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## The Slovakia Spending Review Project

David Coady and Ignatius de Bidegain

Technical Report | October 2020



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# **Slovak Republic**

## **The Slovak Spending Review Project: Achievements and Challenges**

David Coady and Ignatius de Bidegain



**Technical Report**

**October 2020**

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# CONTENTS

|  |           |
|--|-----------|
| <b>I. BACKGROUND</b>                                 | <b>5</b>  |
| A. Objectives  | 5         |
| B. Project Design                                    | 5         |
| C. Management and Administration                     | 6         |
| <b>II. EVALUATION OF THE SPENDING REVIEW PROJECT</b> | <b>7</b>  |
| A. Establishing the Framework                        | 7         |
| B. Developing Policy Options                         | 8         |
| C. Making Decisions                                  | 9         |
| D. Implementation                                    | 10        |
| <b>III. RECOMMENDATIONS</b>                          | <b>11</b> |
| <b>FIGURE</b>  |           |
| 1. An Institutional Structure for Effective SRs      | 12        |
| <b>TABLE</b>   |           |
| 1. Diagnosis of PFM Support for the SR Process       | 13        |

# I. BACKGROUND

## A. Objectives

- 1. The Spending Review Project (SRP) began in 2015 and matured over four years with support from the EU and the IMF.** Following a request from the Ministry of Finance (MOF), the Fiscal Affairs Department of the IMF provided a series of technical assistance (TA) workshops to support the government's goal to establish a spending review framework and conduct a comprehensive spending review. The technical assistance was financed by the European Union's structural funds and EC/DG Reform.
- 2. The SRP was anchored in the twin objectives of restoring fiscal sustainability and enhancing spending efficiency.** Fiscal consolidation was an important driver, as the government had set a target to return general government finances to balance by 2020 and saw the SRP as an instrument to achieve this objective. This would be supported by a search for greater technical efficiency through measures designed to increase the "value for money" from existing spending allocations. Furthermore, the reviews were also expected to improve allocative efficiency, seeking to reprioritize spending within and between ministries towards projects that would provide better value for money.
- 3. Developing the institutional architecture required to conduct successful spending reviews (SRs) was also a key part of the SRP.** In addition to developing experience in the management of SRs, the project would have to build the infrastructure needed to conduct the SRs. This required strengthening analytical capacity both in the MOF and in the sectors earmarked for SRs, and it would also require building the institutional mechanisms that would frame and sustain the spending review process.

## B. Project Design

- 4. The chosen form for the SRP was a series of rolling sectoral or thematic spending reviews, where each iteration would incorporate the lessons from previous waves.** This allowed for a staggered approach where the institutional framework required to guide successful SRs could be built incrementally and consolidated with each wave. The first stage (in Autumn 2015) was a set of pilot reviews in schools, employment offices and tax offices.
- 5. After the early pilots, the first full wave of sectoral SRs was launched in April 2016.** These SRs were designed so they would conclude in time to inform the 2017 Budget. The sectors identified for this first round of reviews were health, transport and IT, all of which were key to the government's early plans to increase public sector efficiency. The plan envisaged that each round of SRs would cover roughly one quarter of public expenditure, so that most of public spending would be covered over the course of a four-year Parliament.

## C. Management and Administration

### 6. Three types of key teams were either created or developed as the SRP progressed.

- i. The Value for Money (VFM) Unit sits in the MOF and leads on analysis and evaluation, in collaboration with counterparts in the Line Ministries selected for review.
- ii. Analytical Teams in Line Ministries were revamped to strengthen their capacity to scrutinize the value for money and efficiency of spending in their respective ministries.
- iii. The Implementation Unit was initially created in the Deputy Prime Minister's Office and was then moved to the Prime Minister's Office. Its role is to spearhead the drive to identify implementable measures, generate political support for the reviews, and keep the momentum on implementation.

