USAID'S LEADERSHIP IN PUBLIC FINANCIAL MANAGEMENT

Detailed Guidelines for Improved Tax Administration in Latin America and the Caribbean
Chapter 14. Budget Planning and Resource Management

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List of Acronyms and Abbreviations

Acronym	Definition
CIAT	Inter-American Center of Tax Administrations
IT	Information technology
LAC	Latin America and the Caribbean
MOF	Ministry of Finance
OECD	Organisation for Economic Co-operation and Development

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Chapter 14. Budget Planning and Resource Management

Government budgeting is simply a process of allocating limited financial resources to deliver services (roads, hospitals, education, law enforcement, etc.) that will effectively meet the needs of citizens. The tax administration plays a critical role in this process because its overall mission is to collect the revenue needed to fund these services.

In order to carry out its tasks effectively and efficiently, the tax administration requires adequate staffing, equipment, and working facilities. A lack of these resources often handicaps tax administrations. Shortfalls can often be traced to an inadequate budget planning process or a failure to present a strong business case for the resources needed. Tax administration management often settles for taking the prior year budget and increasing it by some percentage, without a full evaluation of what is needed to adequately deliver programs. However, a carefully prepared budget is critical to pursuing the necessary resources to execute program goals and objectives in an effective and efficient manner. A good budget hinges on sound projections that are based on realistic assumptions and a clear means of attaining deliverables.

This chapter will outline the overall budget planning process, budgeting methodologies, elements to be considered by a tax administration in developing a budget, and steps to take in effectively managing available resources in order to meet program objectives.

14.1. Leading Practice

The budget preparation process for the government generally starts nine to ten months before the budget is presented to the legislature. The responsibility for preparing the government's overall budget normally lies with the Ministry of Finance (MOF), with input from the line agencies. A typical budget preparation process may consist of variations of the following activities:

1. The government's financial team, which may consist of representatives from various agencies, including the Budget Office, the MOF, Planning and Economic Development, Legal Counsel, etc., commences a series of meetings to analyze past economic trends and monitor revenue flows in order to begin developing revenue projections for the upcoming fiscal year. Through this process, the financial team develops budget ceilings for each agency based on projected revenues.
2. The MOF issues a budget circular to each agency outlining the guidelines and timelines for the submission of budget requests. During this time, MOF staff conduct budget orientation sessions with line agencies to review the contents of the budget circular. As a general rule, the following elements are included in the budget circular:
    - A statement of the country's macroeconomic and financial situation;
    - The overall deficit target and expected resources;
    - Budget priorities;

   - Allocations for continuing policies and programs;
   - An indication of the expenditure savings expected in ongoing programs; and
   - The format for presentation of the line agencies' budget requests.
3. The agencies develop their proposed budgets in agreement with the established guidelines and submit them to the MOF.
4. MOF staff analyzes individual budget submissions and prepares recommendations and develops budget schedules and revenue statements. Agency heads are presented with the MOF recommendations / modifications for review and discussion. If changes are made as a result of the discussions undertaken, the agency's budget is revised accordingly.
5. The agencies' proposed budgets are then presented to the government's financial team for review, recommendation, and approval. After consultation with the President, the recommended budget is finalized and forwarded to the Legislature.
6. The Legislature reviews the budget, supporting bills, schedules, and summaries submitted by the President. The committee responsible for appropriations and budget conducts individual budget hearings for each agency. During the hearings, agency heads, their key financial personnel, and citizens are given the opportunity to testify. Throughout the process, the Legislature may add, change, or delete any item in the proposed budget.
7. Once passed by the Legislature, the President may approve the budget or veto it (partially or in its entirety) and return it to the Legislature with objections.
8. Once the budget is enacted, the President exercises fiscal control of expenditures through the MOF. If the fiscal resources available to the Government in any fiscal year are insufficient to satisfy the appropriations approved for such year, the President may take administrative measures through the MOF (such as reducing budget allotments) to align expenditures with available resources.

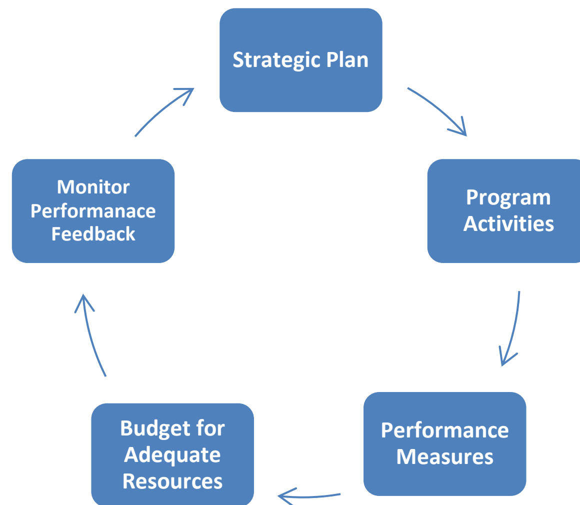
14.1.1. Strategic and Budget Planning Linked

The budget planning process can be a valuable tool for continuous improvement of agency programs. As a result, it is often linked with the agency's strategic plan, taking into consideration the following elements:[1]

- The agency's mandate, consistent with statutory requirements;
- A set of outcomes;
- The approaches to achieving these outcomes;
- A description of how activities and processes will be used to achieve these outcomes; and
- A budget outlining resources needed to deliver projected outcomes.

