3. MAJOR PERFORMANCE AUDIT FINDINGS AND RECOMMENDATIONS

This section discusses the specific findings and recommendations from the performance audit of the planning, budget, and program evaluation processes.

Managing for results

Including federal and other funding sources, North Carolina has a total annual budget in excess of $13 billion, which, if compared to the private sector, would place North Carolina among the nation's largest businesses. The State would rank 30th in revenues among the Fortune 500--approximately the size of the 3M Company or Westinghouse. Although its objectives are much different from those of private sector businesses, the State's need to use its resources wisely is just as significant. The State must develop state-of-the-art management systems to minimize the impact of the fiscal challenges it faces in the next decade.

Today's State planning, budgeting, and program evaluation processes do not meet the State's business management needs. The processes are disconnected, underdeveloped, and focused on financial inputs, financial results, and expenditure control while neglecting performance measurement. The legislative involvement in the budget process is through appropriations. The law does not require the General Assembly to discuss or vote on the State's long-range plan/priorities or performance measures. Yet, there are two examples of the General Assembly making a substantial commitment to long-range plans: (1) the Basic Education Program (about $1 billion since 1984) and (2) highway building program ($9 billion to $10 billion over 13 years).

North Carolina's State budget is full of statistics that describe agency and program activity. The vast majority of these "program statistics" and "objectives and measures" measure work load rather than results (e.g., work load: number of measles vaccinations administered, results: decline in number of children with measles). Only 10 percent of the program statistics in the budget measure program outcomes. Despite the 3,500 pages and the six volumes it comprises, the budget includes little information about whether or not a program is working, or whether it is accomplishing the goals that the General Assembly intended.

To support the Governor and General Assembly in making the difficult budgetary decisions over the next decade, the State needs the following:

- A strategic planning process
- A budget process focused on results
- An effective capital budgeting process

- Legislative oversight focused on program results
- Outcome measures for evaluating program results

A program budget format, structured around the State's strategic plan and including program outcome measures, provides effective support for critical budgetary decisions and integrates the planning, budgeting, and program evaluation processes for the State of North Carolina.

A strategic planning process

The State lacks a strategic planning process. The individual findings and recommendations that support this conclusion are:

- The State's policy planning process is conducted within each department rather than at the State level
- The departmental planning process does not provide for participation by the General Assembly or the public
- The State's departmental plans lack sufficient linkage to resource allocation and implementation

These findings and our recommendations are discussed in detail below.

Finding 1 - The State's policy planning process is conducted within each department but not at the State level.

The only statutory reference to a State planning process is G.S. 143A-17, which requires that departments submit annual plans to the General Assembly. By agreement between the Governor and the General Assembly, the biennial budget fulfills the statutory requirement for annual plans in G.S. 143A-17. Because this planning process is inadequate for a state as large and complex as North Carolina, additional efforts at planning have been undertaken by both the executive and the legislative branches.

In 1990 the Governor initiated a long-range departmental planning process, which is coordinated by the Office of State Planning (OSP), but conducted at the department/agency level. In January 1991, this process produced the State's *Departmental Plans* for 1991-1995. It is now producing departmental plans for 1993-1999.

The Office of State Planning provides the departments with planning instructions and a review of economic, fiscal and demographic trends (entitled "Common Outlook and Assumptions"). When the departmental plans are completed, the OSP compiles them into a publication called *Departmental Plans* and inserts the "Common Outlook and Assumptions"

as an introductory section. This initiative is a significant and important first step to introducing a strategic perspective to North Carolina's planning process.

The State's planning process should solicit external and internal analyses, provide a focal point for the state's future, define measurable objectives, and establish priorities and a plan for implementation. Key elements of corporate and governmental strategic planning are shown in Exhibit 3-1.

A strategic planning process should result in:

- A vision for the State
- Goals and priorities
- Measurable criteria for assessing the attainment of those goals
- A set of priorities among the broadly-defined program areas that are not restricted by departmental organization structure (e.g., public safety, health, economic growth).

