

# Guidelines for State budget spending review

2026



## PURPOSE OF THE GUIDELINES

The Guidelines for State budget spending review (hereinafter – the Guidelines) have been developed to establish a unified, systematic, and transparent approach to State budget spending review, promoting efficient and economical implementation of public policy, regular optimisation of expenditure, and its alignment with the priorities and objectives set out in development planning documents.

The Guidelines define the key principles, process, and institutional framework for spending review, ensuring that during the preparation of the draft State budget law, the expenditure of each budget unit is systematically and comprehensively reviewed at least once every four years, and that the results and proposals of the review are submitted to the Cabinet of Ministers for use in State budget planning.



## REGULATORY FRAMEWORK FOR THE SPENDING REVIEW PROCESS

In accordance with the Law on Budget and Financial Management, the State budget spending review is integrated into the public financial management framework. The Cabinet of Ministers sets annual expenditure reduction targets and efficiency indicators, the Ministry of Finance provides methodological guidance, and the heads of budget units and bodies financed from the budget are responsible for achieving results.

### **Section 2. Financial Management**

(6) The Cabinet sets annual State budget expenditure reduction targets and expenditure efficiency indicators.

(7) The Ministry of Finance provides methodological guidance for the spending review.

(8) The heads of budget units and bodies financed from the budget are responsible for achieving budget expenditure reduction targets and for implementing expenditure efficiency indicators.

### **Section 16.<sup>3</sup> State Budget Spending Review**

(1) In order to implement the State policy in a more efficient and economic manner, and also to regularly optimise the budget expenditures and assess their conformity with the priorities and objectives laid down in development planning documents, the Cabinet shall ensure continuous and systematic State budget spending review.

(1<sup>1</sup>) When fulfilling the obligation specified in the first paragraph of this Section, the Cabinet shall comply with the condition that in the process of developing the draft State budget law, the expenditures of each budget unit are fully reviewed at least once every four years.

(2) The Cabinet shall concurrently take a decision on the scope of the State budget spending review and approve the schedule for the preparation of budget. The Minister for Finance shall, within the deadline specified in the schedule for the preparation of budget, submit to the Cabinet the results of the State budget spending review and suggestions for the use of these results in the process of developing the draft State budget law.



## **DEFINITION, PURPOSE, AND TASKS OF THE SPENDING REVIEW**

### **DEFINITION:**

A spending review is a continuous and systematic process of evaluating State budget expenditure, within which expenditure, processes, and policy areas are analysed to assess the efficiency, economy, and alignment of public spending with policy objectives and priorities, as well as to identify opportunities for expenditure optimisation, resource reallocation, and performance improvement.

## PURPOSE:

The purpose of the spending review is to ensure that public funds:

- are used efficiently and economically to achieve the intended objectives and results;
- are aligned with national priorities set out in development planning documents;
- promote fiscally sustainable policy implementation, taking into account their impact on medium- and long-term financing needs.

## TASKS:

The main tasks of the spending review are:

1. to evaluate and improve public administration processes, budget programmes, and policy instruments to ensure more efficient and economical implementation of public policy;
2. to analyse the structure of expenditure and the use of funding, assessing the efficiency of resource use;
3. to prepare evidence-based proposals for expenditure optimisation, resource reallocation, and policy development, based on a performance and long-term impact assessments.



## INTER-INSTITUTIONAL WORKING GROUP OF THE SPENDING REVIEW

**The inter-institutional working group** (hereinafter – the Working group) has been established to prepare and evaluate proposals for improving the efficiency, economy, and alignment of expenditure with national priorities. The Working group evaluates analytical results, discusses possible solutions, and provides recommendations to the Minister of Finance on the use of the results of the spending review in the preparation of the draft State budget law.

The Working group is established and approved by order of the Minister of Finance. The Working group includes representatives from the Ministry of Finance, the State Chancellery, and the Bank of Latvia. A representative of the State Audit Office participates as an observer. The Government's social and cooperation partners – representatives of the Employers' Confederation of Latvia, the Latvian Chamber of Commerce and Industry, the Latvian Confederation of Free Trade

Unions, and the Latvian Association of Local and Regional Governments – may be invited to the meetings.

The Working group provides recommendations to budget units, identifies horizontal topics or functions to be included in the scope of the following year's spending review, and also promotes the use of best practices in other budget units.



