

## **FINANCIAL ARRANGEMENTS FOR NEW INSTITUTIONS**

1 The sub-Committee considered possible financial arrangements for the new political institutions. (References to "institutions" in Northern Ireland should be interpreted by reference to the other work of the sub-Committee). The following considerations emerged.

### **Levels of Public Expenditure**

2 The sub-Committee noted that the existing financial arrangements were designed to ensure that, against a background of parity of taxation, the people of Northern Ireland received levels of public services broadly comparable with those in Great Britain. Levels of local expenditure are determined as part of the UK public expenditure annual survey and are not constrained by the revenue generating capacity of the region. The difference between expenditure and revenue is then made up by a subvention from the UK Exchequer (currently about £2.5 billion, or more than £1 in every £3 of public expenditure in Northern Ireland).

3 In the view of the sub-Committee, it is important that this expenditure based (rather than a revenue based) arrangement for the determination of the quantum of spending should be preserved. Moreover, new NI political institutions should seek to preserve as far as possible the present comparability mechanism which has provided useful stability in effecting annual adjustments to the NI PE Block ("the Block") total while leaving maximum local flexibility in determining how resources should be allocated. Maintaining the integrity of the Block in this way should also mean that NI could expect to benefit from future savings in operational programmes whether through achieving greater economy or, for example, as a result of a reduction in security-related expenditure.

4 In view of the sub-Committee the sources of funding should remain on broadly the same basis as at present ie: attributed taxation, grant-in-aid, rates, charges and EC receipts. The local administration would be free to vary the level of the regional rate. However, it would be essential that the exercise of this power should genuinely increase regional resources rather than simply offsetting other sources of funding such as the grant-in-aid. A local administration with legislative powers would be able to change the rating system and could consider raising revenue [for local authority type services] in other ways. It would be able to determine the level of charges for a wide range of public services (eg: parking, vehicle testing, planning applications). The local administration would also intend to give higher priority to the earning of EC receipts. In each of these cases, the intention would be that the resources should be used to fund additional local expenditure.

### **Role of Secretary of State**

5 Under the new arrangements, the Secretary of State would retain responsibility for expenditure on particular functions and the local political institutions will assume responsibility for a range of services which might represent a large proportion of the NI Block. It was recognised that local institutions will operate within the UK public expenditure framework and the annual Public Expenditure Survey will be the main determinant of the overall level of resources.

6 In view of the UK dimension to expenditure decisions, it would be the Secretary of State's responsibility to secure resources in the Survey for the Block as a whole out of which



those services within his own responsibility and those administered by local institutions would be funded through an allocation mechanism yet to be agreed.

7 It would be particularly important to ensure that a strong bid was made, as an integral element of a political settlement, to provide the new administration with extra resources to tackle the major problems which NI continues to face.

8 Under the new arrangements there would be a supporting role for the local administration, which would give the Secretary of State a detailed annual assessment of its financial requirements to inform his handling of the Survey. (This was considered at Annexes A and B to the Report of 10 June). The local administration would wish to be represented at negotiations between the Secretary of State and the Chief Secretary on the level of resources. This would be particularly important where the pressures on the Block were such that bids were being pressed over and above the normal workings of the comparability mechanism.

### **The Discretion of the Local Administration**

9 Within its own area of responsibility the local administration would have a very wide measure of discretion (equivalent to that currently exercised by the Secretary of State) to allocate its resources in line with its view of Northern Ireland's needs. It would, however, be necessary to take account of the following:

- (a) the local administration would be constrained by UK commitments to the European Community;
- (b) the Treasury would, as a condition of financial support, wish to continue to be assured that the local administration used its resources with due regard for value for money. This, of course, is an interest which any local administration would share, provided that efficiency savings are retained within the Block;
- (c) transfers of resources could not be made from an agreed parity such as Social Security to other areas; but additional funding for Social Security would not be a call on the Block.

### **Authority to Spend and Accountability**

10 At present Northern Ireland operates a structure through which Parliament authorises expenditure out of the Northern Ireland Consolidated Fund. The local political institutions would provide this authority under the new arrangements for expenditure on devolved services. The mechanism for this would be through the approval of a detailed annual budget which would give Departments both the authority to spend and would set the framework within which they would have to account for the expenditure. (This was considered in Annexes A and B to the Report of 10 June).

