



HM TREASURY

Government response to the House of Commons Treasury Committee 4th Report of Session 2010-11:

Office for Budget Responsibility



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Commons Treasury Committee
4th Report of Session 2010-11:
Office for Budget Responsibility

Presented to Parliament by
the Economic Secretary to the Treasury
by Command of Her Majesty

November 2010

This document contains the Government's response to the House of Commons Treasury Committee's report on the Office for Budget Responsibility (OBR). The Government thanks the Committee for its work in this important area.

On 23 October 2010, the Government published the Budget Responsibility and National Audit Bill. This includes the Government's detailed design for the OBR.

The response is organised into five parts, following the structure of the Committee's report.

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1

Introduction

Recommendation- the interim OBR

1.1 (1) The interim OBR produced a Pre-budget report and a Budget report in a very short space of time. It has increased the transparency of the forecasting process. Members of the Budget Responsibility Committee came to give evidence to us twice, and were exemplary witnesses. We wish to put on record our appreciation of the interim OBR's work, and, in particular, of the leadership given by Sir Alan Budd, Geoffrey Dicks and Graham Parker. (Paragraph 8)

Response

1.2 The Government agrees with the Committee's conclusions. The interim OBR made an important, and hopefully long-lasting, contribution to the development of economic policy-making in this country. The Government echoes the Committee's appreciation of the OBR's work and remains very grateful to Alan Budd, Geoffrey Dicks and Graham Parker, in being the first to lead this new venture.

Recommendation- independent forecasting

1.3 (2) The MPC has a clear policy objective, with a measurable target and control of the instruments to achieve it. If the inflation target is breached, the Governor has to explain to the Government, the Treasury Select Committee and the public. In contrast, the OBR provides a forecast and commentary; it has no responsibility for policy on which it comments or which its work may influence internally. This requires the exercise of particular care and restraint by the OBR. (Paragraph 12)

1.4 (3) The previous Government wished to improve monetary policy-making by giving control of interest rates, within a policy framework set by Government, to an independent Bank of England: the current Government aims to improve fiscal policy making by giving responsibility for forecasting to an independent body. It is a bold step. However the MPC has a clear task and controls the means to achieve it. The OBR has a more complex relationship with Government. (Paragraph 13)

Response

1.5 The Government agrees that there are profound differences between the method and purpose in which monetary policy is undertaken by the Monetary Policy Committee (MPC), and the outsourcing of public finances and economic forecasting, analysis and assessment functions to the OBR.

1.6 The OBR will be required to exercise particular care and restraint in the performance of its duty to examine and report on the sustainability of the public finances. This is why the Budget Responsibility and National Audit Bill, Clause 5 (2) requires that the OBR perform its duty objectively, transparently and impartially, and that the Charter for Budget Responsibility explain this requirement. The Charter for Budget Responsibility will set out this and other guidance to the OBR, as required by Clause 6 of the Budget Responsibility and National Audit Bill.

1.7 The creation of the OBR is a bold step that places the UK at the forefront of international fiscal policy-making and fiscal transparency. The OBR's relationship with Government is important and this is why, as well as the legislative underpinnings in the Budget Responsibility and National Audit Bill and the guidance provided by the Charter for Budget Responsibility, the OBR will agree Memoranda of Understanding (MOUs) providing a framework for interaction with appropriate parts of Government, for example HM Treasury, the Department for Work and Pensions and Her Majesty's Revenue and Customs.

Recommendation- independent fiscal councils

1.8 (4) *The Government has taken a significant step, which is not without risk in seeking to give an independent body responsibility for the forecast. Official forecasts may influence expectations. The benefits of surrendering control over the forecast can only be achieved if the OBR's independence is beyond doubt and its competence is established. The OBR will have to demonstrate a commitment to transparency, objectivity and impartiality over a sustained period if it is to command and retain public confidence. (Paragraph 23)*

Response

1.9 The Government agrees with the Committee's recommendations. The OBR must be independent and expert, and be perceived as such, in order to provide credible fiscal and economic forecasts. In order to achieve this, the Budget Responsibility and National Audit Bill sets out that the OBR must perform its duty "objectively, transparently and impartially". In addition, the OBR will have complete discretion in the performance of this duty, subject to its statutory obligations. Further, the Chair and Members of the BRC have been and will be subject to Treasury Select Committee scrutiny to ensure their independence.

Recommendation

1.10 (5) *In this Report we examine some of the ways in which the independence of the OBR can be fostered, but one key factor, for which it is impossible to legislate, will be the quality of the organisation's people, and of the work they produce. The interim OBR, led by Sir Alan Budd, made an excellent start on which the permanent body can build. (Paragraph 24)*

Response

1.11 The Government agrees that the interim OBR, led by Sir Alan Budd, made an excellent start on which the OBR can build.

1.12 The OBR is designed so that it can attract high quality staff who can produce high quality work. This is reflected in the recent appointments, confirmed by the Treasury Select Committee, of Robert Chote as Chair and Professor Stephen Nickell and Graham Parker as Members of the Budget Responsibility Committee.

