

The New Zealand Fiscal Management Approach

An Explanation Of Recent Changes

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An Outline of the Changes Made to Further Integrate the Annual Budget Process with the Government's Fiscal Policy Approach

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Introduction

This paper builds on Treasury working paper 2001/24, *Budget Management that Counts: Recent Developments in Budget and Fiscal Management in New Zealand* (Barnes and Leith), which outlined the evolution of the New Zealand's fiscal management until 2001. 2001/24 noted the use of "fiscal provisions" as a tool for setting limits and allocating resources for budget management purposes, and (along with subsequent papers, including 2001/25) posed challenges for further development of the Government's fiscal management approach.

This paper and its annexes:

- outline the changes that have since been made to the New Zealand fiscal management approach (see Table 1 for a useful summary)
- explain how these changes fit within New Zealand's wider fiscal management framework
- provide the rationale behind these changes
- provide further detail on how the budget process will be managed
- discuss the risks and challenges with the new approach respectively

Table 1 – Comparison between the previous fiscal provisions and the revised fiscal management approach

| | Previous Fiscal Provisions | Revised Fiscal Management Approach |
|---|---|--|
| When is the Government's fiscal policy, including long-term fiscal objectives, set? | At the start of each parliamentary term. | No change. |
| What factors are taken into account when setting short-term spending intentions? | <ul style="list-style-type: none"> ▪ The current macroeconomic outlook, including the estimated impact of cyclical factors and fiscal stance; ▪ NZ Super Fund pre-funding requirements; ▪ Pressures on operating and capital baselines; ▪ Relative priorities between operating and capital; ▪ Progress of the operating and debt tracks towards objectives for the five-year forecast period; ▪ Progress of the operating and debt tracks towards objectives for the 10 year outlook tracks. | No change. |
| How often are short-term spending intentions set? | Once at the start of each parliamentary term. However, in practice they are changed from time to time on the basis of spending pressures, or if there is a significant economic shock such as the Asian crisis in 1998. | Formal reassessments at the start of each annual Budget process around September, with a "road-check" against the latest fiscal information before each Budget is finalised. Greater use of top-down information than previously. |
| Is an operating and capital spending amount entered into the forecasts? | Yes. Provision focuses only upon "controllable spending" (i.e. discretionary initiatives and cost pressures). | Yes. The "forecast new spending amount" encompasses all impacts on the operating balance with the exception of a few pre-specified volatile items. |
| How are spending intentions expressed? | Spending intentions are communicated via a fixed three-year aggregate fiscal provision in nominal dollars. Provision focuses only upon "controllable spending" (i.e. discretionary initiatives and cost pressures). | Spending intentions are communicated via a desired operating balance and debt track consistent with overall fiscal policy. While the nominal amount will be communicated, the focus upon this will be lower than with the fiscal provisions. Spending intentions will be noted to: <ul style="list-style-type: none"> ▪ cover a wider range of impacts than previously ▪ be subject to reassessment ▪ have a different status depending upon the time period referred to – the closer the time horizon, the firmer the intentions. |
| Is there an amount for new spending for internal budget management? | Yes on the basis of a provision in the forecasts. | Yes on the basis of an amount in the forecasts. However, <ul style="list-style-type: none"> ▪ this amount must manage more impacts ▪ budget processes will more explicitly accommodate the potential for changes to the size of the amount at the end of the Budget process. |

