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Northern Ireland Draft Budget 2011-2015

PwC response to consultation

February 2011

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Contents

Executive Summary

The Budget 2011-15 represents the most challenging spending review to face government in Northern Ireland for over a generation.

It is therefore encouraging that the Executive reached a consensus in December in terms of putting the Budget out to consultation. It is also commendable that the aspiration is for a four year Budget as that should offer greater longer term certainty and confidence to the Northern Ireland private and voluntary sectors.

In that regard, Ministers and their officials are to be congratulated.

However, while the degree of political consensus already achieved is welcome, the way this process has been managed is unhelpful.

The draft Budget was delivered to the Assembly by the Finance Minister on 15 December 2010, but it was made clear that consultation would be managed not by DFP, but by individual Departments. The Minister said: *"…This process will not be led by DFP but by individual Departments who will now publish their savings plans and spending proposals. This will allow interested parties to provide the views that will shape the final Budget position that I will bring before this Assembly in February."*

This implied that Departments could *"… publish their savings plans and spending proposals"* in a manner of their own choosing. We believed at the time that this could result in a lack of transparency and an inability to compare Departments in a like-for-like manner. We believed this would be true especially in terms of relating individual Departmental spending and savings proposals, both to each other and to the draft Budget statement of 15 December. This has proved to be the case.

Furthermore, even with an extension to 16 February, the delay in the publication of Departmental plans left consultees with little time to rigorously scrutinise these plans. It also means that the Executive has almost no time to consider the responses. The publication by DHSSPS of its McKinsey Report (we believe on 10 February), containing estimates not in the DHSSPS plan, was particularly challenging as it was (and remains at the time of writing) difficult to determine if the two documents collectively comprise the Health Department's Budget plan.

In responding to consultation(s), we have compiled a single document, which is being provided to all Departments as the formal PwC response to consultation. In that regard, this Executive Summary includes general comments applicable to all Departments, while Departmental comments are contained (with some exceptions) in the section-specific Departmental plans.

In overall terms, we conclude that the draft Budget (as defined by the published plans of the 12 Departments) does not balance. A calculation based on a standard formula (Departmental baseline, plus inescapables, minus resources, plus savings) suggests that, in the absence of information not currently available to consultees, there is a cumulative shortfall that could exceed £2.0bn by 2014-15.

We note that to a large extent Departments have not exercised opportunities to raise revenues and/or effect savings where opportunities exist to market-test a wide range of services currently provided within the public sector. We would have expected Departmental proposals to externalise service delivery, to dispose of publicly-held assets and operations and to consider more radical mechanisms for finance-raising and asset-leveraging to fund essential infrastructure investment.

We have also identified a number of areas where cross-departmental activities may conflict. For example, an examination of the plans for the Desertcreat College suggests that, while sufficient capital may be available from DOJ to complete the campus, DHSSPS has insufficient resources to fund its proposed share of revenues costs. And we note the further deferral of domestic water charging will have the effect of subsidising DRD to the extent of around at least £800m over the period of the draft Budget.

We note that the consultation process does not relate to the current Programme for Government (PFG) nor does it set out the high-level aspirations for any new PFG. Consequently, we must conclude that the 2011-15 Budget will be agreed ahead of any consensus on targets and outcomes for public services or economic rebalancing over the next four years. This is a reversal of what should be the sequence of decision making (agree strategy, define outcomes, set key performance indicators [KPIs] and finally, assign appropriate budget lines) and represents one of the greatest concerns and potential weaknesses in the entire draft Budget process.

We are therefore deeply concerned at the almost complete absence of economic and social targets and outcomes underpinning the draft Budget and departmental plans for the period to 2014-15.

It is both striking and depressing that the only periods since 1921 when the Northern Ireland economy has managed any substantial move towards convergence with the rest of the UK have been ones where there was a very rapid increase in public spending.

It is therefore worth remembering that, based on the 22 June UK Budget, public spending is forecast to fall in real terms for each of the next four years. However, public spending fell in real terms in only five years in the four decades between 1970 and 2010 and, over that period, public spending declined for two consecutive years on only one occasion (1996/97-1997/98).

Furthermore, despite having created around 124,000 new jobs in the decade to 2008 - a remarkable performance and on par with US rates of job creation - Northern Ireland's key productivity and performance metrics were worse at the end of the decade than they were at the beginning. Moreover, almost a third of those jobs had been lost in the 24 months to mid-2010.

Given this correlation between high levels of public spending and economic activity, the cumulative £4bn fall in public spending over the period of the draft Budget does not auger well for the economy. In addition, the hitherto underestimated reliance on economic activity in the Republic of Ireland will further impact on Northern Ireland's economic performance until RoI experiences significant recovery.[1]

We are therefore facing an unprecedented public sector spending round. Also, one where the OBR UK growth estimates that informed the 22 June Budget have since been marked down. And one where Northern Ireland remains the single UK region not to demonstrate any real measure of recovery. Consequently, the Executive should not underestimate the potential for public spending to become even tighter over the current CSR period.

We would temper our criticism of the draft Budget and Departmental plans by commenting that the lack of holistic, cross-departmental cohesion in the plans is, at least in part, understandable given the multi party, 'forced coalition' model of government. A tight budget is difficult enough to deliver across Departments in a 'traditional' model of democratic government and this is significantly exacerbated by the political situation in Northern Ireland.

Nevertheless, the draft Budget, including the Departmental plans, comprises a patchwork of unaligned spending proposals. It is unrelated to a Programme for Government or to cross-departmental economic or social objectives. In fact, based on the information available, it may not be deliverable in its current form.

[1] For example, 10% of manufacturing output is sold to the Republic of Ireland.

Background: the emergency Budget and the Comprehensive Spending Review

In the aftermath of the 2010 general election and the formation of the Conservative/Liberal Democrat coalition, there was widespread public debate about the necessity for, and timing and level of, fiscal consolidation in the UK.

The priority of the coalition was to reduce the budget deficit which was £155 billion in 2009/10 and the emergency Budget of 22 June set out plans to cut the deficit, with the Chancellor announcing £17 billion of spending cuts by 2014/15, in addition to the reductions in spending which had been planned by the previous Labour government.

The outcome of the 22 June Budget was that public spending was forecast to fall in real terms for each of the next four years. To put this in context, public spending fell in real terms in only five years in the four decades between 1970 and 2010 and, over that period, public spending declined for two consecutive years on only one occasion (1996/97-1997/98).

Despite the cuts announced in the emergency Budget, public spending, as a share of the economy in 2015/16 will still be higher than it was in 2003/04.

The underlying objective of the 22 June Budget was to cut the structural budget deficit to zero over the following five years. This was to be achieved through a combination of taxation and public spending restraint, intended to deliver an additional fiscal consolidation of around £40 billion by 2014/15, over and above the measures included in the (pre-election) Budget of March 2010. The consolidation was heavily weighted towards spending cuts rather than tax rises – with a ratio close to the 4:1 promised by the Conservatives prior to the election.

The Budget statement also included a restatement of the commitment contained in the coalition Programme for Government to publish by autumn 2010 a *"...paper examining potential mechanisms for changing Corporation Tax*[2] *in Northern Ireland."*

The implications of the 22 June Budget statement were in addition to the £6.2 billion of public spending reductions announced for 2010/11 by the coalition the previous month. In May 2010 the Northern Ireland Executive's share of these reductions amounted to £127.9 million.[3] And while this was mostly managed through the in-year monitoring process, there was an option for the Executive to carry forward the reductions into 2011/12. On 29 September 2010 DFP officials gave evidence to the Finance and Personnel Committee where an official stated: "*As we leave September monitoring, the position is that the over commitment is cleared on the capital side, and we still have a balance of just under £17 million of an over commitment on the current side.*"[4]

2 The Coalition. May 2010, *Our Programme for Government*, London.

3 DFP Press release 25 May 2010, available online at: http://www.northernireland.gov.uk/news/news-dfp/news-dfp-25052010-wilson-cut-in-public-spending.htm

4 http://www.niassembly.gov.uk/record/committees2010/FinancePersonnel/100929_OutcomeofSpendingRound.htm

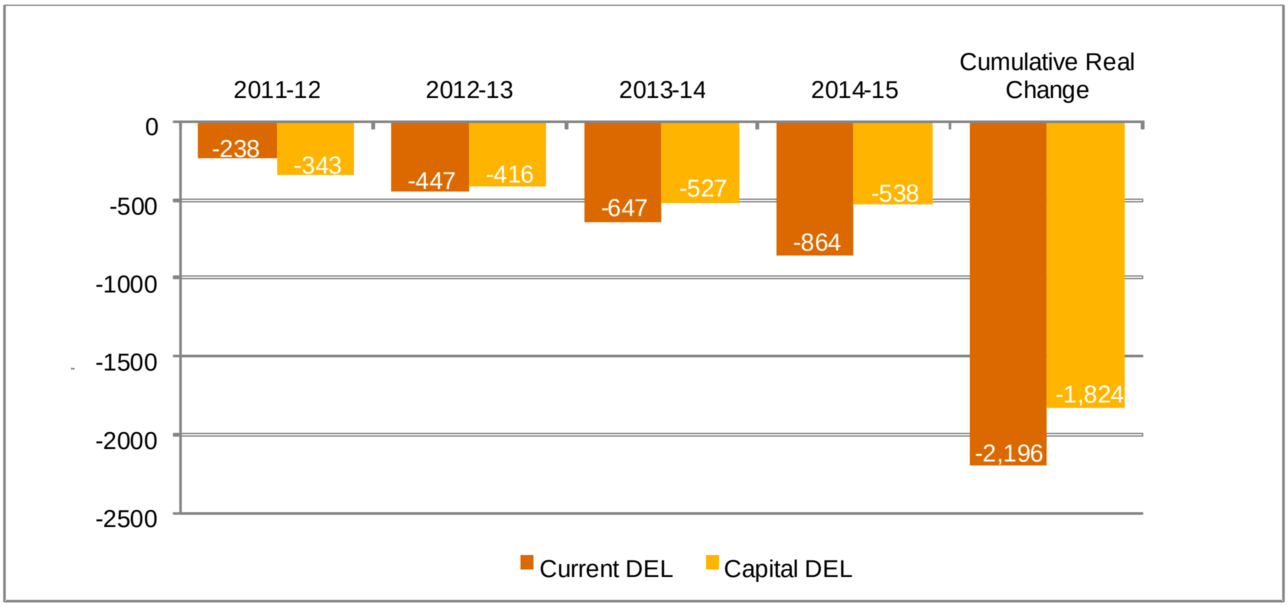
That left the Executive to find an additional £17 million in the remaining monitoring rounds of 2010/11 (December and February) if there was to be no carrying over of over commitment into 2011/12. Assuming the Executive was to find the £17m it would start the next fiscal year with a clean slate.

