

Incentives, Certification and Targets in Performance Budgeting

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I. Introduction

Budget decision makers require useful information in the claims advocates present. When they want performance and efficiency savings information, many if not most decision makers find it difficult to gain and even more difficult to analyze and apply. Three major budget reforms have competed over the last two decades in using or ignoring information: an incentives approach, a certification approach, and a spending target approach. All three have tried to connect budgeting with larger efforts called either managing for results or expenditure control.

Our research question takes for granted that each reform promises decision makers productivity increases and actual dollar savings. The research question asks: which of these reforms does a seasoned public manager use, which can allocate discretion most decisively, which controls aggregate spending, and which can produce trust in government?

The methods employed to find the answer to the research question rested on a series of focus groups and instrumented interviews of seasoned public managers and decision makers. The three models we investigated come from a trade—budget details for totals—creating a results-rewards system based on target budgeting, performance measures, and retained savings. We begin by providing the impetus for the research, the performance reforms, and the model in its entirety.

II. Background

In 2000, we received an email from Alec Andrus, budget officer for the City of Boise, Idaho, USA replying to a question asked about gain sharing, another name for retained savings or fiscal year carry forwards. He sent an exchange of email correspondence with Debbie Bair in the City of Tempe Arizona, USA describing the relative merits of biennial budgeting instead. The Andrus description admired gain sharing, but we suspected that the gains shared had more to do with technical details of biennial budgeting or multi-year budgeting than with actual retention of savings by departments. We wondered whether anyone actually used the delegated budgeting idea that became reality in retained savings.

The problem of incentives for savings comes from several sources. Reflecting one of the oldest stories students tell teachers about their experience with government budgets, Barrett and Greene (2002, 74) point out that “When a state or local agency has money left at the end of the year, a spendthrift mentality tends to take over.” They tell the story of purchases of goods not already budgeted and overtime for employees unbudgeted as well.

Yet budget theory suggests the incentive for a spendthrift mentality. Since empirical research began to accumulate, some have warned budgeters to “avoid too good results” (Wildavsky, 1964, 93). The support for the warning about the reaction to unspent funds by political leaders is not hard to find. Wildavsky quotes a typical budget reviewer as saying, “Since you are doing so well, as we have heard for fifteen minutes, you surely do not need [a bigger budget].” Warren’s empirical test (1975) confirms Wildavsky’s view. Other budget behavior observers, such as Schick (1978, 179), have agreed, pointing out that the “budget process conventionally confronts managers with the uncomfortable risk of a loss of funds if they try to purge inefficiencies from their agencies.” The fact that an agency performs well does not inform the decision about the need for additional resources: “[S]hould 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?...If a program is doing badly, and showing few results, does this

mean it should be terminated, or provided with more resources to do a better job?” (Caiden, 1998, 44). In broader issues of resource allocation, Caiden finds performance somewhat irrelevant in deciding “whether a given sum of money is too little, too much, or just right to preserve a species, operate a system of trauma centers, or monitor or control contagious diseases.” Political popularity and the necessity of balancing budgets often become the sole reasons for budget decisions.

The idea of savings collided with budget reform when a professor described target base budgeting to a budgeting classes. A student reacted, “The politicians are forcing savings to finance their pork barrel!” Finally, it was realized that the soft version of a savings incentive could collide with the hard, target version in real life budgeting. Why would a set of policy makers choose one reform over the other? Thus, the implicit subject of this research is the reason for choice of a retained savings policy over a target base budget discretionary reserve policy.

Current reform efforts strive to strengthen government accountability by tightening the link between budget decisions and government performance. The belief in tightening the link, widely held, rests on the idea that the public, recognizing and understanding the performance-funding linkage and the success professionals in the public sector have in achieving results, will see the public sector, and public managers, as a productive, necessary, and important part of society.

The current performance-based reforms hail from some obvious places. Critics constantly beset governments with the complaint, why can't you operate like a business? Many have rebutted the notion behind the question: by the very nature of their work, government leaders aim for efficiency as only one goal among several. The fact remains that taxpayers, even politicians and managers, need a bottom line to tell them quickly whether their decisions are probably right or probably wrong and whether they are succeeding in their efforts to do their jobs well.

We recognize one major response to much of the taxpayer revolt in the message delivered by the “price of government” wing of the “reinventing government” movement both led by David Osborne. He argues that the movement he leads stems from the public servants’ extreme discomfort when they think traditionally and, finding that they do not know how to communicate how well or how poorly their work serves the public, face latent opposition at best and either incipient or fully developed revolt at worst (Osborne, and Hutchinson, 2004, 41-61).

One definition of the current problem—no one in government knows how to communicate how well they are doing what they think the citizens want them to do -- reflects an insider view. As many have observed, the citizen often is very far away from the issue of concern, the manager and elected official somewhere between citizen and issue (King, Feltey, and Susel, 1998).

As tax revolts and citizen complaints have mounted, the issues that most citizens, managers, and officials are alarmed about have surfaced in the budget. The budget directly or indirectly reflects every issue, with a power to force action in the direction citizens’ desire. Therefore, a second definition of the current problem emerges and reflects an outsider view – “Does the budget instill trust and confidence in how leaders spend citizens’ money?” How well has budgeting met not only professional standards of accountability, but how well has it achieve government’s broader obligations?

The present performance-based reforms have focused attention more than ever on allocating discretion in budgeting. Sharing information about what governments do well, through performance measurement and reporting, can go a long way in reducing cynicism (Berman, 1997). Broader and deeper participation in trading off various goals and means to achieve them, as well as in measuring progress

made as principals allocate resources, will yield better decisions and a sharing of risks among citizens, public managers, and elected officials.

III. What Is a Budget?

The current reform efforts in the United States reflect similar concerns in the private sector. These reforms have emerged through state and local government reforms in the National Advisory Council on State and Local Budgeting (1997). The reforms also arose through statute in the Government Performance and Results Act in the federal government. Other reform stories have appeared in the literature as expenditure control budgets or the so-called entrepreneurial budgets found in Schick's research in British Commonwealth and Scandinavian countries. These private and public sector examples as four models. The four models lead to the reasoning we used to proposal a synthesis in our own model.