New Zealand's fiscal management approach – the changes

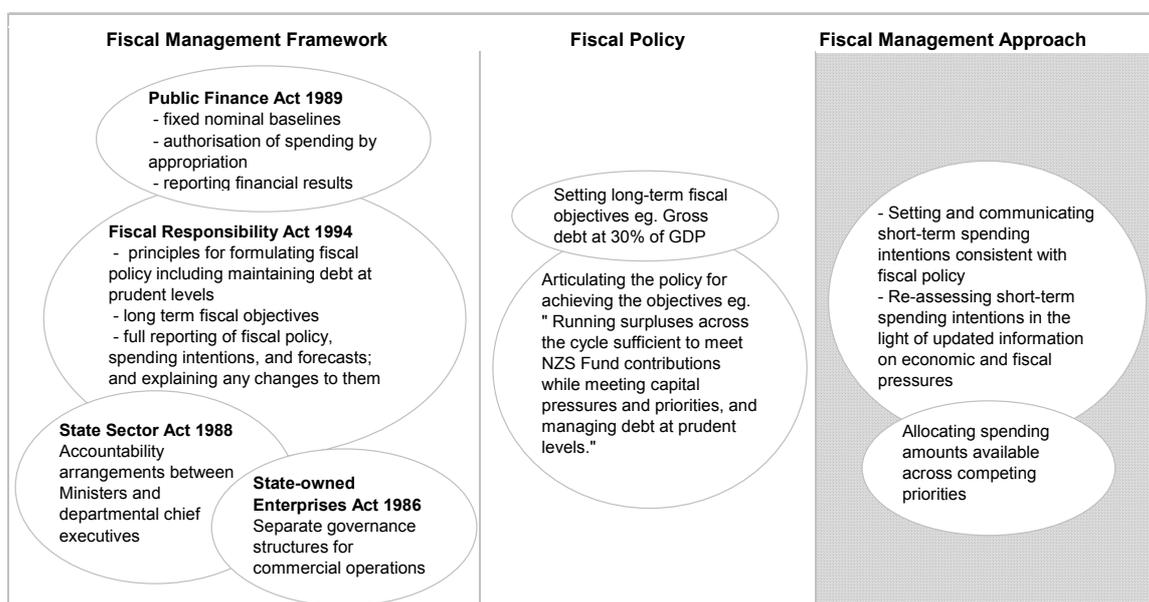
The use of fixed three-year limits (“the fiscal provisions”) as part of the Government’s fiscal management approach was introduced at a time when the advent of proportional representation heightened need to demonstrate fiscal credibility. They represented a significant advance for fiscal management in New Zealand. The Government has run surpluses for the six years the fiscal provisions have been in place.

As with any fiscal management approach, over time a number of issues arose with using a three-year fixed nominal limit from both an external communication perspective and an internal budget management perspective. The challenge in revising the approach to address these issues was to retain the advances achieved by the fiscal provisions. In addition, recognition had to be given to the realities of fiscal management. Allocating scarce resources among competing priorities will always involve an element of friction.

The wider fiscal management picture

It is important to be clear about how the changes to the Government’s fiscal management approach fit into the wider fiscal picture.

Figure 1 – New Zealand’s fiscal management approach: the context (shaded area indicates where the changes have been made)



Four pieces of legislation comprise New Zealand’s fiscal management framework (see Figure 1). The framework, with its focus upon the longer term and its requirements around transparent fiscal management, establishes the context for developing overall fiscal policy and translating that into shorter-term spending intentions.

A key anchor for the Government’s fiscal policy is the long-term gross Crown debt objective, currently set at 30% of GDP. To achieve this objective, the Government’s current policy is to run surpluses across the economic cycle, while also meeting NZS Fund contributions and capital pressures and priorities.

An important aspect of this Government’s fiscal policy is to not adjust spending intentions in response to “economic shocks”. This allows “automatic fiscal stabilisers” to operate.¹

This overall fiscal framework and fiscal policy remain unchanged. The revisions outlined in this paper focus upon the Government’s fiscal management approach for setting, communicating and managing short-term spending intentions (the shaded area in Figure 1).

The changes

The ideas behind the revisions to the fiscal management approach are to:

- get closer linkages between the Government’s fiscal management approach and its overall fiscal policy and progress towards long-term fiscal objectives, which is influenced by factors which are constantly changing;
- simplify the rules around allocating the amount available for new spending, which were becoming increasingly difficult to maintain.