[1] The tax administration's strategic planning process is discussed in further detail in Chapter 15.

Figure 14.1. Budgeting and the strategic plan



The result of this exercise is a document outlining the agency's plans and, most importantly, how these plans are to be achieved. If done effectively, the agency properly budgets for each item in the strategic plan, which serves as the roadmap for everything the organization does on a daily basis.

14.1.2. Budgeting Methodologies

The approach taken by the agency in developing its proposed budget in support of the strategic plan can directly influence the level of funding that it is allotted. Outlined below are a number of approaches often referred to when discussing the budgeting process.

- The **top-down approach** to budget planning generally refers to the assignment of spending ceilings to agencies before annual budget requests are prepared. Often, officials establishing the ceiling limits are somewhat removed from the day-to-day budgetary challenges experienced at the front line in implementing policies and procedures. This can lead to a budget that does not adequately reflect the resources needed at the front line. As a result, agencies may feel they are required to meet impossible standards without adequate resources.
- A **bottom-up budget** is generally created by middle managers and submitted to upper management for approval. Although prepared by individuals implementing the budget, bottom-up budgeting has its drawbacks, because managers may tend to overestimate the resources needed in anticipation of potential cuts as it goes through the review process. Since line managers may view things from the perspective of their individual programs, little appreciation may be given to the big picture, e.g., the challenges of allocating resources for the entire country.
- A **line item budget** is simply a listing of each of the agencies' revenue sources and each item that will be purchased during the fiscal year. The line-item budget has historically been the most widely used budgeting methodology, because it is relatively easy to prepare and requires limited financial skills. The simplicity of the methodology also allows for management officials to easily monitor revenue and expenditures. The major deficiency of line-item budgeting is the difficulty in determining the actual results generated as a result of resources expended. It is also difficult to

establish priorities and determine the quantity or quality of services which could be generated at various expenditure levels.

- A **program budget** provides the agency with the opportunity to identify the total cost of each program and set spending limits and priorities. A downside, however, is that programs tend to overlap, which can make allocating resources and collecting data difficult.
- **Performance budgeting** similarly reflects the budget of each program, but also incorporates performance information. Specific goals and objectives are tied to expenditures for each program. The focus is on what will be accomplished with the resources provided.
- **Zero-based budgeting** starts with **"zero"** and requires all departments to justify funding for their programs. Budgets are established based upon what is needed for the upcoming period, regardless of whether the budget is higher or lower than prior allotments. The department must also reflect the various levels of service which could be provided with different levels of funding options available. A justification document is also required to reflect the effects of various funding levels (e.g., maintaining the current level, reducing funding by a certain percentage, or increasing funding by a certain percentage).

Although the line-item budget methodology has historically been the most widely used, international trends have been moving towards performance-based budgets. This change has occurred because line item budgets reflect what resources will be spent on (e.g., salaries, benefits, office supplies, travel, utilities, equipment, etc.), whereas performance-based budgets reflect on what will be accomplished as a result of the resources expended in terms of measurable results achieved (e.g., increased revenue collection, increased customer satisfaction, etc.). The attention to program results in a performance-based budget provides an advantage over traditional budgeting approaches.

A comparison of the pros and cons of the various budget methodologies is presented in the figure below.

Figure 14.2. Comparison of budgeting models

TYPE BUDGET	PURPOSE	CHARACTERISTIC	RESPONSIBLE PARTIES	SUCCESS FACTORS	PROS	CONS
1. Line Item	a. Aims to spend resources according to plan b. Prevents misappropriation of funds c. Promotes financial accountability	Focus on prior year allocation as starting point	Central budget managers	Minimum amount of staff time and expertise needed to create and track the budget	Works well when time is short and there is considerable complexity, with multiple stakeholders and a high potential for conflict	Not good for dealing with questions of efficiency, effectiveness, and future and/or previously neglected concerns
2. Program	a. Aims to ensure that programs are achieving goals and objectives b. Promotes program accountability and effectiveness	Focus on program plans, goals, and objectives	Program analysts and managers	Requires the resources necessary to develop program plans, goals, and objectives	Provides a clear linkage between program activities and budget allocation	Requires considerable investment of resources and has a high potential for conflict
3. Performance	a. Aims to ensure that programs are effective b. Aims to ensure that program are efficient (cost effective) c. Promotes efficiency / effectiveness	Performance measurements utilized to determine efficiency and effectiveness	Mid–level managers	Requires considerable resources to develop reliable measures and time to develop the skill sets of those responsible for developing measurements	Provides an objective way of documenting accomplishments	Time-consuming and expensive, with a high potential for resistance because of fear of measures being used to reduce funding
4. Zero-Based	a. Assesses continuation of programs annually b. Focuses on priorities	Annual evaluation of current program activities	All levels of management	Requires considerable time and resources to assess all programs annually	Provides an opportunity for activities to be evaluated annually and an opportunity to reallocate resources	Places a high burden on organizational resources, and it is difficult to achieve comparability across organizational units

14.1.3. Budget Preparation

In the tax administration, budget formulation starts at the headquarters office, well in advance of the start of the calendar or fiscal year, and with consideration and joint deliberations by top-level officials of the impact of applicable Ministry and/or government-wide directives and resource ceilings, long-term strategic objectives of the tax administration, and historical performance data to develop annual work plans for the operations functions, from which costs for budget formulation can be computed. From these deliberations, after approval by the Deputy Director General (Operations),[2] each of the operations chiefs issues, to each district/field office director and division heads, higher-level directives, an outline of expectations, and planning assumptions for the development of annual work plans. These "assumptions" include the changes or improvements in laws, procedures, methods, systems, or resources that are expected for the next year and should be considered by each of the operations functions in planning for results.

