



House of Commons  
Treasury Committee

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# The 2007 Comprehensive Spending Review: prospects and processes

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**Sixth Report of Session 2006–07**

*Report, together with formal minutes, oral and  
written evidence*

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6.17 Government must decide if it is serious about meeting the demographic, social, environmental and economic challenges of the future. If it is, investing in local services is crucial and local government is ready to play its part. If not, local councils and local taxpayers need to know, so they can prepare for the consequences.

*January 2007*

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**Memorandum by Professor David Heald, specialist adviser to the Committee**

**COMPREHENSIVE SPENDING REVIEW 2007: URGENT ISSUES FOR PARLIAMENT**

**INTRODUCTION**

1. The Treasury is expected to publish Comprehensive Spending Review 2007 in July, shortly before the summer recess. Since the new public expenditure framework was established in 1998, a pattern of biennial Spending Reviews (1998, 2000, 2002 and 2004) had developed, which implied that there would be an SR2006. The postponement to 2007, announced on 19 July 2005 (Browne, 2005), was perceived not as a technical decision but as a political calculation relating to the likely timing of change in the leadership of the Labour Government. The Treasury stated that CSR2007 would be a more ambitious review than the biennial Spending Reviews, echoing CSR1998 at the beginning of the Labour Government. This postponement shortened the period over which government departments and their sponsored bodies had forward-year figures. With biennial SRs, the July announcement involves a rolled-forward first year starting eight months ahead and a brand-new second year starting 20 months ahead. In contrast, in July 2007, departments would receive brand-new 2008–09 plans only eight months before the start of that year. The Treasury's recognition of this difficulty may have been one reason for some early CSR2007 settlements.

2. Recent public expenditure history has been astonishing in terms of continuing strong growth, only made possible by 2006–07 being the 15th successive year of real GDP growth. Total Managed Expenditure (TME) has increased by 66% in “cash”<sup>91</sup> and 39% in real terms in the period from 1998–99. There is a spectacular contrast with the preceding five years: real-terms expenditure was almost identical in 1998–99 to what it had been in 1994–95 (Treasury 2006a, Table 3.1 on page 42). After a long period of feast, CSR2007 will start a period of relative famine. Pre-Budget Report 2006 (Treasury 2006d, Table B16 on page 240) does not provide TME figures beyond 2007–08. However, public sector current expenditure, which constitutes 91.7% of planned TME in 2007–08, is planned to grow in real terms by 2.0% in 2008–09 and by 1.9% in each of the years 2009–10 to 2011–12 (para B26 on page 223). These growth rates are below the expected growth rate of the economy and, because of the Relative Price Effect, are likely to overstate the effective purchasing power of public-service providers.

3. There are two further background points. First, the 1998 public expenditure system has, unlike its predecessors, never been tested in years of (relative) famine. As for the past, it is impossible to prove whether the 1998 system contributed positively towards the long period of economic growth, or whether it was the economic growth that both allowed the system to hold and the remarkable rates of real public expenditure growth to be sustained over such a long period. Second, there is no consensus as to the quality of the additional spending, particularly whether improvements in public-service outputs have been commensurate with the additional resources. Notwithstanding all the performance indicators that have been another key feature of the post-1998 period, there are plenty of commentators prepared to claim, often on anecdotal grounds, that these additional resources have been squandered.

**TRANSPARENCY OR OPAQUENESS**

4. Over the past 10 years there has been an explosion of references to transparency, in terms of both claims by government to be transparent and demands that government and other public organisations should be transparent. One of the difficulties of interpreting developments is that this has been the age of “spin”, which has accentuated the decline in trust in government. This is also the age of formal evaluation, often externally conducted but sometimes framed in terms that might be described as “self-assessment with only positives mentioned”. “Fiscal transparency” is one of the five principles of fiscal management in the statutory Code for Fiscal Stability (Treasury, 1998). The Chancellor of the Exchequer and the Treasury like to portray the United Kingdom as leading the way on international best-practice in fiscal transparency. In reality, however, there are several systematic features of UK practice that damage this claim. The positive developments of which the Treasury can justifiably be proud<sup>92</sup> are offset by undesirable practices. Obstacles to transparency do not only include a lack of openness about documentation and data, but can also be erected by overload, complexity, disorder and/or manipulative presentation (Heald, 2006).

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<sup>91</sup> This labelling by the Treasury is misleading as these are accruals figures; the point is that the figures have not been adjusted to take account of inflation.

<sup>92</sup> For example: full implementation on schedule of Resource Accounting and Budgeting; the introduction in 2002 of both the End-of-Year Fiscal Report and the Long-term Public Finance Report; continuing improvements to the annual Public Expenditure: Statistical Analyses; and the development of an excellent website that greatly enhances document accessibility.