## STAGES, TIMELINE AND RESPONSIBILITIES FOR THE SPENDING REVIEW 2026

The spending review process is carried out in three sequential stages. In accordance with the timetable for the preparation of the draft State budget law.

<b>Stage</b>	<b>Deadline</b>	<b>Responsible institution</b>	<b>Main activities</b>	<b>Outcome</b>
<b>I. Definition of scope</b>	February - March	Ministry of Finance	Prepares a proposal for the scope of the spending review and provides methodological guidance.	Draft scope prepared
	March - April	Cabinet of Ministers	The scope is approved together with the budget preparation schedule for the following year, including the determination of expenditure reduction targets and efficiency indicators. The minimum expenditure reduction target shall take into account fiscal space requirements.	Scope and objectives approved.
<b>II. Data analysis and preparation of proposals</b>	April-July	Ministry of Finance	Carries out data analysis, reviews international practices, conducts a horizontal review of State budget programmes, reviews the funding allocated for priority measures, analyses the implementation of performance indicators and the use of allocated funding, prepares calculations and proposals.	Analytical information prepared
		Line ministries	Carry out the tasks of the Cabinet of Ministers specified in the scope, including: <ul style="list-style-type: none"> <li>➤ prepare proposals to achieve the expenditure reduction target;</li> <li>➤ review at least 25% of the planned expenditure of the basic functions of the budget unit's basic budget.</li> </ul>	Budget unit proposals prepared
		Working group	Evaluates results, discusses solutions, and provides recommendations.	Directions for solutions agreed
<b>III. Preparation of the Information report and decision-making by the Cabinet of Ministers</b>	August-November	Ministry of Finance	Prepares the Information report and its draft decision (protocol), coordinates with line ministries and relevant institutions, and submits to the Cabinet of Ministers.	Report submitted
		Line ministries	Provide proposals for the content of the Information report, comment on it, and coordinate it, including the possibility of submitting fiscally neutral proposals to ensure budget priorities.	Information report clarified/updated
		Working group	Reviews, comments on, and coordinates the Information report.	Working group opinion
		Cabinet of Ministers	Reviews the report and makes decisions.	Decisions to be included in the draft State budget law



## SCOPE OF THE SPENDING REVIEW 2026<sup>1</sup>

### **EXPENDITURE EFFICIENCY**

Line ministries shall analyse budget expenditure in the areas under their responsibility, prepare proposals for expenditure optimisation, including improving efficiency, optimising functions, evaluating public services, and implementing structural reforms, and submit them to the Ministry of Finance for consolidation and submission to the Cabinet of Ministers for consideration of possible changes to sectoral policy and funding reallocations.

### **REVIEW OF EXPENDITURE OF ALL BUDGET UNITS (4-YEAR CYCLE)**

Budget units shall annually review at least 25% of planned expenditure of the basic functions of the budget unit's basic budget, detail the expenditures down to the lowest level of expenditure units (service/measure/activity) and submit relevant information to the Ministry of Finance for inclusion in the Information report on the basis of the State basic budget and the State special budget and the results of the public spending review.

### **HORIZONTAL REVIEW OF STATE BUDGET PROGRAMMES**

The Ministry of Finance, in cooperation with line ministries, shall carry out a horizontal review of the State budget programmes, including a review of funding allocated to priority measures, as well as an analysis of performance indicator implementation and the use of allocated funding in 2025.

The objective of expenditure reductions is to improve efficiency and to redirect funds through the spending review primarily to strengthen fiscal space and finance government priorities.

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<sup>1</sup> It will be approved by the Cabinet of Ministers together with the timetable for the preparation of the draft law "On the State Budget for 2027 and the Budget Framework for 2027, 2028, 2029, and 2030".



## SCOPE IMPLEMENTATION PLAN

Given that three main directions have been defined for the 2026 scope – expenditure efficiency (including reductions), review of expenditure of all budget units (4-year cycle), and horizontal review of State budget programmes – this section provides methodological guidance for their implementation.

### EXPENDITURE EFFICIENCY

The Cabinet of Ministers sets annual State budget expenditure reduction targets and expenditure efficiency indicators.

The objective of expenditure reduction is to improve efficiency and to redirect funds obtained through the spending review primarily to strengthen fiscal space and finance government priorities.