Setting short-term spending intentions involves considering:

- the current macroeconomic outlook, including the estimated impact of cyclical factors and fiscal stance;
- NZ Superannuation Fund pre-funding requirements;
- the level of “bottom-up” pressures on operating and capital baselines, such as cost pressures and budget initiatives;
- relative priorities between operating and capital considerations;
- progress of the operating balance and debt tracks towards objectives for the five-year forecast period;
- progress of the operating balance and debt tracks towards objectives for the 10-year outlook tracks.

The previous fiscal management approach (using the fiscal provisions) worked through these factors to determine spending intentions. The revised fiscal management approach considers the same factors. However, there are three key differences around how spending intentions are communicated and managed.

1. *Focus on Progress of Operating Balance and Debt Tracks Towards Objectives:* under the old approach using the fiscal provisions, spending intentions were translated into cumulative three-year nominal operating and capital limits (“fiscal provisions”). These provisions formed a focus for communicating spending intentions.

Under the new approach the focus is more upon overall progress towards fiscal objectives, and what the operating balance and debt tracks over a longer timeframe (five- and ten-year horizons) could accommodate, rather than translating spending intentions into three-year fixed nominal limits.²

¹ That is, by not reducing spending in a downturn or increasing spending in an upturn the Government does not exacerbate swings in the economic cycle.

² Spending intentions over the parliamentary term will also be tracked for accountability purposes.

2. *Spending Intentions have a Different Status* - the factors influencing the Government's fiscal position outlined above frequently change.

Under the previous approach, the fiscal provisions were generally perceived as fixed, and were only to be reassessed if there were a significant economic event, such as the Asian crisis in 1998.

Spending intentions will now be regularly reassessed in light of changes to the factors noted above in order to ensure short-term spending intentions remain consistent with overall fiscal policy and progress towards long-term objectives.

Spending intentions will therefore have a different "certainty" status depending on the time period referred to. The closer the horizon, the firmer the intentions, as there are fewer uncertainties around the various factors influencing the fiscal position. The language in the Budget documents will reflect this.

Reassessments of spending intentions will take place at the beginning and the end of each Budget process. The following points clarify the role of the reassessments and the limited potential for movement:

- Overall fiscal policy is set at the start of the parliamentary term. Actual spending levels may be fine-tuned for various factors (e.g. relative priorities between capital and operating considerations). However, the need to achieve the desired OBERAC and debt tracks over the medium term will limit the potential for significant movements.
- Changes in the economic outlook reflect a mix of cyclical and longer-lasting factors. Keeping spending and tax plans unchanged during upswings and downswings allows for the operation of automatic fiscal stabilisers. In practice it is difficult to distinguish between cyclical movements and a change in the medium-term economic outlook. The reassessments will need to allow for this uncertainty. In this sense, the current fiscal policy of a bias to no change will be maintained.
- Changes resulting from the final reassessment in particular will need to be minimised, in order to maintain the credibility of the amount set at the start of the Budget process.

3. *Wider Impacts Managed* - similar to the previous fiscal provisions approach, spending intentions will still be incorporated into the forecasts, and these amounts will still set the parameters for developing Budget packages.

However, in order to reinforce the focus upon the bigger picture of achieving the desired operating balance and debt tracks, the constraint must take account of a wider range of operating and debt impacts than previously, including demographically driven funding increases and decreases, settlements of legal claims, and student loan provision movements.

Now, all impacts on the operating balance and debt also impact on either the available operating or capital spending amounts, with the exception of a few pre-specified volatile items expected to net out over time.

Consistent with fiscal policy, these pre-specified volatilities are not generally expected to impact on spending intentions, and are therefore left for consideration in the assessment stages. The pre-specified items are mainly revaluations and cyclical tax, finance costs, interest income and benefit re-forecasts. They are

incorporated into the forecasts via the technical baseline update process, and therefore are approved by delegated authority rather than requiring formal Cabinet consideration.