Concern over their future direction has caused some states to initiate major strategic planning processes in recent years. Key features of the strategic planning processes in Oregon, Minnesota, Texas, and Utah are highlighted in Exhibit 3-2.

Oregon, in particular, demonstrates some of the possibilities offered by state-level strategic planning. In 1989, the Oregon Progress Board used strategic planning techniques to develop a 20-year vision for the state, with specific goals and "strategic priorities." In 1990, the Board identified benchmarks for measuring the attainment of those goals. These selected benchmarks are shown in Exhibit 3-3, and are intended to keep the State of Oregon focused on and accountable for achieving its long-range goals. These efforts were cited as part of the reason for Oregon's rise from 16 to 6 in *Financial World* magazine's 1992 ranking of states according to standard financial management criteria.

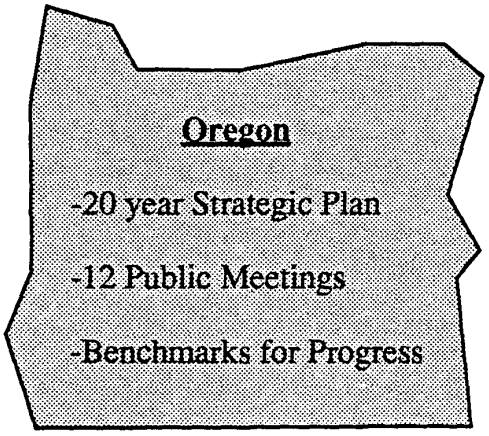
North Carolina's current planning process does not address the broader issues of state government. The absence of a high-level policy planning process limits the ability of the General Assembly and the Governor to govern with foresight, to make policy decisions that anticipate future events, and to position the State to avoid problems. Without effective long-range planning, government leaders are thrown into a reactive mode, where crisis-and-response becomes a repeated pattern.

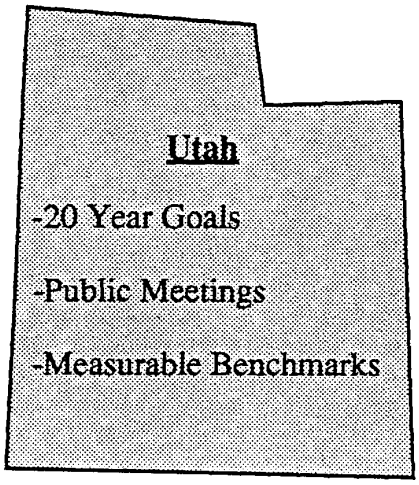
The State has been forced by the court to react to crises in the areas of children with serious emotional disturbances, mentally retarded, and prison inmates. The consent decrees Willie M. and Thomas S. and court-ordered action in the Department of Correction are examples of the State government in a reactive mode.

Exhibit 3-1
Elements of Strategic Planning

Planning Element	Corporate Focus	Government Focus
External Analysis	Customers	Citizens
Internal Analysis	Profitability Growth	Benchmarks Outcome Measures
Mission/Vision	Customer Service	Public Service
Long Range Goals	Bottom Line	Quality of Life
Strategies/ Priorities	Products/Services	Programs
Implementation Plans	Business Plan	Budget