Each of the division heads, with input from subordinate managers and coordination and approval of the district-field office director, develops and submits to headquarters an annual work plan to meet the expectations outlined by their respective headquarters offices. The annual work plans are corrected, adjusted, and consolidated at headquarters. Costs are then computed for salaries, training, capital improvements, etc., and the tax administration's proposed budget is presented to the MOF. The tax administration's representative at the MOF for budget purposes should be the Deputy Director General (Administrative Services) and/or his or her Chief Budget Officer.

To ensure an all-inclusive process, consideration should be given to utilizing the following approach in developing the agency's work plans and budget.

- Ensure that an Information Technology (IT) representative is included at all functional meetings for work plan development. There is often a disconnect between IT and the operational units, and efforts to bring them together early in the budget planning process can enhance overall program delivery;
- Participants at all levels should come to an agreement on the overall approach to be utilized throughout the work plan and budget planning process, including but not limited to the following:
    - Considering lessons learned from prior work plan and budget planning exercises to capitalize on successes and address problems experienced in the past;
    - Developing reporting templates (as needed) and automating as much of the process as possible to save time and ensure that everyone follows the same overall approach; and/or
    - Blocking off dedicated meeting time and brainstorming on the overall objectives of the organization and the resources needed to accomplish those objectives. If each function

[2] An organizational structure for the tax administration is suggested in Chapter 4.

is working in isolation and not taking into consideration the overall objective of the administration, resources will not be utilized in the most effective manner;

- Participants at all levels should be expected to work together to reconcile budget allocations that will allow the tax administration to achieve its objectives. This may include discussions on programs and activities that should receive additional funding, others that should remain at the previous year's level of funding, or even some that should undergo cuts. These discussions, including decisions to cut programs, should keep the need to achieve tax administration objectives as their focal point.
- Documentation and communication are critical to ensure that there are no misunderstandings as the process unfolds. Documenting and communicating the budget and work plan process timelines, the established guidelines, and the budget assumptions utilized will help keep everyone on the same page; and
- The final proposed budget document for the tax administration should reflect a consolidated and complete view of the resources needed to effectively deliver the administration's programs.

14.1.4. Developing Cost Estimates

Regardless of which budget methodologies they utilize, agencies will need to prepare their best estimate of the actual costs for delivering program results. In preparing an appropriate cost estimate to formulate the budget, it is critical to think through what is required in a logical manner. Consideration should be given to resources required to effectively deliver current programs, new programs, and capital investments, such as integrated tax management systems. Particular care should be taken with regard to cost estimates for IT and training needs, including determining true needs and computing and communicating cost-benefit analyses for both, as discussed below. Tax administrations must now have a variety of modern IT systems to be effective and efficient in the modern business environment and, as discussed below and in Chapter 12, the acquisition of technology is one of the major expenditures undertaken by most tax administrations. Training of staff – not just basic training, but continuing professional education and "refresher" courses – are vital for top performance and delivery of expectations by tax administration staff. Training is, unfortunately, often relegated to a low level of priority in many tax administrations because of budget shortfalls.

Clearly, for all costing, budgets should require a justification which explains the rationale for each budget category and how the agency arrived at its cost estimates. Tax administrations must be able to show how the allotted resources will ultimately enhance revenue collections (directly or indirectly). Some preliminary questions to consider during the costing exercise include:

- What resources are needed to implement ongoing programs, including staffing, facilities, equipment, office supplies, transportation, fuel, telephone, etc.?
- What resource constraints hindered the agency from meeting last year's goals and objective?
- Are there new laws, policies, and procedures that must be implemented?
- Are the current resources sufficient to implement new laws, policies, and procedures and, if not, what additional resources are required? and

- What capital investment initiatives are being considered, and what resources are needed to bring these initiatives to fruition?

Every planned activity should have a cost attached. The typical costs incurred to deliver tax administration programs are outlined below.

1. **Personnel Costs:** Personnel costs generally comprise the largest amount of requested funds.
   a) **Salaries:** Salaries are monetary compensation paid to the administration's employees, including executives, managers, technical staff, administrative staff, etc. Based upon the information included, consideration should be given to:
      - Whether cost of living increases or merit awards will be given. The tax administration must budget accordingly for the cost of these items; and
      - Whether there is a need to recruit new hires. Before deciding to recruit new hires, the tax administration should evaluate whether staffing in other departments can be utilized to accommodate vacancies. If additional staffing is needed, the cost of new personnel should be included. If the recruitment process has not been finalized, the normal salary rate for the position being recruited should be included.

   b) **Fringe benefits:** Fringe benefits are additional benefits provided to supplement an employee's regular pay. Some examples of fringe benefits include:
      - Life and health Insurance;
      - Social security;
      - Retirement plans;
      - Transportation; and/or
      - Accommodation.

   c) **Consultants:** Consultants are individuals who provide expert advisory or other services for brief or limited periods of time. The budget justification for consultants should include:
      - The consultant's name and organizational affiliation (if applicable);
      - The services and/or advice they are going to provide;
      - Their daily rate of pay, and the number of days they will work on the project or program; and
      - Costs to cover any travel and per diem for bringing outside consultants to the agency.

