



Australian Government

The Treasury



Australian Government

Department of Finance and Deregulation

Joint Select Committee on the Parliamentary Budget Office

Submission

Department of the Treasury
Department of Finance and Deregulation

January 2011

CONTENTS

1. INTRODUCTION	1
2. BACKGROUND	1
2.1. The rationale for a Parliamentary Budget Office.....	1
2.2. The Australian federal context.....	2
2.3. Roles of the Treasury and Finance	4
3. MANDATE FOR AN AUSTRALIAN PARLIAMENTARY BUDGET OFFICE.....	7
4. DESIGN OF AN AUSTRALIAN PARLIAMENTARY BUDGET OFFICE	11
4.1. Institutional location and governance	11
4.2. Interaction with government agencies.....	12
4.3. Confidentiality.....	13
4.4. Resourcing	14
5. CONCLUSION.....	15
APPENDIX A: TERMS OF REFERENCE	17
APPENDIX B: JURISDICTIONAL CASE STUDIES.....	18
Canadian Parliamentary Budget Officer (PBO).....	18
US Congressional Budget Office (CBO).....	20
Netherlands Bureau for Economic Policy Analysis (Central Planning Bureau (CPB))	22
UK Office for Budget Responsibility (OBR).....	24
New South Wales Parliamentary Budget Office (PBO).....	25
APPENDIX C: ADDITIONAL INFORMATION ON ECONOMIC FORECASTING AND POLICY COSTINGS.....	27
1. Treasury domestic economy forecasting.....	27
2. Forecasting tax and modelling taxation new policy proposals.....	28
3. Costing new expense, capital and non-tax revenue proposals	30

1. INTRODUCTION

In its post-election agreements with the Australian Greens and Independent MPs, signed between 1 and 7 September 2010, the Government agreed to establish a Parliamentary Budget Office (PBO) within the Parliamentary Library within 12 months, with its structure, resourcing and protocols to be subject to the decision of a special committee of the Parliament. The 'Agreement for a Better Parliament' also specified that the PBO would provide independent costings, fiscal analysis, and research to all members of parliament, especially non-government members.

The Joint Select Committee on the Parliamentary Budget Office was established on 18 November 2010, to report by 31 March 2011. The terms of reference for the inquiry are at Appendix A.

The Departments of the Treasury (the Treasury) and Finance and Deregulation (Finance) have been invited to make a submission to the Inquiry.

The Treasury and Finance welcome the opportunity to provide a submission to the Inquiry. This submission addresses the rationale for a PBO in the Australian context, key issues concerning the design of a PBO, and provides information on the role of, and work conducted by, the Treasury and Finance.

Overall, the departments see merit in the establishment of a PBO. In particular, we consider that a PBO could present an opportunity for members of Parliament, particularly non-government members, to have available additional analysis of the Budget, evaluation of fiscal policy settings independently from government and policy costing advice.

In considering the most appropriate design of a PBO in Australia, it will be important to take into account the broader context in which the PBO will operate. Australia's fiscal and budget frameworks, underpinned by the *Charter of Budget Honesty Act 1998*, the *Financial Management and Accountability Act 1997* and the *Commonwealth Authorities and Companies Act 1997*, are seen as strong and credible, including by the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF). However, a well-designed PBO with a clear mandate could further enhance these frameworks.

In addition, we note that there are a number of key design issues, for example around access to information and confidentiality which, if not adequately addressed, could impact on the PBO's ability to fulfil its mandate.

2. BACKGROUND

2.1. The rationale for a Parliamentary Budget Office

In recent years a debate has emerged internationally and in Australia about the possible role of independent fiscal institutions. As countries struggle with fiscal deficits and rising public debt, some observers have pointed to evidence of inadequate fiscal discipline and weak fiscal management by some governments.¹

1 Debrun, X et al 2009, 'Independent fiscal agencies', *Journal of Economic Surveys*, vol 23, no. 1.

In response, international organisations such as the OECD and IMF have advocated for more robust and transparent fiscal frameworks and an increased role for national legislatures in scrutinising fiscal policy and budgetary matters in order to enhance transparency and accountability.²

It has also been argued that the establishment of an independent fiscal agency or budget office can help to facilitate this scrutiny by being a source of independent advice and analysis for parliamentarians.

More recently, in light of significant fiscal difficulties in some economies, it has also been argued that such institutions can support the credibility of a government's fiscal consolidation plans by undertaking independent fiscal forecasts and reporting.

A number of independent budget offices exist internationally and also more recently within Australia at the state government level. While these institutions have generally been established with the same broad objective, their functions, institutional location and size vary considerably.

Pre-existing institutional and fiscal frameworks and the circumstances which led to the establishment of each institution differ from country to country and have influenced the design and functions of the agencies.

These institutions' responsibilities range from acting as an additional source of information for parliamentarians on budget and fiscal policy matters and policy costings, assessing and analysing the Government's fiscal reporting, conducting economic and fiscal forecasting separately from government agencies, to being provided the authority for instituting and achieving fiscal targets similar to the role of independent monetary institutions.

Prominent examples include the US Congressional Budget Office, which is an institutionally distinct, well-resourced office whose inputs are essential to the preparation and approval of the US budget, the Dutch Central Planning Bureau, the Canadian Parliamentary Budget Office, and the Swedish Fiscal Policy Council. In Australia, New South Wales passed legislation to establish a Parliamentary Budget Office in 2010.

Further information on a selection of existing independent budget offices can be found at [Appendix B](#). While these examples of existing independent budget offices provide valuable case studies and information, there does not appear to be any 'off-the-shelf' model which can be simply translated into the Australian context.

Given this, the work of the Committee in considering design options for the circumstances that apply in Australia is clearly necessary so that it is possible to take into account the pre-existing institutional and fiscal frameworks in which it will operate.

2.2. The Australian federal context

In Australia, fiscal policy is a key responsibility of the Australian government. Australia's fiscal framework is based on the principle that the government determines fiscal policy and reports on the country's economic and fiscal position.

² Anderson, B 2009, 'The changing role of Parliament in the Budget process', OECD Journal on Budgeting, vol 1.

The **Charter of Budget Honesty Act 1998** (the Charter), which provides one of the legislative bases for fiscal policy, requires the government to set out a fiscal strategy based on principles of sound fiscal management and to publish and table in the Parliament regular fiscal reports. This includes the publication of an economic and fiscal outlook report with each budget, a mid-year economic and fiscal outlook report, a tax expenditures statement and a final budget outcome. These reports contain multi-year forward estimates, medium-term projections (along with regular inter-generational reports) and extensive risk assessments and sensitivity analysis.

The Charter also requires the Secretaries of the Treasury and Finance to publish an economic and fiscal update within 10 days of the issue of writs for a general election, and provides for the Treasury and Finance to cost election commitments submitted by the major political parties during election periods.

These overarching fiscal frameworks are underpinned by more detailed portfolio-specific requirements, where agencies must assess, monitor and report on their respective outcomes against agreed performance objectives and benchmarks.

This reporting is supported by formal accountability arrangements including for example, the Auditor-General, who is an independent officer of the Parliament and reports to Parliament on areas of public administration, including public sector finances.

These reporting and accountability arrangements are taken into careful consideration by international organisations such as the IMF and the OECD when evaluating the quality of fiscal frameworks in Australia and other countries. Our frameworks have consistently been recognised as strong and credible.³

This has enabled the Federal Parliament to play its important role in scrutinising government finances. While the executive branch of government has carriage of fiscal policy and is responsible for developing and managing the budget, the Parliament has the constitutional oversight of government finances. Australia's Constitution states that 'no money shall be drawn from the Treasury of the Commonwealth except under appropriation made by law'.

The budget, in the form of appropriation bills and any associated bills introducing new policies, therefore has to be approved by both Houses of Parliament. Similarly, the government has to seek the Parliament's approval of taxes which have to be imposed by legislation.

In addition, estimates of proposed annual expenditure of government agencies are referred by the Senate to committees for examination and report. This process provides an opportunity for senators to question and scrutinise government expenditure and programs.

