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BRIEFING PAPER

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Office for Budget Responsibility and Charter for Budget Responsibility

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Office for Budget Responsibility

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Summary

The Office for Budget Responsibility (OBR) was established within days of the Coalition Government coming to power in May 2010 with the aim of improving the credibility of fiscal policy.

The body was initially established on an interim basis with Sir Alan Budd as chair. Robert Chote, a former director of the Institute for Fiscal Studies, has been chair of the OBR since October 2010. The Treasury Committee has the power of veto over this appointment. The Budget Responsibility and National Audit Act 2011 provides for the establishment of the OBR, and sets out its functions and broad governance structure.

The Charter for Budget Responsibility

The Charter for Budget Responsibility (the Charter) sets out the OBR's role, how it performs its duties and the required content of its key publications. The Charter also sets out the Government's targets for the public finances – which are often referred to as its fiscal targets – and how the Government's policy for the public finances operates.

The Charter has been changed on several occasions since its introduction in 2011. The latest version was proposed alongside Autumn Statement 2016 and came into force on Tuesday 24 January 2017 when the House of Commons approved it.

The OBR's role

Part of the OBR's role, as laid out in the Charter, is to produce forecasts for the economy and the public finances. These are produced independently of the Government. In the past, the Treasury's forecasts have been based on the Chancellor's judgement. This has led to the suspicion that forecasts may be over-optimistic. It is hoped that any perception that the forecasts could be politically motivated is removed by an independent body producing them.

The OBR also comments on whether the Government's policies have a better than 50:50 chance of meeting the Chancellor's targets for the public finances which are set out in the Charter. It also examines the long term sustainability of the public finances, risks surrounding the public finances, spending on welfare and devolved taxes.

The Government's fiscal targets

The Charter includes the Government's targets for the public finances. The targets are designed to achieve the Government's overall objective for fiscal policy, which is to return the public finances to balance at the earliest possible date in the next Parliament. Currently government spends more than it receives from taxes and has to borrow to make up the difference. The Chancellor wants to reach a position where the budget is in balance and there is no need to borrow. At the time the objective was introduced, in autumn 2016, its wording suggested the deficit would be eliminated by 2025 at the latest. Its interpretation now is questionable, given the early General Election in 2017, but the Conservative Manifesto suggests the Government are still aiming at the 'middle of the next decade'.

The Charter includes targets for the deficit (public sector net borrowing), debt and the welfare cap.

The Government's borrowing target – its 'fiscal mandate' – requires structural borrowing to be below 2% of GDP in 2020/21. Structural borrowing is the borrowing that remains once elements related to the ups and downs of the economy are removed. It is the

amount of borrowing we would expect to remain if the economy was running at a normal, sustainable level of employment and activity.

The fiscal mandate is supplemented by two further targets: for the public sector's debt-to-GDP ratio to be falling in 2020/21, and selected welfare spending in 2022/23 to be within a cap and margin set by the Treasury at Autumn Budget 2017.

The Chancellor can review the targets if there is a significant negative shock to the UK economy.

Reviews of the OBR

Both an external review and a Treasury review reported positively on the OBR. Both have praised the OBR's credibility and reputation, and the integrity brought to the fiscal forecasts. Both reviews made recommendations for the future of the OBR, including the need to undertake succession planning for key and long-serving members of staff. The Treasury review recommended the changes currently being made to the OBR's role.

1. What does the OBR do?

The OBR's role and how it performs its duties are laid out in the Charter for Budget Responsibility (see section 3). [1]

1.1 OBR's role

Producing five-year forecasts for the economy and public finances

The OBR produces forecasts for the economy and the public finances at least twice every financial year.[2] Previously, these forecasts had been produced by the Treasury. The forecasts are set out in the OBR's economic and fiscal outlook (EFO) documents that accompany the Budget and Autumn Statements.

Each autumn the OBR assesses their forecasts against actual outturns in their forecast evaluation report.

The legislation does not require the Chancellor to use the OBR's forecasts, but they have been used since the OBR's inception. When formulating policy, the Government has the right to disagree with the OBR's forecasts, but must explain the reasons for doing so.[3]

Judging the Government's performance against its fiscal targets

The OBR uses its forecasts to report on whether, in its judgement, the Government's policies have a better than 50:50 chance of meeting the fiscal targets in set out in the Charter for Budget Responsibility (see section 3).

The OBR will monitor spending against the welfare cap in its forecasts, but will only make a formal assessment in its first forecast of each new Parliament. The Library briefing The welfare cap provides further detail.

Scrutinising the Treasury's costing of tax and welfare spending measure

Ahead of the Budget the Treasury produces draft costings of tax and spending measures. The OBR scrutinises the costings and, in the EFO and the Treasury's policy costing documents, states whether they endorse the costings that the Government publishes as reasonable central estimates.

The OBR also performed this role ahead of autumn statements, but from 2017 these will no longer happen. The Chancellor, Philip Hammond MP, has announced that there will no longer be two fiscal events – there will just be an Autumn Budget from 2017.[4]

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1 For further information see the OBR' website: http://budgetresponsibility.org.uk/about-the-obr/what-we-do/

2 The latest forecasts are available on the OBR's website: http://budgetresponsibility.org.uk/

3 HM Treasury. Charter for Budget Responsibility (autumn 2016 update), January 2016, para 3.9

4 For more see section 5 of Library briefing The Budget and the annual Finance Bill.

Assessing the long-term sustainability of the public finances

The OBR produces long-term projections for different categories of spending, revenue and financial transactions and assess what they imply for public sector debt. Projections are set out in the OBR's annual fiscal sustainability report, which also analyses the public sector's balance sheet.

Since autumn 2015 the OBR has been required to make these detailed projections every other year, rather than every year. In the interim years the fiscal sustainability report will include in-depth analysis of specific sustainability issues.

Producing a welfare trends report

The OBR produces an annual welfare trends report that discusses trends and drivers of welfare spending.

Producing a fiscal risk report

In autumn 2015 the OBR took on a new role: producing a biennial fiscal risk statement. This additional role was recommended in HM Treasury's review of the OBR (see section 6.2). The Treasury will be required to respond to the fiscal risks statement within a year of publication.

The OBR published its first fiscal risk report in July 2017. The report reviews a wide range of risks from the economy and financial system, to tax revenues, public spending and the balance sheet, and includes a fiscal stress test.

Producing forecasts of devolved taxes

Forecasts of taxes devolved under the Scotland Act 2012 and Wales Act 2014, are published alongside the OBR's EFOs.

In support of all the above activities, the OBR undertakes other research and provide briefings on public sector finance releases.

Box 1.1: Budget Responsibility and National Audit Act 2011

The OBR was established by the Budget Responsibility and National Audit Act 2011 (the Act).

The Act sets out its functions and broad governance structure.

Before the Act came into force, the OBR was governed by terms of reference published by the Chancellor. Further details of the OBR's governance and management arrangements are set out in a Framework document.

1.2 Role of other fiscal watchdogs

Similar institutions in other countries have, in some cases, been given a quite different role. The Treasury Committee noted that "most fiscal councils do not themselves produce the forecast which the government uses in making its fiscal judgements". Often the role of the council is to assess the official forecast, or provide an alternative, after it has been published.[5] Lars Calmfors, Chair of Sweden's Fiscal Policy Council,

5 Treasury Committee, Office for Budget Responsibility, HC 385, 21 September 2010 para 20

contrasted the OBR’s arrangements with those in Sweden where there is less on-going contact between the fiscal council and the finance ministry. He argued that requiring the OBR to publish a forecast with the Budget makes it very difficult to “avoid behind the scenes ‘negotiations’ ... with the Treasury”. He concluded:

> And the most important lesson is this: one cannot have it both ways – the OBR cannot be both an independent watchdog and an in-house provider of input into the Treasury's work.[6]

Annex 2 discusses other fiscal watchdogs further.

