HOUSE OF LORDS

In Focus

Budget Responsibility and National Audit (Fiscal Mandate) Bill [HL] (HL Bill 14 of 2016–17)

Key Provisions

The Budget Responsibility and National Audit (Fiscal Mandate) Bill [HL] is a private member's bill introduced by Baroness Kramer (Liberal Democrat). The Bill received its first reading in the House of Lords on 24 May 2016, and is scheduled to have its second reading on 9 September 2016.

The Bill would amend the Budget Responsibility and National Audit Act 2011. The Act provided that the Treasury must prepare a Charter for Budget Responsibility and that the Charter must include a fiscal mandate to show how the Treasury's objectives, in relation to fiscal policy, would be attained.[1] The Bill contains two clauses. Clause 1 would provide that, in preparing the fiscal mandate under section 1(2)(b) of the Budget Responsibility and National Audit Act 2011, the Treasury must have regard to:

- the need for continued investment in infrastructure;
- the need to ensure that the fiscal mandate does not have a substantially negative impact on intergenerational fairness; and
- the need to ensure that the economy of the United Kingdom remains competitive.

Clause 1 of the Bill would also ensure that, in considering the above provisions, the Treasury "must consult independent experts". Clause 1 states that the meaning of "infrastructure" would be taken in accordance with section 1(2) of the Infrastructure (Financial Assistance) Act 2012; therefore "water, electricity, gas, telecommunications, sewerage or other services; railway facilities (including rolling stock), roads or other transport facilities; health or educational facilities; court or prison facilities, and housing". Clause 1 defines the term "intergenerational fairness" as "the overall wealth of future generations". Clause 2 states that the legislation would be applicable to the whole of the United Kingdom.

Background

The Budget Responsibility and National Audit Act 2011 created a legal responsibility for the Treasury to prepare a document known as the Charter for Budget Responsibility, which must set out: the Treasury's objectives in relation to fiscal policy and its policy for the management of the national debt; the means by which the Treasury's objectives in relation to fiscal policy would be attained ("the fiscal mandate"); and the requirements of the Financial Statement and Budget Report.[2] The Act provided that the Treasury may "from time to time" modify the Charter and that it must lay the Charter (or modified

Charter) before Parliament. The Charter would not come into force until it had been approved by a resolution of the House of Commons.

When the Coalition Government introduced the first Charter in 2011, its fiscal mandate was for the cyclically-adjusted current budget to be balanced by the end of the rolling five-year forecast period.[3] The "current budget" is defined as the difference between government revenue and current expenditure (rather than capital expenditure).[4] In December 2014, the Government published an updated Charter which explained that the fiscal mandate would "aim to achieve cyclically-adjusted current balance by the end of the third year of the rolling five-year forecast period".[5] The Treasury explained that this meant that at Budget 2015, the target year for the fiscal mandate would be 2017/18. The Treasury stated that the update reflected "the progress that has been achieved in tackling the deficit" which meant that the mandate could be "safely shortened to create a tighter constraint on future fiscal policy choices".[6]

At the 2015 general election, the Conservative Party manifesto pledged to achieve an overall budget surplus, noting that it "will ensure that in normal economic times, when the economy is growing, the Government will always run a surplus in order to reduce our national debt and keep our economy secure".[7] The manifesto described this as a "new fundamental principle of fiscal policy".[8] The Institute for Fiscal Studies (IFS) explained that the "major difference" between the Conservative Party proposal and what the Coalition's fiscal mandate aimed to achieve was that "the Conservative Party want to achieve an overall budget surplus—rather than just a surplus on the current budget—in other words, the Conservatives want to ensure that government revenues are sufficient to pay not only for current spending but also for investment spending".[9]