Line ministries, when implementing expenditure efficiency (including reductions), shall also assess the necessary amendments to legislation.

#### **Line ministries:**

(1) prepare proposals to improve expenditure efficiency (including reductions) at the level of their respective budget sub-programmes – by optimising functions and public services and implementing structural reforms;

(2) report on the results and proposals at the Working group meeting.

#### **Ministry of Finance:**

(1) compile the submitted information;

(2) include information in the spending review information report for submission to the Cabinet of Ministers.

Expenditure that cannot be reduced shall be subject to an assessment of its effectiveness, insofar as the regulatory framework allows it.

It is also necessary to agree on possible policy changes, including the discontinuation of functions that have not delivered the desired results.

## REVIEW OF EXPENDITURE OF ALL BUDGET UNITS (4-YEAR CYCLE)

### PHASE I - DIVISION OF SUB-PROGRAMMES BY YEAR

To ensure that the sub-programmes of the State basic budget and the State special budget basic functions are reviewed by at least 25% each year, budget units divide the sub-programmes into four groups over a four-year cycle. At the same time, budget units retain the option to review larger amounts of expenditure or re-evaluate specific areas.

The Ministry of Finance recommends dividing sub-programmes using the Strategic Review Form. Completing the Strategic Review Form ensures a transparent classification of sub-programmes by cost and performance, enables the identification of both high- and low- performing areas, and helps determine where expenditure optimisation, reduction, or performance improvement is needed.

#### **Classification by financial capacity**

Each sub-programme is evaluated based on its share of the ministry's total expenditure (base expenditure):

**High capacity** – >10% of the unit's total expenditure;

**Medium capacity** – 4–9%;

**Low capacity** – ≤3%.

#### **Classification by performance**

Each sub-programme is evaluated based on the level of policy implementation and performance results:

**High performance** – ≥ 90%;

**Medium performance** – 50–89%;

**Low performance** – ≤ 49%.

#### **Classification of sub-programmes in the Strategic Review Form**

Sub-programmes are classified in the Strategic Review Form, which determines the next action:

**High capacity / high performance** – maintain while identifying opportunities for efficiency improvements;

**High capacity / medium performance** – carry out targeted reforms;

**High capacity / low performance** – review as a priority, assessing reduction or restructuring options;

**Medium capacity / low performance** – consolidate or optimise;

**Low capacity / low performance** – consider merging or terminating.

**BUDGET SUB-PROGRAMME ANALYSIS - STRATEGIC REVIEW FORM (PRIORITY FOR REVIEW INDICATED IN BRACKETS)**

	<b>High performance</b>	<b>Medium performance</b>	<b>Low performance</b>
<b>High capacity</b>	maintain (retain), optimise	reform	prioritise for review
<b>Medium capacity</b>	maintain (retain)	improve performance	consolidate
<b>Low capacity</b>	maintain (retain)	simplify processes	terminate or merge

Budget units submit a four-year sub-programme review plan to the Ministry of Finance, which determines the sequence of sub-programme reviews by year, including priority sub-programmes to be reviewed in the first year. In the first review year, priority is given to sub-programmes with high financial capacity and low performance.

**PHASE II - DIVISION OF SUB-PROGRAMMES INTO THE LOWEST OPERATIONAL LEVEL (SERVICE/MEASURE/ACTIVITY)**

Budget units ensure that the sub-programmes of the basic functions of the State budget, **which are planned to be reviewed in the current year**, are broken down into the lowest level of expenditure units (service<sup>2</sup>/measure/activity)<sup>3</sup>.

The purpose of analysing the lowest level of expenditure units (service/measure/activity) is to assess the cost-effectiveness of each activity, in order to justify decisions on its maintenance, improvement, consolidation, or termination.

Services, measures, or activities are identified based on regulatory enactments, documents regulating the activities of ministries, and development planning documents, by defining the content, purpose, and expected results of each service, measure, or activity.

As part of the analysis, budget units shall assess the following aspects:

- **need for the service/measure/activity - relevance** (whether the service/activity/measure is necessary and justified);
- **performance of the service/measure/activity - effectiveness** (what results are achieved);

<sup>2</sup> Budget units shall primarily identify the services provided under the sub-programme as registered in the State Information Resources, Systems and Interoperability Information System (VIRSIS).

<sup>3</sup> The Ministry of Finance shall prepare an information request in the necessary detail for budget units.

