



Performance-Based Systems

1 Why reflect on performance-based systems?

Performance-based systems were introduced in the public realm in the late 1980s, during the first wave of New Public Management (i.e. performance-based grant or financing systems, balance scorecards, environmental performance assessments, competitions, certification schemes, etc.). For this Policy Brief, we define performance-based systems as a **goal-oriented approach to the provision of public goods focusing on results rather than inputs or processes**.

This Policy Brief is a synthesis of a process that took place in 2021,¹ where insights were gathered from **donor-supported** performance-based development projects (i.e. those of SDC, the EU, Sweden, the Norwegian Government, Austrian Cooperation, etc.). These projects are mainly focused on local development and decentralisation, which are implemented at local, national and regional levels; however, we believe that the findings are relevant for any project which intends to use a performance system as a driver for change.

To understand the relevance of performance-based systems for civil society and private sector projects, selected civil society and private sector experts² were involved at various stages of analyses.

Writing a Policy Brief in this field is complex. There are **multiple actors at different governance levels** involved: central government (responsible ministry, ministry of finance, line ministries, state agencies); local government/municipalities (including the local councils, associations of municipalities and their membership networks); independent institutions (i.e. audit, commissioner for the right of information and public participation, ombudsman); civil society and the private sector (including local communities and interest groups);

Box 1. Performance-based systems projects in the Western Balkans and Southeast Europe*

- Decentralisation and Municipal Support (DEMOS), Kosovo
- Bashki te Forta (Strong Municipalities), Albania
- Municipal Environmental and Economic Governance (MEG), Bosnia and Herzegovina
- Municipal Economic Development in Eastern Serbia (MED), Serbia
- NALAS Decentralization Observatory in Southeast Europe located in Northern Macedonia

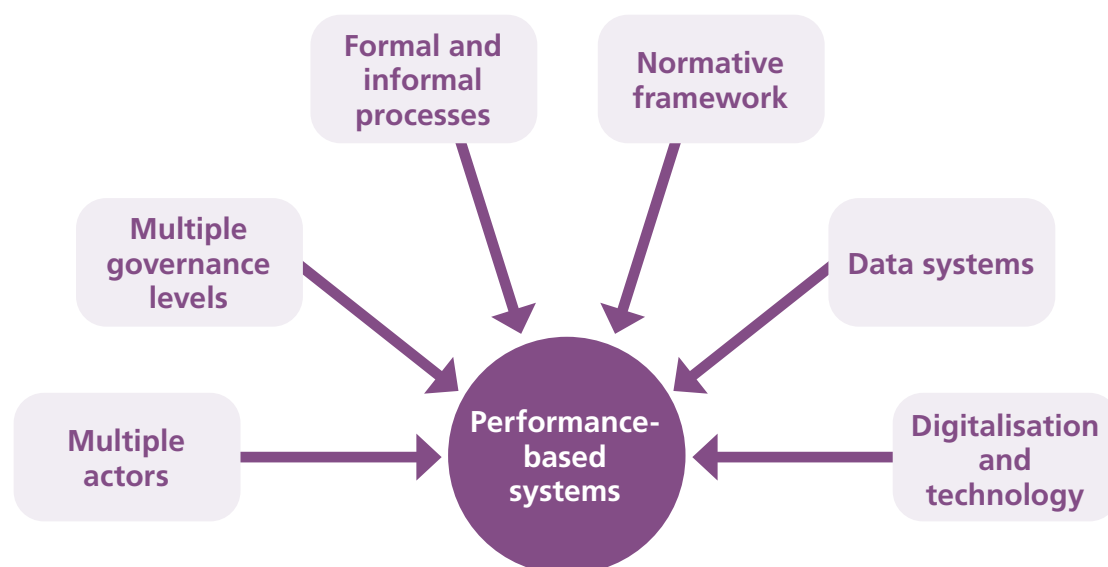
* For further information, see: DEMOS, Bashki te Forta (Strong Municipalities), MEG, MED and NALAS.

and donors with their own coordination and financing mechanisms. Also, performance-based mechanisms are part of or include myriad different **public formal and informal processes** (i.e. municipal strategic and investment plans, performance-based budgeting and auditing, service standards and their monitoring, public consultation and information, intergovernmental fiscal transfers, competition and advocacy, election campaigning) with their respective **normative frameworks** (i.e. laws on local finances and budgeting, on municipalities, on public information and consultation, and laws/regulations on local councils and on performance grants). In addition, they are increasingly integrated in overarching **data systems** that have their own laws and regulations (compliance tools for performance monitoring and reporting, annual reports on municipal performance, e-surveys) – a topic that is becoming more important than ever. While there is a huge potential with **digitalisation and the use of new technologies**, the process of their introduction, security and good governance (including maintenance) is an issue.