Following the 2015 general election, the Conservative Government published a draft Charter, at the Summer Budget 2015, which included in its fiscal mandate the Government's new principle of fiscal policy—to achieve an overall budget surplus.[10] In an Autumn 2015 update, the current Charter was introduced by George Osborne, the then Chancellor of the Exchequer. This contained within it the same mandate for fiscal policy that had been published in July 2015.[11] It was laid before the House of Commons on 12 October 2015 and was passed by 320 votes to 258 on 14 October 2015. The fiscal mandate, within the new Charter, included three key targets. It set an interim target for a surplus on public sector net borrowing—that is, on the public sector's overall budget—by the end of 2019/20.[12] Once a headline surplus has been achieved, the mandate sets a target for a surplus on public sector net borrowing in each subsequent year. In addition, the mandate set out that, until 2019/20, there would be a supplementary target: for public sector net debt to fall as a percentage of GDP in each year.[13] The mandate explained that the targets in the Charter applied "unless and until the Office for Budget Responsibility (OBR) assess, as part of their economic and fiscal forecast, that there is a significant negative shock to the UK".[14] A significant negative shock is defined in the mandate as "real GDP growth of less than 1 percent on a rolling four-quarter-on-four-quarter basis".

Mr Osborne explained that the updated mandate was required because the UK should reduce its "exorbitant debts" and run a surplus in normal times to "prepare for the future so that it has the resources to help the poorest and the most vulnerable when economic bad times come".[15] However, the mandate received some criticism. When the Charter was laid before the House of Commons, the Labour Party and the Scottish National Party (SNP) both argued that, while tax and receipts should cover day-to-day spending, the Government should borrow for capital investment. The Shadow Chancellor of the Exchequer, John McDonnell, expressed Labour's view that "[t]he Government's refusal to invest will be embedded in this Charter as it now moves on to limit all public sector borrowing".[16] He stated that the deficit should be tackled, but "to a timescale that does not jeopardise sustainable growth in our economy".[17] Speaking on behalf of the SNP, Stewart Hosie, Shadow SNP Westminster Group Leader for the Economy, explained that "to set out a charter with a fixed target with a fixed timescale—namely, to run a fiscal surplus by 2019/20—is precisely to remove any flexibility that might be required in the meantime".[18] He stated that, "essentially" the Chancellor was cutting billions more than was "necessary" to run a balanced budget, by cutting from welfare and from "essential" capital expenditure.[19] He added: "[w]hat we need more than anything is growth, and governments cannot cut their way to growth".[20]

Following the UK vote to leave the European Union in the 2016 referendum, George Osborne made a statement on 4 July 2016 which suggested that the Government's fiscal targets may be withdrawn:

> We must be realistic that the target for a surplus is unlikely to be achieved in 2019–20. The Office for Budget Responsibility will conduct a formal assessment when it produces a new independent forecast in the Autumn, and then we will have a clear idea of what additional measures are required to maintain fiscal credibility.[21]

Since then, the new Prime Minister, Theresa May, and the new Chancellor of the Exchequer, Philip Hammond, have both suggested that the Government's fiscal targets will be suspended.[22] On 19 July 2016, Mr Hammond noted that the surplus rule "came with the caveat" that if the Office for Budget Responsibility forecast four rolling consecutive quarters of less than 1 percent annualised real GDP growth, the target would be suspended—which is likely to be forecast in the 2016 Autumn Statement.[23] On 20 July 2016, Mrs May explained that the Government had "not abandoned the intention to move to a surplus" but that it "will not target that at the end of this Parliament".[24] On the same day, the Financial Secretary to the Treasury, Jane Ellison, said that:

> Any revision of our responsible fiscal framework would be set out following a thorough assessment of the economic data. […] That is why we have no plans to withdraw the Autumn 2015 update of the Charter for Budget Responsibility. As the Chancellor and Prime Minister have made clear, we will update the House with further details in the usual way, through an Autumn Statement later this year.[25]