Exhibit 3-2
Recent Strategic Planning Efforts in Other States





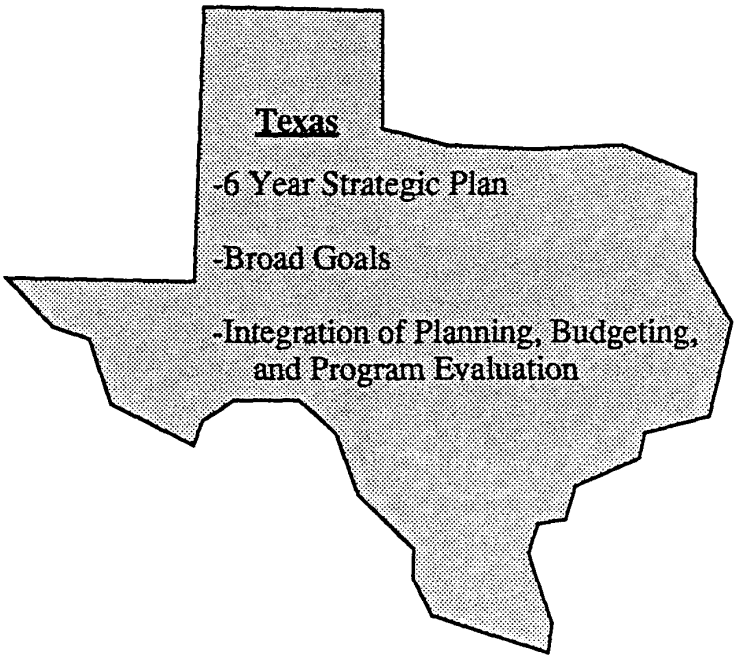


Exhibit 3-3
Oregon's Choices Made Through Strategic Planning

Key Benchmarks: **Enduring Measures of Oregon's Well-Being**

Key Benchmarks for People:
- **Adult Health**
- **Basic Student Skills**
- **Comparative Math Skills**
- **Adult Literacy**

Key Benchmarks for the Economy:
- **Personal Income**
- **Industrial Economic Diversity**
- **Manufacturing Exports**
- **Job Distribution**

Key Benchmarks for Quality for Life:
- **Air Quality**
- **Natural Resource Lands**
- **Groundwater**
- **Affordable Housing**
- **Crime**

Lead Benchmarks: Priorities over the next five years

Lead Benchmarks for People:
- **Teen Pregnancy**
- **Readiness to Learn**
- **Drug-Free Babies**
- **Job Skill Preparation**
- **Crime/Social Harmony**
- **Work Force Adaptability**

Lead Benchmarks for the Economy:
- **Workers' Compensation Costs**
- **Value Added Wood Products**
- **Industrial Land Development**
- **Tax Burden**
- **Public Infrastructure Investment**

Lead Benchmarks for Quality of Life:
- **Air Quality**
- **Affordable Housing**
- **Urban Mobility**
- **Health Care Access**
- **Rural Health Care**

In situations in which government fails to adopt a meaningful long-range policy planning process, civic organizations have stepped in to play this role, acting as "keepers of the long term agenda" and turning that agenda into government policy "by engaging as political activists and lobbyists" (*Reinventing Government*, p. 248). This can place government leaders in a still more reactive role, further contributing to public disillusionment with government and the political process.

The statute governing State policy planning does not go far enough. It requires departmental plans but not a strategic planning process.

Recommendation: Establish a strategic planning process for the State.

The General Assembly should revise G.S. 143A-17, which authorizes the current annual planning process, to establish a strategic planning process for the State.

The legislation should address the following elements:

- **Vision:** The State should consider alternative futures as they pertain to quality of life, safety, health, and the environment.
- **Statewide goals:** Concrete goals for the entire state should be established in those areas that matter most to citizens.
- **External assessment:** The State should solicit ideas, opinions, and concerns from the citizens regarding how well the State is meeting its goals.
- **Internal assessment:** The planning process must involve the legislature, top executive branch management, and selected personnel at all levels of State government.
- **Agency goals:** Agencies should develop clearly defined goals that are consistent with statewide goals.
- **Objectives and measurable results:** To track the State's progress toward achieving statewide and agency goals, it must develop indicators of program results.
- **Planning/budget document:** The biennial budget document should reflect the State's long-range plans.
- **Performance measurement and monitoring:** Once indicators of program results are set, the General Assembly must establish a process to review the performance of State programs periodically.

Finding 2 - The departmental planning process does not provide for participation by the General Assembly or the public.

The State's current planning process solicits input from program managers and top management in the agencies. The process does not include a procedure for incorporating the views and preferences of citizens. Neither does the process provide for participation by the General Assembly. The State Policy and Planning Board, which involved citizens in the NC 2000 process, has no role in the State's ongoing planning process. The General Assembly's only role in departmental planning is to receive the *Departmental Plans* when they are published.