2. **Non-personnel cost:** Consideration should be given to the tools personnel need on a daily basis to carry out their activities.
   a) **Furniture and equipment:** Work stations, chairs, file cabinets, computers, etc.
   b) **Materials and supplies:** Materials and supplies include items such as paper, pencils, computer software, photocopy paper, ink, toner, etc.
   c) **Communication:** Communication costs include the cost of various mediums utilized in communicating with taxpayers, such as telephone installation, monthly telephone charges (landlines, mobile phones, voice over Internet protocol), Internet service providers, printing, photocopying, and related duplicating expenses, such as binding, postage, etc.

d) **Travel:** Travel costs include transportation (air, boat, auto, ground, etc.), housing (hotel, motel, guest house, etc.), meals, tips, phone calls, and similar expenses. Consideration should be given to local, domestic, and international travel needs. A budget justification for travel should address:

- The purpose of the travel;
- The specific destination, if known, of each trip;
- The number of individuals going on each trip;
- The mode and cost of transportation to be used; and
- The number of days of per diem and the per diem rate.

e) **Other expenses:** Other expenses should be as carefully defined as other categories outlined in the budget. One example of this type of expense is:

- Training and staff development: Since a large portion of an agency budget is spent on training and staff development, it is important to budget carefully.[3]

3. **Indirect costs:** Indirect costs, sometimes referred to as overhead or facilities and administrative costs, are those costs that are not specifically attributable to a particular program, but are valid expenses associated with the general operation of agency. These may include:
   - Office rental;
   - Operations and maintenance of facilities; and/or
   - Security;
4. **Capital investments**: Capital investments include the acquisition of capital assets, which, in government accounting, are simply assets that are expected to be productive over several years. These include:
   - Vehicles;
   - Building construction or renovation; and/or
   - Information technology.

One of the major capital investments undertaken by most tax administrations worldwide is the acquisition of integrated tax systems and data warehouses. Depending on the size and the needed functionality of the system, the cost of this investment could range from US$10 million to over US$100 million.

Capital investment initiatives are often faced with implementation delays, cost overruns, and funding constraints. Therefore, in establishing a budget for these types of investments, the tax administration should utilize the "Twelve Steps of a High-Quality Cost Estimating Process" shown in Appendix 14.A. Outside assistance from subject matter experts should also be considered to help identify the size and range of costs generally associated with the effort under consideration.

[3] According to the American Society of Training and Development, in the United States, major organizations spend over 3 percent of their total payroll on training (American Society for Training and Development (2012), p. 7.). In addition, in 2010, 15 out of 34 OECD tax administrations reported major planned changes in staff training (OECD (March 2011), p. 103).

14.1.5. Managing Budget Execution / Implementation

Once the budget has been approved, the next step is budget execution – also referred to as budget implementation. The budget execution process involves ensuring that the financial resources made available to an agency are directed towards achieving the program deliverables outlined in the strategic plan for which the funds were appropriated.

Once the budget authorization is received, the tax administration may obligate funds to carry out program activities. However, the final budget may often be less than what was originally reflected in the strategic plan. A review of the plan in light of the actual budgetary allocations should be conducted, modifications made as appropriate, and responsible parties designated for the delivery and periodic reporting of results.

Each tax administration unit is responsible for evaluating programs and examining projects to ascertain whether they are meeting their targets and objectives on an ongoing basis. Generally, most tax administrations have established monthly reporting of key performance indicators for program deliverables. The tax administration should assess not only the effectiveness of the program, but also the effective use of the allotted budget in executing the program.

Some common problems associated with budget execution include:

- Large deviations between the approved budget and the proposed budget, thereby undermining policy and planning efforts;
- Spending above approved levels;
- Weak internal controls that allow waste, fraud, and abuse;
- Insufficient record-keeping, hindering effective audits; and
- Untimely reporting, hindering the agency's ability to manage spending;

Operational reviews should therefore be conducted periodically to monitor, measure, and evaluate performance. Reviews should take into account the points listed below.

- The tax administration should evaluate its financial performance relative to the final budget. Regular monitoring of budgetary performance provides an early warning of potential problems and gives decision makers time to consider modifications if major deviations in budget-to-actual results occur;
- The tax administration should monitor and evaluate external factors that may affect budget performance and achievement of goals. Factors outside the administration's control, such as the national or regional economy, statutory changes, and legislative mandates, may affect achievement of goals. Monitoring these factors helps the administration to evaluate and respond to the effect of these external influences on programs in a timely manner;
- The tax administration should monitor, measure, and evaluate capital program implementation. Monitoring the status of capital projects helps to ensure that projects are progressing as planned, problems (such as delays in key milestones and cost overruns) are identified early

enough to take corrective action, funds are available when needed, and legal requirements are met;

- The budget should be adjusted in light of unforeseen events. The budget is a plan based on a set of assumptions that may not always match actual experiences during the implementation phase. The tax administration should watch for significant deviations from expectations and modify the plan to reflect revised expectations; and
- The tax administration should monitor and evaluate taxpayer satisfaction with programs and services. Often, the main contact for many taxpayers with the tax administration is through the programs and services that it provides. Therefore, it is important for the administration to be aware of and respond to taxpayers' perceptions of these programs and services. The taxpayers' perception of the quality of services is an important factor in their overall perception of the administration and has a potential impact on the allocation of resources.

