because things have been done differently for a considerable number of years and, secondly, because some of these reforms require a culture change. Nevertheless, as regards the CSR, the findings show that, though the results of the CSR exercise were not incorporated in the 2015 budget (with some exceptions), the line ministries made an effort to take into account what was learnt from the CSR process during the 2015 budget preparation. This implies that even though the first CSR undertaken might not have had a huge impact on the budgetary framework, it served as a catalyst for kicking off a change in the public officials' approach to the budget process.

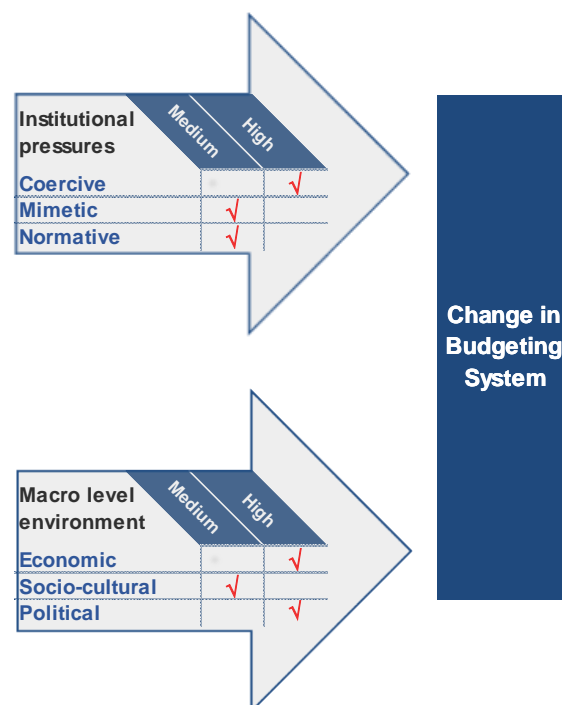
### **7.2.5 Summary**

As discussed above, the current line-item budgeting system is deeply embedded in government's existing practices and routines. There are, however, both institutional pressures and influences at macro-level, which might trigger a budgetary reform. This observation is

further substantiated by the fact that a number of recent reforms have been launched to the budgetary framework as part of the overall fiscal discipline process being carried out by the public administration, in an attempt to control the deficit and bring down government's debt.

The pressures for change in the budgeting system are summarised in Figure 26 (Source: Munir et al, 2011: 98) (Adapted)

**Figure 26: Pressures for change in the budgetary framework**



Coercive isomorphic pressures appear to be strong: the IMF's advice vis-à-vis the budgetary process, the influence of Malta's membership in the Eurozone as well as the country's regular monitoring by credit rating agencies are significant forces for change. Mimetic and normative pressures also drive the introduction of PB – replicating the effectiveness levels of private organisations by shifting the focus on performance and modelling the new budgeting system on that adopted by dominant countries. The findings indicate that there are issues which might



weaken mimetic and normative pressures. These include social and political factors which assume significant importance in the public sector; the slowness of the pace of decision-making in the civil service; the lack of accounting and finance background of a number of Maltese politicians; and the challenges encountered to recruit high-calibre people to work for the public sector which leads to financial illiteracy within government.

There are also strong economic and political pressures and moderately strong socio-cultural influences for the implementation of PB. The fact that interviewees are claiming that the current budgetary system needs a radical change because it is not serving the purpose of effective economic decision-making is a very strong stimulus for change. In addition, political considerations are highly significant, since the current practice of having civil servants within the MOF finalising the budget allocations may be leading to sub-optimal results.

In conclusion, the analysis suggests that the institutional pressures coupled with the macro-level influences should lead to action by government for implementing budgetary reform, notwithstanding the stumbling blocks highlighted above. Nevertheless, the consideration as to whether these pressures will, in effect, trigger changes to the budgetary system has to be made in the light of an analysis of the opposing pressures which inhibit change (refer to section 7.5).

### **7.3 The current line-item budgeting system**

#### **7.3.1 Are budget cuts being carried out across the board?**

The findings reveal that, in view of Malta's need to keep the fiscal deficit under tight control, it has become normal practice for the MOF to effect budgetary cuts during the year, in order to shift funds to expenditure items which were not planned for in the budget estimates

approved before the commencement of the fiscal year<sup>47</sup>. In line with this, Murray and Efendioglu (2011) maintained that, in times of fiscal turbulence, budgetary cuts may be required in order to ensure fiscal consolidation.

A representative from the Budget Office (who is usually involved in identifying the items which will be subject to an expenditure cut) acknowledged that this practice could disrupt the plans of a ministry/department, particularly where diligence and caution were applied towards the beginning of the year in order to save funds for a particular activity. The Budget Office official and the senior civil servant within the MOF stated that, for the purpose of budget cuts, the line items selected are believed to include an element of surplus allocated funds - this judgement is formed on the basis of close monitoring of the line ministries' spending patterns by the MOF. The latter interviewee strongly argued that the MOF does *not* make budget cuts across the board.

The majority of the other interviewees disagreed with the statements made by these two respondents. In this respect, the majority claimed that when government effects expenditure cuts during the year, they are carried out *across the board*. The Prime Minister stated that reduction in expenditure during the year is carried out across the board. This seems to be inevitable in order to keep the deficit under control. A Permanent Secretary added that expenditure cuts are mainly carried out arbitrarily.

According to Murray and Efendioglu (2011), the reduction of expenditure across the board, rather than decreasing resources for ineffective programmes, is, in reality, one of the limitations of a conventional line-item budgeting system. Van Reeth (2002) maintained that in traditional budgeting systems, budgetary cuts are made across the board in order to minimise

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<sup>47</sup> Vide section 6.5.2

political conflict. However, as claimed by an interviewee, this ‘one-size-fits-all’ solution might not be the most appropriate, since the impact on programme performance should be fully assessed prior to carrying out a budget cut.

Though the two respondents from the MOF (mentioned above) are claiming that this assessment is being made, the findings indicate that it is not as effective as it should be, since a number of interviewees maintained that the budget cuts during the course of the year are upsetting the plans of the ministries/departments. Notwithstanding the MOF’s efforts to target areas which are the least sensitive for expenditure reduction, in the absence of information on performance and information on whether the programmes are delivering the desired results, it is very difficult to take decisions which are not potentially harmful from an economic and social perspective.

With a PB system which provides information on the outputs and outcomes expected from the budget allocations, the MOF would be in a better position to identify ineffective or lower priority programmes, such that the required budgetary cuts could be better targeted. The findings suggest that there is an element of waste in government spending; at the same time, expenditure in certain sectors such as health and infrastructure is tight. It can be argued that, firstly, expenditure cuts across the board are definitely inappropriate because they might be harming sensitive sectors which are already operating under tight funding conditions. Secondly, there appears to be scope for expenditure reduction in view of the wastage referred to by the respondents; however, such reduction has to be targeted at those programmes/activities which are ineffective. Allocative efficiency in public expenditure could be enhanced through the introduction of PB (Robinson and Brumby, 2005).

### 7.3.2 Underspending the budget

All the interview participants confirmed that where a department/ministry spends less than the amount allocated through the budget, the excess funds are returned to the MOF<sup>48</sup>. Ministries are currently not allowed to carry forward any unspent funds to the next fiscal year. Furthermore, the department's budget is usually reduced for the following year, in line with what was stated by Murray and Efendioglu (2011).

As suggested by the findings, this practice is leading to 'shopping sprees' by the line ministries towards the end of the year, such that any remaining funds would be fully utilised, in order not to 'lose' unspent funds and not to have the following year's budget reduced. In this regard, there is the risk that this last-minute expenditure would not be applied to address government's priorities. A former Finance Minister maintained that excess funds are being spent carelessly and public money is being wasted. Representatives from the MOF counter argued that the budget allocation made to some departments is so tight that the funds are necessarily fully utilised. Nevertheless, the Budget Office official and the senior civil servant within the MOF claimed that, during the last few months of the year, the MOF monitors closely what is being spent by the ministries and on what, in order to *try* to identify any reckless spending. It was stated that where such issues are discovered, the MOF intervenes to claw back the funds. The issue, however, remains that where such situations are not identified in time by the MOF, there is the danger that public funds will not be applied to the country's most pressing needs.

The findings also show that this practice is discouraging cost-savings (Kong, 2005) and it is demotivating ministries who seek to implement efficiency measures. Furthermore, a

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<sup>48</sup> Vide section 6.5.2

Permanent Secretary and an advisor to the MOF mentioned that some departments, which have the potential for revenue generation, do not feel that it is worth the effort to do so since all the income generated will go to Finance. In summary, the majority of the interviewees feel that this practice is penalising those ministries/departments who have been effective (McNab and Melese, 2003).

Some respondents who were or are involved in the MOF justified this system by stating that it is only logical that if a department/ministry needs less funds than what was allocated through the budget, such funds should be clawed back by Finance to be used elsewhere. Though this reasoning might seem 'logical', it is certainly having undesirable consequences. For instance, ministries which have been diligent in their spending during the year 'lose' unspent funds and receive a lower budget allocation during the next year, whilst ministries which spend more freely potentially receive a higher allocation in the following year because their budget did not suffice. As stated by the Prime Minister, the current practice is rewarding expenditure rather than savings.

A way forward could be to consider allowing line ministries to carry forward a percentage of the unspent funds for use by the ministry. This has, in fact, happened in the past as mentioned by a former Prime Minister who had previously held the position of a Minister for Social Policy. After lengthy negotiations with the MOF, the then Minister for Social Policy managed to obtain half of the funds saved for use in the following year. However, this was a one-off occurrence and it was the result of informal budget negotiations, since there is no formal structure/policy for carrying forward unspent amounts.

The possibility of carrying forward a portion of the saved funds would act as an incentive mechanism for motivating public officials to identify cost saving opportunities and to spend

more wisely. If ministries carry forward a portion of the remaining funds (which has to be significant, say 40-60%), it would be a win-win situation for both the line ministries and the central agency, since the former will have funds at their disposal to be applied to the departments' activities, whilst government, as a whole, would also be benefitting from the savings made and could, as a result, undertake, new initiatives. It is important that the projects/programmes on which the funds carried forward are applied, would be approved by the MOF, in order to maintain control on public expenditure and ensure that value for money projects are being embarked on. This incentive mechanism will not, however, get rid of the budget game (where line ministries request excess funds from the MOF). This risk is mitigated if PI is *available* to support government's decision making, as advised by Joyce (2011) and Hammerschmid et al (2013).

### **7.3.3 Closing remark**

Whilst the current line-item budgeting system has a number of strengths, including its relative simplicity and the potential control on public spending through the thorough specification of inputs (Shah and Shen, 2007), the findings show that there are a number of issues with this system, which need to be addressed.

Firstly, though it is understandable that government may need to effect expenditure cuts during the year in order to shift funds to unexpected expenditure which was not planned for in the financial estimates, such expenditure cuts should be carefully targeted towards allocations which contain an element of waste or towards ineffective programmes. However, in order to be able to identify wastage and/or ineffectiveness, a budgeting system incorporating performance measurement has to be in operation.

Secondly, it is very important to encourage cost saving and revenue generating initiatives by ministries/departments, especially in Malta's context, where tight control on the deficit is a top government priority. It follows, therefore, that practices which discourage such initiatives should be avoided. The findings show that where ministries underspend their budget, the excess funds are returned to the central agency and the following year's budget for the said ministry is reduced accordingly. It has been revealed that this practice is considered as unfair. Thus, it is suggested that a significant percentage of the unspent funds would be available to the ministry in question during the following year, to be used on projects which are approved by the MOF. This encourages cost savings and revenue generation by the ministries, it benefits the whole of government through the availability of additional funds and it potentially leads to fiscal deficit reduction.

The findings also show that the current budgeting system adopts a short-term perspective, focusing on year-to-year changes in expense categories (Murray and Efendioglu, 2011). It was stated by a Permanent Secretary that where a ministry requests the same level of funds of the previous year for an expenditure item, such funds are granted with no questions asked. It was confirmed by a number of respondents within the MOF, including the Minister for Finance, that the current budgeting system adopts an incremental approach, such that line ministries expect the same budget allocation of the previous year plus something extra to cover for inflation. The senior civil servant within the MOF also confirmed that a number of budget line items have been kept constant for a number of years. A Health Ministry official referred to the fact that whilst new programmes are introduced under 'programmes and initiatives', there is no discipline to terminate old programmes. The reason for this is political, since it was found that politicians do not accept that a line item is removed. As stated by an academic and advisor to the MOF, the incremental basis does not allow for a review of

performance, because it assumes that everything is perfect. In view of the lack of performance measurement, the funding of existing programmes is renewed in each budget without analysing the success of such programmes. As a result, elements of waste are neither identified nor eliminated, because they are inbuilt into the system. In addition, potentially ineffective programmes continue to be funded year after year, because there is no public accountability for the results attained. By shifting the focus from inputs to outcomes and results, PB will potentially address this situation, directing any elements of waste to more pressing needs.

## **7.4 Performance information in budget documents**

### **7.4.1 Will the inclusion of PI in budgets enhance accountability?**

King (1995) maintains that continued efforts for the implementation of PB stem from the need for public accountability. In line with this, the majority of the interviewees agree that the inclusion of PI in budget documents would enhance accountability and transparency<sup>49</sup>. The compilation of PI would be useful for measuring the outputs/outcomes expected to be delivered with the budgeted expenditure. According to a former Minister for Finance:

*“The approach to the budget preparation is wrong because the budget is not being compiled on the basis of what a ministry/department could deliver in terms of outputs, but on what that ministry/department is going to spend, irrespective of outputs/outcomes.”*

It was stated that performance measurement is fundamentally important in view of the fact that public officials are dealing with public funds and thus, they are accountable for the results obtained, to the citizens. In this regard, a performance budget facilitates the citizens’

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<sup>49</sup> Vide section 6.5.1



understanding of government's achievement vis-a-vis the programmes being undertaken (Shah and Shen, 2007 and McGeough, 2014). The respondents highlighted the constant pressure being exerted upon government to deliver more services with less funding, especially in the current fiscal and economic environment – this emphasises the indivisibility of policy results, budgeting and performance, as suggested by Lu et al (2015). Furthermore, the availability of PI enhances allocative efficiency in public spending (Robinson and Brumby, 2005 and Shah and Shen, 2007). Though research has shown that PB plays a limited role in determining final budget allocations, it still adds value to discussions and negotiations during the budgetary process (Ho, 2011).

There was also general agreement that PI should be used to hold public officials responsible for the actual performance of their department/programmes<sup>50</sup>. According to Young (2003), the inclusion of PI in budgets serves to hold public officials accountable for service quality, cost-efficiency, and programme effectiveness. Demaj and Summermatter (2012) maintain that PI provides the basis for performance appraisals by politicians.

Though public officials should be held accountable for the public money being spent, a few respondents maintained that where a target is not reached, emphasis should be placed on analysing the reasons for the underperformance in order to derive corrective action. Thus, the appropriate way to use PI would be to allow for better future performance, rather than to punish public officials for past underperformance. It was explained that it could be problematic to hold public officials responsible on the basis of PI, since there may be factors which affect the achievement of performance targets that are beyond the civil servants' control. In this respect, the Accountant General mentioned the unexpected expenditures which arise during the year, and which have to be provided for by reducing the allocated funds on

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<sup>50</sup> Vide section 6.5.1

other programmes. This, in turn, results in under achievement of the originally established targets for the programmes which suffer a budget cut. A public official from the Education Ministry referred to the measurement of the number of ‘early school leavers’, which is an important KPI in the education sector. It was explained that though considerable effort is made to reduce this figure, there are factors which affect this indicator that are outside the control of the classroom teacher or the school administration, including the child’s home environment. Another problem mentioned by a Permanent Secretary is political interference in the work of the civil service, which might result in a programme/activity going off track vis-à-vis the expected deliverables.

Nevertheless, unless public officials are made accountable for their performance, it would be difficult to obtain their commitment for reaching the stipulated targets. Having said that, where the outputs and outcomes are not reached, an analysis of the reasons and justifications for such underperformance has to be carried out for the sake of fairness, before holding any persons accountable for the under achievement. Furthermore, if the target is not attained, a key question that should be asked is whether the target was achievable and realistic in the first place. Therefore, any decision to increase or decrease the budget for a programme/activity and to hold a public official accountable for his/her performance has to be taken after careful analysis of all the factors which might have influenced the achievement of the pre-established target.