On 20 October 2010, the Comprehensive Spending Review (CSR) set out UK departmental spending limits for the four years until 2014-15 whereby public spending as a percentage of GDP will return to the level seen in 2006-07, and in real terms it will return to around the level seen in 2008-09. The CSR increased the capital envelope by £2.3 billion a year by 2014-15 relative to the Budget plan. For the first time, the CSR covered Annually Managed Expenditure (AME) in addition to Departmental Expenditure Limits (DELs) for each government department and for the devolved administrations.

The CSR provided the immediate context for the Northern Ireland draft Budget 2011-15, and the settlement for the Northern Ireland Executive shown in Figure 1. Comparing 2014-15 to 2010-11, there was an 8% real terms decrease in the total monies allocated to Departmental Expenditure Limit (DEL) current expenditure[5] and a 40% decrease in the monies allocated to DEL capital expenditure[6] over the four year period.

The total cuts over this period represent a cumulative real terms decrease of £4 billion compared to the baseline in 2010-11. The 15 December 2010 draft Budget document comments: *"While the level of reductions faced by the Northern Ireland Executive is lower than that faced by many Whitehall departments, it still represents a significant challenge for the Executive"*.[7]

Figure 1: NI total Departmental Expenditure Limit spending allocation from The Spending Review, £m real terms reductions relative to 2010-11



[5] DEL current expenditure is the money that is used to provide the services of government Departments and includes staff costs and operating costs of providing those services.

[6] DEL capital expenditure is the money used to provide infrastructure projects e.g. road building, upgrade of the water and sewage systems, hospital buildings.

[7] DFP 15 December 2010, D*raft Budget 2011-15*.

Immediately after the publication of the CSR, PwC produced a briefing paper for the Assembly Research and Library Service on the likely impact of the CSR on Northern Ireland, the key findings of which were as follows:

- Departmental Expenditure Limit (DEL) funding for all Northern Ireland departments (including the Department of Justice) will be £0.3bn less in 2014/15 than in 2010/11. In real terms, this is equivalent to a reduction of £1.4bn.[8]
- With regards to the estimated impact on GVA, PwC estimates that a reduction in DEL of £1.4bn would be equivalent to -4.6% of Northern Ireland GVA in 2014. However, a caveat on this estimate is that it does not account for cuts in welfare components of Annually Managed Expenditure (which are likely to be significant). Thus, taking the draft Budget in isolation is likely to understate the true scale of the effect of the public spending cuts and reform being driven by the London coalition.
- With regards to public sector jobs, PwC estimates that if the entire cut was offset against public sector employment (an unlikely situation but useful in reflecting, in terms of jobs, the indicative or "worst case" magnitude of the impact), this would result in a reduction in public sector employment of about 40,000. Once again, this figure is intended to reflect the "job equivalent" of the cuts, and is not a projection for job-losses.
- In respect of private sector jobs, PwC estimates that when multiplier effects are accounted for, Northern Ireland could be facing the largest potential reduction in private sector jobs in the UK with a potential 3% loss in total employment (private and public sector) over the five year period.[9]
- In terms of the potential welfare reform, this is likely to have particular significance for Northern Ireland. There is a relatively greater reliance upon the welfare system in NI, with benefits representing 10% of household income here, compared to a UK average of 7%. Welfare recipients represent a 50% greater proportion of the population in NI compared with the UK average. Furthermore, Northern Irelands 60+ share of the population is projected to grow more rapidly than in GB over the next fifty years.
- Finally, with regards to the Investment Strategy for Northern Ireland (ISNI2), the planned reduction of £500m in capital DEL (40% in real terms) over the next four years will have significant implications for the economy and upon the local construction sector.

[8] As calculated by PwC on the basis of Treasury and DFP assumptions regarding inflation rate expectations.

[9] Based on Northern Ireland taking it's *pro rata* share of the revised (i.e. lower) OBR forecast for public sector employment losses across the UK.

The economic context of the Northern Ireland draft Budget 2011-2015

Northern Ireland's economic performance has been, and remains, deeply unsatisfactory.

Over the entire period since 1921, Northern Ireland has failed to achieve sustained economic convergence relative to the UK average; levels of GDP per capita, for example, continue to languish at 80 percent of the UK average. The argument that radical action is needed to rebalance the economy is supported by a recent PwC *Government Futures* report[10] demonstrating that 15 government-sponsored economic development reviews and strategies – the earliest (Isles and Cuthbert) going back to the late 1940s – had failed to close the productivity gap with GB.

PwC concluded that half a century of reviews and strategies had made no substantive improvement to the region's productivity and competitiveness. Indeed, in the ten years to 2008, while Northern Ireland created 124,000 new jobs, comparative productivity (relative to the UK average) actually fell to below where it had been in the mid-1980s.

The figures presented in Isles and Cuthbert[11], for example, suggest that relative income per head in Northern Ireland compared to the UK average jumped from only 55 percent in 1938 to about 67 percent in 1942 and then stabilised at that level.[12] There was to be no sustained improvement on the mid Second World War comparative position until the mid 1970s and things have stood still over the last three decades. It is striking and depressing that the only periods when the Northern Ireland economy has managed any substantial move towards convergence with the rest of the UK have been ones where there was a very rapid increase in public spending; first of all during the Second World War and then during the early phase of the Troubles.

Furthermore, despite having created around 124,000 new jobs in the decade to 2008 - a remarkable performance and on par with US rates of job creation - the key productivity and performance metrics were worse at the end of the decade than they were at the beginning, while almost a third of those jobs had been lost in the 24 months to mid-2010.

Given this correlation between high levels of public spending and economic activity, the cumulative £4bn fall in public spending over the period of the draft Budget does not auger well for the economy. In addition, the hitherto underestimated reliance on economic activity in the Republic of Ireland will further impact on Northern Ireland's economic performance until RoI experiences significant recovery.

That means the Executive must focus the reduced resources of the draft Budget towards economic regeneration, wealth creation and increasing the efficiency of service delivery, while significantly reducing the cost (and potentially the size) of government and we would expect this to be a clear priority in the draft Budget and in any new Programme for Government.

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[10] PwC. (2010), Business as Usual? The need for radical change to the delivery of economic policy, *Government Futures Publications,* PwC, Belfast.

[11] K.S. Isles and N.Cuthbert1957, *an Economic Survey of Northern Ireland*, HMSO, Belfast.

[12] Isles and Cuthbert, *op.cit*.

In the absence of the coalition's anticipated paper on Corporation Tax and any significant move towards designating Northern Ireland (or parts thereof) as an Enterprise Zone[13] the region lacks any unique factor(s) that would deliver a step change in economic activity. And while we believe that a significant reduction in the level of Corporation Tax in Northern Ireland would be advantageous in attracting new foreign direct investment, we have calculated that the inevitable cost to the region could be disproportionate.[14] We believe that obtaining tax varying powers (which would include the power to vary Corporation Tax) might offer greater flexibility at less cost, but obtaining such powers could be subject to European Union approval and obtaining such agreement could take a prolonged period of time.[15]

Nevertheless, any new measures to make the Northern Ireland economy more competitive must attract significant levels of FDI, while stimulating increased productivity, exports and international competitiveness amongst both FDI and indigenous businesses. Most research suggests that, as compared to indigenous undertakings, FDI brings to the host region higher levels of productivity, greater capital investment and more highly skilled labour opportunities. So, only by targeting and delivering FDI that significantly outperforms the median will the Northern Ireland economy begin to rebalance from public sector dependency to private sector dominance.

The *Independent Review of Economic Policy* (IREP)[16] suggested that many Invest NI-supported investments have been in relatively lower value added sectors, with only 46 percent of new FDI service jobs in the mid 2000s paying salaries above the NI private sector median. IREP pointed, in particular, to contact centres, where only around 33 percent of new FDI jobs were above the NI private sector median.[17] However, whilst IREP's analysis is accurate and provides a valuable basis for analysing past shortcomings, it offers no clear strategy towards radical change, nor does it offer suggestions as to where resources should be prioritised.