Still, the budget management role of the Parliament in the Australian political system is different to that in some other countries with independent fiscal institutions. The US Congress, for example, has a more explicit role in budgetary processes due to the strict separation of the legislature and executive in the US,

3 For example: IMF Staff Report for the 2009 Article IV Consultation (<http://www.imf.org/external/pubs/ft/scr/2009/cr09248.pdf>, accessed 25/01/2011); OECD, 2010, Economic Survey of Australia, OECD Economic Survey series.

which underpins the distinct structure and design of the Congressional Budget Office.

2.3. Roles of the Treasury and Finance

The Treasury and Finance jointly play a central role in Australia's fiscal framework. These departments have responsibility for providing advice to the government on the economy, government finances, the budget and fiscal policy issues.

The departments prepare the annual budget and other reports required under the Charter. This includes managing budget processes and conducting the analysis necessary for providing information on the economic and fiscal outlook.

The Treasury conducts extensive macroeconomic modelling and prepares macroeconomic forecasts, including medium and longer-term projections. These economic forecasts provide an understanding of the broad developments within the economy and the balance of risks surrounding the economic outlook. They inform policy settings and underpin the calculations of budget estimates of expense and revenue.

The departments also provide advice on taxation (the Treasury) and effective government spending arrangements (Finance and the Treasury). This involves proposing and analysing policy options and costing new policy proposals. These costings play a central role in informing government decision-making.

The departments also conduct costings for the Government and the Opposition during the caretaker period under the Charter and the Secretaries release the Pre-Election Economic and Fiscal Outlook within 10 days of the issue of writs for a general election.

Fiscal estimates and policy costings

As part of their roles, the Treasury and Finance provide advice on policy development as well as fiscal estimates of revenue and expense, and costings for new policy proposals.

Significant resources are devoted to the estimates updates and costing exercises, both by the Treasury and Finance, as well as the Australian Taxation Office (ATO), and relevant Australian Government agencies for expense proposals.

A key element that informs this quantitative analysis is the outlook for the economy.⁴ Treasury generally has two major forecasting rounds in the year. One is used as the basis for the Government's forecasts published in the budget each May. The other forms the basis for the revised forecasts published in the Mid-Year Economic and Fiscal Outlook (MYEFO) in October-January. Two other rounds are also held, around June and December.

The forecasts are developed using a mix of explicit econometric models and other forecasting tools, information from business liaison discussions, as well as specific expert professional advice and judgement, including that from other organisations

⁴ The outlook includes forecasts for the major macroeconomic aggregates such as GDP and the CPI and a considerable number of economic parameters for revenue and expenses purposes.

such as the Australian Bureau of Agricultural and Resource Economics and the ATO (see [Appendix C](#) for more information).

The forecasts are also subject to an external quality test at the Joint Economic Forecasting Group meeting, where the forecasts are discussed with representatives from the Reserve Bank, the Departments of the Prime Minister and Cabinet and Finance and Deregulation, and the Australian Bureau of Statistics (ABS).

The considerable resources devoted to this exercise across the Australian public service (including as part of their duties around 30 Treasury officers on the domestic economic outlook and a smaller group on the international side) provide decision makers with a robust and consistent view of the economic outlook upon which to base policy decisions.

From a policy development perspective, there are obvious advantages in using consistent forecasts and assumptions for the economic outlook when considering alternative policy options. It also helps reduce disagreements or confusion about the financial impacts of policy which would otherwise be driven by differences in view about the economic outlook.

The Treasury is accountable for costing new taxation policy proposals and forecasting taxation revenue over the forward estimates period, while Finance undertakes the costing of new expense, capital and non-tax revenue proposals and forecasting expense and non-tax revenue over the forward estimates period.

In relation to the revenue and expense bases, the two departments generally utilise existing models to forecast changes in particular revenue and expense heads drawing upon the updates to the economic forecasts. Any new policies are assessed and quantified against these baselines.

The challenge with costing any new revenue or expense policies is that data on the relevant tax base or eligible recipient in the case of an expense item, is often incomplete, and may need to be drawn from a variety of sources of varying reliability and in many cases may require supplementation by professional assumptions and judgement.

It may also be the case that some data is subject to legal constraints, for example with respect to taxpayer secrecy provisions or confidentiality constraints in ATO, ABS and other data. This may affect the capacity of both the Treasury and Finance to access underlying data, or provide it to other organisations.

In addition to these constraints, when working with and interpreting these data it is very important to have an intimate understanding of the data sources, how the data are constructed, and the limitations in their measurement.

Costing new policies often requires the development of complex models, and in many cases it may not be possible to model the full detail of proposals and simplifying assumptions will be required. It is often also just as important to model the direct cost of proposed changes, as well as likely behavioural effects.

Understanding these likely impacts invariably requires considerable policy experience and research. Research used in a costing can vary along a spectrum ranging from academic research, in-house data analysis, and information obtained from sources such as industry (for instance, through consultations), or other Australian Government entities.

The experience of past similar policy changes or the application of sensitivity analysis and judgement as to the likely magnitude of responses is also assessed.

Major policy proposals (such as climate change policy) that are likely to have an economy-wide impact may be modelled through computable general equilibrium techniques. Staff trained in calibration and interpretation of these models are able to analyse the economic impact of a major policy, which then forms the basis for estimating its revenue impact.

The costing of policy proposals cannot credibly be undertaken in isolation from broader policy development. In practice, costings are a highly iterative process, and require close links to policy developers to produce reliable estimates.

From a quantitative perspective, different modelling skills are required to build, maintain and use the range of external and in-house models and, in many circumstances, case specific models. These skills range from econometric skills through to statistical analysis, micro simulation and actuarial skills.

In addition to these basic modelling skills, modelling of taxation policies requires a strong working knowledge of the taxation system across a broad range of policy areas. Advice from officials in the ATO on complex tax interactions may be required. This is also true of expense proposals, where the experience, skills and judgement of Finance officials is supported by expert advice from officials in a range of other Australian Government agencies.

Generally speaking, the combination of specific policy development knowledge, experience and quantitative skills are in short supply and require considerable time to develop.

Significant resources are devoted to policy costings across the public service. In both the Treasury and Finance, because of the integrated nature of policy costings and development, it is difficult to clearly demarcate between officers solely devoted to policy costings and other policy officers.

In the Treasury, taxation policy costings and revenue estimation are undertaken by the Tax Analysis Division which has around 50 staff. Staff are also engaged in Revenue Analysis Branch of the Australian Taxation Office to provide costing advice for revenue new policy proposals, support the revenue estimation processes and prepare taxation statistical information. As well as providing input and support to the Treasury, these staff also provide analytical support within the ATO. The Budget Policy Division and other Divisions in the Fiscal Group of the Treasury also provide advice and input on Budget estimates and their evolution through time.

In Finance there is no costing unit per se. Rather, the officials available to analyse and cost proposals constitute the Budget Group of around 250 employees. The Group is broken down into Agency Advice Units (AAUs) which are typically responsible for an individual portfolio, where they hold expertise not only in estimates and financial matters, but also policy and legislation. They seek data and the advice of officials in other Australian Government agencies when required.

More detail on the nature of the estimates and costings approaches, and forecasting processes adopted by Treasury and Finance is included in [Appendix C](#).

3. MANDATE FOR AN AUSTRALIAN PARLIAMENTARY BUDGET OFFICE

The mandate for the PBO will determine its role in Australia's institutional framework, the scope of its work and its clients. For it to be effective, the PBO's responsibilities and functions will need to be clearly articulated, including in any enabling legislation. This will provide the Parliament, the government and the public with certainty about its role and inform associated questions such as appropriate resourcing and staffing.

As noted earlier, in considering an appropriate mandate for the PBO, it is important that the fiscal policy context in Australia and the Australian political system more broadly are taken into account.

In this respect it is worth recognising that, especially since the legislation of the Charter, Australia's fiscal frameworks are already well regarded internationally, particularly in respect of the detail and transparency provided through the publicly released documentation.

