



Parliamentary
Budget Office

Linda Ward
Acting Parliamentary Budget Officer

Ms Lucy Wicks MP
Committee Chair
Joint Committee of Public Accounts and Audit
Parliament House
CANBERRA ACT 2600

Dear Ms Wicks

Thank you for the opportunity to appear at the public hearing on 7 February 2020 as part of the 2019–20 review of the Parliamentary Budget Office (PBO).

At that hearing we took two questions on notice. One related to comparisons between a PBO and Treasury costing of proposals to make franking credits non-refundable, while the second sought the resourcing implications of a change to the PBO's legislation to include minor parties in the election commitments report.

This letter contains responses to those questions, along with some additional material on the published costing of a change to the PBO's mandate relating to the Intergenerational Report, which was requested and subsequently provided at the hearing.

Please let me know if there is any additional material that would assist the Committee.

Yours sincerely



Linda Ward

20 February 2020

Parliamentary Budget Office (PBO) and Treasury costing of a proposal to make franking credits non-refundable

The question asked by the Committee was whether the PBO could provide further information around how our modelling differed to that done by Treasury in respect to a costing of a proposed change to the refundability of excess franking credits.

In 2018, the PBO and Treasury both costed a proposal to make franking credits non-refundable. The proposal costed by Treasury was estimated to raise about \$10 billion (18 per cent) less over the period to 2028–29 than the proposal costed by the PBO.¹ Comments were made about these differences and the PBO responded in a media release on 18 June 2018 (see [Attachment A](#)).

Costings of a policy proposal prepared by different agencies at different points in time are likely to differ, sometimes considerably. This can be due to a number of factors, including:

- the year of data and budget baseline differing, particularly if costings are prepared at different points in time
 - For example the PBO’s costing was based on taxation data from 2014–15 and the 2017–18 Mid-year Economic and Fiscal Outlook baseline, while Treasury’s was based on 2015–16 taxation data and the 2018–19 Budget baseline.
- differences in the details of the policy specification
 - The detail underlying a costing, that is the policy specifications, can have a significant effect on the financial impact. As the specifications for the PBO costing have not been released publicly, it is not possible to comment on whether they are comparable with the Treasury costing.
- differences in assumptions.
 - Assumptions about how people or organisations affected by a policy would change their behaviour usually require a degree of professional judgement, and different experts are likely to make different assumptions.
 - While the PBO’s behavioural assumptions remain confidential, the PBO media release on 18 June 2018 noted that ‘the PBO explicitly assumed that there would be significant behavioural changes that would flow from this policy, particularly for trustees of self-managed superannuation funds’. Treasury’s costing notes that a behavioural response from individuals and self-managed superannuation funds is incorporated, but this is not separately quantified.

¹ The PBO costing minute remains confidential as it has not been publicly released by the Australian Labor Party, although the financial impacts of the relevant proposal were published by the ALP on 27 March 2018. The PBO’s later costing of the Australian Labor Party’s 2019 election commitment was published in the election commitments report.

Expanding the scope of the election commitments report to require the inclusion of minor parties

The Parliamentary Budget Office's (PBO's) legislation currently requires that it publish a report containing the costings of all of the election commitments of 'designated' parties, commonly referred to as major parties (those with five or more Members or Senators in Parliament immediately before the caretaker period).

Following a recommendation from the 2016 review into the PBO that parties with fewer than five Members or Senators should have the option of being included in the report, the PBO published guidance to parliamentarians to outline arrangements for minor parties to opt in to the report. No legislative changes were required to enable the PBO to do so. For the 2019 general election, no minor parties or independents chose to be included in the report.

The question asked by the Committee on this matter was if the word 'option' were removed for parliamentary political parties with fewer than five Members or Senators, to what degree would that impact on the resource capability of the PBO.

Requiring the PBO to include in the report all parties represented in Parliament before the election would require a legislative change. For the 2019 election, had legislation been in place to require this, seven minor parties² would have been included in the report. If the PBO had been required to publish the platforms for all of these parties, the overall financial implications would have been relatively minor for the PBO (involving an increase to the PBO's election year supplement). However, the timing of publication for the minor parties' component would have been later than that for the major parties, and there would likely have been flow-on effects to the delivery times for other PBO work, such as costings and publications.

This assessment of the likely resourcing impact is based on the expectation that minor parties, consistent with the behaviour of the major parties, would have engaged with the PBO in the lead-up to polling day and would have provided the specifications for their policies to enable costings to be undertaken.