6 “How it’s done in Sweden”, *Guardian*, 29 July 2010

2. Who are the OBR?

2.1 Appointments to the permanent OBR

In October 2010, Robert Chote became chair of the OBR and member of the Budget Responsibility Committee (BRC). This appointment was made by the then Chancellor, George Osborne, subject to a veto by the Treasury Committee.

Mr Chote was formerly director of the Institute for Fiscal Studies (IFS). The IFS is well known for its independent analysis of the public finances, and Mr Chote frequently gave evidence to the Treasury Committee in his role there. An article in the Independent described Mr Chote as "widely respected" and said that his appointment was "likely to do much to restore faith in the integrity of the OBR" following some political controversy involving the interim OBR (see section 2.2).[7] Mr Chote commented widely on the OBR in the IFS's 2010 Green Budget,[8] evidence to the Treasury Committee[9] and the 2009 Scottish Economic Society/RBS Annual Lecture.[10]

Mr Chote was originally appointed for an initial term of five years. In September 2015 he was re-appointed for a second term following a nomination by the then Chancellor, George Osborne, which was subsequently approved by the Treasury Committee.[11, 12] This will be Mr Chote's final term – the Act restricts members of the BRC to serve two terms.[13]

In October 2010, the then Chancellor, George Osborne, announced that Sir Stephen Nickell and Graham Parker were his preferred candidates as members of the Budget Responsibility Committee.[14] These appointments were also confirmed by the Treasury Committee. Both were re-appointed to serve a second (and final) term.

In August 2016 the Chancellor, Philip Hammond, nominated Sir Charles Bean, former Deputy Governor of the Bank of England and currently Professor of Economics at the London School of Economics, to join the BRC. The Treasury Committee has approved the appointment.[15]
Sir Charles joined the OBR at the beginning of 2017 and replaced Sir Stephen Nickell who completed his final term.

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7 "Osborne appoints critic to top job at Treasury watchdog", *Independent*, 10 September 2010
8 IFS Green Budget 2010, Chapter 11, "Reforming UK fiscal institutions"
9 Treasury Committee, Office for Budget Responsibility, HC 385, 21 September 2010
10 IFS Press Release, Keeping official fiscal forecasts honest, 12 November 2009. This contains the text of the section on the OBR of Robert Chote's November 2009 Scottish Economic Society/Royal Bank of Scotland Annual Lecture
11 HM Treasury Press Release, Chancellor backs Robert Chote as Chair of Office for Budget Responsibility, 3 September 2015
12 Treasury Committee News Release, Treasury Committee approves reappointment of Chair of the OBR, 15 September 2015
13 Graham Parker's term will last until 25 October 2019. Stephen Nickell's term will last until 26 October 2018.
14 HM Treasury Press Release, Chancellor announces Professor Stephen Nickell and Graham Parker as his preferred candidates for members of the Budget Responsibility Committee, 12 October 2010
15 Treasury Committee, Seventh Report of Session 2016-17, HC642, 13 Sept 2016

The OBR currently has two non-executive members who, along with members of the BRC, make up the five members of the OBR's Oversight Board.[16] The non-executive members are nominated by the OBR and appointed by the Chancellor.

Box 2.1: The Budget Responsibility Committee and the Oversight Board

The **Budget Responsibility Committee (BRC**) has executive responsibility for carrying out the OBR's core functions, including judgements reached on its forecasts. The BRC currently consists of: Robert Chote (Chairman), Steve Nickell CBE, and Graham Parker CBE.

The **Oversight Board** ensures that effective arrangements are in place to provide assurance on risk management, governance and internal control of the OBR. The Oversight Board consists of the members of the BRC and two-non executive members. Currently the non-executive members are Lord Burns and Sir Christopher Kelly.

2.2 Interim appointments

The OBR was initially established on an interim basis on 17 May 2010.[17] Sir Alan Budd was appointed as chairman. Two other members were appointed to the BRC: the aforementioned Graham Parker and Geoffrey Dicks. The interim body also included a secretariat of eight Treasury employees on secondment. It had, therefore, to rely on the Treasury's expertise.[18]

The interim OBR published two sets of economic forecasts. The first was published before the June 2010 Budget and was based on the previous Government's economic policies.[19] The second forecast was published alongside the June 2010 Budget.[20]

The interim OBR did, however, become involved in political controversy over the release of employment forecasts. Some argued that this damaged its perceived independence. Sir Alan Budd expressed regret about this in evidence to the Treasury Committee:

> Chair: You do understand, though, Sir Alan, do you not, that this has done quite a bit of damage to the early reputation of the OBR?
>
> Sir Alan Budd: And, as I have said, I regret that enormously, Chairman.[21]

16 http://budgetresponsibility.org.uk/about-the-obr/who-we-are/
17 HM Treasury Press Notice, Chancellor announces policies to enhance fiscal credibility, 17 May 2010
18 Establishing the Office for Budget Responsibility, Letter from the OBR to the Chancellor, 12 July 2010, para 47
19 OBR, Pre-Budget forecast, June 2010
20 OBR, Budget forecast, June 2010
21 Treasury Committee, June 2010 Budget, HC 350, 20 July 2010, Q14

3. The Charter for Budget Responsibility and the fiscal targets

The Charter for Budget Responsibility (the Charter) sets out the OBR's role, how it performs its duties and the required content of its key publications (see section 1).[22] The Charter also sets out the Government's targets for the public finances – which are often referred to as its fiscal targets – and how the Government's policy for the public finances operates. The OBR assesses and reports on progress against the Government's fiscal targets in its economic and fiscal outlooks.

The Government's fiscal targets have changed a number of times since the Charter was first introduced in 2011 (see Appendix 1). The current fiscal targets were proposed in a revised Charter published alongside Autumn Statement 2016. The Charter came into force on 24 January 2017 after it was approved by the House of Commons. A new objective for fiscal policy and new fiscal targets were introduced.[23] [24] The targets are, in the opinion of the OBR, "less constraining" than the immediate predecessors".[25] The Institute for Fiscal Studies (IFS) – an economic think-tank – view them as 'more relaxed' and 'much looser'.[26]

The previous fiscal targets were introduced in the autumn 2015 Charter update, which the House of Commons agreed on 14 October 2015.[27] The targets had been announced alongside Summer Budget 2015.

3.1 The current fiscal targets

Background to the introduction of the current targets

Following the EU referendum the then Chancellor, George Osborne, said that the Government's main fiscal target – which was then to reach a budget surplus in 2019/20 – would be suspended. Reaching a surplus would mean government spending less than it receives in taxes. Currently government has to borrow money to make up the difference between its spending and its tax income.

George Osborne suggested that the economic shock of the referendum vote would be sufficient enough for the target to be suspended.[28] Section 3.2 has more on the previous budget surplus rule and how it could be suspended following an economic shock.

22 HM Treasury. Charter for Budget Responsibility: autumn 2016 update, January 2016
23 ibid, page 7.
24 The revision also includes an operational amendment requiring a debt management report to be published annually rather than as part of the budget report.
25 OBR. Economic and fiscal outlook – November 2016, para 1.10
26 IFS. Autumn Statement 2016 briefing: Paul Johnson's opening remarks, 24 November 2016
27 HC Deb. 14 October 2015:c427-456
28 'Osborne abandons 2020 budget surplus target', BBC, 1 July 2016; HC Deb. 4 July 2016:c622

Both the current Chancellor, Philip Hammond, and the Prime Minister confirmed that the Government would not be aiming to reach a budget surplus in 2019/20.[29]

The revised Charter published alongside the Autumn Statement 2016 began the process of replacing the surplus target. The Chancellor also took the opportunity to revise the Charter's other fiscal targets – the supplementary debt target and welfare cap – both of which were being breached in the OBR's assessment prior to Autumn Statement 2016. The Charter came into force on 24 January 2017 after it was approved by the House of Commons.