In some countries independent budget offices have been proposed in response to a need to improve the reliability and transparency of fiscal estimates. However Australia's arrangements have generally performed well in this regard.

Given this, it is likely that a PBO would have the potential to help strengthen existing fiscal institutions by enhancing information flows and providing some tailored analysis to non-government parliamentarians on budget and fiscal policy issues.

Research and analysis of budget and fiscal policy issues

In particular, a PBO could present an opportunity for Parliament to have available additional analysis of the budget and evaluation of fiscal policy settings independently from government, beyond that which is already available through existing research support from the Parliamentary Library.

This would give Parliament greater resources to obtain information and an additional avenue for scrutinising the government's budget and fiscal policies. A PBO also has the potential to boost accountability by making this type of work available to the public at large.

In addition, a PBO could be a valuable resource for members of Parliament on financial issues. This could help provide all Parliamentarians with access to a deeper and more comprehensive view of the key issues and factors impacting on fiscal estimates.

By also taking on an educational role, a PBO could improve the capacity of Parliament to assess the annual budget and make decisions when considering related legislation, in particular appropriation bills and other legislation with fiscal implications, which also improves existing accountability mechanisms such as the Senate Estimates Committee process.

In view of the scope for an educative role for a PBO, there may be merits in a PBO producing: regular publications such as an annual post-Budget commentary which analyses the government's budget papers; research items covering relevant topics on

budget and fiscal policy issues; and educational products and seminars for members of parliament.

This work could focus on making available relevant information which may provide parliamentarians with greater access to advice on fiscal and budget policy issues.

In addition, it may be desirable that members of parliament are able to request the PBO to undertake non-routine work should they require specific research and other analytical work on budget and fiscal policy issues. The PBO may be able to address such requests confidentially, an issue which is further discussed below.

Costings

The 'Agreement for a Better Parliament' states that the PBO would provide independent costings. The agreement does not specify the nature of these costings but could potentially encompass: analysis of major costings made by the Government on key initiatives; costings of policy proposals by non-government members of parliament; and/or costings of election commitments during caretaker periods.

When considering these options it will be important to remain mindful of the considerable resources required to undertake costings. As outlined in section 2.3., costings require highly professional skills in policy knowledge and quantitative capabilities, as well as specific case models and other more generic models, alongside comprehensive data.

While it would not be cost effective to replicate the resources of the Treasury and Finance within the PBO, there are a number of private sector entities which could provide assistance to the PBO in costing or analysing various policies where its in-house capacity is being developed, or in relation to highly specialised requests.

In this respect, a PBO which is well placed to analyse costings of major government initiatives could enhance Parliament's consideration of proposals which have wide-ranging implications for the budget and the economy more broadly.

Many of these policies require legislation to be passed by Parliament, and a PBO could help to improve the capacity of the parliament to scrutinise legislation and to target questions about the financial implications of such policies and pose policy alternatives or variations.

However, having two separate publicly funded set of costing arrangements duplicating each other's role would not be cost-effective from a public finance perspective, may create confusion, and is unlikely to be feasible in any case, certainly in the short term, given that many of the necessary resources are already in short supply.

A PBO may place a greater strain on existing Treasury/Finance resources because of the likely need to assist the PBO with its work, analyse, check and potentially respond to PBO costings.

Fully duplicating the costing role of the Treasury and Finance has the potential to lead to confusion or conflict around estimates, rather than the substance of government policy options.

As explained in section 2.3, because costings often depend heavily on assumptions and rely on a wide range of input sources and models tailored specifically to a particular policy issue, differences in costings would not necessarily improve public knowledge. It will therefore be important to avoid confusion over costings as it has the potential to undermine some of the main objectives surrounding the establishment of a PBO.

However, this issue may not arise as prominently in the case of policy costings of non-government proposals. At present, non-government members of Parliament generally do not have the opportunity to have their policies separately costed at taxpayer expense.⁵ However, issues may still arise where PBO costings performed for an opposition or minor party become Government policy at a future time (for instance, due to a change in government) and the Treasury/Finance recosting does not align with the PBO estimates.

Many new policy proposals have far-reaching financial implications and require complex costings and access to and familiarity with specific data in order to provide a good indication of their costs. Providing non-Government parliamentarians with access to such costings via a PBO could enable policy proposals to be assessed early in their development.

For such arrangements to work effectively, close cooperation between a PBO and Treasury/Finance in matters such as costing conventions, benchmarks, data and methodology would be necessary to ensure that costings produced by a PBO can be undertaken on a compatible basis with Budget costings.

Providing this service could also help non-government members cost policies in the lead-up to an election being called. Such an arrangement was in place for the 2010 election.

In response to the Labor Government's Operation Sunlight paper and the Murray Review of Operation Sunlight which argued the benefit of providing better access to costings, funding was provided to the Parliamentary Library to 'enhance the capacity of the Parliamentary Library to assist non-Government parties in developing policies in the lead-up to federal elections'.

The Library established the Pre-Election Policy Unit (PEPU), which conducted and commissioned a number of costings prior to the 2010 election. While the timing of the election and resourcing limited the use of the facility in 2010, an evaluation after the election indicated that the services of the PEPU were valued, and that there is a need for a comparable service to be available to parliamentarians on an ongoing basis.⁶

Election costings

Currently, the Prime Minister and the Leader of the Opposition, through the Prime Minister, can request the Secretaries of the Treasury and Finance to cost their publicly released policies during the caretaker period under the Charter of Budget

5 The post-election agreements between the current Government and the Australian Greens and the Independent Members of Parliament include the provision that these parties' may submit new policy proposals to the Office of the Prime Minister for analysis by the relevant portfolio Minister and department, and where required, for costing by the Departments of Treasury and Finance.

6 Bartos, S 2010, 'Evaluation of the Pre-Election Policy service', Australian Parliamentary Library. LECC consultancy report.

Honesty. This provision is aimed at making the resources of the public service available to both major parties and reducing incumbency advantage and the Charter arrangements have generally served this purpose well.

Should the mandate of the PBO include the costing of election commitments under the Charter, a number of challenges could arise.

This type of work requires significant resources during an election period when there is a high demand for costings. During the 2010 election period, for example, the Treasury and Finance released 128 costings. This involved the work of approximately 300 staff who currently work in costing-related areas. For the PBO to be able to respond to these costing requests in a timely manner, the PBO would require similar staffing levels to those employed by the Treasury and Finance, which would duplicate existing resourcing.

As discussed earlier, costings require highly experienced specific professional skills, access to and familiarity with specialised data, as well as ‘off the shelf’ and tailored financial and economic models designed for specific public policy costings.

Further issues could arise with regards to potential differences between costings done by the PBO during the caretaker period and subsequent costings by the Treasury and Finance once the government has taken office.

Protocols may need to be established to allow the Treasury and Finance to ensure that budget estimates are robust and that consistency is maintained across all costings included in the budget.

The Charter would also need to be amended to remove or change the role of the Treasury and Finance in relation to election costings.

Given the context of costings in the Australian political system, a PBO which performed a costing role primarily for proposals of non-government members of Parliament, with the capacity to analyse the costings undertaken by government on major initiatives, could be a workable mandate for the PBO.

We consider that during the caretaker period the current Charter arrangements should remain in place and allow for election costings to be undertaken by the Treasury and Finance for the major parties, although some greater clarity around the possible role of the PBO in costing proposals from other Parliamentarians may be required.

This approach would seem to strike an appropriate balance between additional support to non-government parliamentarians and cost effective costing resources funded by the public purse.

Clients

Consistent with the post-election agreements that state that the PBO would conduct its work for members of Parliament, the services of the PBO should be available to all members and senators of the Federal Parliament. Additionally, there may be scope for the PBO to conduct work for parliamentary committees, as occurs in Canada.

Workload

In establishing the PBO, consideration will need to be given to establishing protocols that allow the office to manage its workflow and ensure that high quality output can be produced in a timely manner.

Regardless of the options chosen, the PBO would have to be able to balance its responsibilities with regards to routine output with requests for non-routine work from members of parliament.