If minor parliamentary parties were compelled to have their platforms costed in each general election, their use of the PBO outside the caretaker period could increase in response. There is considerable uncertainty around the potential increase in demand for the PBO's costing resources; in the event that demand exceeded the available resources, the PBO would continue to use its published principles for prioritising costing requests.³ This could result in an increase to median response times for costings for all parliamentarians.

The size and duration of the impact on resources required to cost minor parties' platforms would be heavily influenced by the number of minor parties and the complexity, novelty and size of their policy platforms.

- If Parliament was to choose to expand the scope of the report, one option for managing the increase in the resourcing pressure could be staggering the timing of its publication, for example with parties of five or more members having their platforms published first.

² The Australian Conservatives, Centre Alliance, Derryn Hinch's Justice Party, Katter's Australian Party, the Liberal Democratic Party, Pauline Hanson's One Nation and the United Australia Party.

³ *PBO costing processes, timeframes and prioritisation framework*, is available on the Information papers page of the PBO's website.

- The feasibility of costing minor party platforms within the current legislated deadline would also depend upon the extent of engagement those parties have had with the PBO prior to the caretaker period. For complex proposals, it is a more substantial task to cost a proposal ‘from scratch’ than it is to update proposals that have been costed prior to polling day.

The PBO has experienced cooperation from the parties represented in the election commitment reports to date, which is necessary for the timely delivery of the report. Beyond the process set out in legislation, the PBO cannot compel parties or individuals to engage in vital aspects of the report process, such as providing their list of election commitments and clarifying the policy specification for identified commitments. That said, if any party were not to participate to the degree required to complete robust election commitment costings, the PBO could include a statement of that fact in the report in lieu of costings.

It is important to note that if a proposal to amend the PBO’s legislation resulted in the inclusion of parties with fewer than five members in the election commitments report, careful consideration would be required to determine whether such an amendment would capture parties that were not represented in the Parliament at the time an election was called. To include those candidates or parties not represented in Parliament prior to the election would likely have significant resourcing implications, depending on the nature of the proposed change.

Resourcing implications of the PBO undertaking the Intergenerational report (IGR)—additional remarks

At the public hearing on 7 February, Committee members enquired about the resource implications of the PBO being given responsibility for undertaking the IGR, and the PBO provided the Committee with a hardcopy of the ALP’s election commitment costing *Expanding the mandate of the Parliamentary Budget Office (PBO)*, PER406 (see [Attachment B](#)). That policy would have expanded the PBO’s mandate to include both the IGR and the preparation of independent macroeconomic forecasts.

If the Parliament was to expand the mandate of the PBO to include the IGR only, the resource implications would be closer to the estimate in Attachment A of the costing for undertaking the IGR alone. This is based on the assumption that the PBO would use the Treasury’s long-term forecasts to prepare the IGR. If the PBO was asked to also undertake the macroeconomic forecasts that underpin the IGR, this would require further amendments to the PBO’s legislation and additional funding.

The costing indicated that secondments of staff, including from the Treasury and the Reserve Bank of Australia, may be required during a transition period. This related to the specific proposal for the PBO to prepare the IGR from 2020 and prepare independent macroeconomic forecasts from the 2020–21 Budget. Should the Parliament decide to expand the PBO’s mandate to include the IGR function from 2025 or a later date, this capability would be developed in-house over time, drawing on existing appropriately skilled staff members and normal recruitment processes.



Jenny Wilkinson
Parliamentary Budget Officer

18 June 2018

Media release

Imputation credits policy costing

Earlier today, comments have been made about the Parliamentary Budget Office (PBO) estimates of the gains to revenue that may flow from the Australian Labor Party's (ALP's) policy to make imputation credits non-refundable.

“The PBO brings our best professional judgement to the independent policy costing advice we provide. We have access to the same data and economic parameters as The Treasury and draw upon similar information in forming our judgements,” Parliamentary Budget Officer Jenny Wilkinson stated today.

“We stand behind the PBO estimates that have been published by the ALP in relation to this policy, noting that all policy costings, no matter who they are prepared by, are subject to uncertainty.” In its advice, the PBO is explicit about the judgements and uncertainties associated with individual policy costings.

The PBO confirms that it always takes into account current and future policy commitments, as well as behavioural changes, in its policy costings. In this case, as outlined at the recent Senate Estimates hearings, these included the superannuation changes announced in the 2016–17 Budget and the scheduled company tax cuts. In addition, the PBO explicitly assumed that there would be significant behavioural changes that would flow from this policy, particularly for trustees of self-managed superannuation funds.