#### **7.4.2 Should rewards and sanctions be established?**

If PB is used to hold public officials accountable for their actual performance, a system of rewards and sanctions has to be established in order to reward civil servants who deliver the targeted results and to penalise public officials who perform poorly, as suggested by Hou et al

(2011). The table below summarises the suggestions made by the interview respondents vis-à-vis the reward and sanction mechanisms that could be applied<sup>51</sup>:

**Table 36: Rewards and sanctions**

Reward and sanction mechanisms suggested by interviewees
The award of performance bonuses to civil servants at the end of the year could be linked to the achievement of stated objectives.
Where the targets are reached, a department/ministry could be allowed to carry forward any savings made during a particular year to the following year, for use on a specific project.
Where a ministry/department achieves its targets, it would be allocated a higher budget in the subsequent year.
Given that government employees in managerial positions are subject to contracts that are renewable every three years, consideration for renewing or terminating a manager's contract could be based on his/her performance.
The achievement of performance targets could be one of the factors affecting a person's career development opportunities.

*Source: Interview data collected between August 2014 and April 2015*

With respect to the award of performance bonuses, there is already such a system in place in the public service's management structure; however, it was claimed by a number of respondents that the bonus is presently being considered as an extension of the basic salary and not as a reward for performance. If the performance bonus is to be used as a means for motivating performance, it is important that the bonus amount would be based on the measurement of the actual results attained by the civil servants, vis-à-vis the pre-established targets. This would only be possible if PI is compiled. Furthermore, an assessment of performance by the direct superior of the public official being appraised may pose a familiarity threat, because of the direct and close working relationship between the appraiser and appraisee. The appraiser may be too sympathetic to the appraisee's interests; he/she may

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<sup>51</sup> Vide section 6.5.1

wish to avoid any friction with his/her subordinate in order to preserve the relationship; or the evaluator may be too accepting of the appraisee's work. This would lead to the award of a higher bonus than that which the appraisee actually deserves. Thus, if performance bonuses are used as a means for rewarding achievement of targets, it is suggested that an independent body would be responsible for carrying out these appraisals, in order to ensure objectivity, accountability and transparency.

A few respondents expressed concern regarding the establishment of mechanisms to reward or sanction public officials for the achievement and non-achievement of performance targets respectively, in view of the risk of data manipulation by civil servants in order to show a positive picture of the results attained. Although this risk exists, the lack of a reward/sanction mechanism would not motivate public officials to strive to achieve the stated objectives. In order to mitigate this risk, it may be advisable to set rewards/sanctions at an entity level, rather than at a personal level, as suggested by a Health Ministry representative and in line with what was proposed by Burgess and Ratto (2003). Thus, it is suggested that adjusting a ministry/department's budget upwards in the following year or allowing such ministry/department to carry forward a portion of its savings to the next year, would be preferable than awarding performance bonuses or linking the achievement of targets to one's career development or employment contract.

### **7.4.3 Way forward**

In summary, the findings reveal that it is believed that the inclusion of PI in budget documents would enhance managerial and public accountability (Sinclair, 1995) and transparency and would enrich the decision-making process covering the allocation of resources (Shah and Shen, 2007). Furthermore, the data gathered shows that such PI should

be used to hold public officials responsible for the actual performance of their department. Where the actual performance is short of the pre-established targets, justification should be sought for such underperformance, in order to determine whether there were any factors impinging on performance that were beyond the control of public officials, and also, to implement corrective action. Additionally, it was determined that reward/sanction mechanisms have to be established, in order to be able to hold public officials accountable for their performance. It is suggested that such mechanisms would be set at an entity level, rather than at a personal level, in order to avoid data manipulation, lack of social responsibility, greedy behaviour and possibly focusing on short term results at the expense of longer term gains.

### **7.5 Influences prohibiting the implementation of performance budgeting and potential mitigating factors**

The assessment set out in section 7.2 above concludes that the institutional and macro-level pressures, which manifest themselves in the Maltese context, should potentially trigger the implementation of budgetary reform. Subsequently, section 7.3 discusses a number of shortcomings of the current line-item budgeting system, reinforcing the need for reform. Section 7.4 then establishes that it is desirable to start including PI in budget documents both for accountability and transparency purposes, as well as to enhance allocative decision-making in public expenditure. This analysis suggests that there are a number of factors which are pointing towards the need for the Maltese government to introduce a performance-based budgeting system.

Nevertheless, the findings also reveal that there are opposing forces which might inhibit the implementation of PB, as discussed hereunder.

### 7.5.1 Resistance to change

As discussed earlier, the current line-item budgeting system is deeply embedded in the Maltese government's existing practices and routines. Jepperson (1991) and Burns and Scapens (2000) suggest that changes to an embedded system or to existing 'routines and institutions' might come up against resistance from the parties who will be affected by the changes. Similarly, Greenwood and Hinings (1996) maintain that resistance to change could be a result of an organisation's embeddedness in its institutional context. In line with these observations, all the interview participants claimed that should government decide to introduce a PB system, there would certainly be resistance to change from public officials<sup>52</sup>. A number of respondents attributed this resistance to the fact that a PB system would tighten the control on government spending and clearly, "*nobody likes to be controlled*".

Though the empirical data is suggesting that stricter control might be undesired, there might be some line ministries that are delivering results, who would welcome these additional controls. In this regard, the establishment of reward mechanisms for motivating those public officials who are achieving the desired results<sup>53</sup>, assumes significant importance. If, as a result of the budgetary reform, civil servants who achieve the performance targets get rewarded, they would perceive the new system as being in their interest and would willingly collaborate in its implementation.

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<sup>52</sup> Vide section 6.6.1

<sup>53</sup> Vide section 7.4.2

A former Prime Minister summed up the views of a number of interviewees in the following statement:

*“Resistance would be unavoidable, because a performance based budgeting system will shed light on the performance of public officials, inevitably highlighting weaknesses. Though the positive performance would be disclosed together with the negative performance, it is the negative performance which would be given the most prominence. Thus, if only one out of ten items shows negative performance, it is that item which will feature in the front page of a newspaper, with nobody mentioning the remaining nine positive achievements. Both the civil servants and the responsible minister would not be too happy to be in the limelight for negative performance issues.”*

The implication of this statement is that the budgetary reform is expected to come up against resistance from both the civil service and the politicians, who would then have to justify their department’s or ministry’s spending in terms of outputs and outcomes.

The findings imply that the reform would be going against a deeply established culture, where the civil servants and the politicians are not used to performance measurement. In this regard, Burns and Scapens (2000) have referred to ‘mental allegiance’ to established ways of thinking and doing, which is an element that gives rise to resistance to change. Both the civil service and politicians might, in fact, perceive the practice of performance measurement as threatening their positions because weaknesses would be highlighted and responsibility would have to be assumed for such weaknesses. These concerns might stem from an unwillingness of public officials to be fully committed to delivering results; however, they might also arise from a genuine fear that the pre-established targets might not be reached due to political interference or economic factors, which are beyond the civil servant’s control. In the former case, in order to mitigate the resistance of going against a culture of inertia, the reform has to be championed by a person/s who is/are in a high position of power, presumably the Prime

Minister, the Minister for Finance and/or the Permanent Secretary within the MOF<sup>54</sup>. Kasek and Webber (2009), Ho (2011) and Willoughby (2011) mention that strong leadership and championing by key people are fundamental elements for successful budgetary reform. According to Shields and Young (1989), a champion is a manager who comes from the higher level of the hierarchy within the organisation, guides the implementation team and raises resources for the implementation of the system. The existence of a powerful champion is also critical for ensuring the cooperation of the line ministers in the implementation of the reform. The most effective champion would be the Prime Minister, who has the power to appoint or remove from office, the ministers. In order to address the genuine fear of not reaching targets which are uncontrollable by the public officials, the budgeting process should include a procedure (such as the compilation of a report) which carries out a variance analysis with justifications, in situations where the actual performance falls short of the stipulated targets.

Resistance to change is also shown where the parties affected by the change are uncertain as to what the reform involves and whether it will impact their work load, financial situation and/or career opportunities. This issue could be addressed through the communication of adequate information to the parties that will be impacted by the change. Furthermore, the importance of the provision of training to public officials, both at development stage and on an on-going basis, cannot be underestimated.

In addition to the mitigating factors discussed above, some other suggestions put forward by the interviewees are summarised in the following table:

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<sup>54</sup> It became very clear through the empirical data collection process that the MOF's Permanent Secretary is highly involved in the decision-making process covering the budget allocations.



**Table 37: Factors mitigating resistance**

Factors identified by interviewees for mitigating resistance to change
External consultants, with adequate experience in the implementation of PB systems in other countries, should be brought in to assist in the reform process.
The PB system should be designed in such a way that underperformance is highlighted earlier on in the year, in order to allow for corrective action. Where circumstances change during the year, such as reducing the budget for a ministry/department, there should be the possibility of revising the performance targets.
Civil servants should be consulted and involved during the system development stage. In this respect, a communication and training strategy should be in place.
The necessary resources should be dedicated for the implementation of the budgetary reform. This includes recruiting people with the required expertise in the ministries.
It has to be ensured that the established performance targets are realistic and that the system for measuring public officials' performance is fair.
Obtaining the support of the general public for the implementation of PB would certainly facilitate the reform process, since the citizens are naturally in favour of enhanced accountability and transparency. This could be achieved through feeding the local media with information on the objectives of the budgetary reform.

*Source: Interview data collected between August 2014 and April 2015*

In summary, the findings show that should government decide to implement PB, resistance will be **high** and it will be encountered from all parties involved, possibly including the line ministers. The overarching reason for this is that the reform will have to bring about a change in culture and in people's mind-set. As discussed above, there are a number of steps that could be taken to mitigate the resistance to change. Nevertheless, the fundamental element for overcoming the resistance and making the change happen is to have strong political commitment from the top, that is, the reform has to be championed by a powerful person/s at the top.

### 7.5.2 Personnel issues

The findings reveal that there is lack of adequately qualified public officials in government employment, which might act as a stumbling block for the implementation of PB<sup>55</sup>. Burns and Scapens (2000) claim that this factor could constitute an element of resistance to change.

This situation is a result of a number of factors, as explained hereunder:

- The person holding the position of an ‘accountant’ in the ministries, referred to as the ‘Director, Corporate Services’, is not required to have an accounting qualification. Such position could be held by a civil servant of any background, who would have moved up the civil service ranks. It was stated by the senior civil servant within the MOF that the finance function within the ministries, which is overseen by the Director, Corporate Services, is presently not very strong. One of the reasons for this could be that the person heading this function does not have the appropriate competences. In addition, a number of ministries do not employ an accountant, as observed by the Accountant General. As mentioned by an academic and advisor to the MOF, the weak finance function within the ministries is resulting in the line ministries placing heavy reliance on the MOF, for budgeting and other financially related matters. Unless the required human resource complement is recruited, this reliance on the central agency would be augmented with the implementation of PB, in view of the requirement to quantify performance measures and in view of the increased reporting obligations.
- It is very difficult for government to compete with the private sector for the employment of accountants, in view of the significantly higher remuneration packages paid by private

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<sup>55</sup> Vide section 6.6.2

employers. It is also difficult to change this situation, because if government increases substantially the salaries of a certain category of its employees, such that a significant disparity would be created between civil servants' salaries, unions would put pressure upon government to increase salaries across all the civil service, which would lead to higher government spending on salaries, resulting in a higher deficit.

- Low salaries are also an issue in the case of Maltese top civil servants, who are paid a considerably lower salary, compared to remuneration packages awarded to people in similar ranks within the Maltese private sector and compared to salaries paid to top civil servants in some other countries. This constrains the recruitment of high-calibre people for top positions with government.
- In order to achieve a high executive position in the civil service, a person has to be considerably older than for similar positions in the private sector, according to a former Prime Minister.
- There is lack of interest and motivation on the part of certain civil servants to learn, thus hindering staff development – a couple of respondents mentioned how difficult they find it to persuade people under their responsibility to attend courses. This finding ties in with what was discussed above regarding the need to go against a culture of inertia, in order to make the reform happen<sup>56</sup>.

Some of the above issues were highlighted by a Budget Office official, who observed that:

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<sup>56</sup> Vide section 7.5.1

*“Finding the right people to champion PB in the line ministries could be quite challenging. This is due to the existing limited human resources in the public sector; the employee turnover within the ministries/departments; and the fact that people, in particular, accountants, prefer the private sector for employment, both because of more attractive remuneration packages and also because of the perception that jobs in the private sector are more prestigious. There is the need to increase the staff complement and upgrade existing skills to have more accounting competences, in the ministries and departments, including within the Budget Office.”*

Overcoming the above obstacles is undoubtedly challenging; however, there are a few steps that could be taken to counterbalance these issues.

It is clear that the finance function within the line ministries lacks the appropriate human resources which are required to embark upon a budgetary reform. Therefore, if the reform is to happen, the finance function within the line ministries has to be strengthened, through the employment of suitably qualified staff. An increase in professional staff complement seems also to be required within some departments, including the Budget Office. Admittedly, as revealed by the findings, there are a number of challenges to recruit accountants and other professionals to work for the public sector; however, such challenges might potentially be overcome if government is truly committed to implement PB. As mentioned by a former Minister for Finance, government had, in the past, been successful in recruiting people with the appropriate IT expertise, when a decision was taken to modernise the IT system. In the same way, it could dedicate the necessary effort to employ people with the right competences, in order to enhance the ministries' finance function and possibly to lead the reform implementation process. It was also explained by a Permanent Secretary how the Health Ministry has managed to recruit a network of financial controllers by finding creative ways of offering a more generous package than that paid to accountants employed directly by government, whilst at the same time avoiding the distortion of government salaries.

As regards the lack of motivation shown by public officials to enhance their knowledge base through their participation in training courses, it is suggested that a minimum number of hours of training (say, 20 to 30 hours per annum) would be made mandatory for civil servants in certain grades, especially for those who hold managerial posts. This could also link to continuing professional education requirements of some professional bodies. In addition, the public administration organises and holds a number of courses, free of charge for employees, which are targeted at filling knowledge gaps within government departments. The fulfilment of the minimum mandatory training requirement by public officials could be linked to the award of their performance bonus and also to their career progression prospects.

As a recap, the findings indicate that the lack of suitably qualified personnel within the ministries and departments might prohibit the implementation of PB. As discussed above, there are possible solutions to these concerns, some of which have been successfully applied by the public administration in the past. Thus, personnel issues are being considered as having a **medium** influence on the prohibition of budgetary reform.

### 7.5.3 Political factors

The findings demonstrate that the political dimension is a very important consideration in the local context, which could seriously constrain the implementation of PB<sup>57</sup>. In this respect, a number of politically-related issues have been identified during the empirical data gathering process, as outlined in the table below.

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<sup>57</sup> Vide section 6.6.4

**Table 38: Political issues**

Political issues that might hinder PB implementation, as identified by interviewees
a) There could be an issue with holding public officials accountable for the actual performance of their division, in view of political interference. A Permanent Secretary claimed that public officers are not free to shift people around, even if they believe that such transfer could lead to better results.
b) The financial plans compiled by a line ministry are sometimes superseded by a political decision. This was explained in detail by a public official from the Education Ministry, who stated that during the course of the year, certain political decisions are taken which increase the ministry's spending and which, thus, send the ministry off track vis-à-vis the financial estimates that would have been prepared as part of the annual budget process.
c) It appears that government has no leeway, whatsoever, when it comes to reducing the staff complement of the public sector, in view of a heavily unionised environment. If a PB system is implemented, the ministries/departments would have to specify the human resources necessarily required for the programmes they plan to undertake, in order to link inputs to deliverables. It would be a problem to justify the salaries of those staff who are not contributing towards the outputs/outcomes of projects and activities; at the same time, government has its hands tied when it comes to making its employees redundant.
d) Government is also reluctant to decrease its staff complement, in view of the political damage that would be caused. In Malta, this has, in fact, never happened. Thus, certain practices, which are inefficient and which are absorbing a significant amount of public funds on a yearly basis, remain. For instance, as was mentioned by a number of respondents and as was determined by the National Audit Office (2015), there are a number of government schools with very small class sizes. Such schools are incurring an amount of fixed costs per annum, including teachers' and administrative staff salaries, maintenance costs and administrative expenses, amongst others. This practice and the exorbitant costs being incurred questions the need for a primary school in every locality in Malta, considering that the country is so small and commuting from one locality to another takes just a few minutes. However, government seems to be dragging its feet in taking action, because of potential political consequences. Another example of inefficiency identified during the interviews was the salaries paid to watchmen in schools which run into millions of Euros per annum – it would be much more cost effective to install CCTV cameras in schools than to pay these annual salaries. Again, reluctance to take action stems from the fear of political damage. Should government decide to take action in respect of the above-mentioned situations, teachers, administrative staff and watchmen, to name just a few categories, would have to be laid off, which will not happen in Malta. Alternatively, they have to be shifted to other jobs, increasing the salary cost of other government departments.
e) There is the political risk that government's effectiveness would be questioned should the actual performance fall short of the pre-established targets. Furthermore, PI which is below the expected targets could be used by the Opposition party to criticise government and hence gain political advantage. According to a former Prime Minister, though PB is undoubtedly the best budgeting system from a technical perspective, unless the potential negative political fall-out is addressed, the reform will not go through from a political perspective.
f) In circumstances where the set performance targets are not attained, there is the risk of data manipulation by civil servants in the performance reports that set out the actual results vis-à-vis the targets. To overcome this challenge, a culture and mentality change is needed, if PB is to be effective, according to a former Prime Minister.