11 The Northern Ireland Audit Office, which is independent of the Executive, would continue to examine the propriety and regularity of expenditure, and the economy, efficiency and effectiveness with which policy is carried out. It should report to a special committee (a local equivalent of the Public Account Committee) set up by the new local institutions with power to summon Accounting Officers to give evidence, and to make reports.

## A LOCAL ADMINISTRATION AND FINANCE

### Introduction

1 Whatever for a local administration may take one of its central functions will be to decide how best to allocate its available resources to meet its objectives in those areas for which it is responsible. It will also probably have to decide how much to raise locally through rates or their equivalent; to negotiate the size of its grant from Whitehall; and to ensure that resources are spent in a way which achieves value for money.

2 This paper describes how the existing financial system for the Northern Ireland (NI) Departments and the Northern Ireland Office (NIO) works. Some features of the present system are set down in legislation (eg the Grant-in-Aid); others are internal arrangements within Government for the conduct of business (eg the Northern Ireland Block). But for the purposes of this paper we shall discuss the present arrangements as a complete system. Under the NI Constitution Act the NI Departments are responsible for "transferred" matters (eg agriculture, industry, health) and the NIO for some "reserved" and "excepted" matters (eg security, police, elections, prisons). Other "reserved" and "excepted" matters are dealt with by other UK Departments (eg tax, immigration). NI Departments and NIO expenditure is referred to collectively as the "NI Block". This reflects the fact that for some purposes they are managed together. The "Block" is the main subject of this paper.

2 Total Block expenditure of approximately £6.4 billion in 1991/92 can be broken down broadly as follows:

	£M
Agriculture	213
Industry, Energy, Trade and Employment	389
Transport	163
Housing	258
Other Environmental Services	170
Protective Services (Fire)	35
Education	1,122
Health and Personal Social Services	1,162
Social Security	2,107
Other Public Services	66
Law and Order (NIO)	<u>776</u>
Total	6,449

Note: This includes expenditure by Government Departments, public corporations, statutory bodies and grants to local authorities.

3 NIO and NI Departments expenditure does not represent the totality of Government expenditure in or for Northern Ireland. The Ministry of Defence and the NI Court Service also spent considerable sums in 1991/92. IN addition, the revenue - raising departments (Customs and Excise and Inland Revenue) spend resources on their activities in Northern Ireland; and the Home Office runs immigration facilities and the Passport Office. Other departments also spend small amounts of resources either in or on behalf of Northern Ireland.



## Funding

- 4 NI Block expenditure is at present financed from six sources:
- the proceeds of central taxation eg VAT, Income Tax (Called "attributed taxation") raised in Northern Ireland (S.15 NI Constitution Act);
  - a grant-in-aid paid by the Secretary of State for Northern Ireland to the Northern Ireland Consolidated Fund (S.16 NI Constitution Act);
  - issues from the NI National Insurance Fund (including some resources transferred from the GB Fund);
  - the regional rate, excluding that portion raised by district councils;
  - miscellaneous receipts eg water charges, sales of land and buildings (but not proceeds from privatisation).
  - NIO expenditure voted from the UK Consolidated Fund.
- 5 The relative importance of these different sources can be shown by looking at 1991/92 Block expenditure, which was funded as follows:

	£M
(a) -attributed taxation	2,950
(b) -grant-in-aid	1,500
(c) -national insurance fund and other non-voted expenditure eg external financing or public corporations	950
(d) -regional rate	200
(e) -miscellaneous receipts	100
(f) -NIO expenditure	<u>750</u>
Total	6,450

NIO expenditure (£750m) relates to those services administered by the NIO which under the NI Constitution Act 1973 are "reserved" or "excepted" matters and is therefore paid for out of Estimates Voted by Parliament from the UK Consolidated Fund (the grant-in-aid is voted in the same way). The remainder (£5700m) is for "transferred" services, which are financed from the NI Consolidated Fund, which receives attributed taxation, the grant-in-aid, and the product of the regional rate. Money is voted from the NI Consolidated Fund by separate Northern Ireland Government Estimates which are currently, in the absence of a NI Assembly, voted at Westminster. In all cases "miscellaneous receipts" are taken into account in individual Votes. For example, the Vote for Water Services, which covers current and capital elements, is reduced by the amount of expected receipts for water charges.