The PBO was established as an independent institution in 2012 with broad support from the Parliament. A key rationale for the formation of the PBO was to develop a more level playing field, by providing independent and unbiased advice to all parliamentarians about the estimated fiscal cost of policy proposals. The purpose of establishing the PBO was to improve the public's understanding of, and confidence in, policy costings and enable policy debates to focus on the merits of alternative policy proposals.

Contact Officer: **Jenny Wilkinson**





Parliamentary
Budget Office

Policy costing

| Expanding the mandate of the Parliamentary Budget Office (PBO) | |
|--|------------------------|
| Party: | Australian Labor Party |
| <p>Summary of proposal:</p> <p>This proposal involves expanding the mandate of the Parliamentary Budget Office (PBO). The PBO would:</p> <ul style="list-style-type: none"> • produce the five-yearly intergenerational report from 2020 • prepare independent macroeconomic forecasts, from the 2021-22 Budget, that would underpin the estimates of revenue and expenditure published in the Government's economic and fiscal updates • join the Joint Economic Forecasting Group (JFIG). | |

Costing overview

This proposal would be expected to decrease both the fiscal and underlying cash balances by \$26.6 million over the 2019-20 Budget forward estimates period. These impacts are entirely due to an increase in departmental expenses over this period.

A breakdown of the financial implications of this proposal over the 2019-20 Budget forward estimates period is included at [Attachment A](#). The proposal would be expected to have an ongoing impact beyond the 2019-20 Budget forward estimates period.

The proposal represents a substantial extension of, and change in, the mandate of the PBO and would require a significant increase in the size of the PBO, with an associated expansion in the PBO's skills base, information technology (IT) infrastructure and office accommodation.

The costing provides for the PBO to draw on subject-matter experts within and outside government in the development of the intergenerational report. It is anticipated that the PBO would have access to the Treasury's models that have been used in the course of preparing previous intergenerational reports.

The macroeconomic forecasting component of the costing is based on the approach to forecasting used by the Treasury. Macroeconomic forecasts would be published at least two times a year alongside the annual Budget and the Mid-year Economic and Fiscal Outlook report, with provisional updates to the macroeconomic forecasts being provided confidentially to government ahead of the budget process to inform budget decision making.

The costing anticipates that the PBO is provided access to the Treasury's forecasting models and frameworks, including the macroeconomic forecasting model that is under development, and that a memorandum of understanding would be agreed to enable the PBO to use this and other relevant Treasury models in the forecasting process.

The costing provides for the Parliamentary Budget Officer to appoint a three-person advisory panel of eminent macroeconomists. The panel would examine and provide guidance on the PBO’s economic forecasts. Panel members would be remunerated and the panel’s role would be an advisory one, with the Parliamentary Budget Officer having ultimate responsibility for the independent economic forecasts.

The costing provides for a business liaison program. Based on the Treasury program, this would require in excess of 100 face-to-face interviews per year involving quarterly meetings with companies across a range of critical sectors of the economy, and targeted contacts with specific sectors that are important to the forecasts.

A provision for consultancies to assist with model development, review and analysis has been included.

Table 1: Financial implications (\$m)^{(a)(b)}

| | 2019–20 | 2020–21 | 2021–22 | 2022–23 | Total to 2022–23 |
|--------------------------|---------|---------|---------|---------|------------------|
| Fiscal balance | -6.5 | -6.8 | -6.6 | -6.7 | -26.6 |
| Underlying cash balances | -6.5 | -6.8 | -6.6 | -6.7 | -26.6 |

(a) A positive number represents an increase in the relevant budget balance; a negative number represents a decrease.

(b) Figures may not sum to totals due to rounding.

Key assumptions

The PBO has made the following assumptions in costing this proposal.

Legislation

- The required legislative amendments to the *Parliamentary Service Act 1999* and the *Charter of Budget Honesty Act 1998* are made to enable the PBO to assume the additional functions outlined in the proposal.

Modelling capability

- The PBO would have access to the Treasury’s macroeconomic forecasting and intergenerational report models.

Staffing levels

- Appropriately skilled and experienced staff could be recruited to carry out the expanded mandate. Given the small pool of qualified macroeconomic forecasting staff, this would likely require the secondment of staff from Treasury, and possibly the Reserve Bank of Australia, during a transition period.
 - The costing provides for a scaling up of PBO staff on the basis that the PBO would be fully staffed by 30 June 2020 in preparation for producing macroeconomic forecasts, and documents to support these forecasts, to underpin the 2021-22 Budget.
- Additional staff would be required to cover the additional administrative, publishing and corporate support activities commensurate with the increase in the PBO’s size and responsibilities.
- There is no change to the Treasury’s resourcing as a result of this proposal.