Recommendation

1.13 (6) *There is no "correct" model for an independent fiscal council; each arrangement will have its own advantages and drawbacks. In this Report we do not conduct an exhaustive examination of the various ways in which a fiscal council could be structured but focus on the Government's proposals and how they can be made to work. (Paragraph 28)*

1.14 (7) *The OBR's contribution to the formulation and improvement of public policy will be made through the substance of its work, which over time, can contribute to greater public confidence in fiscal policy making. It must avoid the trap of convincing itself (and consequently convincing the general public) that it or any other body has a monopoly of wisdom on short term forecasting, which is an inherently uncertain process. The OBR can only be effective if it is*

independent. Our proposals are designed to strengthen the OBR's independence, and the perception that it is independent, notwithstanding its involvement in drawing up the Government's forecast. (Paragraph 29)

Response

1.15 The Government agrees with the Committee that there are various models of fiscal councils which reflect their local context and specific objectives. The proposed design of the OBR reflects the UK context and the Government's objective for the OBR to examine and report on the sustainability of the public finances. The independence of the OBR remains central to it being able to effectively produce the official economic and fiscal forecasts. Independence is therefore at the heart of the design of the OBR, as set out in the Budget Responsibility and National Audit Bill. This is reflected in various dimensions of the design outlined below.

Recommendation

1.16 (8) *The OBR should avoid being drawn into seeking to apply political pressure through its commentary—even though many commentators will encourage it to do so. The OBR is not, and should not be, running fiscal policy. (Paragraph 30)*

Response

1.17 The Government agrees with the Committee that the OBR must not seek to apply political pressure through its commentary. To do so could undermine the perceived impartiality and independence of the OBR.

1.18 The Government agrees with the Committee that as a political judgement, policy rightly remains the domain of Government Ministers, accountable to Parliament and the public. The OBR should not be seen to advocate or arbitrate between alternative fiscal or other policy scenarios, and should not provide normative judgements regarding the policies set out by the Government of the day.

Recommendation

1.19 (9) *This Committee will have a key role both in holding the OBR to account and in upholding its independence. The NAO audited OBR independence at the time of the Budget and identified the following criteria by which the independence of the judgement underlying the forecasts could be judged:*

- *The Budget Responsibility Committee had full discretion over the scope and nature of its judgments on the forecasts.*
- *The interim Office for Budget Responsibility had unrestricted access to the necessary data and analysis.*
- *The interim Office for Budget Responsibility had control over sufficient resources to consider the evidence and form a robust judgment.*
- *The interim Office for Budget Responsibility effectively scrutinised, questioned and challenged the information and advice it received.*
- *The Budget Responsibility Committee formed its judgments independently of any views of officials or Ministers.*
- *The Budget Responsibility Committee had autonomy over the content of its published reports and the means of dissemination.*

We consider that these criteria provide an excellent foundation by which to judge the future OBR, and will bear them in mind in our future work. (Paragraph 31)

Response

1.20 The Government welcomed the NAO's audit of the OBR's independence. The NAO's report concluded that, on the basis of the criteria set out above, "the key economic and fiscal assumptions underpinning the interim Office for Budget Responsibility's forecasts have been independently arrived at". The Government welcomes the Committee's commitment to bearing the NAO's framework in mind for its future work.

Recommendation

1.21 (10) *In this Report we have started from the framework proposed by the Chancellor: the OBR will be a new body, and it is reasonable to see whether those arrangements can be made to work. However, given the lack of institutional experience of bodies such as the OBR, and the range of views on the matter, we consider that the arrangements adopted for the permanent OBR should be subject to comprehensive review no later than five years after it is established by statute. (Paragraph 32)*

1.22 (11) *The review should include an assessment of the OBR's performance, remit and institutional accountability arrangements. In particular, we believe that the review should consider in the light of experience the case for the OBR becoming a Parliamentary body with its resources determined by a House of Commons body, such as the Public Accounts Commission. (Paragraph 33)*

1.23 (12) *This review should be carried out by a small team of external experts, possibly commissioned by the National Audit Office, and should report to us as well as to the Chancellor. This Committee should be consulted both about the scope of the review and about the arrangements for carrying it out. (Paragraph 34)*

Response

1.24 It is best practice for all public bodies to be subject to regular review, as set out in the latest Cabinet Office guidance¹. This ensures that all public bodies are delivering high quality services, efficiently and effectively and that they fit within the Government's overall delivery structure. The Government envisages a regular review process for the OBR in line with this guidance.

1.25 Given that this approach is clearly set out in Cabinet Office guidance, the Government does not believe that it is necessary to include a special extra provision for a review in the legislation.

1.26 The OBR has been established with dual accountability to both Parliament and the Chancellor. This dual accountability reflects the OBR's executive role in producing the official economic and fiscal forecasts for the Government. This is an important consideration in determining the most appropriate institutional status for the OBR.

¹ "Public Bodies, A Guide for Departments" can be found at <http://www.civilservice.gov.uk/about/resources/public-bodies.aspx>.

2

The tasks of the permanent OBR

Recommendation- forecasting

2.1 (13) *One of the ways in which we will judge whether the OBR is a success is whether there is greater public understanding of the purpose and limitations of the forecasting process, and realistic expectations of what it can deliver. (Paragraph 38)*

2.2 (14) *There should, and will certainly, be analysis of the accuracy of OBR forecasts. Their quality and authority can be measured over time, relative to other forecasts. Absolute accuracy is not a useful criterion. Persistent pessimism or optimism will become apparent over time, justifiable on the basis of published explanations and methodology. (Paragraph 39)*

Response

2.3 The Government welcomes the Committee's commitment to consider the OBR's impact on public understanding of forecasting.

2.4 The Government agrees that there should be analysis of the accuracy of the OBR forecasts. To deliver this, the Budget Responsibility and National Audit Bill sets out a duty on the OBR to prepare "an assessment of the accuracy of fiscal and economic forecasts previously prepared by it", at least annually.

