

Hon Dr Wayne Mapp
Minister of Defence
Minister of Research, Science and Technology
Parliament Buildings
WELLINGTON

Dear Wayne,

As outlined in the *Budget 2010: Indicative Share of the Operating Allowance* Cabinet paper discussed on 2 November, I committed to write to you providing further details to assist you for the remainder of the 2010 Budget process.

You are aware that we continue to face a tight economic and fiscal environment, where the need for restraint is still necessary. Departments have received significant baseline increases over the last few years, so Vote Ministers are encouraged to look at current baselines as the first source of funding for any new priorities, or should existing programmes require increased funding.

As agreed by Cabinet, you are indicatively not receiving any *additional* operating allocation in Budget 2010 over and above existing baseline funding for:

- Vote Defence
- Vote Defence Force
- Vote Research, Science and Technology

I should mention that the indicative allocations outlined in this letter could potentially differ from those that we finally agree for Budget 2010. There are a number of factors that may influence the final allocations, such as:

- The detailed examination of various social sector Votes' baselines. Currently, as agreed by Cabinet on 2 November, the requirement to complete a detailed examination of the baselines only applies to Votes Education, Health, Social Development and Justice sector Votes¹. The objective of the detailed examination of these Votes is to ensure that these Votes can deliver priorities within their current baselines and any indicative allocation;
- The fact that some Votes may not be able to deliver on their priorities within existing baselines and may write to me seeking increased funding after carrying out a detailed examination of their Vote's baselines, in line with that expected of the social sector Votes;

¹ Justice Votes: Attorney-General, Courts, Corrections, Justice, Police and Serious Fraud.

- Should a Vote Minister be successful in their request for additional funding, this funding will necessarily result in either existing indicative allocations being reduced, or the reduction of centrally held provisions, e.g. the between Budget contingency;
- Ministers' feedback and their progress in aligning their baselines with priorities; and
- *[Deleted in order to maintain the effective conduct of public affairs through the free and frank expressions of opinions].*

Detailed Examination of Social Sector Votes

Cabinet agreed to a *detailed examination* of the social sector Votes to determine how well these Votes are placed to meet the challenges and expectations in their areas. These reviews are to be completed by 21 December 2009, unless the respective Vote Minister determines that additional funding will be required. In this case, the respective review needs to be completed by 30 November 2009.. The detailed examinations are to be conducted by the Vote Minister and department concerned, but Vote Ministers may ask the Minister of Finance for supplementary assistance from the Treasury.

The detailed examination of these Votes should include a reconciliation of where baseline increases have been applied in each Vote and what value has been obtained. Treasury has developed a terms of reference of the essential information that Vote Ministers must include in the detailed examination of baselines. The terms of reference are attached to this letter.

Process for All Other Votes

The indicative funding allocations agreed by Cabinet mean that the majority of Ministers will not receive any *new* marginal funding increases through this process. Given the substantive baseline increases over the last few years for the majority of Votes, Ministers will be expected to reprioritise from existing baselines to find savings that can be used to manage pressures and achieve their priorities from existing funding.

Vote Ministers should use their baselines to meet their highest priorities. However, there may be instances where some low priority, but still valuable programmes cannot be funded from baselines. In these cases, Vote Ministers are invited to submit to me a request for additional funding, accompanied by a detailed examination of their Vote consistent with those requested of the social sector Votes, by 30 November. This will allow Cabinet to consider these proposals and agree any changes to baselines prior to Christmas.

Baseline Alignment Proposal

All Vote Ministers, including those who will be completing a detailed examination of their Votes at the end of 2009, must submit a Baseline Alignment Proposal by 8 March 2010. This proposal shows how the baseline will be used to meet priorities, detailing any changes that need to be made. These submissions will be considered by Budget Ministers to prepare the final Budget Cabinet paper. More information on how these proposals should be put together will appear in the Budget guidance released by Treasury. The template will be loaded on CFISnet and will be attached to the guidance.

Increases in Policy Capability

One area of spending where I would encourage you to focus on is policy advice. Full Time Equivalent employees in the public service have increased by 10,351 between 2003 and 2008. It is reasonable to assume that a proportion of these are policy advisors.

The Ministry of Defence has had a 8% increases in staff numbers between 2003 and 2008, whereas the Ministry of Research, Science & Technology had a 19% increase in the same period.

Individual departments have information on their increases in both numbers of policy advisors and analysts and the cost of policy advice. Vote Ministers may want to ask their departments about growth in the number and cost of policy advisors.

Questions that you may want to ask are:

- How much does the department spend on policy advice?
 - What is the trend information on this spending since 2003?
 - What percentage is this of the total *departmental* spend? (i.e. excluding non-departmental appropriations)
 - Has the percentage changed since 2003?
- How many FTEs are dedicated to policy advice? How has this number changed since 2003?
- Has there been a commensurate increase in the quantity/quality of policy advice over this time and do you need to continue purchasing the same quality/quantity of policy advice in the future?

Savings

The general rule for savings is that they can be retained in a Vote to manage pressures and achieve Ministerial priorities. However, there are two refinements to this rule:

- If a saving is generated by reducing or stopping a major programme or activity, it requires Cabinet approval. Cabinet will determine the proportion of the saving to be retained within the Vote and that to be returned to the centre.
- Where a saving has been generated by efficiency improvements or where a Vote Minister has actively decided to reduce or stop a programme or activity, the saving can be retained in the Vote. Where active management decisions to stop programmes or activities have not been taken, such as underspends from reduced volume or demand, these savings are to be returned to the centre.

Capital

A similar process will be run for capital as in Budget 2009. This will involve Ministers submitting business cases for investment against our stated aim of using improvements in national infrastructure to drive productivity growth. At this early stage, there are a number of large commitments which will be difficult to fit within the capital allowance of \$1.45 billion. This will put a premium on finding innovative ways to manage our balance sheets and deliver services.

Guidance

Treasury will release the Budget 2010 guidance for departments, which outlines in detail how the process will work and the expectations on departments. This guide will be available both on the CFISnet and the Treasury website.

Yours sincerely

Hon Bill English
Minister of Finance

Cc:

Mr John McKinnon – Chief Executive and Secretary of Defence

Dr Helen Anderson – Chief Executive Ministry of Research, Science and Technology

Lt Gen Jerry Matepare – Chief of Defence Force

Terms of Reference for Detailed Examination of any Other Vote for which Additional Funding is being Sought

The Vote Minister will need to:

- Detail how all increases to the Vote since 2005 have been applied and what value has been obtained from that additional expenditure;
- Demonstrate that they have reviewed all areas of expenditure within the Vote and identified any that are not consistent with this government's priorities;
- Demonstrate that they are unable to handle the pressures facing the Vote from within the funding available to the Vote;
- Demonstrate that they have reviewed the number of policy advisors in, and cost of policy advice provided by, their department(s) and whether some reduction in that number or cost can be made; and

Demonstrate that any fiscal savings expected as a result of the department implementing its performance improvement actions have been taken into account.