



PAPER 04(07), APRIL 2007, YEREVAN, ARMENIA  
ECONOMIC DEVELOPMENT AND RESEARCH CENTER (EDRC)

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# Public Programs: why monitor them and how

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White Paper # 3

*The present publication was prepared in the framework of Support to PRSP Process project with the assistance of the UNDP and Oxfam GB.*

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Public Program: Why Monitor Them and How

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# The Essence of Public Demand and the Need for Budgetary Reforms

## What is Public Demand in a Free and Democratic Society?

In everyday life, people have various individual needs: need for food, for clothing, hairdressing and other services, as well as education, etc. At the same time, living among other people creates other needs, such as having educated, literate and healthy environment, safe and secure country, clean streets, etc. Thus, the needs can be divided into 2 groups (consequently, so can be the demand): (i) individual and (ii) public. For the first group, needs are satisfied within constraints of individual opportunities. To that end, commercial entities, lead by market forces; provide goods on certain terms and conditions. For the second group, a common demand is created which, in turn, triggers the need for the state to formulate public demand and to satisfy it. The society, after "creating" the state, authorizes it the functions to formulate the public demand, production and development of rules of usage thereof at its own (society's) expense and funds.

Types of state organisation vary depending on principles of public demand formulation and implementation. E. g., under monarchy, the decision-making was delegated to monarchs who relied on the needs and interests of a limited and non-representative stratum of the society. Thus, the decisions taken not always corresponded to the needs of the majority (i. e. those who funded those decisions). The democratic system implies that the society has more opportunities to express its views and receive all services that they need.

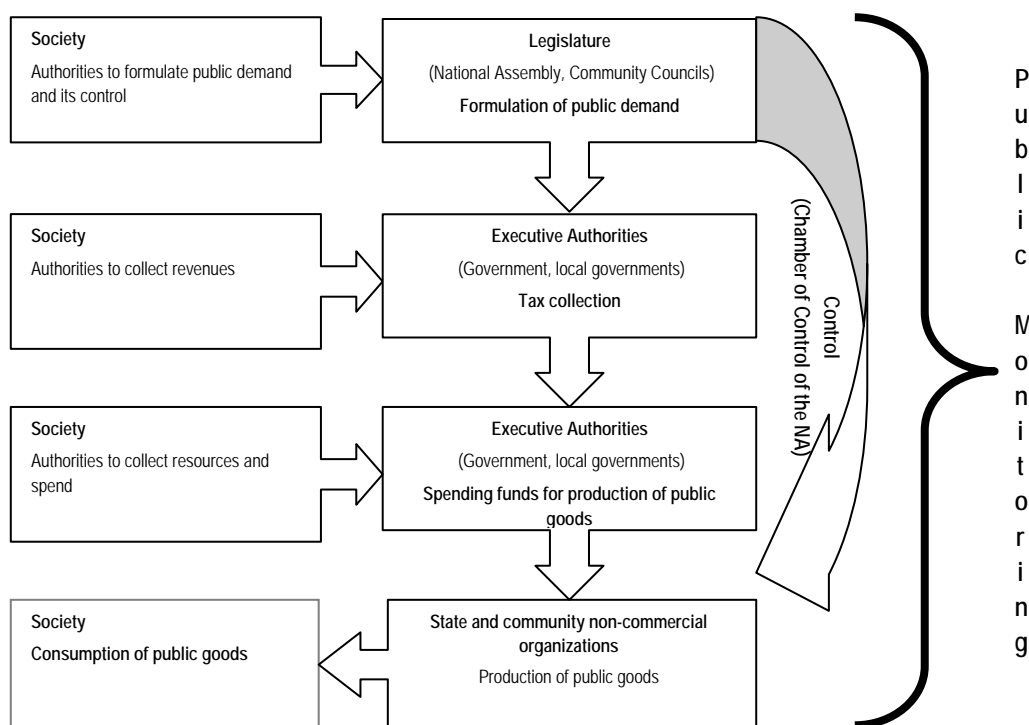
When having democratic principles as basis for the state, each member of the society participates in the governance of the country through electoral, political and other public mechanisms. In such societies, decisions are taken through elections: an institute which consists of representatives elected by individuals takes the public decisions. The public sector is a system which formulates and procures the public demand, which is conditioned by the clear definition of interrelations between the following three institutes: 1. **society**, 2. **legislature (representation bodies)** and 3. **public administration bodies**.