External analysis is a critical element of any successful strategic planning process. For governments, external analysis involves recipients of government services, citizens, taxpayers, and the legislature.

Balancing the needs of taxpayers, state employees, and the recipients of government services will pose challenges as serious as those that can be seen in economic and demographic trends. A plan that does not consider these attitudes will not produce a realistic scenario for the future.

The guiding vision, long-range goals, strategies, and policies and plans for service delivery must come from the leadership of the government - the Governor and the General Assembly. Long-range policy planning for any organization should contribute to the organization's policy decisions - therefore, the policy-makers should be involved. The Council of State Planning Agencies' *The Game Plan* suggests that the nation's governors use the following "general guideline": that "legislative involvement should begin as early and as intensively as is politically feasible." In the absence of this involvement, the legislature is likely to enact legislation that is inconsistent with the strategies of the long range plan -- or fail to enact legislation that is needed to implement the plan.

G.S.143A-17, which governs State policy planning, does not specify procedures for citizen or legislative input.

Recommendation: Create a process for citizen and legislative participation in the planning process.

There are several ways to involve citizens and the legislature in the discussion of alternative futures for the State of North Carolina. Public participation can be obtained from existing sources available to the departments, or from additional public surveys and meetings. General Assembly participation can be obtained through a legislative process to establish the State's "Common Outlook and Assumptions." (OSP is now considering this step.) A legislative commission with the appropriate authority, such as the Joint Legislative Commission on Future Strategies, could comment formally upon the long-range perspective and assumptions on which the planning effort is based.

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Finding 3 - The State's Departmental Plans lack sufficient linkage between resource allocation and implementation.

The *Departmental Plans* includes each department's mission, goals, objectives, and outcome measures. The 1991-1995 volume of *Departmental Plans* was given to the members of the General Assembly and their staffs as an informational document in time for the 1991-1993 budget deliberations. It was not, however, a part of the budget deliberations nor was it used by the legislators or staff in making appropriations decisions.

A successful strategic planning process must have a plan for action. Several essential elements improve the chances that a plan will be executed through operational planning and action. These include:

- **Indicators of program results**: Plans should include specific, measurable indicators of performance that can help managers and policymakers assess the effectiveness of operating programs in meeting State goals.

- **Line manager involvement:** Program managers responsible for carrying out the plans should be involved in decision making in the planning process.

- **Implementation plans:** Detailed plans should indicate required action, responsibility, and milestones to meet the State's long-range goals.

- **Linkage between strategic plans and budget formulation:** A process is needed to ensure that biennial budget decisions are made within the context of the State's long range plan.

The North Carolina budget is a plan, but it is more often than not inconsistent with the *Departmental Plans.*

Several factors contribute to the separation between the planning and the budgeting processes. Among these are:

- Most line managers are not full participants in the planning process and therefore are not stakeholders in the plan

- Competing planning processes cause confusion among program managers

- Outcome measures, which are critical to linking the two processes, are different for planning and budgeting

- The planning process in North Carolina is developed separate and apart from the budget and program evaluation processes

The State is now beginning to develop a system to incorporate the planning process with the budget process. These efforts have yet to integrate the planning and budgeting processes completely.

As fiscal pressures increase, other states are forging a stronger link among planning, budgeting, and program evaluation. Texas, which recently adopted a Strategic Planning and Budgeting System, has rewritten its budget instructions to make a clear connection between the State's planning, budgeting, and program evaluation processes.

Recommendation: Include program managers in department planning process.

The Office of State Planning should be required to involve all levels of the organization in preparing the departmental plans--an approach that will ensure the internal analysis necessary for a successful strategic planning process. This can be done by (a) providing guidance to agencies in the planning process and (b) and by providing on-site technical assistance and process leadership to the departments, as needed, in the course of the planning process.

Recommendation: Establish linkages between planning, budgeting, program delivery and program evaluation processes.