5. The following are examples of practices that scar the Treasury's record on fiscal transparency, some of which may not originally have been intentionally obstructive:

- Announcing Spending Review settlements in July, at a time that precludes effective Parliamentary scrutiny.
- Leaking materials to favoured newspapers ahead of Pre-Budget, Budget and Spending Review announcements, some of which are authentic and some calculated to bring relief when the actual announcement differs.
- Overloading users and media by publishing a vast array of loosely connected reports and materials on the announcement day or just before, thus diverting attention from key fiscal numbers and making it difficult to find key material quickly.
- Adopting a rhetorical tone and propagandist style in parts of the Pre-Budget and Budget Reports that can descend into self-parody, almost as if some drafters are having a private joke at the Government's expense.
- Making repeated changes to the dating of the current economic cycle in a way that has brought the golden rule into disrepute, so that commentators cynically expect the results to be manipulated.
- Maintaining ambiguity for 10 years about whether the 40% sustainable investment rule is a ceiling in each financial year or whether it must be met on some kind of average basis over the economic cycle as a whole.<sup>93</sup>
- Undermining trust in government figures, with the effect that many people will not believe claims of, *inter alia*, efficiency savings, staffing reductions or service improvements.

#### THE EARLY CSR2007 DOCUMENTATION

6. The Treasury's (2007, emphasis added) website still contains the following statement about CSR2007:

To lay the groundwork for the CSR, the Government is taking forward a programme of work involving:

- an examination of the key long-term trends and challenges that will shape the next decade—including demographic and socio-economic change, globalisation, climate and environmental change, global uncertainty and technological change;
- **a national debate to build a shared understanding of how the UK and public services need to respond to these challenges (further details of the opportunities to participate in this debate will be set out in the coming months);**
- detailed studies of key areas where cross-cutting, innovative policy responses are required to meet these long-term challenges;
- an ambitious and far-reaching value for money programme to release the resources needed to address the challenges, involving both further development of the efficiency areas developed in the Gershon review, and a set of zero-based reviews of departments' baseline expenditure to assess its effectiveness in delivering the Government's long-term objectives; and
- a more strategic approach to asset management and investment decisions, ensuring the UK is equipped with the infrastructure needed to support both public service delivery and the productivity and flexibility of the wider economy.

The promise of a "national debate to build a shared understanding" may have originally seemed useful compensation for the cancellation of SR2006. However, there is no sign of a national debate, not least because—after much vacillation—the Treasury published its first CSR preview document (Treasury 2006b) in the Parliamentary dead-time of July 2006. The second preview document (Treasury 2006c) came shortly before the 2006 Pre-Budget Report. In the meantime, certain departments made early CSR2007 settlements, and these were announced in the March 2006 Budget, and there have been others since. Even if there were a national debate, there is no mechanism for that to feed into decision-making on future spending priorities, especially when early settlers include the Home Office whose recent service-delivery and financial performance have attracted much criticism and public concern. Rumbling in the background—and sporadically flaring up in media interviews given, for example, by serving and recently retired military officers—is a great deal of traditional politicking about expenditure allocations. This may be fuelling a public mood that "the country is falling apart" and that the massive increases in public expenditure have

<sup>93</sup> Chart 2.5 of the 2006 Pre-Budget Report (Treasury 2006b, page 32) suggests that the precise formulation may be important in the next economic cycle.

been wasted. A more measured debate is desperately needed, but currently looks unattainable. The Treasury Committee's (2006) inquiry may come too late to affect substantive CSR2007 outcomes. However, valuable procedural gains for Parliamentary scrutiny of public expenditure would follow from adoption of the proposals made in the following paragraphs of this memorandum.

7. The two CSR preview documents (Treasury 2006b,c) contain much interesting contextual material but do not address how to prioritise public expenditure or how to manage it when the inevitable slowdown of real growth bites from 2008–09. The Foreword to Treasury (2006c, page 2), signed by Tony Blair and Gordon Brown, holds out the prospect of “an open discussion about future priorities”. However the gloss that this document places on expenditure outcomes over the period since 1997, where only positives are mentioned, has its converse in widespread media negativity about supposedly disintegrating public services that is influencing public perceptions. Although difficult for governments that have been in office for a long time, a realistic assessment of successes and failures is imperative.