Recommendation

2.5 (15) *The legislation establishing the OBR should not require future Governments to use OBR forecasts. It is possible that the power of the Government to use its own forecasts will counterbalance any incentive the OBR might have to be overly pessimistic. The OBR's reputation would suffer if it were shown that its forecasts were so significantly biased that the Government no longer considered them a reasonable base for policy-making. However, it would be a major step for Government to do this. Once the decision had been made, the OBR's credibility would be severely, and possibly terminally, damaged. (Paragraph 41)*

Response

2.6 The Government is establishing the OBR as a part of its reforms to the fiscal framework so that an independent fiscal agency is required to produce fiscal and economic forecasts, at least twice a year. The Chancellor has made clear that it is his intention that the OBR forecasts are used as the official forecasts, while agreeing that the OBR legislation should not require this. In the formulation of policy, the Government will retain the right to disagree with the OBR's forecasts. If the Government does so, this will have to be explained to Parliament. This will further enhance parliamentary accountability.

Recommendation- controls of models and data

2.7 (16) *The OBR should have discretion in the models it uses in drawing up its forecasts. It is a matter for the organisation itself as to whether it is content to use the Treasury models, or wishes to make changes. Whatever course the OBR takes, there would be benefits in it being as*

transparent as possible about the models it uses. The OBR should also be cautious about attempting to increase the sophistication of the model in search of dubious increases in accuracy. As many witnesses pointed out, a sophisticated model cannot remove the need for forecasters to exercise their judgement and incremental benefits to an already highly complex model may be nugatory or perverse. (Paragraph 44)

Response

2.8 The Government will provide the OBR with full access to Treasury and other forecasting models, as well as support to scrutinise and develop these models. As set out in the Budget Responsibility and National Audit Bill, the OBR will have a right of access and assistance to all Government information that it may reasonably require to examine and report on the sustainability of the public finances (subject to data protection principles and confidential taxpayer information).

2.9 The design of the models that the OBR uses to produce its economic and fiscal forecasts is rightly a matter for the independent OBR.

Recommendation

2.10 *(17) The OBR should have the power to check the quality of fiscal data itself, and to request that the ONS does so. It should also be free to use any existing data it thinks fit in constructing the forecast, and to recommend changes in data collection, if it considers that this would improve the forecast or its ability to assess the likelihood of achieving the fiscal mandate. Where a recommendation may increase the overall cost of the OBR's work, it should be required to seek an external view on the benefits and costs of the change, and report this to the Treasury and to this Committee. (Paragraph 45)*

Response

2.11 As set out in the Budget Responsibility and National Audit Bill, the OBR will have a right of access to all Government information which it may reasonably require in examining and reporting on the sustainability of the public finances (subject to requirements of confidentiality such as wider data protection principles and in relation to confidential taxpayer information). The role of the ONS in auditing data relevant to the OBR's analysis is a matter for the OBR and the ONS.

2.12 Where the OBR reasonably requires additional or different data from Government sources, it will have the opportunity to commission these data through frameworks set out in formal Memoranda of Understanding. Where these may have cost implications, this should be consistent with the OBR's value for money requirements, set out in the Budget Responsibility and National Audit Bill.

Recommendation

2.13 *(18) While forecasting will be a key task of the OBR, there is no point in devoting resources, either to increase detail or frequency, to forecasts which will have no practical application or benefits. In normal circumstances, the OBR should produce two sets of forecasts a year. An extra forecast would be desirable if there were significant monetary or fiscal policy changes or significant external shocks. (Paragraph 46)*

Response

2.14 The Government agrees with the Committee's conclusion. The Budget Responsibility and National Audit Bill requires the OBR to, at least twice each financial year, prepare "fiscal and economic forecasts". This allows for two sets of forecasts each year, with the option of further forecasts should these be considered necessary.

Recommendation- sustainability analysis

2.15 (19) *We support the interim OBR's recommendation that the permanent OBR should produce an annual report on the long-term sustainability of the public finances. This report should contain no policy recommendations. (Paragraph 50)*

Response

2.16 The Government believes that an annual report on long-term sustainability of the public finances would be a useful report for the OBR to produce. The Budget Responsibility and National Audit Bill therefore requires the OBR to, at least once for each financial year, prepare "an analysis of the sustainability of the public finances". The Government agrees that this should not contain policy recommendations.

Recommendation- commentary

2.17 (20) *The OBR's contribution to public understanding should not be confused with self promotion. This commentary function should be one of informing public debate through disseminating better understanding of fiscal policy and long-term economic trends, identifying possible risks in the structure of the economy and provision of data. Beyond any duties set out on the face of the legislation, the statute should give the OBR absolute discretion over the work it undertakes. The legislation should leave the OBR able to conduct work on the fiscal policies of political parties along the lines proposed by Robert Chote in evidence on 16 September 2010. There may be also particular subjects which the Treasury, or this Committee, consider should be examined by the OBR. We would expect the OBR to consider such proposals carefully and, where appropriate, explain its decisions. (Paragraph 58)*

2.18 (22) *We agree with Mr Chote that it would be inappropriate for the OBR to have a role in setting the fiscal mandate. This should be a political decision. Once the mandate is set, any OBR commentary should be based on aggregate fiscal figures, not on individual measures. (Paragraph 64)*

Response

2.19 The Government agrees that the OBR will play an important role in informing the public debate on issues regarding the sustainability of the public finances. This will be supported by the requirement to act transparently, set out in the Budget Responsibility and National Audit Bill.

