

Chair
CABINET

BUDGET 2010: INDICATIVE SHARES OF THE OPERATING ALLOWANCE

Proposal

1. This paper seeks approval of:
 - the amount of the Budget 2010 operating allowance that is to be made available for allocation to Votes; and
 - indicative allocations of this amount to some Votes.

Executive Summary

2. Cabinet invited Budget Ministers to report back on 19 October 2009 with an indicative sharing across relevant Votes of new operating funding for Budget 2010 and any grouping of Ministers and Votes for the remainder of the Budget process [Cab Min (09) 34/12 refers].
3. Although the operating allowance for Budget 2010 has been set at \$1.1 billion, only half of this amount is available for allocation to Votes. Once deductions for the ACC non-earners account shortfall, a 2010/11 between Budget contingency, funding for a “rolling maul” of initiatives to be announced both in Budget 2010 and throughout 2010/11, and funding for the operating impacts of capital expenditure decisions have been made, \$550 million remains available to be allocated to Votes. The final amount to be allocated to Votes will be set in December 2009 and will be informed by the latest economic and fiscal forecasts, detailed examination of Social Sector Votes, Ministers’ feedback and their progress in aligning their baselines with priorities.
4. A detailed examination by the respective Vote Minister and their departments, of the pressures and expenditure in each of the key areas of the social sector (Health, Education, Social Development and the Justice Votes) is required to assist in aligning baselines to Government priorities and, where appropriate, identify where additional resource should be directed. The reviews of these four areas are to be completed by 21 December 2009.
5. Budget Ministers propose that Vote Health be indicatively allocated \$300 million and Vote Education \$250 million as the maximum level of additional funding available. It is not proposed that any other Vote will be indicatively allocated additional funding in Budget 2010.
6. There have been substantial increases in baselines across Government over the last six years (see Annex A). This provides a significant opportunity for Vote Ministers to reprioritise away from activities which are inefficient, ineffective or inconsistent with where we want to make progress and so realise significant savings with which to manage pressures and achieve their priorities within their existing baselines.
7. Budget Ministers have decided to not establish groupings of Ministers and Votes specifically for Budget 2010.

8. The Minister of Finance will write to all Vote Ministers in the next few days providing more details to assist them for the remainder of the 2010 Budget process.

Background

9. The 2010 Budget process has the following broad features [Cab Min (09) 34/12 refers]:

- An initial strategic phase in which the Government collectively sets priorities and allocates shares of the operating allowance to relevant Votes.
- A separate process for Cabinet to consider options to reduce spending in a discrete number of specific areas, with these savings offsetting the impact of the \$1.1 billion operating allowance on total Government spending.
- Ministers and Chief Executives working together to align baselines with priorities and report back to Budget Ministers on how they propose to deliver the Government's priorities from within available funding.
- A multi-year ECC work programme to establish appropriate relativities between areas of expenditure and update baselines to reflect these.

10. The success of the 2010 Budget process is dependent on two key factors:

- Vote Ministers and departmental Chief Executives working together to advance Government priorities and manage cost pressures;
- Chief Executives, Vote Ministers, and in some instances Cabinet, being prepared to reduce or stop lower priority programmes / activities.

11. Cabinet invited Budget Ministers to report back on 19 October 2009 with an indicative sharing across relevant Votes of new operating funding for Budget 2010 and any grouping of Ministers and Votes for the remainder of the Budget process [Cab Min (09) 34/12 refers].

Amount of Operating Allowance Available for Allocation to Votes

12. Although the operating allowance for Budget 2010 has been set at \$1.1 billion, only half of this amount is available for allocation to Votes. The following amounts have currently been deducted from the total:

- \$128 million to cover the ACC non-earners account funding shortfall¹;
- \$200 million to establish a between budget contingency for 2010/11;

¹ The non-earners account is entirely demand-driven and funds ACC claimants who are not covered by employer, earners or other levies. This differs, for example, from DHB deficits which are affected by a mixture of demand-driven elements such as population and discretionary prioritisation decisions such as the mix and volume of goods and services purchased or provided by the DHB.

- \$122 million for a “rolling maul” of initiatives to be announced both in Budget 2010 and throughout 2010/11 for the Government’s key economic and social priorities; and
- \$100 million for the operating impacts of capital expenditure decisions.

13. This leaves \$550 million available to be allocated to Votes. The final amount to be allocated to Votes will be set in December 2009 and will be informed by the latest economic and fiscal forecasts, detailed examination of Social Sector Votes, Ministers’ feedback and their progress in aligning their baselines with priorities.