In our country (as well as in a number of other countries), the society created two major bodies that formulate the public demand – the National Assembly and the Community Councils – in order to protect the regional interests and moving towards the democratic values. The National Assembly is authorised for taking those interests that are common to the entire society, whereas, the local governments are authorized to take decisions regarding which the regional interests may be conflicting.

### Why do people pay taxes?

Formulation of public demand and its implementation implies transfer of certain authorities and resources. Members of the society, coming to a consensus on the common public demand, agree also on authorization of collecting financial and non-financial resources.

The transfer of authorities, in fact, is a contract, that is signed between the society and the state by voting for the constitution which establishes the institutes that formulate the demand for publicly-consumed services and satisfy it. The logic of interrelations of authority transfer, formulation of public demand and its consumption is depicted in the following diagram.



If the society realizes that the public institutes (National Assembly, Government, etc.) are established and authorized by the society itself and the taxes they pay are merely for the procurement of goods and services the society demands, the necessity to oversight public programs becomes evident. This will lead to a situation where the transparency, monitoring and impact evaluation requirements towards public programs and adjacent functions will increase. Only monitoring and transparency of public programs will allow taxpayers to understand how each unit of its taxes was spent and if he/she will be further willing to pay taxes to the government or not. Of course, payment of taxes is mandatory, since the tax legislation, on behalf of the entire society, represents the consensus of the society to pay and collect taxes. Nonetheless, if taxpayers do not receive the needed public goods or services, or receive them in poor quality, tend to evade taxes. Furthermore, under current state of international integration, many unsatisfied taxpayers opt for leaving the mother country for other countries; where they can pay taxes, in turn, receive public services of adequate quantities and qualities. Unfortunately, this option is very realistic and it is valid for many highly-qualified professionals, artists of our country.

## Need for Budget Reforms, Previous System and Current Requirements

Armenia inherited the old budgeting and accounting systems of the public sector from the Soviet Union. However, these systems, regardless if they were imperfect or comprehensive, would not satisfy the needs of the new Armenia that is moving towards free, democratic society and market economy.

Budget reforms started in 1991 and continue up to day. This time period can be conditionally divided into two periods. The first period lasted from 1991 to 2002 when the legal framework was developed and put in place with the adoption of laws: Laws on Budget System, Treasury System, and Public Procurement. The Budgetary classification was put into conformity with the IMF Government Financial Statistics (GFS) 1986 Manual, as a result of which we now have an internationally compatible budget classification.

By introducing 1986 classification and achieving a budget different from Soviet times, alas, the budgeting principles, in fact, remained the same – mostly input-based, whereas budget decisions are mostly taken based on norms.

Budget reforms process, moving towards the contemporary needs, entered into its second phase which started in 2003 when the Government of Armenia adopted the program of Second Generation Reforms of Public Sector Accounting and Treasury Systems. Under this program, the Government committed to introducing new budgeting system, GFS 2001

classification standards, reforming the public sector accounting which still based on old Soviet accounting principles. These created bases for moving towards output-based or performance-based budgeting (program budgeting) that allows seeing the link between financial and non-financial resources and outcomes.

Output-based budget is a system of public expenditure planning where the links between funds spent on program objectives and expected results can be easily seen. In other words, the budget shows what problems need to be solved in order to achieve the desired objective, what financial and human resources are needed, who are (and how many) direct and indirect beneficiaries, how much will be spent per each beneficiary, what indicators can help to evaluate the program and, eventually, what the results of the program will be.

Program Budgeting clearly differentiated between goals and objectives. Goals are long term targets, whereas objectives are clear, measurable and achievable in short-run that allow seeing what problems need to be solved to achieve the overall objective under available budget resources. For example, general education program aims at providing quality education to school-age children: this implies, as long as, there are school-age children and need for education, the program will be continuous. Within that program, the objectives is to educate the children of 6-18 years (which constitutes about 14 000 children each year). This will allow calculating the necessary budget funds. While at the end of the school year, we can see the number of schoolchildren graduated and passed to the next grade and evaluate to what extent the problem was solved.

#### **Why the Government should be interested?**

When developing program policies, the followings are put on the basis: economic policy principle, projections of fiscal position, as well as the pre-election program of the President, Government activities program, promises given by political forces, etc. Program policies are derived from all the above; furthermore, the sector policies and implementation documents are developed, along with the separation of sectoral responsibilities between political forces and determination of priorities. From this perspective, the expenditures on public services are evaluated by the economic policies, while in order to evaluate program policies one needs to know what services will be provided, for whom and at what cost. If the ruling force, i. e. the Government is eager to pursue its promises, it should be very interested to present the society the financial plan of how to achieve those promises in accordance with program budgeting principles per sectoral program policies. Eventually, this makes monitoring and oversight function of the Government easier. When the plans are presented in this manner, the society will be in a position to understand what was brought or done by each political party which will greatly help in making choices in the next elections. If a ruling political party is willing to retain the sympathy of the majority of voters, program budgeting can be a tool that can clearly show the work done, programs implemented and prove that promises are kept.