An added complication is that, from January 2011, changes to EU State Aid rules will reduce the maximum assistance that Invest NI can provide to companies in respect of regional aid (principally Selective Financial Assistance but not including R&D and training grants), further complicating the creation of appropriate incentives for FDI that will operate in the high productivity/GVA per capita sectors.

Consequently, to adequately recognise where resources should be prioritised, any new strategy emerging from IREP should seek to identify and attract organisations, whether in the manufacturing or tradeable service sectors which:

- Pay salaries above the NI private sector median
- Can generate labour productivity levels (GVA/hour) above the NI average
  and hence
- Generate GVA per capita above the NI private sector median
- Deliver GVA per job filled above the NI private sector median

Only by targeting and delivering FDI and indigenous investment that significantly outperforms the average can we begin to rebalance the economy; and if the price of attracting such investment is a penalty on foregone tax, that element too, should be factored into the mix.

Creating this strategy, particularly in an election year, will take political courage to make the hard choices, but it is the inescapable requirement of the Executive's current fiscal dilemma.

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13 The Coalition May 2010,*Our Programme for Government,* London.

14 PwC2011, Corporation Tax: Game Changer or Game Over*?, Government Futures Publications,* PwC LLP, Belfast.

15 PwC2011, *op.cit.*.

16 Professor R. Barnett 2009, *Independent Review of Economic Policy,* DETI and Invest NI, Belfast.

17 Barnett, *op. cit.*

Relative scale of the Departments

The relative scale of the various Northern Ireland devolved Departments is shown in Table 1 and shows the percentage share of the total current spend by all the Departments - £10.3 billion - and the total capital expenditure - £1.5billion.

Table 1: Percentage shares of the total for all Northern Ireland Departments, 2010-11

Departments	*% of total current spending*	*% of total capital spending*
DARD	2	n/a*
DCAL	1	4
DE	19	10
DEL	8	2
DETI	2	4
DFP	2	1
DHSSPS	41	12
DOE	1	11
DOJ	12	5
DRD	5	34
DSD	5	16
OFMDFM	1	1
Non-Ministerial Departments.**	1	0.3
Total	**100**	**100**

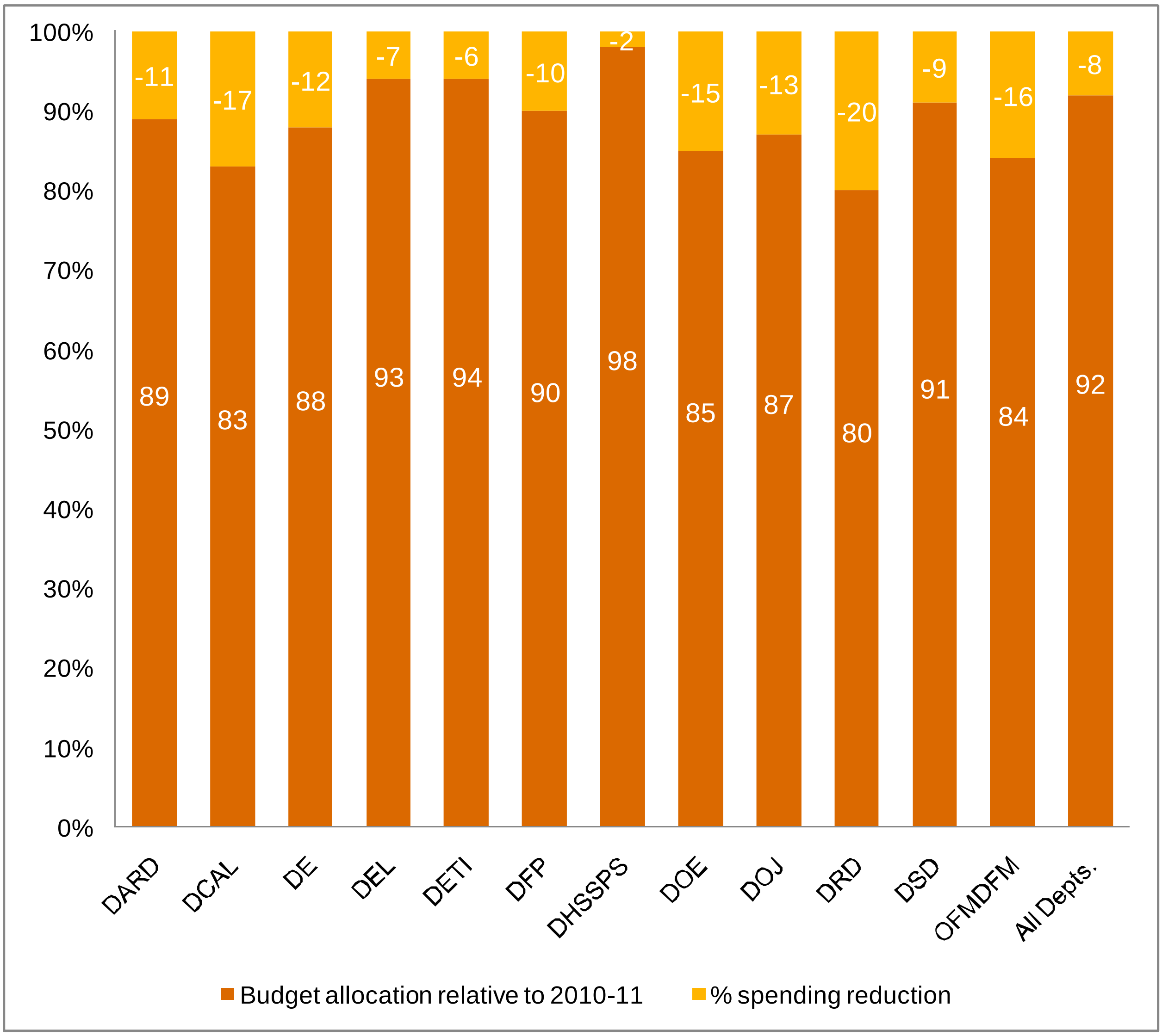
Note:*: In 2010-11 the net capital spending for DARD was reported as negative because of a high level of expected receipts from asset sales.
**: Assembly Ombudsman/Commissioner for Complaints, Food Standards Agency, Northern Ireland Assembly, Northern Ireland Audit Office, Northern Ireland Authority for Utility Regulation and Public Prosecution Service.
Source: DFP 15 December 2010, *draft Budget 2011-15*.

Table 1 demonstrates the wide variation in terms of the scale of spending across the Northern Ireland devolved Departments. In terms of current spending, Health (DHSSPS) is dominant with a share of about two-fifths. Education (DE) represents almost one-fifth of total current spending and Justice (DOJ) another 12%. Collectively, these three departments account for 72% of current spending, with DHSSPS and DE representing 60%. The dominance of these departments, and particularly the impact of DHSSPS is noteworthy insofar as any significant overspend (or in the case of DHSSPS the submission of an unbalanced budget) could impact significantly on smaller departments.

A different pattern emerges with respect to the relative shares of capital spending. The Department of Regional Development (DRD) dominates with just over one third, the Department of Social Development (DSD) has 16%, DHSSPS 12%, DOE 11% and DE 10%. Currently two/three departments dominate with DRD and DSD accounting for 50% of capital and the addition of DE taking the three departments to a dominant 60% of total capital spending.

We address individual departmental spending in greater detail in a later section, but the first and most significant general observation, shown in Figure 2, below, is that no Department has managed to entirely preserve current spending in real terms and only one department, DHSSPS, comes close with a real terms decline of “only” 2%.

Figure 2: Real terms current expenditure outcomes of the Northern Ireland Departments in 2014-15 as % of 2010-11



At the *Balancing the Budget* Conference, organised by the Chief Executives' Forum on 3 December 2010, the First Minister described the overall impact of the draft Budget on current spending as 8% over the four-year period and as such he thought this was "achievable". However, the relatively modest real terms impact on DHSSPS, which accounts for 41% of current spending, has the effect of concealing the real impact of the draft Budget on other departments, some of which (DE, DRD, DOE) face real terms cuts of 15-20%.

Furthermore, the DFP paper[18] proposes that, as in England, the level of spending on the "health" element of the departmental budget should be protected in real terms. Translated from England to Northern Ireland (as the departmental portfolios do not align precisely), this protection applies to the 77% of the DHSSPS budget which is "health" related (as defined in the CSR), as opposed to personal social services. That protection is relative to general inflation across the economy (the GDP deflator measure as used here and in Tables 1 and 2) but does not relate to any higher inflation rate which is, or which may be, specific to the health sector, such as the cost of drugs, new technology, staff pay increases or other awards specific to the sector.

[18] DFP 15 December 2010, *op cit*.

Table 2: Proposed expenditure outcomes (current and capital) for the Northern Ireland Departments, in real terms, 2014-15 compared to 2010-11 baseline

Departments	***Real current spending 2014-15 as a % of 2010-11***	***Real capital spending 2014-15 as a % of 2010-11***
DARD	89	n/a*
DCAL	83	130
DE	88	75
DEL	93	68
DETI	94	36
DFP	90	170
DHSSPS	98	74
DOE	85	4
DOJ	87	93
DRD	80	91
DSD	91	64
OFMDFM	84	194
Non-Ministerial Departments.**	78	131
All Departments***	92	84

Note: Using the HM Treasury (22 December 2010) forecast GDP deflator for 2014-15 compared to 2010-11, i.e. 1.10. If construction costs actually dip during 2010-11/2014-15, perhaps as a result of the downturn and its aftermath, then it would be less appropriate to use this "general" economy rate of inflation to deflate capital spending and real terms outcomes will be more favourable than those projected here.
*: In 2010-11 the net capital spending of DARD was reported as negative given a high level of expected receipts. 66% is the real terms growth in change 2014-15 compared to 2011-12 (there being a positive level of net capital spending in that latter year).
**: Assembly Ombudsman/Commissioner for Complaints, Food Standards Agency, Northern Ireland Assembly, Northern Ireland Audit Office, Northern Ireland Authority for Utility Regulation and Public Prosecution Service.
***: All 12 devolved Departments plus the Non-Ministerial Departments.
Source: DFP 15 December 2010, *draft Budget 2011-15*.