### 7. New developments in tracking and transparency were fundamental to ensuring public visibility, maintaining momentum and coordinating cross-government work on the SRP. A dedicated section of the MOF's website became the repository of a series of key documentation underpinning the SRs:

- i. Terms of Reference. Each sectoral review starts with the publication of a concise set of agreed objectives as well as some broad expenditure trends and an overview of the size of different types of spending to provide context for the review.
- ii. SR Reports. As each SR matures, an Interim Report is published setting out expenditure trends and preliminary analysis to identify areas with the greatest potential for efficiency improvement and highlighting important issues which require deeper insights. Once the SR is concluded, a Final Report is published setting out the measures to generate savings and reprioritize expenditure, as well as the analysis that led to those conclusions. The Final Reports also offer a plan for implementation which lists the measures and a timeline for their financial impact.
- iii. Implementation Reports are then published by the Implementation Unit to track and evaluate progress on the full list of measures. This shows the government where extra political initiative may be needed to keep momentum on ongoing reforms.

These initiatives helped cultivate political and public support for the SRP and avoid reform fatigue.

## II. EVALUATION OF THE SPENDING REVIEW PROJECT

**8. The success of a spending review depends on careful execution in four distinct stages.** These stages are: establishing the framework, developing policy options, decision-making, and implementation. For each one of them, the Slovak SRP has had both achievements and challenges which are described below.

### A. Establishing the Framework

#### Achievements

**9. A judicious selection strategy for initial activities allowed for a pragmatic start in a controlled environment.** The Autumn 2015 pilot reviewed schools, tax offices and the administration of active labor market policies in employment offices, thus focusing on small operational units which were easy to study and could provide early scalable measures to improve efficiency. By setting a realistic level of ambition for the first steps, the government was able to gain some quick insights and build some early capacity ahead of the first major sectoral reviews.

**10. The analytical and monitoring architecture were greatly enhanced** by the creation and development of new teams (paragraph 6) and the new published documentation (paragraph 7). This gave the government the tools it needed to determine the scope of the reviews and thus ensure that the SRs addressed some key policy priorities for the government.

**11. Senior political buy-in was greatly improved as the SRP progressed.** This commitment culminated in the reform of the Budget Law after three rounds of spending reviews in 2019, which institutionalized the 4-year cycle of rolling spending reviews and committed future governments to continue the process. Sufficiently strong political buy-in has provided the stability needed for many of the SRs to confidently explore long-term VFM structural changes.

#### Challenges

**12. Senior ministerial buy-in did not often extend beyond broad high-level support.** Though there was broad support for the launching of the SRP, and for the general goal of increasing efficiency, this was not always translated into actionable political goals for ministers in charge of spending ministries. A well-designed steering committee should bring together the Minister of Finance and relevant Line Ministers to provide strategic guidance, resolve disputes and approve final proposals and reports, thus fostering collective ownership of the contributions that each ministry should make to advance the common SR agenda (paragraph 30).

**13. The Terms of Reference (ToRs) could be strengthened to sharpen the focus of the reviews.** The broad TORs allowed an unconstrained search for opportunities to reduce and reallocate spending. Whilst this enhanced the creativity of the process, the TORs did not typically provide specific saving targets or quantitative anchors to guide the outcomes of each SR, which had

an impact later on in the process (paragraph 20). This may be easier to achieve with improved ownership from the relevant Ministers.

## **B. Developing Policy Options**

### **Achievements**

**14. Important improvements in the information available to the Ministry of Finance (MOF) and the center of government.** The SRs improved access from the center (the MOF and the Prime Minister's Office) to better information traditionally disseminated across Line Ministries. For example, data on salaries, vacancies and headcounts were collected from key Line Ministries to offer a comprehensive assessment of relative workforce pressures across all of government. Up to this point, the MOF did not have a strong basis to monitor the very significant spending allocations for departmental wage bills. The Social Exclusion SR brought together multiple sources of administrative data from education, social policy and other areas, and built an integrated government view of key multi-dimensional drivers of social exclusion and potential social policy reforms that are difficult to address if each ministry acts separately. In addition to the internal analytical work, external experts were brought in to advise and offer new insights from other countries and give the center an independent and fresh look at each of the sectors.

**15. Benchmarking used to provide better context on efficiency.** Once data were collected and analyzed, the SRs made use of international comparators to help draw conclusions. For instance, international comparisons showed comparative scarcity or surplus of different types of public sector workers and comparing SOEs to Czech analogues informed the government's view on the efficiency of spending by these institutions. Benchmarking also helped to identify efficient employment offices and distill best practices to improve the performance of less efficient offices.