A. Model 1. A private-sector model of budgeting takes a definite input-output-outcome form (Lazere, 1998; Churchill, 1984; Hax and Majluf, 1984; Knight, 1981; Trapani, 1982). First, forecasts of the economy, regulations governing business, and markets--customers and competitors--establish some horizon of opportunities and threats. Strategic goal setting follows with analysis of organization strengths and weaknesses. The result is the formulation of specific goals, including what market share the business and its business units can achieve over five or so years and what new business units might be created with what new products or services. The goals translate into annual or tactical performance plans--essentially what and who should do what this year. Plans include targets so that one knows whether one is making progress in achieving strategic business unit goals. The business unit also establishes measurable outputs and outcomes, called substantive and financial scorecards, weighting them in such a way that they balance emphasis and focus attention as intended. Budgets, in lump sum and having few process controls, follow plans and give considerable discretion to lower-level managers. Budgets also count in accrual terms, in that future spending is discounted to the present. Finally, individual employee performance plans follow from annual plans. Just as important, these individual plans and their measurable objectives tie into each individual's compensation. Needless to say, finance underlies and integrally relates all of these components: What does it cost and how much will that cost lever in earnings? The private-sector budget model differs from the public sector model we have known. There is accrual of spending and a multiyear period that budgets must span; previously hidden future spending is recorded in the present. Present decisions must accord with long-term goals. Structures are decentralized and budgets lump sums, especially where performance measures are adequate, policies farsighted, and managers adept.

B. Model 2. A similar picture develops in the operation of the Government Performance and Results Act of 1993 (Radin, 1998), and likewise in state and local results acts and executive orders (Melkers and Willoughby, 1998). To implement the federal Results Act, each agency must first develop strategic plans covering a period of at least five years. The strategic plan must include a mission statement, outcome-related measurable goals and objectives, and plans that agency managers and professionals intend to follow to achieve these goals through their activities and through their human, capital, information, and other resources. Those in the agency must consult Congress and others interested in or affected by the plans; in other words, they must consult stakeholders. As with the private-sector budget model, agency managers and professionals must develop annual performance plans that include performance indicators that will cover relevant outputs, service levels, and outcomes. With these performance plans, "Congress intended... to establish a direct annual link between plans and budgets" (GAO, 1999, 3) and to capture the long-range implication of choices and decisions with new methods of recognizing and measuring transactions in the budget (GAO, 2000; see also GASB, 1999).

C. Model 3. In their outline of expenditure control, Commonwealth and Scandinavian budgeting reforms, Cothran (2001) and Schick (2001) draw the dimensions of the fourth model along lines of central control of goals, decentralization of means, and accountability for results. First, central agencies and

leaders control the aggregate or total spending, allocating the aggregate among either existing agencies, commands, or strategic goal related activities. The contract between central and subordinate agencies relies on the total in which “a local government may impose a total spending ceiling of \$100 million for [a] fiscal year . . . , while a national government may restrict the total budget increase [for the] next year to, say, 7 percent” (Cothran, 2001, 156). Second, the central agencies and leaders delegate responsibility for spending the allocation to subordinate agencies, relying on expertise in subordinate agencies, as well as their desire to realize and retain savings, to provide the motive power to make devolution succeed. According to Cothran (2001, 157), “Government managers . . . might be given more discretion to move money around [among either line items or accounts] . . . [and] allowed to carry over a significant portion of a year-end surplus . . . to the new fiscal year in order to avoid the ‘waste’ of the surplus in a year-end spending spree.” Third, the contract between central agency decision makers and subordinate ones rests on trust and confidence, “greater evidence of program achievement, particularly efficiency” (Cothran, 2001, 157).

D. Model 4. Recalling once again the roots of reform in U. S. government budgeting leads to the present situation this research contemplates. Reformers during the 1900s proposed criteria for a good, modern, government budget. According to the last major review, National Advisory Council on State and Local Budgeting (1997), a budget should clearly define policy direction; translate taxes and revenues received into concrete levels of service; show consequences of increases or decreases in service and communicate this to stakeholders; facilitate control over expenditures; motivate and give feedback to employees; and evaluate employee and organization performance and make adjustments.

What the four models may be interpreted to mean is either a mixture of different reforms or muddle of piecemeal reforms titled with a vivid metaphor, performance budgeting. Given the history of reform movements in the United States at all levels of government, we may ask, how is this reform similar to the past? Larkey and Devereux (1999, 167) categorize past reforms in five different ways:

First there are the rationalizing reforms that emphasize enhanced analysis and reason. Second, there are ad hoc norms such as balance and annularity that have been evolving over the last 150 years or so in Western democracies and have been expressed in a variety of administrative reforms. Third, there are democratizing reforms that seek to open the decision processes to inform and involve citizens better. Fourth, there are power shifting reforms such as line-item vetoes that adjust authority and responsibility for budgeting, particularly between executives and legislatures. Fifth, there are control reforms such as auditing, tax limitations, and balanced budget amendments that attempt to impose external constraints on decisional behaviors.

E. Summary. These budget process reforms, with their emphasis on economic analysis of costs and benefits or marginal utility, especially Planning, Programming Budgeting System (PPBS) and zero-based budgeting (ZBB), belong to the rationalizing reforms category. The concepts of budget balance, comprehensiveness, and annularity belong to the ad hoc norm tradition. Freedom of information and sunshine laws are part of the democratizing movement, and the right to know and ability to penetrate fiscal illusion in this movement are values performance budgeting may share. The line-item veto is one of a number of reforms in the power shifting tradition, in which reform shifted some element of control among executives, legislators, and public managers. The fifth tradition, greater control, usually developed to address “the problems of fraud, waste, and abuse in the handling of public money . . . auditing the auditors who audit . . . the handling of public money . . . overseen by legislators looking for political advantage and a sporadically attentive public” (1999, 178). The reform tradition, therefore, includes changes to make budgeting more rational, professional, democratic, authoritative, and honest.

The performance-based reforms combine elements of all five movements. Additional elements include techniques related to planning, relative value comparisons, and productivity analysis. Ad hoc norms among performance-based reforms arise from what Larkey and Devereux call “decisional efficiency,” primarily the savings in time and effort that come with decentralization, and “feasible comparisons,” the stimulation of competition or cooperation, as appropriate, among agencies in solving particular problems. Democratizing reforms come from the wider scope of accountability problems the reforms try to tackle to yield greater stakeholder and citizen participation and involvement. Power-shifting reforms entail broad decentralization of power over budgets, implicit incentives to reallocate funds from lower to higher priority programs, and the retention of savings when improvements in efficiency provide them. Finally, performance-based reforms produce a reversal of the traditional reform emphasis on increasing input controls to provide greater output controls. Thus, performance-based reforms clearly signal a massive effort to reform government.

The present concern for results or performance nevertheless builds on the past while contributing much that is new. According to Cothran (2001, 158), later reforms built on earlier reforms, and the later ones

contain elements of the earlier reforms. They contain performance measures from performance budgeting, functional categories from program budgeting, negotiation of objectives from management by objectives, and ranking of objectives from zero-base budgeting. But there are some differences . . . [The latest reforms] are generally simpler, more streamlined, and require less paperwork and analysis. They involve more discretion by line managers than did the earlier reforms, and there is a much greater emphasis on accountability than under the older formats. Finally, the recent reforms are motivated by a desire to change fundamentally the culture of public management by turning bureaucrats into entrepreneurs. The present wave of budgetary reform aims to stimulate motivation [rather than simply legality, efficiency and effectiveness]. The new approaches [seek the old and the new;] they seek to achieve them through decentralized incentives that give program managers greater authority . . . but that hold [them] accountable for the results.