The relatively favourable outcomes for Employment and Learning (DEL) and DETI with a real terms decline of only 6-7% may be interpreted as evidence of the Executive's previously stated commitment (in the *Programme for Government 2008-11*) to make the economy a top political priority. However, it should be noted that comparisons between 2010-11 and the draft Budget forecasts for both DEL and DETI are distorted by changes in the categories of spending included in the definition of baseline spending for the period of the draft Budget, as compared to 2010-11.

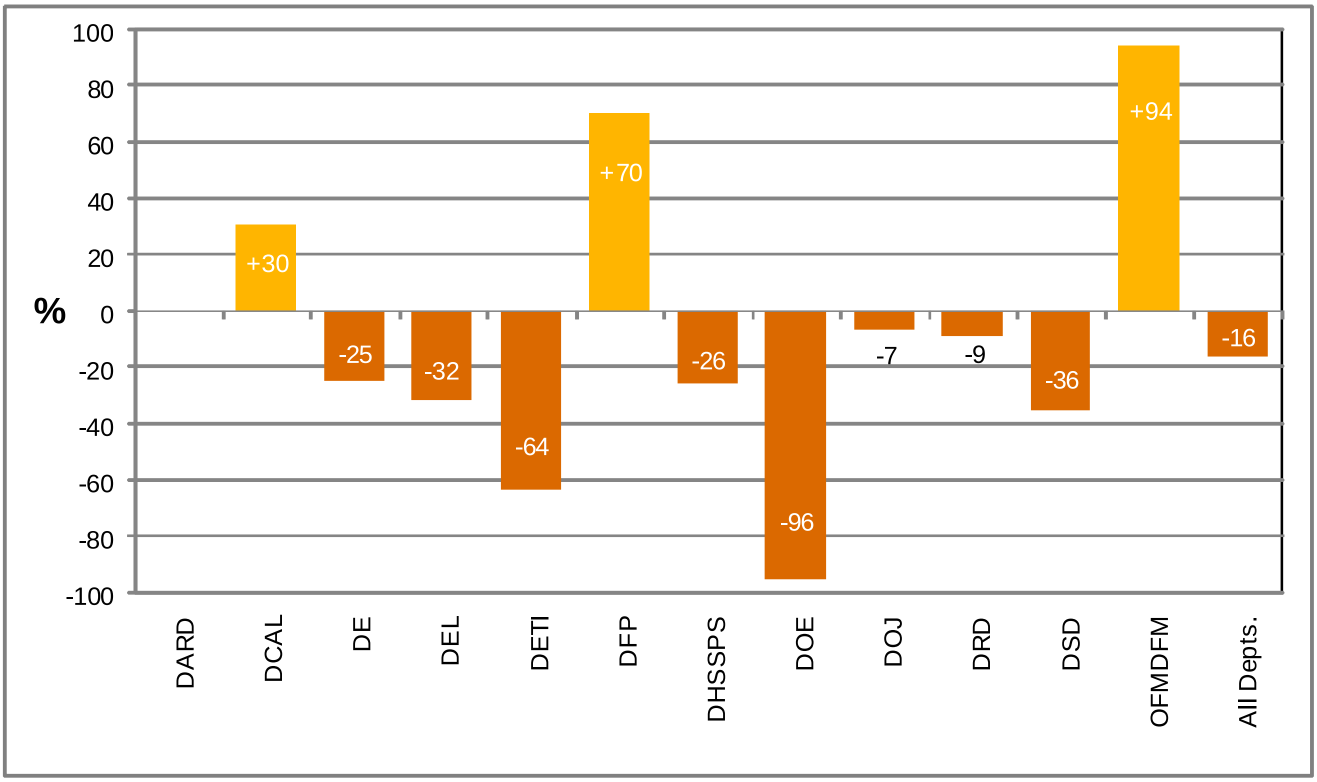
DEL's baseline 2011-12/2014-15 is to include a ring fenced Barnett consequential and DETI's baseline is to include a spending line (comprising various compensation payments) for which it previously bid in-year; so it could be argued that both the DEL and DETI proposed outcomes look slightly better than they really are relative to 2010-11 and we elaborate on this in our more detailed departmental analysis below.

Turning to capital, the average across all Departments is a 16% real terms decline in capital spending when comparing 2014-15 to 2010-11. This is notably better than the capital outcomes decline of 40% indicated by Northern Ireland's settlement in the Comprehensive Spending Review of 20 October 2010. However, the seemingly improved position contained in the draft Budget arises largely from the use of various additional sources of income such as RRI (Reinvestment and Reform Initiative) borrowing,[19] some switches from current to capital and the Irish government's contribution to the A5 and A8 road building programmes (£274m over the Spending Review period).

However, we note that the A5 Western Transport Corridor dualling project is certain to go to public enquiry and that such an enquiry is unlikely to begin before mid 2011 and with an uncertain end-date. If the enquiry is protracted it may make the Irish element of funding less certain and may also impact on DRD funds currently allocated for this project.

Three Departments show quite dramatic growth in real terms capital spend: DCAL, DFP and OFMDFM (as well as the Non Ministerial Departments) as shown in Figure 3 below (DARD's capital spend in 2010-11, net of receipts, was negative and so a comparison cannot be shown against that baseline).

Figure 3: Real terms capital investment outcomes of the Northern Ireland Departments in 2014-15 as % of 2010-11



However, the apparent growth in capital spending allocated to DCAL, DFP and OFMDFM is deceptive since all three start from a very low base. Conversely, DOE shows a spectacular decline (from about £200m to only £4m in 2013-14). Despite the previously stated Executive commitment to make the economy a political priority, the draft Budget shows DETI suffering a two-thirds decline in planned capital spend in real terms. DHSSPS will receive a one quarter reduction and DRD - the largest spending Department in terms of investment - will face a reduction of about 9%, well below the 16% average.

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[19] The Reinvestment and Reform Initiative (RRI), was announced by the then Prime Minister and Chancellor of the Exchequer on 2 May 2002 and was designed to address the deficit in infrastructure provision resulting from 30 years of concentration on security needs whilst at the same time providing for the modernisation of key services. The Investment Strategy for Northern Ireland (ISNI) and the handover of ex-military sites to the Northern Ireland Executive also form part of the RRI programme.

Individual Department proposals – background and methodlogy

In undertaking an analysis of the draft Budget (as presented by the Finance Minister) and separate departmental submissions, we were initially rather confused by the seeming parallel consultation process agreed by the Executive. The draft Budget was delivered to the Assembly by the Finance Minister on 15 December 2010, but it was made clear that consultation, subsequently extended, would be managed not by DFP, but by individual Departments, with the DFP Minister saying: "…This process will not be led by DFP but by individual Departments who will now publish their savings plans and spending proposals. This will allow interested parties to provide the views that will shape the final Budget position that I will bring before this Assembly in February."

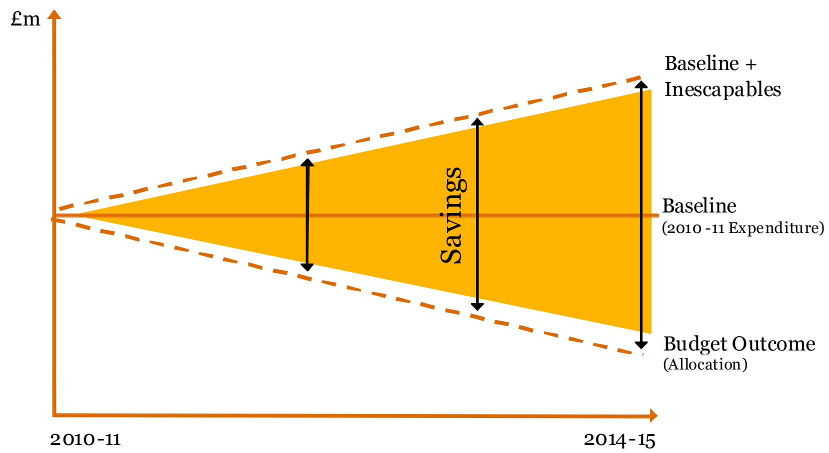
This inferred that Departments would "… publish their savings plans and spending proposals" in a manner of their own choosing and we believed at the time that this could result in a lack of transparency. There could in fact be an inability to compare Departments in a like-for-like manner and to relate individual departmental spend and save proposals, both to each other and to the draft Budget statement of 20 December. This has proved to be the case.

Our general approach in such an exercise would be to analyse individual Departmental spending and savings plans and to arrive at consistent and comparable outcomes, as follows:

- First, set out the projected level of spending outcomes, both for current and capital, over the next four years.
- Second, add to the 2010-11 baseline (i.e. the amounts actually spent in the most recent year) an estimate of the spending which would be needed given the Department's assessment of "inescapable spending demands" (i.e. by how much would spending have to increase to cope with unavoidable demands to do "new things" compared to what they were already doing in 2010-11).
- Then, third, by comparing the outcome in terms of allocated resources against the baseline adjusted for inescapables, any "gap" (as will usually be the case in this draft Budget 2011-15) between the figure for baseline, plus inescapable, minus the figure for outcomes, has to be "filled" by savings.