*Source: Interview data collected between August 2014 and April 2015*

The above summary shows that issues are still very much politicised in Malta, despite the significant political and economic progress that the country has made. Could these political influences be mitigated?

With respect to the potential reduction in government's staff complement (discussed under points (c) and (d) above), this is very unlikely to be put into practice in Malta, in view of the strongly unionised environment and the political damage that would be caused to the party in government, as explained above. Having said that, employee reduction in the public sector could be carried out through natural attrition, by not replacing civil servants who leave employment, retire or die. It is appreciated that it will take time for the public sector to shed the excess personnel in government employment. In addition, government might need to fill certain posts which require specific skills and experience by recruiting employees externally; and it might not be able to transfer its excess employees to such posts. Where staff mobility across government is appropriate for removing excess staff from certain jobs and filling other posts, this practice should be put into operation.

There is certainly an element of political sensitivity, should actual PI be published, as mentioned under point (e) above. Nevertheless, the present government is committed to enhance accountability and transparency in its financial dealings, as revealed by the findings. Furthermore, as part of the budgetary reform, a performance report would be prepared after year end, comparing the performance targets with the actual results. If the reason for under performance in certain programmes is justified in view of unexpected circumstances or constraints which cropped up during the year, then the public would still appreciate government's efforts to deliver results. This view is also shared by the Prime Minister who stated that:

*“The publication of PI which highlights what has been successfully achieved and what needs improvement, would gain the public’s appreciation. The purpose of the publication of information has to be to encourage public officials, rather than to demotivate people who are delivering.”*

There is the risk that other more important/urgent issues will take precedence over budgetary reform implementation. For instance, will the Maltese government lose interest in PB if affected by issues such as mass immigration? This risk can be mitigated if the reform is pushed forward by a person/s at the top.

In summary, the findings show that the implementation of PB could be hindered by the **high** political influences discussed above, coupled with the limited mitigating factors that could be applied.

#### **7.5.4 Summary**

The elements constituting resistance to change as outlined by Burns and Scapens (2000), namely resistance due to competing interests, resistance due to lack of knowledge and experience and resistance due to a ‘mental allegiance’ to established ways of thinking, are all substantiated by the interview findings. In addition, the data demonstrates that resistance is also envisaged in view of the fact that PB is believed to tighten the control on spending by public officials and to highlight weaknesses in performance; thus, it may be perceived as threatening the positions of civil servants and of politicians. Resistance might also stem from a genuine uncertainty as to what the reform will consist of and how it will impact the work of the public officials involved in the budgetary process.

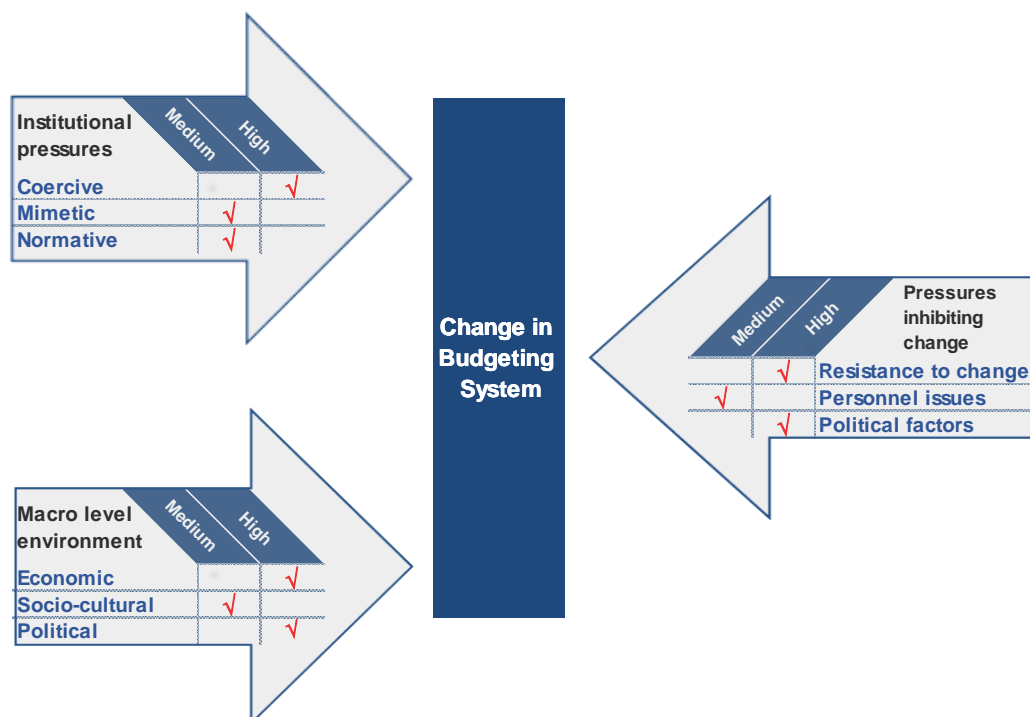
The political aspect is a very significant influence in the Maltese scenario. The reason for this could be that in Malta, there are two main political parties, and the party that wins the general election usually surpasses the other party by a small margin, typically by a few thousand



votes. As a result, the political impact of decisions is weighed very carefully before any action is taken by government, in view of the fact that a politically unpopular decision could tilt the balance in favour of the opposing party.

The discussion set out in this section necessitates an update to Figure 26<sup>58</sup>, which had incorporated the pressures supporting change in the budgetary framework. The revised figure, set out below, now takes into consideration the pressures prohibiting the implementation of PB.

**Figure 27: Pressures supporting and inhibiting change in the budgetary framework**



The analysis shows that there are medium to high pressures supporting a budgetary reform and opposing medium to high influences against change. The successful implementation of PB depends on whether the pressures inhibiting change can be effectively mitigated. The discussion has outlined a number of steps that could be taken in this respect. The most

<sup>58</sup> Vide section 7.2.5

important element for successfully reforming the budgetary system is strong political support from a powerful person/s at the top, who has/have the power to overcome the obstacles hindering change.

## **7.6 Type of organisational change expected**

The discussion so far has established that there are both institutional and macro-level pressures that support change in the Maltese budgetary framework. In addition, the current line-item budgeting system exhibits a number of weaknesses which further emphasise the need for change. Furthermore, the incorporation of PI in budget documents is considered as a desirable practice for enhancing accountability and transparency and bettering budget allocation decisions. In contrast, the analysis has shown that there are influences which might prohibit the implementation of PB and which, therefore, need to be controlled, in order for the reform to go through.

In light of this, this section seeks to determine the type of change expected in the local context, if any, using as a basis for analysis the Greenwood and Hinings' (1996) model<sup>59</sup>. This model has been used by Argento and van Helden (2009) for explaining reform processes. The internal dynamics of an organisation, namely, stakeholders' dissatisfaction, value commitments, power dependencies and capacity for action, determine whether it undergoes radical change as against convergent change<sup>60</sup> (Greenwood and Hinings, 1996). According to the authors, radical change could be problematic where a practice/system is deeply embedded in its institutional context, as is the case with the existing Maltese line-item budgeting system. The response of the Maltese public administration to the institutional pressures for change

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<sup>59</sup> Vide section 3.2.3

<sup>60</sup> Radical organisational change involves the transformation of the organisation, whilst convergent change refers to the fine tuning of the existing orientation (Greenwood and Hinings, 1996).

will be analysed through an examination of the internal dynamics surrounding the budgetary framework. The endogenous or internal dynamics of the model have been classified by Greenwood and Hinings (1996) as precipitating dynamics (stakeholders' dissatisfaction and value commitments) and enabling dynamics (power dependencies and capacity for action).

### **7.6.1 Diverging levels of stakeholders' dissatisfaction with the current system**

The interview data shows that there are, mainly, two groups of stakeholders which can be distinguished with respect to their diverging level of dissatisfaction with the existing budgeting system.

The first group, which consists of the majority of the research participants, believe that the existing budgetary system needs to undergo a total reform.

It was claimed by an economist and advisor to government that the existing line-item, expenditure based budget, is out-dated. Furthermore, a few respondents stated that budget allocation decisions are largely in the hands of civil servants within the MOF. The line ministers, who would have been involved in discussions with the MOF vis-à-vis their business plans and corresponding request for funds, would be informed on the actual amount of funds voted to their ministries a few days before the budget is laid before Parliament for approval. This was also confirmed by a representative from the MOF who added that allocations to the respective line ministries (which are usually lower than the funds originally requested) are not done in the line ministers' presence, in order to avoid disagreements between the MOF and the line ministers. This lack of confrontation between the ministries and the MOF on the finalised budget allocation is frustrating and demotivating for the line ministries, who do not have the opportunity to contest or, at least, understand the rationale behind the MOF's actions.

Another issue that came up during the interviews and which clearly shows dissatisfaction with the current budgeting process is the lack of performance measurement within the system. A few participants mentioned that budget allocations are done irrespective of value for money concepts, since no analysis is carried out as to what an activity is costing in terms of its expected outcomes. In this regard, two former Finance Ministers and the Minister for Finance presently in office mentioned that the business plans presented by the line ministries are not measured in terms of the objectives and outputs expected to be achieved. The Minister for Finance stated that:

*“When line ministries submit their business plans in support of their funding requests, they do not present any output indicators. Unfortunately, the ministries expect that the MOF will accept all the requests for funding, without having carried out a detailed analysis of the outputs and outcomes to be delivered through the inputs, without having ascertained what their priorities are and without having identified where efficiency gains can be made.”*

This concern was substantiated with examples brought up during the interviews – a case in point is the issue in the education sector where recurrent expenditure and capital outlays are always on the increase, notwithstanding the decline in the country’s birth rate. It was mentioned that the results being attained in the education sector are not commensurate with the spending dedicated to this sector. This situation signals the need for radical change in the budgeting system such that the allocated funds would be better justified in terms of the outcomes/results obtained.

The incremental approach presently adopted was heavily criticised by a Permanent Secretary who stated that priority should be given to expenditures that are genuinely needed, rather than allocating funds to programmes simply because such expenditure had featured in previous years’ budgets. This issue could be addressed with the inclusion of PI and targets in budgets.

Another issue mentioned during the interviews was the short timeframe allowed for the preparation of the budget. This is resulting in the line ministries not having enough time to consider any measures of efficiency during the budget compilation process and the MOF lacking the time to analyse in detail the business plans submitted by the line ministries.

The second group of stakeholders, consisting of a Budget Office official and the MOF senior civil servant, demonstrated a much lower level of dissatisfaction with the current budgeting system itself. The former mentioned that some budget reforms have already been implemented recently, adding that there might be the need for further *small* improvements. This implies that the respondent does not envisage the need for a radical change in the Maltese budgetary system, but is more in favour of convergent change.

The senior civil servant within the MOF attributes the problems in the country's public finance to the policies being employed by government in the high spending sectors, including education, health, social welfare (inclusive of pensions), and the care of old people. Communicating a feeling of frustration, the respondent claimed that changes are required in respect of policy stances in these areas, rather than *vis-à-vis* the budgetary framework. Though the interviewee is clearly dissatisfied and concerned with the constantly increasing government expenditure which is not always being adequately compensated by the increase in revenue generation, the statements made imply that this participant does not see the need for a reform in the budgeting process since such reform will not be enough to address the fiscal deficit issues being faced by the country.

Care has to be exercised when analysing the comments made by the second group of stakeholders – these respondents are public officials from the MOF who are heavily involved in the decision-making underlying the budgetary process. Therefore, it is understandable that

they might be reluctant to criticise the current budgeting system, of which they form an integral part and to which they are significant contributors.

Thus, the views expressed by the first group of stakeholders, representing the majority of the interviewees, are potentially more objective than those expressed by the second group, given that the respondents from the second group have a vested interest to preserve the current system in order to avoid self-criticism. The strong dissatisfaction with the current budgeting system, expressed by the first group of stakeholders, can be considered a stimulus for radical change according to Greenwood and Hinings (1996). Nevertheless, given the influential position of the MOF representatives, their diverging views can give rise to an element of resistance to change. This can possibly be managed and controlled, depending on the significance of the other intraorganisational dynamics comprised in the Greenwood and Hinings' (1996) framework, as discussed below.

### **7.6.2 Preference for the existing versus the alternative system**

Argento and van Helden (2009) advise that dissatisfaction does not automatically provide an alternative option. Greenwood and Hinings (1996) maintain that radical change will only occur if the dissatisfied stakeholders link the problems being faced to the existing system, and there is the possibility of an alternative template. The above discussion shows that the first group of stakeholders is linking government's position of disadvantage in designing the right policies and making optimal budget allocation decisions to the existing budgeting system. These stakeholders firmly believe that the current system needs to be reinvented, since it is not adequately serving its purpose as a tool for decision makers to make the best budget allocation choices in the country's economic interest. The findings demonstrate that there is the possibility of an alternative system – in this regard, a large number of participants from

the first group of stakeholders referred to the usefulness of moving towards a PB system, which would allow for the measurement of efficiency and effectiveness in government's programmes and initiatives. In addition to the need for performance measurement, there are other issues which have to be addressed if the reform goes through. To recap on the above discussion, it is recommended that ultimate responsibility for budget allocation decisions should lie with government, rather than with civil servants within the MOF. Additionally, the actual amount of funds voted to the ministries should, ideally, be carried out in the line ministers' presence in order to ensure transparency; if this is not practical in view of the possible clashes and difficulty to reach agreement, the vote (which is usually lower than what the ministries had originally requested) should be communicated to the ministries as soon as it is decided, in order to allow for adequate adaptation by the ministries and departments. Finally, the time frame allowed for budget compilation should be lengthened in order to provide enough time for detailed planning.

In accordance with Greenwood and Hinings (1996), a significant factor which may give rise to reform is the pattern of value commitments. Radical change is only possible if stakeholder dissatisfaction is complemented by a competitive or reformative pattern of value commitments (Greenwood and Hinings, 1996). The findings and the foregoing discussion suggest a competitive commitment, whereby the first group of stakeholders expressed their wish to see an alternative system, whilst the second group were not against the template-in-use. Though the second group of stakeholders did not criticise the existing system, they are certainly aware of the country's fiscal deficit issues and the need to control government spending by being more effective and efficient. However, one of the respondents is attributing these issues to government's policies rather than to the budgeting system, stating that PB will only improve the public finance situation slightly. Thus, the effectiveness of the budgetary

reform in solving the country's public finance issues is being questioned by this top civil servant, even though the interviewee did not voice his opposition to the implementation of PB.

### **7.6.3 Does the budgetary reform have support at the top?**

Power dependencies have been identified by Greenwood and Hinings (1996) as enablers of radical change. Where there are divergent views on the proposed reform (competitive pattern of value commitment) as is the case with the implementation of PB in the Maltese scenario, radical change will be possible if the people in positions of power support the proposed change (Greenwood and Hinings, 1996). This observation was substantiated by the interviewees, who claimed that political support will push the reform to happen and will ensure that it is carried out faster from a timing perspective. McGeough (2014) suggests that when PB is in operation, political drive is also fundamental to stimulate the use of PI and the development of performance targets.

A number of interview respondents who hold powerful positions appeared to be supportive of budgetary reform implementation. Some of the powerful people interviewed who are in favour of PB include an economist and advisor to government, an academic and advisor to the MOF, the Minister for Finance and the Accountant General. As shown by the findings, there were other respondents who strongly support the implementation of PB; however, they are not considered key people in strategic positions, even though they could still influence the reform process.