- **costs of the service/measure/activity** (what is the cost of implementing the service/measure/activity, if possible - unit costs);
- **alternatives** (whether the service/measure/activity can be delivered in a different way or at lower cost).

**Evaluation of alternatives:** digitalisation, centralisation/shared services, outsourcing, merging with other functions, policy change or termination.

### PHASE III DETAILED ANALYSIS OF BUDGET SUB-PROGRAMMES (ECC<sup>4</sup> LEVEL)

Budget units carry out **an in-depth analysis of the services/measures/activities** of budget sub-programmes, **allocating expenditure to the Economic Classification of Expenditure (ECC)<sup>5</sup>** and carrying out a cost analysis to support decisions on maintaining, optimising, reallocating, or reducing expenditure.

As a result of the analysis, budget units identify ECC items and classify them according to their impact on the achievement of service/measure/activity objectives, distinguishing between essential expenditure, expenditure that is transparent and efficient, and expenditure that can be reduced or discontinued without affecting the achievement of those objectives.

#### Framework for evaluating the economic classification of expenditure (ECC) for services/measures/activities

Expenditure to be reduced	<b>Red</b>	Expenditure that can be reduced or discontinued without affecting the objectives of the service/measure/activity	Prepare proposals for reduction or discontinuation
Reviewable expenditure	<b>Yellow</b>	Expenditure that can be made more efficient or optimised while ensuring that the objectives of the service/measure/activity are met	Assess opportunities to improve efficiency and reduce costs
Essential expenditure	<b>Green</b>	Expenditure that is directly and critically necessary to achieve the objectives of the service/measure/activity	Maintain at the current level; no reduction is permitted without significant impact

As a result of the analysis, budget units, the Ministry of Finance and the Working group obtain information on the allocation of expenditure to ECC items for the

<sup>4</sup> Economic Classification Codes

<sup>5</sup> three-digit ECC

implementation of services, measures, and activities, as well as an assessment of their justification, effectiveness, and relevance.

#### **Evaluation of each ECC item identified as service/measure/activity expenditure:**

1. How important is the role of the ECC in achieving the objective of the service/measure/activity?
2. If the level of the ECC were reduced by 10–30%, what would be the impact on the result?
3. To what extent can expenditure be reduced in the short term (1–3 years)?
4. Can these costs be replaced by a more efficient solution? Assess the feasibility of replacing ECC expenditure with more efficient or alternative solutions (e.g., process digitalisation, remote solutions, outsourcing, etc.).
5. Are the costs proportionate to the results achieved? Assess whether the volume of ECC expenditure is proportionate to the results achieved (value for money). Are there opportunities to improve the efficiency of expenditure or optimise it?

In the process of evaluating and compiling the submitted information, the Ministry of Finance and the Working group may request additional and clarifying information from budget units.

#### **PILOT MINISTRIES – SYSTEMATIZATION OF SERVICES<sup>6</sup>**

By August 15, 2026, the Ministry of Finance, the Ministry of Economics and the Ministry of Transport shall systematize the public administration services of their budget units and determine the costs of achieving results for inclusion in the explanations to the draft law "On the State Budget for 2027 and the Budget Framework for 2027, 2028, 2029 and 2030", as well as apply the principles of the "zero-based budgeting" approach to the budget sub-programmes of their budget units in a pilot project at the level of specific policy areas, which constitute at least half of the expenditure of the State basic functions programmes of the budget unit.

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<sup>6</sup> Minutes of the Cabinet of Ministers meeting No. 45 of 28 October 2025 – Paragraph 36

## **HORIZONTAL REVIEW OF STATE BUDGET PROGRAMMES**

The Ministry of Finance carries out a horizontal analysis of data by reviewing all State budget programmes according to the same criteria, including:

- ❖ analysis of priority measures for which funding has been allocated for 2025–2027;
- ❖ analysis of performance indicators and allocated funding;
- ❖ analysis of expenditure efficiency index<sup>7</sup>;
- ❖ international comparisons.

In carrying out a horizontal analysis, the Ministry of Finance takes into account the information submitted by the relevant budget unit and proposals to reduce expenditure when calculating the amount of expenditure reductions.

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<sup>7</sup> It is calculated by looking at the level of execution of the basic budget performance indicators (DRR)/the level of execution of basic budget expenditures (%).