Northern Ireland Fiscal Council

Bringing transparency to NI's public finances

The NI Executive's 2022-23 Budget: an update

November 2022

Contents

1 Introduction

The Northern Ireland (NI) Fiscal Council was established in 2021. The Council's Chairperson is Sir Robert Chote. The other Council members are Maureen O'Reilly, Professor Alan Barrett and Dr Esmond Birnie. Our aim is to bring greater transparency and independent scrutiny to the region's public finances, focusing in particular on the finances of the NI Executive. In doing so we hope to inform both public debate and policy decisions to the benefit of everyone in NI.

Within this mission, our Terms of Reference require us to *"prepare an annual assessment of the Executive's revenue streams and spending proposals and how these allow the Executive to balance their budget"* (as it is required to do). In January we published an assessment of the 2022-25 Draft Budget published by the Department of Finance in December 2021. We noted that it did not have the endorsement of the Executive and that it lacked evidence of strategic intent and prioritisation, but we concluded that:

> *"…the Draft Budget achieves balance in the sense that proposed departmental spending allocations and forecast debt interest costs are fully covered by a combination of external (primarily Block Grant) funding, Regional Rates revenue and capital borrowing that lies within the limits set down in legislation and subsequent agreement with the Treasury."*[1]

Since that time, however, the NI political and fiscal position has changed materially:

- **The Executive has collapsed**, leaving the Draft Budget consultation unfinished and precluding agreement on either a further Draft Budget or Final Budget. However, a Budget Bill was passed providing legal authority for departmental spending in the early months of the financial year;
- As a result of no Speaker being nominated**, the Assembly has ceased to function,** and the Committee system has stopped operating;
- **But Ministers remained in post as 'caretakers' until the end of October and continued to make spending commitments**, although they were not permitted to take cross-cutting or controversial decisions;
- The Minister of Finance warned on 11 October 2022 that **departments expected to overspend their indicative allocations** by a significant margin, more than sufficient to exhaust the available funding;[2] and,
- With the deadline for the NI parties to reform an Executive on 28 October 2022 having passed **the UK Government is preparing to set and legislate for an NI Budget**. And a new Assembly election will take place next year.

[1] https://www.nifiscalcouncil.org/publications/ni-executives-2022-25-draft-budget-assessment

[2] http://www.niassembly.gov.uk/assembly-business/official-report/written-ministerial-statements/department-of-finance---2022-23-budgetary-position/

With the budget position now substantially different from that on which we commented in January, we thought it would be helpful to publish a brief update.

Without corrective action or additional funding, the control totals set by the Treasury are likely to be breached this year on current trend, thus 'unbalancing' the budget in the sense we are asked to monitor. This is almost unprecedented, certainly in terms of the scale of the projected overspend. Under the Treasury's *Statement of Funding Policy*, any overspend "…*would represent serious financial mismanagement. The presumption is that the following year's Block Grant would be reduced by an amount equal to the breach*".[3] This would intensify an already severe squeeze on NI departmental budgets relative to equivalent spending in England.

In the rest of the paper we:

- Set out the latest available forecasts of **departmental spending** and assess whether they imply overspends against available funding;
- Review **how NI's public finances got to this point** and what the key contributing factors appear to have been;
- Consider what the **next steps** are likely to be, including interventions by the Northern Ireland Office (NIO); and
- Offer some **concluding reflections** on what might be learned from the current crisis and its causes.

[3]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1030043/Statement_of_Funding_Policy_2021_-_FINAL.pdf (Paragraph 8.14)

2 Budgets and forecasts for 2022-23

In December 2021, the Department of Finance published a Draft Budget consultation document setting out spending allocations for the NI departments for the three financial years 2022-23 to 2024-25, with some funding proposed to be held centrally for later allocation. The Executive did not agree to these allocations but was content that they be published for formal consultation, only for that consultation to be suspended when the Executive collapsed.

Under 'normal'[4] circumstances, by this stage in the year the Executive would have:

- Completed the **consultation on the Draft Budget**, normally undertaken through the course of the previous financial year;
- Set a **Final Budget** that the Assembly would have debated and endorsed;
- Carried out and published the details of an **In-Year Monitoring Round in June.** This would have: modified the total spending envelope to reflect any change in the Executive's overall funding; allocated some centrally-held funding to specific departments; and reallocated some funding between departments to reflecting changing needs and priorities;
- **Legislated for the Final Budget** through a Main Estimates Budget Bill; and
- Carried out a further **In-Year Monitoring Round in October**.