To put it more simply, leaders want results and control over spending totals. Results justify spending levels, but control over spending totals also permits control of the politics related to tax regimes. Leaders may be willing to trade micromanagement of work methods and program choices for control of the totals. Work methods and program choices leave lower level managers responsible for the results leaders know less about how to achieve. The decision: control the totals, surrender the details or delegate the choice about getting results with the totals.

IV. Model

The model we try to understand comes from this “trade the details for the totals” scheme based on three approaches: the spending target approach, the certification approach, and the incentives approach.

Because roots for aggregate control lie in target budgeting (TBB), that form of budgeting, one that may have come into being as early as 1929 in Berkeley, California, USA may work as precedent (Buck, 1929; Rubin, 1998, 57-59). We call this the spending target approach. In Cincinnati, Ohio, USA, the target approach gave the legislative body a significant role in allocating, initially, 10% of the revenue estimate for the coming fiscal year among competing proposals from departments for new programs. The approach forced reallocation of the remaining 90% among existing programs (Wenz & Nolan, 1982). Forced savings in Cincinnati led to innovation.

A management-oriented incentive system based on retained savings or even greater discretion lies at the other end of a continuum based on decentralization. The “retained-savings strategy, variations of which have been proposed by a number of persons would allow agencies to retain amounts saved from appropriations, rather than being required to return them to the general treasury. Proposals vary on whether any of the retained savings could be paid directly to employees or merely be retained and spent on other things the agency would like to do. In addition to recommending retained savings, [some have] recommended greater degrees of freedom from restrictive controls (that is, awarding lump-sum appropriations) to reward well-managed agencies. Their proposal deserves close attention, as it may be more politically feasible than the retained-savings strategy. In their important review of exemplary practices in the public sector, [the reviewers] recommend both administrative autonomy and monetary incentives to stimulate productivity” (Klay, 2001, 221-222). Savings, according to Klay, leads to efficiency and effectiveness.

The hinge lies in the measurement of performance, the trade made by central agency staff with subordinate bureau managers. The certification approach designed by Maricopa County, Arizona, USA, for example, required the Internal Audit [Department to perform] ongoing independent evaluations of departmental performance measure collection methods, accuracy, and reporting. Upon completing these evaluations, [the IAD assigns] certification ratings and report out conclusions (whether performance measures are relevant, timely, reliable, understandable, and verifiable). [Budget decision makers reading the performance information that accompanied budget requests might have greater confidence in the veracity of what they read] (Tate, 2003, 6-8). The certification approach leads to accountability, higher quality communication to stakeholders, and perhaps greater trust in government.

Perhaps the dynamic is some connection between performance levels and the decision about targets, as below:

TBB → performance measures (PM) → rewards based on measures

The system connects by linking all three:

TBB → funding based on level of service → measured by PM → linked to rewards and future budget targets

The latter concept’s funding-service connection may be implicit in many ideas, but the connection seldom gets the attention and technical explanation needed to understand how anyone connects the two.

Feit (2003) confirms the existence of such a dynamic at least in part. He summarizes the State of Minnesota’s transportation department transition to performance measures and its attempt to link performance management (PM) to funding. The department followed four key criteria for a PM system. Feit (p. 39) describes the requirements:

1. It must be clear from the start that the objective is to improve performance.
2. All top-level managers must give the implementation strong initial and constant support.
3. Funding must be tied to level of service by service type.
4. The reward system must be tied to performance results based on objective evidence.

In Minnesota the “objective was to measure, track and evaluate whether customer needs and public goals are being met throughout the state with the most efficient use of resources,” according to Feit (p. 40). Furthermore, the Minnesota transportation managers ask themselves, “Why we are doing this?” The answer came in the form of a list (Feit, p.40):

1. Provide information on which to base key investment decisions;
2. Enable customers and stakeholders to communicate with Mn/DOT about their choices and priorities;
3. Guide employees and partners in focusing on resources, time, energy, and creativity, on the most important work—the focus of our measures;
4. Use performance measures to identify and define gaps between customer/stakeholder expectations and actual Mn/DOT performance; and
5. Target process improvement areas for better product and service delivery.

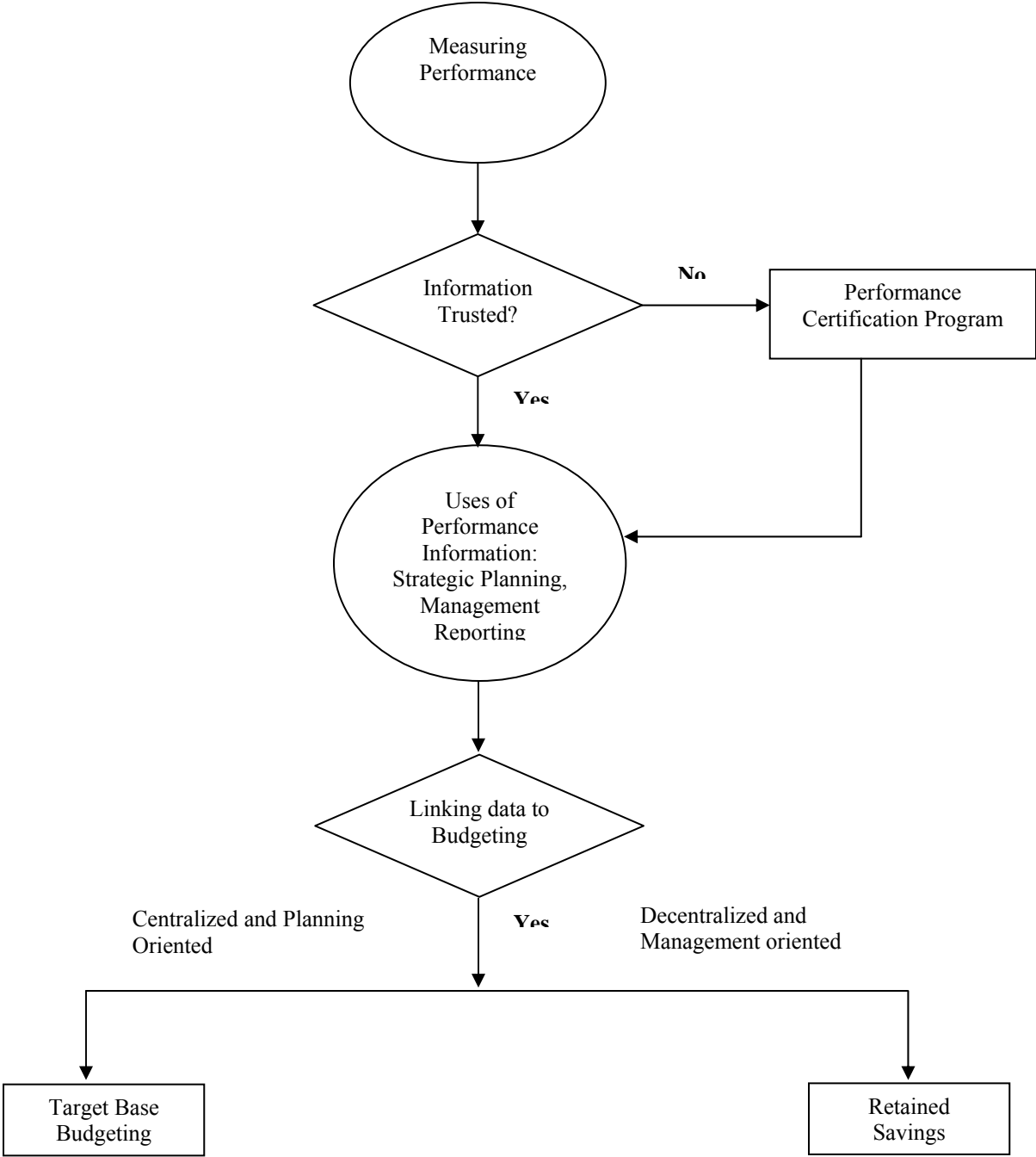
The result? Feit reported that the department managers found it difficult to get agreement on the measures. Therefore, the department hired a consultant who created “performance dashboards.” Simple and easy for everyone to understand, the 45 dashboards were red, amber, and green -- but also blue to represent “too much performance”— and 100 performance measures replaced the standard data tables. The dashboard display provided a comment section where the department managers explained the variances or why the department had not achieved the goals. The dashboard idea got top level management support and led to creation of a database.