2.20 The OBR is designed to enhance the accountability of the Government by examining and reporting on the public finances and the long-term impact of the Government's decisions.

2.21 The Government agrees that it would be inappropriate for the OBR to have a role in setting the fiscal mandate. As the Chancellor of the Exchequer made clear when he established the OBR on 17 May 2010,² it is for the Chancellor to set his fiscal policy target, the fiscal mandate. This is a political decision for the Government of the day. The fiscal mandate is required by the Budget Responsibility and National Audit Bill Clause 1 (2) to be included in the Charter for Budget Responsibility such that Parliament, through the House of Commons, is required to approve the Government's fiscal target.

² http://www.hm-treasury.gov.uk/d/press_01_10.pdf

2.22 However, as required by Clause 4 (3) (b) of the Bill, the OBR has a role assessing the probability of the Government's fiscal policy stance achieving the fiscal mandate. This independent assessment will add credibility to the Government's mandate and the Government's fiscal policy. Not only will the forecast on which the Government's fiscal policy is based be independently developed, but judgements on the key factors of the mandate and the overall assessment of the Government's progress against the mandate will be independently reached by the OBR. The Government will not be judging its own progress against its own targets.

2.23 In line with the Government's view that the OBR should not have a role in setting fiscal mandates, it is also the view of the Government that the OBR should not provide normative judgements regarding Government policies, and should not examine alternative fiscal or other policy scenarios, including those proposed by political parties. Policy will rightly remain the domain of Government Ministers. To be seen to apply political pressure through its commentary, or to advocate or arbitrate between alternative scenarios, could undermine the perceived impartiality and independence of the OBR (Recommendation 8).

2.24 The Civil Service Code tightly prescribes the extent to which civil servants may look at the policies of other political parties, for reasons of political impartiality³. With respect to potential OBR analysis of opposition policies, political impartiality applies equally to the OBR.

2.25 The Government recognises that this issue is of particular interest to the Committee and looks forward to debating the issue in the House as the legislation passes through Parliament.

2.26 The Government agrees that, beyond those duties set out in statute, the OBR should have complete discretion over the work it undertakes. This is reflected in the Budget Responsibility and National Audit Bill. The Chancellor and the Treasury Select Committee will both have the ability to request analysis from the OBR. However, the final decision over the particular subjects the OBR analyses, will be taken by the OBR itself.

Recommendation

2.27 (21) *As an additional defence of OBR impartiality, we recommend that the OBR's core tasks should be set out on the face of the legislation. (Paragraph 59)*

Response

2.28 The Government agrees with the Committee's recommendation. The Budget Responsibility and National Audit Bill sets out the core tasks of the OBR under Clause 4.

³ Civil Service Code, November 2006 (www.civilservice.gov.uk/about/values/cscode/index.aspx)

3

Staffing and resources

Recommendations- staffing and resources

3.1 (23) *Sir Alan Budd argued that it would not be cost-effective or practical to duplicate or move into the OBR all the officials who spend some of their time on the Budget forecasts. We accept that there is a trade-off between delivering the most robust independence and perception of independence and making the most efficient and effective use of resources. (Paragraph 72)*

Response

3.2 The Government agrees with both Sir Alan Budd's advice and the Committee's conclusions. Core forecasting staff have been transferred into the OBR to ensure the OBR has control over forecasting expertise. All OBR staff report to the Chair of the OBR. Provisions set out in the Budget Responsibility and National Audit Bill will ensure the OBR has access to the expertise only available in Government to fulfil its remit and produce independent forecasts.

Recommendation- core staff

3.3 (24) *The core staff of the OBR should be sufficiently large to support an investigative team which would be able to go into a department and scrutinise the data a department used or the way a particular part of the forecast had been drawn up. The OBR should also have sufficient resources to hire outside contractors to look into particular aspects of the forecast data. (Paragraph 76)*

3.4 (25) *Section 156 of the Finance Act 1998 gives the Comptroller and Auditor General a right of access to all relevant Government documents he may reasonably require to carry out his audits of budget assumptions, and the right to have explanation of those documents. We recommend that, with the exception of material related to individual taxation, the OBR should have similar rights of access to all relevant documents. (Paragraph 77)*

3.5 (26) *The model chosen by the Chancellor means that the OBR will not be the full time employer of many of the people supplying information and analysis which it will, after challenge, use in making its forecasts. Nevertheless, the permanent OBR will need to be larger than the interim organisation, and to command more resources. It will also need to be able to draw on expertise within the Treasury, the Department for Work and Pensions and Her Majesty's Revenue and Customs. We do not attempt to suggest precise numbers for core staff, as the OBR might choose to hire people for specific tasks, or contract out some research, but note that in addition to the 10 Treasury staff whose functions should move to the OBR, we have also identified a need for a research director, macroeconomic expertise, and some sort of investigative team to ensure data are properly used. The BRC must be confident that the OBR has the core staff it needs. The safeguards over funding we propose in paragraph 112, and the independent directors we propose in paragraph 96, should ensure that any concerns are raised with us as part of its budget procedure, as outlined by Mr Chote on 16 September. (Paragraph 84)*

Response

3.6 The Government agrees with the Committee's recommendation that the OBR needs to be bigger than the interim OBR and core forecasting staff have been transferred to the OBR. All OBR staff report to the Chair of the OBR and it is expected that the OBR will operate with a staff of around 20 in total. This staffing will ensure the OBR both scrutinises the data it receives and controls the production of the forecasts, making all the judgements that underpin them. The OBR staff will include macroeconomic expertise and strong intellectual leadership will be provided by the independent BRC. Funding for the OBR for the Spending Review period has been agreed with the OBR and this will allow the OBR to draw on expertise outside Government, as committed in the Terms of Reference agreed between the OBR Chair and the Chancellor.

