Finance Committee

Review of the Budget Process

Submission from Professor Arthur Midwinter

Introduction

1. The annual budget is a key instrument of parliamentary accountability for public finance, and a mechanism for political choice over expenditure priorities. This Memorandum responds to some of the issues raised in the Committee’s Consultation Paper, through a focus on the budget document itself.

2. In my five year period as Budget Adviser to the Committee, my key role was to seek to strengthen the robustness and transparency of the budgetary information provided to Parliament by the Scottish Executive. Progress with this task was greatly assisted by the constructive relationship between the Finance Committee and Finance Ministers during this period. My approach as Adviser was to provide constructive criticism to improve budgetary practice. This is the approach used in this Memorandum.

3. This review exercise provides me with the opportunity to express my concerns over the reduction in the quality and transparency of the information presented in the revised format adopted by the new Scottish Executive in the Scottish Budget for Spending Review 2007, which was apparently adopted without prior consultation with the Parliament.

4. My approach, therefore, focuses largely on the budget information provided in Stages 1 and 2 of the process. The Consultation Paper does raise important procedural issues in relation to budget scrutiny and approval which are important for ensuring Parliamentary support for the budget, particularly in the context of a Parliament of minorities.

5. Whilst FIAG recommended a power-sharing approach to the budget between public, Executive and Parliament, and the procedures adopted have facilitated greater parliamentary input to the process, nevertheless the process remains dominated by the Scottish Executive’s control of information and the largely consultative role of Committees. This is a particular concern in a context of a minority Executive, and the review provides an opportunity to develop Parliament’s role in budget decision-making, rather than simply making recommendations as at the moment.

6. This Memorandum suggests ways in which the parliamentary input could be strengthened through the development of more relevant information, focussed on the margins of choice.

7. The previous Executive inherited a budgetary model in which a very detailed set of objectives and targets were published in the Scottish Office’s Annual Expenditure Planning Report. This contained 406 targets. Following Spending Review 2002, the Executive modified the budget documents into a
format similar to Public Service Agreements in Whitehall. In 2004, further rationalisation took place, eliminating most of the process-based targets, leaving a mix of outputs/outcome measures. This approach was intended to enhance financial and performance reporting, and did so in some portfolios. Budget strategy, and the setting of strategic priorities and targets, remained problematic. The incorporation of efficiency targets in Spending Review 2004 further blurred lines of accountability.

Problems in Stage 1

8. In principle, Stage 1 of the budget process should occur every second year, and focus on the Annual Evaluation Report (AER). This allows performance reporting against past targets, and a discussion of strategic priorities for the next Spending Review period. In previous documents, the Executive made a concise statement of its spending priorities in the introduction.

9. Strategic priorities should be based on major crosscutting issues, which provide a basis for judging competing bids for resources from portfolios, in terms of their contribution to the Executive’s wider objectives. In his foreword to the new Scottish Budget, Mr. Swinney reports the Executive’s “purpose” as “to focus our resources” on the prime objective of “increasing sustainable economic growth”. It also sets out five strategic objectives to deliver this “purpose”. These are a “wealthier and fairer, smarter, healthier, safer and stronger, and greener Scotland”. The remainder of the opening section provides a narrative of how departmental programmes are contributing to these objectives.

10. A major gap in the document, however, is any exposition of how the budgetary allocations have been targeted on these objectives, to show that these objectives have actually been allocated priority funding.

11. The Spending Review states that the Executive’s approach, with a further nine purpose targets, fifteen national outcomes and forty-five performance indicators, focuses resources in a new way, linking government activity to outcomes through the alignment of public policy and resources.

12. In fact, there is nothing new in this approach at all. The five strategic objectives, which broadly relate to ministerial portfolios, are so vague that any programme could be presented as a priority. These objectives are very similar to the five priorities set out in the 2002 Spending Review, which Audit Scotland described as a hierarchy of policy aims and programmes with output measures and other milestone indicators so that progress against the plans can be measured.