3.2 The objective for fiscal policy

The Treasury's objective for fiscal policy, as stated in the Charter, is to return the 'public finances to balance at the earliest data in the next Parliament'. The objective aims to provide sustainable public finances, ensure confidence in the economy, and support the effectiveness of monetary policy.[30]

Objective for fiscal policy: *return the public finances to balance at the earliest possible date in the next Parliament*

At the time the objective was introduced, in autumn 2016, its wording suggested the deficit would be eliminated by 2025 at the latest. Its interpretation now is questionable, given the early election, but the Conservative Manifesto suggests the Government are still aiming at the 'middle of the next decade'.[31] Given the uncertain interpretation, in its November 2017 forecast the OBR considered both possibilities – a balance in 2025/26 or 2022/23. The OBR found that meeting either interpretation would be challenging, with their forecast for 2022/23 showing a deficit of 1.1% of GDP.[32]

The fiscal targets aim to achieve the government's overall objective for fiscal policy.

3.3 The fiscal targets

The fiscal mandate

When government spends more than it receives in taxes and other revenues it has to borrow. Formally this is known as public sector net borrowing, although it is often referred to as the deficit. The fiscal mandate focuses on an adjusted version of borrowing. The Treasury's fiscal mandate is:

- a target to reduce cyclically-adjusted public sector net borrowing to below 2% of GDP by 2020/21

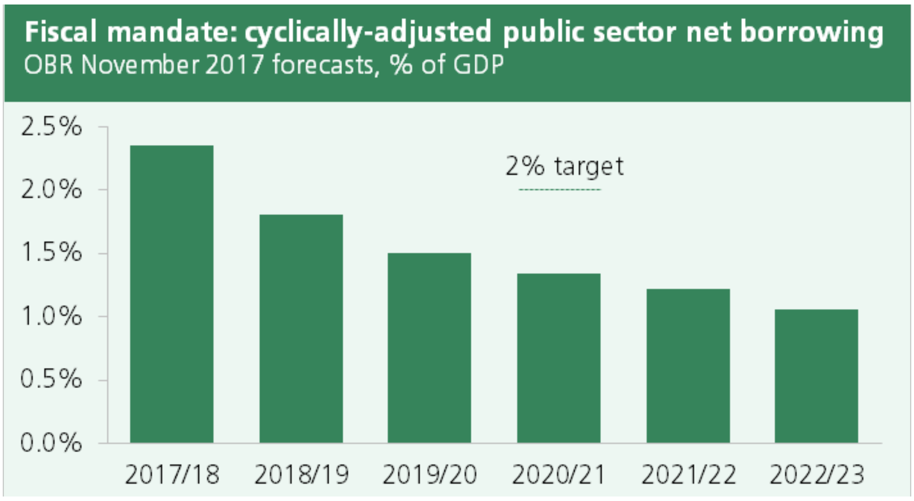
Fiscal mandate: *a target to reduce cyclically-adjusted public sector net borrowing to below 2% of GDP by 2020/21*

The adjustment means the target focuses on structural borrowing, or the element that remains once borrowing related to the ups and downs of the economy are removed. This is what is meant by 'cyclically-

29 House of Lords Economic Affairs Committee, Chancellor of the Exchequer Oral Evidence, 8 September 2016; HC Deb 20 July 2016:c818-819
30 HM Treasury. Charter for Budget Responsibility: autumn 2016 update, January 2017, para 3.1
31 2017 Conservative Manifesto, page 14
32 OBR. Economic and fiscal outlook – November 2017, paras 5.17 – 5.18

adjusted': removing the parts of borrowing related to the economic cycle. There is more on this in Box 3.1.

As the chart below shows, the OBR forecast that the Government are currently meeting the fiscal mandate.



Box 3.1: Structural borrowing, cyclical elements and the output gap

Structural borrowing

Structural borrowing is the level of borrowing we would expect to remain if the economy was running at a sustainable level of employment and activity. Structural elements are the underlying or persistent part of government borrowing, which are unrelated to the economic cycle. The OBR never know what the economy's normal level is, so they estimate it through the output gap (see below).

Cyclical elements of borrowing

Cyclical elements of borrowing refer to the effect of the economic cycle on the level of government borrowing. In a recession, government borrowing tends to increase as tax receipts are reduced and spending on benefits increases. The reverse happens when the economy is growing strongly. These effects are sometimes known as the economy's 'automatic stabilisers'.

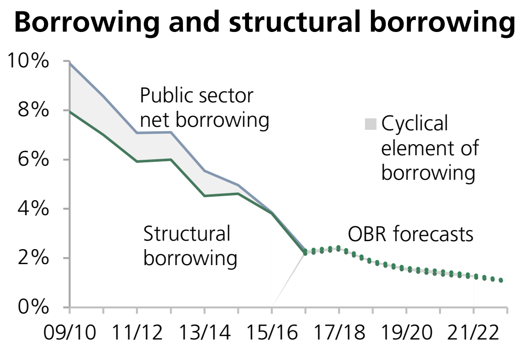
The output gap

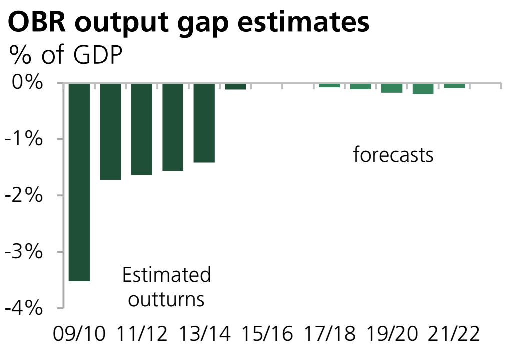
The difference between the actual level of economic output and what could be achieved if the economy was operating at full potential is known as the 'output gap'. A negative output gap suggests that the economy is operating below its potential level and has idle resources. A positive output gap suggests that the economy is operating above potential or overheating.

A big problem for policymakers is that the level of potential output cannot be directly measured and consequently neither can the output gap. Therefore economists must estimate what the output gap is.

November 2017 estimates

The OBR estimates that the economy was operating slightly below its potential in 2016/17, with a small output gap of -0.3%. As the economy was running slightly below capacity the OBR judged that public sector net borrowing was slightly larger than structural borrowing. This means that there is a small cyclical element of borrowing that can be eliminated through economic growth.



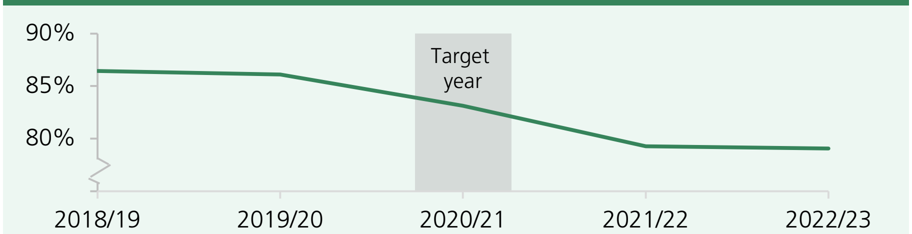


Supplementary debt target

The fiscal mandate is supplemented with a target for public sector net debt as a percentage of GDP to be falling in 2020/21. As the chart below shows, the OBR forecasts that the Government are currently meeting the fiscal mandate.

Supplementary debt target: *a target for public sector net debt as a percentage of GDP to be falling in 2020-21*

Supplementary debt target: public sector net debt
OBR November 2017 forecasts, % of GDP



Welfare cap

The welfare cap was introduced, in its original form, in Budget 2014 and sets limits on the amount that can be spent on certain benefits.[33] Currently the cap covers around 55% of welfare spending, excluding pensions and Jobseekers Allowance payments, but including tax credits, child benefit and disability benefit.

The target for the welfare cap is a target to ensure that expenditure on welfare in 2022/23 is contained within a predetermined cap and margin set by the Treasury at Autumn Budget 2017.[34]

Welfare cap: *a target to ensure that expenditure on welfare in 2022-23 is contained within a predetermined cap and margin set by the Treasury at Autumn Budget 2017*

The OBR will assess spending against the welfare cap and margin in its first forecast of each new Parliament. At the same time the Government will set its new cap for welfare.