The previous fiscal provisions only took account of items deemed “controllable”, and had a detailed set of rules to govern this definition.³ We anticipate having a wider constraint will simplify budgeting rules for Ministers, as all items before them that impact on the operating balance and debt should now impact upon spending intentions.

Concluding remarks

The Government’s superannuation pre-funding policy highlights the need to take account of long-term demographic and other pressures. These pressures, as they draw nearer, will increase the importance of setting and achieving long-term fiscal objectives.

The revisions outlined above will improve the Government’s fiscal management by shifting more attention to progress of the operating balance and debt tracks towards the Government’s long-term fiscal objectives.

This paper has three annexes, which set a backdrop to the changes to the approach, and expand upon the points above:

- Annex 1 - Evolution of the fiscal provisions, and issues prompting revisions.
- Annex 2 - Further detail on how Budget packages will manage wider impacts.
- Annex 3 - Risks and challenges.

³ This focus upon controllable items was to allow for planning certainty within the Budget process.

Annex 1

Evolution of the Fiscal Provisions, and issues prompting revisions

Evolution of the Fiscal Provisions

In the context of the 1990s, the Barnes and Leith paper notes two major legislative changes to New Zealand's fiscal management framework, being the:

- Public Finance Act 1989, which removed much of the automatic indexation from all departmental baselines (“fixed nominal baselines”);
- Fiscal Responsibility Act 1994 (FRA) which sought to:
 - bring a responsible long-term focus to annual budgeting;
 - increase the transparency of policy intentions and the fiscal impact of these;
 - allow people to assess the consistency of the Government's fiscal policy with its long-term objectives.

The FRA requires the Government to set long-term fiscal objectives that will maintain total Crown debt at prudent levels. These long-term objectives establish the context for developing the Government's shorter-term Budget strategy.

The FRA requires the Government to assess and demonstrate the consistency of its annual Budget with its long-term objectives (and general principles of responsible fiscal management). The principal means of doing this is by producing forecast operating balance and debt tracks over both the short- and longer-term (10-year) horizons with spending intentions factored into these tracks.

Pre-1997, the fiscal forecasts did not allow for increased spending in future Budgets, which resulted in unrealistic operating balance and debt profiles in the forecasts. As a result, it was difficult to assess the Government's short-term spending intentions and their consistency with its long-term objectives.

“Fiscal provisions” developed at a time when the government needed to establish its fiscal credibility

On the political side, the Barnes and Leith paper noted that the establishment of the \$5.9 billion fiscal cap was motivated by:

- concerns that a coalition government would usher in a period of instability; the government needed a way to demonstrate fiscal prudence;
- the risk that portfolio Ministers from different coalition parties would bid up spending in their sector, were the issue to become a coalition dispute. Some kind of overall cap needed to be agreed by both parties.

This fiscal cap evolved into a mechanism known as the “fiscal provisions”. It comprised a pre-determined fiscal limit across the parliamentary cycle ie three years, and a set of rules for “counting” against that limit.

The fiscal provisions focused upon decision-making. Therefore only discrete decisions which either changed existing policy, or introduced new policy “counted” against the limit. It did not consider any fiscal items that the Government could not control (without changing existing policy), and therefore excluded any:

- changes to output prices resulting from automatic indexation;
- formula-driven changes such as demographically driven funding, or unemployment increases;
- changes in liability estimates (eg provisions for doubtful debts).

The focus was upon policy impacts over the parliamentary term. The provision limit was set as the cumulative impact of new spending upon the operating balance over three years.

An important aspect of the Government’s overall fiscal policy was to allow “automatic fiscal stabilisers” to operate. The pre-set nature of the fiscal provisions was consistent with this policy, while retaining sufficient flexibility to respond to shocks where a more lasting impact on the fiscal position was anticipated (for example, adjustments made for the 1998 Asian crisis).