3.7 The OBR will have a right of access to all Government information which it may reasonably require in examining and reporting on the sustainability of the public finances (subject to requirements of confidentiality such as under the data protection principles and in relation to confidential taxpayer information), as set out in the Budget Responsibility and National Audit Bill. The Government also intends to publish frameworks for co-operation between the OBR and its principle Government partners in formal MOUs. We intend for these to include formal commissioning and accountability arrangements between Government departments.

Recommendations - duplication

3.8 (27) *We accept that the Treasury may wish to replace some of those staff who we propose should be moved to the OBR. Given the limited number of posts involved, we consider that the advantages of independence are well worth the costs of any duplication. The staffing of the OBR should be one of the subjects examined in the five year review we recommend (Paragraph 85)*

Response

3.9 The Government has stated that it intends to adopt the OBR's forecasts as the official forecasts for the annual Budget. Core forecasting staff have been transferred into the OBR and the BRC has control over all the judgements underpinning the forecasts. In the formulation of policy, the Government will retain the right to disagree with the OBR's forecast. If this is the case, the Government will have to explain why it disagrees with the OBR's forecast to Parliament. The Treasury will continue to maintain the necessary analytical and macroeconomic expertise to provide on-going advice the Government.

4 Independence

Recommendations- independence status

4.1 (28) *The body should have the maximum independence possible. It should operate from offices outside the Treasury and have its funding secured by the measures set out in paragraph 112. We believe the best structure for this would be to have the OBR established as a Non Ministerial Department. The Statistics Authority offers a useful model of how such a department can function. It is roughly the size we envisage for the permanent OBR (or even smaller), with 27 staff—23.6 full time equivalents. While a Non Departmental Public Body could be established in ways which maximised its independence, it would appear to be linked to the Treasury because of the Estimates process, and there would be inevitable doubts about its independence. (Paragraph 91)*

Response

4.2 The Government sees the location of the OBR as a matter for the OBR. The Chair of the OBR has written to the Committee explaining his decision to locate the Office outside the Treasury. The Government fully supports his decision and notes that it concords with the Committee's recommendation.

4.3 The Government agrees with the Treasury Select Committee on the importance of the OBR's independence and that funding arrangements can play a part.

4.4 However Managing Public Money advises Departments considering setting up arm's length bodies "to consider the Non Ministerial Department (NMD) option only if neither agency nor Non Departmental Public Body (NDPB) status seems suitable"⁴.

4.5 We believe that given the size of the OBR, the NMD model would not support value for money (vfm)⁵. Though there is room for some variation, there are additional overheads associated with the governance of NMDs and there is normally some duplication of functions which represent poor vfm and additional administrative costs for the NMD. The OBR's small size could make the imposition of a fixed Departmental Expenditure Limit of its own (as is the norm for NMDs) difficult to make work in practice. The NDPB funding model allows for security to be provided through a multi-year budget settlement while retaining flexibility to respond to changing circumstances. The resources provided to the OBR will be transparent in the Treasury's Estimate, enabling Parliamentary scrutiny of the OBR's funding and spending plans on an annual basis, further supporting the OBR's independence.

4.6 We therefore propose to establish the OBR as a grant-funded NDPB. This would provide the OBR with its own legal personality. The Government agrees with the Committee that there are ways of maximising independence within the NDPB model. The Treasury has therefore agreed with the Chair of the OBR that:

⁴ Managing Public Money, Annex 7.2 Setting up arm's length bodies, A.7.2..3, p 172.

⁵ The Government would like to clarify that for the purposes of the Estimates process and other administrative purposes the Statistics Authority, as a Non Ministerial Department, includes the ONS. The UK Statistics Authority's departmental resources accounts for the financial year 2009-2010 show that it employed 3,302 FTE members of staff, and that its net resource outturn was £206,475,000. It is therefore a much larger organisation than the OBR.

- the OBR will be provided with a multi-year budget settlement
- the statutory OBR will have at least one separate line in the Treasury's Estimate which will show an estimate of budget expenditure.
- the OBR will be able to itself submit an additional Memorandum alongside that of the Treasury.

4.7 These will protect the independence of the OBR and aid effective Parliamentary scrutiny of the OBR's resources.

Recommendations – independence structure

4.8 (29) *We agree with the Government's assumption that the BRC should have three executive members, including its Chairman, reflecting the balance of skills required to undertake the OBR's functions. Although it will be essential for the Committee to contain respected economists, as the ICAEW suggests, other skills may also be appropriate. While the organisation will not have any direct political role, the BRC should have sufficient political awareness to avoid involvement in political controversy. (Paragraph 94)*

4.9 (30) *The permanent OBR should also have a small group of non-executive directors containing two or three people working on a pro bono basis, with a senior nonexecutive director, drawn from those with considerable experience in relevant fields, such as the Treasury forecasting, the Bank of England or the private sector, and at least one should have had some forecasting experience. Previous political experience should not necessarily be a bar to appointment. (Paragraph 96)*

4.10 (31) *The non executives should not be involved in the forecasting process. Their primary role should be to safeguard the independence of the OBR and they should have a duty to warn this Committee of anything which appears to threaten that independence, including any questions about resources. They should be available to advise to the Chair and members of the BRC, and, if necessary, the Treasury Committee. (Paragraph 97)*

Response

4.11 The Government welcomes the Committee's conclusions on the composition and skills of the BRC. The Government agrees with the Committee that the OBR must avoid being drawn into political controversy and provisions set out in the Budget Responsibility and National Audit Bill will support the perceived impartiality and independence of the OBR. The letters of appointment for the BRC set out that they should abstain from all controversial political activity.