Such a mechanism will be particularly important if the mandate for the PBO includes costings. As mentioned above, costing requests could lead to a very high workload, especially in the lead-up to an election and during the election period.

Protocols would have to be transparent in how the PBO makes decisions on workflow and outputs. In considering an appropriate mandate for the PBO, workload and resourcing, which is further addressed below, will need to be taken into account.

4. DESIGN OF AN AUSTRALIAN PARLIAMENTARY BUDGET OFFICE

4.1. Institutional location and governance

The post-election agreements state that the PBO should be established within the Parliamentary Library. The Parliamentary Library sits under the Department of Parliamentary Services (DPS) which provides services to the Parliament. The functions of the Library are outlined in the *Parliamentary Service Act 1999* (PS Act) which establishes the Parliamentary Librarian as a statutory office holder.

Locating the PBO within the Parliamentary Library ensures that the PBO can operate, and is seen to be, fully independent from the executive government. It also offers opportunities for leveraging the existing resources, structure, reputation, and legislation of the Parliamentary Library and DPS.

The Parliamentary Library currently provides independent, high-quality information, analysis and advice to Parliament, and is well-respected in this role.

In this respect, the Library already conducts some research related to the budget and had expanded that role when it was provided with funding in 2010 to assist members of parliament in costing of policies ahead of the federal election.

Within the context of establishing the PBO within the Parliamentary Library, there are a number of options with regards to governance arrangements:

- 1) The PBO is established within the Parliamentary Library structure and the functions of the PBO are specified in legislation, but assigned to the Parliamentary Librarian (as the independent statutory office holder), through amendments to the PS Act. The head of the PBO would not be a statutory office holder;
- 2) The PBO is established within the Parliamentary Library structure and headed by a Parliamentary Budget Officer who would be designated as an independent statutory office holder under the PS Act, but he/she would still

report to and be accountable to the Parliamentary Librarian as the head of the Parliamentary Library; or

- 3) The PBO is established within the Parliamentary Library structure and headed by a Parliamentary Budget Officer who would be designated as an independent statutory office holder under the PS Act, and the Parliamentary Budget Officer and the Parliamentary Librarian have joint responsibility/accountability for the functions of the Parliamentary Library.

While all options are consistent with the agreements and ensure the independence of the PBO, the first option offers the greatest opportunity for effectively making use of the existing structures and processes of the Parliamentary Library. This is likely to reduce the need for significant additional resources for the PBO that relate primarily to pure administrative arrangements.

The first option also provides the greatest clarity with regards to accountability and reporting structures. Establishing a Parliamentary Budget Officer alongside the Parliamentary Librarian could create tension and uncertainty around the respective responsibilities and/or accountabilities of the two officers. This appears to have been problematic in the Canadian context. Assigning the functions of the PBO to the Parliamentary Librarian could help avoid these potential issues.

4.2. Interaction with government agencies

In order for the PBO to conduct high quality analysis and provide useful advice, the PBO will likely need access to a range of economic and financial information from government agencies.

As outlined earlier in section 2.3 in relation to the functions of the Treasury and Finance, specific policy expertise and judgements as well as data and models are used to produce advice on fiscal and economic matters.

During the course of their work, the Treasury and Finance rely heavily on data from a variety of sources, as well as models which have either been developed over many years or are specifically set up to deal with a new issue.

At present, the Parliamentary Librarian can request information from government agencies. There are no provisions within the PS Act empowering the Parliamentary Librarian to compel government agencies to provide information.

As access to data and information will likely be important to the work of the PBO, consideration may need to be given to establishing arrangements to facilitate access to information, where that information cannot be accessed via other sources or substitutes found.

Formal protocols around information sharing, for example a memorandum of understanding or other protocols between the PBO and relevant agencies, could be put into place. Alternatively, legislation could be put in place that would compel agencies to provide requested information. However, compelling agencies to provide information could create conflict with the *Public Service Act 1999* (Public Service Act), which requires agency heads to manage their departments for the benefit of their Minister. This would be in conflict with the statutory responsibility for the Parliamentary Librarian to provide confidential services.

Information protocols, on the other hand, could incorporate the flexibility required to balance agencies' responsibilities under the Public Service Act and the confidentiality requirement under the PS Act. The protocols would need to take into account the type of information government agencies are able to provide, capacity constraints and public release of information.

The use of information protocols would require careful drafting, especially in relation to the *Freedom of Information Act 1982* (FOI Act) which regulates the release of information by Australian Government agencies. Provisions would need to be made to allow agencies to refuse requests on the same grounds that documents can be exempted under the FOI Act and for the review of those decisions.

This would include commercially valuable information (for example purchased inputs and equations), information produced for the purpose of deliberative processes or the national economy, and documents produced for the dominant purpose of submission to the Cabinet or produced for the dominant purpose of briefing a Minister about such a document.

There are also other types of data which government agencies use in their work that could not be provided to the PBO. This includes administrative data from the tax and transfer systems to which access is limited due to privacy and taxpayer secrecy provisions and some private sector information which is provided to agencies on a confidential basis with legal sanctions that could apply if not handled appropriately.

In establishing protocols, consideration will also need to be given to the potential of PBO requests placing pressure on the resources of government agencies. Government agencies will need to put in place mechanisms to set priorities for responses to PBO requests *vis-a-vis* other activities, especially work requested by the government to which the public service is held to account. Of particular concern are times when capacity is already stretched, such as in the lead up to the budget and other fiscal and economic updates.

In addition, it is important to note that access to information held by Australian Government agencies alone will not enable the PBO to provide independent advice to Parliament. In order to carry out high-quality and credible work which complements the work conducted by the Treasury and Finance, the PBO cannot rely on access to raw data alone, but will need to develop an appreciation for and familiarity with such data and alternative sources.

4.3. Confidentiality

It will also be necessary to establish whether the outputs of the PBO would remain confidential or publicly disclosed. The PS Act currently provides that advice from the Parliamentary Librarian to members of Parliament should be performed 'in a timely, impartial and confidential manner'.

Under current protocols, the Parliamentary Library publishes routine output, but provides responses to non-routine requests from parliamentarians on a confidential basis, unless otherwise agreed. These arrangements allow the public to benefit from the routine research of the Library, but enable parliamentarians to seek confidential advice.

In keeping with the PBO's providing enhanced research and support capability to the Parliament, it is suggested that a similar arrangement could be adopted for the outputs of the PBO.

Where output from the PBO includes, or is based on, information obtained from Australian Government agencies, agencies will need to retain their obligation to inform their Minister about requests in line with the Public Service Act, however it is envisaged that caretaker provisions will continue to apply to the Public Service.

In some cases, Australian Government agencies may also wish to make the information provided to the PBO publicly available, similar to the practice of publishing information released under the FOI Act.

This is particularly important should potential problems arise if confidential PBO advice is later revealed to be in conflict with advice provided by government agencies.

4.4. Resourcing

Funding

In order for the PBO to operate effectively, the resources provided need to be aligned with its mandate. This is important in order for the PBO to engage the appropriate staff and potentially consultants, and develop the necessary expertise required to produce high quality output.

If the PBO is unable to fulfil its functions due to limited resourcing, it will likely be unable to establish and maintain the necessary credibility and authority. The Canadian PBO, for example, experienced some issues during its establishment phase with regards to resourcing.⁷

Funding will be required for the head of the PBO, appropriately qualified staff (see below), purchasing of data and economic models, and engagement of consultants, if necessary. The exact initial and ongoing resourcing implications cannot be determined until a final decision has been made on the mandate, design and operation of the PBO.

In considering the mandate for the PBO and its resource implications, consideration will need to be given to duplication of work. If the PBO is provided with the same or similar functions to those of the Treasury and Finance, two distinct streams of activity would be funded to provide essentially the same product.

By virtue of being established within the Parliamentary Library, the PBO could leverage the existing resources of the Library. This may limit the need for significant additional resourcing, particularly for the establishment phase. The PS Act provides that the DPS Secretary must provide resources to the Parliamentary Librarian in accordance with an annual agreement approved by the Presiding Officers.