This year, with the outgoing Executive failing to agree a Budget and then collapsing – but with 'caretaker' Ministers remaining in place under the NI (Ministers, Elections and Petitions of Concern) Act 2022 (MEPOC) – the process looks rather different:

- The Department of Finance gave each department an unpublished **'contingency planning envelope'** at the beginning of the year. These reflected baselines calculated from the previous year's allocation adjusted for any one-off factors, any ring-fenced funding for the current year and previous Executive commitments. With some funding held centrally for later allocation, the Minister said that departments *"were not constrained to these totals"* and that they *"should not make decisions to cease services where there was a reasonable expectation that they will receive further funding"*.
- In the absence of an agreed Budget, **spending decisions within departments** were taken initially by individual Ministers[5] and their top civil servants, with Ministers having the final say. The legal authority to spend in the early months of 2022-23 was initially provided under the Vote on Account in February 2022 as part of the Budget Act (Northern Ireland) 2022. This was capped at an amount equivalent to 45 per cent of voted provision in 2021-22 including Annually Managed Expenditure (AME). However, with

[4] By 'normal', we mean a year in which the budget process runs in practice as it should in theory. The reality is that, for a variety of reasons, it has been a long time since a normal year so defined has occurred.
[5] Under the Northern Ireland (Ministers, Elections and Petitions of Concern) Act 2022 https://www.legislation.gov.uk/ukpga/2022/2/contents/enacted

no Budget Bill agreed to provide legal authority for the remaining amount of spending in 2022-23, and no functioning Assembly in place to pass it, power to make these decisions passed to the Permanent Secretary of the Department of Finance in July (but operating under the direction of the Minister as he remained in place under the terms of MEPOC).

- The Department of Finance has **revised the Draft Budget** through the year, to the limited degree possible in the absence of an Executive. (In effect, this has also updated the initial contingency planning envelopes the departments were asked to work to.) The updates reflect policy decisions deemed to have been taken by the outgoing Executive as well as hypothecated funding received for particular purposes from the Treasury. Due to the lack of an Executive, none of this funding has formally been allocated to departments, as only the Executive (or Secretary of State) can do this, but departments need some indicative allocations to plan. We discuss this in more detail in chapters 3 and 4. The indicative allocations in the revised Draft Budget have not been published until this report, but they did inform the Finance Minister's 11 October 2022 Statement.

- The Permanent Secretary of the Department of Finance has used emergency powers granted under the NI Act 1998 to give departments **gradual access to the funding necessary to finance their spending**. In aggregate, departments are currently authorised to spend the equivalent of 65 per cent of their final planned Net Cash Requirement for last year (and 67 per cent of their Net Resource Requirement, which excludes net capital requirements but includes non-cash items such as depreciation, impairments and movements in provisions). But there are significant variations by department, with the proportion of Net Cash from last year authorised for spending ranging from 77 per cent for the Department of Agriculture, Environment and Rural Affairs to 45 per cent for the Department of Finance.

- On 11 October 2022, the Finance Minister issued a Written Ministerial Statement[6] which said that **departments were expecting to overspend** against their revised Draft Budget indicative allocations for resource spending (i.e. on the day-to-day costs of public services, grants and administration) by £961 million and that only £300 million could be offset by the allocation of centrally held funds. This is on the assumption that this funding is not used for another purpose such as a response to the rise in the cost of living. The Minister said that this financial position was *"hugely concerning"* and that he had asked Ministers *"to take appropriate steps to ensure that our spending remains within the overall budget provided to us"*.

- Under the terms of MEPOC, the 'caretaker' Ministers ceased to hold office on 28 October 2022, leaving civil servants alone to take the limited decisions permissible without an Executive. With the Secretary of State required soon

[6] http://www.niassembly.gov.uk/assembly-business/official-report/written-ministerial-statements/department-of-finance---2022-23-budgetary-position/

to call an Assembly election, the **NIO is now preparing to set a budget** for NI which the UK Parliament would be asked to legislate for.