The cap is only breached if spending exceeds the cap at the point of the OBR's formal assessment, which will take place in the first fiscal event of a new Parliament. However, the OBR will monitor welfare spending against the cap in each of its forecasts before the formal assessment. The OBR's last formal assessment was made at Autumn Budget 2017:

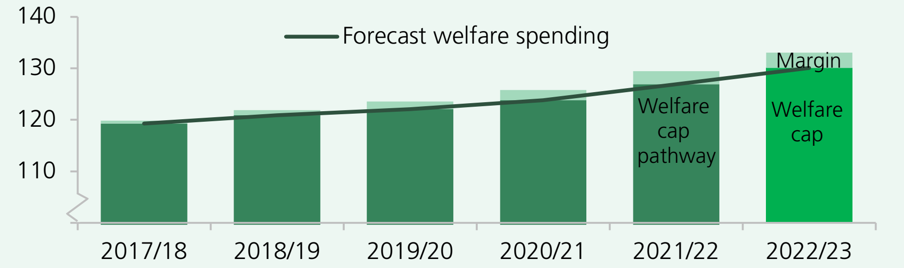
33 It entered into the Charter in the March 2014 update.
34 HM Treasury. Autumn Budget 2017, para 1.45

the OBR judged that the terms of the target were being met.[35] At this point the welfare cap applied in 2021/22.

As well as setting a cap level for 2022/23, the Government has set a pathway for the cap in the years running up to the target year, and a margin. As the chart below shows forecast welfare spending is within the pathway and margin in each year, and within the cap level and margin set for 2022/23.

The Library briefing The welfare cap has more on the cap.

Welfare cap, pathway and margin, £ billion



Negative shock to the UK economy: reviewing the targets

The Treasury can review the appropriateness of the fiscal targets if there has been a 'significant economic shock to the UK economy'. The Charter doesn't define what would be considered a shock, it is left for the Treasury to decide. The replaced fiscal targets could also be reviewed if there was a negative shock, however there was a specific statistical definition of what a shock would entail, and it was for the OBR to judge whether a shock had occurred (see section 3.4)

Any changes the Chancellor wishes to make to the fiscal targets must be approved by a vote in the House of Commons. The Chancellor will explain the reasons for the changes and present them in a revised Charter.

3.4 The previous fiscal targets

The previous targets, which were replaced by the latest Charter update, were announced in Summer Budget 2015 and came into force in autumn 2015.[36]

The previous fiscal mandate

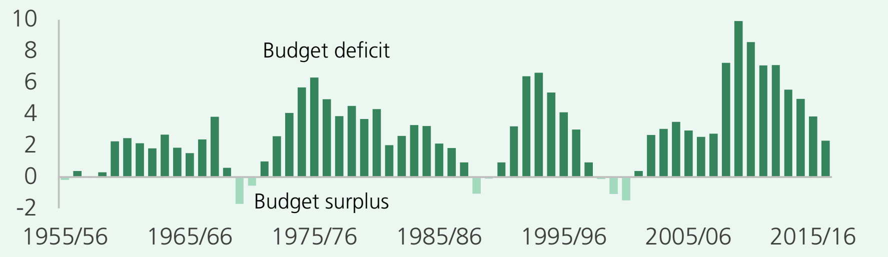
The interim fiscal mandate was for public sector net borrowing to be in surplus by 2019/20. Once this was achieved the target would have was then for a surplus to be achieved in every subsequent year.

Achieving the fiscal mandate was thought by many to be challenging. Over the previous six decades budget deficits have been the norm; surpluses have been rare. Since 1955/56 the UK's public sector budget has been in surplus in only eight years; the last surplus was recorded in 2000/01.

The OBR said that requiring a budget surplus by 2019/20 was "ambitious relative to the fiscal performance of past governments."[37]

35 OBR. Economic and fiscal outlook – November 2017, para 5.14
36 OBR. Charter for Budget Responsibility, autumn 2015 update, October 2015
37 OBR. Economic and fiscal outlook July 2015, 8 July 2015, para 5.18

Public sector net borrowing, 1955/56 - 2016/17, % GDP



The previous supplementary debt target

The fiscal mandate was supplemented with a target for public sector net debt to fall as a percentage of GDP in each year until 2019/20.

Economic shock: revising the targets

To allow it to respond to significant changes in the economy, the Government had the option to change the targets if the OBR assessed that there had been, or was to be, a significant negative shock. The OBR would judge there to have been a significant negative shock if annual real growth in the UK economy was less than 1%. If the OBR made such an assessment the economy would be judged to be out of normal times.

A significant negative shock was previously defined as real GDP growth of less than 1% on a rolling 4-quarter-on-4 quarter basis.

If the OBR judged a negative shock to have occurred, or would occur over the forecast period, the fiscal targets could be suspended. The Treasury would then have been required to set out a plan to return the budget to surplus including temporary fiscal targets. A vote in the House of Commons would have been required to approve the plan.

Welfare cap

In the first Budget of each Parliament, the Treasury was required to state what welfare spending would be included in the cap, and what the cap level will be for the forthcoming five years. The Treasury was also required to set out a forecast margin to allow for forecast judgements that may push up expected spending. The margin could not be used to accommodate changes to policy.

The target was for forecast welfare spending to be below the welfare cap level in each of the five years in the OBR's latest forecasts.

Performance against the cap level was assessed by the OBR. The OBR reported in each Autumn Statement whether or not relevant welfare spending was forecast to be under the welfare cap.

3.5 Targets prior to 2015

When the Coalition Government introduced the first Charter for Budget Responsibility its fiscal mandate was for the cyclically-adjusted current budget to be balanced by the fifth year of the forecast period.[38] This

[38] ibid

was shortened to the third year of the forecast period in the December 2014 Charter update.

The current balance is the difference between government revenue and current – rather than capital – expenditure. Focusing on the current budget therefore protects public sector capital investment. The mandate used a measure of the budget balance adjusted for the economic cycle – like the current fiscal mandate – allowing flexibility to run a deficit during recessions and a surplus during booms.

The Coalition Government's fiscal mandate was a forward-looking aim to achieve a cyclically-adjusted current balance.

The fiscal mandate was accompanied by a supplementary debt target. Originally this was for public sector net debt to be falling as a % of GDP in 2015/16 – this was moved to 2016/17 in the December 2014 update of the Charter.

Appendix 1 summarises the revisions to the fiscal targets, and introduction of the welfare cap, in the four versions of the Charter.

4. Rationale for the OBR

In recent years, governments in a number of countries have sought to improve their fiscal policies by the introduction of fiscal rules or by strengthening fiscal institutions. These measures can improve the credibility of fiscal policy. Governments may be tempted to adopt short-term policies, such as cutting taxes or increasing public spending in an unsustainable way, which may be harmful to the economy in the long-term. By adopting fiscal rules or frameworks, which constrain their behaviour, governments can signal that they will not adopt these short-term policies and can thereby give their fiscal policy increased credibility.

A number of attempts have been made in the UK to gain credibility in this way. These include the fiscal rules adopted by the previous Labour government and the Fiscal Responsibility Act 2010 which placed a legal obligation on the Treasury to reduce borrowing and debt by specified amounts. The fiscal frameworks must find a balance between placing constraints on policy with the need for flexibility in response to unanticipated economic events. This point was made by Lord Burns in the second reading in the Lords debate on the Bill:

> The challenge is to have a framework that both constrains fiscal behaviour in a responsible way and is capable of dealing with the range of surprises and unexpected events that inevitably occur. All attempts to frame budget responsibility in this way have at some stage met that particular problem-some have dealt with it better than others. [39]

In the past, attempts were made to add caution to the Treasury's fiscal forecasts. For example, the National Audit Office (NAO) examined the assumptions used in the projections of the public finances to ensure that they were reasonable and cautious. In addition, the Budget and Pre-Budget Reports used a cautious assumption for trend GDP growth in making projections for the public finances. For example, the March 2010 Budget assumed that trend GDP growth was ¼% lower than the Treasury's main economic forecast. The OBR does not use "cautious" assumptions in this way. It presents a central case and seeks to emphasise the inevitable uncertainties involved in economic forecasting.