Fiscal provisions provided a tangible budgeting constraint

The development of the fiscal provisions provided a significant advance for New Zealand’s fiscal management in that they:

- provided a tangible and publicised constraint for Ministers to budget against;
- shifted decision-making from a one-year to a three-year focus;
- provided a more realistic spending profile in the fiscal forecasts and thereby gave a better indication of expected progress towards the Government’s long-term objectives;
- introduced greater certainty to fiscal planning.

While the Government has run operating surpluses every year since 1994, the introduction of fiscal provisions has assisted in ensuring spending was managed to enable surpluses. Gross Crown debt has fallen from 38% to 30% of GDP over the period of the fiscal provisions since their introduction in 1996. Over the same period, coalition governments have established their credentials around prudent fiscal management.

Issues Prompting Revisions

As with any fiscal management approach, over time a number of issues arose with using a fixed three-year nominal dollar limit from both an external communication perspective and an internal budget management perspective.

Economic and fiscal pressures constantly change

Preparing a Budget consistent with long-term objectives requires balancing a number of economic and fiscal pressures, which constantly change. Under the fiscal provisions approach, the Government at the start of the parliamentary term set operating and capital spending limits intended (and communicated) to be fixed for the three year term.

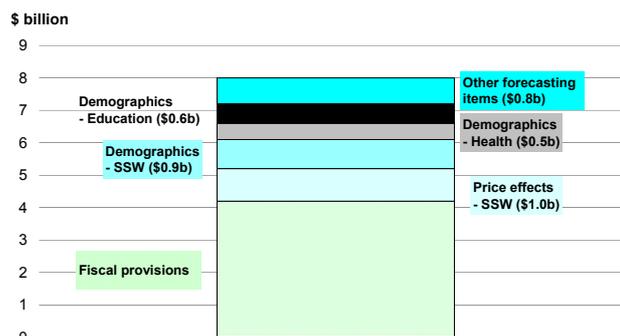
Experience showed that both the operating and capital provisions were actually changed most years. While the operating provision was generally altered at the margins⁴, there were more significant changes in the capital provision as new information on pressures came to light. These relative changes introduced a question around whether appropriate trade-offs were being made between capital and operating spending.

Provisions sometimes resulted on over-focus upon one aspect of fiscal policy

Given the provisions were perceived as “hard” spending limits that could provide a tangible measuring stick, there was heavy external attention upon these limits (particularly the operating limit) and the Government’s ability to keep within them.

However, the provisions captured only one aspect of fiscal policy: items deemed “controllable”. For example, the operating provision did not capture other impacts on the operating balance and debt such as demographically driven expense funding, or superannuation pre-funding. As such, the heavy focus upon these limits sometimes diverted attention away from the main focus: how the fiscal aggregates were tracking towards the Government’s long-term fiscal objectives. This problem was exacerbated by the limit being expressed as a cumulative three-year total (e.g. the “\$6 billion cap”) which resulted in stakeholders having difficulty linking back to the operating balance and debt tracks.

Figure 2 – Expense increase components 2001/02 to 2005/06



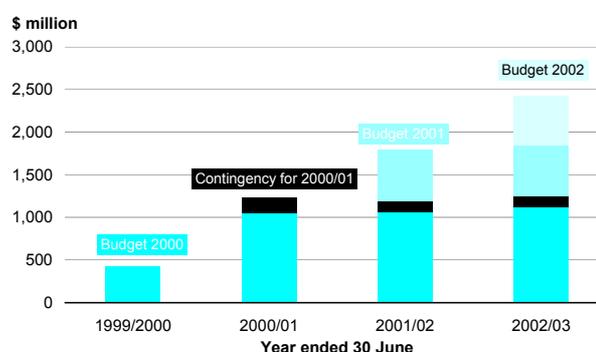
Source: The Treasury

Calculation and rules around managing the fiscal provisions limit

Calculating the limit in this way created some potential issues for the Government to manage:

- Spending increases in the third year “counted” only a third as much as spending impacts in the first year (see figure 3), despite having the same permanent impact looking forward.
- Any initiatives resulting in spending increases beyond the parliamentary term were not appropriately captured.