4.12 The Government agrees with the Committee's recommendation there should be a small non-executive presence at the OBR. These non-executives will play an important role in safeguarding the independence of the OBR, but should not be involved in the forecast process. We further agree that they should be available to attend the Treasury Select Committee and would expect them to warn the Committee of anything which appears to them to threaten the OBR's independence. We do not propose to give this moral obligation the force of law or in any way dictate how the non-executives should behave. Instead we rely on their personal integrity as public servants.

4.13 The Government believes it is important that the non-executives who will play a role in the OBR's governance should not become competing voices on the public finances to that of the Chair. This could be counterproductive and damaging to the credibility of the OBR. We therefore do not propose the non-executive members should be there in the capacity of technical experts. Experience of public life or running a similar organisation may be relevant. However the OBR will

be free to establish advisory panels of experts to contribute advice if it sees fit. The legislation makes this clear.

Recommendations- appointment and dismissal

4.14 (32) *We consider that to avoid the politicisation of the BRC's role, candidates should be judged against clearly defined criteria. We intend to use the criteria of personal independence and professional competence as the basis for our hearings with BRC members. (Paragraph 104)*

4.15 (33) *We support the Chancellor's proposals for a "double lock" on the appointment and dismissal of the OBR Chair. We should also have the right to veto other BRC executive members proposed by the Chancellor. (Paragraph 107)*

4.16 (34) *While we welcome a statutory role for the Committee in the appointment and dismissal of the Chair of the Budget Responsibility Committee, the relevant provisions will have to be carefully drafted to ensure that the legislation does not purport to dictate parliamentary proceedings, or expose them to judicial review. (Paragraph 108)*

Response

4.17 The Government welcomes the Committee's intention to use the criteria of personal independence and professional competence as the basis for their hearings with members of the BRC.

4.18 The Government agrees with the Committee's recommendation that the Committee should have the right to veto the appointment and dismissal of the BRC to ensure that there is no doubt that the individuals leading the OBR have the support and confidence of the Committee. This has already worked well for the recent appointments to the BRC with the Chancellor providing the Committee with an effective veto before legislation is in place. Provisions for the Committee to have a statutory veto over the appointment and dismissal of the BRC have been set out Budget Responsibility and National Audit Bill in paragraphs 1 and 27 of Schedule 1. These provisions carefully follow the precedent for the involvement of the Chairman of the Committee of Public Accounts in the appointment of the Comptroller and Auditor General under sections 1 and 13 of the National Audit Act 1983.

Recommendations – finances and back of office support

4.19 (35) *The OBR needs to have full control over its communications, and this function should not be shared with the Treasury press office. (Paragraph 109)*

4.20 (36) *If the OBR is not to be a fully Parliamentary body, it needs transparency in the resources it is given, and the House needs to know the Government's proposals in time for intervention to be effective. To that end we recommend:*

- *the OBR budget should be given its own line in the estimates;*
- *that budget, accompanied by an explanatory memorandum prepared by the OBR itself, should be sent to the Treasury Committee in confidence at least six weeks before the Estimate is laid.*

These measures will allow us to ensure that the BRC and the non-executives are content with what is proposed. They should have a duty to raise any concerns they have with the Committee. (Paragraph 112)

4.21 (37) *While we accept that there is a case for those employed by the OBR to be civil servants, we consider that the OBR should have sole responsibility for hiring and firing its employees. Although many of its staff may come from within the civil service, it should draw its staff from as wide a range of sources as possible.* (Paragraph 115)

Response

4.22 The Government agrees with the Committee's recommendation that the OBR should have full control over its communications. Staff to perform these functions have been recruited by the OBR.

4.23 The OBR is free to choose a supplier of back office, corporate services, although it makes sense economically to pool resources to achieve scale. Some back office corporate service functions such as finance and procurement support will continue to be provided by Treasury, governed by a Service Level Agreement specifying the contractual roles and responsibilities of Treasury and OBR in providing these corporate services. Sharing of back office services is important in reducing costs across Government, and has been recommended by the Treasury Select Committee.

4.24 The Government agrees with the recommendation that there should be transparency in the resources that are provided to the OBR. As an NDPB of the Treasury:

- the statutory OBR will have at least one separate line in the Treasury's Estimate which will show an estimate of budget expenditure.
- the OBR will be able to itself submit an additional Memorandum alongside that of the Treasury.

4.25 The Treasury and the OBR will endeavour to send their Estimate Memoranda in accordance with the deadlines set out in the Estimates Manual. This requires the Treasury and the OBR to send these as early as possible after the completion of the Estimates, and certainly no later than the date of publication.

4.26 The Government agrees with the Committee's recommendation that the OBR should have sole responsibility for hiring and firing its own employees. The Government welcomes the Committee's conclusion that it is appropriate for OBR employees to be civil servants, and note that this entails that the OBR's power of appointment and dismissal will be exercised in accordance with the appropriate civil service employment guidelines.