The aim of the OBR is to make the Government's forecasts for the economy and public finances independent. Until now, the Treasury's forecasts were based on the Chancellor's judgements. This could lead to the suspicion that the forecasts were over-optimistic, and potentially to a loss of credibility in fiscal plans. By giving the forecasting role to the OBR, the danger that the forecasts could be politically motivated is removed and the credibility of the fiscal framework enhanced.

In the second reading debate in the Lords, Lord Sassoon said:

> Now, through the Bill, the Government are strengthening the framework of the UK's fiscal institutions.
>
> The greatest single step forward is the establishment of the independent Office for Budget Responsibility, which will make

[39] HL Deb 8 November 2010 c34

independent assessments of the public finances and the economy. Up until the new Government's first Budget, the responsibility for producing the official forecasts had rested with the Chancellor. The key judgments were made by Ministers, but the possible incentive to forecast optimistically, whether on lower borrowing or higher growth, led to scepticism over the credibility of the forecasts. Budget forecasts over the past decade consistently underestimated borrowing, compared to both its actual level and to what other independent forecasters expected at the time. The coalition Government intend to take a different approach. [40]

[40] HL Deb 8 November 2010 c12

5. OBR's accountability to Parliament

The Treasury Committee has the right of veto over both the appointment and dismissal of all three members of the Budget Responsibility Committee (BRC). The Chancellor gave the Committee this power for the appointment of the three current members of the BRC. The Act contains statutory provisions to this effect.

The OBR lays its reports directly before Parliament and members of the BRC appear before the Treasury Committee to be questioned about their forecasts.[41]

The OBR is a non-departmental public body (NDPB). Prior to its establishment there was some discussion over the institutional form the OBR should take. One possible model would have introduced the OBR as a Parliamentary body, similar to the NAO. Some fiscal councils overseas, such as the Congressional Budget Office and the Parliamentary Budget Office in Canada, have close links with their legislatures. The Treasury Committee recommended that this arrangement should be considered as part of the five year review suggested by the Committee.[42]

However, the Treasury Committee also noted that such arrangements might be more suited to an OBR whose function was to validate official forecasts, rather than producing them itself.[43] As Lord Turnbull said in the second reading debate on the Bill in the Lords, the OBR has an "executive role" in supplying forecasts used by the Government:

> The real choice is between an OBR that is on the executive side of the fence and one that is an emanation of Parliament, like the NAO. Both the Treasury Select Committee and the Government have opted for the former, which I believe is right. The OBR is not just a commentator or expert auditor. It has an executive function: it supplies the Treasury with the basis for its projections.[44]

The Treasury Committee recommended that the OBR should be a Non Ministerial Department similar to the UK Statistics Authority. The Government disagreed with this recommendation and proposed establishment of the OBR as a grant-funded NDPB. This was because of concerns over whether the OBR's establishment as a Non Ministerial Department would provide value for money.[45]

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41 HM Treasury, Office for Budget Responsibility and HM Treasury: Framework Document, May 2014

42 Treasury Committee, Office for Budget Responsibility, HC 385, 21 September 2010 p4

43 Treasury Committee, Office for Budget Responsibility, HC 385, 21 September 2010 para 91

44 HL Deb 8 November 2010 c22

45 HM Treasury, Government response to the House of Commons Treasury Committee 4th Report of Session 2010-11: Office for Budget Responsibility, Cm 7962, November 2010, paras 4.4 – 4.6

6. Reviews of the OBR

The first external review of the OBR was published in September 2014 - a HM Treasury review followed in September 2015. Both reported positively on the OBR, particularly on its credibility and reputation, and the greater trust if has brought to the fiscal forecasts.

6.1 External Review

The first external review of the OBR was published in September 2014. The review led by Kevin Page, former Parliamentary Budget Officer for Canada, concluded that the OBR is seen to be credible and independent and has succeeded in reducing perceptions of bias in economic and fiscal forecasting.[46]

The review made five recommendations to support the OBR's future work:[47]

- undertake long-term succession planning for the transition of the OBR leadership team
- introduce a fiscal community-wide staff development and rotation programme to maximise the talent pool from which the OBR can draw its analysts
- exercise caution in the expansion of the OBR's mandate
- provide more material that increases the accessibility of reports for non-technical readers
- survey Parliamentarians to understand their perceptions and use of the OBR's work

6.2 HM Treasury Review

HM Treasury published a review of the OBR in September 2015. The review was led by Sir Dave Ramsden, Chief Economic Adviser to HM Treasury.

The objective of the review was to build on the findings of Kevin Page's external review, focusing on the existing regime and the OBR's framework and its role in enhancing UK fiscal credibility.[48]

On reputation and credibility the review echoed the findings of Page's external review: the OBR has a strong reputation and credibility that has led to greater trust in the integrity of the forecasts. However the review made some recommendations to aid the OBR in holding the Government to account and improve its own resilience and capacity.

The review recommended some changes to the products produced by the OBR:

- a new annual report on fiscal risks should be produced covering a range of risks including economic shocks and potential future costs. This requirement should be added to the Charter

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46 Kevin Page for the OBR. External review of the Office for Budget Responsibility, September 2014

47 OBR. External review of the Office for Budget Responsibility, 3 September 2014

48 HM Treasury, HM Treasury led review of the Office for Budget Responsibility: terms of reference, 11 June 2015

- the OBR should no longer be required to include long-term projections in every annual sustainability report – biennial projections should be sufficient. However, the OBR should carry out more in-depth analysis on specific fiscal sustainability issues
- the Welfare Trends Report, the arrangements for which are currently set out in an exchange of letters between the Chancellor and OBR Chair, should be added to the Charter.

The above recommendations were incorporated into the Charter in autumn 2015.

To ensure the OBR has access to the relevant information to fulfil its remit the review recommended:

- that the Government and devolved administrations amend legislation to ensure the OBR has access to appropriate information, explanation and assistance. Similar arrangements should be put in place for city deals with significant fiscal devolution
- that the Memorandum of Understanding (MoU) (see section 7.1) between the OBR and government departments should be reviewed by September 2016
- that the OBR should consider agreeing Memoranda of Understanding with the aforementioned devolved administrations and city deals

To ensure that the OBR has the right calibre and amount of staff, the review recommended that:

- the OBR works with the Treasury to produce a succession plan to manage the transition of BRC membership (all BRC members are currently serving their last term)
- to increase the pool of potential candidates for the BRC, candidates should be sought within the UK and internationally, and the job description should be more flexible
- the Treasury ensures the OBR is resourced to deal with turnover in long-standing staff members

As discussed further in section 7.2 the review rejected calls to expand the OBR's remit to include costing of Opposition policies or other areas. However, it recommended that the Government and OBR should make more tools and data available so that third parties can cost alternative policy options.

7. Issues

7.1 Independence

The OBR's independence from the Treasury is seen as an important issue. As noted above, the Treasury Committee has a veto over appointments to the BRC. However, the OBR's remit means it has to work closely with government departments.

Central to the issue of independence is the extent to which the OBR makes use of expertise within the civil service. Civil servants in the Treasury, HM Revenue and Customs and the Department for Work and Pensions have considerable expertise in fiscal forecasting and the implications for the forecast of changes in taxes and benefits. How far should the OBR make use of this knowledge? There are advantages if the OBR could use this knowledge but too close contact could damage the perception of independence. The alternative would be to build up knowledge within the OBR but this could lead to wasteful duplication of resources.