Establishing an effective budget execution process increases the tax administration's ability to more efficiently and effectively deploy resources and to introduce modifications to the plan, if required, in a timely manner.

14.2. Common Trends

With the current worldwide economic situation and revenue pressures experienced by government, many tax administrations have started evaluating options to secure the resources needed to deliver programs. One area receiving increased attention is self-budgeting based on a percentage of revenue collected. Opponents have expressed concern that tax administrations that are paid based on revenue collected may use pressure tactics to collect the maximum amount.

The first country in LAC to implement self-budgeting based on a percentage of revenue collected was Peru in 1991, using 2 percent of tax revenues collected, followed by Argentina, Bolivia, and Guatemala.[4] The concept of basing the tax administration's budget on collected revenue has been embraced in theory by a number of countries, especially those which have created revenue authorities.[5] To increase the base revenue collections upon which the percentage would be taken, other tax administrations have assumed collection of non-tax related services, such as stamp duty, motor vehicle registration, and transfer of motor vehicle ownership.

In some countries, such as Kenya, the annual budget disbursements made to the tax administration have historically been less than the specified percentage. To correct this problem, some have argued that agencies should be allowed to deduct their allowable percentage first, and then transmit the balance to the general account, rather than depositing the full amount of revenue in the general account and waiting for the disbursement later. This practice should be discouraged. If the tax administration is allowed to retain a fixed percentage of revenue collected, it will have no incentive to become more cost efficient in the programs they execute. In addition, and equally important, the tax

[4] Inter-American Center of Tax Administrations (CIAT) et al. (2012), section 2.1.
[5] Revenue authorities are discussed in Chapter 4.

administration will have a very strong incentive to ignore the rights of taxpayers and generate unjustified additional assessments or undertake unwarranted enforcement actions in order to increase their budget.

Another issue gaining increased attention is the policy adopted by many governments whereby unspent funds lapse at the end of the year. This practice encourages managers to use funds near the end of the fiscal year for fear of budget reductions in subsequent years. This year-end spending spree, however, may not lead to the most effective use of resources. Effective management and monitoring of budget expenditures in line with program deliverables throughout the year may leave some funds unspent at the end of the year. Thus, some have argued that agencies should be allowed to automatically carry up to two percent of the budget forward to the next year.

14.3. Tax Administration Maturity

The use of a maturity model allows the tax administration to self-assess its operations and design strategies for adopting leading practices. Since the budget planning process is critical to the overall success of the administration, opportunities for continuous improvement should always be explored.

Evaluating existing operations against the following maturity model is the first in a series of steps that should be taken. Consideration should be given to: 1) targeting a specific maturity level for each key area; 2) determining the maturity level of current practices and identifying the gap between the current practices and the desired maturity level; 3) assessing the risks to the agency and the biggest opportunities for improvement; 4) establishing priorities and assigning accountability for developing and implementing improvement strategies; and 5) implementing a process to ensure continuous improvement through routine monitoring and periodic assessments.

Budget Planning and Resource Management: Maturity Level 1

Key word: "Scattered"

- The tax administration has some financial management practices (e.g., for budgeting, managing cash flow) in place, but they are inadequate, with many gaps that affect day-to-day operations.
- Managers know many of the costs of their activities, but there is no consideration of the impact of operational, programmatic, or strategic changes on costs.
- No benchmarking of costs of other agencies is performed, which limits the administration’s ability to understand its cost drivers.
- There is limited project planning or project management for capital investments. Occasional projects may have project plans with risk management arrangements and timetable for delivery, but the use of plans is inconsistent and there is no aggregation of project plans at program level. No projects are subjected to rigorous expenditure appraisal (a detailed analysis for the project rationale, relevance, effectiveness, efficiency, and impact).
- Budgets are finalized after the start of the fiscal year.

- There is a lack of monitoring of expenditures. There is a distinct lack of automated processes, and most monitoring is paper-based.
- The tax administration has no awareness of the data and corresponding IT needs of different users, both internal and external and users find that the reports they receive do not give them the information they need.
- Financial and operational performance is not openly discussed with external stakeholders.
- Financial and operational performance information is reported separately, and their formats are incompatible. They are often reported at different times and use different metrics, making it impossible to assess a single activity or output from both a financial and operational perspective.
- Staff who monitor the budget tend to use their own spreadsheets rather than the existing financial systems, leading to significant manual work and duplication of monitoring.

Budget Planning and Resource Management: Maturity Level 2

Key word: "Basic"

- The tax administration has basic financial management practices in place that allow it to function on a day-to-day basis, but that are not adequately linked to the administration's operational performance data.
- Managers know many of the costs of their activities, but there is little understanding of the impact of operational, programmatic, or strategic changes on costs.
- No benchmarking of costs of other agencies is performed, which limits the administration's ability to understand its cost drivers.
- There is still limited project planning or project management for capital investments. Significant projects may have project plans with risk management arrangements and timetables for delivery, but the use of project plans is inconsistent and there is no aggregation of project plans at program level. A few major projects are subjected to rigorous expenditure appraisal (a detailed analysis for the project rationale, relevance, effectiveness, efficiency, and impact).
- Budgets are finalized after the start of the fiscal year.
- Monitoring information is not provided to senior management until the second half of the fiscal year and contains little forecast information.
- The tax administration's different systems produce contradictory internal monitoring information reports, and the year-end statutory accounts are difficult to reconcile with management information. Little investment is made in IT.
- Financial and operational performance information is openly discussed with external stakeholders, but the presentation is likely to be unclear and lacking sufficient explanation for non-finance professionals, giving rise to the risk that users will fail to understand the impact of the information.
- Financial and operational performance information is still reported separately, and their formats are incompatible. They are often reported at different times and use different metrics, making it

impossible to assess a single activity or output from both a financial and operational perspective.