In the analysis that follows, we provide further and more up-to-date detail of revised Draft Budget and forecast positions, based on information requested from the Department of Finance following the Minister's Statement. We set out the latest indicative departmental allocations (which are the same as those to which the Finance Minister referred implicitly) and the latest departmental spending forecasts (which are also slightly more up to date). And we do so for conventional capital and financial transactions capital (FTC) as well as resource spending. This allows us to update our assessment of whether the budget is still on course to be balanced (spoiler: it is not) and to assess the implications for what lies ahead.

The three sets of figures that we report and compare are:

- The **Draft Budget**: As we reported in January 2022,[7] the Draft Budget published in December 2021 'balanced' in the sense that proposed departmental spending allocations (including those held centrally to begin with) and forecast debt interest costs were fully covered by a combination of external (primarily Block Grant) funding, Regional Rates revenue and capital borrowing within the limits set down in legislation and subsequent agreement with the Treasury. And the Draft Budget balanced not just in total, but also in each subset of spending for which the Treasury sets separate control totals: namely, ring fenced resource, non-ring fenced resource, capital and FTC spending.
- The '**revised Draft Budget'**: On the funding side of the equation, the Block Grant funding available has increased since the Draft Budget in part because of the 'Barnett consequentials' of higher UK Government spending, while Rates revenue and borrowing costs have been updated. But the capital borrowing proposed in the Draft Budget through the Reinvestment and Reform Initiative (RRI) cannot be taken forward by Ministers in the absence of the Executive. On the spending side, the indicative allocations for all but one department have been increased by utilising centrally-held funding and Block Grant funding earmarked for particular purposes. But (as noted) the Department of Finance does not have the power to allocate this funding formally. The NIO or a returning Executive may take a different view.
- The '**latest forecast position'**: This represents the Department of Finance's latest assessment of where spending (and any gap between spending and funding) would end up based on departments' own September forecasts of their full year spending "barring interventions and policy changes". (Importantly, in this instance the departmental forecasts assume that recent UK-Government-agreed public sector pay settlements are implemented in NI.) As we shall see, resource and capital spending are projected to be higher than in the revised Draft Budget but funding slightly lower as the estimate of Regional Rates revenue has been reduced. When the Finance Minister referred to impending overspends in his Statement last month, he

[7] https://www.finance-ni.gov.uk/sites/default/files/publications/dfp/Northern%20Ireland%20Draft%20Budget%202022-25_0.pdf

was referring to the gap between the latest forecast position for funding and spending forecasts made by departments in August (i.e. a month earlier).

Resource spending

Non-ringfenced Resource spending (as the Treasury calls it) is the largest component of the Executive's budget and covers day-to-day spending on public services, grants and administration. Pay accounted for 57 per cent of this spending in 2019-20, prior to the distortions arising from the response to Covid-19. Table 2.1 shows how resource spending plans for 2022-23 (and the anticipated funding to pay for them) evolved between the Draft Budget and the revised Draft Budget and how this compares to the latest forecast position.

Table 2.1 - Non-ringfenced resource spending and financing

	Draft Budget	Revised Draft Budget[1]	Latest forecast position[2]	Change from Draft Budget (£ million)
FINANCING				
Block Grant	12,994	13,384	13,384	390
Regional Rates (post debt repayment)	577	595	580	3
TOTAL FINANCING	**13,571**	**13,980**	**13,964**	**393**
pays for				
SPENDING				
Departmental spending	13,484	13,633	14,557	1,073
Held centrally/unallocated Block Grant funding	42	303	14	-29
Debt interest (RRI)	46	43	43	-2
TOTAL SPENDING	**13,571**	**13,980**	**14,614**	**1,043**
NI Executive Underspend (+)/Overspend (-)	*0*	*0*	*-650*	*-650*

Notes:

[1] Includes the allocation of hypothecated Block Grant allocations from Treasury and previous Executive spending commitment funding held centrally at draft Budget

[2] Forecast outturn spending by departments implicitly includes the unallocated Block Grant funding (if included as unallocated then over spend calculation w ould be overstated)

Source: Department of Finance

From the Draft Budget to the revised Draft Budget

Table 2.1 shows that the Draft Budget made provision for £13,571 million of resource spending in 2022-23, almost entirely financed by the Block Grant but with the Regional Rates also contributing £577 million. Of this, £13,484 million was allocated to departments, £42 million held centrally for later allocation and £46 million earmarked for debt interest payments on past capital borrowing.