Unfortunately, most Departments have not provided sufficient detail to allow this process to be followed fully; which also constrains how much we can say about inescapables and savings plans. We believe that represents a serious shortcoming that should be corrected as part of the consultation debate. Nevertheless, where possible, we have outlined in the following subsections the likely changes in spending at Departmental level, analysed in this way.

Figure 4: Analysing change at the level of the individual Departments



Department of Finance and Personnel (DFP)

Table 3: DFP Budget summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	182.9	190.5	187.1	179.9	180.9
Capital investment	15.2	16.5	12.1	10.6	28.4
Inescapable spending		12.4	10.3	10.3	10.3
Capex to maintain existing services		16.5	12.1	10.6	11.6
Capex to enhance services		-	-	-	16.8
Savings		5.3	8.9	11.3	12.6

Summary

- In cash terms the current spending outcome shows an initial increase compared to the baseline but it declines thereafter. By the end of the Spending Review period cash spending is slightly lower than at the start. Taking into account inflation over the four years the real amount of current spending in 2014-15 is about 10% lower than in 2010-11.
- Capital spending outcomes are indicated to rise slightly in 2011-12 and then decline substantially. There is a major upsurge in the final year of the Spending Review (driven largely by spending on the civil service estate).
- The 'inescapable' pressures are a combination of extra money needed in 2011-12 to run the Census (£2.1m), £5m annually to Land and Property Services (LPS), £2m in each of the years for essential maintenance to NI Civil Service (NICS) buildings and £2.8m in each of the years to NI Direct.
- Capital expenditure is deemed essential to either maintain existing services (e.g. in terms of reducing accommodation costs through consolidating leases or investing in LPS to deliver a higher level of Rates collection) or to enhance services (i.e. the £16.8m in the final year of the Spending Review which is to be invested in improving NICS buildings).

Issues arising

- DFP justifies the extra spending in LPS by pointing to a projected increase in rates revenue collection from £960m in 2009-10 to a planned level of £980+m in 2010-11. However, in light of the £157m of arrears declared by LPS as of 31 March 2010, we wonder if an aggressive arrears programme could raise more than £20m.
- We wonder if deferring the £16.8m spending on NICS buildings will let the condition of the estate in the intervening years fall to a level whereby rectification will require greater cost in the next CSR period (when finances may improve).
- DFP plans to end capital funding for the Central Energy Efficiency Fund (to incentivise public sector bodies to become more energy efficient) as gains from any reductions in public sector energy costs plus the Carbon Reduction Commitment system should be sufficient to promote efficiency. We are less certain.

Department of the Environment (DOE)

Table 4: DOE Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	129.6	121.8	123.6	121.0	121.5
Capital investment	182.4	6.1	5.9	4.0	7.6

The DOE spending plan does not detail inescapable demands so the full analysis cannot be completed

Summary

- In cash terms the Budget outcome for current spending shows an initial decline and is fairly flat thereafter. Obviously, a more substantial real terms reduction is implied (about 15%).
- The baseline capital expenditure of £180m in 2010-11 is distorted by the re-allocation of a large amount in 2010-11 originally intended for the Strategic Waste Infrastructure Fund. In practice, this money was not spent by DOE and was largely re-allocated to DARD through in-year bids as “compensation” for the much less than expected receipts from the sale of the agricultural research station at Crossnacreevy.
- The DOE spending plan does not detail inescapable demands. However, it notes that £1.6m will be required next year for NICS pay progression and two areas where there is likely to be a reduction in available funds. First, fees paid to the Planning Service are likely to remain depressed (£21.3m in 2007-08 but only £12.4m projected for 2011-12). Second, the Plastic Bag Levy is intended to yield £4m annually, but the DOE has made contingency arrangements in case the revenue collected is less than this.
- Whereas the previous CSR provided £200m to the Strategic Waste Infrastructure Fund, DOE now has only £24m for all its capital expenditure over the next four years. This implies that in the absence of other sources of funding DOE will no longer be in a position to fund site purchases or finance projects, creating potential cost implications for local government.
- DOE is proposing to invest £1m and £0.5m respectively in 2011-12 and 2012-12 to restore the Roe Valley Hydro Scheme (built in the 1890s and one of the world’s first hydro-electric power plants). Although an example of renewable energy generation, the tourism/heritage potential is probably more significant. Return on investment is estimated as about eight years.
- Significant investments are required in the NI Driving Licensing System (a total of £4.2m over the four years) partly to ensure compliance with EU Directives, and partly to replace the system.
- Substantial savings of £15.4m annually are planned, with 80% on staff costs and 200 posts already removed and a further 150 planned even before the draft Budget 2011-15. A further reduction of 150 from Planning Service is dependent on staff redeployment.
- The Resource element of the General Grant to District Councils is being reduced by £1.2m next year. The grant for Listed Buildings is ending. The Second Survey of buildings with historical/architectural interest is being suspended. There is to be a slowdown in the declaration of Areas of Special Scientific Interest (ASSIs).

Issues arising

- We had expected some savings or capital realisation relating to possible change in the ownership of Vehicle (MOT) Centres.
- A number of the DOE proposals will have implications for the District Councils, e.g. the Planning and Local Government Group and it is possible that some previous DOE costs will be devolved down to Local Government level
- The Plastic Bags Levy works as either a deterrent to bag use *or* as a revenue raising instrument but it cannot really do both well at the same time.

Department of Enterprise, Trade and Investment (DETI)

Table 5: DETI Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	199.5	204.9	211.6	203.5	205.5
Capital investment	73.5	71.6*	44.7*	16.2*	29.1*
The DETI spending plan does not detail inescapable demands so the full analysis cannot be completed					

*: DFP 15 December 2010, *Draft Budget 2011-15*, gives slightly different figures for the four years, i.e. 71.7, 44.9, 16.0 and 28.8.

Comment

- In cash terms the Budget outcome shows an initial increase in current spending which is then partially reversed and, in real terms, DETI ends the period with about 6% less spending in 2014-15. There is a complication in comparing 2010-11 with 2011-12 and thereafter in that DETI now has an £8m annual provision in its baseline to make compensation for asbestosis and pleural plaques - something for which previously it had to rely on in-year bids.
- The position with respect to capital spending is more striking. After 2011-12 there is a major decline which is only partly reversed in 2014-15. Real term spending in that year is 64% down on 2010-11.
- The DETI spending plan does not detail **inescapable spending demands, however**, it notes that Invest Northern Ireland (INI) made forward investment commitments before the reduction in EU permitted maximum State Aid levels on 1 January 2011. This mean DETI carries forward very substantial spending pledges into the Spending Review period,[20] where INI is likely to have a priority call.
- DETI also has some inescapable (legal) commitments, e.g. to make compensation payments relating to asbestosis and pleural plaques.
- There is a substantial reduction in capital spending. Nevertheless, DETI argues it will fulfil its commitments relating to tourism infrastructure, e.g. Titanic Quarter.

[20] These could amount to £270m. Over 2011-12 to 2014-15 INI's total budget is to be about £670 m. However, it is important to stress that grant payments are usually made only when an investment project has actually been completed and jobs are delivered on the ground. Some of the investment projects "promoted" and agreed in the run up to 1 January 2011 may not reach that stage until after 2014-15.

Issues arising:

- INI's forward investment commitment means that it will be constrained in its ability to support new Foreign Direct Investment projects – a real challenge if tax varying powers are devolved and FDI increased over the period of the draft Budget.
- We note the Short Term Employment Measure to spend £19m over the Spending Review to create 5,000 jobs, suggesting that dealing with indigenous unemployment may now be as big a challenge as attracting new FDI.[21]
- Given the Budget restraint, will DETI struggle to meet NI objectives regarding sustainability and the promotion of the renewables sector?
- We note that spending on tourism promotion is substantially reduced at a time when tourism offers a real possibility for employment and economic activity.
- INI will be substantially constrained in respect of acquiring land for economic development purchases, an area where the organisation has previously been vocal in articulating the necessity of acquiring industrial development land.[22]

[21] This is confirmed by the current DETI consultation (January 2011, *Northern Ireland Executive Economic Strategy Consultation on Priorities for Sustainable Growth and Development*) which suggests and immediate priority to "rebuild" the economy after the downturn alongside the longer term goal to rebalance towards the private sector.

[22] The counter argument would be that INI/DETI is now increasingly chasing a type of FDI (e.g. business services) which tends to opt for a city centre location; that type of property is currently readily available.

Department of Culture, Arts and Leisure (DCAL)

Table 6: DCAL Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	113.3	112.5	113.2	110.0	103.0
Capital investment	59.9	11.8	21.9	22.2	85.8

The DCAL spending plan does not detail inescapable demands so the full analysis cannot be completed

Summary

- In cash terms the Budget outcome shows a continuous decline in current spending which accelerates towards the end of the period. In real terms, DCAL ends the period with about 17% less spending.
- The decline in capital spending is even more substantial if the period up to 2013-14 is considered (during the first three years of the Spending Review the amount of cash spend declines by almost two-thirds). In 2014-15, however, the planned level of investment rises to a level higher than that in 2010-11, largely related to intended spending on the sports stadia.
- The DCAL spending plan does not detail **inescapable spending demands.** It does, however, note that they have received £6m to spend on the World Police and Fire Games and £4m on creative industries. It also notes that "some protection" is to be given to current spending on libraries and National Museums Northern Ireland.
- DCAL notes that its capital allocation will enable the construction of the 50 metre swimming pool and the Metropolitan Arts Centre (in Belfast). The resurgence in capital spending in the final year of the Review should allow some progress regarding the upgrade of the regional sports stadia.
- DCAL has committed itself to savings of £1.8m, £3m, £8.3m and £10.3m in years one, two, three and four of the Spending Review.