The Treasury Committee described this problem as follows:

> In the run up to the Budget it [the OBR] is producing the official forecasts for government, in the light of policy options that have not yet been settled —let alone made public. The requirements for confidentiality and access to internal government information and knowledge are therefore much higher. The question is, how to ensure these requirements are met without compromising the OBR's independence? [49]

It went on to say:

> We accept that there is a trade-off between delivering the most robust independence and perception of independence and making the most efficient and effective use of resources. [50]

In its advice on setting up the permanent body, the interim OBR favoured using departmental resources but also called for those at the "core of the forecasting process" to be moved to the OBR:

> The question of the use of departmental, especially Treasury, resources is more difficult. The scepticism this process produced is unfortunate since, in our view, this is the best way for us to perform our task. Detailed forecasts of receipts and expenditure are necessary for the Budget and few outsiders appreciate the complexity of fiscal forecasting. At its peak the process involves more than 100 people in the Treasury, HMRC and DWP. It is not a full-time job for most of those involved. Between forecasts, the officials are engaged in such tasks as policy analysis and advice and monitoring of fiscal flows. It would not be practical to duplicate the forecasting activities within the OBR. The cost would be unacceptably high and there would be a severe peak-flow problem, given that forecasting is an intermittent activity. Further, those currently engaged in forecasting use the skills and knowledge they gain on their other activities: there are synergies

[49] Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, para 68

[50] Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, para 72

> in developing expertise that can be applied to both forecasting and other analysis.
>
> For these reasons we rule out wholesale duplication. That means that either the OBR continues to rely on official resources as now, while accepting full responsibility for all judgements and scrutinising all policy costings, or its forecasting task is changed. For example, it might just produce aggregate fiscal forecasts without taking responsibility for the full details of revenue and expenditure as published with the Budget. This could lead to consistency issues with policy costings and other problems. We do not believe that this approach would be consistent with your expressed wish to use the OBR as the source of the Budget forecasts.
>
> The way forward therefore would appear to be to build on the system used for the pre-Budget and Budget forecasts but to reinforce the OBR's technical independence. Since the OBR is responsible for producing the forecasts it would be reasonable for those at the core of the forecasting process to be part of it. That can be achieved by moving a number of posts from the Treasury to the OBR such that core tasks can be fully controlled and coordinated within the OBR. [51]

The OBR has around 20 staff, civil servants who have in the main transferred from HM Treasury. [52] The Act gives the OBR the right of access to government information which it may reasonably require for the performance of its duty. The Government has published frameworks for co-operation between the OBR and its main government partners in formal memoranda of understanding. [53]

The OBR is currently located in the Attorney General's Office on Victoria Street. [54] The interim body had been located in the Treasury. [55] In its advice on setting up the permanent body, the OBR recommended that it be located outside the Treasury while noting that it would be difficult to have a close working relationship with the Treasury if it was located too far away. [56]

7.2 Costing Opposition polices

The issue of whether the OBR should cost Opposition parties' fiscal proposals was discussed when the office was being established.

The issue re-emerged in 2013 when Labour's then Shadow Chancellor, Ed Balls MP, proposed that the OBR should independently audit the

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51 Establishing the Office for Budget Responsibility, Letter from interim OBR to Chancellor, 12 July 2010, paras 44-46

52 OBR, Annual report and accounts 2013-14, 4 June 2014, para 4.17 – 4.19

53 HM Treasury. Memorandum of Understanding between Office for Budget Responsibility, HM Treasury, Department for Work and Pensions and HM Revenue & Customs, April 2011; OBR. Memorandum of Understanding between the Office for Budget Responsibility and HM Treasury – the macroeconomic model

54 Letter from Robert Chote to Andrew Tyrie, Chairman of the Treasury Committee, 12 October 2010

55 HL Deb 17 June 2010 c133WA

56 Establishing the Office for Budget Responsibility, Letter from interim OBR to Chancellor, 12 July 2010, para 57

costings of the spending and tax measures contained in Labour's manifesto for the 2015 election.

HM Treasury's 2015 review of the OBR ruled out expanding the OBR's role to include costing of opposition policies as it 'risks the credibility of the institution and a loss of focus'. [57]

Role discussed and ruled out prior to the OBR's introduction

The costing of Opposition parties' fiscal proposals happens, for example, in the Netherlands, and was discussed when the OBR was being introduced. Professor Simon Wren-Lewis of Oxford University was in favour of this model:

> David Rutley: There seems to me some consensus amongst you that there needs to be a wider commentary function for the OBR going forward. Just to test the outer limits though, you have mentioned the fiscal council in the Netherlands, which has gained a reputation for costing government policies and also opposition policies. Would the OBR or should the OBR go that far, just, again, trying to test what the outer limit should be, in the commentary function?
>
> Professor Wren-Lewis: Can I start by a simple answer, and that is "yes". I think that is a good thing to do anyway because I think it will raise the level of public debate around elections, it would stop opposition parties promising to do everything without costing it properly. I also think it would foster independence, the notion of independence, because you would start a dialogue not just between the OBR and the Government, which is a necessary dialogue and is always going to be there, but you also start a dialogue with the Opposition. I think that would be useful for independence as well. [58]

In October 2010, the Chancellor said that the House should debate and decide whether the OBR should cost Opposition parties' policies:

> this is genuinely a matter that should be debated in the House in a non-partisan way, because it does not affect just this Parliament. There is a question of whether we want the OBR to be able to cost Opposition policies at the time of a general election. I propose to have discussions with Opposition party leaders about whether that is the appropriate thing to do, and it would be a legitimate matter for the House to debate and decide. [59]

In its response to the Treasury Committee report, however, the Government rejected this idea, saying that the OBR "should not examine alternative fiscal or other policy scenarios, including those proposed by political parties." [60] This was because the Civil Service Code tightly controls the degree to which civil servants may examine Opposition parties' policies and that the principle of political impartiality

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57 HM Treasury, HM Treasury review of the Office for Budget Responsibility, Led by Sir Dave Ramsden, Chief Economic Adviser to HM Treasury, September 2015, page 6

58 Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, Q86

59 HC Deb 12 October 2010 c142

60 *Government response to the House of Commons Treasury Committee 4th Report of Session 2010-11, Office for Budget Responsibility*, Cm 7962, November 2010, para 2.23

should also apply to the OBR. The Government re-iterated its view in the light of Labour's September 2013 proposal discussed below. [61]

Issue re-emerges prior to 2015 General Election

In his speech to the 2013 Labour Party Annual Conference Mr Balls said that the Party would ask the OBR to cost its manifesto for the 2015 General Election. [62] Labour's Shadow Chancellor followed this up with a letter laying out the proposal to the OBR's Chairman, Robert Chote:

> The reform I am proposing would mean the Opposition would submit costings for proposed manifesto commitments on spending and tax – obtained for example, from the House of Commons Library, Parliamentary Questions or the Institute for Fiscal Studies – and the OBR would 'provide independent scrutiny and certification' of these costing. [63]

Robert Chote provided some support for the idea in principle whilst suggesting that practical issues may stand in the way of the OBR performing such a role for the 2015 general election:

> As I have discussed [in oral evidence to the Treasury Select Committee] I believe that independent scrutiny of preelection policy proposals could contribute to better policy making, to a more informed public debate, and could help facilitate coalition formation when party programmes need to be reconciled. But we should not underestimate the significant practical issues that would need to be addressed - issues that would affect the political parties and the civil service at least as much as the OBR.
>
> First and foremost, it would be essential to establish clear 'rules of the game' for all involved, well before the election, and to ensure that adequate resources were in place to do the job properly. To embark on this exercise in a rush, or with insufficient resources, could be very disruptive for the parties and very damaging to the OBR.
>
> Putting it bluntly, if Parliament wished us to play this role in the 2015 election, we would need a clear steer in the very near future to have any hope of putting the necessary practical arrangements in place in time to deliver a smooth process. Indeed advocates of the reform may now feel that it would be better to consider these issues at the beginning of the next parliament- with a view to being fully prepared before the subsequent election- rather than rush into it for 2015 and risk undermining support for the idea in the longer term. [64]

Legal advice provided to the OBR suggests that primary legislation would be required for the OBR's role to include the costing of Opposition parties' fiscal proposals. [65]

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61 For instance see: HC Deb 29 April 2014:c693; HC Deb 11 March 2014:c165; HC Deb 10 December 2013:c118

62 Ed Balls MP's speech to Labour Party Annual Conference 2013

63 Letter from Ed Balls MP to Robert Chote, Chairman of the OBR, 22nd September 2013. A copy of the letter is available from http://budgetresponsibility.org.uk/transparency/letters/

64 Letter from Robert Chote to Andrew Tyrie, Chairman of the Treasury Committee, 12 March 2014. A copy of the letter is available from http://budgetresponsibility.org.uk/transparency/letters/

65 As discussed in a letter from Robert Chote to Ed Balls MP on 23rd September 2013, available from http://budgetresponsibility.org.uk/transparency/letters/

HM Treasury's internal review recommends no expansion of OBR's remit

HM Treasury's 2015 review of the OBR (see section 6) concluded that its role should not be expanded to include the costing of Opposition policies. The review concluded that such an extension of the OBR's clearly defined and focused remit would risk its credibility and a loss of focus.[66]

In particular the review was concerned about the potential impact on the civil service. Policy costings are not produced by the OBR themselves; rather, costings are produced by the Government and certified by the OBR. The review's opinion was that costing opposition policies would raise constitutional issues and conflicts of interest for civil servants, who work the Government.[67]

To help third parties cost alternative polices the review recommended that the Government and the OBR should make more data and tools available.