The Prime Minister, who is the head of the public service and who arguably holds the most powerful position in the public administration, stated the following when asked whether PB should be introduced: “*yes, an unqualified yes...*” Nevertheless, the findings also show that



the respondent is very cautious of changing the current system, given that this system is an institutionalised practice which has worked and served the country for years. This fear could be a result of the fact that the new administration has been in office for a relatively short time (since 2013) and it is still in the process of gaining in-depth understanding of how the budgeting system is working. This has been implied by the comment made by the Prime Minister, stating that the existing system is presently controlled by a handful of civil servants spread across a number of ministries. This statement also reinforces the claims made by some respondents who maintained that the budget allocation process is largely in the hands of public officials, rather than in the hands of government who is ultimately responsible for the budget<sup>61</sup>.

Another person in a key position is the senior civil servant within the MOF. As discussed earlier on, this stakeholder has reservations vis-à-vis the implementation of PB. Although it is acknowledged that a budgetary reform which shifts the focus from inputs to results “*will improve the public finance situation slightly*”, the real issue that needs to be addressed if financial sustainability is to be improved is the change in policies that has to be effected in the high spending sectors, according to the interviewee.

The preceding analysis suggests that the key people holding positions of power have diverging views with respect to the implementation of the reform, with some of them being strongly in favour of the change and others having some reservations. The occurrence of radical change depends on whether those powerful people in favour of the budgetary reform are in a position to exert enough influence on government to ensure that the change is embarked on. The support and championing of the reform by the Prime Minister is, nevertheless, fundamental for the change to happen. It is pertinent to mention that there are

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<sup>61</sup> Vide section 7.6.1

both institutional and macro-level pressures (including high coercive isomorphic pressures and high economic and political influences) for changing the current budgeting system<sup>62</sup>, which could possibly push government to implement the budgetary reform.

#### **7.6.4 Capacity for action**

Another enabler of radical change is capacity for action, which is the ability of transitioning from the existing system to the alternative system, according to Greenwood and Hinings (1996). The Greenwood and Hinings' framework (1996) proposes that if capacity for action is supported by a competitive pattern of value commitments (as is the case in the Maltese scenario), radical change would be possible.

The findings indicate that the competencies required to operate within the new system might be lacking, in view of the limited number of adequately qualified public officials in government employment<sup>63</sup>. The analysis carried out earlier on indicated that personnel issues could act as a deterrent for the implementation of PB. It was, however, argued that a number of solutions could possibly be applied to overcome this barrier; thus, personnel issues were considered as having a medium influence on the prohibition of budgetary reform<sup>64</sup>.

The interview data also showed that investment in an accounting and IT system is required if government decides to implement a performance based budgeting system<sup>65</sup>, since the existing accounting and information system is old, it is not user-friendly and it is incapable of allowing data manipulation for producing reports as required. In this regard, government is presently in the process of changing the current accounting system in view of its plans to implement accrual accounting. Thus, this hurdle is presently being addressed.

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<sup>62</sup> Vide section 7.2

<sup>63</sup> Vide section 6.6.2

<sup>64</sup> Vide section 7.5.2

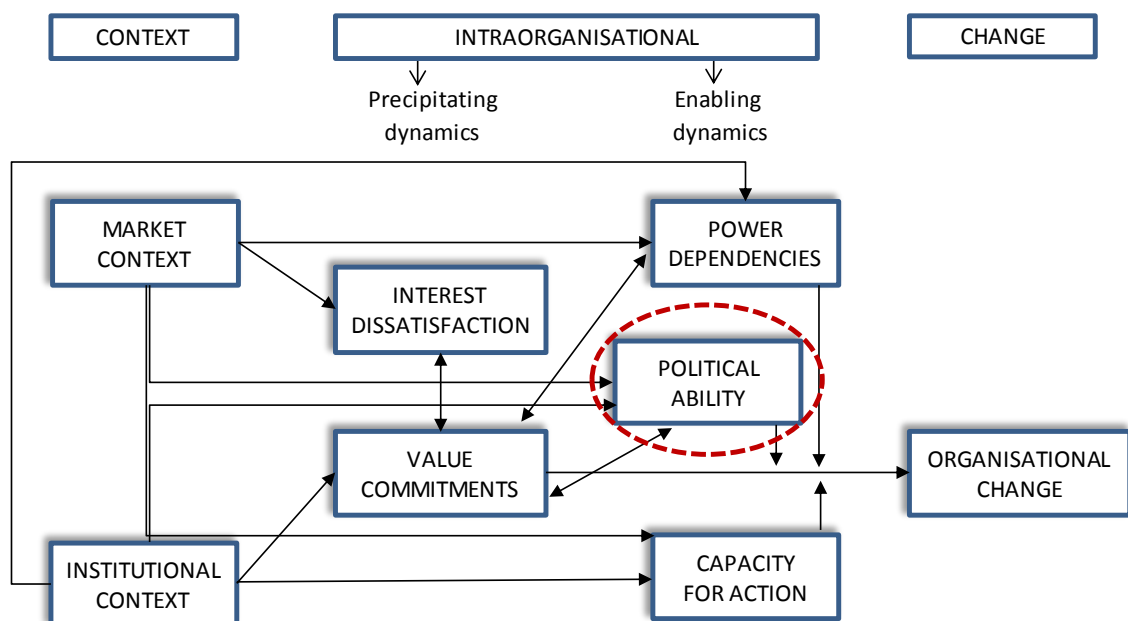
<sup>65</sup> Vide section 6.6.3

In accordance with Greenwood and Hinings (1996), a further important element for facilitating the transition to the alternative template is to have a good understanding of the new system and a clear road map to ensure that the design of the system captures the pre-established objectives and addresses the weaknesses of the template-in-use. This emphasises the importance of bringing in external consultants who have the appropriate experience in budgetary reform implementation, as well as having in place, a communication and training plan for civil servants.

### 7.6.5 Political ability

The findings suggest that within the Maltese scenario, there is a third enabler of radical change, being the political ability required to make the reform happen. As a result, an adjustment to the Greenwood and Hinings' (1996) framework is suggested in respect of the intraorganisational dynamics of the model, as set out below.

**Figure 28: Model for understanding organisational change (Adapted) (Source: Greenwood and Hinings, 1996: 1034)**



The interview participants mentioned a number of political issues which could constrain the implementation of PB<sup>66</sup>, as summarised in the table below.

**Table 39: Political concerns constraining PB**

Political issues which could constrain the implementation of PB
a) Political interference in the running of government departments does not allow civil servants the freedom to restructure operations and work processes for the purpose of enhancing efficiency and effectiveness. In this respect, it was mentioned that top civil servants do not have a free hand to transfer people around even if it is believed that performance would be improved as a result of such transfer.
b) It is extremely difficult for government to shed any excess staff, in view of the heavily unionised environment in public sector employment and because of the political damage that government would suffer. This problem is very relevant, given that wages and salaries of government employees represent a significant portion of the ministries' recurrent expenditure.
c) The financial plans and estimates prepared by the ministries as part of the budget process are sometimes overridden during the course of the year by a political decision. An example was cited in this regard of a programme which had been adequately provided for in the financial estimates, but which subsequently suffered a huge cost overrun, because of a decision taken by the Minister to open the programme to a much wider audience.
d) There is the political risk of putting government's effectiveness into question, should actual performance not reach the pre-set targets. This could also be used by the party in opposition to gain political advantage.

*Source: Interview data collected between August 2014 and April 2015*

In terms of the first three issues, former Prime Minister Dr Sant (2012: 112) observes that:

*“The public sector provides the scope for a spoils system that helps parties to cement their political ties with supporters”.*

A PB system embraces the measurement of performance and linking the expenditure to the planned results and outcomes. This requires shifting staff around activities, if necessary, and may also necessitate reducing the staff complement for certain programmes, in order to better the allocation of resources with the purpose of improving outputs. Additionally, expenditures

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<sup>66</sup> Vide section 7.5.3

on programmes should be justified in terms of the expected results and should also not exceed the budget allocation, unless unexpected events crop up.

In this respect, transferring people around or making staff redundant would definitely be politically unpopular actions which would result in the loss of political points (translated into loss of votes during a general election) for the party in government. Conversely, widening the scope of an activity or programme, as mentioned above, would win votes for the governing party.

In view of the above discussion, the following question needs to be answered: can the political forces prevalent in the Maltese context be addressed in order to enable radical change?

The analysis carried out earlier established that the political factors are considered as having a high influence on the prohibition of PB implementation in the Maltese public sector. In order to address the issue of political interference, the problem of budget plans being overridden by political decisions and the issue of political sensitivity when actual results falling short of targets are made public, a culture change is required throughout the civil service and amongst the politicians. The findings reveal that this is far from an easy task in the local scenario. Such culture change requires time and extensive education and training. In order to start introducing this culture change, support from the people at the top is fundamental. Thus, radical change would only be possible if the people in positions of power support the new way of doing things and dedicate the required resources to drive the reform. Furthermore, better planning is called for to tackle the issue of plans being superseded by certain political decisions – there has to be the willpower from the top to turn down line ministries' requests for funding which would not have been planned for in the budget (unless it is a matter of

national or strategic importance). Such initiatives/programmes could be postponed and subsequently included in the following year's budget.

The reduction in staff complement within government is highly unlikely in Malta, and thus, as discussed earlier on, this problem has to be mitigated through the application of the concept of natural attrition, where employees who leave employment, retire or die, would not be replaced. This is applicable, for instance, in the education sector where government might end up with an excess number of teachers and other administrative staff, should it decide to close down schools with a small number of students and transfer such students to other schools. In other situations, staff mobility should be put into practice, whereby excess employees in certain posts could be shifted to other roles which have a shortage of staff, if the skill set of such employees is compatible with the new role.

Therefore, the political forces within the Maltese context could, to a certain extent, be controlled, thus, making radical change possible. This is a challenging endeavour, which requires effort, resources and championing from the top. If political ability is supported by a competitive (as is the case in Malta) or reformative pattern of value commitments, then radical change would be possible.

### **7.6.6 Recapitulation**

Institutionalisation can obstruct change because practices in an organisation become deeply embedded within that organisation, according to Argento and van Helden (2010). In line with Greenwood and Hinings (1996), a radical change to the existing Maltese budgeting system could be problematic, due to the fact that the system is an institutionalised practice and thus, change could be resisted from the parties affected by the reform. Nevertheless, as discussed

earlier, there are a number of institutional and macro-level pressures which might trigger the implementation of PB.

In summary, two main groups of stakeholders can be distinguished with respect to their differing degrees of dissatisfaction with the current budgeting system. The first group, consisting of the majority of the interviewees, opined that the budgetary system needs to be reinvented. The second group, consisting of two top civil servants from the MOF, demonstrated a considerably lower degree of dissatisfaction with the existing system. The findings show that the first group of stakeholders is attributing the difficulties faced by government in making optimal budget allocation decisions to the existing budgeting system. A number of participants suggested that government should embrace a PB system as an alternative template. As a result, a competitive pattern of value commitments prevails, whereby the first group of stakeholders have expressed their wish for the implementation of an alternative budgeting system, whilst the second group did not criticise the template-in-use. (It is pertinent to note that the second group did not openly oppose the alternative template). In line with Greenwood and Hinings (1996), in the case of a competitive commitment, radical change is possible if powerful people are supportive of the reform. The analysis concludes that there are diverging views vis-à-vis the reform, amidst the people holding positions of power in the Maltese public administration, with some of them being strongly in favour of the change and a few having some reservations. As regards the ability of moving from the current to the alternative template, there are some deficiencies in the competencies required to operate within the new system, which could be addressed through the recruitment of qualified personnel and through the engagement of consultants who have already been involved in the implementation of PB systems in other countries. The findings have revealed a further enabling dynamic for radical change in the Maltese context, being the political ability to

embark on the reform. It has been shown that this requires overcoming a number of barriers of a political nature. The analysis shows that this is not an easy feat, and requires considerable time, effort and resources, and above all, championing from the people at the top.

In conclusion, it is suggested that the most significant impediment to radical change in the Maltese context is the political dimension. As stated above, if the reform is to go through, it has to be championed at the top, possibly by the Prime Minister and the Minister for Finance. It has been mentioned that the Prime Minister is, in principle, in favour of the implementation of PB, but has some reservations about changing a system which has served the country for years. There are, however, a number of key persons in positions of power (as stated above) who strongly advocate PB. Furthermore, it is important to restate that there are significant isomorphic influences and macro-level pressures for changing the budgeting system, which coupled with the internal dynamics discussed above, could lead to a radical change. In respect of coercive forces, an interviewee stated that:

*“PB is the only way forward, even because the EU Commission is pressing us to go that way.”*

## **7.7 Implementation strategy and underlying issues**

Hill and Hupe (2014) discuss the extent to which an implementation process should be positioned in its institutional context. The authors observe that:

*“...an examination of a policy process – and accordingly of an implementation process – needs to be seen as occurring in organised contexts where there are established norms, values, relationships, power structures and ‘standard operating procedures’ (Hill and Hupe, 2014: 37).”*

As established earlier, the existing line-item budgeting system is an ‘institution’ (Douglas, 1986) which has become deeply embedded in the country’s processes. In this respect, the



implementation of the budgetary reform has to occur within the existing organised context and thus, institutional theory is particularly pertinent and complementary to the study of policy implementation.

### **7.7.1 Top-down versus bottom-up perspective for budgeting**

The interview findings show that the existing budgeting system is largely based on the top-down approach<sup>67</sup>. It has also been suggested by the interview participants that should government decide to introduce a PB system, a more bottom-up approach should be followed in respect of the budgetary process<sup>68</sup>. For the purpose of the analysis, the ‘top’ represents the central agency, namely the OPM and the MOF, and the ‘bottom’ stands for the line ministries and the departments and agencies falling under their responsibility.

This proposed change in approach from top-down to bottom-up might be reflecting the need for more involvement of the line ministries in the preparation of the budget figures. This higher level of involvement of line ministries assumes greater importance if performance targets covering the ministries’ programmes and activities are introduced as part of the budget process, since the ministries and departments would have to assume ownership and responsibility for the achievement of such targets. Furthermore, a more bottom-up approach could serve to facilitate acceptance of the change to the existing deeply embedded system by the line ministries; thus, reducing resistance to the budgetary reform.

#### ***The existing budgeting system***

The current budgeting process mainly follows a top-down approach, according to the majority of the respondents. This was indicated by some of the comments made (see table below):

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<sup>67</sup>Vide section 6.7.1

<sup>68</sup> Vide section 6.7.2

**Table 40: Interviewees' comments on the existing budgeting process**

Interviewees' opinions on the approach followed by the existing budgetary process
<i>"...ultimately the budget allocation is decided by the MOF, with the ministries having to manage their projects within the allocated envelope of funds."</i>
<i>"...the budget process is strongly top-down...with the final allocation decisions lying with the MOF."</i>
<i>"The current budgeting system is very much top-down...the involvement of the central agency [is necessary] in order to arrive at a mature decision as to which programme should be prioritised."</i>
<i>"...the [allocation] decisions are taken centrally and the line ministries do not really have a say in the budget allocation."</i>
<i>"Although the system could be viewed as bottom-up because the line ministries are asked to make their budget submissions, the decisions are then taken from the top; and the decisions are final...much of the results of the bottom-up process are discarded."</i>

*Source: Quotes from interviews conducted between August 2014 and April 2015*

Though the line ministries are requested to compile financial plans covering their expected operations, such submissions are not analysed in detail by the MOF, according to the findings. It was stated that line ministries sometimes complain that it was useless preparing financial plans to back up their requests for funding, since the final allocation decisions were then determined by the MOF, with no consultation with the line ministries.

A number of interviewees attribute the adoption of the top-down approach for the budgeting process, to government's need to conduct its financial business within the parameters stipulated by the EU. In justification of the top-down approach, a few respondents stated that the MOF is responsible for supporting government in achieving its priorities and in carrying out its electoral promises; and thus it has to allocate funds to reflect such priorities. It was added that, in the absence of control by the MOF, the fiscal deficit would shoot up. The current system suggests a centrally located actor – the MOF – which is perceived as being the most relevant for achieving government's goals, in line with what was proposed by Paudel (2009). The top-down perspective has been justified by Hogwood and Gunn (1984 cited in

Hill and Hupe, 2014) on the basis that those who design policies are elected in a democratic way. The findings indicate that the budget allocation is very much in the hands of top civil servants within the MOF. In this respect, it should be noted that such civil servants were not democratically elected and therefore, it is important that the budget process, which has huge economic, political and social implications, should be revisited by government to ensure that the final allocation decisions are under government's control.