Figure 3 – The Government’s fiscal provisions



Source: The Treasury

The rules around which spending was “controllable” and therefore “counted” against spending limits were sometimes difficult to maintain in practice. There was also

⁴ More significant adjustments were made during the Asian crisis in 1998.

an (inevitable) element of gaming in the Budget process, where items which didn't "count" against the spending limit were sometimes considered "free" despite having just as much impact on the operating balance and debt as items that counted.

Room for improvement

While these issues were quite manageable in practice, it became clear that there was scope for improving the Government's fiscal management approach in order to:

- increase the focus upon overall fiscal policy (giving better effect to the spirit of the FRA);
- take better account of the changeable nature of influences upon the Budget process;
- introduce more direct trade-offs at a high level between capital, operating and NZS Fund commitments;
- have a budgeting constraint with a more simple set of rules around its allocation;
- take better account of the impact of budget spending beyond the parliamentary term.

At the same time, it was important that the fiscal management approach retain the strengths of the fiscal provisions.

An approach that manages more closely to the fiscal aggregates (i.e. the operating balance and debt tracks) is seen as the best way of addressing the identified issues.

Annex 2

Further detail on how Budget Packages will manage wider impacts

There is still a nominal spending amount, but it will manage a wider range of impacts

The nominal dollar amounts entered into the forecasts will form the new spending amount for capital and operating for the purposes of facilitating internal trade-offs during the Budget process, similar to the fiscal provisions. These are referred to as the “forecast new operating and capital spending amounts.”

As noted earlier, one criticism made of the old approach was a perception that “if it doesn’t count it is free.”

The new approach adopts a simpler and more encompassing amount for budgeting, whereby all issues and changes to baselines in front of Ministers that impact upon the operating balance and gross debt also impact upon either the available operating or capital spending amounts. The concept of “count/ does not count” is therefore eliminated from all decisions presented to Ministers. Having to take wider fiscal impacts into account during the Budget process will involve Ministers focusing more upon the bigger picture.

The new approach introduces a qualitative assessment at the end of the Budget. This will allow more of an opportunity to consider the aggregate of all decisions or potential decisions in light of the fiscal tracks with the latest available information. It also provides a more informed forum in which to make the more difficult (and inevitable) marginal decisions.

How these concepts are built into the fiscal management approach is outlined in more detail below.

Spending intentions not altered for some pre-specified volatilities

Under the proposed approach, everything that impacts against the fiscal aggregates now matters in a Budget management sense. However, spending intentions will not be altered for some pre-specified items (major volatilities expected to largely net out over the forecast period) arising during the Budget process. These items will be left until an overall assessment at the end of the process.

Tables 2 and 3 outline this distinction in more detail.

The previous fiscal provisions approach had rules to determine which items were “controllable” and therefore “counted” against the limit. Therefore separate recommendations had to be made in Cabinet papers in order to indicate to Ministers the “counting” impact of initiatives.

Under the revised fiscal management approach items impacting directly (see Tables 2 and 3) upon the new spending amount cover everything that goes to Ministers on a regular basis. Therefore there is no need for separate counting recommendations; the financial recommendations will only show the operating and debt impacts of items.