- Staff who monitor the budget are unable to access monitoring information online and in a format that allows them to monitor or forecast information easily.

Budget Planning and Resource Management: Maturity Level 3

Key word: "Rigorous"

- The tax administration has in place professional financial management practices which enable it to cope effectively in challenging times and will identify opportunities to improve its performance.
- Managers and staff can demonstrate their understanding of costs, different ways in which costs can be measured, and the ways in which costs can change when discussing current operational and future plans. They are, however, not always aware of the costs of outcomes and programs and the impact of changes on those costs.
- Cost analyses are regularly updated and there is an effort to benchmark costs across operational units, but there is little effort to look for benchmarks outside of the administration.
- The administration has a rigorous approach for capital expenditure appraisal and project management. All plans are produced to an acceptable level of quality. The business case, along with program and project management processes, is meaningful and adds value to the agency. All significant programs and projects consider the expenditure appraisal (a detailed analysis for the project rationale, relevance, effectiveness, efficiency, and impact), risk management plan, and project plan.
- Budgets are agreed at least a month before the start of the fiscal year and managers are fully aware of what budget levels to expect.
- Managers are able to use the financial systems to produce accurate, timely monitoring information, but not always forecasts. A comprehensive set of tailored reports is available for internal use. The systems enable the creation of reports that drill down as necessary and meet specific needs. The administration occasionally reviews the ongoing relevance of the suite of reports.
- There are reliable IT systems that are linked across all primary financial statements and that can be accessed remotely by managers. The system is integrated to minimize duplication of information and maximize interface possibilities.
- Financial and operational performance is openly discussed with external stakeholders and appropriate information is presented in a relevant and useful manner for external stakeholders.
- A set of operational performance metrics is reported jointly with financial information and aligned to the strategic objectives of the tax administration.
- Staff who monitor the budget and operational managers can access the reports and monitoring information easily. There is a clear and visible trail from the regular management accounts to the year-end financial statements.

Budget Planning and Resource Management: Maturity Level 4

Key word: "Strategic"

- The tax administration has in place financial management practices that allow it to anticipate both challenges and opportunities for improvement.
- Managers and staff can demonstrate their understanding of costs, different ways in which costs can be measured, and the ways in which costs can change when discussing current operational and future plans. They are aware of the costs of outcomes and programs and the impact of changes on those costs.
- Cost analyses are regularly updated and there is an effort to benchmark costs across operational units and outside of the administration.
- The administration has a rigorous approach for capital expenditure appraisal and project management. All plans are produced to an acceptable level of quality. The business case, along with program and project management processes, is meaningful and adds value to the agency. All significant programs and projects consider the expenditure appraisal (a detailed analysis for the project rationale, relevance, effectiveness, efficiency, and impact), risk management plan, and project plan. There is a readily applicable methodology for small to medium project appraisals.
- Budgets are approved one to two months before the start of the fiscal year as a result of a well-organized planning process and are updated to reflect any significant events close to the end of the year.
- Managers are able to use the financial systems to produce accurate, timely monitoring information and forecasts. A comprehensive set of tailored reports is available for internal use. The systems enable the creation of reports that drill down as necessary and meet specific needs. The administration routinely reviews the ongoing relevance of the suite of reports.
- There are reliable IT systems that link across all primary financial statements and that can be accessed remotely by managers. The system is integrated to minimize duplication of information and maximize interface possibilities.
- Financial and operational performance is openly discussed with external stakeholders and external reports contain information tailored to users' needs and are developed in collaboration with key external groups and partners.
- A set of operational performance metrics is reported jointly with financial information and aligned to the strategic objectives of the tax administration.
- Staff who monitor the budget and operational managers can access the reports and monitor information easily. There is a clear and visible trail from the regular management accounts to the year-end financial statements.

14.4. Latin America and the Caribbean

In 2006, the OECD surveyed the budget agencies in the following seventeen countries from Latin American and the Caribbean (LAC) to solicit comparative data on budgetary procedures and institutions:

Argentina, Barbados, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Guatemala, Jamaica, Mexico, Panama, Paraguay, Peru, Trinidad and Tobago, Uruguay, and Venezuela. Survey results from 13 countries responding indicate that many LAC countries have introduced performance information into the budgeting process.[6] The constitutions of countries like Brazil, Colombia, and Mexico actually mandate the linkage of performance budgeting to objectives reflected in their National Development Plans.

Individual countries, however, are at different stages of implementation. Argentina, Chile, and Mexico have been developing performance measures for almost fifteen years, while Ecuador, for example, had just started a pilot program at the time of the survey, and Venezuela had not developed any performance measures.

The following table reflects the approach used to evaluate performance in different LAC countries.