1 A joint learning journey between the Western Balkans – Swiss Development Cooperation and Helvetas, January–June 2021.

2 Consulted civil society projects LEVIZ and ACT. Private sector project RECONOMY.

Figure 1. The complexity of performance-based systems



Source: Authors' own.

What role can a donor-funded project play in **supporting performance-based systems**? It can:

- Make the **actors talk to each other** by assisting them to better play their role and enable **multilevel dialogue**;
- Provide **technical assistance** (and financial assistance to accelerate certain processes) wherever there is a gap, i.e. tools and processes;
- Support the process of establishing a **legal basis for building and implementing a performance-based system** by bringing 'on system' the learnings of performance projects; and
- Enable actors in the process to find **innovative solutions** (including the introduction of technology and digitalisation).
- Also, it may tailor incentive packages which accelerate **change in behaviour** of public administration and public and political representatives.

Throughout the last ten years, the neoliberal and possibly mechanical understanding of goal-oriented public services became more political with a focus on the **power dynamics** between different actors and the **incentives** that drive them. In addition, **governing through integrated data systems** and the **use of technology** to make this possible seems to be a future trend.

As such, the focus shifted to **performance-based systems for regularly measuring and reporting**

publicly on performance, with the aim to improve results for the citizens (by transforming public administration practices). Therefore, the following questions in the design and implementation of performance-based mechanisms are pertinent:

- **When is a system credible** (to both the administration and the public)?
- **When are incentives that a system provides beneficial** – or at least do no harm?
- **How can we model performance incentives** in a way that rewards positive change (behavioural change), and how can we mitigate possible risk connected to these incentives?
- **How can we ensure a better participation of citizens** (including the private sector) in these systems?

2 Credible performance systems

There are several challenging issues to address when introducing a performance-based system, like the cacophony of reform expectations at the local level, the absence of comparable entities for benchmarking and data quality, or the inadequate use of strategic planning and reporting. Also, the overall impact of any performance depends strongly on what we call the 'credibility' of the system, and there are a number of important aspects that determine this credibility.

First, **a clear and realistic vision and objectives that should be achieved through the system.**

Once this has been jointly agreed upon by the involved stakeholders, a metric is set for selected areas. Areas in public administration that are often measured by a performance system are: (1) service performance; (2) good governance; (3) financial management; (4) human resource management; (5) legal/rule compliance; and (6) scale of a policy implementation (e.g. decentralisation). Thus, there needs to be a clear vision of what good performing systems are so that feasible objectives can be set.

Second, credibility depends upon **accurate, timely and reliable data** which mirrors the realistic vision and objectives, and a **data-gathering process** that is tested and improved periodically in different rounds to maintain consistency. Sometimes to gather only **quantitative data** is not enough; therefore, **qualitative data** is introduced in addition. Qualitative data can be made more objective by increasing the number of respondents or detailing the measure of an indicator in descriptive scales.³ For quantitative data, it is important to first pre-assess its availability and/or the actions needed to generate it. While **some of these activities do not depend on predisposition or resources**, others do.

Third, **it is important that projects and donors do not arrive with their own indicators**. The best way to ensure credibility is to **co-design indicators with all stakeholders**, especially if they are linked with financial incentives. This takes time. The Kosovo example shows that there is a **lengthy process** to adopt an indicator, including decisions taken on: (a) purpose (like criteria-based fund allocation); (b) data availability; (c) possibility/feasibility of verification; (d) credibility and availability of the source of data; (e) responsibility for data gathering; and (f) definition of the process of decision-making to take up an indicator. The Kosovo and Bosnia Herzegovina examples present a possible solution: **120 indicators** were collected and used at the local level, but only some were selected and used at the national level to be **linked with incentives/ a performance grant (30 indicators)**. Indicators might be **used sequentially in a strategic way**: at the beginning, they drive **changes in the management** and at a later stage, in **behaviour**. The example of Serbia shows that at first there was a financial incentive for municipalities to increase their own property tax, and in the second phase, performance was linked to soft requirements, i.e. participation mechanisms needed to be applied.

3 With the involvement of the local community, using a scale of 1–5, where 1 is not at all, 2 at information level, 3 consultation level, 4 dialogue, and 5 partnership with a narrative description for each scale.

Fourth, the credibility strongly depends on the **data-gathering process**, from the generation and collection at the local level to the aggregation at the national level. Thus, the aim is to assure a **data quality process** (with different quality assurance loops at both local and national levels). For example, the process in Kosovo is as follows: (1) The local level generates the data; (2) a dedicated officer in the municipality is made responsible; (3) collection takes place at the municipal level through this officer and is then (4) approved by the mayor (or another body). The data is processed at the national level (ministry and auditor) and reassures the quality (checks for outliers and/or other checks, including penalties for the wrong data). This aggregated data is then linked with the financial incentive based on objectives. In Albania, the legal framework on local self-government foresees the establishment of the so-called Performance Units as part of organogram for all municipalities, which are at the core of data-gathering and quality assurance processes of a performance-based system.