The OSP and OSBM should continue their efforts to link policy planning with budget formulation. Exhibit 3-4, shows the proposed relationship among the planning, budgeting, implementation, and program evaluation processes. Effective linkage among these processes should include:

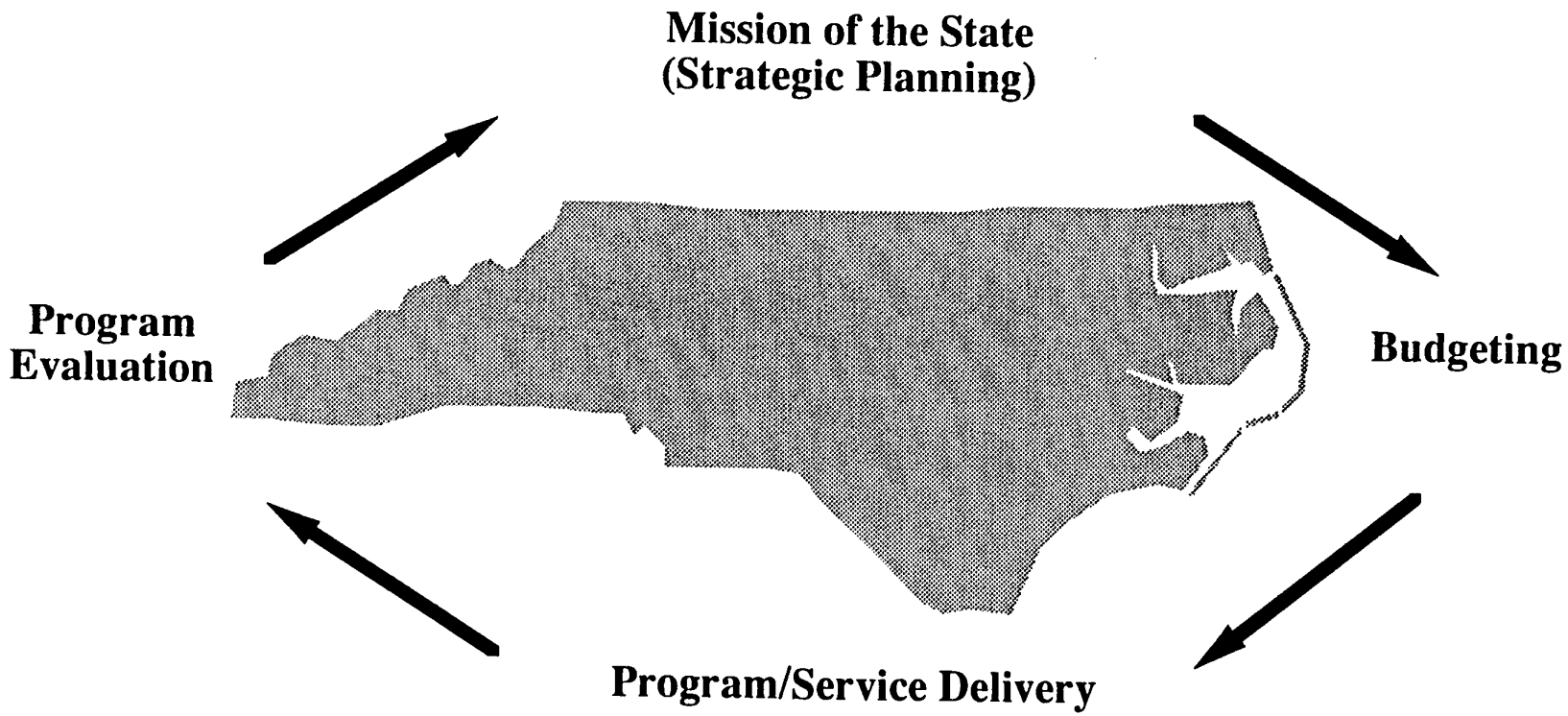
- Unified planning/budgeting instructions for use by the agencies in developing their long-range plans and biennial budgets
- Budget strategies and objectives that implement the strategic plan
- Use of identical performance measures for planning and program evaluation

Recommendation: Develop program outcome indicators for the planning process that are identical to those used for ongoing program monitoring.