13. In the new budget, the key difference is that there is no direct link between budgets and outcomes, as the National Performance Framework is set out in a separate chapter from budgets, compared with the objectives and targets set for each portfolio in the previous document.
14. The underlying assumption is that all programmes contribute to the strategic objectives and national purpose, but there is no evidence in the document to support that view.

15. This fundamental weakness in the format was commented on by several Committee expert advisers. One of the Finance Committee’s key tasks is to scrutinise budget priorities – how overarching objectives are met by budget allocations across portfolios. It is not the Committee’s task to suggest alternative priorities, but to scrutinise and monitor the effectiveness with which the Executive targets priorities in the budget.

16. The Executive fails to demonstrate how it has achieved this. As the Budget Adviser reported, some aspects of the budget were not consistent with increasing “sustainable economic growth as the primary aim of government strategy”, and further “it is not yet clear whether the move towards outcomes-focussed management of public sector bodies will deliver the hoped for improvement in economic performance”.

17. This remains the case. Another senior economist, Peter Wood, gave consideration to the “fit” between the resource allocation priorities implied by the budget and the economic strategy. His analysis was that “most of the spending areas relevant to economic growth are set to grow at a slower rate than the budget as a whole”, and “that some are set to decline”. In other words, programmes linked to economic growth were not budget priorities.

18. A third adviser, Professor Bebbington, a specialist in sustainable development accounting, similarly observed that

“In an effective outcome budgetary system that mainstreams sustainable development, it would be expected to see clear and explicit logic links between high level outcomes, intermediate outcomes, output measures, actions, input measures, and budget resources. Unfortunately, nowhere is there such a clear link between these critical components.”

19. Professor Bebbington then further argues that such links are necessary to facilitate scrutiny, and the provision of estimates of spending on the strategic objectives. There is no systematic linkage and alignment between resources and results as claimed in the document.

20. This is consistent with evidence presented to the Finance Committee by the Executive’s Chief Economic Adviser. In Draft Budget 2005-6, despite being pressed by the Committee to set a target for its top priority – economic growth – the Executive declined to do so, as the economy “is heavily influenced by economic performance worldwide, and the global economic cycle. It would not be credible to claim specific changes in GDP were directly linked to specific Executive spending” (p181).

21. I agree with this judgement. Although there are now growth targets, the Spending Review 2007 assertion that every action of government is aligned to support the national purpose is, frankly, nonsense. Moreover, it raises serious
doubts over the merits of adopting, as a top priority, a target for which the Executive has no responsibility, and few policy levers with which to influence it.

22. The current set of budgetary priorities is not fit for purpose. It does not provide a meaningful framework for resource allocation, and does not provide the analysis of spending allocations necessary for rigorous scrutiny by the Committee.

23. Section 2 of the Scottish Budget sets out the spending priorities and plans for each portfolio. The new Scottish Executive was heavily critical of its predecessor for a lack of clear priorities, drawing on the Howat Report’s review of the budget, and the First Minister told the Parliament (23rd May 2007) that his government will be more “strategically focussed”, and “break down the boundaries and borders that exist in government”.

24. The Executive has reduced the numbers of ministerial portfolios in the budget. But despite this efficiency rhetoric, it has increased the number of portfolio priorities from 78 to 110. Moreover, 26 of them are within the portfolio of the Finance Minister who also has responsibility for expenditure programmes – not a particularly sensible combination in a period of slower expenditure growth.

25. The First Minister may claim to lead a strategically focussed government, but this is not reflected in the budget documents, making Parliament’s scrutiny role more difficult. A more systematic approach to setting strategic budgetary priorities is needed.

Problems with Stage 2

26. Stage 2 of the process is concerned with authorising the Executive’s detailed spending proposals, and making alternative spending proposals if discontented with the Executive’s response to its Stage 1 Report. Whilst only minor recommendations – mostly on a consensus basis – were made by Parliament over the 2004 Spending Review, it is clear that the Executive responded positively to most of these. In the context of minority government, formal moving of amendments increased in the 2008-9 Budget round.