Process for Health, Education, Social Development and Justice Sector Votes

14. Looking across the major social sector Votes, Budget Ministers see real pressures in many areas, but are of the view that for Social Development and the Justice Sector² Votes these can be addressed from within their existing funding.

15. Given the scale of the pressures in Votes Health and Education, it is likely that some additional funding will be necessary for these Votes. Budget Ministers propose that Vote Health be indicatively allocated \$300 million and Vote Education \$250 million as the maximum level of the additional funding available.

16. Budget Ministers propose a detailed examination be undertaken by the respective Vote Minister and their departments, of the priorities, pressures and existing expenditure in each of Health, Education, Social Development and the Justice Votes to assist in aligning baselines to Government priorities and, where appropriate, identify where additional resource should be directed. As part of the detailed examination Budget Ministers are seeking a reconciliation of where increases to baselines the Vote has received since 2005 have been applied and what value has been obtained (see Annex A). Budget Ministers also expect Vote Ministers to review the cost and numbers of policy advisors in their departments. Full Time Equivalent employees in the public service increased by 10,351 between 2003 and 2008. It is reasonable to assume that a proportion of these are policy advisors. The question to be answered is whether, in the current tight fiscal environment, the same numbers of policy advisors are needed. The main concern for Vote Ministers should be whether the policy advice they receive from their departments meets their needs in terms of quantity, quality and subject matter.

17. I will discuss the terms of reference for the reviews with affected Ministers before bringing a paper to Cabinet proposing further details on the process and conduct of the reviews.

18. The reviews of these four areas are to be completed by 21 December 2009, unless the Vote Minister determines that additional funding over and above the indicative allocation is required, in which case the reviews are to be completed by 30 November 2009. I am open to requests from Ministers for the Treasury to provide supplementary assistance to Ministers if wanted.

Process for all other Votes

19. It is not proposed that any Vote, other than Education and Health, will be indicatively allocated additional operating funding in Budget 2010.

20. There have been substantial increases in baselines across the board over the last five years (see Annex A). This provides a significant opportunity for Vote Ministers to reprioritise away from

² Justice Sector Votes: Attorney General, Courts, Corrections, Justice, Police, Serious Fraud.

activities that are inefficient, ineffective or inconsistent with where we want to make progress and so realise significant savings with which to manage pressures and achieve priorities within Votes' existing baselines. As in the detailed examinations of major social sector Votes, Budget Ministers expect departments to review the cost and numbers of policy advisors.

21. Each Vote Minister will be invited to show how they intend to use their baselines to advance their priorities in March 2010. This will give Cabinet an opportunity to test those priorities, the level of ambition, and to support the changes required in each Vote.

22. I expect that Vote Ministers will use their baselines to meet their highest priorities. Where Ministers have lower priority activities which they do not consider they will be able to fit within their baselines, but they still think are of value, they are invited to submit to me a request for additional resources accompanied by a detailed examination of their Vote, consistent with that proposed for Health, Education, Social Development and Justice Votes, by 30 November. This will allow Cabinet to consider these activities and finalise any changes to baselines in early-mid December.

23. In the time available, this exercise will not be comprehensive. Budget Ministers propose an ongoing programme of review by the Cabinet Expenditure Control Committee (beginning after Budget 2010) to consider different sectors in detail and determine whether the allocation of resources matches our priorities.

Savings

24. In general terms any savings identified by Vote Ministers can be retained within the Vote to manage pressures and achieve Ministers' priorities. Refinements to this general rule are:

- If a proposed saving will be generated by reducing or stopping a major programme or activity it is to be brought to Cabinet for approval. In these instances Cabinet will determine the proportion of the saving to be retained within the Vote and that to be returned to the centre.
- Where a Vote Minister has actively chosen to reduce or stop a programme or activity, or where the saving has been generated by efficiency improvements, the funding can be retained within the Vote. However "windfall" savings (such as underspends resulting from reduced volume or demand), where active management decisions have not been taken, are to be returned to the centre.

25. I may also bring proposals to Cabinet to reduce spending in specific areas, with the resulting savings to be used to partially offset the impact of the \$1.1 billion operating allowance on total Government spending.

Capital

26. I intend to run a similar process for capital as in Budget 2009. This will involve considering business cases for investment against our stated aim of improving infrastructure to drive productivity growth. At this early stage, I am already aware of a number of large commitments which will be difficult to fit within the capital allowance. This will put a premium on finding effective ways to manage agency balance sheets and deliver services. Budget Ministers will be considering these matters further.