Finally, credibility of the system depends on the **possibility for municipalities to improve**. Thus, while the national level is interested to introduce a minimum standard, there also needs to be targets that help with improving the current standard, which might vary among municipalities. Thus, so-called Performance Action Plans are needed with feedback loops that are regularly monitored, that give municipalities the possibility to get better.

3 Incentives for positive change

How can we **model performance incentives** in a way that rewards positive change (behavioural change), and how can we mitigate possible risk connected to these incentives (i.e. political marginalisation, disparities or fairness aspects)?

The incentives to change are mostly based on **financial incentives** linked to the performance management system (be it in a system integrated in intergovernmental transfers or from a fund or through project co-financing). Financial incentives can also bear risks. Often, financial incentives need **absolute thresholds**;⁴ however, incentives work differently for different municipalities (i.e. size or geographic location). Also, sometimes financial incentives can incentivise a project-based approach vs a systemic-based approach that is interested in long-term sustainability. Thus, often financial incentives remain short term if they are not institutionalised (brought 'on system').

4 It is recommended that not less than 2.5 per cent of the general annual grant is transferred through intergovernmental transfers (in the case of Kosovo) or not less than 10–20 per cent of allocated capital investments.

Of course, financial incentives often go hand in hand with interrelated **non-financial incentives**. For example, the possibility for local political leaders to gain public recognition because they claim responsibility for good performance scores; networking of experts as an opportunity for career development; performance benchmarking used on electoral campaigns, etc. Of course, these incentives can be beneficial not only for one person (e.g. the mayor), but for the municipality as a whole to gain further influence within a system (i.e. advocacy through local associations). Often, the driver of change is individuals when there are opportunities to tailor formal financial incentives with less formal activities – such as competitions, public events, etc. – that lead to better performance. At the same time, a negative performance can sometimes also be used to undermine the credibility of a performance-based system.

The financial incentive of a lot of performance-based projects is not intended to be permanent, but to be in place until a point where all the changes have been attained (i.e. more inclusion, more efficiency, more environmental sustainability, etc.). However, at the same time, it could be also an overall goal to **link these performance-based mechanisms permanently with the overall intergovernmental transfer system** and introduce a culture of accountability within the public finance system. Some of the actors may not be well positioned for achieving the set targets which allow access to financial incentives. It is important to apply fair procedures especially if a benchmarking approach is applied (e.g. by measuring and rewarding efforts vs results).

4 Introducing or moving a performance-based mechanism 'on system'

How can programme-based or donor-supported performance-based systems be best introduced from the beginning or brought into the partner country system at a later stage? To introduce or move a performance-based mechanism 'on system', it is important to understand where and how a mechanism already uses existing government systems. The various examples show different ways in which existing partner country systems interact with the project system. For example, the performance-based system is linked with the intergovernmental transfer systems (processes and rules), but the finances are still transferred directly from donors to partners. The project brings the benchmarking/performance criteria, but the transfers come from a national fund, private sector (in the case of Bosnia Herzegovina) or from both government and

project funds. While approaches today have mainly focused on including the 'systems' **in the respective legislative frameworks** (i.e. law on municipal finance or sectoral laws on water, waste or the environment, dedicated performance grant laws), there is an open question of how best to move all (in the case of Kosovo, which concluded with the Draft Law on the Municipal Performance Management System and the Performance-Based Grant Scheme) or the most relevant parts of a project 'on system' (in the case of Albania on integrating data/statistics and reporting, which concluded with a Decision of the Council of Ministers 'On the approval of the rules for keeping, updating, and publication of the waste statistics').

It is also important to note that bringing a performance-based mechanism 'on system' is **often gradual and evolves over time**. In Kosovo, for example, after a period when only approximately half of all municipalities were part of the performance-based system, it was rolled out to all municipalities. The roll-out in such a way was only possible because there was already a tested and long-standing co-financing mechanism established between the Ministry of Local Government Administration and the donor community. Now, it has developed even further as the donors are no longer part of the system but are only observers (with a veto power). One reason for not being 'on system' for a long time was **the audit of the overall process**, which is commissioned by the SDC and implemented through the DEMOS project. Also, it is interesting to note that the better a performance system is established, the more actors might profit from it, including internally within the administration. For example, because municipalities establish a process of data gathering that is trustworthy, line ministries start to use this data for their policy planning and more donors join the performance grant.