The budget manages next tried to fund services based on the level of need. Need came from customers; therefore Mn/DOT managers conducted market research which “identified the following key customer segments: commuters; carriers, shippers, emergency vehicle operators, farmers, personal travelers, community and neighborhood groups” (Feit, 2003, 42). Market research revealed that customers had a long-range view as well as immediate needs. In the long view, customers valued “Improving heavily traveled routes between cities; providing funds for local governments; developing a long-range, 20-year, transportation plan; and [the lack of information] about safety related issues.” The near term issues and services of concern to customers were “plowing, sanding, and salting; maintaining roads and bridges; building roads and bridges; removing debris from roadways; posting signs; maintaining lighting, guard rails, and pavement striping; and communicating road and traffic conditions” (Feit, 2003, 43). Not rocket science but management, the market research gave a sense of focus to activities by forcing priorities among a laundry list of needs.

The dashboards underlie decisions on service levels. Service levels couple to funding. The entire set of connections, backward or forward looking as the case may be, are service levels → workload levels → staffing levels → support levels associated with staffing (materials, equipment, services, support staff, overhead) → rewards → budget funding. Despite these linkages in Minnesota, a last issue remained at the time of Feit’s 2003 article—linking the reward system to performance results based on objective evidence.

The conceptual links we draw and the Minnesota case reveals lead us to a general model. The diagram below (Figure 1) illustrates the interrelationships among four components of managing for results system: (1) performance measures, 2) the quality of data collected 3) multiple uses of performance information 4) balancing between centralized control over goals and decentralized incentives.

Figure 1
Performance Certification, Targets, and Savings



Performance based resource allocations must require the identification of performance measures and performance indicators. Generally, the following types of performance measures are suggested: input, workload, outputs, outcomes, efficiency, and effectiveness. However, these types of measures must be converted into indicators for the collection of data. It is desirable if performance data related to each indicator are collected on a regular basis.

Once performance measures are identified and data for these measures are collected, the focus moves to the quality control issue. It is important to note that performance information is worthy only if decision makers trust the quality of the data (Tate, 2003). Although program managers are principally responsible for the control over the quality of performance data, there is always a room in which data might be manipulated, exaggerated, or intentionally concealed. Thus, mechanisms are needed to assure the quality of performance data collected (Hatry, 1999, 216). In practice, however, this is often overlooked (Tate, 2003)

In addition to the issue of quality control over performance data, the use of performance measures is another critical issue. According to Schick (1990), performance measures may be more easily applied if the uses of performance measures are not limited to resource allocation but extended to internal management, strategic plans, and accountability. Indeed, these measures may be more valuable if they are used as a tool for evaluating the extent to how efficiently government operates, how fully the objectives of government programs and activities are achieved, and whether individuals in government are held accountable for the results of their work.

Finally, recent budgetary reforms, trying to link performance information to resource allocation, have employed two devices in order to make government accountable for results: “central control of goals” and “decentralization of means.” Policy makers in government want to control total expenditures, targets, and priorities for public services they provide. In order to succeed, policy makers demand that departmental objectives be listed and ranked as well as specific indicators developed to measure the achievement of such objectives. Once policy makers have made such decisions, they seek to attain those ends through decentralized means. The decentralized means intend to “stimulate motivation” by giving public managers “considerably more discretion over how they spend their money.” Such incentives include setting and transferring priorities among expenditure items within departments or transferring money “from operations to capital expenditures,” sharing or carrying over year-end surpluses, and even paying employees for the work with gain sharing. Cothran argues, “Centralization and decentralization can go together” (Cothran, 2001, pp. 156-158).

V. The Research Questions

Our major focus of in this research is to confirm the existence of our model further. More specifically, we ask four questions:

1. Do TBB, PM, and RS elements of the model exist?
2. What configuration of the three elements do managers believe allocates discretion most decisively?
3. What configuration do managers prefer to control aggregate spending?
4. What elements produce trust in government?

Investigating these questions involved a three-step process. First, two focus groups were convened. The first involved 28 seasoned public managers from the state of New Jersey who provided the insiders’ view to targets, performance reforms, and retained savings. The second focus group, comprised of 19 members, was asked to provide the outsiders’ view—the public—from the view of the manager on

the impact of these three approaches and their ability to improve trust in government. Next, we analyzed department responses to a survey administered by the state of Washington's Office of Financial Management on its retained savings program. Finally, using the information we gathered from the focus groups and the Washington survey, we created our own survey, the survey on local government financial management tools. The survey consisted of 24 questions focusing on target base budgeting, retained savings, and performance measures and certification.