Groupings of Ministers and Votes for the Remainder of the Budget Process

27. Budget Ministers have decided to not establish groupings of Ministers and Votes specifically for Budget 2010.

Next Steps

28. I intend writing to all Ministers in the next few providing more details to assist them for the remainder of the 2010 Budget process, and will shortly bring a paper to Cabinet proposing further details on the process and conduct of the detailed examination of the major social sector Votes.

Consultation

29. This paper reflects what was agreed by Budget Ministers at their meeting on 14 October 2009. DPMC were consulted in the preparation of this paper.

Recommendations

30. I recommend that Cabinet:

1. **note** that on 21 September 2009, Cabinet:
 - 1.1 **invited** the Prime Minister, Minister of Finance and Associate Ministers of Finance as Budget Ministers to report back to Cabinet on 19 October 2009 with:
 - 1.1.1 an indicative sharing across relevant Votes of new operating funding for Budget 2010; and
 - 1.1.2 any grouping of Ministers and Votes for the remainder of the budget process;

[CAB Min (09) 34/12]
2. **note** that given the tighter fiscal conditions success of the 2010 Budget process is dependent on two key factors:
 - 2.1 Ministers and departmental Chief Executives working together to advance Government priorities and manage cost pressures;
 - 2.2 Chief Executives, Ministers, and in some instances Cabinet, being prepared to reduce or stop lower priority programmes / activities;
3. **note** that the following amounts have been provisionally deducted from the \$1.1 billion operating allowance for Budget 2010:
 - 3.1 \$128 million to cover the ACC non-earners account funding shortfall;
 - 3.2 \$200 million to establish a between budget contingency for 2010/11;
 - 3.3 \$122 million for a “rolling maul” of initiatives to be announced both in Budget 2010 and throughout 2010/11; and
 - 3.4 \$100 million for the operating impacts of capital expenditure;

4. **agree** that \$300 million be indicatively allocated to Vote Health and \$250 million be indicatively allocated to Vote Education;
5. **agree** that detailed examinations of the baselines of Votes Health, Education, Social Development and the Justice Sector Votes (Attorney General, Courts, Corrections, Justice, Police, Serious Fraud) be undertaken by the respective Vote Minister and their departments, reporting to Budget Ministers by 21 December 2009, to assist in aligning baselines to Government priorities and, where appropriate, identify where additional resource should be directed;
6. **agree** that if through their detailed examinations social sector Vote Ministers determine that additional funding over and above the indicative allocation is required, the reviews are to be completed by 30 November 2009 and are to include a reconciliation of where increases to baselines the Vote has received since 2005 have been applied and what value has been obtained;
7. **agree** that no other Vote be allocated additional funding at this time;
8. **invite** the Minister of Finance to write to all Vote Ministers in the next few days providing more details to assist them for the remainder of the 2010 Budget process;
9. **invite** the Minister of Finance to report back to Cabinet on 2 November 2009 proposing further details on the process and conduct of the detailed examination of the major social sector Votes;
10. **invite** Vote Ministers who consider that they are unable to deliver priorities and cater for cost pressures from within their existing baseline and indicative share, to submit to the Minister of Finance, a request for additional resources, accompanied by a detailed examination of their Vote, consistent with that proposed for Health, Education, Social Development and Justice Sector Votes, by 30 November 2009;
11. **note** that if additional funding is provided to Votes other than that indicatively allocated, this will reduce the increase available for Votes Health and Education, and/or require a reduction in funding proposed for other activities, for example funding for a “rolling maul” of initiatives;
12. **agree** that the final allocation of additional funding to Votes will be set in December 2009 and will be informed by the latest economic and fiscal forecasts, the detailed examination of social sector Votes, Ministers’ feedback and their progress in aligning their baselines with priorities;
13. **agree** that savings can be retained within Votes, except for “windfall” savings which are to be returned to the centre;
14. **agree** that proposals to reduce or stop major programmes or activities are to be brought to Cabinet for approval, and that Cabinet will determine the proportion of the resulting savings to be retained within the Vote and that to be returned to the centre;
15. **note** that the capital process for Budget 2010 will be similar to that employed in Budget 2009;
16. **note** that Budget Ministers have decided to not establish groupings of Ministers and Votes specifically for Budget 2010.

Hon Bill English
Minister of Finance

October 2009

Annex A: Baseline Increases 2005-2009 (\$000)

What the table shows

This table shows nominal growth in baselines by Vote since 2004/05 financial year. Inflation was about 12.4% over the period so the group of Votes at the bottom of the table have had flat or negative growth. The rest of the Votes have grown faster than inflation.