### *A performance budgeting system*

According to the interviews, the implementation approach for PB should embrace a mix of the top-down and bottom-up perspectives, with a tendency towards the bottom-up approach. This is in line with what was suggested by Berman (1980), who stated that when major policy changes are envisaged, as in the case of the Maltese budgetary framework, a bottom-up approach is recommended. Nevertheless, central intervention (through the involvement of the OPM and the MOF) is still required to ensure that government's priorities are being addressed and that this is done within the available funding.

With a PB system, the business plans of the line ministries have to incorporate performance measures and targets covering their planned programmes and activities. In order to ensure ownership and responsibility for the attainment of performance targets, the line ministries should be involved in their development – this suggests that a more bottom-up approach should be embraced, as suggested by the OECD (2007). Subsequently, the line ministries would be judged by the central agency on the achievement of the performance measures that they would have developed themselves. Cooperation between the parties involved, namely the central agency and the line ministries, increases the likelihood of successful implementation, according to Scharpf (1978).

Furthermore, according to the respondents, tending towards the bottom-up approach is advisable such that the ideas for programmes and initiatives would emanate from the people on the ground, who are more in contact with the needs of the public, in line with the idea of the street-level bureaucrats proposed by Lipsky (1980). In this respect, a former Prime Minister observed that:

*“The priorities should be set at OPM level, but then the programmes should be born from those people with experience on the ground. Government’s priorities and the ideas on the ground will then have to come together.”*

In their discussion of the variables involved in the implementation process, Mazmanian and Sabatier (1983) claim that successful implementation is more difficult to achieve where the extent of the behavioural change required is greater. The authors argue that if the group whose behaviour is subject to change is large, then it would be more challenging to achieve the stipulated objectives of the policy. In the local context, both the degree of behavioural change and the target group are significant and this implies that the top-down model may not be the most appropriate approach, because more involvement and participation by street-level implementers is required during the implementation stage to obtain their support and commitment to a PB system.

The local implementers should hold the relevant skills to operate the new system, if successful implementation is to be achieved, as observed by Hjern (1982). This emphasises the need for providing the required training to the individual ministries and departments prior to the implementation stage – in this respect, Greenwood and Hinings’ framework (1996) highlighted the importance of having the capacity for making the transition to the new system, which includes having implementers who have been trained and who have acquired the necessary skills.

It is envisaged that the role of the central agency would still be of fundamental importance. Firstly, government's strategies and priorities and the resulting policies have to originate from the OPM. As argued by Matland (1995), policy control should be in the hands of people who have been elected democratically and who are, thus, accountable to their voters. The programmes and initiatives proposed by the line ministries, together with the corresponding performance measures, have to reflect government's priorities and to take into consideration the spending ceiling set by the MOF. In this respect, the initiative recently introduced by government which requires that line ministries link their budget plans to the promises contained in the electoral manifesto, is a step forward for ensuring that government's priorities are being addressed. Secondly, with regard to the development of the performance targets by line ministries, the central agency would be responsible for ensuring that the targets stipulated are reasonable and appropriately benchmarked against international key performance indicators. In addition, the role of the central agency should involve issuing budget guidelines and monitoring how the line ministries are performing vis-à-vis the pre-established performance measures, on an on-going basis.

A former Finance Minister summarised his views as follows:

*“The bottom-up process would ensure commitment by the ministries/departments for achieving the pre-established performance targets. In addition, the role of the central agency would consist of the following: to coordinate the whole exercise; to monitor that the process is being carried out properly; to reconcile the available funds with the spending; and to negotiate with the ministries, if over-spending is envisaged, as to which projects would be given priority on a national basis.”*

The suitability of adopting the top-down versus the bottom-up approach for the implementation of PB in the Maltese scenario is further discussed hereunder, using Matland's (1995) ambiguity/conflict framework.

***Matland's (1995) Ambiguity/Conflict model***

Matland's (1995) ambiguity/conflict model<sup>69</sup> seeks to explain when it is appropriate to apply either the top-down or the bottom-up approach for policy implementation.

The findings show that a number of stakeholders consider PB as being the best system to adopt, from a technical point of view. Nevertheless, as discussed earlier, there are a number of influences potentially prohibiting the implementation of PB<sup>70</sup>, which might give rise to high *policy conflict*. Furthermore, there are divergent views as regards the planned activities and schedule for implementation. For instance, there are different opinions as regards the timeframe indicated for the successful implementation of PB, with some stakeholders proposing a timeframe ranging from ten to fifteen years, and others suggesting a shorter time period of between three to five years. The interviews also revealed diverging views with respect to whether the budgetary reform should be enacted in law or by means of policy guidelines. For the purpose of mitigating the potential conflict arising from the reform, it is advisable to involve key stakeholders at policy formation stage (including the OPM, line ministers, Permanent Secretaries and the Heads of government departments). This is in line with what was suggested by Van Meter and Van Horn (1975), who stated that the participation of involved parties at the policy formation stage facilitates goal consensus, which in turn increases the probability of successful implementation. Furthermore, the provision of training to involved personnel on their new responsibilities is fundamental to obtain their support for the new policy, according to the study carried out by Howard et al (2010) utilising Matland's model.

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<sup>69</sup> Vide section 3.3.5

<sup>70</sup> Vide section 7.5

In terms of *policy ambiguity*, the goals of the policy have been reasonably well defined during the interviews and include: better allocation of public funds, improving value for money obtained from government's programmes and enhancing the accountability and transparency of government's dealings. In addition, the means for achieving the policy objectives have also been identified during the empirical data collection process, though they may not yet be in place. It has been determined that the budgetary reform requires investment in an accounting and IT system – in this respect, plans are under way to change the existing accounting system. There is also the issue of lack of adequately qualified personnel to operate the new system – a number of solutions were proposed for tackling this issue<sup>71</sup>.

In accordance with Matland's (1995) model, the implementation of PB in Malta might be viewed as a *political implementation*, characterised by *high conflict* and *low ambiguity*. Matland (1995: 163) maintains that in this type of implementation, "*outcomes are decided by power*", that is, the implementer needs to have the power to force his/her will on the parties involved in order to reach agreement on actions. Similarly, Howard et al (2010: 940, 937) note that "*the central variable for successful implementation with political implementation is power*", that is, successful implementation is dependent on "*the power of the leadership to force compliance with the policy*". This substantiates the analysis coming out of the Greenwood and Hinings' (1996) model, which concluded that if the implementation of PB is to go through, it has to be championed at the top, possibly by the Prime Minister and the Minister for Finance.

Matland's (1995) model suggests that a political implementation process reflects more closely the orientations of a top-down perspective. This suggestion is in conflict with the conclusions coming out of the interview findings. Though the interviewees have suggested that a PB

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<sup>71</sup> Vide section 7.5.2

system should comprise a mix of both the top-down and bottom-up approaches, it has been advised that the latter approach should be emphasised in order to enable successful implementation in the local context. In this regard, the line ministries should be allowed to come up with their own performance indicators within the priorities established by government, on which they would subsequently be judged by the central agency. As such, the model proposed by Matland (1995) might be inadequate to describe the budgetary reform implementation in Malta, even because it might be impractical to label policies in such a rigid manner (Hill and Hupe, 2006).

Though no attempt is being made to make a new contribution to the typologies proposed by Matland (1995), the findings demonstrate that the proposed implementation in the local scenario cannot be analysed through a neat policy type. In this respect, it might be problematic to transfer policy learning across international boundaries, since such policies might undergo a transformation in a new institutional context. As regards the proposed budgetary reform in the Maltese scenario, the existing budgetary system is deeply embedded in its institutional context and as a result, policy implementation has to occur within this organised context. In these circumstances, a more bottom-up approach could be a better solution for facilitating the change from the existing institutionalised process to a performance based system and for mitigating the resistance that is expected to be put up by the parties involved.

### ***Way forward***

In view of the fact that the existing budgetary system is deeply embedded in its institutional context and in view of the major policy changes involved in order to implement a PB system, a combined approach, with more emphasis on the bottom-up perspective, is recommended.



The shift from the current top-down approach to a more bottom-up approach is potentially possible if a performance based system is adopted, since such a system allows for better control by the central agency. This is because the results obtained by the line ministries can be better assessed by comparing actual PI against the pre-established targets.

Nevertheless, central intervention is still fundamental in the local scenario, in order to ensure that government's priorities are being addressed and that this is being done within the established spending ceiling. This is important to ensure that government's objectives for the country are being met and also to observe the parameters laid down by the EU, including the targets stipulated for the fiscal deficit.

It is proposed that the top-down and bottom-up approaches are brought together as follows in the implementation of PB: from a top-down perspective, government's strategies and priorities and the resulting policies should originate from the OPM, in order to ensure that the objectives set by government for the country are being addressed. Subsequently, the budgetary framework setting out government's priorities and policies, should be approved by a Cabinet decision. This approval should happen early in the year, say in March, in order to allow ample time for the budgetary process. If the budget is to include PI, sufficient time should be allowed for a detailed analysis of such information as advised by Raudla (2012) who found that one of the reasons for the lack of use of PI by the Estonian finance committee was time constraints during the budget process. Approval by Cabinet ensures that politicians who have been democratically elected and who are, therefore, accountable to their voters, assume responsibility for the policies pursued, in line with what was argued by Matland (1995). The Minister for Finance would have the role of ensuring that government's strategic framework is achievable with the funding available.

The Cabinet decision would then be communicated to the MOF and to the line ministries, such that the financial plans that would be developed would reflect government's strategies and priorities. The responsibility for developing performance measures and targets would then lie with the line ministries, reflecting a bottom-up perspective. The request for funding by the line ministries should reflect the targeted performance. In view of the fact that line ministers are members of the Cabinet, they would have been part of the team approving the budgetary framework and thus, the programmes and corresponding demands for funds should be within government's strategic framework. Subsequently, the MOF would be responsible for reviewing the financial plans together with the performance measures that would have been developed by the line ministries in support of the funds requested to carry out the planned programmes.

The final budget allocation for the line ministries has to be determined by the MOF, who is responsible for overseeing the whole budget process. However, in contrast to what is presently being done, the budget allocation proposed by the MOF should be discussed with the line ministries before it is finalised, to ensure that any concerns that line ministries have vis-à-vis the planned activities and the corresponding funding are being addressed. The availability of PI could provide the basis for dialogue between the MOF and the politicians, as suggested by McGeough (2014) and Ho (2011). This dialogue would potentially reduce the existing problem of ministries regularly approaching the MOF during the year, to request additional funds. Another concern which was raised during the interviews was the fact that budget allocations are largely in the hands of civil servants from the MOF – the findings imply that a higher level of involvement of the Minister for Finance is desirable in the budget allocation process. In addition, if line ministers are involved in the discussions leading to the final budget allocations, this concern would be further mitigated.

## 7.7.2 Other implementation issues

### *Performance audit reports*

For the purpose of carrying out audits with respect to the quality and coverage of PI, the interviewees identified the following units as potential candidates for taking on this role<sup>72</sup>:

- the National Audit Office;
- a Quality Assurance Unit to be set up, possibly reporting to the NAO;
- an Internal Audit function to be set up under each ministry, reporting to the MOF; or
- the Fiscal Council.

In a number of countries, such as Canada, Australia and the UK, the Auditor-General audits the quality and coverage of departmental performance reports, on a sample basis (OECD, 2007). It is pertinent to point out that the Auditor-General does not audit budget material (OECD, 2007), as is the case in Malta.

In Malta, there are currently fourteen ministries – if each ministry, including the departments falling under that ministry, is audited every four years, three to four ministries would be audited every year.

The unit selected for this audit role could also assume responsibility for issuing principles of good practice for PI. This would ensure that performance reports compiled by the line ministries adhere to such principles and in turn, facilitate, the auditor's scrutiny process.

### *Type of performance budgeting*

There was general agreement amongst the respondents that it is best to start off with presentational PB<sup>73</sup>, where PI is included in budget documents as background information for

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<sup>72</sup> Vide section 6.7.4

the purposes of accountability and it does not play a role in decision-making (OECD, 2008). It has also been suggested that once the civil service and the politicians build up confidence in the new budgeting system, it would be advisable to move to performance-informed budgeting, where the compiled PI is used for budget decision-making, but it does not determine the amount of resources allocated (OECD, 2008). There might be certain areas or sectors where it would be appropriate to introduce direct budgeting, such that the funding allocated would reflect the results attained – the feasibility of this has to be assessed during the system design stage.

The discussion which follows explores the different type of PB systems (presentational, performance-informed and direct) and their bearing on the different levels of changes (radical versus convergent change and evolutionary versus revolutionary change).

Presentational PB provides no linkage between PI and funding (OECD, 2007), with the purpose of this type of PB being to enhance accountability rather than to influence the allocation of resources. As such, it can be argued that the adoption of presentational PB does not constitute a radical change (Greenwood and Hinings, 1996) from the existing system, since PI is provided as background information in budget documents and decision-making is not affected. Should the reform process stop with the introduction of this type of PB, there is the risk of fostering a symbolic rather than functional use of PI (Mimba et al, 2013), in view of the focus placed on presenting PI in budget documents rather than on utilising such information to inform and affect allocative decision-making.

Conversely, a performance-informed budgeting system makes use of PI in the budget decision-making process, even though the link between PI and funding is loose or indirect

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<sup>73</sup> Vide section 6.7.5

(OECD, 2007). In view of the fact that allocative decision-making is affected with this type of PB, it is argued that the adoption of such a reform would represent a radical change (Greenwood and Hinings, 1996) from the existing line-item budgeting system. Clearly, direct PB which involves allocating resources based on results achieved, would constitute a radical change from the existing line-item budgeting system. However, this PB type cannot be introduced across the board, since in certain sectors, it might be unfeasible to link underperformance to a reduction in the budget allocation in view of political, economic and social considerations, amongst others. Thus, it is advisable that direct PB would only be considered for selected areas, after careful consideration of the ensuing implications.

Radical change (Greenwood and Hinings, 1996) can be both evolutionary and revolutionary, depending on the pace of change. As mentioned above, the empirical evidence has indicated the respondents' preference to kick off the budgetary reform with presentational PB and then, once the parties affected by the reform build up confidence in a performance measurement system, performance-informed budgeting would be introduced. This suggests an evolutionary (gradual) rather than a revolutionary change (Greenwood and Hinings, 1996), starting off with presentational PB (which does not constitute a radical change), but then moving on to a performance-informed budgeting system and perhaps direct PB in selected cases (both of which represent a radical change from the existing system). This proposed course of action also makes sense in view of the cultural change required in the civil service to embrace a performance based system and in view of the challenges that have to be addressed<sup>74</sup> for the successful implementation of PB.

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<sup>74</sup> Vide section 7.5

***Reform enacted in law or through policy***

The Maltese public administration has to consider whether the budgetary reform should be enacted in law or by means of policy guidelines. Countries, which have implemented PB, have taken diverse routes in this respect - some (US) have introduced the reforms through legislation, others (Canada) have a mixture of policy guidelines and legislation, whilst other countries (UK) have not enacted the reforms in legislation but the central agency issues formal requirements (OECD, 2007).

The findings show diverging views on this issue, with some respondents arguing that if the reform is enacted in law, less monitoring might be required, and others stating that legislating the reform will not make a difference to successful implementation<sup>75</sup>. In the Maltese context, where it appears to be difficult to introduce change, as suggested by the findings, it might be advisable to introduce the reform through legislation. Though this will not guarantee successful implementation, the potential consequences of breaking a law might secure the ministries' and departments' cooperation in introducing the new system.

According to the OECD (2007), introducing the reforms through legislation ensures permanence if there is a change in government – the interview respondents did not attribute much importance to this, stating that if the system is working well, a new government will certainly not abandon the reform.

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<sup>75</sup> Vide section 6.7.5

### ***Timeframe for introducing performance budgeting***

As regards the indication of a reasonable timeframe for the successful implementation of PB, some respondents suggested a time period ranging from ten to fifteen years, whilst others proposed a shorter timeframe of between three to five years.

