# PART III IRELAND'S PUBLIC EXPENDITURE FRAMEWORK IN COMPARATIVE PERSPECTIVE

## Introduction

The Government is committed to returning Ireland's public finances to a sustainable path and to ensuring that they remain on such a course into the future. The reforms to the expenditure budgetary architecture, announced in the *Comprehensive Expenditure Report 2012-14*, are one element of this commitment. These reforms establish a framework for effective and efficient multi-annual expenditure management that will support better decision making and value for money.

This section of the *Expenditure Report 2014* sets Ireland's public expenditure framework in the context of international experience.[5] It is vital to assess this system on an on-going basis against international experience to ensure any necessary changes are made in a timely and appropriate way.

## International Experience of Key Elements of Effective Public Expenditure Management

An effective public expenditure framework has several key elements. First, there needs to be a clear statement of the overall volume of resources available and how these are to be allocated to individual spending areas over a number of years. Second, in order to be in a position to determine these allocations there is a need for regular reviews of expenditure programmes that take account of whether or not programmes are delivering against the targets set for them, changes in government priorities and proposals for new expenditure programmes. Third, reviews of expenditure programmes should be informed by relevant evaluations of the effectiveness and efficiency of programmes and agencies. Finally, evaluations should be based on information relating to how well programmes have been performing over a number of years.

### *Medium Term Expenditure Framework*

The overall context of public expenditure is set by the amount of money a State is able to raise through taxation and borrowing. In order to live within these limits, many OECD countries have put in place medium term expenditure frameworks that set out expenditure ceilings for government-as-a-whole and individual Departments; typically for a period of between three and five years. Finland, the Netherlands and Sweden have been at the forefront in Europe in terms of developing multi-annual budgeting approaches.

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[5] In particular, this section draws on OECD (2011) *Government at a Glance 2011*; OECD (2013) Spending Reviews, Paper for the Annual Meeting of OECD Senior Budget Officials, Paris, 3-4 June 2013, OECD GOV/PGC/SBO(2013)6 [Paper prepared by Marc Robinson]; and Marc Robinson (2013) "Aggregate expenditure ceilings and allocative flexibility", OECD Journal on Budgeting, Vol. 12/3. It also draws on Department of Finance (2011) *Reforming Ireland's Budgetary Framework: A Discussion Document*.

New rules introduced by the European Union over the past few years impact on the wider context in which Ireland's resource allocation decisions are made (i.e. a 'balanced budget rule', a 'debt brake', an automatic correction mechanism, stronger surveillance by the EU, more robust sanctions for non-compliance and a common budgetary timetable). These rules also constrain public expenditure because each Government in the Eurozone is now bound by the 'expenditure benchmark' which means that growth in General Government Expenditure is linked to the potential real growth of the economy and is fixed for three years. Expenditure will not be allowed to grow by a rate that is faster than economic growth unless offsetting permanent tax increases are introduced. In Ireland, following on from its expenditure benchmark, the Government must set a 'Government Expenditure Ceiling' which is the maximum volume of financial resources that it can use in each of three years. The Government then decides upon the share of the overall expenditure ceiling across Government Departments. These Ministerial Expenditure Ceilings will also be set for three years.

This top-down approach to setting Departmental spending ceilings ensures the allocations decided in the budgetary process are consistent with aggregate fiscal objectives. The multi-annual approach provides clarity about the resources Departments will have available over a number of years and reinforces fiscal discipline, as decision makers and the public are aware of the budgetary parameters. Such an approach should also facilitate a more strategic approach to resource allocation by emphasising prioritisation of key services over reaction to day-to-day pressures.

The credibility of any medium term expenditure framework rests on how it balances the need to be firm and yet responsive. An overly mechanistic framework could be unresponsive to needs, changing priorities or unexpected challenges, whereas an overly flexible system will be seen as a paper exercise rather than real expenditure control. There is also a need to be cognisant of 'demand led' schemes that are sensitive to variation in economic performance (e.g. social protection payments).

### ***Spending Review***

Spending reviews are used to examine all areas of public expenditure in order to give the Government improved information to inform its decisions on the level of aggregate expenditure and the relative priority of expenditure programmes.