Figure 14.3. Performance evaluation measures in LAC[7]

	Performance Measures	Evaluation	Benchmarking	Other
Argentina	X			
Bolivia		X		
Brazil	X	X		
Chile	X	X	X	X
Colombia	X	X		
Costa Rica	X	X		
Ecuador			X	
Guatemala	X			
Mexico	X	X		
Paraguay	X			
Peru		X	X	
Uruguay	X	X		

However, the survey also noted that, in many LAC countries, information on performance is not used in negotiations between the Ministry of Finance and agencies. In addition, the survey noted that most countries in the region, with the exception of Bolivia and Uruguay, rely on an organic budget law – one that establishes budgeting fundamentals, but that countries vary in many aspects of the budgeting process.[8] For example, the time frame for budget negotiations between the central budget department and agencies varies between half a month (Brazil) to five months (Colombia) and that the number of mid-year budget amendments can be as little as none (Chile, Guatemala, Mexico) or as high as 20 (Venezuela).[9]

[6] Curristine et al. (2007), p. 4.
[7] Ibid., p. 23.
[8] Ibid., p. 5.
[9] Ibid., p. 19. The number of supplementary budgets is for the two years prior to the report.

According to a high-level study of budgeting in tax administrations by CIAT, the budget process for tax administrations in the region has been affected significantly by the trend to establish semi-autonomous revenue agencies.[10] The following are highlights:

- Only the Guatemalan tax administration has the autonomy to determine its own budget. All tax administrations are subject to the supervision of the Comptroller or Court of Auditors.
- In 1991, Peru was the first LAC country to introduce a model for financing whereby 2 percent of revenue collections were allocated to the tax administration budget. This model was followed by other countries, such as Argentina, Bolivia, and Guatemala.[11]
- Not all semi-autonomous revenue agencies, however, use salary scales that are separate from the civil service scales. Argentina, Bolivia, Colombia, the Dominican Republic, Guatemala, Honduras, Nicaragua, and Uruguay can do so.
- The tax administrations' budgets grew significantly during 2006-2010, by approximately 25 percent on average, but individual countries vary. While spending on tax administration in Argentina and Honduras increased by over 100 percent during the period, Bolivia, El Salvador, Guatemala, and Nicaragua show decreases.
- In 2010, 68 percent of the tax administrations' budgets were directed to staff costs, which is in line with averages across OECD (72 percent[12]). Approximately 4 percent were directed to investment, although there were large variations.[13]
- The average cost of tax collection – the ratio of the tax administration budget to collected revenue – was 1.37 percent, which was over the OECD average of 0.96 percent.[14]

14.5. Key Benchmarks and Guidelines

The evaluation of the overall budget is the responsibility of an independent government auditing office. This office generally has the role to evaluate the execution of the budget regulations and, if necessary, conduct investigations regarding any violations of the legal framework by public officials, as well as suggest sanctions when appropriate. All agencies, however, should conduct their own internal reviews to:

- Ensure resource allocations are within statutory limits and used for their intended purpose;
- Examine the extent to which desired results are being achieved and whether they can be achieved at a lower cost alternative to reach the desired results;
- Evaluate the efficiency of the operation, including the utilization and control of resources (e.g., duplication of efforts, mismanagement of equipment, supplies, etc.);
- Evaluate whether financial records are complete and reliable;

[10] Inter-American Center of Tax Administrations (CIAT) et al. (2012), section 2.1.
[11] In addition, as discussed in Chapter 10, Brazil and Chile have undertaken initiatives to reward tax collectors based on their collection effort.
[12] OECD (March 2011), p. 118.
[13] There is no comparable OECD information, but the study does indicate that the amount may be insufficient (Inter-American Center of Tax Administrations (CIAT) et al. (2012), section 2.4).
[14] Ibid., section 2.5.

- Determine whether program implementation targets are being met;
- Determine the degree to which the goals and objectives outlined in the strategic plan are being achieved;
- Determine whether data are being collected and reporting guidelines are being followed;
- Determine whether there is supporting documentation for all funding documents issued;
- Determine whether the operating units verify availability of funds prior to obligating funds; and
- Determine whether performance against obligation plans is evaluated monthly, and whether the tax administration researches the cause of deviations that exceed plus or minus 5 percent.

With respect to tax administrations, various quantitative benchmarks can be devised but should be used with caution, as circumstances – legal and economic – can impact benchmarks significantly. An important benchmark is the cost of collection ratio discussed above (i.e., expenditures of the tax administration over revenues collected). The cost of collection in OECD countries on average is approximately one percent. Other benchmarks are discussed above and in various chapters of this product, such as expenditures on IT over total expenditures (11 percent), the cost of the collection function over total expenditures (30 percent), and expenditures on salaries over total expenditures (70 percent).