7.3 A commentary role

Another issue is the extent to which the OBR should have a wider "commentary" role in addition to its fiscal forecasting duties. Tim Besley, Professor of Economics at the LSE, and a former member of the Bank of England Monetary Policy Committee, has argued that the OBR should be able to look at all issues relating to fiscal sustainability:

> I am strongly of the view that if the broad object of the organisation is to safeguard fiscal sustainability in the UK, it has to have a remit that allows it to range over the entire set of issues that are germane to that. Taking an example from the past, had the OBR existed since, say, 2000, I would hope it would have produced commentary on some of the risks around fiscal policy with respect to the taxation that was being raised from the financial sector and that it would have felt perfectly justified to raise such an issue independently because it felt it was an important part of the outlook. To constrain artificially in any way the ability of this body to comment on what is germane to that broad objective I think would compromise its independence and compromise its institutional integrity. I feel pretty strongly that some aspect of a commentary function has to be accepted within its remit under the broad heading of achieving fiscal sustainability.[68]

The IFS has argued that while it is sensible for the fiscal target to be set by the Government, it would be appropriate for the OBR to make a public assessment of whether "any changes to the rules it is tasked with policing are consistent with the ultimate objective of long-term

66 HM Treasury, HM Treasury review of the Office for Budget Responsibility. Led by Sir Dave Ramsden, Chief Economic Adviser to HM Treasury, September 2015, page 6
67 Further discussion is available in paras 3.61 – 3.93 of HM Treasury review of the Office for Budget Responsibility
68 Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, Q82

sustainability". The IFS warned against the OBR advising on broader economic policy issues.[69]

The Government decided, however, to limit the OBR's "commentary" role. The Charter for Budget Responsibility states that the OBR:

> The OBR should not provide normative commentary on the particular merits of Government policies.[70]

The Treasury Committee is in agreement with this arguing that it would be inappropriate for the OBR to play a role in setting the fiscal mandate and that comment should not be made on individual measures.[71]

7.4 Establishing credibility

It is clearly important that the OBR has credibility. However, fiscal forecasting is notoriously difficult. For example, government borrowing is the difference between revenue and expenditure – both very large numbers. Small errors in forecasting these can make a large difference to the forecast for borrowing.[72] There is a danger that if the OBR is judged solely by the accuracy of its short-term forecasting it will lose credibility. The issue was raised by Tim Besley in evidence to the Treasury Committee:

> The problem with putting too much weight on the short- and medium-term forecasting is that this organisation is bound to fail if that is the way in which we judge it, because we know that the success of short-term economic forecasting is extremely limited, and for good reasons; it is just not a science, if you want to call it a science, or an art, that is fully developed to a point where we can rely wholly. It does not mean forecasts are unintelligent or based on deliberately misleading data. It is just the nature of the exercise, and so if this organisation is judged on the basis of whether it happens to forecast well over a two-year horizon and we come back in two years and say, "Oh, you got it wrong and therefore this organisation is not serving an important social purpose," I think that would be the wrong way to look at it. What matters is the quality of the commentary around fiscal risks and fiscal sustainability that will make this organisation useful in the public debate, and we have to firmly put that at the centre of what we are trying to achieve with OBR, in my view.[73]

Professor Wren-Lewis agreed with this point:

> I could not agree with that more. I think the dangers to the credibility of the organisation of focusing on the short-term forecasting role are very large because forecasts are always wrong. Also, I think it would be unfortunate because it puts the focus on the short term, whereas issues to do with fiscal policy much more medium and long-run in nature. So I think it is essential for the OBR to not just provide that role but also to look

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69 Institute for Fiscal Studies, The IFS Green Budget: February 2010, pp257-58

70 HM Treasury, Charter for Budget Responsibility autumn 2016 update, para 4.12

71 Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, para 64

72 For example, in its June 2010 Budget forecast the OBR forecast receipts of £548 billion and spending of £697 billion in 2010/11, giving a deficit of £149 billion (Table C7 p90). If receipts were 1% higher and spending 1% lower, the deficit would be £137 billion – a difference of £12 billion or over 8%.

73 Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, Q82

> at issues of long-run sustainability, doing medium to long-run forecasts as well, in a sense possibly putting that at least on an equal footing with its role in producing the pre- and post-budget forecast.[74]

In its report on the OBR, the Treasury Committee argued that while there should be scrutiny of the OBR's forecasts, "absolute accuracy is not a useful criterion." Their quality could be assessed relative to other forecasts.[75]

The OBR assess the performance of their forecasts annually in their forecast evaluation report.

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74 Ibid

75 Treasury Committee, Office for Budget Responsibility, Fourth Report of Session 2010-11, HC 385, 21 September 2010, para 39

Appendix 1: Previous fiscal rules of the Charter for Budget Responsibility

The table below provides any changes to the fiscal rules contained in the Charter for Budget Responsibility.

Charter	The fiscal mandate	Supplementary debt target	Cap on welfare spending	Interim target from 2015/16
April 2011 Charter	a forward-looking target to achieve cyclically-adjusted current balance by the end of the rolling, 5-year forecast period.	a target for public sector net debt as a percentage of GDP to be falling at a fixed date of 2015-16….	cap not introduced until March 2014 Charter update	n/a
March 2014 Charter upate	same as April 2011 Charter	same as April 2011 Charter	the cap on welfare spending, at a level set out by the Treasury in the most recently published Budget report, over the rolling 5-year forecast period, to ensure that expenditure on welfare is contained within a predetermined ceiling.	n/a
December 2014 Charter update	a forward-looking aim to achieve cyclically-adjusted current balance by the end of the third year of the rolling, 5-year forecast period.	an aim for public sector net debt as a percentage of GDP to be falling in 2016-17….	same as March 2014 Charter update	n/a
Autumn 2015 update	[in normal times] a target for a surplus on public sector net borrowing in each subsequent year	[for the period until 2019/20] a target for public sector net debt as a percentage of GDP to be falling in each year	same as March 2014 Charter update	a target for a surplus on public sector net borrowing by the end of 2019-20
Autumn Statement 2016 update	a target to reduce cyclically-adjusted public sector net borrowing to below 2% of GDP by 2020-21	a target for public sector net debt as a percentage of GDP to be falling in 2020-21	that expenditure on welfare in 2021-22 is contained within a predetermined cap and margin set by the Treasury at Autumn Statement 2016	

Previous versions of Charter for Budget Responsibility

- Autumn 2016 update
- Autumn 2015 update
- Autumn Statement 2014 update
- March 2014 update
- April 2011

Annex 1: International examples of fiscal councils

The OBR maintains a list of fiscal councils overseas.

Simon Wren-Lewis, Professor of Economics at Oxford University, has produced the following list which is taken from his website:

Austria

The Government Debt Committee was established in 2002, comprises 14 members, and receives financial support from the Austrian Central bank. It provides recommendations on the direction of fiscal policy, and the overall fiscal stance.

Australia

Following the recommendations Joint Select Committee (see here), a Parliamentary Budget Office is to be established in 2012. The focus is on project costing, but the office may also decide to comment on macroeconomic budgetary issues. Mr Phil Bowen has been appointed as the inaugural Parliamentary Budget Officer.