Since the beginning of the economic crisis, spending reviews across OECD member countries have become associated with identifying large numbers of specific savings proposals. The UK's 2010 *Comprehensive Spending Review* covered nearly all government expenditure as well as tax expenditures. Some spending reviews set savings targets. For instance, the Canadian *Strategic and Operating Review* process required agencies to present options for a 10% cut from their lowest-priority, lowest performing programme spending. The Dutch *Comprehensive Expenditure Review* of

2010 required the development of options capable of delivering at least a 20% reduction in expenditure over a four-year period.

However, spending reviews should not be regarded only as a tool of reducing budgets. Instead, the OECD (2013: 31) suggests that they should be a permanent feature of the budget preparation process as a core instrument for ensuring good expenditure prioritisation. In the years prior to the economic crisis, three OECD countries already carried out spending reviews on an on-going basis: *Interdepartmental Policy Reviews* in the Netherlands, *Special Studies* in Denmark and *Productivity Program* in Finland. (OECD, 2013: 9) Spending reviews have been used to examine how to accommodate new spending proposals. The primary budgetary objective of the Canadian *Strategic Reviews* was to create additional fiscal room for new spending initiatives and, consistent with this, spending ministries were permitted to present options for new spending that could be financed by savings ("reinvestment proposals"). In Denmark, typically between 10-15 special studies were carried out each year and, up until the recent crisis, these focused on increasing the space for new expenditure priorities. (OECD, 2013: 10, 13)

***On-Going Evaluation***

Many countries have guidance and rules in place to ensure that policy decisions are underpinned by a solid evidence base and that the effectiveness and efficiency of resource allocation is maximised (e.g. the *Green Book* in the UK and the *Guidance and Instructions on Public Sector Performance and Financial Management System* in New Zealand). From the 1970s to the 1990s, many OECD governments undertook efforts to build government-wide evaluation systems but the use of evaluation for budgeting purposes proved disappointing as these tended to focus upon management / policy improvement objectives rather than budget decisions and failed to provide timely or conclusive information to managers (Robinson, 2013).

To be fully optimised, spending reviews require relevant, timely and high-quality evaluations of expenditure programmes. The absence of such evaluations has meant that spending reviews have had to rely upon quite informal expenditure analysis. There is also a growing acceptance that the evaluation groundwork should be undertaken over the longer period outside the formal spending review process as tight timetables of the latter mean that it is often very difficult to deliver high quality evaluations. For example, in Australia, the Expenditure Review Committee of Cabinet commissions *Strategic Reviews* of programmes and processes and, while generally not required to recommend options for budget decisions, the better quality information that they provide is used to inform the Government's options. (OECD: 26-27)

### *Performance Budgeting and Performance Information*

The most widespread form of performance budgeting classifies expenditure by "programmes" based on objectives and types of services and include performance information in budgetary documentation. While the main objective of this approach is to improve expenditure prioritisation, the OECD (2013: 29) notes that the reality internationally has been one where decision makers have shown limited desire to become fully engaged in expenditure reallocation, resulting in performance budgeting systems that are "all dressed up with nowhere to go". Furthermore, it has been seen more as a matter of "filling" budget documents with performance indicators than of ensuring the relevance of those indicators for budgetary decisions.

The OECD suggests that the economic crisis provides an opportunity for performance budgeting to demonstrate its true worth as a tool for expenditure prioritisation. Performance information will not by itself provide clear and conclusive decisions. Instead, it is the evidence that informs relevant, timely and high-quality evaluations of the effectiveness and efficiency of the ways in which public resources are allocated.

## Ireland's Public Expenditure Framework

Over the last number of years, Ireland has introduced a number of changes to its budgetary architecture. Some of these changes are a consequence of new EU rules while others build on the Government's determination to ensure sustainable public expenditure by developing and linking existing procedures with new mechanisms that taken together will enhance overall public expenditure management. Together, these developments will mean that public services in Ireland will be delivered efficiently and effectively while ensuring a sustainable medium term fiscal path.

### *Medium Term Expenditure Management*

The reformed Stability and Growth Pact (SGP), including the so-called 'six-pack' and 'two-pack' of EU Regulations and one Directive, have introduced significant changes to the way in which EU Member States manage public resources. This was complemented by the *Treaty on Stability Coordination and Governance in the EMU* ("Fiscal Compact"), which was ratified by referendum in 2012. In Ireland, these changes have been placed on a statutory footing by means of the *Fiscal Responsibility Act 2012 and 2013* and the *Ministers and Secretaries (Amendment) Act 2013*.