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Appendix 14.A. The Twelve Steps of a High-Quality Cost Estimating Process

Figure 14-A.4. The twelve steps of a high-quality cost estimating process

The Twelve Steps of a High-Quality Cost Estimating Process[15]	
1. Define the purpose of the estimate	a. Determine the estimate's purpose, required level of detail, and overall scope; b. Determine who will receive the estimate.
2. Develop estimating plan	a. Determine the cost estimating team and develop its master schedule; b. Determine who will do the independent cost estimate; c. Outline the cost estimating approach; d. Develop the estimate timeline.
3. Define program characteristics	In a technical baseline description document, identify: a. The program's purpose and its system and performance characteristics and all system configurations, as well as any technology implications; b. Its program acquisition schedule and acquisition strategy; c. Its relationship to other existing systems, including predecessor or similar legacy systems; d. Support (manpower, training, etc.) and security needs and risk items; e. System quantities for development, test, and production; f. Deployment and maintenance plans.
4. Determine estimating structure	a. Define a work breakdown structure (WBS) and describe each element in a WBS dictionary (a major automated information system may have only a cost element structure); b. Choose the best estimating method for each WBS element; c. Identify potential cross-checks for likely cost and schedule drivers; d. Develop a cost estimating checklist.
5. Identify ground rules and assumptions	a. Clearly define what the estimate includes and excludes; b. Identify global and program-specific assumptions, such as the estimate's base year, including time-phasing and life cycle; c. Identify program schedule information by phase and program acquisition strategy; d. Identify any schedule or budget constraints, inflation assumptions, and travel costs; e. Specify equipment the government is to furnish, as well as the use of existing facilities or new modifications or developments; f. Identify the prime contractor and major subcontractors; g. Determine technology refresh cycles, technology assumptions, and new technology to be developed;

[15] Adapted from U.S. Government Accountability Office (2009), p. 9.

The Twelve Steps of a High-Quality Cost Estimating Process[15]	
	h. Define commonality with legacy systems and assumed heritage savings; i. Describe the effects of new ways of doing business.
6. Obtain data	a. Create a data collection plan with an emphasis on collecting current and relevant technical, programmatic, cost, and risk data; b. Investigate possible data sources; c. Collect data and normalize them for cost accounting, inflation, learning, and quantity adjustments; d. Analyze the data for cost drivers, trends, and outliers and compare results against rules of thumb and standard factors derived from historical data; e. Interview data sources and document all pertinent information, including an assessment of data reliability and accuracy; f. Store data for future estimates.
7. Develop point estimates and compare to an independent cost estimate	a. Develop the cost model, estimating each WBS element, using the best methodology from the data collected, and including all estimating assumptions; b. Express costs in constant year dollars; c. Time-phase the results by spreading costs in the years they are expected to occur, based on the program schedule; d. Sum the WBS elements to develop the overall point estimate; e. Validate the estimate by looking for errors like double counting and omitted costs; f. Compare the estimate against the independent cost estimate and examine where and why there are differences; g. Perform cross-checks on cost drivers to see if results are similar; h. Update the model as more data become available or as changes occur, and compare results against previous estimates.
8. Conduct sensitivity analysis	a. Test the sensitivity of cost elements to changes in estimating input values and key assumptions; b. Identify effects on the overall estimate of changing the program schedule or quantities; c. Determine which assumptions are key cost drivers and which cost elements are affected most by changes
9. Conduct risk and uncertainty analysis	a. Determine and discuss with technical experts the level of cost, schedule, and technical risk associated with each WBS element; b. Analyze each risk for its severity and probability; c. Develop minimum, most likely, and maximum ranges for each risk element; d. Determine the type of risk distributions and reasons for their use; e. Ensure that risks are correlated; f. Use an acceptable statistical analysis method (e.g., Monte Carlo simulation) to develop a confidence interval around the point estimate;

The Twelve Steps of a High-Quality Cost Estimating Process[15]	
	g. Identify the confidence level of the point estimate; h. Identify the amount of contingency funding and add this to the point estimate to determine the risk-adjusted cost estimate; i. Recommend that the project or program office develop a risk management plan to track and mitigate risks.
10. Document the estimate	a. Document all steps used to develop the estimate so that a cost analyst unfamiliar with the program can recreate it quickly and produce the same result; b. Document the purpose of the estimate, the team that prepared it, and who approved the estimate and on what date; c. Describe the program, its schedule, and the technical baseline used to create the estimate; d. Present the program's time-phased life-cycle cost; e. Discuss all ground rules and assumptions; f. Include auditable and traceable data sources for each cost element, and document for all data sources how the data were normalized; g. Describe in detail the estimating methodology and rationale used to derive each WBS element's cost (more detail is better than less); h. Describe the results of the risk, uncertainty, and sensitivity analyses and whether any contingency funds were identified; i. Document how the estimate compares to the funding profile; j. Track how this estimate compares to any previous estimates.
11. Present the estimate to management for approval	a. Develop a briefing that presents the documented life-cycle cost estimate; b. Include an explanation of the technical and programmatic baseline and any uncertainties; c. Compare the estimate to an independent cost estimate (ICE) and explain any differences; d. Compare the estimate (life-cycle cost estimate (LCCE)) or ICE to the budget with enough detail to easily defend it by showing how it is accurate, complete, and high in quality; e. Focus in a logical manner on the largest cost elements and cost drivers; f. Make the content clear and complete so that those who are unfamiliar with it can easily comprehend the competence that underlies the estimate results; g. Make backup slides available for more probing questions; h. Act on and document feedback from management; i. Request acceptance of the estimate.
12. Update the estimate to reflect actual costs and changes	a. Update the estimate to reflect changes in technical or program assumptions or to keep it current as the program passes through new phases or milestones;

The Twelve Steps of a High-Quality Cost Estimating Process[15]	
	b. Replace estimates with earned value management (EVM) estimate at completion (EAC) and independent EAC from the integrated EVM system; c. Report progress on meeting cost and schedule estimates; d. Perform a postmortem and document lessons learned for elements whose actual costs or schedules differ from the estimate; e. Document all changes to the program and how they affect the cost estimate.