Where the numbers come from

The numbers are budget data that is published on the Treasury website from the Crown Financial Information System. The percentage change is a straight calculation from the first year.

What the numbers include

The figures used are departmental and non-departmental output and other expense appropriations. This includes money spent by departments or allocated through departments mostly for the purchase of goods and services. Other expenses are often output-like expenses so they have also been included. Other expenses for Votes Social Development, Finance and Revenue have been excluded because this spending is mostly items like loan write-offs and the purchase of KiwiRail, which is not a fair reflection of Vote growth. Other Votes will also have items like these in their baselines that distort the picture somewhat but these have not been removed as they do not have such a disproportionate effect on the growth of the Vote.

Vote	2005 Total	2006 Total	2007 Total	2008 Total	2009 Total	2010 Total	% change
Racing	\$188	\$180	\$204	\$579	\$4,206	\$4,362	2220%
Treaty Negotiations	\$31,937	\$47,803	\$67,020	\$252,282	\$98,736	\$231,028	623%
Communications	\$16,121	\$17,269	\$25,002	\$29,381	\$26,696	\$79,429	393%
Environment	\$49,994	\$52,581	\$54,904	\$57,815	\$86,512	\$168,197	236%
Housing	\$40,226	\$80,664	\$95,438	\$96,507	\$116,669	\$134,408	234%
Veterans' Affairs - Defence Force	\$4,474	\$4,227	\$14,739	\$8,477	\$11,155	\$13,250	196%
State Services	\$89,326	\$132,442	\$160,785	\$178,536	\$207,417	\$254,673	185%
Energy	\$117,492	\$133,494	\$125,447	\$198,772	\$211,316	\$248,012	111%
Corrections	\$537,694	\$653,874	\$765,941	\$924,049	\$970,530	\$1,065,476	98%
Transport	\$1,050,106	\$1,266,868	\$1,421,336	\$1,470,174	\$1,769,439	\$2,034,806	94%
Foreign Affairs and Trade	\$225,453	\$249,975	\$299,710	\$319,394	\$371,023	\$431,724	91%
Economic Development	\$202,760	\$273,814	\$238,924	\$477,795	\$322,783	\$380,289	88%
ACC	\$570,124	\$599,847	\$673,604	\$725,067	\$955,589	\$996,092	75%
Sport and Recreation	\$38,294	\$45,828	\$55,349	\$63,752	\$75,387	\$66,893	75%
Audit	\$42,709	\$51,700	\$67,345	\$67,861	\$72,370	\$72,641	70%
Agriculture and Forestry	\$137,705	\$111,933	\$112,500	\$144,847	\$167,054	\$231,832	68%
Commerce	\$69,854	\$74,660	\$79,340	\$90,374	\$103,394	\$117,143	68%
Ombudsmen	\$4,925	\$5,511	\$5,802	\$6,875	\$7,993	\$8,018	63%
Courts	\$432,309	\$485,900	\$547,614	\$691,305	\$673,918	\$701,883	62%
Justice	\$171,146	\$203,312	\$200,948	\$232,144	\$274,443	\$276,630	62%
Serious Fraud	\$4,607	\$4,795	\$4,880	\$5,057	\$5,770	\$7,369	60%
Official Development Assistance	\$312,648	\$347,908	\$356,345	\$392,308	\$511,064	\$500,000	60%
National Library	\$47,293	\$50,941	\$52,235	\$55,556	\$69,060	\$72,400	53%
Internal Affairs	\$103,211	\$122,919	\$135,063	\$127,381	\$130,561	\$157,871	53%
Community and Voluntary Sector	\$29,641	\$38,418	\$41,542	\$48,473	\$58,001	\$44,989	52%
Office of the Clerk	\$12,127	\$13,196	\$14,455	\$17,172	\$20,287	\$18,115	49%
Immigration	\$134,149	\$167,266	\$159,233	\$172,676	\$200,985	\$198,701	48%
Climate Change	\$337,435	\$142,098	\$34,621	\$50,055	\$47,081	\$499,244	48%