In this respect, it is advisable to dedicate sufficient time for the introduction of the reform, in view of the significant work and effort involved to establish PB, including design of the system, change in accounting and IT system, recruitment of adequately qualified personnel and training of staff, amongst others. Having said that, a time period of, say, three to five years should be reasonable. A longer timeframe would influence negatively the morale of the project team leading the implementation, the civil service and the politicians, since the absence of tangible results in the form of improvements in input-output relationships, would lead to complacency. In this respect, it is important to have a clear road map for the project, with clear milestones and timelines for achieving them. It is pertinent to note that the CSR exercise launched during 2014 could potentially be considered as a useful intermediary for embarking onto this budgetary reform, thus saving on the time required for introducing the reform. Through the CSR process, ministries were asked to determine what output was produced for each budget line item under 'programmes and initiatives'. In contrast to the proposed reform, the CSR focused on selected past expenditure; furthermore, the results emanating from the exercise were not fed into the budget.

Successful implementation within the stipulated timeframe requires high calibre people overseeing the whole project, possibly including representatives from the MOF working hand in hand with external consultants. In addition, a project leader from each line ministry should hold responsibility for coordinating with the central agency.

## 7.8 Synthesising Institutional Theory, Change Theory and Policy

### Implementation Theory

The foregoing discussion has established that the current line-item budgeting system has become deeply embedded within government's existing practices. Indeed, in accordance with institutional thinking (Douglas, 1986), the current system could be considered an 'institution'. Nevertheless, the empirical data has revealed institutional isomorphic pressures (DiMaggio and Powell, 1983) and macro-level forces (Munir et al, 2011) which might trigger a change in the Maltese budgetary framework. At the same time, there are potential impediments which might hinder PB implementation, including the envisaged strong resistance to change (Burns and Scapens, 2000), the lack of capability (knowledge and experience) to cope with such change (Burns and Scapens, 2000) and the political influences and interference prevalent in the Maltese scenario.

A review of Change Theory (Greenwood and Hinings, 1996) in combination with the gathered empirical data has shown that two groups of stakeholders can be distinguished with respect to their diverging degrees of dissatisfaction with the current budgeting system. The first group, comprising the majority of the interview participants, strongly believe that the existing system needs to be *radically* changed since it is not serving the purpose of effective and efficient allocative decision-making. Conversely, the second group which consists of two top civil servants within the MOF, showed a lower degree of dissatisfaction with the existing system, demonstrated some cynicism vis-à-vis PB implementation and were more inclined towards the implementation of *convergent* change. This analysis reveals a competitive pattern of value commitment (Greenwood and Hinings, 1996), whereby the first group prefers an alternative system whereas the second group is not overly critical of the existing system. It



has been determined that *radical* change in the Maltese budgetary framework is possible if this competitive pattern of value commitment is combined with: (i) the availability of resources and competencies required to operate the new system (capacity for action); (ii) championing of the reform from the people at the top (power dependencies); and (iii) the political ability to embark on the reform. In this regard, the empirical data suggests that the Greenwood and Hinings' (1996) model lacks an intraorganisational enabling dynamic which has been found to be significant in the Maltese context (being the political ability to embrace the reform). In accordance with Greenwood and Hinings (1996), a competitive commitment will lead to evolutionary (rather than revolutionary) change in view of the resistance encountered from certain groups.

This assertion is supported by the empirical data, which shows the interviewees' preference for a slow and gradual (evolutionary) change. Indeed, there was general agreement amongst the respondents that reform implementation should kick off with presentational PB and then, move towards performance-informed budgeting, once the civil servants and politicians build up confidence in the new system.

The findings point towards a combined (emphasising the bottom-up) approach for the implementation of PB. In accordance with Matland's (1995) ambiguity/conflict model, PB implementation in Malta is characterised by high conflict and low ambiguity, potentially leading to a political implementation. Matland (1995) suggests that a political implementation process contemplates a top-down approach, which assertion conflicts with the research findings.

By integrating institutional theory, change theory and policy implementation theory, this study seeks to address gaps identified in the individual theoretical frameworks.

Institutional theory has contributed towards the understanding of the institutional context surrounding a budgetary reform in the Maltese context and towards the identification of institutional pressures (DiMaggio and Powell, 1983) and macro-level influences (Munir et al, 2011) which might trigger such a reform. At the same time, change theory (Greenwood and Hinings, 1996) was valuable for determining the type of organisational change expected in the budgetary framework, for understanding the envisaged pace of change (evolutionary versus revolutionary), and for identifying the enabling dynamics (institutional capacities, power dependencies and political ability) required for a radical change to occur. Nevertheless, it was felt that these theories lacked the potential to indicate the implementation approach that should be followed for the introduction of PB in Malta. As a result, it was considered useful to complement institutional and change theories with policy implementation theory, in particular Matland's (1995) model which puts forward a theoretically based approach to implementation.

In this respect, it is suggested that Matland's (1995) existing implementation model be augmented to embrace other variables that affect the implementation process as revealed by the theoretical review and the empirical evidence. When determining the type of implementation which is most relevant for a policy process (top-down versus bottom-up view), in addition to the conflict and ambiguity levels surrounding the policy, it is proposed that the institutional context within which the implementation is occurring should be examined and taken into consideration. Where the policy being implemented represents a departure from an existing deeply embedded system, the literature review (Burns and Scapens, 2000) corroborated by the empirical data, indicates that the implementation would come up against strong resistance to change, which has to be addressed and mitigated. Furthermore, the application of change theory (Greenwood and Hinings, 1996) has

demonstrated a competitive pattern of value commitment where some parties fully support PB implementation, whilst others are not against the system currently used. Such value interests also point towards the expectation of change resistance coupled with the preference for an evolutionary change, as demonstrated by the empirical data. The findings show that a combined implementation approach (tending towards the bottom-up perspective) is the most appropriate within this organised context – this approach leads to a higher level of involvement of street-level implementers (Lipsky, 1980), thus obtaining their support and commitment to the new policy, which would in turn potentially reduce the envisaged resistance to change.

In summary, when seeking to establish the appropriate policy implementation approach (top-down versus bottom-up), it is suggested that Matland's (1995) model which is based on a policy's ambiguity and conflict level, should also consider other variables surrounding the implementation. Such variables comprise the institutional context within which the new policy is being implemented including the level of embeddedness of an existing system; the envisaged resistance to change; the pattern of value commitments; and whether a revolutionary versus an evolutionary change is expected. For instance, if an existing system is deeply embedded within its institutional context, such that a new policy would be expected to give rise to change resistance, then a combined (emphasising the bottom-up) approach would be more appropriate in order to obtain the street-level implementers' support (Lipsky, 1980) and ensure their ownership of the new system, thus mitigating the resistance to change. Furthermore, where a competitive pattern of value commitments prevails, whereby some of the people that will be affected by the reform are resisting the changes, the combined approach is also the most appropriate, according to the findings, for the reasons discussed above. Where resistance to change is expected, evolutionary change is the indicated course of

action (Greenwood and Hinings, 1996) in order to ensure acceptance of the new system before embarking on more challenging reforms (starting off with presentational PB and then moving on to performance-informed budgeting). An evolutionary change and a combined (emphasising the bottom-up) approach are complementary, since a slower pace of change is more conducive to a higher involvement of street-level implementers in policy implementation. This is because there is more time for allowing the street-level implementers to come up with their ideas/programmes and subsequently engage in discussion with the central agency before the policy is implemented. Conversely, a revolutionary change, which occurs quickly, is facilitated by the top-down approach where clear direction for policy implementation has to come from the central agency to ensure successful and quick implementation.

## **7.9 Relationship between PB and other institutional reforms**

This section discusses the relationship between PB reform and other institutional reforms that may be required within the Maltese public sector.

The findings show that it may be premature to introduce accrual budgeting in the Maltese scenario<sup>76</sup>. One reason for this is that the public administration is presently in the early stages of implementing accrual accounting for historical reporting (with the target date having been set for 2019/2020). As a result, public officials would first have to get used to financial reporting on the accrual basis, before government considers the adoption of accrual budgeting. Another argument brought up during the interviews was that politicians are more comfortable with a cash budget for the purpose of making allocation decisions, because the cash basis is simpler to understand, whilst the accruals system is more cumbersome. During

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<sup>76</sup> Vide section 6.8.1

the interviews, it was confirmed by the Accountant General that there are currently no plans to implement accrual budgeting. This position was taken notwithstanding the advice set out in the report compiled by the UK CIPFA, recommending that the budget framework should move to a full accrual basis in the medium to long-term, if the benefits of accrual reporting are to be realised<sup>77</sup> (Camilleri, 2014).

In line with Diamond's (2002) arguments, a number of interview participants claimed that accrual budgeting is not a prerequisite for the implementation of PB<sup>78</sup>. In this regard, there are countries, such as the US, Canada, Sweden and the Netherlands, which have a budget based on cash and commitments, and which have adopted a PB system (Sterck and Scheers, 2006: 66; Sterck, 2007). It was, however, argued by some interviewees that an accrual accounting system which presents a more complete picture of government's reported revenues and costs, is important for the successful implementation of PB.

Within this context, it can be concluded that though the adoption of accrual budgeting does not feature within the immediate plans of the Maltese public administration, this should not be considered as an obstacle for the implementation of PB. As regards the accurate reflection of revenue and costs in government's financial statements, this is currently being worked upon through government's plans to introduce accrual accounting for historical financial reporting. The implementation process for PB could still be kicked off in parallel with the preparation for the launch of accrual accounting, as the two systems are independent of each other. Once the accrual accounting system is up and running, the information fed from this system into the budgeting process would perhaps be more comprehensive, thus leading to an improvement in the development of performance measures and in the resulting budget allocation decisions.

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<sup>77</sup> Vide section 1.4.4

<sup>78</sup> Vide section 6.8.2

The implementation of PB would potentially support other institutional reforms needed in the Maltese public sector, including the promotion of good governance and the strengthening of the macroeconomic situation.

With regard to good governance, the publication of PI in budget documents keeps the citizens informed of what government is delivering with the public funds invested, thus enhancing transparency in government's dealings (Shah and Shen, 2007). Another aspect of good governance is the simplification of procedures – whether in fiscal matters, investment or other areas, administrative procedures have to be as simple as possible. In this respect, the findings have revealed that, since 2014, the highest-ranking civil servants (Permanent Secretaries) are being appraised on specific indicators, including 'simplification of procedures', amongst others. As has been discussed earlier, it is suggested that PB implementation will be complemented with the establishment of reward and sanction mechanisms, in order to 'remunerate' or 'penalise' public officials in accordance with their performance, on the basis of pre-established KPIs. 'Simplification of procedures' could be one of the indicators specified for performance measurement. A further area of good governance that government should focus on is the fight against corruption – this is imperative for strengthening economic management efficiency and promoting healthy competition.

Lu et al (2015) believe that PB has an important role to play in public budgeting and governance, provided that PI is used in a functional rather than in a symbolic way for the sole purpose of establishing legitimacy (Mimba et al, 2013; Van Reeth, 2002). In turn, good governance promotes the development of a dynamic private sector, which is essential in view of its function as the main engine for economic growth. Thus, transparency vis-à-vis the spending of taxes paid by the private sector should be enhanced, burdensome bureaucratic or

regulatory procedures that could slow the private sector's expansion should be minimised, and corruption which stifles competition should be tackled.

The literature review (Robinson and Brumby, 2005; Murray and Efendioglu, 2011) and the empirical data have shown a link between PB and the macro-level environment. PB potentially enhances productive and allocative efficiency by directing resources towards programmes that are delivering products and services effectively and targeting budget cuts at programmes which contain wasteful spending or which are ineffective. In this regard, Caiden (1998) and Aristigueta and Justice (2006) claim that the application of outcome information in resource allocation could be problematic. According to the interviewees, PB will help to control the country's deficit situation and to facilitate the achievement of a balanced budget in structural terms, thus leading to the stabilisation of the macroeconomic situation. In this context, as discussed earlier, the recently enacted Fiscal Responsibility Act is an important institutional reform comprising a number of reforms impacting the budgetary framework. This law, which has placed budget process under greater scrutiny, will potentially pave the way for PB implementation.

## **7.10 Education and health**

As part of the research undertaken, a number of interviews were conducted with representatives from the education and health sectors, as indicated in the discussion set out in this document. In this respect, it was considered important to take into account the views of the line ministries, in addition to the views of the central agency and those of other stakeholders in the budget process. The education and health ministries were selected for this purpose, firstly, because they represent the two largest spenders, and secondly, because expenditure within these ministries is expected to keep increasing.

With respect to the education sector, the main concern which was brought up by a number of interviewees was the fact that the student population is decreasing, yet expenditure in this sector continues to rise. It was mentioned that one issue which is contributing to this situation is the inefficient use of resources and the lack of economies of scale which is driving up costs in this sector. In this respect, there are a number of government primary schools with a very small number of students; these schools, however, still include the full complement of teachers, administrative and maintenance staff. It was suggested that unless these primary schools, which are catering for a handful of students, are closed down, with the children being transferred to other schools, the costs in the education sector cannot go down substantially. This finding was subsequently substantiated by the results of a performance audit carried out by the NAO (National Audit Office, 2015) which suggested that the resources being consumed by schools with a small student population could be dedicated to other pressing needs within education.

Another related issue which was mentioned during the interviews was the inferior academic results being achieved by Maltese students in comparison with students from other EU countries, notwithstanding the high spending on education and the low ratio of teachers and Learning Support Assistants to students. It was stated that this ratio is considerably lower than that of other EU countries, which possibly suggests a waste of resources.

These issues could be partly addressed by the implementation of PB, which emphasises the results obtained rather than the money spent, as suggested by Carter (1994). Through the development of performance measures which link expenditure to deliverables, the input-output relationship being achieved becomes clearer, such that allocation decisions would better reflect the results being targeted. The performance measures could also be benchmarked against international key performance indicators. If the input-output relationship



is made clear, then it might be difficult for government to ignore the inefficiencies that the interviewees have referred to.

As regards the health sector, expenditure is constantly increasing, in view of the country's ageing population. The main concern of a number of respondents, in respect of this sector, is whether free healthcare is sustainable in the long run. Whilst some interviewees argued that the existing free healthcare system can be maintained, others were of the opinion that providing free healthcare for all is unsustainable. Furthermore, the latter group argued that whilst the purpose of free healthcare is to provide accessibility to all, in reality, given the limited resources and the huge demands on healthcare, healthcare is only accessible to people who have contacts and/or money. In effect, the existing 'free' system is giving rise to long waiting lists, overcrowding and bed shortage. In this respect, there are doubts as to whether any government would take the plunge and make the provision of healthcare against payment, because this could potentially result in a political fall-out for the party in government.

If the possibility of changing government's policy vis-à-vis the provision of free healthcare is remote, PB would at least provide a measure of performance in relation to the expenditure being dedicated to the various areas within the health sector. This could result in identifying areas where cost savings are possible and focusing public funds on other areas which require further investment.

The findings have demonstrated that there are political considerations which are impeding government (and which have hindered past administrations) from addressing the structural problems in a number of policy areas, including education, health and the social welfare system (comprising pensions). In this context, PB assumes greater importance; firstly, because inefficiencies in the delivery of certain services might be uncovered resulting in cost

savings, and secondly, to measure performance in the high spending sectors (education, health and social welfare, amongst others) such that underperformance would become evident and would possibly be addressed.

### **7.11 Malta's small size factor**

This section seeks to ascertain whether the concept of a small nation impinges on the budgetary reform. During the empirical data collection process, reference was made by a number of interviewees to the size factor of Malta (being the smallest EU country), as discussed below.

The findings revealed that there is lack of adequately qualified public officials in government employment, which might hinder the implementation of PB. In this regard, the Minister for Education opined that the provision of training to civil servants has not been adequate in certain areas such as management, leadership, finance and administration. These skill deficiencies impede public officials who move up the ranks within the civil service. Civil servants who reach managerial positions have had to deliver results, notwithstanding the lack of training and professional development. The Minister attributes these constraints to Malta's small size, adding that it is common that "*people have to wear different hats*" in small countries. Specialisation is indeed difficult in a small country where people have to be fairly competent in various fields rather than excelling in one particular area.

It was found that there is an element of political sensitivity and risk, should actual PI be made public. A former Prime Minister argued that though from a technical point of view, PB is undoubtedly the best budgeting system, from a political perspective, it is very risky to publish the actual outputs/outcomes achieved because of instances where performance falls short of

the pre-established targets. It was suggested that in order to address this problem, government could consider keeping parts of the performance reports internal. However, the former Prime Minister cautioned that it is difficult to withhold information in a small island like Malta, where everyone knows everybody else.

