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## **Submission to the Review of the Parliamentary Budget Office**

Dear Secretary

Thank you for the opportunity to make a submission to the Review of the Parliamentary Budget Office (PBO). My general submission is that after just over 2 years in operation, the PBO is operating effectively and appears to be carrying out its mandate. As the PBO becomes established and Parliamentarians, government departments and the public come to understand its role, expectations and use of the PBO may change and so Parliamentary oversight through the JCPAA should be done on a regular basis.

### **Terms of reference**

The terms of reference for the Committee are as follows:

- PBO statutory information gathering powers and access to information, including the Contingency Reserve
- PBO reporting of Government progress against a new set of fiscal rules, as recommended by the National Commission of Audit
- PBO reporting against medium-term projections of fiscal outlook beyond the forward estimates
- best practice for independent fiscal institutions, as identified by the International Monetary Fund
- PBO implementation of the recommendation from Australian National Audit Office Report No. 36 (2013-14), and
- the need for any legislative change.

## The value of “best practice” or comparative experience

In responding to several of the terms of reference for this review, it is useful to ask what is the purpose and function of the PBO? In establishing the PBO, Australia has joined a global trend of establishment of what are generally termed “independent fiscal institutions” (IFIs).<sup>1</sup> However, these IFIs are quite heterogeneous, with different powers, skills, funding and mandates. Some are based in the executive or a government department (eg, The Netherlands), or are established as an independent agency (eg, the UK), rather than being located in the Parliament. Some determine the economic forecasts and estimates that must be followed by the Treasury; in Australia, the opposite occurs as the PBO must utilise the estimates of the Treasury. Some have a substantial economic forecasting role or exclusive responsibility for that task; in Australia, that role is carried out by the executive government through the Treasury.

The heterogeneity of IFIs means that comparative experience can be useful but should be referred to with caution. Similarly, “best practice” principles are useful but may be at a too general level to be directly relevant to some issues for the PBO in Australia. The ANAO report acknowledges the diversity between IFIs but does not explicitly identify the difference in location of Australia’s PBO in the Parliament, compared to others, which is likely to significantly affect its function and outcomes.<sup>2</sup>

**Recommendation 1.** Caution should be used when referring to comparative or “best practice” experience for IFIs. As the PBO is located in the Australian Parliament, it must be assessed in this light, as having the fundamental goal of enhancing the functions and operations of the Parliament in fiscal decision-making in our legislative democratic system.

## Fiscal rules and constraining deficits

It is not currently the purpose of the PBO to control fiscal deficits or to enforce fiscal rules and nor does the PBO have the power to do so. Both of these purposes would require powers to constrain or limit Parliamentary legislative power to spend or to raise or lower taxes. It is a matter for the Parliament, in a system of Parliamentary democracy, to determine its own processes. However, any attempt to delegate or constrain Parliamentary decision-making power about taxing and spending should be carefully considered as potentially anti-democratic.

Similarly, the PBO does not currently, and in my view should not have, the power to address fiscal crises, for example by making emergency changes to tax rates or expenditures; this is a function of the Government in Parliament itself, as was done through the fiscal stimulus package in 2008 in response to the Global Financial Crisis.<sup>3</sup>

Fiscal rules may take many forms; for example, a requirement for fiscal balance or 1 per cent of GDP surplus in each year (as proposed by the government and approved by the National Commission of Audit); or a rule that the fiscal deficit must not exceed 3 per cent of GDP (the basic rule of the Maastricht Treaty in the European Monetary Union).

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<sup>1</sup> As discussed in Stewart M and Jager H, “The Australian Parliamentary Budget Officer: Shedding Light on the Dark Arts of Budgeting” (2013) 24 *Public Law Review* 267, and in analyses by the OECD and IMF.

<sup>2</sup> Australian National Audit Office Report No. 36 (2013-14), 16.

<sup>3</sup> This executive and legislative action in response to fiscal crisis was upheld as an appropriate use of executive emergency powers by the High Court of Australia in *Pape v Commr of Taxation* [2009] HCA 23.

However, a fiscal rule that is focused on balancing the budget or intended to constrain deficits is not the same as a rule that sets a limit on the size of government itself. The Commission of Audit report, to which there has not yet been a formal response by the Government, conflates the goal of fiscal prudence with a limit on the size of government itself. It does this in its proposal that there be a fiscal rule or “cap” on taxation by the government such that “tax receipts remain below 24 per cent of GDP”.<sup>4</sup> The size of government (funded by taxation) is a political decision that has no necessary connection with the fiscal sustainability of government. A government of any size (in the sense of size of expenditures funded by taxes as a proportion of GDP) may be fiscally prudent or imprudent.