Issues Arising:

- The DCAL document talks of some protection for libraries with some libraries in north and west Belfast to be refurbished and some spend on National Museums, but this is not elaborated upon.
- We note that the Invest to Save spending of £1m, £3m and £5m over the first three years, "…will be transferred to capital in due course" and are uncertain of the meaning or intent.

Department of Justice (DOJ)

Table 7: DOJ Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	1,223.7	1,213.1	1,189.0	1,166.7	1,176.4
Capital investment	80.0	78.3	64.5	51.8	82.0
The DOJ spending plan does not detail inescapable demands so the full analysis cannot be completed					
Savings		36.3	88.2	147.1	161.6

Summary:

- The above figures are taken from the DFP 15 December 2010 *draft Budget 2011-15,* as the figures in the DOJ's own spending plan would appear to be based on some anticipated level of End Year Flexibility.
- In cash terms the Budget outcome shows a decline in current spending. In real terms, DOJ ends the period with about 13% less spending (in 2014-15) compared to 2010-11.
- To an extent the allocation to DOJ is "ring fenced" as a consequence of the understandings with Treasury at the time of the devolution of criminal justice in 2010. Consequently, even if it wished, the Executive could not opt for a lower allocation for DOJ than that proposed here as Treasury may feel the previous agreement had been breached and deduct the 'reduced' balance from the block grant.
- Capital spending in 2014-15 is comparable to that in 2010-11 in cash terms. In the second and third years there is a substantial dip.
- The DOJ spending plan does not detail or quantify **inescapable spending demands.**
- DOJ notes that its capital allocation will enable it to deliver the following: an upgrading to forensic science accommodation, Desertcreat College[23]; redevelopment of Magilligan; improved facilities for female prisoners; and essential maintenance.
- DOJ has committed itself to substantial savings over the course of the Spending Review, the majority of these savings, especially in the first and second year, are to be in the PSNI but much more clarity is required regarding the detail.

Issues Arising:

- The DOJ Budget contains some aspirations (give priority to frontline policing, protect service delivery outcomes for the public and protect the community and voluntary sectors) but we have some concerns as to the caveat "… as far as possible" and believe that, if DOJ provides further detail about both its spending and savings plans, this may become clearer. However, other questions may then present themselves.

[23] We note that, while DOJ seems to have sufficient funds to complete Desertcreat College, the DHSSPS Budget seems unable to meet its share of Desertcreat operating costs and this will have further implications for DOJ and even for the viability of Desertcreat.

Department for Employment and Learning (DEL)

Table 8: DEL Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	798.9	775.4	767.4	785.6	813.8
Capital investment	37.6	41.2	32.3	18.5	28.3
Inescapable spending		56	66	87	119
Total requirements		855	865	886	918
Total resources*		775	762	765	777
Implied deficit		-80	-103	-121	-141
Savings		40	72	108	144

Note: *: DEL outcome in terms of current spending (not adjusted for inflation) but adjusted downwards to excluded ring fenced Barnett consequential of monies related to higher English student fees.

Summary

- In cash terms the Budget outcome shows a decline in years one and two, but recovery by the end of the period, with the real terms current spend in 2014-15 7% down on 2010-11.
- Part of the current DEL allocation relates to a ring-fenced Barnett consequential to cope with the higher loans associated with student fee changes in England, comprising £0m, £5m, £20m and £36m. Ideally we would have subtracted these totals to give a better indication of the resources available to the Department when comparing 2010-11 with 2011-12/2014-15 on a like for like basis.
- On the capital side, the decline (both cash and real terms) is more marked, albeit with some recovery towards the end of the period.
- In terms of inescapable demands, the Budget includes the impact of higher unemployment on the Employment Service (with associated administrative costs), student support, continuing support for innovation (given that the previous Funding for Innovation ceases in March 2011), the Assured Skills programme and pay and price inflation. The bulk of the pressure comes from student support and pay/price inflation.
- When the DEL resource (current) outcomes are set alongside the above inescapable, a substantial funding gap is implied.
- The proposed allocations to DEL enable it to fund contractually committed elements in respect of PFI contracts at two FE colleges (Belfast Metropolitan and South Eastern Regional), fund the ongoing development works at Springvale E3 campus of Belfast Metropolitan College; support further education in terms of minor Health and Safety and other works; and fund some teaching and research infrastructure in the universities and university colleges.
- DEL has indicated that major building projects such as the University of Ulster's proposals for York Street are not dependent on DEL funding and it is expected that this project will go ahead if the University of Ulster can raise the required funding.
- Given the funding gap (baseline plus inescapables minus resources), DEL has had to propose very substantial savings. However, in the first three years of the Review (and particularly years one and two) the proposed savings fall short of the gap identified between requirements and resources, leaving the Department to face a deficit of £40m in year one and £31m in year two and a cumulative deficit of around £81m by 2014-15.

Issues arising

- On the basis of these proposals DEL faces a funding deficit and, while the document lists a range of services that could be scaled back, albeit with a very significant negative impact, DEL is seeking the views of stakeholders as to what to do about this situation. Nevertheless, in technical terms and based on the figures available to consultees, the DEL Budget is not balanced within the existing funding envelope.
- We thought there may be scope for DEL to follow its counterpart in England (DWP) in making greater use of private sector training companies (perhaps incentivised by payments by results) to work with the long term unemployed to get them off the register and into employment. Perhaps there is a role for social enterprises in this regard?
- The universities will have to respond to the significant reduction in their funding.
- The Executive may be constrained in respect of some of its targets/measures relating to raising the level of innovation in the economy, particularly in respect of the 300 additional science related PhD places put in place under the *Programme for Government 2008-11*.
- There are no explicit assumptions here regarding raising the cap on tuition fees but given the scale of the hit on universities funding it must surely be strongly implied that Northern Ireland is going to follow the lead set by policy in England? The independent review to the Minister (Stuart report, February 2011) suggests an increase to a ceiling of about £ 5,750 but this will require Ministerial/Executive approval.

Department of Education (DE)

Table 9: DE Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	1,914.8	1,852.2	1,857.3	1,861.6	1,847.7
Capital investment	169.3	127.4	100.4	101.5	139.4
Inescapable spending		76.6	125.8	172.4	236.3
Total requirements		1,991.4	2,040.6	2,087.2	2,151.1
Total resources		1,852.2	1,857.3	1,861.6	1,847.7
Implied deficit		-139.2	-183.3	-225.6	-303.4
Savings		143.2	188.4	230.8	308.7

Summary:

- In cash terms the Budget outcome for DE shows a significant decline in 2011-12 compared to 2010-11 and then remains flat thereafter (at a level about 3% lower than the baseline). The real terms reduction by the end of the period is 12%.
- On the capital side, the initial decline is quite steep with partial recovery in the final year. In real terms the reduction is 25% by the end of the period.
- We understand that the DFP Minister has agreed with his DE counterpart (21 January 2011) that DE in general, and schools in particular, should be compensated for no longer having access to End Year Flexibility Funds. Whilst we are not aware of the details of this arrangement, we believe that compensatory monies will be found from within the block. This could mean DE having a first call on money during in-year bids, where previously DHSSPS had this advantage and such an arrangement may put previously unplanned pressure on overall Northern Ireland Executive funding resources.
- DE does not provide a breakdown of inescapable pressures, but argues that 44% and 35% of the draft Budget capital allocations for 2011-12 and 2012-13 respectively will be required to meet inescapables. This may be due to DE being allocated £738m less than the Investment Strategy (ISNI2) proposals, but the proposed DE allocation will not enable it to support planned new build school projects.
- When the DE resource (current) outcomes are set alongside these inescapables, a large and growing gap in funding is implied. DE places these in context by saying that the schools estate (valued at about £4 billion) has a maintenance backlog of £300-£400m.
- Given the funding gap (baseline plus inescapables minus resources) already identified, DE has to make substantial savings to close that gap, increasing to £308.7m in 2014-15. These savings are slightly larger than those required to close the funding gap, thus enabling small increases in spending on Free School Meals and Pre-School.
- Some of the largest savings include reduced Professional Support for Schools, ICT in schools and the Entitlement Framework. DE has also proposed (subject to Executive approval)[24] a transfer of £41m of capital spend to current spend in year one, which it counts towards "savings".

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[24] And, significantly, DE's likely request of £41m of capital to current transfers exceeds the total sum (£38.5m) which the Executive has to move in that direction.