Indicators of program results provide the necessary link between planning and program evaluation. They should be identified during the planning process and measured and reported as part of the evaluation process. Definition, measurement, and reporting of program results tend to focus programs on achieving the purposes for which they were created and to strengthen the accountability of program managers to policy-makers.

Exhibit 3-4

Managing the State's Business



Focusing on Results

For example, the results of the State's economic development programs could be measured by counting the net number of jobs created as a result of assistance provided by the State's economic development program. Job creation is one of the expected results from economic development programs. If the State chooses to use net job creation to measure the performance of economic development programs, it should use the same indicator for planning purposes. In other words, the State should appropriate funds to the economic development program with explicit objective of creating a certain number of jobs. The State should plan and measure performance based on the same indicators of program results.

A model for the North Carolina strategic planning, budgeting, and program evaluation system is shown in Exhibit 3-5.

A budget process focused on results

The State budget document focuses attention on inputs--individual line items of expenditures such as personnel, equipment, and utilities. The budget document does not indicate whether or not a program is effective and does not facilitate meaningful comparisons among programs and priorities. The individual findings that support this conclusion are:

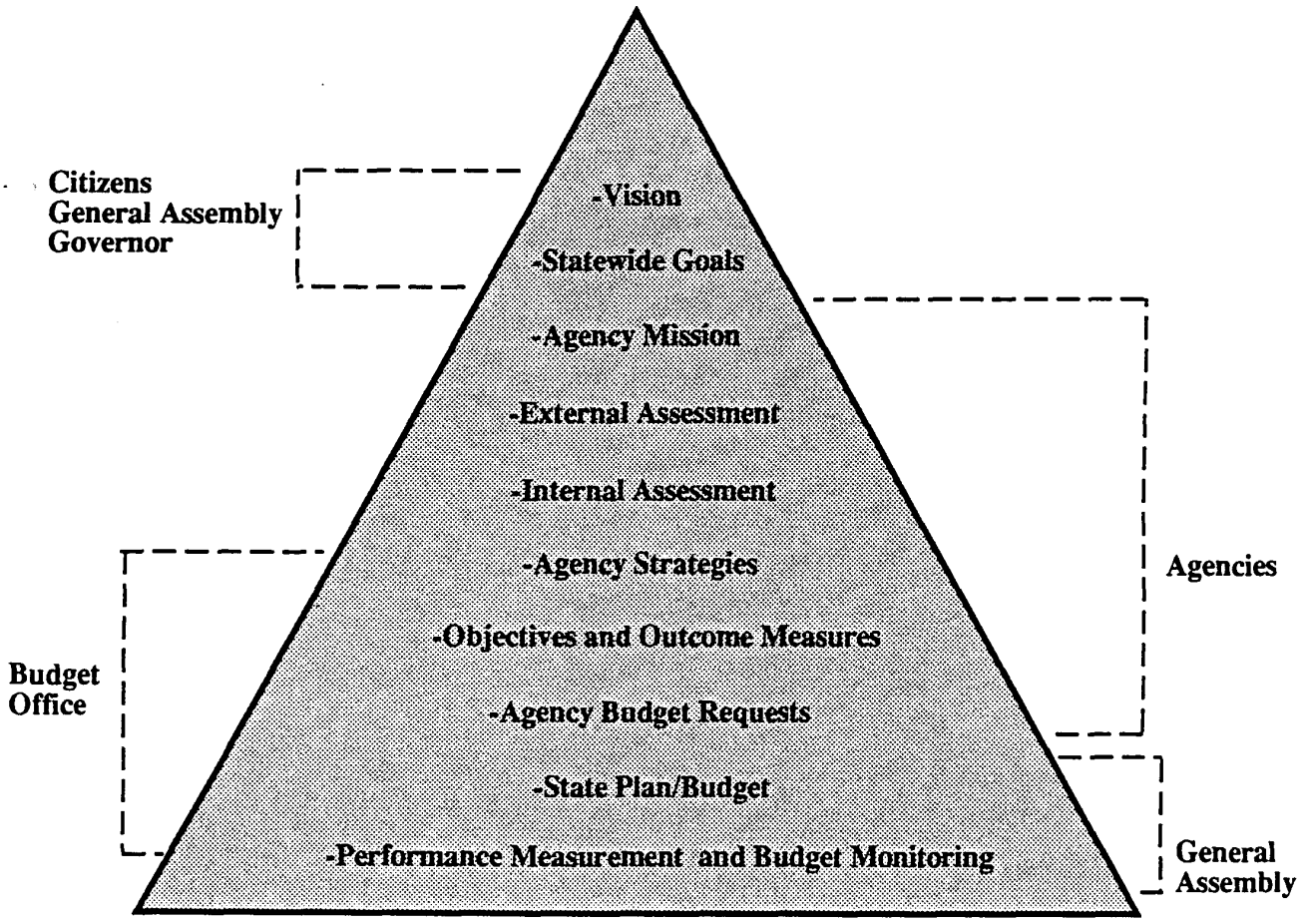
- The General Assembly's budget process makes it difficult to weigh new priorities against old priorities
- The State budgets more than is needed for salaries
- The State's budget format encourages legislators to focus on control issues rather than on government management and policy issues
- The State lacks an effective capital budgeting process