27. Changes to the budgetary format reduced the transparency of the budget, made it more difficult to monitor changes, and constrained the budget choices open to Parliament. A significant reduction of Level 3 budget lines was made without prior consultation with Parliament, and this process of consolidation often resulted in a new name for the budget line. In a tight timescale, this meant Committees has to pursue the relevant information to attempt to track spending changes.

28. A further regressive change was the removal of GAE information from the budget, and the rolling up of 43 specific grants into the block grant to local government. This is the Executive’s assessment of what councils need to spend to provide a standard level of service in the current statutory and policy context. Without them, Parliament cannot tell what provision has been made to meet national priorities in the grant settlement.
29. That is why GAE figures were repeatedly asked for by Subject Committees and introduced formally into the budget in SR2004. Removing them makes it easier for the Executive to evade scrutiny. This is highlighted in the local government chapter, where eleven uncosted spending commitments are listed, and already the Executive and COSLA have made conflicting statements over what councils are expected to deliver within the funding package.

30. The result is that Parliament has endorsed £11 billions of finance for the delivery of uncosted service developments through three budget lines with scant information on services. This format is in contradiction to the agreement between Parliament and the Executive, which requires a set of programme aims, objectives indicators and targets, when, as noted earlier, there is no link between budgets and performance indicators.

31. The Finance Minister believes this gives authorities freedom to focus on outcomes. This is difficult to take seriously. Only around 10 of the 45 indicators in the Performance Reporting Framework are actually outcome measures, and half these are health indicators (see Appendix One). These are not linked to budgets, so Parliament has approved an £11 billions budget without being told what it will purchase, at what price, and what impact it will have. Moreover, the Single Outcome Agreements are not yet in place. This is budgeting in the dark.

32. Moreover, the guidance issued regarding Single Outcome Agreements acknowledges that “an organisation or service is unable to control outcomes”. This completely undermines the outcome budgeting model, which outlines a process linking budgets to inputs to outputs to outcomes, on a programme basis. Such links are even more difficult to make within block grants.

33. Parliament has endorsed a budget format which has reduced the volume and transparency of budgetary information, which fails to provide information on objectives and targets on a programme basis as agreed between Parliament and Executive and which utilises a National Performance Framework which is not fit for purpose, has failed to link resources with results, and which provides an inadequate basis for parliamentary control of expenditure.

Conclusions

34. The revised budgetary format introduced by the new Scottish Executive without prior consultation has reduced the transparency of the budget documents and made rigorous scrutiny more difficult in practice. In the Scottish Budget, it is not clear how strategic priorities are reflected in the budget, despite the exaggerated claims of ministers that policy and resources are aligned to deliver the overarching purpose of sustained economic growth. Spending allocations are no longer linked directly to outputs, and the outcome focus claimed by the Executive is not delivered in practice, as the National Performance Framework contains few genuine outcome measures.
35. There is considerable scope for improving both the rigour and the transparency of the budget document, which is necessary if the sharing of power sought by FIAG, and endorsed by the Parliament, is to be achieved.

36. Firstly, in Spending Review years, there should be a statement of budget strategy, focussed on strategic objectives, but using fewer than at present, to make priority setting meaningful. With the current vague strategic objectives, almost any spending programme could be regarded as a priority. Setting clear priorities within the control of the Executive is a major gap in current practice. Making economic growth the overarching objective for a devolved administration with only microeconomic functions is misleading the public. The SNP Administration has set a target which is a poor measure of economic performance, and which its economists have stated cannot be linked to budget allocations. Setting realistic priorities which it can influence would be a major step forward.

37. Secondly, the budget strategy should make explicit what the Executive means by a priority, and show how this is reflected in the budget. This should be focussed on changes at the margins, through budgetary growth and redistribution, where effective choices lie, and not by simply rehearsing triple counted budget lines for existing programmes.