#### **Why the Society should be interested?**

Output-based budgeting automatically increases transparency, planning and reporting principles allow closely monitoring the processes and identify the consequences of each decision and adequately respond them. These are, in the first place, very important for the society who should be well aware of public decisions to be taken, what will be provided to people in the given budget year instead of merely knowing how much the government intends to spend in each sector and whether those allocations have been reduced or increased.

Along with all these, program budgeting increases the responsibility of the government, makes all alternatives easily measurable which, in turn, allows taking the right decisions under the given budgetary constraints. The government also has the chance to better explain and substantiate its programs based on expected outcomes in front of the National Assembly and the society. It is worth noting, that such explanation is a very important factor in the eyes of the society.

Until now, the draft annual budget was accompanied by the Budget Message which is, first, not accessible for the wide groups of the society and, second, is not comprehensible without professional interpretation. Therefore, the expenditure planning and approval processes, to a certain extent, remain obscure. Under program budgeting, one can easily open the Budget Law and see, e.g. that 450 disabled will be given wheelchairs in 2009 or 126000 households will receive benefits, etc.

In summary, one can state that program budgeting implies both top-down and bottom-up systems at the same time.

## Public Program Planning Systems

As it was noted, the society, legislative and public administration bodies bear the responsibility of formulating the public demand and its implementation. Due to that, those bodies also bear the responsibility for planning of public programs.

Draft plans for public programs (draft budgets) in local and central levels are prepared by public administration bodies (Government, local governments): subsequently, they are discussed and approved by the Parliament or Community Councils. Therefore, those are the bodies responsible for the formulation of public demand.

When we speak about purchases of an individual, he or she attempts to prepare a plan on income and spending on goods and services for one or more years. That is why, people follow price fluctuations, try to make projections, and asks the manufacturers to present a preliminary version of future products to be purchased, propose alternatives so that they can plan, choose and, eventually, order the goods and services.

The same takes place for public demand. Public administration bodies draft the preliminary plan of public services (draft Budget) on the basis of which those who represent the “purchasers” (National Assembly, Community Councils) formulate and approve the final plan.

However, in contrast to individual purchases, when an individual decides how to manage the entire process, the public purchases should be decided upon through an institutionalized system by applying the mechanisms that are agreed on by everyone.

For individual purchases, we would prefer to have long-term planning to the extent possible under our projections, however, this is mandatory for public purchases since without long-term planning and activity plans economic shocks will be inevitable, and the consequences thereof – difficult to manage.

Overall, the most acceptable option is the three-layer planning system; long-term, medium-term (which will allow comparing long-term plans and short-term, i.e. annual plans) and short-term plans which should be a more precise plan of measures.

Separation of those three sub-systems allows, first, to plan the more general indicators, and then use the more detailed indicators. In fact, these subsystems mainly differ in the degree of indicators' aggregation and moving from general indicators to precise activity plans: those subsystems imply that special links exist between them that need to be followed.

## Long-Term Planning Systems

Long-term planning sub-system usually provides the projections of overall revenues, expenditures and deficits of the public sector.

Prior to 2002, long-term planning in Armenia took place on the basis of Socio-Economic Development plans developed by the government. In 2002, new principles of long-term planning were introduced and new documents were developed. Strategic papers were developed for a number of areas, such as: Anti-Corruption Strategy, @003-2015 Strategy on Preserving Mothers' and Children Health, whereas the former Socio-Economic Development plans were replaced with the Poverty Reduction Strategy Paper (PRSP).

In contrast to sectoral strategies, that normally define the general principles and objectives of the government's policy in each area, the PRSP is more general and is further reflected in the financial documents of the country. The PRSP, in fact, is a paper that regulates the budget process. The PRSP is prepared over a 12-year horizon: since it is very complex and unrealistic to make detailed projections for 12 years, the PRSP indicators are quite generalized and are usually presented in the form of a range, and not a precise figure. Overall, the income level of the country is projected, as well as the fiscal position under that income assumption (budget deficit, total budget revenues and expenditures) and the level of intensity of sectoral intervention.