The survey was distributed via email using an interactive form where respondents could simply check the appropriate box or type their responses. We developed a non-random sample of 54 US cities by consulting the literature or using the Google search tool to determine which cities promote performance, savings, and targets. Of the 54 cities, eight responded, a 15 percent response rate. In addition to the survey, we conducted two phone interviews to probe a bit deeper. Although the number of responses is low, the qualitative data collected through all three steps—the focus groups, the state survey, and local government survey—are quite robust. The findings are discussed next.

VI. Findings

Two focus groups, one investigating the insiders' view and the other the public's view, yielded interesting results. First the public manager focus group.

A. The initial focus group. In a focus group of 28 seasoned managers from state and local governments in New Jersey, we asked whether their organizations had a retained savings program. Specifically, we asked whether "retained savings already exists in [your] organization in various forms, from formally accounted-for reserves to information overestimates of spending." About 40% of the group did recognize that their organization pursued retained savings. Then, we asked whether the retained savings required certification informally or formally. Almost three-fourths of those with organization retained savings said budget authorities required proof, and almost two-thirds of the entire focus group said evidence should be required. Said one person, "The agency should be able to show how it delivered its program economically, thereby resulting in the savings." Another noted, "Retained savings does, indeed, depend on the ability of the agency to account for the incurred savings [and] occurs because the budgeting consists of . . . performance targets [including] indicators [that] are identified and analyzed."

When asked about the necessity of merit pay, individual sharing in these retained savings, the group turned negative. Of those having retained savings programs, only about one-eighth thought individual shares necessary to gain savings. In the focus group as a whole, one-fourth thought individual shares were required as an incentive. One individual noted, ". . . government retained savings should never be used to award monetary bonuses. Public administrators are evaluated on their ability to appropriately develop and spend what they have budgeted."

We probed the role of certified performance information in producing savings, asking whether high performing organizations, certified or not, were those that produced savings. Only two of the twenty-eight members of the group thought performance led inevitably to savings. In fact, one-half of the group thought the performance information "could actually provide the rationale for increased spending." One focus group member argued, "If data are accurate and all systems are working well, then there may be a 'comfort' level with allowing increased spending, . . . [but] there must be a level off openness and trust among the players with everyone's goal being the same."

The discussion in the group focused on where the three reforms, incentives, certification, and targets, would lead. In simple terms, we wanted to know what reform would allocate discretion in a

decisive way toward achieving control of aggregate spending or regaining public trust. Targets, the group said, give top decision makers more control. Moreover, targets hold the greatest power to control aggregate spending.

On regaining trust, the group chose among the three reforms again. By a large margin, the group thought the certified performance approach would work best. However, by an even larger margin, group members admitted that they did not know what would help regain the public's trust.

B. The second focus group. Next, we investigated the public's view via a second focus group. We assume that the public might know better what might instill trust. We assumed that the appeals administrators made to the public might have some more convincing basis if they were explained as the result of retained savings, certified performance, or targets and innovation.

Individuals convened in this focus group received instructions along the lines of the focus group questionnaire presented in Appendix 1. The focus group leader (Miller) instructed the nineteen members to think of budget reforms primarily as efforts to promote management for results as well as the traditional efficiency goal, through both innovation and actual savings. The leader recognized the members, in the introduction, as concerned taxpayers and citizens. The task given the group was to decide what reform or combination of them would lend belief or suspension of disbelief to stories managers told them about savings and innovation, usually as the basis for budget testimony in support of claims for spending increases. The focus group's choice? A note taker provided the following record (and brackets indicate the copyediting of the notes for greater readability):

[The focus group members, according to the note taker,] answered the questions more from the perspective of a manager than a taxpayer.

On target budgeting, will the taxpayers still get the service they need? [The target approach] fosters competition among departments, . . . a negative, [but this] approach forces them to save. [The group members] seem in general turned off by having the political influence [the target approach allows]. [The target approach, group members defined] as punishment.

On audit and certification of performance measures, there was a certain amount of risk aversion among the students and they were attracted to this approach. In reality there can only be a limited amount of creativity involved with budgeting (the garbage still needs to get picked up) and some thought this structure was a good thing. [One group member noted that] in reality our governments are not getting reinvented so why pretend they will be?

Accountability is related to trust, [and] certification gives some type of blueprint [for what working and why]. The differences between public and private organizations were noted—government doesn't make a profit, and largely government doesn't have competition. [So, certification and audit of performance measures forces the scrutiny that's need:] you get to look at every penny.

On the incentives including retained savings, [this incentive] may not serve the interests of the public. [While tying] compensation and performance allows people to take ownership, [more members of the group preferred] reinvesting the money in programs and [rather than handing them] out as bonuses. Bonuses don't always motivate.

There was the concern that if [a claimant's spending would] go under budget, the budget will just be cut the next year. On the other hand, [the incentive] gives you something to work towards. [However, savings] can't go on forever; at some point you've trimmed all the fat. [Two of the biggest questions:] What about the roles of unions? [What about the chance that retained savings would lead to an inevitable choice --] that pet projects would be funded.