As the PBO would be located within the Parliamentary Library, the resourcing of the PBO could also be determined in accordance with this provision. Explicit

⁷ Jeffrey, B 2010, 'Accountability and Officers of Parliament: The Case of the Parliamentary Budget Officer', Canadian Political Science Association.

arrangements for allocating funding between the PBO and Parliamentary Library may also need to be considered.

Funding would be appropriated to DPS which will have to request the initial funding and any future increases through the budget process.

Staffing

The appointment of the head of the PBO will be dependent on the institutional location of the PBO. Matters such as the credibility of the PBO and the need to avoid any perceptions of a politicisation of the appointment process will also need to be considered.

Subject to the structure and institutional location of the PBO, the appointment of the head of the PBO could be determined by the Presiding Officers for a defined term (for example, three years) as is the case for the Parliamentary Librarian. Due to the technical speciality that is required for this role, the Presiding Officers may wish to seek advice on such an appointment from the Secretaries of Finance and the Treasury.

To enshrine the security of the position, the grounds for termination (for example, misbehaviour or physical or mental incapacity) could also be subject to a decision by the Presiding Officers as is the case for the Parliamentary Librarian.

Remuneration and level of the head of the PBO must be determined in context of the mandate of the PBO and institutional design. Staffing of the PBO will play an important role in ensuring the effective operation of the PBO. The staff will need to be highly qualified in areas such as economics, government finances and public policy. In considering the appointment of the head of the PBO and other staffing, it is important to note a shortage of skilled professionals in these areas.

In particular, should the mandate of the PBO include the costing of policies, it will likely take some time to attract the right mix of in-house skills and during the establishment phase, there may be a need to draw more heavily on external consultants.

While the PBO may be able to access financial information and models from the Treasury and Finance, extensive professional knowledge and experience will also be required to utilise and interpret the information (see Appendix B for elaboration).

5. CONCLUSION

The post-election 'Agreement for a Better Parliament' outlined a commitment to establish a PBO within the Parliamentary Library. The idea of establishing an additional publicly funded fiscal organisation has been raised on a number of occasions, with proposals for widely varying mandates.

In the Australian context, and given the role of the Parliament in scrutinising budget proposals put forward by the executive, a case can be made for additional support and analysis to non-government parliamentarians.

While significant public resources are already devoted to preparing fiscal estimates and policy costings, these resources are in practice legislatively aligned to support the workings of government.

A PBO could present an opportunity for members of Parliament, particularly non-government members, to have available additional analysis of the Budget and evaluation of fiscal policy settings independently from government. This has the potential to enhance and expand the information available to the Parliament.

A mandate which also enables the PBO to undertake costings for proposals of non-government members of Parliament, with the capacity to analyse the costings undertaken by government on major initiatives, with election costings continuing under the Charter arrangements, would appear to be a workable model.

Consistent with the 'Agreement for a Better Parliament', the PBO would be located within the Parliamentary Library. This would also offer opportunities for leveraging the existing resources, structure, reputation, and legislation of the Parliamentary Library and DPS.

Additional arrangements, including appropriate staffing arrangements and funding, memoranda of understanding and information protocols with various government agencies, would need to be put in place so that the PBO can fulfil its mandate.

It will also be necessary to recognise that the development of in-house expertise, particularly in respect of policy costings, will likely take some time to develop and that external consultant support may be a feature of the PBO during its establishment phase.

APPENDIX A: TERMS OF REFERENCE

The Joint Select Committee will inquire into and report on:

- (a) the appropriate mandate for the Parliament Budget Office (PBO);
- (b) the nature of information needed to assist the Parliament in its consideration of matters related to the budget;
- (c) the role and adequacy of current institutions and processes in providing this information, and the areas in which additional support is required;
- (d) the scope for a PBO to fulfil its mandate in a cost-effective manner; and
- (e) bearing in mind these considerations, the most appropriate structure, resourcing and protocols for a PBO, including but not limited to:
 - (i) the PBO's functions and lines of accountability and oversight;
 - (ii) the routine work expected of the PBO and the minimum reporting requirements;
 - (iii) the protocols for members of parliament requesting non-routine work of the PBO, including the types of work and the rules for prioritising and carrying out these requests;
 - (iv) the protocols around access to and disclosure of the PBO's work and any confidentiality requirements;
 - (v) the protocols around the PBO's relationships with other institutions and processes, including government departments and agencies; and
 - (vi) an appropriate level of staffing, appropriate qualifications for staff, and resources to allow the PBO to fulfil its mandate; and
- (f) in conducting its inquiry, the Committee may choose to consider the operation and effectiveness of similar offices in other parliamentary democracies and their relevance to Australian circumstances

APPENDIX B: JURISDICTIONAL CASE STUDIES⁸

Canadian Parliamentary Budget Officer (PBO)

The position of the PBO was created due to the following factors:⁹

- parliamentarians expressed frustration over the persistent underestimations of projected federal budgetary deficits followed by a period of persistent underestimations of federal surpluses; and
- parliamentarians also indicated they do not have sufficient access to financial expertise to effectively scrutinise the budget.

Following the change of government in 2006, the *Parliament of Canada Act* (the Act) was amended, establishing the position of the PBO in December 2006. The appointment of the first PBO commenced in March 2008.

Mandate

Section 79.2 of the Act assigns the PBO four main duties:

- provide analysis on the state of the nations finances and trends in the national economy to both chambers of Parliament;
- undertake the above research upon request of any of the listed committees (these include all committees with a mandate to consider government estimates);
- when requested by such a committee, conduct research into those estimates; and
- upon request by individual members of parliament or a committee provide estimates of the financial cost of proposal over which Parliament has jurisdiction.

In providing independent analysis to parliamentarians the PBO provides three core products and services:

- research conducted on request from committees and parliamentarians
- regular analysis products such as fact sheets, briefing notes, and in-depth economic and fiscal reports working papers, and
- independent research initiated from within the PBO on economic issues.

The PBO provides these products based on a publishing operating model, with collaboration with external experts. Priority is given to the potential to contribute to

⁸ This section has been compiled with information from a variety of sources, including the Submission to the Inquiry into the Parliamentary Budget Office Bill 2010 by the Parliamentary Library, July 2010.

⁹ Submission by the Canadian Parliamentary Budget Officer to the Senate Standing Committee of Finance and Public Administration Inquiry into the Parliamentary Budget Office Bill 2010, July 15 2010.

increasing budget transparency or analysis that may impact the government's finances or the Canadian economy.¹⁰

Governance

Section 79.1 of the Act establishes the position of the Parliamentary Budget Officer, 'the holder of which is an officer of the Library of Parliament'. The Act does not provide for the creation of a separate office as this function is encompassed within the Parliamentary Library.

Section 79.5 of the Act provides the PBO the power to, in the performance of their mandate, enter into contracts and memoranda of understanding and to engage contractors.

The PBO reports to the Parliamentary Librarian who, in turn, is under the direction and control of the Speakers of the Senate and the House of Commons. The Speakers are assisted by the Standing Joint Committee on the Library of Parliament in conducting this overseer's role.

Resourcing

In the 2010-11 financial year, the PBO employed 13 staff and had a budget of CAD2.8 million.¹¹

Appointment of the Head of the PBO

A committee, formed and chaired by the Parliamentary Librarian, submits a list of three names to the Governor in Council who selects the PBO. The appointment is for a renewable term of not more than five years.

Relationship with Government agencies/confidentiality

Section 79.3 of the Act provides that the PBO is entitled to request information from government departments required to fulfil the mandate. However, this power does not extend to seeking access to confidential Cabinet papers (equivalent to the Cabinet-in-Confidence security rating) or information restricted under the *Access to Information Act* (equivalent to the *Freedom of Information Act 1982*).

The PBO currently operates under a 'product-release' approach, which the Standing Joint Committee on the Library of Parliament has found to be incompatible with the current services of the Library of Parliament.¹² The Library guarantees the confidentiality of questions submitted to it by parliamentarians and the support services provided to parliamentary committees. Section 79.4 of the Act also provides that the information received pursuant to section 79.3 must remain confidential.