Reference was made by a number of respondents to the lack of economies of scale and the inefficient use of resources in the education sector, which is driving up government expenditure. It was mentioned that there are a number of government schools with a small number of students; yet such schools include the full complement of teachers and administrative staff. Lack of economies of scale and the resulting inefficiencies are an inherent issue of small countries, according to an interviewee.

On a positive note, the findings show that the country's small size factor is contributing positively to the collaboration between the Budget Office and the EPD during the process of the fiscal projections compilation. An EPD official claimed that this strong liaison is possible in view of Malta's small size, where holding physical meetings between the two departments is very easy.

As indicated above, the small size concept could potentially impinge on the budgetary reform. The lack of adequately qualified personnel, which is partly attributable to the difficulty of specialising in one area in a small country, has to be addressed by creating the necessary competences and capacities for the implementation of PB<sup>79</sup>. Keeping PI internal is difficult in a small country because of potential information leakages – thus, government should publish this information, also in view of its commitment to enhance transparency and accountability in the use of public funds. Regarding the lack of economies of scale in education (and

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<sup>79</sup> Vide section 7.5.2

potentially in various other sectors) arising from the country's small size, PB would make clear the input-output relationship, such that government would, as much as is possible (in the context of a small country), address the inefficiencies. The strong collaboration between government ministries and departments, which is feasible in view of their physical proximity, could facilitate the implementation of PB, since oversight by project leaders could be carried out more effectively through site visits.

## 7.12 Conclusion

This chapter has discussed the findings derived from the interviews carried out, seeking to satisfy the research objectives<sup>80</sup> underlying the study and linking back the findings to the theoretical framework selected and the literature reviewed.

In summary, the current line-item budgeting system has become deeply embedded in its institutional context. Nevertheless, institutional pressures and macro-level influences come into play which might trigger a budgetary reform. In addition, the findings have revealed a number of weaknesses in the current system, including its short term perspective, arbitrary budget allocations, lack of accountability for the results obtained, ineffective programmes which continue to be funded year after year and budget cuts effected across the board, amongst others. Furthermore, the inclusion of PI in budget documents is considered to be desirable, since it is believed to improve managerial and public accountability (Sinclair, 1995) and transparency and to enhance budget allocation decisions. Lu et al (2015) maintain that policy results, public service performance and budgeting are indivisible and thus, PB will remain important in public budgeting and governance. However, there are opposing forces which might inhibit the implementation of PB, including strong resistance to change,

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<sup>80</sup> Vide sections 1.6 and 6.1

personnel problems and high political influences. Such opposing pressures need to be effectively mitigated in order for the budgetary reform to happen. In this regard, it has been ascertained that political support from a powerful person/s at the top is fundamental for successfully adopting PB.

The type of organisational change expected in the Maltese context has been analysed through an examination of the internal dynamics surrounding the budgetary framework, drawing upon Greenwood and Hinings' (1996) model. A third enabler of radical change has been identified, being the political ability required to make the reform happen – this element is perhaps the most significant impediment to radical change in the Maltese budgeting system. In this regard, it has been determined that the reform has to be championed at the top, in order to ensure successful implementation.

In view of the current system's deep embeddedness in its institutional context and the major policy changes involved to transition to PB, it has been established that successful implementation of the reform in the Maltese context requires a combined implementation approach, with more emphasis on the bottom-up perspective. Nevertheless, central intervention remains important for ensuring that government's priorities are being achieved and that this is being done within the available funding.

On a final note, the interviewees have shown considerable support for the implementation of PB. It is to be noted that a number of participants who took part in the research are prominent people in the Maltese public financial management scenario, and thus, their opinions are highly valued and could potentially influence the budgetary reform decision.

**CHAPTER 8:  
CONCLUSION AND  
RECOMMENDATIONS**

## **8.1 Introduction**

This chapter summarises and concludes the study. In this respect, section 8.2 provides a brief summary of the research, whilst section 8.3 sets out the conclusions drawn. Next, section 8.4 lists the contributions of the research to the existing body of knowledge. This is followed by section 8.5, which presents a summary of the policy recommendations proposed. Section 8.6 considers the value of the methods used, whilst section 8.7 makes some personal reflections. Section 8.8 then concludes the chapter.

## **8.2 Summary**

The main aim of this study was to assess why and how the Maltese public administration might transition from the existing line-item budgeting system to a PB system. To this end, the research sought to identify both the pressures which support the implementation of PB in the Maltese scenario, as well as the opposing forces which inhibit such reform. The study also aimed to find out what recent reforms were implemented by the public administration, in the budgetary framework. It also endeavoured to ascertain the implications of including PI in budget documents and of holding public officials responsible for the performance of their department/programme. Furthermore, the study sought to propose a suitable implementation approach for adopting PB, highlighting the potential issues surrounding implementation.

To achieve these objectives, a qualitative approach was embraced, using data gathered from documentary sources, corroborated with empirical evidence collected from the conduct of twenty-eight in-depth, semi-structured interviews. Access was obtained to discuss relevant issues with senior politicians from the government and the opposition, including former ministers and Prime Ministers.

According to the respondents, the current line-item budgeting system exhibits a number of shortcomings. The existing system adopts a short-term perspective, focusing on changes in expenditure categories from one year to the next (Murray and Efendioglu, 2011). Also, an incremental approach is embraced, whereby ministries expect the same budget allocation of the previous year plus something extra to cover for inflation. As a result, elements of waste are neither identified nor eliminated, because they are inbuilt into the system. In view of the lack of performance measurement within the current system, ineffective programmes continue to be funded year after year, because there is no public accountability for the results attained. The findings also reveal that budgetary cuts by the MOF during the course of the year have become a normal occurrence – these are aimed at keeping the fiscal deficit under control. Unfortunately, these budget cuts might disrupt the plans of the ministry/department affected (Van Reeth, 2002), in particular if diligence was practised during the year in order to save funds for future use. In this regard, the implementation of PB would potentially help to target budgetary cuts at programmes which contain an element of waste or which are ineffective. The empirical data shows that when ministries underspend their budget, the excess funds are returned to the central agency and the following year's budget for the said ministry is reduced accordingly. This practice has been strongly criticised by the interviewees, on the basis that it discourages cost saving and revenue generating initiatives by the ministries.

The findings demonstrate that the current line-item budgeting system has become deeply embedded in government's existing practices. Indeed, institutional thinking suggests that the current system is an 'institution' (Douglas, 1986). Nevertheless, there are both institutional pressures and macro-level forces which might trigger a budgetary reform. The three areas of institutional isomorphic pressures, namely, coercive, mimetic and normative influences (DiMaggio and Powell, 1983), manifest themselves in the proposed budgetary reform. In



particular, coercive pressures for change appear to be strong and comprise the EU's and the credit rating agencies' influence on Malta for reforming a number of sectors in order to reduce the fiscal deficit and the debt burden, together with the advice given by the IMF to Malta as regards improving its budgetary process. Furthermore, macro-level forces, including economic, political and socio-cultural influences (Munir et al, 2011), have been found to be significant factors which might drive the implementation of PB in Malta. In this regard, the participants have claimed that the current budgetary system should be radically changed, because it is not serving the purpose of effective economic decision-making. Political considerations are also highly relevant, since the existing high involvement of civil servants in budget allocation decisions might not be leading to the best results from a strategic, whole of government perspective.

The empirical data also reveals that there are opposing pressures which might inhibit the implementation of PB. According to the respondents, changing the existing budgeting system will come up against high resistance (Burns and Scapens, 2000) from public officials and possibly also from politicians, for a number of reasons, including the fact that the stricter control on government spending offered by a PB system might not be viewed positively. Furthermore, a PB system will provide information on the performance of departments and programmes, necessarily highlighting weaknesses and underperformance, which would have to be justified. Resistance is also envisaged in view of the fact that the reform would be going against a deeply established culture, where the civil servants and the politicians are not used to performance measurement. In addition to resistance to change, the findings also show that the lack of adequately qualified public officials in government employment might act as a stumbling block for the implementation of budgetary reform. Furthermore, the implementation of PB could be seriously hindered by high political influences and

interference, which at times might result in making popular rather than economically-viable decisions. It was determined that the successful implementation of PB depends on effectively mitigating the pressures inhibiting change. An important element identified for successfully reforming the budgetary system was the need for strong political support from a powerful person/s at the top (Willoughby, 2011), who has/have the power to overcome the obstacles hindering change.

In the last couple of years (since the change in government in March 2013), a number of reforms have been effected in the budgetary framework. These include the launch of a Comprehensive Spending Review exercise to review expenditure on budget line items; the initiative to start preparing three-year revenue and expenditure projections covering the government ministries; the appointment of a Minister responsible for the implementation of the electoral manifesto who ensures that the yearly budget is linked to the pledges contained in the manifesto; the publication of a document entitled ‘The Implementation of the Budget’, which sets out the implementation status of the budgetary measures that had been included in the previous year’s budget; the establishment of specific indicators against which the Permanent Secretaries responsible for each ministry are appraised, for the purpose of awarding performance bonuses; and the enactment of the Fiscal Responsibility Act, aimed at ensuring sustainable public finances and enhancing accountability and transparency in government’s financial activities. It was established that these reforms were driven by a combination of coercive, mimetic and normative isomorphic forces together with economic, political and socio-cultural pressures. Some of these changes could be a catalyst for a change in culture amongst the civil service and could thus be important precursors which will help promote the introduction of PB.

The study ascertains that the inclusion of PI in budget documents is desirable, since it is believed that it will enhance managerial and public accountability (Sinclair, 1995) and transparency and it will enrich and guide the budget allocation process. The findings also show that public officials should be held responsible for the actual performance of their department, on the basis of the PI compiled. This requires the establishment of reward/sanction mechanisms (OECD, 2007; Hou et al, 2011) which should ideally be set at an entity level, rather than at a personal level, in order to avoid dubious behaviour by individuals.

As regards the implementation approach for PB, a combined approach, with more emphasis on the bottom-up perspective, was recommended. A PB system allows for better control by the central agency in view of the fact that PI has to be prepared and presented by the line ministries; thus, shifting from the current top-down approach to a more bottom-up perspective appears to be feasible. Central intervention is, however, still important in order to ensure that government's priorities are being addressed and that this is being done within the pool of funds available.

### **8.3 Conclusion**

The study concludes that PB could be a way forward for addressing the issues and weaknesses surrounding the existing budgeting system. Indeed, the majority of the interview respondents have shown considerable support for the implementation of PB within the Maltese public administration.

A number of reasons have been identified for rationalising the introduction of PB. Amongst others, increased transparency, enhanced accountability and better allocative decision-making (Shah and Shen, 2007) have been highlighted by the interviewees as clear objectives for

implementing a PB system. In addition, it is believed that performance measurement assumes greater importance where a country faces fiscal deficit and high debt issues, as is the case in Malta. The fact that the business plans currently compiled by the line ministries do not incorporate any output indicators to support their requests for funding shows that value for money concepts and efficiency measurement are not being adequately emphasised during the budget preparation process. In this regard, a PB system will serve to shift the focus of budgeting from inputs to expected outputs and outcomes. Also, the element of arbitrary budget allocations would potentially be reduced since decision-making would be better informed through the availability of PI. Furthermore, PB could serve as a tool for identifying ineffective programmes such that any budget cuts required during the course of the year, could be better targeted. Moreover, the EU Commission is also pressing the Maltese public administration to embark on this budgetary reform, according to the respondents.

Notwithstanding the various reasons supporting the introduction of PB, there are a number of challenges which have to be tackled should this reform be launched. Amongst others, these include the envisaged strong resistance to change (Burns and Scapens, 2000) from the civil service and politicians alike; the required change in culture and in people's mind-set in order to embrace a performance measurement philosophy; the need to deploy suitably qualified personnel within ministries and departments in order to successfully implement and operate a PB system; the financial and time resources required for introducing a reform; and the political dimension that needs to be addressed since certain decisions that might be triggered as a result of the reform might be politically unpopular. Clearly, these challenges can only be overcome if the reform is championed by a person/s who is/are in a high position of power.

In view of the challenges involved, it might make sense to introduce the reform gradually, by starting off with presentational PB (where PI is included in budget documents as background

information, without playing a role in decision-making) – this could serve to start changing the culture and mind-set within the civil service. Eventually, moving towards a performance-informed budgeting system (where the compiled PI would be used for budget decision-making) would be a natural transition, since, at the end of the day, investing in the reform would only be beneficial if decision-making is influenced and improved accordingly. In accordance with Greenwood and Hinings, 1996, this course of action suggests an evolutionary rather than a revolutionary change, starting off with presentational PB (which does not constitute a radical change), but then moving on to a performance-informed budgeting system and perhaps direct PB in selected cases (both of which represent a radical change from the existing system). This takes into account the need for gradual introduction of PB in view of the challenges that have to be addressed to ensure successful implementation.

#### **8.4 Theoretical contributions**

This section sets out the contributions made by the study to the existing body of knowledge.

Firstly, the research may lead to a refinement of the Greenwood and Hinings' (1996) model, which was utilised for analysing the type of change expected in the Maltese context. The model comprises internal or intraorganisational elements, which are classified into precipitating dynamics and enabling dynamics. The current model lists *stakeholders' dissatisfaction* and *value commitments* as precipitating dynamics, and *power dependencies* and *capacity for action* as enabling dynamics. Within the Maltese scenario, a third enabler of radical change has been identified, being the *political ability* required to make the reform happen. Indeed, it has been determined that the potential lack of political ability to embark on the reform is perhaps the most significant impediment to radical change in the Maltese context. It is suggested that the Greenwood and Hinings' (1996) model might require an

adjustment to incorporate the political dimension. Political ability, supported by a competitive or reformative pattern of value commitments and backed by top people in positions of power, could lead to radical change.

A further contribution is made to the policy implementation theory, in particular to Matland's (1995) ambiguity/conflict model, which seeks to explain when it is appropriate to apply either the top-down or the bottom-up approach for policy implementation. The findings contradict Matland's (1995) assertion that a political implementation process reflects more closely the orientations of a top-down perspective. It has been established that the implementation of PB in Malta mainly reflects a political implementation; however, the suggested implementation approach is a mix of both the top-down and bottom-up approaches, with more emphasis on the bottom-up approach. Though no attempt is being made to make a new contribution to the typologies proposed by Matland (1995), the research shows that the implementation of budgetary reform in the Maltese scenario cannot be analysed through a neat policy type. A further lesson learnt is that it might be difficult to transfer policy learning across international boundaries, since such policies might undergo a transformation in a new institutional context. This implies that externally imposed policy recommendations might be problematic. Thus, where international bodies, such as the EU, impose blanket policy rules on countries they need to be aware of context and of the wide differences between countries.

Furthermore, this study has integrated institutional theory, change theory and policy implementation theory, seeking to address gaps identified in the individual theoretical frameworks. Institutional theory has facilitated the understanding of the institutional context within which a budgetary reform in Malta would be implemented. It has also contributed towards the identification of institutional isomorphic pressures (DiMaggio and Powell, 1983) and macro-level influences (Munir et al, 2011) which might trigger such a reform. Change

theory (Greenwood and Hinings, 1996) has been useful for determining the type of organisational change expected in the budgetary framework (radical versus convergent). This theory has also shed light on the envisaged pace of change (evolutionary versus revolutionary) and on the enabling dynamics required for a radical change to happen (institutional capacities, power dependencies and political ability). However, institutional and change theories were inadequate for indicating the most appropriate implementation approach for PB introduction in Malta. This shortcoming was addressed by complementing institutional and change theories with policy implementation theory, in particular Matland's (1995) model. The integration of the three theories has helped to address some limitations identified in Matland's (1995) model by linking to institutional and change theories. In this respect, it is being suggested that Matland's (1995) existing implementation model, which is based on a policy's ambiguity and conflict level, be augmented to embrace other variables that affect the implementation approach, as revealed by the theoretical review and the empirical evidence. Such variables comprise the institutional context within which the new policy is being implemented including the level of embeddedness of an existing system, the envisaged resistance to change, the pattern of value commitments and whether a revolutionary versus an evolutionary change is expected. Where an existing system is deeply embedded in its institutional context, such that a new policy would be expected to come up against resistance to change, then a combined (tending towards the bottom-up) approach would be more appropriate to ensure the support of street-level implements (Lipsky, 1980), thus reducing change resistance. Similarly, a competitive pattern of value commitment, whereby some groups are resisting the budgetary reform, is more supportive of a combined approach, in order to obtain the trust and build up the confidence of the groups resisting the changes. Where resistance to change is expected, the indicated type of change is evolutionary

(Greenwood and Hinings, 1996), in order to ensure acceptance of the new system before embracing more challenging reforms – this suggests that PB implementation should kick off with presentational PB and then move on to performance-informed budgeting, as was also recommended by the interview respondents. The study indicates that an evolutionary change and a combined (emphasising the bottom-up) approach are complementary, since a slower pace of change is more conducive to a higher involvement of street-level implementers in policy implementation, in view of the fact that more time is available for street-level implementers to come up with their ideas and subsequently engage in discussion with the central agency before the policy is implemented. Conversely, a revolutionary change, which occurs quickly, is facilitated by the top-down approach where clear direction for policy implementation has to come from the central agency to ensure successful and quick implementation.