## The Level of Expenditure



6 The level of Government expenditure, including that for Northern Ireland, is set through the annual Public Expenditure Survey (PES). The level of expenditure for (eg) 1993/94 and the two subsequent years is decided this calendar year (1992), and the level of expenditure for each area of Government is announced in the Autumn Statement. The level of expenditure for Northern Ireland covering both Northern Ireland Departments and the Northern Ireland Office is currently determined within that system.

7 The overall level of Block expenditure provision for Northern Ireland is set primarily by means of a "comparability formula". This ensures that public expenditure levels in NI are adjusted in line with developments in the rest of the UK in so far as they are comparable to those activities which are the responsibility of the Secretary of State for Northern Ireland. This arrangement relies on a calculation on a proportional basis to ensure that we receive 2.75% of the changes in programmes in the rest of the UK since this reflects our proportion of the UK population. This is different from the mechanism for Departments like (eg) the Home Office, who must justify increases in expenditure to the Treasury on a detailed basis. (Scotland and Wales, however, enjoy Block systems similar to those in Northern Ireland).

8 This system is not immutable; it is open to the Treasury to abrogate the operation of the formula by seeking to reduce NO expenditure; it is also open to the Secretary of State to bid for additional resources beyond those available under the comparability formula if he feels that NI needs will be seriously under funded, and he has chosen to do so on several occasions in recent years. Any such bid is taken to suspend the operation of the comparability formula, and leave all NI expenditure open to detailed Treasury scrutiny. The comparability formula has, in technical terms, served Northern Ireland well, by providing a reactively stable basis for the annual adjustment of public expenditure plans in Northern Ireland.

9 Those funds which are made available for Northern Ireland through the PES system, and subsequently through Estimates/grant-in-aid are referred to collectively as the "Northern Ireland Block". Within this Block the Secretary of State has substantial discretion to allocate funds to meet his assessment of public expenditure needs and priorities. (There are some exceptions; social security is funded on a basis which maintains parity with GB and unspent resources cannot be allocated to other programmes).

### **The Allocative Process Within Northern Ireland**

10 Within the Northern Ireland Block DFP operates its own annual Public Expenditure Survey. NI Departments and the NIO submit expenditure proposals for the next three years, including bids for any additional resources which they consider necessary. In the Autumn, when the overall level of resources available for NI programmes becomes known, DFP makes recommendations to the Secretary of State on which bids should be met.

11 The present NI Block includes both "transferred" matters which are the responsibility of the NI Departments, and those "reserved/excepted" matters which are the NIO's responsibility. In making allocations, the Secretary of State has to decide the relative merits of priorities. In practice, security has had to be the highest priority. Strengthening the economy has been the second priority and "targeting social need" third. But not every bid within these categories can be met and other priorities (eg health, social services, environment) must also be met. A successful public expenditure strategy must address the whole range of the Province's needs.

### **Approval by Parliament**



12 The allocations decided by the Secretary of State are announced to Parliament in a statement in late Autumn after the Chancellor's Autumn Statement. These expenditure plans for the year ahead are then incorporated into Northern Ireland Main Estimates which are presented to Parliament at the beginning of the Financial Year, although minor changes may be introduced between the announcement of public expenditure plans and the drawing up of Estimates to take account of changing circumstances. Each NI Department is responsible for drawing up its own Estimates, but these must be approved by DFP. In the case of the NIO, Estimates must be approved by HM Treasury in consultation with DFP. There are usually two or three Parliamentary opportunities to discuss NI public expenditure in the transferred field:

- (a) Main Estimates (usually May/June)
- (b) Autumn Supplementary (December) - taken only if necessary
- (c) Spring Supplementary (February/March)

(Of course, the Main Estimates are too late to provide resources for the beginning of the financial year on 1 April. Therefore, at Spring Supplementaries money is also voted "on account" for the next Financial year, to enable Government expenditure to continue until the Main Estimates. There are rules restricting the scope of votes on account so as not to pre-empt Parliament's eventual decision at Main Estimates). Estimates are formally adopted by orders known as "Appropriation Orders". The debates are an opportunity for Members to raise any matter of public concern in the transferred field, and they avail themselves of this opportunity.