Taking into account that it was quite feasible that since the adoption of the PRSP economic and social developments could result in a change in the situation as well as shift in problems, thus reducing the urgency and validity of the PRSP,

it was anticipated to review the PRSP every 2 years' time based on the monitoring and evaluation results of the PRSP indicators and measures, as well as recommendations of all stakeholders<sup>1</sup>.

According to the PRSP review timeline, the first review was scheduled in 2005. However, the PRSP review time-schedule was not properly followed due to uncertain reasons and we still do not have a reviewed PRSP document.

Meanwhile, the inconsistencies between the Armenian legislation and PRSP document are not yet regulated or removed. In contrast to the medium and short-term planning papers, development, approval, implementation and reporting of which are regulated by the Law on Budgetary System, the PRSP is approved by a Government Decree as a normative legal document. Such legal documents are adopted on the basis of the Constitution and laws in order to ensure the implementation thereof. Furthermore, a normative legal document can regulate relations pertaining to a single-sector, whereas the PRSP is a multi-sector document and contains clauses that relate to a number of areas and sectors.

These inconsistencies can be removed by amending the current legislation of adopting a law which was previously done for the short- and medium-term planning systems.

## Medium-Term Planning Systems

The medium-term planning system, unlike the long-term planning system is applied since 2000 when the Medium-Term Expenditure Framework (MTEF) was first developed. It mainly was focused on projections of macroeconomic environment, medium-term fiscal decision-making, and definition of expenditures' priorities and facilitation of budgeting processes. The MTEF in Armenia is prepared for a 3-year period and allows setting fiscal policy targets based on macroeconomic projections which, in turn, allow drafting the annual budgets within limits acceptable for those targets.

In April 2003, the Law on Budgetary System was amended to include the MTEF process in the law: this made the 3-year MTEF planning mandatory for each year. It is worth noting that the MTEF process underwent serious improvements and developments to which the PRSP contributed as well. The PRSP served as basis for the development of MTEFs in subsequent years.

According to the Law on Budgetary System, the MTEF allows effectively managing the public finances in conformity with the fiscal objectives and policy priorities in the medium term.

Within the MTEF process, the Government of Armenia adopts the major decision on medium-term economic and program policies which are further used as guidelines for drafting the annual budget. The MTEF sets the ceilings for spendings of all government bodies and agencies for the next 3 years: the next year budget is drafted within those ceilings. The MTEF paper has successfully become the basis for the preparation of annual budgets during the last several years.

In these circumstances one should note that the medium-term planning has progressed significantly in Armenia, however, it is applied only at central government level. It is underdeveloped at local government level and it is very unclear whether they do have such medium-term planning tool. Perhaps, long-term planning is not yet urgent for communities, although it would create better chances for improved management and development. Meanwhile, the medium-term planning is an absolute pre-requisite for this level, too: it would allow the communities seeing the medium-term development perspectives, as well as assist in defining the targets and how to address the problems related to those targets. Currently, this to some degree is done through three-year Community development programs, although there is a wide-spread opinion that those programs, if they exist at all, are only formally adopted.

## Short-Term Planning Systems

When speaking about short-term or annual planning systems, one should bear in mind that any production process requires an annual financial plan. Some production processes may not need or may not have long or medium-term plans, but the annual planning is absolutely necessary. This is true about enterprises: any serious business has its long-term planning system – strategic plans, etc.

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<sup>1</sup> See Poverty Reduction Strategy Paper, Yerevan, 2003, page 171.

The same holds true for the production of public goods. One can state that the long and medium-term plans are intended to drafting more accurate, targeted and realistic annual plans.

Annual planning of public programs in Armenia is carried out through Annual Government Budget and Community Budget documents. The Budgets, as the decentralization approach of bodies responsible for formulation and implementation of public demand requires, are prepared in two levels: Government and communities. The Annual Budget of the Government is a law, whereas the Community Budget is a Decision of the Community Council.

The interrelations between bodies involved in the budgetary process are regulated by the Law on Budgetary System.

The Annual Budget, if discussed as a document reflecting the public demand and functions of the public sector, is the document where one can see, on an annual basis, what public services will be provided out of taxes we paid, who will benefit from them, what price will be paid, what are the required resources and, eventually, what the outcome will be.

Drafting of a Government Budget can be presented in brief as follows: Government bodies and agencies prepare their Budget submissions based on the economic and program policy guidelines of the Government and submit them to the Government (in this case, the Ministry of Finance and Economy acts as a coordinator). The Government takes its decision on budget programs based on the submitted Budget bids and analyses thereof.