4.27 The Government agrees with the Committee's recommendation that the OBR should draw its staff from as wide a range of sources as possible. The OBR will have a mix of staff selected by the OBR for their knowledge and expertise and will have strong intellectual leadership from the independent BRC. The establishment of the OBR involves transferring responsibilities from HM Treasury to the OBR. Once the OBR is established by statute, and in line with the guidelines for reorganisation and transfers within the Civil Service set out in the Cabinet Office Staff Transfers in the Public Sector Statement of Practice January 2000 (revised 2007), a number of experts are expected to permanently transfer from HM Treasury to the OBR with their roles. Some new roles have already been filled through open competition within the Treasury and Civil Service to ensure that these staff have the requisite skills and experience to deliver the work of the OBR. Subsequent new roles will be advertised by the OBR as appropriate and the OBR will have sufficient resources to bring in external analytical expertise.

Recommendations – relationship with the civil service

4.28 (38) *There need to be structural assurances that the officials who remain in Government are giving the OBR full and objective advice, and cannot be subject to pressure from the Treasury or other departments. First, their annual appraisals should contain an explicit OBR comment on*

the way they have performed their forecasting tasks. Second, such officials should have the duty to raise any concerns they have with the BRC or with the non-executive board, just as civil servants generally have the right to raise matters with the civil Service Commissioners. If there were widespread concerns about the objectivity of the data or advice fed into the forecasts from within Government, we too would expect to be informed and we would not hesitate to intervene. (Paragraph 116)

4.29 (39) *The relationship between the OBR and Government departments should be set out clearly in formal memoranda of understanding between OBR and departments it deals with: those memoranda should make it clear that during forecasting periods the OBR has the right to control the forecasting resources of Government and that such staff have a duty to give the OBR full and objective advice (Paragraph 117)*

4.30 (40) *The Ministerial Code should be amended to require Ministers to respect the OBR's independence and to note that during the forecasting periods the OBR has the right to control the forecasting resources of Government (Paragraph 118)*

Response

4.31 The Government intends to publish frameworks for co-operation between the OBR and its principle Government partners in formal Memoranda of Understanding (MOUs). We intend for these to include formal commissioning and accountability arrangements between Government departments. The Government intends that formal MOUs will set out procedures designed to ensure the quality and objectivity of information provided to the OBR and is exploring ways in which this can be formally reflected in appraisals. We do not propose to include provisions for the OBR to "control" staffing resources: to do so would generate complex accountability arrangements, magnified by the multiple demands on Government forecasting resources throughout the year.

4.32 The Government notes the Committee's proposal regarding the Ministerial Code and is considering the merits of such an inclusion.

Recommendations – role of the NAO

4.33 (41) *We consider that the establishment of the OBR means that provisions of the Finance Act 1998 requiring the NAO to audit budget assumptions are no longer necessary. However, the OBR should be subject to the same sort of NAO scrutiny as any other part of Government. (Paragraph 119)*

Response

4.34 The Government agrees that the establishment of the OBR makes the provisions of the Finance Act 1998 requiring the NAO to audit the budget assumptions redundant. Clause 10 (b) of the Budget Responsibility and National Audit Bill seeks to repeal sections 155 to 157 (fiscal stability) of Finance Act (1998) and, as there is no specific provision for the NAO to audit budget forecasting conventions and assumptions anywhere in the new framework, this abolishes this specific role for the Comptroller and Auditor General and the NAO. The OBR will be free to choose its own set of assumptions independently of the Treasury and produce economic and fiscal forecasts on the basis of them.

4.35 The Government agrees with the recommendation that the OBR should be subject to the same sort of NAO scrutiny as any other part of Government.

5

Conclusions

Recommendations- legislative framework

5.1 (42) *The Treasury's task is now to prepare the legislation setting up the permanent OBR. As a minimum we recommend that legislation should include:*

- a) establishment of the OBR as an institution with its own legal personality, responsible for appointing its own staff;*
- b) a requirement on the OBR to act transparently, objectively, and independently;*
- c) a clear remit and set of core tasks;*
- d) a requirement that the responsible select committee should have a veto over appointment or dismissal of the Chairman of the permanent body;*
- e) provision for a small independent group to support the BRC;*
- f) a requirement that Government officials support the OBR when it is preparing forecasts and that they have a duty to give the OBR full and objective advice;*
- g) a requirement that the OBR has a right of access to the information it needs;*
- h) a requirement for a review of the organisation five years after it is established.*

We have not set out in detail how these might be accomplished. (Paragraph 120)

Response

5.2 The Government notes the Committee's proposals for the legislation setting up the permanent OBR. The Government agrees that the OBR should be established with its own legal personality and that it should be responsible for appointing its own staff; that it should have a requirement to act transparently, objectively and independently; that it should have a clear remit and set of core tasks; that the Treasury Select Committee should have a veto over the appointment or dismissal of the Chair; that the OBR should have the flexibility to have a small group to support the BRC; that Government officials should be required to support the OBR when preparing its forecasts and that the OBR should have a right of access to the information that it needs. However, the Government is not fully convinced that a legal requirement for a review is necessary.

Recommendation

5.3 (43) *In preparing this Report we have become aware of some anomalies in the current legislative framework relating to fiscal forecasting. The framework for Government economic decision-making is still governed by the Code for Fiscal Responsibility, any revision of which requires approval by the House of Commons. The Code should have been revised as a consequence of the Fiscal Responsibility Act 2010, but although the necessary Order was laid, no steps were taken to approve it. The Code for Fiscal Responsibility requires a Pre-Budget Report, a Budget Report (containing an economic and fiscal projection) and other fiscal reports to be published by the Treasury. The Treasury should bring forward a revised Code for approval*

to ensure the OBR has control of the publication of its forecasts. It should also, if necessary, reflect changes in primary legislation and any changes to the way Government proposes to make its fiscal reports to Parliament. (Paragraph 121)

Response

5.4 The Government recognises that, in the previous Parliament, no steps were taken to approve the revised Code for Fiscal Stability that was published during the passage of the Fiscal Responsibility Act 2010.