Ireland's Medium-Term Expenditure Framework and the Ministerial Expenditure Ceilings operate within the broader expenditure control context arising from the reforms of the Stability and Growth Pact (SGP).

The *Fiscal Responsibility Act 2012 and 2013* imposes a duty on the Government to ensure compliance with the budgetary rule and the debt rule, which are provided for in the Act. The budgetary rule requires that the budgetary position of general government must be either:

- In balance or in surplus and this will be satisfied if the annual structural balance is at the medium-term budgetary objective (MTO); or

- If it is not at the MTO target, on the adjustment path towards adhering to the MTO as set in accordance with the Stability and Growth Pact.

In the event of exceptional circumstances, as defined under the SGP, this rule may not apply.

If there is a failure to comply with the budgetary rule and there is a significant deviation from the MTO or the adjustment path, then the Government will be required to implement the correction mechanism and introduce a plan to restore compliance.

Reforms to the SGP also introduced a complementary expenditure measure known as the Expenditure Benchmark that aims to link the changes in expenditure with growth in the economy. Through application of the Expenditure Benchmark, which takes into account decisions in relation to discretionary revenue measures, a multi-annual upper limit on General Government expenditure is determined,[6] which is the basis in Ireland for setting the Government Expenditure Ceiling. Essentially, the Government Expenditure Ceiling is equivalent to total gross voted expenditure. The *Ministers and Secretaries (Amendment) Act 2013* provides that, upon a proposal of the Minister for Public Expenditure & Reform, the overall Government Expenditure Ceiling shall be apportioned into individual Ministerial expenditure ceilings for both current and capital expenditure for the next three financial years.

An overview of Ireland's obligations under the reformed SGP and the new domestic fiscal framework are set out in a Circular issued by the Department of Public Expenditure and Reform[7]. This Circular also details the rules and arrangements for the management of Government Expenditure Ceilings and Ministerial Expenditure Ceilings, including the carryover of savings from one year to the next and also sanction mechanisms to ensure compliance with the ceilings.

The challenge over the next few years will be to ensure that there is a robust system in place to best inform the allocation of the available resources across the various Departments so that the full

[6] For more details on the expenditure benchmark, please see the *Vade Mecum on the Stability and Growth Pact*, available at http://ec.europa.eu/economy_finance/publications/occasional_paper/2013/op151_en.htm

[7] http://circulars.gov.ie/pdf/circular/per/2013/15.pdf

benefits of this multi-annual approach to budgeting can be realised. Robinson (2013) examined the implementation of expenditure ceilings in OECD countries and noted that developing a strong spending review capacity should be seen as a prerequisite for moving to multi-year expenditure planning.

### *Spending Reviews*

Since the onset of the economic crisis, Ireland has had spending reviews of both current and capital expenditure.

In the area of current expenditure there have been two large-scale exercises resulting in the *Special Group on Public Service Numbers and Expenditure Report* (2009) and the *Comprehensive Expenditure Report 2012-2014*. Both Reports set out recommendations for making savings that informed subsequent Budgets and involved line Departments producing their own papers. In the case of the *Special Group* these papers were considered by the Group before making its recommendation while the *Comprehensive Review of Expenditure* was more akin to the process which takes place in Canada.

In support of both spending reviews, the Central Expenditure Evaluation Unit in the Department of Public Expenditure & Reform provided evaluations of cross-cutting issues that were relevant to a number of Departments (e.g. labour market activation, enterprise supports, science and innovation funding).

In relation to Government capital expenditure, there have been a number of reviews of in Ireland, the most recent of which was carried out in parallel with the *Comprehensive Review of Expenditure*. This review was led by the Department of Public Expenditure & Reform and involved a Government-wide review of the Exchequer Capital Programme in 2011. It contributed to a reprioritisation of capital investment and the publication of *Infrastructure and Capital Investment 2012-2016: Medium Term Exchequer Framework* in November 2011.

The next *Comprehensive Review of Expenditure* will begin in the coming months. Again this will be a line-by-line examination of current expenditure across all expenditure programmes. This *Comprehensive Review of Expenditure* will build on the experience of conducting the previous spending reviews. It will inform Government decisions on future budgetary matters and allow for the Government's reviews and recalibration of ministerial expenditure ceilings in light of changing priorities and evaluations of expenditure. In parallel with this process a review of the medium term capital investment programme will also take place over this period.