The Ministry of Finance and Economy, on behalf of the Government, develops the draft Budget law, whereas the government bodies and agencies prepare justification and explanations for their programs. The budgeting phase is completed upon the submission of the draft Budget law to the National Assembly. The latter, acting on behalf of the society and as the body responsible for formulating the public demand, analyses, discusses, reviews and revises the draft budget prepared by government bodies. Thereafter, the Budget draft is adopted as a law, i.e. the public demand – based on the votes of the majority of MPs. Starting from this point the public administration bodies start the budget implementation as approved by the Parliament.

## Monitoring of Public Programs

**As our personal purchases, the public purchases also should be monitored**

If an individual decides to buy some goods, he or she first tries to make his choice: chooses the goods and their quality corresponding to his needs, collects information on prices, i.e. passes a certain process before actually buying. Furthermore, for large purchases or for goods that will be used by all family members, the purchase is usually first discussed with household members in order to have the views of all of them and make necessary adjustments. After the purchase, it is necessary to evaluate the quality, price and utility of the product in order to finally be sure that it was the right choice.

The same, of course, holds true for public purchases. If we think of public purchases as a collective purchase of a group of individuals, it will be absolutely necessary to follow the same steps, be aware of the purchase and be able to evaluate its efficiency.

In recent years, the term “Monitoring of Public Programs” becomes more and more widely used. It is a new concept for post-Soviet countries.

Monitoring means follow, watch; while in practice it means to act as an observer of a process and give opinions. The term “monitoring” can be used in various fields: political elections, when local and international observers monitor the election process, international organizations monitor inter-ethnic conflicts, implementation of strategic program of governments are monitored, etc.

The society, by giving its authorities to any body, should monitor the execution of those authorities, the activities of that body, as well as the use of financial resources by that body, etc.

Efficiency and targeting of public programs largely depends on the introduction of an effective monitoring system. The Government, when adopting strategic programs, should, in parallel, introduce monitoring systems. Program monitoring is complex and costly; however, the efficiency of programs without monitoring becomes questionable.

Monitoring is the simple tool that the society can use to be aware of the services provided to it, decision regarding those services, formulation of public demand and its implementation. Without monitoring, thus, in unaware society, regardless if the decision was good or bad, efficient or inefficient, the perception on the rendered services will always be negative. This may lead to a situation where the work done by legislative and executive bodies, their decisions and public programs are underestimated. One could state that the public programs' monitoring is necessary both for the society and governments in order to create an environment of mutual trust and consensus.

#### **How to monitor public programs? Is it currently feasible?**

As it was already discussed, efficiency of public program shall be, first of all, measurable. That should be allowed by the document which formulates the public demand, as well as the implementation report.

In this regard, the PRSP is not an exception: it is further reflected in medium-term and annual plans. The PRSP document, determined by its importance with regard to social and economic development of the country, is under the scrutiny of the society. That is explained by the fact that the annual budgets of the last 4 years take the PRSP targets as basis for directing the taxpayers' money to those strategic programs in the annual plans. Therefore, the monitoring system thereof is the strongest tool for the society to follow the implementation process of this crucial program.

The PRSP monitoring is one of the preconditions to PRSP evaluation, as well as should serve as information basis for PRSP reviews.

After the PRSP adoption, measures were taken to introduce the monitoring system: The concept paper on PRSP monitoring indicators was adopted by the Government of Armenia in November 2004.

Monitoring indicators were categorized into the following 6 groups:

1. Poverty reduction and increase in welfare,
2. Education,
3. Health care,
4. Basic utilities and housing problems,
5. Civil isolation and inequality,
6. Sustainable environmental development.

A separate set of indicators is defined for each group. Overall, the PRSP monitoring system consists of 177 indicators that are grouped into two groups: main or target (36 indicators) and explanatory or factor indicators (141 indicators).

The objective of differentiating the indicators was to give the information signals to those who make policies and implement them on "activities-results" basis. The main (target) indicators are those that describe the achievement of objectives (output indicators), while the factor indicators are intermediary indicators and describe the quantitative indicators (outputs) or the use of resources (inputs).

The description above was a direct citation from PRSP monitoring concept: the reason of citation was to use exactly the same terms which are program budgeting terms. It is clear from this that various groups of society can monitor only if the budget is presented in a similar classification.