#### WHAT PARLIAMENT SHOULD NOW ASK FOR

8. Parliament is entitled to more respect from the Government, and a good place to start would be with the Treasury's relationship with the Treasury Committee. Here are some suggestions:

- The announcement of the publication dates of key fiscal documents well in advance, and dates only subsequently changed by Government if there is a genuinely compelling reason.
- Streamlined documentation which explicitly provides information that the Committee and other users actually want to receive,<sup>94</sup> and which cuts out the hype and digressions.
- The programming of oral evidence sessions with Treasury officials and ministers well in advance, with sufficient time between publication day and the meeting with officials for the Committee to prepare.
- The avoidance of artificially compressed timetables that, together with the sheer volume of ancillary material, leave Treasury officials under-briefed for oral evidence sessions.
- The provision to the Committee on a monthly basis of a running tally of announced early CSR2007 department settlements, showing the numerical amounts in each financial year on a basis comparable to the latest Pre-Budget Report or Budget Report (or alternatively with reconciliations, for example if departmental structures have changed).
- A clear statement of exactly how the golden rule and sustainable investment rule will be formulated in the next economic cycle, with a commitment to transparent disclosure of the numerical impact of any reformulation later in the cycle.
- A Treasury announcement in July 2007 that SR2009 (assuming the return to a biennial timetable) will be published in May 2009, thus allowing time for serious Parliamentary consideration, in the first instance by select committees, but also on the floor of the House of Commons.
- Although the Treasury provides in the annual Public Expenditure: Statistical Analyses a 41-year time series of Total Managed Expenditure, the Departmental Expenditure Limit and Annually Managed Expenditure figures only cover eight years.<sup>95</sup> This may be sufficient for the Treasury's planning and control function but it is certainly not sufficient for users wishing to analyse, for example, public expenditure behaviour over the economic cycle or the public expenditure policy of a government that has won multiple terms of office.
- A thorough review of the role of the National Audit Office in auditing macroeconomic assumptions, which currently breaches the fundamental principle of auditing that the auditor, not the auditee, chooses what is audited and when.<sup>96</sup>

<sup>94</sup> There are two excellent current examples. First, in oral evidence on the 2006 Pre-Budget Report, Chote (2006, Q30) expressed concern that the Report did not contain an explicit statement that the Treasury had changed its forecast of the end-date of the current economic cycle. Second, the Treasury has consistently refused to publish in the Pre-Budget Report and Budget Report a comprehensive analysis of departmental savings under the Gershon efficiency programme. Bizarrely, given what else the Treasury publishes about departments, centralised publishing of efficiency savings is claimed not to be appropriate (Brivati, 2006). In consequence, the Treasury Committee has to prepare its own table based on the incomplete and not necessarily consistent data that can be extracted from departmental reports.

<sup>95</sup> In the 2006 edition, these are: five outturn years starting in 2000–01; estimated outturn 2005–06; and two plan years ending in 2007–08 (Treasury, 2006a, Table 1.1, page 11).

<sup>96</sup> My own view (Heald and McLeod, 2002) is that this is an entirely unsuitable role for the National Audit Office, which cannot match the macroeconomic expertise of the Treasury, is exposed to reputational damage and might have its relationship with Parliament compromised when made to share blame. There is something dangerously seductive about the term “auditing” that can bring false reassurance. “Although the NAO only edits certain forecasting assumptions, and not forecasting systems or methodology (para 505)”, this distinction might be lost in practice. However, if the role is to continue, it is imperative that the right to determine the timing and substance of this audit process is passed from the Treasury to the Comptroller and Auditor General.

9. What is achievable may fall short of what is desirable. Nevertheless, after a long period of an Executive made even more over-dominant by large Parliamentary majorities, Parliament must be ready to grasp whatever window of opportunity arises. Henke (2007) reported:

The chancellor, interviewed by Andrew Marr on the BBC TV's AM programme, sketched out how he wants to change the way the country is run by giving more power to parliament and ordinary people and less to the state . . .

He envisaged constitutional change to give parliament a stronger role than existed under Mr Blair, arguing that new issues were emerging that required better parliamentary scrutiny. "We have got to look at the relationship as a whole between the executive, the law-making body which is parliament and the people themselves."

There are uncertain days ahead for the Treasury itself. The default position in British government is that it is the dominant department. However, its power and effectiveness can be eroded if the Chancellor of the Exchequer does not carry weight in government and in Parliament. Since May 1993 the Treasury has reasserted its role within government, a process facilitated by two commanding Chancellors of the Exchequer. By addressing the issues raised in this memorandum, the Treasury might gain allies through persuasion and would promote effective fiscal transparency.

January 2007

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#### Letter from the Chief Secretary to the Treasury to the Committee

Thank you for your letter regarding the Committee's inquiry into the 2007 Comprehensive Spending Review (CSR).

I regret that I am not able to provide the Committee with a copy of the Treasury's draft Public Service Agreement (PSA) targets for the CSR period: all PSAs across government are still in the early stages of their development and remain the subject of discussion internally. However, I would be interested to hear the Committee's thoughts on the Treasury's PSAs when we meet on 30 January.

With that in mind, it might be helpful if I set out briefly how we propose to develop the performance management framework in the CSR. Building on the evolutionary reforms of consecutive Spending Reviews, we will set in the CSR a refreshed and smaller suite of "corporate" PSAs which articulate the Government's highest priority outcomes for the period. By setting PSAs across government according to the key challenges we face, rather than solely on a department-by-department basis, we hope to encourage better-focused and coordinated action.