10 PBO, 'Operational Plan', PBO website, viewed 1 November 2010, http://www2.parl.gc.ca/Sites/PBO-DPB/documents/Operational_Plan.pdf

11 PBO, 'About the PBO', PBO website, viewed 1 November 2010, <http://www2.parl.gc.ca/Sites/PBO-DPB/AtAGlance.aspx?Language=E>

12 Standing Joint Committee on the Library of Parliament, op cit, p 5.

US Congressional Budget Office (CBO)

The CBO was established by the *Congressional Budget and Impoundment Control Act of 1974*. It evolved from a small research unit within Congress to a large office very central to budgeting in the United States.¹³

Mandate

CBO's mandate is to provide the 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
- The information and estimates required for the Congressional budget process.

Budget and Economic Outlook

In late January of each year, CBO reports on the economic and budget outlook, including estimates of spending and revenue levels for the next 10 years under current law. This 'budget baseline' serves as a neutral benchmark against which Members of Congress can measure the budgetary effect of proposed legislation. The budget baseline occurs before the President submits his budget to Congress in February.

Each summer, CBO updates its baseline projections, incorporating a new economic forecast and the effects of laws that have been enacted to date in that session of Congress.

Analysis of the President's Budgetary Proposals

Each year CBO provides an independent re-estimate of the President's budget proposals. This analysis is delivered to the Congress approximately one month after the President submits his budget for the following fiscal year (October 1 to September 30). It permits the Congress to compare the President's spending or revenue proposals to other proposals using a consistent set of economic and technical assumptions.

Cost Estimates

To assist the Budget Committees and the Congress with enforcement of the budget resolution, CBO analyses the spending or revenue effects of specific legislative proposals. It prepares cost estimates of pending legislation and tracks the progress of such legislation in a scorekeeping system. CBO's cost estimates and scorekeeping system show how individual legislative proposals would change spending or revenue levels under current law and help to determine whether those budget effects are consistent with the targets in the Congress's most recent budget resolution.

Governance

The CBO is a federal agency that sits within the legislative branch of the United States government. It employs approximately 250 people, who are appointed by the Director. On the basis of pay and employment benefits, all staff are treated as employees of the House of Representatives.

13 Anderson, B 2009, 'The changing role of Parliament in the Budget process', OECD Journal on Budgeting, vol 1

Resourcing

The Legislative Branch Appropriations Act, 2010 (P.L. 111-68) provided the agency with US\$45.2 million in FY 2010 funding. The CBO employs around 250 staff. The agency is composed primarily of economists and public policy analysts. About three-quarters of its professional staff hold advanced degrees, mostly in economics or public policy.

In addition to its own staff, the CBO also draws upon two expert panels. The Economic Panel consists of eminent economists (including some previous CBO Directors) who serve two-year terms. The panel meets twice yearly and reviews and comments on CBO's preliminary economic forecasts. The Health Care Panel consists of acknowledged experts who meet periodically to examine frontier research in health policy and to advise the agency on its analyses of health care issues.

Appointment of the Head of the CBO

The Director is appointed by Speaker of the House and President of the Senate. The Director appoints all CBO staff below him/her.

Relationship with Government agencies/confidentiality

CBO uses data sources available from the government's statistical agencies. Those sources include the national income and product accounts, the census of manufacturers, the Statistics of Income, the Current Population Survey, and various national health surveys. CBO also uses information provided by relevant government agencies and industry groups to meet specific needs. It appears that all work of the CBO is published, apart from costs estimates for legislative proposals that have not been made public (this is upon request).¹⁴

¹⁴ CBO, 'Preparing and distributing estimates and analyses', CBO website (<http://www.cbo.gov/aboutcbo/policies.cfm>, accessed 25/01/2011).

Netherlands Bureau for Economic Policy Analysis (Central Planning Bureau (CPB))

CPB Netherlands Bureau for Economic Policy Analysis (CPB) was founded in September 1945. It primarily conducts scientific research aimed at contributing to the economic decision-making process of politicians and policymakers.¹⁵

Mandate

The legislated mandate of the CPB is the production of a Central Economic Plan in March which provides estimates for future growth in production, price figures, and national income. The CPB then submits to Parliament a Macroeconomic Outlook (equivalent to the Mid-Year Economic and Fiscal Outlook) in September, which is submitted at the same time as the Government's budget proposals prepared by the Ministry of Finance. As part of the annual debate in Parliament regarding the Government's budget proposals, the CPB will be asked to cost opposition parties' budgetary proposals. These alternative proposals, along with the budget, are considered by Parliament with the budget being approved in December.¹⁶

In addition to the budget process, the CPB also has a role in the election process. Leading up to the election the CPB publishes medium-term estimates of the Dutch economy and public expenditures, taxation revenues etc. Upon request, the CPB publishes an economic analysis of each party's election platform.¹⁷ Due to the prevalence of coalition governments in the Netherlands (the lower house is proportionally represented, similar to the Australian Senate), the CPB also has a role in analysing the economic impacts of coalition agreements.¹⁸

Ongoing work of the CPB includes short, medium and long-term economic forecasts and estimates of economic effects of policy proposals.

Governance

CPB is a part of the Ministry of Economic Affairs, Agriculture and Innovation. In contrast to the majority of parliamentary budget offices, the CPB is actually part of the executive and not the legislature. Its director is appointed by the Minister, in consultation with other members of the government. However, CPB is considered fully independent as far as the contents of its work are concerned. It also has its own legal mandate and an independent executive and advisory committee.¹⁹

Resourcing

The budget of the CPB is drawn from the Ministry of Economic Affairs. CPB has its own independent external advisory body, the Central Planning committee. The CPC reviews CPB's work plan and provides advice about priorities in this plan.

15 Central Planning Bureau Netherlands Bureau for Economic Policy Analysis (CPB), 'What does CPB do', CPB website, viewed 25 January 2011, <http://www.cpb.nl/en/what-does-cpb-do>.

16 Frits Bos, The Dutch Fiscal Framework: History, Current Practice and the Role of the Central Planning Bureau, OECD Journal of Budgeting Volume 2008/1, p 29
<http://www.oecd.org/dataoecd/42/63/43410966.pdf>

17 *ibid*, p 27.

18 *ibid*, pp 27-28.

19 CPB, 'What does CPB do', CPB website, viewed 25 January 2011, <http://www.cpb.nl/en/what-does-cpb-do>.

The CPB employs over 170 people, most of which are researchers or information analysts.

Appointment of the Head of the CPB

The Law provides that the CPB is to be managed by a board of directors comprising one Director and two Deputy Directors. Their appointment and dismissal is subject to a decision by the Minister of Economic Affairs in consultation with seven other Ministers mentioned in the Law.

Relationship with Government agencies/confidentiality

The CPB publicly releases a number of reports and economic updates, as well as economic policy studies. It appears that all its work is made public.

UK Office for Budget Responsibility (OBR)

The interim OBR was launched in May 2010 ‘to make an independent assessment of the public finances and the economy for each Budget and Pre-Budget Report.’ It will have direct control over the economic forecasts that underpin the budget plans and make all the key judgments that drive the official projections. It will also assess the prospects for achieving fiscal policy objectives, as determined by the Government.

The OBR produced its first forecast before the 2010 June emergency Budget, based on existing policy. It published forecasts for growth and public finances, including figures for the structural deficit — the deficit that remains even when growth in the economy returns — and the cost to service the debt.

Mandate

The interim OBR was tasked with making an independent assessment of the public finances and the economy for the June 2010 Budget. The interim OBR was also tasked to produce forecasts in advance and at the Budget, incorporating the impact of new policy measures. It also has the additional role of assessing the public sector balance sheet and fiscal sustainability.

Governance

The OBR is accountable to parliament to deliver on its terms of reference. The Chancellor retains responsibility for fiscal policy and will set the mandate.