- While responsibility for preparing the macroeconomic forecasts that underpin budget updates would be transferred from the Treasury to the PBO, the Treasury would still be expected to need macroeconomic capabilities in order to advise government on: macroeconomic developments, the appropriate macroeconomic policy responses to developments in the economy, and the macroeconomic impact of policy proposals being considered by government.

Accommodation and infrastructure

- The PBO remains in Parliament House and would require a provision for fitout of office accommodation and additional IT infrastructure necessary for the increased staff and enhanced responsibilities.
- If the PBO were unable to remain in Parliament House, funding in addition to that presented in this costing would be required to rent and fitout alternative premises, establish the IT infrastructure to maintain the PBO's protected IT network, and move existing PBO staff and infrastructure to the new premises. The estimated additional expense would be in the order of \$1.6 million in 2019-20 and around \$1.0 million ongoing each year.

Methodology

Estimates of the number and composition of staff required to prepare the intergenerational report and independent economic forecasts are based on the Treasury's approach to macroeconomic forecasting set out in the *Review of Economic Modelling at the Treasury* report produced by Independent Economics in 2017.

Staffing and related infrastructure costs are estimated using the Department of Finance's standard departmental costing calculator, and advice from the Department of Parliamentary Services.

The estimated costs of the advisory panel of eminent macroeconomists are based on the Remuneration Tribunal's determination for sitting fees for similar panels.

Data sources

The Treasury, 2012. *Review of Treasury Macroeconomic and Revenue Forecasting*. [Online] Available at: <http://www.treasury.gov.au/PublicationsAndMedia/Publications/2013/Forecasting-review> [Accessed April 2019].

Independent Economics, 2017. *Review of Economic Modelling at the Treasury*. [Online] Available at: <http://research.treasury.gov.au/external-paper/review-of-economic-modelling-at-the-treasury/> [Accessed April 2019].

Tease, W., 2016. *Forecasting in Treasury*, Address to CEDA's Economic and Political Overview Conference, Brisbane, 18 February 2016. [Online] Available at: <http://www.treasury.gov.au/~media/Treasury/Publications%20and%20Media/Speeches/2016/Forecasting%20in%20Treasury/Downloads/PDF/Forecasting-in-Treasury-Warren-Tease.ashx> [Accessed April 2019].

Tease, W., 2015. *Review of Treasury's Macroeconomic Forecasting Capabilities*. [Online] Available at: <http://www.treasury.gov.au/~media/Treasury/Publications%20and%20Media/Publications/2016/Review%20of%20Macroeconomic%20Forecasting%20Capabilities/Downloads/PDF/Review-of-Macroeconomic-Forecasting-Capabilities.ashx> [Accessed April 2019].

The Department of Finance provided the Standard Department of Finance departmental costing calculator.

Attachment A – Expanding the mandate of the Parliamentary Budget Office (PBO) – financial implications

Table A1: Expanding the mandate of the PBO – Fiscal and underlying cash balances (\$m)^{(a)(b)}

| | 2019–20 | 2020–21 | 2021–22 | 2022–23 | Total to 2022–23 |
|---|-------------|-------------|-------------|-------------|------------------|
| Expenses | | | | | |
| <i>Departmental</i> | | | | | |
| <i>PBO to produce intergenerational report from 2020</i> | -2.5 | -1.4 | -1.4 | -1.4 | -6.7 |
| <i>PBO to prepare economic forecasts from 2021-22 Budget, and join the Joint Economic Forecasting Group</i> | -4.0 | -5.4 | -5.2 | -5.3 | -19.9 |
| Total – departmental | -6.5 | -6.8 | -6.6 | -6.7 | -26.6 |
| Total – expenses | -6.5 | -6.8 | -6.6 | -6.7 | -26.6 |

(a) A positive number for the fiscal balance indicates an increase in revenue or a decrease in expenses or net capital investment in accrual terms.

A negative number for the fiscal balance indicates a decrease in revenue or an increase in expenses or net capital investment in accrual terms.

A positive number for the underlying cash balance indicates an increase in receipts or a decrease in payments or net capital investment in cash terms.

A negative number for the underlying cash balance indicates a decrease in receipts or an increase in payments or net capital investment in cash terms.

(b) Figures may not sum to totals due to rounding.