A common criticism of Australia’s Charter of Budget Honesty and fiscal framework is that it is not strong or certain enough. While it would be possible to legislate – or even include in the Constitution subject to a successful referendum – a numerical fiscal rule, the experience internationally is that such rules tend to be honoured in the breach, especially in times of economic uncertainty or change. The existence of a fixed or numerical rule also is likely to increase the temptation of governments to practice “creative accounting” in order to meet the numerical rule, undermining fiscal transparency and accountability. Ultimately, a numerical rule that the Parliament and the government are not able or willing to meet because of political or economic constraints or decisions, will lose credibility.

Fiscal rules are political in nature and cannot be enforced through legal or “independent” political mechanisms. A better approach is to establish guidelines, procedures and institutions that can educate, cost and publish fiscal policies and outcomes with a prudent and longer term framework and as transparently as possible. This is a reason why IFIs have become increasingly recommended in recent years, as it is recognised that institutional and procedural approaches are needed to ensure fiscal prudence. The Australian approach of a flexible and transparent fiscal framework is sensible. A risk is that the short-term timeframe of our political process will undermine medium and long term goals of fiscal sustainability. There is a role for the PBO in publicising the medium term consequences, not just immediate fiscal consequences, of policies.

**Recommendation 2.** The Parliament should maintain the current mandate and role of the PBO concerning fiscal prudence or discipline. It is not recommended that Parliament adopt a numerical fiscal rule or “cap” on taxation or expenditures, or that the PBO be given powers to enforce or monitor government performance in line with such a rule. The PBO can usefully report on immediate and medium term costs of spending and tax policies and structural budget implications. It can do this through its independent research function.

## Enhancing fiscal transparency and accountability

When considering mechanisms of fiscal accountability, it is important to consider whether it is the legislature (or its members), or the executive government, which is to be held accountable by a particular process, institution or rule. Publication and explanation of methods of costing government expenditures and estimating revenue, and of actual costings especially during an election period contribute to this. In addition, the independent research reports of the PBO play a valuable role in explaining the broader framework and structure of Australia’s fiscal position to the public and media. The Parliament can also call

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<sup>4</sup> The Report of the National Commission of Audit, Phase One, Chapter 5, 5-1,  
<http://www.ncoa.gov.au/report/phase-one/part-b/5-1-fiscal-framework-and-rules.html>

for submissions by the PBO on broader fiscal matters if desired, under the current framework.

Primarily, its role is to support the Parliament, through its costing and reporting roles for Parliamentarians. In our representative democracy, it is appropriate that Parliamentary representatives should be supported in better interpreting, understanding, proposing and enacting realistic policy and law. Members of Parliament will, presumably, be enabled to provide better representation to the people of Australia in these core functions.

The PBO does not have a direct role to play currently, in enforcing or enhancing accountability of the executive government. The PBO's role as currently established is to enhance fiscal transparency both for and of Parliamentary decisions. Indirectly, through independent research, the PBO has power to inform the legislature of structural fiscal constraints and challenges. The PBO also has power through its advice on costing, to support Parliamentarians' proposals for policy change, or critiques of policy.

Currently, apart from releasing its reports and costings where required to the public, the PBO does not have a focus of increasing fiscal transparency or accountability directly to the Australian people.

The post-election report on policy costings, which was produced by the PBO as mandated after the 2013 election, has the potential to increase fiscal transparency for the benefit of the public as a whole. It may also serve to discipline parties that are elected (and minor parties or Independents that may control the balance of power in some instances) to keep to their original electoral policies as costed. The knowledge that such a report will be issued post-election may also constrain politicians from overstating the benefits or understating the costs of a policy going into an election. However, the post-election report when issued did not attract much public debate or comment and it is arguable that such a report comes at a time in the electoral cycle when it is least likely to attract public attention and policy debate – immediately after a government has been elected to power. While there may be no downside to such a report, enhancing transparency and information prior to the election could be more beneficial for fiscal transparency and accountability.

The PBO could play a broader role in educating the public about the budget, and enhancing the participatory nature of budgeting through engaging the public in budgetary or fiscal processes. As this is not currently part of the PBO's mandate, such a change of focus may require legislative reform. However, it is likely that significant steps could be taken, simply through additional simplified and publicly accessible website reporting of aspects of the budget; factsheets; or interactive web tools that enable members of the public including young people to develop an understanding of the budget.