These findings and our recommendations are discussed below.

Finding 4 - The State's budget process makes it difficult for legislators to weigh new priorities against old priorities.

The Governor submits a budget document that distinguishes between expenditures for operating and maintenance (continuation budget) and funding for proposed expansion and capital improvements (expansion budget). The appropriations committees in the General Assembly consider the continuation and the expansion budgets separately. The committees first review, discuss, and sometimes vote on a continuation budget before they consider the expansion budget. Separate subcommittees review related programs.

Exhibit 3-5
Model for North Carolina Planning, Budgeting, and Program Evaluation System



North Carolina statutes require that the budget "differentiate between General Fund expenditures for operating and maintenance, special fund expenditures, and proposed capital outlays." The Executive Budget Act does not include a requirement for the separation of the budget into continuation and expansion sections. The continuation and expansion budgets are the current manifestations of a tradition that began over 30 years ago. Beginning in 1959, the Governor submitted "A" and "B" budgets, which corresponded to the present day continuation and expansion budgets. The practice of separating the continuation and expansion budgets arose during a time when revenue growth exceeded expenditure growth. Today's fiscal realities require a departure from past fiscal management practices.

The State's budget process should allow a meaningful comparison among programs. Only by weighing the benefits and costs of various programs can the General Assembly determine the best allocation of State revenue to meet the State's needs.

Placing an automatic priority on funding existing programs limits the State's ability to respond quickly to emerging needs. Under the current system, the General Assembly would not compare the relative merits of funding tuberculosis screening, an old priority, with AIDS testing and education, a new priority. Both of these communicable diseases deserve the State's attention, but AIDS is a growing problem with deadly consequences while tuberculosis has leveled off in recent decades and is treatable. With the separation of the continuation and expansion budgets, legislators are hindered from shifting the focus of the State's disease prevention program, for example, from relatively controllable diseases to emerging public health threats. A budgeting process that separates continuation and expansion budgets has the following major faults:

- Appropriations committees focus on the expansion budget (10 percent), rather than on the continuation budget (90 percent)
- Generally, the relevance or effectiveness of existing programs is ignored
- The State is hindered in shifting its resources to address emerging problems
- Obsolete programs go unnoticed and continue to be funded indefinitely

Legislators can make the best resource allocation decisions when all of the State's priorities are presented and discussed at one time. The current system favors maintaining funding for past priorities, and provides funding for emerging priorities only if funds are available. Separate subcommittees now review related programs.

The length of the legislative session and the post April 15 revenue update play crucial roles in maintaining the separation of the continuation and expansion budgets. The revenue estimate update occurs at the beginning of May, three months into the legislative session and two months before it ends. Furthermore, the revenue estimate update usually informs