**16. Innovative analysis has added depth to the traditional budgeting and spending control functions.** The SRs focus both on technical and allocative efficiency and find a broad range of measures based on new analytical techniques and new data sources. For example, the Wage Bill SR makes use of regressions to estimate the public sector pay premium and conducts a demographic analysis of the workforce and of the general population to identify structural workforce issues. Outcome indicators and input-output analysis are used in both the Health and Education SRs to compare Slovakia to peer countries.

### **Challenges**

**17. Working-level engagement from different ministries with the SRs was very variable.** The low degree of ownership from ministers leading some of the sectors under review led to an over-reliance of the SRP on the initiative of the VFM Team and the Implementation Unit, who found that their commitment to the sectoral reviews was sometimes greater than that of their counterparts in the Line Ministries under review. This affects the ability of the SRs to generate reform proposals that are aligned with the priorities of the minister in charge of implementing them.



**18. Recommendations from the SRs are mostly built on purely analytical findings.** The potential savings and value for money measures recommended in the SR reports emerge from a copious body of analytical work, but the reviews did not typically explore potential institutional and operational obstacles to implementation, and how surmountable they are. These should be key considerations when building a realistic set of policy options, but their inclusion in the process relies on strong engagement from the ministry under review.

## C. Making Decisions

### Achievements

**19. The SR reports are a big step forward for evidence-based policy making.** The Reports offer a substantial volume of evidence underpinning their recommendations. They are a valuable source of insights to help ministers understand their portfolios better and more strategically. Additionally, the case for reform is presented in a clear and accessible manner and made available for public scrutiny; this helps ground the public debate on policy decisions in solid evidence.

### Challenges

**20. Lack of political ownership from ministers in spending ministries weakens the potential impact of SRs on decision-making.** The risk of broad TORs (paragraph 13) without fiscal targets or guiding political objectives is that the relevant minister may see the proposed measures as emerging from a narrow analytical perspective, as technocratic solutions in search of a problem that is not on their policy agenda. Furthermore, new policy discussions may arise outside the boundaries of the SR with unintended financial consequences. This was the case with the new bill on drugs; during its later stages in parliament it was unexpectedly amended to greatly expand access to certain drugs, committing additional health expenditures in a way that was not anchored in the abundant analytical work on the value for money of different types of health expenditure. In general, throughout the SRP, ministers have had few incentives to undertake long-term structural reforms with short-term political cost and gains in efficiency that only materialize in the medium to long term.

**21. Cross-cutting SRs make it difficult for all actors to align to make joint decisions.** Some of the SRs are not contained within a single ministry, and instead straddle various accountability and delivery structures. For example, the cross-cutting wage bill review found that teachers were underpaid but that wage-bill savings could be achieved across government by reducing excess administrative staff and reducing the size of the police force. The SR led to a pay rise for teachers, but other ministries did not implement workforce reductions to generate fiscal savings that would fund the teacher pay rise.

**22. The SR process as currently designed does not force clear within-sector budget trade-offs.** As a result, most ministers have had few incentives to squeeze savings from existing programs and the only sectoral SR to produce net fiscal savings has been the Health SR. However, even in this case, savings fell short of the objective set out in both stages of the Health review. Under the

Education review, savings initiatives have remained largely unimplemented, though they could have helped to fund part of the pay rise for teachers. Setting a clear Education budget baseline (including the wage-bill) as the target for the Education SR could have helped highlight expenditure trade-offs.

## D. Implementation

### Achievements

**23. The Institutional architecture needed to track and evaluate implementation has been consolidated.** The Implementation Unit has established itself as a high-profile team at the heart of government, and the regular publication of its Implementation Reports every six months is valuable in two senses. Firstly, it holds Line Ministers accountable by rating progress on the reforms of each sector. Secondly, it empowers the center to focus additional efforts in reform areas which show a risk of losing momentum. The regularity of the publication ensures ongoing follow-up at the most senior levels.

**24. Practical recommendations from the SRP have been adopted by the Government's program for 2020–2024.** The process is robust in its diagnosis, justification, proposal and tracking of identified measures, and this has helped build support for important measures over time. The published list of policy commitments reflects practical recommendations from the SRs such as the need to train more medical assistants, or to take a more proactive role in managing the numbers of medical specialists being trained to meet current shortages and projected needs.

**25. The SRP has also shown an ability to address difficult systemic changes where institutional obstacles blunted practical success.** The Health SR successfully argued that volatile funding from Health Insurance revenues and the lack of credible medium-term budgets were an obstacle to the most important strategic VFM reforms identified in the SRs, such as a rebalancing between primary and specialist care. The Government's 2020-2024 program now commits to introducing predictable long-term funding for Health through centrally allocated budgets.