Table 2 – Managing the forecast new operating spending amount

| Impacts directly | High-level assessment |
|---|--|
| Items that impact directly on the forecast new operating spending amount throughout the budget process (and during the year i.e. regular updates to Ministers will take account of these items) | Pre-specified items that may be taken into account in the qualitative assessments (but generally will not impact on the forecast new operating spending amount) |
| <ul style="list-style-type: none"> • Policy decisions, including those over State-Owned Enterprises (SOEs), and Crown Entities. • Operating balance and debt impacts of the baseline updates. • Demographic changes (normally picked up in a baseline update). • Changes in existing policy forecasts (eg student loan provisioning). • Non-controllable (eg. legal claims). • Any other impact on the operating balance and debt not in the high-level assessment. | <ul style="list-style-type: none"> • Tax re-forecasts. • Changes in net finance costs (interest costs on debt and interest income on gains/losses on marketable securities and deposits (MSDs)). • Benefit re-forecasting changes (including indexation changes). • Re-forecasts of SOEs and Crown Entities retained surpluses. • Revaluations of assets and liabilities (excluding provisions). This includes MSDs. • Gains/losses on sale of assets. |

Table 3 – Managing the forecast new capital spending amount

| Consider items directly | High level assessment |
|--|--|
| Items that impact directly on the forecast new capital spending amount throughout the Budget process (and during the year i.e. regular updates to Ministers would take account of these items) | Pre-specified items that may be taken into account in the qualitative assessments (but generally will not impact on the forecast new capital spending amount) |
| <ul style="list-style-type: none"> • All non-depreciation funded capital decisions. • Equity injections into SOEs and Crown Entities, and other capital purchases made by SOE and Crown Entities resulting from a policy decision (e.g. changes in housing stocks). • Movements in advances, including Student loan receipts, payments and movements. • Any other impact on debt not in the high-level assessment. | <ul style="list-style-type: none"> • All debt impacts driven by the operating balance (already picked up by the operating framework – includes revaluations). • Shifts in MSDs and shareholdings associated with Reserve Bank activities (neutral from a total Crown debt perspective). • Changes in super pre-funding rates (volatile). • Changes in SOE and Crown Entity dividend flows (volatile). • Autonomous self financed SOE and Crown Entity capital decisions (only impact on total debt, not core Crown gross debt). • International capital subscriptions (significant and unpredictable). • Refinancing of existing Crown entity debt (neutral from a total Crown debt perspective). |

A wider spending amount will involve wider management, and wider information flows

In addition to the information Budget Ministers currently receive, there will be new items impacting directly upon the new spending amounts that the Minister of Finance previously did not have to take into account when considering the fiscal provisions. Examples include changes in doubtful debt provision levels, and demographic items. Information provided to Ministers will need to be changed to ensure they are aware of everything that impacts on the level of operating and capital new spending amounts available.

There are likely to be margin cases of items assumed to impact directly on new spending amounts that the Minister of Finance may not want to take into account when considering spending intentions, for example a change in the level of Courts debt provisioning. These sorts of issues will be picked up during the qualitative assessment phase at the end of the Budget process, where the Minister of Finance will make final

decisions on the overall level of new spending amounts in the context of the overall fiscal tracks (including what is happening on the investing side and cyclical considerations). While there is some flexibility, the Minister will need to weigh up the future incentives the decisions may create for other Ministers e.g. if the Minister of Finance looked through one-offs or some cyclical components other than those listed, this could create incentives for Ministers to seek one-off (unsustainable) funding or change re-forecasts.

Final qualitative assessment just a “road-check”

It's at this qualitative assessment phase where the Minister of Finance will also look at the pre-specified items set aside (see “high level assessment” list). The underlying rationale here is to “quarantine” the few major items in the forecasts that tend to fluctuate⁵ - and therefore should not automatically affect the new spending amount available for the annual Budget. The Minister of Finance will make a decision around whether to “look through” these items, or whether to adjust the new spending amount for some items (or components of them) for example reducing overall spending in light of an increase in forecast hospital deficits.

Bilateral Budget agreements between the Minister of Finance and portfolio Ministers will need to be qualified to reflect the potential for the new spending amount to change in this final assessment. However, it is important to note that this qualitative assessment stage at the end of the Budget process is expected to be a “road-check” only with a stated bias to no change to spending intentions. The key assessment is at the start of the Budget process, which allows Vote Ministers planning certainty against a stable constraint. Changes at the final assessment stage must therefore be minimised to ensure the credibility of the new spending amount set at the start of the process.