Arrangements for establishing the OBR as a permanent institution are yet to be announced. The interim OBR has been asked to provide a recommendation for the permanent OBR’s roles and responsibilities, aims and objectives, and appropriate size, status, and funding.

Resourcing

The interim OBR consists of a Budget Responsibility Committee (BRC) of three and a secretariat of eight from the HM Treasury. It has full access to the HM Treasury’s resources; however, the BRC should make the key judgements and assumptions underpinning the OBR’s forecasts, analysis and advice.

Appointment of the head

The members of the Budget Responsibility Committee are selected by the Chancellor, but appointments can be vetoed by a committee.

Relationship with Government agencies/confidentiality

The OBR has full access to the HM Treasury’s resources. However, the BRC should make the key judgements and assumptions underpinning the OBR’s forecasts, analysis and advice.

New South Wales Parliamentary Budget Office (PBO)

The position of the Parliamentary Budget Officer was created due to perceived biases by the NSW Treasury in the costing of election commitments towards the incumbent Government.²⁰

The *Parliamentary Budget Office Act 2010* (the Act) was introduced into the NSW Legislative Assembly on 19 October 2010 and was assented to on 1 November 2010.

Mandate

Section 12 of the Act provides that the role of the Parliamentary Budget Officer is to provide independent costings of election promises, however, this is limited to leaders of parliamentary parties only. Section 31 of the Act repealed the *Charter of Budget Honesty (Election Promises Costing) Act 2006* which previously provided for the costing of election commitments by the NSW Treasury.

Section 13 of the Act also provides that the Parliamentary Budget Officer may (at the request of any Parliamentarian, not just a leader of a party), prepare a costing of a proposed policy and ‘provide any analysis, advice or briefing of a technical nature on financial, fiscal, and economic matters (including in relation to the costing of proposals included in the State budget)’.

Governance

The Parliamentary Budget Officer is a statutory office holder of Parliament established by section 5 of the Act. Section 11 of the Act provides that the PBO is to comprise of the Parliamentary Budget Officer in addition to staff members appointed by the Presiding Officers. Section 11 also provides that the staff of the PBO are ‘under the joint control of the Presiding Officers’.

Resourcing

The Minister for Finance confirmed that up to \$4 million will be provided in 2010-11 to establish the PBO, with recurrent funding of up to \$3 million per year with approximately 12 to 16 appropriately qualified staff.²¹

Appointment of the Head of the PBO

Section 6 of the Act provides that the Parliamentary Budget Officer is to be appointed by the Presiding Officers based on recommendations from a panel comprising the Ombudsman, the Information Commissioner and the Chairperson of the Independent Pricing and Regulatory Tribunal.

The Parliamentary Budget Officer is appointed for a period not less than four years and not greater than nine years, with the first Parliamentary Budget Officer to be appointed for a non-renewable period of nine years (Section 7 of the Act).

20 ‘Agreed to in Principle’ speech by the Hon Michael Daley MLA, Minister for Finance, Parliament of New South Wales website, viewed 5 November 2010, [http://www.parliament.nsw.gov.au/prod/parliament/nswbills.nsf/6355a6928b367630ca256e6700008afa/f98fad8032e8ce72ca2577c100208572/\\$FILE/LA%208310.pdf](http://www.parliament.nsw.gov.au/prod/parliament/nswbills.nsf/6355a6928b367630ca256e6700008afa/f98fad8032e8ce72ca2577c100208572/$FILE/LA%208310.pdf)

21 *ibid.*

Relationship with Government agencies/confidentiality

Section 16 of the Act provides that the Parliamentary Budget Officer is entitled to access to information from Government agencies, unless that access is prohibited by the *Government Information (Public Access) Act 2009* (this restriction extends to confidential Cabinet material).

Sections 17 and 22 of the Act provide that information and documents prepared by the PBO are to remain confidential (except to the Parliamentarian who requested it), however if the policy which is the subject of the costing has been publicly announced, the Parliamentary Budget Officer must release the costing.

APPENDIX C: ADDITIONAL INFORMATION ON ECONOMIC FORECASTING AND POLICY COSTINGS

1. Treasury domestic economy forecasting

The Treasury generally has two major forecasting rounds in the year. One is used as the basis for the government's forecasts published in the budget each May. The other forms the basis for the revised forecasts published in the MYEFO in October-January. Two other rounds are also held, around June and December.

As they come soon after the intensive forecasting for the budget and MYEFO (usually published in November) respectively, these rounds tend to be less formal. Sectoral analysts continually monitor economic developments, assessing these data for their implications for the forecasts. Before the start of each forecasting round, information is gathered from business liaison visits. These involve Treasury economists visiting some of the state capitals to speak with businesses, industry organisations and State Treasuries.

The forecasting round enters its intensive phase with the release of the quarterly national accounts, about two months after the end of the quarter to which they refer. The national accounts form the framework for the forecasting exercise.

The technical assumptions about interest rates, exchange rates and oil prices are reset in the light of recent developments.²² The Treasury's International and G20 Division provides its latest assessment of the world outlook. Any changes to fiscal policy are also incorporated. A range of other statistical releases from the Australian Bureau of Statistics and information from other government departments and private sector surveys are also analysed.

Sectoral teams within the Domestic Economy Division assess the implications of all this information for their forecasts using a mix of single-equation econometric models, partial indicators (for example, retail sales for private consumption), leading indicators (for example, housing loan approvals for dwelling investment), business surveys (for example, private sector surveys covering confidence and hiring intentions and the ABS survey of capital expenditure intentions), and advice from specialist agencies such as the Australian Bureau of Agricultural and Resource Economics and Sciences and the Tax Office.

The judgement is informed by economic theory and assessments of recent economic analysis. The teams present and discuss their forecasts with Treasury colleagues and management.

An iterative process is used to ensure consistency between the various elements of the forecast (for example, employment is an important influence on private consumption and hence GDP, but GDP also strongly influences employment). The individual sector forecasts are linked together using the National Accounts Forecasting Framework, rather than in an econometric model. At this stage of the process, the Treasury's macroeconometric model TRYM is used as a consistency check of the forecasts.

An internal quality check of the forecasts follows by presenting them to senior management within the Treasury. They are then subject to an external quality test at the

²² The forecasting rounds assume that the Reserve Bank's cash rate target follows market pricing over the forecasting horizon, and that exchange rates and oil prices will remain around recent average levels. In the case of exchange rates and oil prices, the economic literature suggests forecasters would be unlikely to do any better if they tried to forecast them.

Joint Economic Forecasting Group meeting, where the forecasts are discussed with representatives from the Reserve Bank, the Departments of the Prime Minister and Cabinet and Finance and Deregulation, and the Australian Bureau of Statistics.

2. Forecasting tax and modelling taxation new policy proposals

The Treasury is accountable for costings of taxation new policy proposals (NPPs) and forecasting taxation revenue over the forward estimates period. As the taxation system is an ongoing system of revenue collection, the effect of new policy proposals have to be estimated as the impact on revenue collections that are already included in the forward estimates of taxation revenue, taking account of factors such as the details of the change, the eligible taxpayer population, existing taxpayer behaviour and the impact of the proposal on future taxpayer behaviour.

The challenge with costing taxation NPPs is that such proposals rarely, if ever, involve costing proposals by building the cost up from a zero base, rather they involve measuring the impact of a change on what is a dynamic system. Costings of NPPs are an integral part of the revenue forecasting process, which in turn relies on Treasury's broader economic forecasts and extensive modelling of the impact of the forecasts of parameters on each taxation revenue head.