### Challenges

**26. Some targets were too ambitious to guide practical implementation.** The best way to drive successful reform is through ambitious but attainable overall targets, with realistic milestones along the way. The most prominent tangible objective at the launch of the Health SR was to "reduce avoidable mortality to the average of peer countries by the end of the parliamentary term". However, after factoring in the time to conduct the review, implement the savings measures, and restructure and reform health spending to improve outcomes, there is very little time left for the positive effects to materialize and thus achieve this objective. Implementation can often be guided more effectively by targeting intermediate outcomes that are needed to generate these longer-term gains, e.g., improvements in the average duration of patient waiting times and hospital stays, or the number of doctors and nurses per 1,000 inhabitants.

**27. Even when savings materialized, they were not reinvested in priority “Value for Money” measures identified by the reviews.** Stage I of the Health review identified savings measures in procurement which resulted in substantial savings. However, these savings were not redirected towards VFM reforms as the SR had envisaged. Instead, they were used tactically to make up for budget shortfalls and countered by falls in efficiency elsewhere (e.g. across-the-board spending increases in hospitals attributed to poor management and insufficient cost control).

**28. The Budget Department is not sufficiently integrated in the SR process.** This puts operational pressure on the Implementation Unit, which detracts from its core role. It also undermines implementation, as ongoing spending allocations do not necessarily align with the proposals from the Spending Reviews.

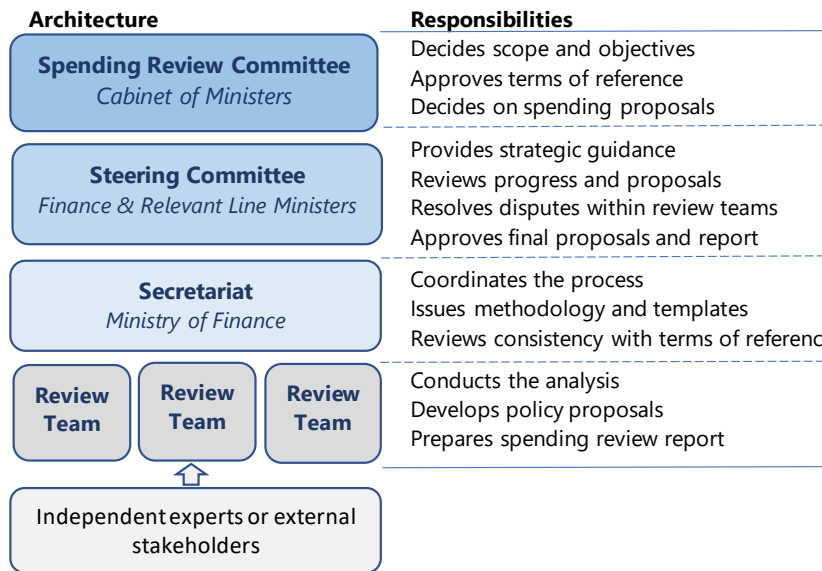
### III. RECOMMENDATIONS

**29. While many of the key operational elements required to run SRs have now been put in place, these can be further strengthened.** Technical capacity has grown both in the MOF and in Line Ministries, and important new developments in the institutional architecture and coordinating mechanisms provide the tools to manage and execute SRs. Using this capacity to maximum effect, however, will require strengthening the institutional framework. Table 1 provides a diagnosis of the key Public Financial Management (PFM) elements and the extent to which they currently support the new SR process.

**30. The governance architecture around the SRP should be reinforced at senior level to lock-in active political ownership.** A strong Spending Review Committee comprising Cabinet Ministers is always important but especially when a new coalition government takes charge. There is an opportunity to tie together the internal discussion on the new government's objectives with leadership of the SR process as the mechanism to deliver those objectives. A stronger Steering Committee, comprising the Finance and relevant line ministers, is needed to address the ownership challenges observed in the SRs to date (Figure 1).