Baroness Kramer's Bill sets out measures that would need to be considered when preparing any new fiscal mandate. During the 2016 Queen's Speech debates, Baroness Kramer noted that the Government's "fiscal plans required continued austerity to cut all public borrowing, which, because of their definitions, means a huge constraint on infrastructure spending for the future".[26] She added that "spending on infrastructure is investment and should not be included as day-to-day spending when considering eliminating the deficit". Baroness Kramer has since explained the purpose of her Bill as "an attempt to reform" the Government's fiscal mandate.[27] She noted her view that "the Charter passed by the Government under George Osborne set three budgetary rules, the most important of which was the aim to create an overall surplus in public sector net borrowing by 2019/20". Baroness Kramer indicated that there was "significant opposition to this rule", stating that:

> [It] moved away from the Coalition definition of the 'deficit', which was based on […] all day-to-day spending, but not including capital expenditure. By changing this definition, the Government was required to also reduce capital expenditure, or pay for capital expenditure by cuts in departmental budgets.

She explained that the provisions in the Bill would require the Treasury to look at "using a measure other than total public borrowing within any fiscal mandate or setting out clearly how infrastructure expenditure is to be continued at a level necessary for growth". The Bill would also "require the Government to consider the impact of fiscal rules on intergenerational fairness", based on Baroness Kramer's concerns that the fiscal consolidation has "disproportionally hit younger generations", and would require any new fiscal charter "to consider the need for the economy to remain competitive". Various aspects of these issues were debated in more detail in a recent House of Commons debate on the Charter for Budget Responsibility on 20 July 2016.[28]

[1] Budget Responsibility and National Audit Act 2011, section 1.
[2] Budget Responsibility and National Audit Act 2011, sections 1(2)(a)–1(2)(c).
[3] HM Treasury, *Charter for Budget Responsibility April 2011: Presented to Parliament pursuant to Section 1 of the Budget Responsibility and National Audit Act 2011*, 4 April 2011.
[4] The House of Commons Library has explained that the current budget is the difference between current receipts and current expenditure (including depreciation). Public sector net borrowing is the difference between current receipts and current expenditure (including depreciation) and public sector net investment. For further information, see: House of Commons Library, *The Office for Budget Responsibility and Charter for Budget Responsibility*, 19 August 2016.
[5] HM Treasury, *Charter for Budget Responsibility: Autumn Statement 2014 Update*, December 2014, p 7.
[6] HM Treasury, 'Updated Charter for Budget Responsibility', 15 December 2014.
[7] Conservative Party, *Conservative Party Manifesto 2015*, 13 April 2015, p 9.
[8] ibid.
[9] Institute for Fiscal Studies, 'How Do the Parties' Fiscal Targets Compare?', 19 September 2014.
[10] HM Treasury, *Charter for Budget Responsibility: Summer Budget 2015*, July 2015, p 9.
[11] HM Treasury, *Charter for Budget Responsibility: Autumn 2015 Update*, October 2015, pp 7–8, paras 3.2–3.7; the proposed budget surplus rule was discussed by the then Chancellor, George Osborne, prior to the Summer Budget in a speech at Mansion House on 10 June 2015. George Osborne had previously noted the Conservative Party's objective of achieving an overall budget surplus in the next parliament in a speech at the Conservative Party conference in September 2013.
[12] HM Treasury, *Charter for Budget Responsibility: Autumn 2015 Update*, October 2015, p 11.
[13] ibid.
[14] ibid.
[15] HC *Hansard*, 14 October 2015, cols 427 and 429.
[16] ibid, col 434.
[17] ibid, col 439.
[18] ibid, col 442.
[19] ibid, col 444.
[20] ibid, col 444.
[21] HC *Hansard*, 4 July 2016, col 622.
[22] HC *Hansard*, 20 July 2016, col 818; and HC *Hansard*, 19 July 2016, col 665.
[23] HC *Hansard*, 19 July 2016, col 665.
[24] HC *Hansard*, 20 July 2016, col 818.
[25] ibid, col 920.
[26] HL *Hansard*, 25 May 2016, col 489.
[27] Text provided by Baroness Kramer on request from the Library.
[28] HC *Hansard*, 20 July 2016, cols 895–926.