At the same time, all examples show that where management of financial resources is handled through the public system, the **overall performance mechanism is only as strong as the public finance system**. Thus, it makes sense to set certain preconditions, as shown in the case of a SECO project in Peru. To bring a performance-based system 'on system', first some 'basics' are needed, like programme-based and multi-annual budgeting. Thus, the central government asks municipalities to achieve targets in selected priority areas: (1) education, (2) health, (3) property tax, (4) investment, and (5) reduction of red tape. The performance municipal investment plan in turn serves as the 'carrot' to introduce measures that are not so popular. As is often the problem (see Section 3), the old practices of performance measurement provided incentives for the rich municipalities, but not

for the poorer ones. To resolve this, tailored targets for different types of municipalities and technical assistance were introduced to help the municipalities to reach their targets. This example shows that building a performance-based mechanism 'on system' from the start takes time unless such a system exists and technical assistance focus is on 'make it work'.

In order to think about the sustainability of a performance-based system, it is important to consider the 'institutionalisation' of the system **at an early stage** and also what sustainable incentives mean, i.e. what if the financial incentive will at some point not be so high or even 'dry out'? A **multi-stakeholder (and thus multi-partisan) approach** to establishing the mechanism is beneficial for its long-term sustainability and acceptance if it should be transferred into the 'public system'. The specific performance system must be understood within the **bigger picture** of either intergovernmental transfers or other incentives that are already present in the public finance system. Apart from rooting the system **vertically** within the public policies and finance structure, it is important to anchor the system **horizontally**, among the municipalities (i.e. through the association of municipalities) and other **system actors representing the 'demand side'**, such as civil society and private sector.

5 The roles of citizens, civil society and the private sector

Most of the mechanisms **work mainly on and in the public administration**. However, in order to anchor them better in the overall democratic process and truly become 'a system', the performance-based systems could also be co-designed and used **by civil society actors, the private sector or citizens directly in terms of asking for accountability**. Here, consideration can be given to if and how performance-based mechanisms could be used by local politicians in shaping their relationship to the public administration, local authorities and interactions with the private sector and civil society. It could be that the stakeholder involvement is as important as the performance system itself.

Some performance-based mechanisms remain within the public administration. For example, this makes sense in the case of the Standing Conference of Towns and Municipalities in Serbia, which has developed a self-assessment tool that is not public, so the association's members do not compete with each other. Performance-based systems can be a management tool: in Albania, the Performance Monitoring System was brought in by a law on finance together with the programme budgeting Classification of the Functions

of Government (COFOG) and is backed up by an integrated policy planning and reporting system at local and national levels (Integrated Planning System (IPS)). It does not always include the public (i.e. performance-based human resource management in Bosnia and Herzegovina).

Factors that influence the possibility of civil society inclusion vary:

- **Political sensitivity of the topics and data** (gender-based budgeting is less sensitive so there is a high chance of receiving positive feedback from local authorities, whereas public procurement issues are less likely to be heard by decision-makers). The involvement of civil society organisations (CSOs) also depends on **cooperation with the local authorities**. In the end, a lot depends on the **timing**: in a pre-election period, requests for greater accountability are more accepted than after elections. Very rarely do local governments recognise CSOs as long-standing real partners that they would want to regularly have at the table.

- Involvement of CSOs themselves in **the delivery of services**. If civil society acts mainly as a service provider, it is part of the performance-based mechanism and has a very specific role or task within the system. While in this role CSOs are much more constructive, they cannot really criticise the government. On the other hand, some CSOs might mainly work on policy issues and can thus serve as a 'watchdog' over the quality of services or the achievement of performance targets. Additionally, most civil society actors are **financed through donors**. They are asking for accountability because they are paid. Work is also needed to make CSOs more independent of donors.

- While some of the project examples have tried to include CSOs, this was quite difficult as real involvement in a performance-based mechanism needs 'number crunching' and some **technical skills** (knowledge about framework conditions, local governance affairs and laws/processes) for which one is not paid. It is challenging not only for CSOs but also for councillors/parliamentarians and even more so for citizens to understand performance-based systems.

If performance-based mechanisms should be used outside the public administration, for accountability purposes, then it would be important to use a **public consultation framework and access information rights** as an entry point to reach policymakers and

administrations. More and more **digital platforms** are providing access to information and opening space for debate and oversight of public affairs (e.g. the cases of Leviz Albania and ACT for a Strong Civil Society in Serbia) beyond the traditional accountability mechanisms. Playing a 'watchdog' role is often confrontational; but at the same time, interesting **results can be achieved through joint action**. For example, co-designing a performance-based system where all the actors are involved (see Section 1) may advance its development through mutual constructive 'pressure'.

Other ways to set a positive balance between supply side (performance system) and demand side (civil society and the private sector, community) are to **invest in communication**, produce reader-friendly information that explains complicated mechanisms, anchor performance information in diverse channels (e.g. collaboration with the media), and provide real-time data and visualisations.

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