13 During the Financial Year it remains open to the Secretary of State to reallocate resources within the Block to meet evolving priorities, proposing Supplementary Estimates as necessary to Parliament. In practice, additional demands are usually balanced by reduced requirements. If this is not the case, it could be necessary to take action to reduce expenditure in discretionary areas and, in exceptional circumstances, a bid on the Reserve may be submitted to the Treasury.

#### **Department of Finance and Personnel**

14 In dealings with the Treasury on the level of the Block, and on all questions of the allocation of resources between Departments, the Secretary of State is advised by the Department of Finance and Personnel. The Department approves Northern Ireland Estimates, and presents them to Parliament. The Department is also responsible for approving major projects and programmes in the NI Departments, seeking any necessary Treasury approvals, and co-ordinating applications for EC resources.

15 Within the Northern Ireland administration, it is also the role of the Department of Finance and Personnel and the Minister in day-to-day control to pursue value for money in Government spending. This includes encouraging the use of the best possible financial techniques, the promotion of the government's various efficiency initiatives including, for example, privatisation and "Next Steps" agencies, and, of course, the rigorous scrutiny of the need for any spending proposals.

16 Since NIO expenditure is borne on the UK Consolidated Funds, its expenditure is scrutinised by Treasury, but the Department of Finance and Personnel also take a close interest because it is a major component of the NI Block.



## **Relations with Bodies Outside Northern Ireland**

17 Although the Secretary of State has a high degree of discretion in spending Northern Ireland resources, decisions on resource allocation must also take account of the requirements of outside bodies. In some areas, (eg industrial development) spending levels are in principle constrained by European Community agreements. But the Treasury has the most important role, and makes a number of requirements. First, the Treasury requires that DFP should effectively control the level of public expenditure from the Northern Ireland Block, and ensure value for money in NI Departments. It has to be assured, for example, that systems are in place to appraise projects using the most up-to-date techniques. It also seeks to ensure that policies such as market testing and privatisation, which should lower the cost of public services, are implemented. To this end, it regularly seeks information from DFP about Northern Ireland public expenditure. Second, the Treasury requires to be consulted about any proposals in Northern Ireland which could have a repercussive effect on public expenditure in other parts of the UK, while in some other areas the level of provision/benefits is determined on a parity basis. Nevertheless, there has been scope for the adoption of a range of distinctive and innovative policies (eg Making Belfast Work) to meet local needs.

## **The Rates**

18 The Regional Rate is struck each year at a level agreed with the Treasury. The principle is that rates should make a broadly equivalent contribution to local services as community charge and business rates do in GB, taking account of a notional amount of Rate Support Grant.

## **Receipts from the European Community (EC)**

19 Northern Ireland earns receipts from a number of EC budgetary sources. The largest is the Guarantee Section of the European Agricultural Guidance and Guarantee Fund, where money is passed from Brussels to the farmer, mainly via the Intervention Board for Agricultural Produce. These payments are additional to the NI Block, although they have to be taken into account by MAFF with other Intervention Board expenditure for public expenditure planning purposes. Most other EC funding is anticipated when the public expenditure total is set, and the public expenditure total is greater than it would have been had the EC receipts not been available. In cash terms, of course, all EC money is paid to its due recipient. Where this is a Northern Ireland department, the receipts are passed to the Northern Ireland Consolidated Fund.

## **Comptroller and Auditor-General**

20 The Comptroller and Auditor-General for Northern Ireland authorises the issue of public funds and certifies the accounts of all Northern Ireland Departments and a wide range of other public sector bodies. He is also responsible for examining the economy, efficiency and effectiveness with which policy is carried out, and probing the basis of expenditure decisions. He currently submits reports to the Public Accounts Committee at Westminster, which will examine officials on those reports where it considers appropriate to do so. This independent ex-post facto examination of Government spending is an important discipline on the system.

## **Future Local Administration**

21 Annex A sets out how the present finance system might be adapted to a local administration having a range of responsibilities on the lines of the 1973 Constitution Act. These arrangements would of course have to be varied if the administration had substantially different powers or was closer in form to a GB local authority.