The research also made a contribution by studying the potential for the implementation of PB within the public sector of a small EU country. This was done by gaining access and interviewing senior politicians and senior administrative players in the country. Amongst others, interviewees in prominent positions included the Prime Minister, Ministers, former Prime Ministers and Ministers, and Permanent Secretaries.

## **8.5 Policy recommendations**

The study makes a number of recommendations as summarised below.

- A. With respect to the recent reforms effected to the budgetary framework, it is suggested that such reforms be taken forward and improved upon. (Section 7.2.3)**



The Comprehensive Spending Review (CSR) process that has been launched in 2014 should be repeated and its scope should be widened to cover other spending areas. The results of the CSR exercise should then be incorporated in the budget process. The importance of this exercise is mainly twofold: to address the issue of waste in government spending such that the fiscal deficit is contained and to kick off a process of changing the culture within the civil service such that the link between inputs and outputs/outcomes will be emphasised. Furthermore, the CSR exercise could serve as a useful intermediary for moving on to a PB system, since ministries have already gained some familiarity in determining what outputs were delivered in respect of selected budget line items.

The initiative of compiling forward estimates covering two years beyond the budget year is a healthy practice which aids medium-term planning. Presently, the revenue and expenditure projections for the two years following the budget year are being prepared by the MOF, rather than by the respective line ministries. It is suggested that the line ministries should assume responsibility for the preparation of forward estimates covering their expected operations, in order to ensure ownership and commitment for adhering to such financial plans.

The Fiscal Responsibility Act has sought to strengthen the powers of the MOF, through the establishment of spending ceilings and through ensuring that the ceilings are consistent with the fiscal rules laid in the law. This law has placed the budget process under greater scrutiny and has laid down more onerous reporting requirements, which are covered by endorsements by the Fiscal Council. If this law is to serve its purposes, enforcement is fundamental; otherwise, the reform would have been carried out ‘on paper’ only, possibly to satisfy EU obligations.

The publication of the 'Implementation of the Budget' document is an important tool of managerial and public accountability and transparency which sheds light on the performance of the ministries vis-à-vis the previous year's budgetary measures. The information contained in this document is of a descriptive and narrative nature, indicating the implementation status of the budgetary measure. It is suggested that the present information would be complemented by output and outcome information (results achieved through the budgetary measure). This will start to pave the way for the incorporation of PI in budget documents. Furthermore, where a budgetary measure of the previous year is still in the process of being implemented a year later, it has to be reported upon in the following year/s.

The system of evaluating the performance of Permanent Secretaries and remunerating them on the basis of their attainments is a mechanism which motivates these people to work hard in order to deliver results. It is important that the criteria against which these civil servants are assessed are fair, challenging yet achievable and within their control. The findings indicate that this performance appraisal system will be cascaded down to other public officials. In this respect, it is suggested that the person or unit which carries out the appraisals should be independent, in order to ensure objectivity and to avoid familiarity threats.

**B. Budget cuts necessarily required during the course of the year should be targeted at ineffective programmes and at activities which contain an element of waste, rather than being carried out across the board. (Section 7.3.1)**

Though the MOF is endeavouring to target budgetary cuts at line items which are believed to include an element of surplus allocated funds, the research indicates that this assessment is not perhaps as effective as it should be, since budget cuts during the course of the year are upsetting the plans of some ministries/departments. The implementation of a PB system,

providing information on the outputs and outcomes expected from the budget allocations, would potentially assist the MOF in carrying out a better assessment, which would result in reducing waste and at the same time, avoiding cutting funds allocated to sensitive programmes which might already be operating under tight funding conditions (Van Reeth, 2002).

**C. A significant percentage of a ministry's unspent funds at the end of the year should be made available to that ministry for the following year, to be used on projects which are approved by the MOF. (Section 7.3.2)**

Allowing ministries to carry forward a portion of saved funds to the next year (which portion has to be significant – in the region of say 40-60%) would potentially encourage cost saving and revenue generating initiatives by ministries/departments. This would, in turn, benefit ministries who can then undertake further projects/activities and at the same time, it would avoid 'shopping sprees' by line ministries towards the end of the year, which spending could potentially be applied on items that do not represent a priority. Furthermore, cost savings and increased revenue would lead to deficit reduction (Murray and Efendioglu, 2011), which is one of government's top concerns. It is also proposed that where 'shopping sprees' are identified, the person/s who would have authorised the expenditure should be penalised, either by negatively affecting the performance bonus awarded or by negatively impacting career progression.

**D. PI should be included in budget documents in order to enhance accountability and transparency and to enrich the decision-making process covering the allocation of funds. (Section 7.4.1)**

The compilation of PI will contribute to effective decision-making, even if the required decision might be difficult and politically sensitive. In this regard, if the outputs and outcomes of a programme do not justify the resources being allocated, corrective action would be inevitable. A case in point relates to the education sector, where it has been revealed that it is difficult to reconcile the increased spending on a yearly basis to the number of students being educated, since the latter is on the decline. PI would certainly highlight these issues, making action unavoidable.

**E. PI should be used to hold public officials responsible for the actual performance of their department/programmes (Young, 2003). Reward/sanction mechanisms should be established in order to be able to hold public officials accountable for their performance (OECD, 2007; Hou et al, 2011). (Sections 7.4.1 and 7.4.2)**

Where the actual performance is short of the pre-established targets, justification should be sought for such underperformance, in order to determine whether there were any factors affecting performance that were beyond the control of public officials, and also, to implement corrective action. The pre-determined performance targets should be achievable and realistic, yet challenging.

It is suggested that reward/sanction mechanisms would be set at an entity level, rather than at a personal level, in order to avoid data manipulation, lack of social responsibility, greedy behaviour and possibly focusing on short term results at the expense of longer term gains. Reward mechanisms at an entity level could comprise adjusting a ministry/department's budget upwards in the following year or allowing such ministry/department to carry forward a portion of its savings to the next year.

**F. Addressing the resistance to change (Burns and Scapens, 2000) that is bound to arise should PB be introduced, is fundamental for the success of the reform. (Section 7.5.1)**

A number of suggestions are being put forward in this respect including the following: (i) external consultants, who have experience in PB implementation in other countries, should be roped in to advise on the reform process; (ii) the civil service should be involved and consulted during the system development stage; (iii) the necessary resources, including financial, time and human resources, should be deployed in order to ensure successful implementation; (iv) the system should be designed in such a way that underperformance is highlighted earlier on in the year, in order to allow for corrective action; (v) where circumstances change during the year which are beyond the control of public officials, there should be the possibility of revising the performance targets; (vi) performance targets should be realistic and the system for measuring public officials' performance should be just and fair; and (vii) the reform has to be backed up by a person/s who is/are in a high position of power, presumably the Prime Minister, the Minister for Finance and/or the Permanent Secretary within the MOF.

**G. Suitably qualified people have to be employed to beef up the finance function within the ministries in order to have the appropriate human resources for embarking upon a budgetary reform. (Section 7.5.2)**

Though this proposal might be quite challenging in view of the obstacles faced by the public sector when seeking to recruit professional people, such challenges could be overcome if government is truly committed to implement PB. People with the right competences could be employed by finding creative ways for offering a more generous package than that paid to

professionals employed directly by government (as has been done in the health sector), thus avoiding distortion in government salaries. Furthermore, in order to ensure continuous professional development by public officials, it is suggested that a minimum number of hours of training (say, 20 to 30 hours per annum) would be made mandatory for civil servants in certain grades, especially for those who hold managerial posts. The fulfilment of the minimum mandatory training requirement by public officials could be linked to the award of their performance bonus and also to their career progression prospects.

**H. The successful implementation of PB will be possible if the people in positions of power support the proposed reform (Willoughby, 2011). (Section 7.6.3)**

Political support will push the reform to happen and will ensure that it is carried out faster from a timing perspective. In this regard, the support and championing of the reform by the Prime Minister is fundamental for the change to happen.

**I. A culture change is required throughout the civil service and amongst the politicians, in order to address the political factors that might hinder the implementation of PB. (Section 7.6.5)**

Political issues include, amongst others, political interference, the problem of budget plans being overridden by political decisions and the issue of political sensitivity when actual results falling short of targets are made public. The culture change required for tackling such issues entails extensive education and training. In order to start introducing this culture change, support from the people at the top of the new way of doing things, is fundamental. This includes dedicating the required resources to the reform and embracing accountability and transparency even where the PI published highlights weaknesses and under performance.

**J. The existing top-down approach should be changed to a combined approach, with a more bottom-up perspective, reflecting the need for more involvement of the line ministries in the preparation of the budget figures. (Section 7.7.1)**

With the introduction of a PB system, performance targets covering ministries' programmes and activities are developed as part of the budget process. An increased level of involvement in the development of performance measures and targets by line ministries becomes highly important, for ensuring that ownership and responsibility for the achievement of such targets is assumed by the ministries. Moreover, this enhanced participation of line ministries could serve to facilitate acceptance of the proposed budgetary system change; thus, reducing resistance to the budgetary reform. A more bottom-up approach is advisable such that the ideas for programmes and initiatives would emanate from the people on the ground, who are more in contact with the needs of the public. Central intervention is, however, fundamental in order to ensure that government's priorities and the resulting policies originate from the OPM; policy control is in the hands of people who have been elected democratically; and government's priorities can be executed within the established spending ceiling.

**K. The top-down and bottom-up approaches should be brought together as follows in the implementation of PB: (Section 7.7.1)**

From a top-down perspective, government's strategies and the resulting policies should originate from the OPM, in order to ensure that government's objectives for the country are being addressed. Subsequently, the budgetary framework setting out government's priorities and policies, should be approved by a Cabinet decision. The Cabinet decision would then be communicated to the MOF and to the line ministries, such that the financial plans that would be developed would reflect government's priorities. The responsibility for developing

performance measures and targets would then lie with the line ministries, reflecting a bottom-up perspective. Subsequently, the MOF would be responsible for reviewing the financial plans together with the performance measures that would have been developed by the line ministries. The final budget allocation for the line ministries has to be determined by the MOF, who is responsible for overseeing the whole budget process. However, in contrast to what is presently being done, the budget allocation proposed by the MOF should be discussed with the line ministries before it is finalised, to ensure that any concerns that line ministries have vis-à-vis the planned activities and the corresponding funding are being addressed. This would potentially reduce the existing problem of ministries regularly approaching the MOF during the year, to request additional funds. Furthermore, a higher level of involvement of the Finance Minister is desirable in the budget allocation process, in order not to leave final budget allocations in the hands of civil servants.

**L. The following suggestions are being made with respect to other implementation issues: (Section 7.7.2)**

- A unit should be selected for carrying out performance audit reports (OECD, 2007), covering the quality and coverage of PI. This would ensure that performance reports compiled by the line ministries adhere to principles of good practice.
- It might make sense to start off with presentational PB and then move on to performance-informed budgeting. Though the former PB category may not constitute a radical change because PI is included in budget documents as background information for accountability purposes, the latter type of PB represents a radical change since it affects allocative decision-making (Greenwood and Hinings, 1996; OECD, 2007). This gradual introduction of PB, representing an evolutionary change (Greenwood and Hinings, 1996) would facilitate the culture change required in the civil service.



- It might be advisable to introduce the reform through legislation. Though this will not guarantee successful implementation, the potential consequences of breaking a law might secure the ministries' and departments' cooperation in introducing the new system.
- A time period of, say, three to five years is advisable for the implementation of a PB system. Whilst the introduction of the reform requires significant time effort, a time frame which is longer than five years would negatively affect the momentum of the reform.

## **8.6 Value of the methods used**

This study is valuable as it accessed elite decision makers. This was possible because of the small scale of the country and the culture of closeness to voters that exists. As a result, the researcher has been able to study processes and policy making in a way that would be difficult to do in larger countries. This means that small country studies have the possibility to make contributions to theory and understanding in a way that larger country studies cannot. In this regard, one of the researcher's future plans is to test the generalisability of the conclusions emanating from this study to see if what happens in a small country is replicated (in a more complex manner perhaps) in larger countries.

## **8.7 Personal reflections**

On a personal note, this research process has been extremely fulfilling and has served as a remarkable learning experience. This is not to say that there were no challenges along the way, but overcoming these challenges was part of the learning and self-confidence building process.

At commencement stage, the researcher had planned to undertake the research on a part-time basis, but during the course of the study, the researcher became so deeply engrossed in the work that more and more time was dedicated to the research, becoming an almost full-time endeavour. This commitment to the study was partly the result of personal sacrifice and willpower, complemented with strong backing from the family. Trying to juggle the studies, the teaching and supervision work at the University of Malta, the directorship at the Malta Financial Services Authority and caring for two young kids is certainly no easy feat! This would not have been possible without the support and continuous encouragement of my extended family – my parents who baby-sat my kids on various occasions, who ran a number of errands for me and who pushed me to go on when it got tough; my mother-in-law who was always willing to baby-sit when needed and who provided us with hot meals on a daily basis; and, last but not least, my husband and mentor who was at my side throughout this journey, shared the kids' responsibilities and house chores with me and was my sounding board when I needed to brainstorm ideas or discuss my work. The strong support received from the University of Malta throughout the period of study, in the form of a reduced teaching and administrative load, was also extremely important for focusing on the study.

One of the most difficult challenges of the study was making contact and getting access to elite interviewees, including the Prime Minister, Ministers, former Prime Ministers and Ministers, Permanent Secretaries and other people in prominent positions in Malta. Persistence and perseverance were extremely important for succeeding – in the case of some respondents, the researcher spent weeks and even months calling the secretary of the potential interviewee on a regular basis, to follow up on the original email sent and secure an appointment for an interview. It was also fundamental to accept without hesitation the date and time proposed by the interviewees for holding the interview – this required total

flexibility and commitment from the researcher during the period when the interviews were being conducted. Support was provided by the Head of the Accountancy Department at the University of Malta and by the Deputy Auditor General at the National Audit Office, who contacted two participants each, on the researcher's behalf. In my view, getting access to the elite interviewees referred to above has been possible because Maltese politicians seek to keep direct contact with the people and may thus be more accessible.

This research is only the beginning of my contribution to the academic world. It is hoped that the researcher will, in the future, contribute further to the wide academic knowledge and literature that already exists.

As mentioned earlier, a future study may test the generalisability of the conclusions emanating from this study to see if what happens in a small country is replicated in larger countries.

The timing of this study was such that it was not possible to comment on the effectiveness of the introduction of PB in Malta, since such reform has not yet been implemented. The analysis of the effectiveness or otherwise of PB implementation, once this reform is introduced, could be the subject of a future research project.

## **8.8 Concluding remark**

Clearly, the Maltese public administration is seeking to improve government efficiency and to exert stricter control on public spending. Indeed, the use of performance measurement in the budgetary process and in particular, the role of such information in resource allocation decisions, is opportune in the country's current economic, social and political context. The Maltese government largely relies on expenditure cuts to meet the fiscal deficit and debt

reduction targets. In this regard, PI would shed light on the efficiency and effectiveness of the programmes and policies undertaken by ministries and departments, which would, in turn, inform decisions of where to cut spending.

OECD (2011: 3) maintain that:

*“Not to be overlooked...is...the role of performance information in promoting greater government accountability through the budget process, and increasing the legitimacy of budgetary decisions...Performance information plays a role in informing the policy debate surrounding the budget, and providing managers and politicians with evidence with which to communicate their policy choices.”*

In her analysis on the 2011/2012 OECD Performance Budgeting Survey results, von Trapp (2014) concludes that:

*“Performance budgeting is here to stay.”*

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