**31. The governance architecture at working level can also be improved to embed the SR process more effectively in the administration.** The design of the Secretariat at the MOF should factor in the need to fully involve the Budget Department in the Spending Review process. The Budget Department should be instrumental in the preparation of budget baselines which, as mentioned below, are essential to ensure that the outcomes of spending reviews are factored into budgetary allocations. The Budget Department should also drive compliance by requiring strict adherence to budget limits, including the financial implications of new legislation, and it should ensure that spending allocations are consistent with the agreed objectives emerging from the SR process. On the other hand, the Implementation Unit should focus more on engaging ministers in the decision-making process and on ensuring that agreed reforms are underpinned by both financial and operational targets and milestones. To make these operational changes effective will require improving work on baselines.

**Figure 1. An Institutional Structure for Effective SRs**



Source: IMF Staff

**32. Developing sectoral baselines should be a top priority to improve the effectiveness of the SR process.** As shown by the PFM diagnosis in Table 1, most of the main challenges encountered in each of the four stages evaluated above are either caused or compounded by not using sectoral baselines as the bedrock of interactions between the MOF and Line Ministries. Spending control is the single most powerful instrument the MOF has to promote change across government. When baselines are the starting point of budget allocations, the MOF can enter negotiations with Line Ministries to encourage trade-offs, increase efficiency and focus resources where they will best contribute to advancing the policy agenda of the government. Without clear baselines, spending is allocated in an incremental fashion that is swayed more by short-term political considerations than by the government’s own long-term priorities. This has a direct impact on the relevance of the SR outputs, and on the early involvement of ministers in the setting of TORs and objectives for reviews in their sectors.

**33. On the basis of sectoral baselines, the government should then work on setting binding annual and medium-term budgets.** This will allow the government to use the SR process to frame ministers’ decisions within a financially coherent medium-term perspective. As a result, line ministries will improve their engagement with the implementation of “value for money” measures and structural reforms addressed in the SRs.

**Table 1. Diagnosis of PFM Support for the SR Process**

|    | <b>Requirement</b>   | <b>Significance</b>   |       | <b>Status</b>  | <b>Action</b>  |
|----|--|---|-------|--|--|
| 1  | <b>Credible annual budget</b>                              | Implement the budget as planned   | Red   | Under-execution of investment budget is large and routine.                                     | Set realistic baselines and protect capex from ad hoc reallocations                            |
| 2  | <b>Sectoral expenditure ceilings</b>                       | Require decision-makers to make trade-offs  | Red   | Further expenditure is routinely added after budget approved                                   | Build binding and program-based budgets  |
| 3  | <b>Clear political priorities</b>                          | Ensure consistency between political ambitions and available resources over the medium-term                         | Amber | TOR good, but Line Ministries have not taken full ownership of VFM reforms                     | Use baseline and budget negotiations to lock in cross-government ownership of agreed reforms   |
| 4  | <b>Financial and non-financial performance information</b> | Compare trends in expenditure, inputs, outputs, and outcomes  | Amber | Savings targets identified, but other metrics should also be established                       | Set operational targets and milestones to track reforms that have been factored into baselines |
| 5  | <b>Analytical capacity</b>                                 | Ability to identify areas of inefficiency and to develop reform proposals   | Green | Strong analytical teams created both in MOF and in LMs   | Develop clear guidelines on how to identify implementable measures in reviews                  |
| 6  | <b>Methodology for accounting for savings</b>              | Ensure that savings identified can be used to offset spending pressures within budgets                              | Green | Agreed savings measures are regularly monitored in IRs   | Continue to monitor savings. More detailed program budgets would allow further scrutiny        |
| 7  | <b>External challenge</b>                                  | Challenge existing ways of working and inject new ideas   | Green | U challenge and SRs with external experts supply fresh ideas                                   | Build on success from Spending Reviews   |
| 8  | <b>Medium-term budget framework</b>                        | Incorporate the results of the review in multi-year budget allocations for each ministry                            | Red   | Current medium-term budget is a mechanism to signal priorities, but is not financially binding | Prepare Sectoral Baselines to build binding medium-term budget                                 |
| 9  | <b>Ability to reprioritize expenditure</b>                 | Capacity to move resources from lower to higher priority areas  | Green | Possible to do   | Continue to link saving measures to VFM measures in SRs  |
| 10 | <b>Time and resources</b>                                  | Sufficient time to undertake analysis, develop reform options, integrate them into budgets, and plan implementation | Green | New Government is in place and the process can start now                                       | Propose next stage of SRs as framework to deliver on the new government's priorities           |

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