### ***On-Going Evaluation***

For many years, Ireland has had processes, procedures and guidance to ensure public money is well spent These arrangements were put in place to promote evidence-based rigorous evaluation and scrutiny of how public resources are used to maximise public welfare and eliminate waste and inefficiency. The *Public Spending Code*[8] has brought together and updated all of the guidance, instructions and Value for money requirements for public expenditure. Departments and agencies must now adhere to these reformed standards across the appraisal, implementation and review activities involved in the different stages of the expenditure life cycle.

It is important to have in place methods for examining expenditure both before and after the allocation of public resources. While appropriate methods have been developed and long used for capital expenditure, evaluations of current expenditure have tended to focus more on how well or otherwise these resources have been utilised rather than on *ex-ante* analysis of new spending proposals. . The implementation of the *Public Spending Code* means that current expenditure proposals are now required to set out relevant evidence and develop business cases. Proper completion of economic analysis at the appraisal stage of expenditure will ensure that there is a clear focus on the intended benefits of a proposed programme. It should also facilitate the integration of appropriate data collection procedures to support cost effective evaluation activities at later stages.

The experience of the two spending reviews, as well as the wish to address limitations of the *Value for Money & Policy Review* process, has informed the development of the *Public Spending Code,* which now includes a further new approach to evaluation via Focused Policy Assessments (FPAs). The FPAs provide shorter, more focused analysis of public expenditure programmes and are particularly useful in addressing issues that cut across a number of Departments or as preliminary assessment that can lead to more complex analysis.

The Irish Government Economic Evaluation Service (IGEES) has been established to enhance the capacity of the Civil Service to undertake evaluations of public expenditure, to provide economic analysis, and to improve the analytical resources available in the design and formulation of policy.

### ***Performance Information***

The performance budgeting initiative has involved a significant reformulation of the Estimates documentation. It has also allowed for the development, on a pilot basis, of the *Ireland Stat*[9] website,

[8] http://publicspendingcode.per.gov.ie/

[9] http://www.irelandstat.gov.ie/

which the Government has decided to extend to all Government Departments. Work is currently on-going to gather relevant and appropriate data.

The aim of the performance budgeting initiative is to strengthen the focus upon what is being delivered with public resources and to build this information into the policy-making process. The inclusion of performance information in the Estimates documentation is intended to support the Oireachtas' examination of the Estimates by providing members of Select Committees with key relevant information about what services are being purchased with public money and the impacts of these services for Irish citizens and for Irish society in general. This information is also intended to contribute to Select Committees *ex ante* discussions of resource allocations as part of the 'whole of year' budgetary process. The development of the *Ireland Stat* website will support the more efficient delivery of evaluation work as it locates, on a single platform, key information that can otherwise only be sourced from a diverse range of publications.

In terms of developing this initiative, the Institute of Public Administration (2013) notes that while significant progress has been made, there are still data gaps and shortcomings, and work will be needed to enhance the quality and relevance of the data. For instance, there is an over reliance on general statements of intent rather than specific, measurable or assessable output targets. Other countries do not include discrete targets in their performance budgeting initiatives (e.g. restructuring of functions or delivery of heads of bill) as these do not allow any monitoring of trends over time. As noted earlier, the experience of other countries is that there is a challenge with ensuring that this type of information is used in arriving at budgetary decisions.

**Conclusion**

It is clear now that Ireland has in place the key elements of a system that will provide for the examination of public expenditure effectively. The Medium Term Expenditure Framework is now supported by legislation and will set the overall context of expenditure decisions. Spending reviews have proven themselves to be a useful means of identifying specific savings options for Government. They also have the potential to be developed in a way that informs expenditure prioritisation and decision making through the years ahead. There has also been significant progress in putting in place a systematic way of collecting and presenting performance information to inform not only those responsible for resource allocation decisions but also Irish citizens; though there is a need to improve the quality and usefulness of the information. The various elements of the public expenditure framework mean that decisions around Irish public expenditure are no longer simply concerned with competing demands for additional resources, but are also focused on the use to which these resources are being put and the impact they are having on people's lives.