Externally in the Budget documentation, the Budget package will still be shown in detail, however spending increases for particular areas will also include other items not previously “counted”, such as demographic increases (these components could potentially be split out in the tables).

⁵ That is, largely net out over time. Some of the fluctuations also involve an automatic fiscal stabiliser component e.g. unemployment spending.

Annex 3

Risks and challenges

Setting and managing fiscal policy is a complex process. While the revisions to the New Zealand fiscal management approach outlined above should represent a significant improvement, any approach will have its weak points and potential for improvement. The extent to which these weak points are tested will depend in part upon political will. Risks and challenges (in no particular order) are outlined briefly below:

- A key focus of fiscal policy is upon the Government's structural fiscal position and progress towards objectives. This focus was present under the provisions approach, and is made more transparent in the revised fiscal management approach. Decisions around what spending intentions can be accommodated within the forecast operating balance and debt tracks will therefore need to weigh cyclical considerations. Some related points are:
 - it is important not to impart a mechanical link between spending intentions and the structural position. This is largely because the estimate of cycle is subject to considerable uncertainty, and it is often difficult to distinguish between the cyclical and longer-lasting impacts of changes in economic conditions;
 - the Government's overall fiscal policy and objectives are set at the start of the parliamentary term. A cautious approach will need to be taken with reassessments to ensure that overall fiscal policy is not unnecessarily tightened or loosened;
 - better information around the Government's structural fiscal position will need to be provided to facilitate both internal and external assessment.
- Managing to the operating balance and debt is limited by the coverage of these fiscal aggregates:
 - From a debt perspective, the focus is upon core Crown sovereign issued debt. This does not cover SOE and some Crown Entity debt as these institutions are considered autonomous from the Crown. In reality, however, they are not entirely separate. From time to time, Ministers make policy decisions that impact upon that sector and come at an economic cost (for example housing stock decisions, the TVNZ charter, and Kiwibank). And vice versa, some sector actions which do not have an immediate impact on core Crown debt, should still have an impact upon the Government's spending intentions (for example, running hospital deficits that may ultimately require funding).
 - Similar to the fiscal provisions, this fiscal management approach adjusts spending to take account of the economic cost of SOE and Crown Entity policy decisions, while recognising an arbitrary element in the approach around identifying policy vs non-policy, and the lack of impact on the fiscal aggregates.
 - There are other items that have an economic cost but do not impact upon the forecast fiscal aggregates, for example the Crown entering into guarantees,

or programmes with consequences beyond the fiscal forecast period (five years).

- Further consideration needs to be given to aligning information processes with decision-making. For example, the Budget Update economic forecasting round is currently designed to be as close as possible to publication release. It leaves little room to reconsider current-year spending intentions in light of this information.
- The fiscal management approach does not discriminate between cost pressure requirements and new initiatives. More thought needs to be given to ensuring appropriate trade-offs are made between accommodating capability needs and new initiatives in the Budget process. This will require improving processes for identifying and assessing capability requirements.
- Under the previous provisions approach, capital spending intentions changed more frequently than operating spending intentions, and there is a question around whether this will remain the case under the revised approach.

Capital spending will always be “lumpy” given the large one-off projects that come along, and frequent delays in capital projects.

At the margins, capital spending has previously been adjusted within the context of the fiscal objective as it is one-off in nature, and therefore does not have the ongoing impact that changes in operating spending generally have.

However, capital decisions will also involve an element of ongoing operating costs, including changes to:

- finance costs
- depreciation expense
- any operating costs associated with the asset (e.g. staffing new prisons).

Under the revised fiscal management approach, rather than using capital to soak up any available spending room within fiscal objectives, the question will turn to being clearer about what the relative fiscal impacts are between operating and capital spending proposals.