***Recommendation 3.*** The Committee should consider whether the PBO could play a greater role in communicating the principles of fiscal policy, taxes, spending and costing of policies, to the public at large, and further whether this could be done under the current mandate or may require legislative reform.

### **Costings of policy**

The main role and activity of the PBO to date, as revealed by its Annual Reports, has been to cost expenditure policies (and estimate tax revenues that may be raised by policies) for members of Parliament. This has taken up the bulk of the time of the PBO's staff. The independent and non-partisan character of the PBO in policy costing is valuable and should be maintained.

This role of the PBO in providing costings for Opposition, Independent and smaller Party members of Parliament enhances the capacity of members of Parliament to engage in sensible policy debate and produce realistic policies. It is worth noting that this role is relatively uncommon and it is not a role carried out by many other IFIs around the world. (The UK is considering whether the ability to cost policy should be provided to the UK OBR). It reflects the history of establishment of the PBO in the context of Australia's parliamentary democracy.

As the PBO is new, a wide use of its costing capacity seems appropriate and serves a useful educative and informative function. In the longer term, there may be a concern about waste of resources if numerous policies are costed that are likely never to become government policy. (Australia's Parliamentary system may be contrasted with that of The Netherlands, one of the few other jurisdictions where policy costing is carried out by the IFI, but where small party policies may often become part of enacted government policy through a long-standing process of forming government by negotiated compromise and coalition).

A waste of costing resources could be minimised, for example by putting a cap on the number of costings to be done for any one party or member of parliament in a year, or by mandating publication of costings after a period of time.

It is important for this role that costings may be made confidentially on request by the member of Parliament, and trust of the PBO by members of Parliament is crucial. However, it must be acknowledged that there is a tension between this confidentiality and trust, and the goal of fiscal transparency that is a key purpose of the PBO. A compromise is reached for costings carried out once an election is called, which must all be made public. However, this compromise may be undermined where a major party – such as the Liberal/National Party which was in Opposition during the last election – has obtained all its costings in confidence prior to the caretaker period and releases them only a day or two before the election, thereby preventing the public or other parties from fully analysing them.

**Recommendation 4.** The Committee consider whether, once an election is called, all costings of policies that are announced by parties (or Independents) should be made public, whether or not they were obtained prior to the caretaker period. The release could be done by the PBO, after notice was given to the parties or Independents concerned, if they did not release the costings themselves within a set period of time. This would require legislative reform.

**Recommendation 5.** The Committee keep under review the amount of expenditure and staff time by the PBO on policy costings and consider whether a reasonable limit should be placed on costings to prevent waste in future. This may be able to be achieved by procedures implemented by the PBO, without the need for legislative reform.

## Resources and staffing

A key issue for IFIs is maintenance of adequate staffing and resources to carry out their tasks and maintain independence. There are instances in other countries of an IFI being maintained in name but having the bulk of its staff and funding cut. Moreover, in the current era of fiscal constraint, when there is significant public criticism of budgetary cuts to spending, it may be difficult to justify or ensure security of funding for the PBO.

The PBO funding is dependent on appropriations allocated in each year. Currently, PBO funding is adequate. There is a risk that if the PBO produces costings or reports that are

critical of government policy or not in favour of the policies of parliamentarians, that its funding will be cut and hence its independence compromised.

**Recommendation 6.** The Committee should consider how to ensure security of PBO funding for a period of several years to ensure its capacity and independence over a longer term.

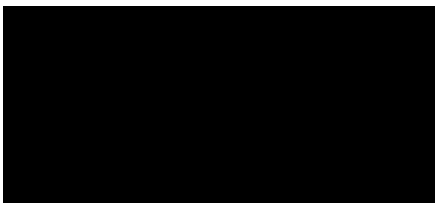
### **Legislative powers to access information**

Timely access to information from government agencies and departments is crucial for effective functioning of the PBO. The ANAO Report notes that the PBO does not have legislative power to demand information from government agencies in its costing or other functions. At present, it appears that the approach of a Memorandum of Understanding (MoU) with government agencies to provide information to the PBO is effective. The experience of the Canadian PBO should be noted, where legislative authority seems not to have been sufficient to enable the PBO to obtain information in a timely fashion.

**Recommendation 7.** The effectiveness of the MoU approach should be kept under scrutiny by the PBO itself and by the JCPAA. However, at present I would not recommend legislative change.

I would be happy to provide further information or explanation if needed.

Sincerely



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