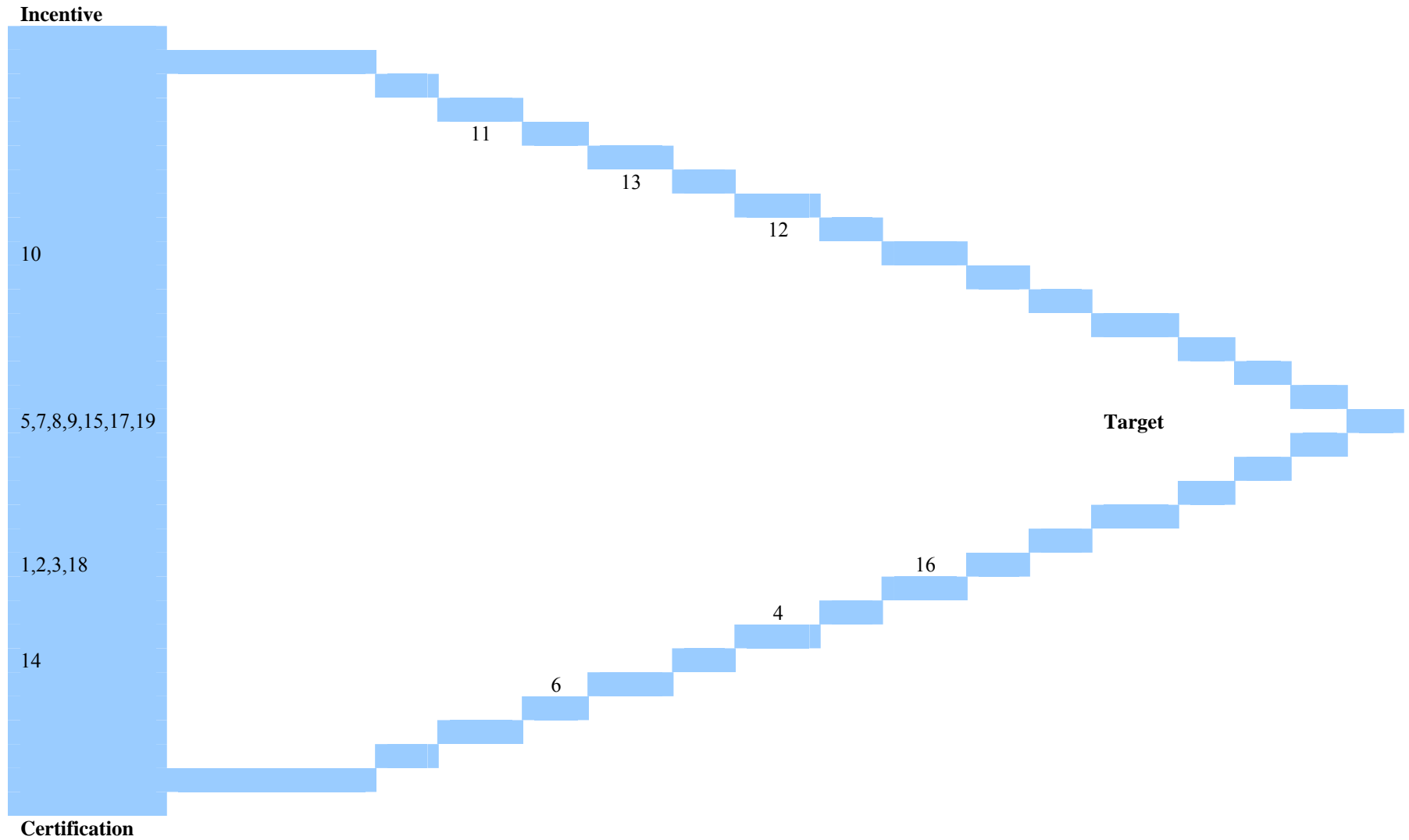
The audit approach and then incentive [might be a workable combination, members said,] “Let me see what you are doing and then... (maybe we’ll give you more money).” [Moreover,] the idea of transferring between funds within an organization had broad support. Some amount of flexibility is good. People liked benchmarks; if benchmarks are met then maybe audit. A very sound argument was made for not just using any one approach.

As a final bit of feedback, we asked the members of the group where their position as individual-taxpayer-and-citizen might be located in a spatial relationship among incentives, certification, and targets. We instructed the individuals to draw a triangle and place each of the reforms in one corner. We explained that a choice of combination that included all three reforms might be in the exact center of the triangle. In Figure 2, the combined evaluation of the reforms appears.

Figure 2 Trust and Results in Government

Note: Question given to focus group members, “As a citizen and taxpayer, which reform would make you trust government more? Which combination of reforms would make you trust government even more?”

Taxpayer-citizen group (N = 19) October 20, 2004 Focus group comments (numbers indicate focus group member)



C. The Washington state government case. The state of Washington, an exemplar of an intelligent approach to budgeting in a time of distrust of government and tax revolts (Osborne and Hutchinson, 2004), provides us with evidence on retained savings. Their conceptual overview of budgeting included four provisions. The first was an analysis of revenue levels of a group of similar governments, city, county, school, or state. Taxpayer analysis followed, and budgeters tried to find the level at which taxpayer resistance might occur within the comparative analysis. The second provision required the budget managers to determine what goods and services citizens wanted and at what level of intensity. The service priorities, third, got funding down to the level of taxpayer resistance. Finally, Osborne and Hutchinson described methods of purchasing and contracting to gain the most efficient services at the “price citizens are willing to pay” (p. 13).

We looked at the state Office of Financial Management’s “Report of Fiscal Year 2005 Savings Incentive Account Expenditures.” This study reported a survey of department participants in the state’s savings program. The survey responses supplement our other work to gain a deeper understanding of the retained savings incentive idea as applied in the state of Washington (State of Washington, 2005).

The Washington retained savings plan grew from Gov. Locke’s “initiative to promote efficiency in agency spending and to help support public schools,” an initiative beginning in 1997. In that plan, “Agencies are credited with one half of all state general fund state (GF-S) savings not related to entitlement or other targeted spending authority.” The savings that remain after the credit “are directed to the Education Savings Account, 10 percent of which is transferred to Higher Education for distinguished professorships, the graduate fellowship trust fund, and the college faculty award trust fund.” The remaining Education Savings Account transfer “may be appropriated for common school construction and educational technology.” The legislature could not further re-appropriate the credits in a future fiscal year. The savings over the seven years following the plan were \$34.4 million, and by FY2005, “agencies had used \$21.1 million of the \$34.3 million.” The ground rules for the plan called for the funds to be used for “one-time activities that improve the quality, efficiency, and effectiveness of customer service in agencies [and not] to create new or expanded services or to incur ongoing obligations.”

Their findings suggest that the incentive effects were imperceptible. According to the report, “Most agencies indicated that the existence of the [plan] had no direct effect on end-of-fiscal-year spending patterns, although it was recognized as a useful management tool” (p. 4). Of the 62 agencies surveyed, 48 (77 percent) said the plan had no effect and 14 (23 percent) said that the plan did have an effect (pp. 20-25).

Of those who said yes, the claims varied. For example, the Columbia River Gorge Commission respondents reported, “Throughout the year, we have managed our spending with the savings incentive fund in mind. We have slowly built a ‘bank’ of savings that we intend to use for training, technology improvements, and work process improvements that have not been funded in our agency budget. The bank is a result of the ongoing efforts of staff to implement cost-saving measures” (p. 20).

The Washington Department of Ecology reported, “Our focus was on carrying out the purpose and objectives of the funded programs, rather than on saving money. But as the end of the biennium was nearing, we had the ability in some activities to spend federal funds, dedicated funds, or [plan funds]. Although the potential for rebates did not cause a reduction in activity, nor did it cause a net savings, it did give us an incentive in some cases to spend federal or dedicated funds rather than [savings credited to the Department]” (p.21).

The Military Department commented that the savings reinforced strategic plan provisions. The survey response stated, “The ability to make one-time quality improvements and/or provide incentives to staff with . . . savings is very beneficial to a small agency like the military department. The opportunity to carry the unspent savings account forward for multiple years gives us a chance to have sufficient dollars to take on a significant one-time expense that promotes the key part of our strategic plan” (p. 23).

Emergencies prompted some uses in small agencies such as the Public Disclosure Commission (PDC).