When costing taxation NPPs, data on the relevant tax base is often incomplete, may need to be drawn from a variety of sources of varying reliability and in many cases may require supplementation by assumptions and judgement. Access to the most detailed data available is important to undertaking costings of new policy, particularly where proposals are affected by factors such as the distribution of taxpayer incomes. In this regard:

- The most detailed and reliable data for undertaking costings of taxation NPPs is tax administrative data, particularly at the unit record level, which provides considerable detail as to the tax base and distributional information for taxpayers. However, access to such data is limited by taxpayer secrecy provisions and the models required to process such data are extremely resource intensive to develop, maintain and run.
- A range of ABS data are available that can be used for modelling taxation NPPs. However, it is often the case that published ABS data lacks the detail required to model taxation proposals and more detailed datasets need to be purchased. The scope of ABS data is also often limited by the scope of the relevant surveys or by confidentiality issues.
 - Other data sources, such as data from other Government agencies has similar issues as ABS data.
- A number of private sector information services offer data and information on companies and industries on a fee for service basis which can be useful information sources in developing costing models.
- Despite the range of data available, it is often the case that data simply does not exist for many taxation NPPs, either because the data is not collected at the level of detail required for a costing or because the proposal itself will result in new as yet unrecorded transactions.

Costing taxation NPPs often requires the development of complex models of the taxation system, with this complexity driven by the complexity of the system itself. In many cases, it may not be possible to model the full detail of proposals and simplifying assumptions will be required. Models of a NPP will require modelling the proposal as the change over the existing system, and ideally would take account of the impact of the proposal on taxpayer behaviour.

Modelling the change in taxpayer behaviour is ideally based on the result of research. The types of research used in a costing can vary along a spectrum including academic research, in-house data analysis, information obtained from sources such as industry (for instance, through consultations), experience of past similar policy changes or the application of sensitivity analysis and judgement as to the likely magnitude of responses. The reliability of the modelling results may vary considerably depending upon the research undertaken.

Costings of NPPs and revenue forecasting are integrated processes, with costings feeding into the revenue forecasts and the overall revenue estimates providing data and parameters for costings. Similarly, costings of taxation NPPs are closely linked to the policy development process, through the costings themselves and analysis of the impact of NPPs. In turn, close links to policy developers is necessary to producing reliable costings of taxation NPPs as close consultation is necessary to properly understand proposals and how they impact on the tax system.

Taxation policy analysis is undertaken using a variety of modelling approaches which in turn requires a variety of skill sets in modellers. Modelling approaches may vary, ranging from:

- ‘tops down’ macro models which use aggregate data and average tax rates to calculate overall tax levels and outcomes (this approach provides revenue estimates but no distributional information);
- ‘grouped distributional’ models which use data that has been categorised according to the ranges of characteristics of taxpayers (e.g. by income bands or by industry) and apply averaged taxation parameters relating to each group to calculate tax outcomes (this approach provides revenue estimates and limited distributional information, but is more data intensive);
- microsimulation models which model taxation outcomes at the individual taxpayer unit record level and apply taxation changes at that level, before aggregating and weighting model outcome to calculate aggregate tax outcomes (this approach provides both revenue estimates and detailed distributional information, but is extremely data and resource intensive); and
- ‘hybrid models’ that combine the approaches above.

Different modelling skills are required to build, maintain and use each type of model above. These skills range from econometric skills through skills in statistical analysis to actuarial skills. In addition to these basic modelling skills, modelling taxation policy requires a strong working knowledge of the taxation system across a broad range of policy areas. Such combinations of skills are in short supply and require considerable time to develop.

The modelling of taxation NPPs is a complex and resource intensive process. This modelling, together with the estimation and forecasting of taxation revenue for the budget, currently directly involves around 50 staff in the Treasury. Additional staff in the

Australian Taxation Office are involved in costings, revenue estimation and forecasting and the preparation and extraction of statistical information from taxation administrative data.

3. Costing new expense, capital and non-tax revenue proposals

Background

The costing of New Policy Proposals (NPPs) is an integral part of the budget process. Finance undertakes the costing of new expense, capital and non-tax revenue proposals while the costing of tax revenue proposals is undertaken by the Department of the Treasury. The majority of costings take place early in the calendar year to ensure that all proposals considered by the Government during the budget process include a financial impact that is reasonable, realistic and comprehensive.

For the purposes of this submission, it is important to differentiate between these 'standard' or agreed costings, and costings undertaken during an election campaign. While the principles used in such costings are similar, the processes are quite distinct, primarily because the process to be followed in costing election commitments is specified in legislation — ie the *Charter of Budget Honesty Act 1998* (the Charter).

The other main difference is the objectives of the respective processes — specifically, the business as usual costing process is often an iterative process, with policy details being finessed as discussions occur about alternative options and assumptions, and these decisions in turn affect the final agreed costing.

With Charter costings, the main purpose is to provide the requesting political party with estimates of particular policies — which can vary considerably in their specificity and development — and they therefore usually require more assumptions than a standard costing. Charter costings also involve interaction between Finance and the author of the proposals which often means, for more complex proposals, policy details may be settled when the policy is being considered for implementation, which may have costing implications.

In terms of the resources available to cost proposals and the relevant organisational structure, there are currently around 250 employees in Budget Group. There is no costing unit per se; rather, Budget Group is broken down into Agency Advice Units (AAUs) which are typically responsible for an individual portfolio.

This has historically been shown to be an efficient organisational structure as it allows AAU staff to build up expertise in their relevant portfolio, in not only estimates and financial matters, but also policy and legislation, and it encourages and promotes effective working relationships with staff within that portfolio. There is also a sharing of knowledge across Finance — for example, AAUs usually seek advice on information technology proposals from the Australian Government Information Management Office.

Agreed costings

Successive governments have applied a budget operational rule that specifies that, prior to being considered by Government, all expense, capital and non-tax revenue NPPs must have had costs agreed with Finance, and all NPPs involving taxation revenue (including tax expenditures/ concessions) must have had costs agreed with the Treasury. While governments retain the right not to always comply with this guideline, successive

governments usually consider this operational rule to be one of good practice and endeavours to ensure compliance as much as possible.

In keeping with this budget rule, therefore, the vast majority of NPPs are subject to a cost assurance process by AAUs within Finance. NPPs are submitted to Finance by agencies and include their estimated financial implications, together with any assumptions, models, data sources, and so on. AAUs then liaise with the relevant agencies seeking further information or clarification to assess the proposal, discuss options and debate relevant issues.

As noted above, the process is an iterative one, with the discussions often assisting the formulation and refinement of policy details. While the quality and access to data and supporting information is obviously an integral component of undertaking a costing, other factors which impact their accuracy include professional judgement based on skills and experience.

The latter is particularly important in this process as knowledge of relevant past and current policies and similar programs, including, for example, existing rates and eligibility criteria — will assist in assessing the costs of alternative options, assessing the expected behavioural responses of industry and/or other groups which would be affected by the new policy or policy change, the viability of the proposed method and timing of implementation, the interplay with other programs, and so on.

Once the costing has been agreed and is submitted to Government for consideration, an NPP becomes a measure if agreed by Government. Although Finance does not formally track NPP costings per se, as costings are undertaken for the majority of measures, it could be assumed that at least 750 costings — exclusive of Charter costings — were undertaken during 2010 as this is the total of both measures that were agreed during 2010 and the number of alternative policy options that were requested by Government. It should be noted, however, that a large number of costings are also undertaken by Finance for NPPs that are considered but ultimately not agreed by the Government. These costings are not included in the above total.

Costing of election commitments

The Charter sets out the principles and processes to be followed in costing election commitments. Under that legislation, the Secretary to the Treasury is responsible for costing proposals affecting revenue, while the Finance Secretary is responsible for costing policies that affect government outlays and expenses.

The process to be followed under the Charter requires election commitments to be submitted by the relevant political party to the Prime Minister who may then refer them to Finance and/or Treasury. Unless the request includes specific assumptions to be used, the costing process undertaken by AAUs would involve such factors as determining the methodology, formulating and defining the assumptions, and determining the type and range of data to be collected.

Under the Charter's guidelines, costings are ideally finalised within five business days and this restriction may limit the amount and type of communication that AAUs have with relevant agencies in terms of seeking supplementary data or information. Once the election costings have been finalised, they are published on the election website.

2010 election costings

In terms of numbers of costings, Finance completed and publicly released 128 Charter costings, with an additional 248 proposals costed by Finance post election. Overall, therefore, a total of approximately 380 costings were undertaken in relation to the 2010 election, bringing the total number of costings during 2010 to in excess of 1,000.