Vote	2005 Total	2006 Total	2007 Total	2008 Total	2009 Total	2010 Total	% change
Police	\$941,646	\$1,018,642	\$1,131,244	\$1,246,453	\$1,376,617	\$1,391,639	48%
Revenue	\$429,359	\$479,654	\$532,204	\$612,085	\$661,810	\$626,998	46%
Statistics	\$75,369	\$122,777	\$93,612	\$89,915	\$99,096	\$107,665	43%
Parliamentary Counsel	\$14,586	\$13,787	\$15,151	\$18,108	\$19,012	\$20,666	42%
Fisheries	\$79,015	\$90,113	\$94,356	\$159,366	\$139,817	\$111,618	41%
Defence Force	\$1,522,510	\$1,657,820	\$1,816,363	\$2,102,637	\$2,102,637	\$2,149,823	41%
Parliamentary Service	\$88,889	\$93,873	\$102,188	\$112,311	\$126,167	\$124,488	40%
National Archives	\$16,400	\$16,519	\$19,482	\$21,328	\$24,054	\$22,835	39%
Education	\$7,716,206	\$8,343,241	\$8,843,148	\$9,495,406	\$10,355,883	\$10,723,418	39%
Attorney-General	\$47,081	\$50,459	\$56,249	\$58,561	\$65,814	\$64,749	38%
Research, Science and Technology	\$541,479	\$617,783	\$640,599	\$621,273	\$682,506	\$743,333	37%
Health	\$9,366,348	\$9,099,603	\$9,857,598	\$10,772,336	\$11,647,049	\$12,623,156	35%
Labour	\$66,420	\$76,024	\$79,971	\$84,355	\$89,179	\$89,442	35%
Conservation	\$262,442	\$283,777	\$301,414	\$326,639	\$372,035	\$351,976	34%
Ministerial Services	\$45,201	\$48,205	\$58,135	\$58,091	\$62,546	\$60,363	34%
Customs	\$95,706	\$105,623	\$110,463	\$118,842	\$125,489	\$126,377	32%
Arts, Culture and Heritage	\$215,980	\$219,702	\$239,137	\$261,640	\$280,338	\$284,618	32%
Food Safety	\$73,763	\$76,580	\$81,079	\$91,195	\$99,389	\$96,871	31%
Lands	\$108,288	\$118,781	\$127,034	\$131,532	\$149,563	\$140,653	30%
Social Development	\$1,144,937	\$1,255,523	\$1,302,499	\$1,363,119	\$1,451,834	\$1,461,173	28%
Tourism	\$77,528	\$90,523	\$89,459	\$82,789	\$84,321	\$96,612	25%
Parliamentary Commissioner for the Environment	\$2,220	\$2,477	\$2,804	\$2,295	\$2,741	\$2,741	23%
Defence	\$8,529	\$8,450	\$9,006	\$9,476	\$11,342	\$10,511	23%
Women's Affairs	\$3,846	\$4,099	\$4,130	\$4,595	\$4,677	\$4,731	23%
Biosecurity	\$151,103	\$174,444	\$175,565	\$181,088	\$183,891	\$185,630	23%
State-Owned Enterprises	\$2,260	\$2,480	\$2,582	\$2,639	\$2,568	\$2,775	23%
Local Government	\$20,656	\$13,471	\$14,027	\$27,215	\$17,885	\$25,079	21%
Maori Affairs	\$143,797	\$154,530	\$149,245	\$168,248	\$200,300	\$173,919	21%
Senior Citizens	\$897	\$955	\$988	\$911	\$1,035	\$1,035	15%
Education Review Office	\$25,244	\$28,381	\$28,739	\$28,560	\$29,537	\$28,852	14%
Finance	\$58,357	\$54,554	\$56,333	\$55,315	\$59,520	\$65,496	12%
Pacific Island Affairs	\$6,697	\$6,916	\$7,200	\$8,412	\$7,871	\$7,420	11%
Prime Minister and Cabinet	\$15,955	\$15,381	\$16,193	\$17,184	\$16,919	\$17,571	10%
Youth Development	\$13,743	\$13,539	\$14,144	\$14,111	\$14,835	\$14,636	6%
Consumer Affairs	\$5,946	\$5,853	\$5,735	\$6,048	\$5,988	\$5,962	0%
Crown Research Institutes	\$1,804	\$970	\$1,162	\$2,409	\$1,838	\$1,074	-40%
Employment	\$27,283	\$13,040	\$13,819	\$15,090	\$18,295	\$15,271	-44%
Emergency Management	\$24,491	\$19,860	\$19,329	\$13,714	\$14,608	\$12,038	-51%
Veterans' Affairs - Social Development	\$3,849	\$3,548	\$3,683	\$4,123	\$914	\$450	-88%
Grand Total	\$28,259,778	\$29,781,380	\$31,926,395	\$35,294,078	\$38,179,359	\$41,009,139	45%