The Commission reported that, having “very limited fiscal flexibility, [savings] rebates are critical to the agency’s ability to manage unanticipated expenses. Having a Savings Incentive Account means the PDC has the wherewithal to fund prudent technology improvements, replace failed equipment, and pay for performance-related employee training beyond the modest amount allotted in the operating budget. . . . PDC staff intentionally left nearly \$40,000 unspent in fiscal year 2005 in order that the rebate would be available for additional technology services in fiscal year 2006, if necessary” (pp. 23-24).

Despite the Public Disclosure Commission’s admission of altered spending patterns, the report found little widespread alteration. The report found, “Actual fiscal year GF-S expenditures (by month) for the nine years of the program’s existence do not demonstrate any expenditure patterns that can be solely attributed to the Savings Incentive Program” (p. 4).

The Washington practice on retained savings found greater impacts among small agencies. The findings also suggest a gain in financial flexibility leading perhaps to greater risk-taking and innovation.

D. A survey of U. S. city budget officials. Finally, our survey and instrumented interviews of city finance officials, usually budget officers followed. The eight cities varied in size from Los Angeles to Sandy, Oregon. The group represented the three major governing structures found in the United States. Table 1 presents the descriptions of the responding cities.

TABLE 1
City Descriptions, Instrumented Interviews on Retained Savings, Performance Measures, and Targets in Budgeting for Selected U. S. Cities

City (Reputation)	Form of Government	Net Assets	Current Year Revenue	Number of Departments	Number of Employees	Population
Austin, Texas (CITISTAT)	Council-Manager	\$3.8 billion	\$2.0 billion	26	11,380	672,001
Boise, Idaho (RS)	Mayor-Council	\$892 million	\$300 million	12	1,515	190,117
Dixon, California (ECB)	Council-Manager	\$158 million	\$33.6 million	10	92	20,100
Lake Forest, Illinois (TBB)	Council-Manager	\$232 million	\$54 million	10	214	20,057
Los Angeles, California (RS)	Strong Mayor-Council (a)	\$1.9 billion	\$5.95 billion	39	38,500	3,819,915
Salina, Kansas (TBB)	Council-Manager	\$101 million	\$60.0 million	13	502	45,833
Sandy, Oregon (RS)	Council-Manager	\$20.8 million	\$13.0 million	7	48	5,385
Urbandale, Iowa (CDGP)	Weak Mayor-Council (b)	\$85 million	\$28.5 million	15	250	31,868

Notes:

All cities have full-service governments.

- a. Mayor is elected chief executive and department heads report to the mayor, and mayor proposes budget.
- b. City manager by ordinance.

CDGP: Citizen driven government performance

CITISTAT: Acronym for management systems using strategic planning, results measurement, and intense, weekly monitoring of agency performance

ECB: Expenditure control budgeting

RS: Retained savings

TBB: Target base budgeting

The interviews showed us that no city in our group uses all three budget reforms as a single formal system. From this set of interviews, we can conclude that the elements of the model exist but not in the tandem way we portray. Two cities rely on both retained savings and targets, Boise, Idaho and Sandy, Oregon. Formal reliance on performance measures, certified or not, does exist, but seems to be the option when neither retained savings nor targets are used.

As Table 2 portrays, where there is TBB, there are PM but often not. No one would say for certain that PM are linked directly to allocations. The weak, if existing, linkage may explain why TBB exists to begin with. PM may seem to legitimate the TBB process perhaps. Budgeters could use the PM as a way to reduce the targets—observing that departments do not live up to potential; department heads could use PM to advocate for more money. In the end, it does not matter, the target will prevail. Also, there seems to be a list of exemptions from the target.

However, as the size of government grows, TBB fits less well. For example, if personnel costs take up 70 percent of the budget and most of this is mandated from collective bargaining -- unions, contracts, the proportion of healthcare and pension costs -- there is little room for TBB to make a difference. If they use TBB, the cities seem less likely to use RS, although we have to be careful not to make leaping associations with such a small number in our group. Sandy, Oregon is the exception here. That city uses TBB to set the proportion of the budget but does not designate additional amounts. Perhaps, this light touch with targets explains why the city uses RS: any additional funding will have to depend on the department's ability to save.

The City of Austin provides a generalizable treatment of savings. According to the city's respondent, "What happens to year-end savings depends on whether or not the department [operates as an] enterprise fund [or is part of the general fund]. Savings for enterprise funds, such as aviation, convention center, water and electric utilities, drainage, and solid waste services, drop into their funds' ending balances. [The fund balances] can be re-appropriated the next year [based on proposals from the enterprise]. Some of these enterprise funds also distribute part of the savings to their departmental employees as end of year bonuses. Sometimes, prior year savings in enterprise funds can offset the need for future increases in service fees. For the general fund, savings [follow fund balance policies below]. In FY 2006, all city employees received a one-time two percent bonus with [surplus] funding, but this [did not relate to] departmental savings within the general fund."

The Austin general fund savings policy comes in two provisions. The first provision states that "unreserved fund balances in excess of required amount shall normally be used to fund capital items in the operating and capital budget. However, if projected revenue in future years is not sufficient to support projected requirements, an unreserved ending balance may be budgeted to achieve structural balance." The structural balance might be a transfer to cover an account that has grown beyond normally forecast general revenue allocations to cover.

The default provision, covering all instances, whether capital and structural imbalance needs exist or not, is the permanent fund balance. Austin's policy states that ". . . at the end of each fiscal year, any excess revenue received in that year and any unspent appropriations at the end of that year will be deposited into the budget stabilization reserve. The reserve may be appropriated to fund capital or other one-time costs, but such appropriation will not normally exceed one-third of the total amount of the reserve, with the other two-thirds reserved for budget stabilization in future years." The Austin policy reflects a consensus among all but two cities in the group we interviewed.