It is worth noting that the monitoring concept paper clearly defines the requirements to monitoring indicators, which are:

1. should be clearly defined without leaving chances for double interpretation ,
2. direct description of a certain process at certain level of aggregation: achievement of targets, evaluation of results, etc.,
3. measurable (even in cases where a process is rather described by qualitative indicators),
4. achievable immediately or in near future.

We would like to pay attention to the requirement set in p. 4. If that requirement is not satisfied, the indicator cannot be monitored or can only be approximated.

Indicators in the monitoring indicators concept paper are clearly defined, as well as their source and the body that shall report it. When reviewing that document, one can clearly see that the sources of indicators' reporting are the government bodies, National statistical service and some international organizations. It is obvious that very few can obtain this information, while the collection process may become a titanic effort: there is no even a chance for public monitoring.

The only sources of data for public monitoring are, in fact, the budget indicators and statistical publications and studies<sup>2</sup> of the NSS.

Coming to the budget indicators, it is clear that without full introduction of program budgeting principles the necessary information cannot be extracted from the budget document. Although the budget reforms have progressed in 4 important social sectors (Social Security, Education, Healthcare and Culture) and the budget of respective ministries are drafted according to program budgeting principles on a pilot basis, the information is not complete.

The following picture can be revealed in the above listed areas if the structure of budget expenditures is analyzed in brief:

- Among AMD 91.8 bln expenditures in education for 2007, only AMD 16.7 bln is classified according to program budgeting principles, which is 18.2% of total expenditures in the sector. This is explained by the fact that the majority of expenditures (60%) in education sector are implemented through Provincial governments (including Yerevan). As long as the Provinces have not applied program budgeting, the picture will remain the same. Therefore, it is too early to speak about program budgeting in education sector.
- The situation is much promising in social security sector: 95.6% of all expenditures in this sector are implemented by the Ministry of Labor and Social Issues; therefore, they are largely presented according to program budgeting principles. In health sector, 97.3% of total expenditures are classified according program budgeting principles.

The listed sectors are the most important ones among focal sectors of the PRSP. Therefore, new classification of expenditures in these sectors was considered priority and the reforms were decided to start from here.

Nonetheless, it is not feasible to cover even half of PRSP monitoring indicators with the existing information sources. I.e., the PRSP monitoring today is extremely difficult (if not impossible) to implement if we only rely on budget indicators. Data on some indicator groups are partially or completely missing.

In summary, one can state that only 7 years remain until the end of PRSP implementation period, however, the monitoring system is not yet in place, thus making the efficiency of the program under a question mark.

Therefore, it is more urgent to introduce the monitoring system which can only be feasible under the collaboration of the Government, society and specialized structures. Only collaboration of those three parties the PRSP indicators can be monitored. Meanwhile, the Government should take more responsibility for the introduction of a monitoring system and should not allow putting the efficiency of its strategic program under question.

## Recommendations

In summary of the paper, one should come to the following conclusions and make the following recommendations:

- The PRSP is the focal document on long-term planning and development guideline for our country, therefore, it is necessary to regulate its elaboration, review and implementation processes through laws. Legal regulation will increase the responsibilities of both the Government and the Society towards the above described processes.
- The society should not be indifferent to how its funds are spent and should require and implement public programs' monitoring.
- The government should immediately undertake monitoring function and perform it in order to prove the efficiency and necessity of its programs. One should take into account that, if a program is difficult to monitor, its urgency and necessity becomes dubious.
- All public programs should have such monitoring systems that are realistic and feasible to implement in order not to leave them as mere declarations on paper.
- Currently, since the monitoring is difficult but not impossible, the society and the government and the international organizations should cooperate with specialized structures. Only persistent and efficient collaboration, under adequate political will, can make the situation more balanced.
- Monitoring results should be presented at least on an annual basis. The government, along with the Annual Budget Implementation Report, shall present the monitoring report as an annex to the draft submitted to the National Assembly: once it is adopted, it shall be published.
- Only monitoring results will allow the society to understand and evaluate the efficiency of public programs, be aware of where it directs public funds and will direct in future.
- Monitoring results, eventually, will allow assessing if the poverty reduction was the consequence of PRSP implementation or it took place due to factors independent of the PRSP.
- From the perspective of good governance and development of local governments, medium-term planning is absolutely mandatory. It is necessary to promote and develop capacities in drafting medium-term planning documents in communities, simultaneously, developing the monitoring capacities among the community members. Measure in those two directions should be taken in a harmonized and inter-related manner which will allow improving the quality of public programs in communities and better target them.