38. Thirdly, especially in the context of the Best Value regime, and the application of efficiency savings, each programme should present budgetary and output baselines, showing how additional inputs will enhance levels of output, or vice-versa, if budgets are reduced. The current approach to reporting efficiency savings should be improved or dropped. There are few genuine efficiencies, and the lack of output baselines makes them impossible to scrutinise properly.

39. Fourthly, the present orthodoxy for outcome measures should be removed from budget documents. If outcomes cannot be robustly measured, and integrated with resource allocation, then they are not fit for purpose in a budgetary document, and accountability is blurred by the pretence that they are meaningful, or have any influence on budget decisions.

40. Fifthly, proposals for new spending should be set out as a menu of policy options for Committees, rather than as plans for ratification. These should be fully costed, the expected outputs set out clearly, with the option’s contribution to wider budget strategy explained. The growth items should allow choice to members. The Executive should retain the right to amend these decisions in the budget bill if it can persuade a parliamentary majority to its view.

41. Sixthly, such Committee decisions should be considered by the Finance Committee from a strategic perspective, to assess their consistency with agreed priorities.

42. These changes would convert parliamentary control of expenditure from a theory of the constitution to a political reality. Ministers would have to convince and persuade Committees to support their preferred options rather than simply reporting and defending them as at present.
43. A budget process in which Committees took decisions and chose from options, rather than simply making recommendations, would be a real sharing of power between Executive and Parliament, and reflect the political reality of a Parliament of minorities.

Arthur Midwinter

April 2008

Professor Midwinter retired as Dean of the Faculty of Arts and Social Sciences at the University of Strathclyde in 1999, and was awarded an Emeritus Professorship at that time. Since then, he has divided his time between research and consultancy in public finance. He was appointed Visiting Professor at the Institute of Public Sector Accounting Research at the University of Edinburgh in 2004, and was Budget Adviser to the Finance Committee of the Scottish Parliament from 2002 to 2007. He has also been a consultant to the Northern Ireland Assembly, the London Assembly, the Government of South Africa, and a range of Scottish councils, health boards, and public sector bodies, and is currently a consultant to Labour in the Scottish Parliament.
## APPENDIX ONE

### OUTCOME INDICATORS IN THE

### NATIONAL PERFORMANCE FRAMEWORK

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<tr>
<td>1</td>
<td>NI 5</td>
<td>Increase the percentage of Scottish domiciled graduates from Scottish HEIs in positive destinations. (Outcomes 2 &amp; 3)</td>
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<td>2</td>
<td>NI 7</td>
<td>Increase the proportion of school leavers in positive and sustained destinations (Outcomes 2 &amp; 4)</td>
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<td>3</td>
<td>NI 10</td>
<td>Decrease in the proportion of individuals living in poverty. (Outcome 2)</td>
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<td>4</td>
<td>NI 11</td>
<td>60% of school children in P1 will have no signs of dental disease by 2010. (Outcome 5)</td>
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<tr>
<td>5</td>
<td>NI 14</td>
<td>Reduce the rate of increase in the proportion of children with their body mass index outwith a healthy range by 2018. (Outcomes 5 &amp; 6)</td>
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<tr>
<td>6</td>
<td>NI 15</td>
<td>Increase the average score of adults on the Warwick-Edinburgh Mental Well-Being scale by 2011. (Outcomes 6 &amp; 8)</td>
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<td>7</td>
<td>NI 16</td>
<td>Increase healthy life expectancy at birth in the most deprived areas. (Outcomes 5, 6 &amp; 7)</td>
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<td>8</td>
<td>NI 17</td>
<td>Reduce the percentage of adults who smoke to 22% by 2010. (Outcome 5)</td>
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<td>9</td>
<td>NI 24</td>
<td>Reduce overall crime victimisation rates by 2% by 2011. (Outcome 9)</td>
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<td>10</td>
<td>NI 32</td>
<td>Reduce overall ecological footprint. (Outcomes 12 &amp; 14)</td>
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