TABLE 2
Results Instrumented Interviews on Retained Savings, Performance Measures and Target-Base Budgeting for Selected US Cities

City	Use Retained Savings	Use Performance Measures	Use Target-Base-Budget
<i>Austin, Texas</i>	Depends on the department and its fund location. Used for bonuses, one time expenses	Always. Sometimes used to assess savings; sometimes measures are audited. But allocations seem to be less dependent on measures.	Never.
<i>Boise, Idaho</i>	Yes. Savings is divided: portions go back to the general fund, bonuses for all city employees, and/or department keeps a portion. Combination depends on overall financial position of the general fund.	Sometimes, but never used to assess savings and never audited. Not tied to allocations.	Sometimes the council sets aside a designated dollar amount but departments are never tied to a proportion of the budget. The target is determined by program type, revenue elasticity, and department performance. Exempt items include collectively bargained amounts and mandated expenditures.
<i>Lake Forest, Illinois</i>	No. Savings that does occur is lost and goes to either a rainy day fund or the general fund.	Never.	Always. Council designates amounts and departments receive a proportion of total budget. Target is determined by last year's budget and judgment on amount needed for exempt items. Exempt items include fixed costs, grant funded expenditures, and mandated expenditures.
<i>Los Angeles, California</i>	No. In the general fund, saving that does occur is lost and goes to either a rainy day fund or unrestricted fund balance. However, most are transferred to departments with shortfalls. Departments with savings during the year in other funds, particularly capital projects, can request to spend those monies during the following year.	Sometimes used; although the new mayor plans to focus more on measures. Currently, they are sometimes used to assess savings and are sometimes audited. Allocations seem to be less dependent on measures. Workload measures are used for staffing purposes.	Always. Council designates amounts but departments never receive a proportion of total budget. Target is determined by last year's budget, judgment about amount needed to cover all amounts not connected to grants. Performance is also a factor, but specifically for fee supported departments. Exempt items include collectively bargained amounts, mandated expenditures, and off budget grants.

<i>Salina, Kansas</i>	No. Savings that does occur is lost and goes to the general fund.	Never.	Sometimes the council sets aside a designated dollar amount but departments are never tied to a proportion of the budget. The target is determined by last year's budget and the judgment about the amount needed to cover all amounts but mandated expenditures.
<i>Sandy, Oregon</i>	Yes. Whole amount goes back to the department for out year, one-time expenditures.	Sometimes. City never requires an audit of measures, but sometimes used them to assess savings. Allocations seem less dependent on performance.	Always used a targeted proportion of the total budget but council never sets aside a designated amount. The target depends on last year's budget, judgment on amount needed to cover exempt items such as fixed costs, unions, grants, mandated expenditures, and inflation.
<i>Urbandale, Iowa</i>	No. Savings is lost and goes to the general fund. The whole amount may go to the department for out year special purchases as long as the agency does not suffer a reduction in service and the savings must not be due to the deferral of legitimate expenditure obligations.	Always requires departments to use performance measures, used to assess savings, and are sometimes audited. Department performance is always linked to next year's allocations. Increased (Decreased) performance does not imply an automatic increase (decrease) in next year's allocations.	Never.
<i>Dixon, California</i>	Calls budget and Expenditure Control Budget with lump sum allocations. Transfers allowed among line-items (e.g. salaries and others) within fiscal year	Never.	Informal use of targets, always basing a department allocation on a previous proportion of the budget but only sometimes allowing the council to set aside a designated dollar amount to appropriate for new programs.

VII. Discussion

Our original research question asked whether the incentive-certification-target system appeared in states and localities in the United States. We asked, "Could we find a convergence among budget reform trajectories?" (Pollitt and Bouckaert, 2000, 64-71). We did not find a convergence. Instead, we found five different models. For example, the Los Angeles, Lake Forest, Illinois and Salina, Kansas budget systems used targets with no carryover or what might be called savings-centered budgeting. In Boise, Idaho and Dixon, California, the budget systems have both ceilings and allow carryovers, a form called "block budgeting" (Pollitt and Bouckaert, 2000, 65). In Sandy, Oregon, the city manager designed a block budgeting system and employs performance measure benchmarking to discipline department budgets, a system Joyce calls "performance-informed" budgeting (2003, 14-17). Fourth, Austin, Texas always employs performance measurement and allows some retained savings even allowing bonuses for employees but no targets. Finally, the Urbandale, Iowa budget system places performance measurement at its center, employs no targets, and allows no retained savings.

In no case, however, did we find the fully developed system our original reading of reform behavior led us to think possible, one linking targets, performance measurement, and retained savings. We expected to find

a locality in which targets represented performance measured in money. Instead we found a major divide in classifying budget systems. On one side we found those aimed toward savings in different ways. On the other side of the divide, we found performance management systems that seemed to drive budgeting, those budget systems in Austin, Texas and Urbandale, Iowa.

Among the savings oriented budget systems, we found savings as savings programs – line-item budget ceilings -- or savings related to both decentralized decision making about the employment of funds and narrow and well-defined targets. Savings, then, had two meanings. In an incentives sense, savings means motivation to reallocate. Reallocation in mild forms takes place in our eight locality group and in the State of Washington. These savings, however, are budget process reforms in which loosening financial controls leads to strategic use of savings and strengthened administrator discretion. The agencies often reported using organization savings as a strategic organization and management aid in the use of funds to keep key employees and to fund capital projects. Little evidence exists that agencies use savings as an incentive to build slack into their management systems or to pay bonuses to employees. In the latter case, in fact, we found resistance among managers; “Doing one’s job” is not a reason for paying a bonus,” one focus group member argued.

In the narrower sense of savings as a protection of the tax rate, we found wide use of top-down targets. In no case did we find top-down targets used in conjunction with certification of performance. We wondered why because targets without performance have little use in managing performance. The most common meaning of budget targets, in fact, refers to contracts for performance in which some effort is made to develop a cost for a preferred level of goods and services agencies will provide. The budget becomes the contract, and budgeting includes considerable effort to monitor performance in reaching targets (Scheps, 2000).

Our conclusion lies in the attitude toward integrating budgeting and management. A checks and balances system may allow budget decisions to check and balance management decisions, and top managers allow the two systems to exist side by side. A management system may integrate budgeting as the system of employing and allocating resources with other resource systems such as personnel and technology. This second, line-staff model of performance budgeting requires strong, top-down management, and a top manager who prefers the traditional advisory model of staff. A third or board-of-directors model may allow a stronger role for budgets, one we called the “protection of the tax rate” model above.

Only in the line-staff model of management and budget do we find a meaningful role for management information in budgets. That is, the new “targets” or performance contracts have more management than financial content – risk sharing, relationship building, feedback, progressive pressure, trust, and goodwill. The line-staff model assumes stable resources, a strategic approach to resource employment, and a smaller role for budget actors in conserving resources, perhaps reducing tax rates, and finding allies among competitors for budget shares. All of these system characteristics have found a place in comparative budget systems models (Straussman, 1979).

Decentralization of means and centralization of control over the totals in budgets has occurred in important but still minor ways. Guarding against the “take the money and run” behavior of agencies receiving devolved functions can be the general case of budget office behavior. Investment in performance management systems is the vanguard, rather than the commonplace.

Commonplace budgeting has a savings focus and has developed in some places as a complement rather than competitor in management decision making. Targets, probably loose ones, often yield savings or fund balances. Financial policies and organization strategy guide the use of these fund balances. The general fund, because its size is a function of the tax rate, gets the most severe scrutiny and control. Enterprise and capital funds management gain flexibility in comparison to the general fund. The flexibility comes with both less scrutiny and a tighter connection among revenues, spending, and management.

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