Belgium

The Federal Planning Bureau, established in 1994, provides a range of services along similar lines to the CPB in the Netherlands. In addition, the High Council of Finance, which was reformed in 1989, overseas the coordination of regional and national fiscal policy. It sets medium term objectives for regional and national budget deficits, and proposes annual targets, which form the basis for government negotiations. The High Council is chaired by the Minister of Finance, but has representatives from inside and outside government. Although it has no formal decision making power, it does exert considerable influence. The influence of the High Council is analysed in Coene (2010).

Canada

The Parliamentary Budget Office provides independent analysis to Parliament on the state of the nation's finances, the government's estimates and trends in the Canadian economy, and upon request estimates of the financial cost of any specific proposals. It has a staff of 14.

Denmark

The Economic Council, established in 1962, prepares economic reports and forecasts on a range of issues including fiscal policy. It has four members and a staff of around 35.

Germany

The German Council of Economic Experts comprises five members and a staff of around 30. The Council was established in 1963 to advise on a wide variety of economic policy issues, including macroeconomic fiscal policy. The federal government has to publish its comments on the Council’s annual report.

Hungary
The Fiscal Council of the Republic of Hungary was set up in 2009 as 'an independent state institution that endeavours to ensure the responsible management of public resources.' It prepared macroeconomic forecasts which represented the baseline for budgetary decisions. It also provided comment and advice on fiscal planning more generally, within the context of existing fiscal rules, with a total staff of around 35. Some of its reports were critical of government proposals or forecasts. In early 2011 the Hungarian government replaced the Council with a three person body that was widely perceived as a less effective fiscal policy watchdog (see, for example, a letter to the Financial Times ($) from three directors of other fiscal councils).

Ireland
After plans outlined here, the members of the Irish Fiscal Advisory Council were announced in June 2011. The Council reports formally at least 3 times per year. It has five members, and a secretariat of three.

Netherlands
The Netherlands Bureau for Economic Policy Analysis (often referred to as the CPB, for Central Planning Bureau) was founded in 1945. It is an independent research institute and has its own independent external advisory body. It provides economic and fiscal forecasts as inputs into the budgetary planning process. It also evaluates (at the party's request) the election programme of government and opposition parties. The Bureau also provides economic expertise over a wide range of specific issues, such as labour market reform, and has a staff of over 110.

Portugal
The Portuguese Public Finance Council (Conselho das Finanças Públicas, CFP) was created in 2011. The CFP was created by the 5th amendment to the Budget Framework Law in May 2011. The members of the board were appointed in December 2011, and took office in mid February 2012. Its mission is to undertake an independent assessment of the consistency, compliance and sustainability of fiscal policy and to enhance, through increased transparency, the quality of democracy and economic policy decision-making and to reinforce the financial credibility of the State. The Council will present reports on: the Stability Programme and other procedures within the European regulatory framework of the Stability and Growth Pact; the multi-annual framework of budgetary planning; the draft State budget; the sustainability of the public finances; as well as on other subjects it considers relevant.

Slovakia
On 27th June 2012 the Slovak Parliament elected the three members of the newly created Council for Budget Responsibility by constitutional majority: Ivan Sramko (chair), Michal Horvath and Ludovit Odor. An early discussion is contained in a paper by Horvath and Odor.

Slovenia
The Public Finance Act of 2009 requires the creation of an independent advisory body to provide assessments of the public finances.

South Korea
The National Assembly Budget office (NABO) was established to support the legislative activity of the National Assembly of Korea in 2003. Its aim is to be a 'fiscal institution that assists in the examination of the national budget and accounts in the legislative body via impartial and non-partisan research and analysis'. It currently employs around 120 staff. It has a wide ranging remit, and provides analysis of particular micro and macro issues as well as macroeconomic trends.

Sweden
In 2007 the Swedish Fiscal Council was established. The Council consists of eight members and is assisted by a secretariat with four employees. The mission of the Council is to provide an independent evaluation of the Swedish Government´s fiscal policy. Its first director, Lars Calmfors, has a paper describing the initial experience of the council. The current director is Lars Jonung.

United Kingdom
In 2008 the Conservative Party outlined its proposal for an Office of Budget Responsibility. Some comments on the original UK proposal are here, and in Chapter 11 of the Institute of Fiscal Studies' Green Budget. The case for a UK Fiscal Council is presented in written form in Kirsanova et al (2007), in Power Point or, to my embarrassment, video form here, and as a dialog between Tim Besley and Romesh Vaitilingam here (see also Besley and Scott (2010)). The new (May 2010) Conservative/Liberal government, as one of its first acts, set up an interim Office for Budget Responsibility (OBR), chaired on an interim basis by Sir Alan Budd. Within weeks it produced its first pre-budget report, and shortly afterwards it produced the forecasts that were part of an 'emergency' Budget. In July 2010 a debate began on the structure of the permanent OBR. The Treasury Select Committee have taken evidence on this issue (its report is here - note that their international evidence is taken from this webpage), and Lars Calmfors, director of the Swedish Fiscal Council, has also made an interesting contribution. Legislation establishing the permanent OBR has recently been approved by parliament. Sir Alan Budd was replaced by Robert Chote, and the OBR has already produced a number of reports. An account of its formation and structure is given in Wren-Lewis, 2011b. When the OBR revised down its estimate of potential output in November 2011, the Chancellor revised his medium term fiscal plans as a result (see here)

United States
The Congressional Budget Office (CBO) has a mandate to provide the United States Congress with 'objective, nonpartisan, and timely analyses to aid in economic and budgetary decisions on the wide array of programs covered by the federal budget and information and estimates required for the Congressional budget process.' Established in 1974, it

provides objective and impartial assessments ('scoring') of policy proposals that have a significant influence on decision making. It also provides an overall assessment of the likely path of deficits and debt into the medium term. It has a staff of around 250. It produces an annual assessment of the outlook for the government budget, including projections that go to 2080.

Other institutions

The European commission also has a survey of all independent and quasi-independent institutions involved is fiscal policy in the EU countries.The Federal Planning Bureau, established in 1994, provides a range of services along similar lines to the CPB in the Netherlands (see below). In addition, the High Council of Finance, which was reformed in 1989, overseas the coordination of regional and national fiscal policy. It sets medium term objectives for regional and national budget deficits, and proposes annual targets, which form the basis for government negotiations. The High Council is chaired by the Minister of Finance, but has representatives from inside and outside government. Although it has no formal decision making power, it does exert considerable influence.

Annex 2: Links to further information

The Act

Budget Responsibility and National Audit Act 2011

Parliament webpage for the Act

The Bill

Budget Responsibility and National Audit Bill [HL]

Explanatory notes to the Bill

OBR

OBR website

Establishing the Office for Budget Responsibility, Letter from interim OBR to Chancellor, 12 July 2010

Treasury

HM Treasury Press Notice, Chancellor announces policies to enhance fiscal credibility, 17 May 2010

Letter from the Chancellor to Robert Chote, Chair of the OBR, setting out terms of reference for the OBR, 12 October 2010

Treasury Committee

Treasury Committee, Office for Budget Responsibility, HC 385, 21 September 2010

HM Treasury, Government response to the House of Commons Treasury Committee 4th Report of Session 2010-11: Office for Budget Responsibility, Cm 7962, November 2010

IFS

IFS *Green Budget 2010*, Chapter 11, "Reforming UK fiscal institutions"

IFS Press Release, Keeping official fiscal forecasts honest, 12 November 2009. This contains the text of the section on the OBR of Robert Chote's November 2009 Scottish Economic Society/Royal Bank of Scotland Annual Lecture

Other

IMF, Fiscal Rules – Anchoring Expectations for Sustainable Public Finances, 16 December 2009. This gives an overview of the theory of fiscal rules and international experience. There is a table on p14 showing fiscal rules in other countries.

How it's done in Sweden, *Guardian*, 29 July 2010, Lars Calmfors (chair of Sweden's Fiscal Policy Council)

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