Issues Arising

- DE has produced a plan to close its funding deficit, however, there is no evaluation of the impacts of the plan on existing or previously planned programmes, including:
  - Extension of Free School Meals Entitlement
  - Change in Common Funding Formula
  - Reduction in ICT in schools
  - Reduction in Professional Support for Schools
  - Reduction in the Entitlement Framework
- We are not certain where the draft Budget and spending plans leave the proposed rationalisation of the schools' estate and/or the proposed greater use of shared services. Neither are we clear as to how the plan impacts on the continued delay in establishing ESA (with its associated intended savings) or on the proposals for Area-based Planning.
- Despite the seeming agreement between DFP and DE in respect of compensating schools for the end of access to End Year Flexibility Funds, DE will allocate most of its funding to schools via the same formula (insofar as no new formula or funding allocation is referred to). We therefore wonder what the impact will be on teacher and staff numbers, given that decisions taken at the level of individual schools will largely determine the impact on the ground of spending reductions.
- We believe that around 800 out of the total of 1200 Northern Ireland schools have some cash surpluses and it is unclear if schools' funding formulae will take these surpluses into account, or whether they will be ring fenced thus offering a hidden buffer against funding pressures.
- Most importantly, we note that DE does not comment on how (if at all) its spending plans will impact on the comparative quality of Northern Ireland education as measured by, say, literacy and numeracy targets, PISA and OECD[25] measures nor if the Department can confidently move closer towards the objective of "every school a good school".

[25] Programme for International Student Assessment and Organisation for Economic Cooperation and Development.

Department of Health, Social Services and Public Safety (DHSSPS)

Table 10: DHSSPS Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	4,303.0	4,348.1	4,427.7	4,543.2	4,629.2
Capital investment	201.7	214.8	278.8	184.9	163.3
Inescapable demands		391	610	869	1,154
Total requirements		4,694	4,913	5,172	5,457
Total resources		4,348	4,428	4,543	4,629
Implied deficit		-346	-486	-629	-828[26]

The DHSSPS spending plan does not detail savings so the full analysis cannot be completed

Summary:

- In cash terms the Budget outcome for DHSSPS shows a slight increase over the period (by 2014-15 up 7.6% on 2010-11) although this translates into a real terms decline of about 2%.
- On the capital side, the decline is substantial, down 19% in cash and about 26% in real terms by the end of the period.
- In terms of current spending, DHSSPS list their inescapable demands to be both large and growing and to include:
  - Demography (fastest growing and most rapidly ageing population in the UK)[27]
  - The costs of new technologies[28]
  - Impact of higher VAT
  - Emergency pressures, e.g. elective care, winter pressures (flu and extra fractures)
  - New buildings
  - Pay costs
  - Goods and services inflation
- It is a moot point how far the second and the last two of these pressures are truly inescapable and how far they are a product of the way in which DHSSPS actually operates.
- DHSSPS lists the proposed capital commitments but notes that it will not be possible to provide revenue funding for the Radiotherapy Unit at Altnagelvin and the Fire and Rescue Service Training College at

[26] A figure confirmed by Northern Ireland Confederation for Health and Social Care January 2011, *Summary Building on Progress- Rising to the Challenge*.

[27] Northern Ireland Confederation for Health and Social Care January 2011, *Building on Progress- Rising to the Challenge*, attribute a 1.3 % p.a. increase in required funding to demography.

[28] Northern Ireland Confederation, *ibid.* attribute a 2.5 % p.a. increase to new technology, drugs and rising expectations.

Desertcreat [29] offering the prospect of new capital projects that cannot be utilised as revenue funding is unavailable.

- DHSSPS does not provide a savings plan but notes that meeting the challenges implied by the draft Budget would *"…require significant change to the nature and extent of delivery of Health, Social Care and Public Safety Service…" but* does not elaborate on what such changes might include.
- We note that the McKinsey Report, *Reshaping the System: Implications for Northern Ireland's Health and Social Care Services of the 2010 Spending Review*[30], was published by DHSSPS on 10 February and specifically comments on the draft Budget proposals and offers new options for Departmental strategy and spending over the Budget period. Submitting such a strategic document so close to the end of the consultation period (four working days) leaves no time for a comprehensive analysis of the McKinsey methodology and assumptions and is therefore unhelpful to consultees.
- The main conclusions of McKinsey include:

  – Northern Ireland's health and social care (HSC) service spends between 7% and 16% less per head than England's, once our higher levels of deprivation and social need are taken into account
  – Growth in need for care and in unit costs, if not managed, will increase DHSSPS required funding from about £4.3 billion in 2010/11 to about £5.4 billion in 2014/15
  – By undertaking a stretching programme of quality and productivity improvement, HSCNI could reduce 2014/15 required funding by about£0.6 billion. Doing so will involve a strategic, evolutionary transformation of our system. This will not be easy, and will require:

    o Significant political, professional and managerial leadership. For each month we delay, the 2014/15 saving that could be delivered reduces by £5 million.
    o Effective communication and engagement with stakeholders including communities, patients, clients, carers, their local political representatives, partners such as GPs, staff and staff bodies.
    o Investment in capacity, capability, technology, facilities, and staff redeployment – including one-off transition costs of about £0.3 billion over the years to 2014/15.

  – A further reduction of several hundred million pounds in 2014/15 provided funding could be secured by introducing co-payment for some services by the service user (e.g., bringing protocols in line with the rest of the UK)
  – Any required reduction in funding beyond this will involve freezing staff pay costs and/ or rationing access to services – thereby transforming the fundamental nature of the system away from the original 1940s NHS model

- The DHSSPS document highlights a forthcoming (April 2011) Commissioning Plan but notes that the proposed reduction in spending in 2011-12 would lead to a range of outcomes, which would include: reductions in community care; fewer hospital beds; "reduction in grants to the voluntary sector"; and job losses of about 4,000.
- An interesting piece of context for considering health spending in either England or Northern Ireland is that in the period since 1997, health sector productivity has been at best static in England, but now a very dramatic improvement is proposed for the next four years in England.[31]

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[29] See analysis of DOJ spending plans.

[30] McKinsey February 2011, *Reshaping the System: Implications for Northern Ireland's Health and Social Care Services of the 2010 Spending Review.*

[31] *The Economist* 15 January 2011, "Health care reform the final frontier".

Issues Arising

- On the figures presented there is an implied cumulative deficit of some £2.29 bn by the end of 2014-15 and the lack of stated compensating savings makes it impossible for consultees to determine if the Budget can be balanced within the Departmental envelope. This is a substantial implicit deficit to be closed and the Department's inability to make matching savings will have significant implications for other Departments.
- The McKinsey report suggests that *"… growth in need for care and in unit costs, if not managed, will increase DHSSPS required funding from about £4.3 billion in 2010/11 to about £5.4 billion in 2014/15."* However, McKinsey suggests that this could be reduced (by adopting its proposals) by some £600m in 2014-15 (which would substantially reduce the unfunded deficit in that year) but at a cost of £300m in earlier years.
- We note McKinsey's comment that *"…reducing unit costs will require a step-change in productivity across all settings,"* and that "*…these changes will substantially impact current services."* There is an inference[32] that such a radical changes could impact significantly on existing structures and require *"…fewer acute hospital sites* [33]*"*.
- While the McKinsey report introduced a useful challenge to the status-quo and opens new avenues of debate, we have not had an opportunity to analyse the report in the detail we would have expected for such an important document. Nevertheless, we wonder just how radical the Department, or indeed the Executive, would have to be to address the very real challenges facing health in Northern Ireland and if the reduction in acute hospitals (e.g. closing a hospital within greater Belfast) is a political decision ministers are willing to make.
- We note the estimate of 4,000 job losses in 2011-12, as compared to the baseline health sector employment of about 65,000. The real terms decline in 2011-12 spending is "only" about 1-1.5% of the baseline current spending, so we cannot reconcile 4,000 job losses with such a modest decline in spending and suspect that the Departmental estimate relates to what would have happened by year four if the shortfall (£5.5 billion is required but only £4.6 billion is available), cannot be eliminated by other means. However, if savings were to be progressive, our sense is that job reductions would have to be weighted towards the start of the Spending Review period.[34]
- Given the almost last-minute publication of McKinsey, we do not see any particular merit in further detailed analysis of the Departmental submission as we sense that it has been superseded by McKinsey.

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[32] McKinsey, February 2011 *ibid*. Exhibit 16, Page 29,

[33] McKinsey, February 2011 ibid. Page 30.

[34] It is worth stressing that reducing staff sometimes has considerable upfront costs, e.g. redundancy payments.

Department for Social Development (DSD)

Table 11: DSD Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	521.1	516.7	532.0	543.0	523.4
Capital investment	269.6	150.3	120.6	98.9	190.2
The DSD spending plan does not detail inescapable demands so the full analysis cannot be completed					

Summary

- In cash terms the Budget outcome for DSD shows a very slight increase over the period, which translates into a decline of about 9% in real terms.
- On the capital side, DSD assumes that, since the capital baseline was, technically, zero there was no need to supply a baseline figure for 2010-11. However, the 15 December draft Northern Ireland Budget[35] indicates a capital allocation for 2010-11 of £269.6m. By that standard, the capital proposals for 2011-12 to 2014-15 seem very adverse, especially in the middle years.
- DSD does not list any inescapable spending demands although it is implied that the administrative cost of welfare reform could be one. Spending to implement Bamford (mental health) could be another one. An increasing spend (£19.5m in year one, rising to £41.7m in year four) on pay and price inflation is noted.
- Pressures relating to the implementation of the Bamford reforms could be considered as an inescapable capital pressure. DSD bid for resources to allow a new build of 2,500 social houses annually but is unclear what the outturns will now be.
- In terms of savings, DSD lists an extensive list of efficiency improvements in order to protect front line services. However, the scale of these savings is not set out.