5.5 This is why the Budget Responsibility and National Audit Bill, which will establish the OBR, intends to repeal extant fiscal legislation including the Sections 155 to 157 of the Finance Act 1998, which will remove the requirement to have a Code for Fiscal Stability, and the Fiscal Responsibility Act 2010.

5.6 The Budget Responsibility and National Audit Bill will create in the place of the Code a requirement for the Treasury to publish and gain the House of Commons' approval for a statutory Charter for Budget Responsibility. This document will replace the Code for Fiscal Stability and make clear changes to the Government's fiscal policy framework and guidance to the OBR on fulfilling its duties in providing independent forecasts, analysis and assessment in examining and reporting on the sustainability of the public finances.

Recommendations – non statutory measures

5.7 *(44) If the OBR is to be credible, members of the Budget Responsibility Committee will need not only to be independent but to demonstrate that independence from the Government's own Treasury team. (Paragraph 123)*

5.8 *(45) Although the forecasts will be produced by a nonpartisan body, the future path of the economy is the subject of intense political debate. The OBR's forecasts will inevitably be used in that debate. To preserve its reputation for political impartiality, it is essential that the OBR takes all reasonable steps in the presentation of its words to inhibit them from being misused or misrepresented. (Paragraph 124)*

Response

5.9 The Government has put in place provisions to help secure the BRC's independence. The BRC have been appointed following an open and fair process and their appointments have been subject to the consent of the Committee to ensure that there is no doubt that the individuals leading the OBR have the support and confidence of the Committee.

5.10 The Government agrees that the OBR should seek to avoid being drawn into political debate, intentionally or otherwise, and provisions set out in the Budget Responsibility and National Audit Bill will support the perceived impartiality and independence of the OBR.

Recommendations- the Committee's role

5.11 *(46) The current proposals for the OBR envisage that this Committee will have a role in controlling both the appointment and the dismissal of the Chair of the OBR. Our role in ensuring the independence of the organisation goes beyond that. Whether or not the OBR is established as a Parliamentary body, it is vital that it commands confidence across party boundaries. We will take evidence from the organisation regularly as part of the budget process. We will intervene if we believe the OBR's independence is threatened. We expect the members of the Budget*

Responsibility Committee or the non-executive directors to report any concerns they have to us. Only if it is independent will the OBR be successful. (Paragraph 125)

Response

5.12 The Government welcomes the Committee's on-going engagement regarding the OBR. The Government confirms that the Committee will be able to directly call members of the BRC to ensure the Committee has the necessary access to the information that it requires.

Recommendations – success criteria

5.13 (47) *The most important sign of the OBR's success will be that it establishes and retains a reputation for independence and impartiality. While its forecasts and publications should improve political debate, the organisation itself will be under pressure to be drawn into partisan disputes. (Paragraph 126)*

5.14 (48) *An important criterion is that the OBR should seek to avoid significant bias over time in its forecasts, its assessment of trend growth, or its judgements about the probability of the Government's mandate being met on the policies announced. (Paragraph 129)*

5.15 (49) *The work of the OBR needs to achieve and retain a high professional standing through objectivity and transparency and by testing the models it uses and its analysis, including work on the long term balance sheet, with outside economists. The OBR should not seek extra resources, either to extend its economic analysis or to get new data, beyond the point at which the benefits can be clearly seen to justify the costs. (Paragraph 130)*

5.16 (50) *The OBR's reports should be comprehensible to non-experts, like the output of the interim OBR, and suitable for use in public debate. Its work should improve the quality of that debate. But the OBR should not itself run education campaigns (Paragraph 131)*

5.17 (51) *There are significant risks facing any new organisation. The approach put forward by the interim BRC avoids the risk that the forecaster will lack information available to Government, or that there will be wholesale duplication of resources. It does, however, increase the risk that the OBR will not be seen as independent, and this could undermine the potential gain from this reform: increased trust in the forecasts used in Government policy making. We will scrutinise this carefully. (Paragraph 132)*

Response

5.18 The Government agrees with the Committee that the OBR needs to establish a reputation for independence and impartiality. The Government believes that the design set out in the legislation, and the Charter of Budget Responsibility and underpinning MOUs should deliver this. The Government agrees that the OBR may come under pressure to be drawn into partisan debates. The Budget Responsibility and National Audit Bill reflects the Government's view that the OBR should not be seen to advocate or arbitrate between alternative fiscal or other policy scenarios, and should not provide normative judgements regarding the policies set out by the Government of the day.

5.19 The Budget Responsibility and National Audit Bill establishes that the OBR must carry out its duties objectively and transparently. The OBR will be expected to report annually on the accuracy of its forecasts. The OBR will have the freedom to test its analysis and models with outside economists. The OBR is expected to be run in a manner that is efficient and cost-effective and this is set out on the face of the Budget Responsibility and National Audit Bill.

5.20 While the OBR has discretion over how to present its reports, the Government would expect the OBR to continue to produce user-friendly reports as the interim OBR has done. The Government agrees that the OBR should not run education campaigns.

5.21 The Government welcomes the Committee's commitment to scrutinising the OBR's independence.



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