Issues Arising

- DSD has not accepted the DFP assessment that £20m per annum could be unlocked from the reserves of the Housing Associations - an impasse that should be resolved immediately post-consultation.
- No decision has yet to be made on NIHE rent increases, however, an inflation-only increase should yield about £12m annually.
- The £20m per annum Social Protection Fund (with guaranteed funding for first year only) lies with OFMDFM but DSD (like other Departments) could bid to this fund. This is also the case for the Social Investment Fund. While this is potentially available, we are not certain if it represents the most appropriate way to manage investments.
- We are also unclear as to how far will DSD be able to implement welfare reform. DSD has been allocated only a small proportion of the funds transferred to the NI Executive consequent on the costs of welfare reform in England.

35 DFP 15 December 2010, *op.cit.*

Department for Regional Development (DRD)

Table 12: DRD Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	517.3	500.3	487.2	459.6	454.0
Capital investment	556.2**	438.3	425.3	540.9	558.8
The DRD spending plan does not detail inescapable demands so the full analysis cannot be completed					
Savings		15.7	28.8	56.4	62.0

**: Taken from draft Budget 2011-15.

Summary

- In cash terms the Budget outcome for DRD shows a continuous and substantial decline over the period (by 2014-15 12% down on 2010-11) which translates into a substantial decrease of about 20%.
- On the capital side, the decline (both cash and real terms) is substantial. In the first two years there is a decrease of about 30% in real terms, with a partial bounce back thereafter so that the final year is 9% down on 2010-11.
- DRD does not include inescapable spending demands and takes the view that the investments required to part fund two major roads (A5 Derry/Aughnacloy and A8 Belfast/Larne with the Irish government funding the rest) are inescapable. DRD's position seems to be that, as the Executive has made a binding international agreement with the Republic of Ireland government regarding the joint funding of these roads, the funding is inescapable.
- £1.1 bn is to be spent over the Review period on roads. Significantly, 70% (£790m) of that is to go to just two roads - the widening of the A5 and A8. By implication, a number of other road improvements will be postponed (A6 Randalstown, A2 Greenisland, York Street and Sydenham bypass).
- DRD believes they will be able to fund a pilot network for a "bus-based Rapid Transit system" in Belfast as well as 20 new trains (on Northern Ireland Railways).
- Similarly, there is money for the Coleraine/Derry railway track upgrade in 2014/15 but not for Knockmore/Lurgan (some of the spend on the Derry line is a follow on from the new facilities which are required to use some of the new train sets on that route).
- There are to be substantial capital investments in NI Water (NIW) but those for 2012-13 are only three-quarters of those previously planned.
- However, we note that the A5 Western Transport Corridor dualling project is certain to go to public enquiry and that such an enquiry is unlikely to begin before mid 2011 and with an uncertain end-date. If the enquiry is protracted it may make the Irish element of funding less certain and may also impact on DRD funds currently allocated for this project.
- A number of programmes are to be reduced in scale, including the Rural Transport Fund, which will decline by £0.3m, £0.6m and £0.8m in the three final years of the Spending Review. This implies that a number of less economic Translink rural routes could probably cease and, similarly, some provision of public transport to groups in rural areas could be scaled back.
- Similarly, the budget for the Transport Programme for People with Disabilities is to be scaled back (by £0.7m, £0.7m and £0.9m in the three final years of the Spending Review). By implication, evening door-to-door services for the disabled could stop and support for group travel organised by disabilities organisations could also cease.

- A number of revenue raising schemes are counted as "savings". Roads Service parking charges are to be increased more rapidly than inflation and cash income is expected to grow by 15% per annum. Penalties for illegal parking are to be upgraded and on-street parking charges are to be extended beyond Belfast-Derry-Lisburn.
- It is also assumed that in the two final years of the Spending Review £15m annually can be released in the form of a dividend from Belfast Harbour Commissioners.
- Additionally, it is assumed that £6m can be switched from capital to current spending in 2014-15 (although this will require Executive approval).
- It is projected that 250 staff posts will be cut by the end of the Spending Review.

Issues Arising

- The A5 and A8 are being preferred over a number of other road improvements but we are uncertain if this is based on a robust analysis of relative socio-economic return on the respective investments or if DRD merely accepted it has no discretion in the light of the agreement with the Irish government.
- Similarly, the Coleraine/Derry railway line is preferred over Lurgan/Knockmore, but we are not aware of passenger numbers or the economic basis of the decision. We note that the Coleraine/Derry railway track upgraded line will not be in place for the 2013 City of Culture year.
- DRD proposes to reduce its maintenance activity on roads or car parks but there is no assessment of the longer term consequences, particularly having regard to the damage to the road network as a direct result of the recent hard winter.
- It is unclear how far DRD is increasing the subsidy to railway operations (the Public Service Obligation) and what the implications may be for fares; we would have expected to see some reference to this and to the implication for Translink bus fares.
- There are adverse equality impacts arising from the cutbacks to rural public transport and transport for the disabled and we wonder if these would leave the Department open to legal challenge.
- We note that the Department does not plan to introduce domestic water charging and by continuing to defer domestic water charging, the Department has forgone savings of some £800m at 2010 prices, over the period of the draft Budget. This continued deferral amounts to a subsidy from other Departments of around £200 per annum.

Office of the First and Deputy First Ministers (OFMDFM)

Table 13: OFMDFM Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	80.2	79.0	80.2	77.0	73.7
Capital investment	12.0	9.1	3.8	8.8	25.6
The OFMDFM spending plan does not detail inescapable demands so the full analysis cannot be completed					
Savings		3.8	6.9	10.3	13.8

Summary

- In cash terms the Budget current spending outcome for OFMDFM is flat which translates into a decline of 16% comparing 2014-15 with 2010-11.
- Capital spending shows that, by 2012-13 capital is 70% down on 2010-11 but by 2014-15 there is a recovery such that spending is to be 90% up on the baseline in real terms.
- OFMDFM does not spell out inescapable demands. However, "key issues/challenges" identified in the document include growing the economy; dealing with poverty and disadvantage; maximising the Executive's international connections (especially with the US and EU); implications of the Barroso Taskforce; urban regeneration; Cohesion, Sharing and Integration; Ministerial Sub-Committee for Children and Young People; development of Commissioner for Older People; and the Victims and Survivors Service.
- Planned investments include steadily rising spending on Maze Long Kesh; spending on Crumlin Road Gaol (in 2011-12 only); and on Ebrington Barracks (weighted towards 2014-15).
- In terms of savings, we note that the Strategic Investment Board (SIB) *"…budget will be reduced by £1.9m"*. The wind-up of the Economic Research Institute of Northern Ireland (ERINI) in 2011 will release £0.9m annually.

Issues Arising

- There is no hint of a new Programme for Government (PFG), although one of OFMDFM's objectives is to drive the process towards an agreed Programme. However, it looks as though the 2011-15 Budget will have to be agreed ahead of any consensus on targets and outcomes for public services over the next four years. This is a reversal of what should ideally be the sequence of decision making (agree strategy, define outcomes, set key performance indicators [KPIs] and finally, assign budget lines as necessary) and represents one of the greatest concerns and potential weaknesses in the entire draft Budget process.
- OFMDFM has correctly identified maximising the economic gain from Europe in the context of the Barroso Task Force, but makes no reference to the reduction in maximum permissible State Aids or how greater EU engagement might directly benefit Northern Ireland.
- The profile of spending on Ebrington Barracks seems curious as much of it comes after the 2013 City of Culture year; although OFMDFM argues that the plans are not sufficiently advanced.
- We are curious as to why the two "central funds", Social Investment and Social Protection, are positioned in OFMDFM as opposed to, say, DSD (with its role concerning urban regeneration and social security). OFMDFM seems to view this positioning as allowing head room for new initiatives.

Department of Agriculture and Rural Development (DARD)

Table 14: DARD Budget Summary (£m current prices, not inflation adjusted)

	2010-11 (baseline)	2011-12	2012-13	2013-14	2014-15
Net current expenditure	224.9	224.9	236.0	222.6	219.0
Capital investment	-173.5**	16.4	13.9	20.0	29.3
Inescapable Demands		13.0	15.5	7.5	6.6
Savings		6.7	8.7	12.8	15.2

**: This considerably negative figure arises given the volume of expected receipts in 2010-11 relative to actual investment spending.

Summary:

- In cash terms the Budget outcome for DARD is relatively flat which translates into a decline of 11% in real terms comparing 2014-15 with 2010-11. On the capital side, there is a decrease in expenditure in 2012-13 but increases thereafter.
- DARD does imply some inescapable spending demands in a list of "additional current expenditure proposals". The spending on the Land Parcel Identity System (£20m over the review period but almost all concentrated in years one and two) is ring fenced as it mitigates the threat of the EU disallowing future land support. There is also some spending relating to animal health, traceability, DARD direct and the EU Floods Directive.
- In addition to making considerable annual capital grants to farmers (£8.5m in the first year, though falling to £7m in the third and fourth years), DARD is proposing to invest £13m in 2014-15 towards the cost of relocating its headquarters to somewhere outside of Greater Belfast.
- In terms of savings, staff numbers have already fallen by 451 since 2005-06 to 2,880 (full time equivalents) in December 2010. A reduction of a further 80 is now envisaged and included in the savings.
- Receipts are to be increased by £1.1m albeit this increase is back-end loaded (only in 2014-15).

Issues Arising:

- We cannot ascertain what assumptions have been made around possible commercialisation of the Forest Service and what the ultimate strategic impact might be.
- We had hoped to see the economic/VFM case behind the relocation to a new HQ in 2014-15 to demonstrate good economic value for money and an acceptable social return.
- We also had hoped to see the total impact, in terms of costs and effectiveness of service delivery, of the proposed changes around procurement.