In the revised Draft Budget, overall funding available for resource spending in 2022-23 has increased by £408 million (or 3.0 per cent) to £13,980 million. This is very largely accounted for by £390 million of additional Block Grant income from the Treasury. This included £120 million in Barnett consequentials arising from increases in planned UK Government spending in 2022-23 and £100 million of funding from increases in UK Government spending in 2021-22 (that arose very late in the last financial year), plus £68 million in funding earmarked for specific purposes and £102 million of funding that the Executive carried forward under the Treasury's 'Budget Exchange' scheme having underspent its control total last year (see Table A.1 in the Appendix for more detail). The net increase in funding also reflects a £6 million reduction to pay for an Assembly election. Beyond the Block Grant, expected revenue from Regional Rates rose by £18 million to £595 million.

Compared to the original Draft Budget, an additional £150 million has been allocated indicatively to specific departments in the revised Draft Budget – £124 million from funding earmarked for particular purposes by the Treasury and £26 million from centrally held funds. As Table 2.2 shows, the Department of Health is the biggest recipient in cash terms and the Department of Finance the biggest in percentage terms. The Department for Communities has seen its allocation reduced.

Table 2.2 - Indicative resource spending allocations

				£ million
	Draft Budget	Revised Draft Budget	Change	Change (%)
Health	6,782	6,863	81	1.2
Education	2,431	2,447	16	0.6
Justice	1,118	1,125	7	0.6
Communities	839	819	-20	-2.4
Economy	832	861	29	3.4
Agriculture etc.	551	571	20	3.7
Infrastructure	444	447	3	0.6
The Executive Office	211	212	1	0.5
Finance	168	179	10	6.1
Minor departments	107	111	3	3.2
Departmental spending	**13,484**	**13,633**	**150**	**1.1**
Held centrally/unallocated Block Grant funding	42	303	261	619.6
Debt interest (RRI)	46	43	-2	-4.6
TOTAL SPENDING	**13,571**	**13,980**	**408**	**3.0**

Source: Department of Finance

Table 2.3 shows the contributors to the changes. The bigger items include £45 million of earmarked Treasury funding for the implementation of the NI Protocol and £43 million of earmarked funding attached to past political agreements. The largest single item is £50 million of additional funding for the Department of Health. This was neither referred to in the Draft Budget nor earmarked for this department by Treasury, so we assume that there was sufficient Executive-level cover of this issue for the Department of Finance to feel it was able to make this addition.

Table 2.3 - Indicative allocations to departments since Draft Budget

	£ million	Source of funding
Funded from additional Treasury Block Grant allocations		
In-Year Monitoring commitment to Department of Health	50.0	Funding from available funding, primarily additional non-earmarked Block Grant allocations from Treasury
NI Protocol	45.7	Earmarked £44.9 million Block Grant allocation from Treasury
IFRS 16	-32.6	Earmarked £33.5 million Block Grant deduction from Treasury in respect of change in accounting treatment of leases
Confidence & Supply	30.0	Earmarked £30.0 million Block Grant allocation from Treasury in respect of Mental Health and Severe Deprivation
Budget Cover Transfers	23.5	Earmarked £23.5 million Block Grant allocation from Treasury for Immigration Health Surcharge, Debt Advice and Assembly election
NDNA - Magee	3.8	Earmarked £3.8 million Block Grant allocation from Treasury for medical school
New Deal for NI	3.5	Earmarked £23.5 million Block Grant allocation from Treasury for Invest NI
Sub-total	**123.9**	
Allocation of funding previously held centrally as Draft Budget[1]		
Targeting Paramilitary Activity	13.0	£13.0 million held centrally in Draft Budget
EU Matched funding	7.2	£11.0 million held centrally in Draft Budget
NDNA - Magee	5.5	£5.0 million held centrally in Draft Budget for medical school
Sub-total	**25.8**	
Total	**149.7**	

Note:

[1]Funding held at Draft Budget that has not yet been allocated- £7.7 million for Delivering Social Change, £1.3 million for Collaborative procurement and £4.1 million for NDNA- Communities in Transition w ith new £1.2 million centrally held funding for Cyber Security (Ringfenced Block Grant allocation)

Source: Department of Finance and HM Treasury

Given the restrictions placed on the Department of Finance in the absence of a functioning Executive, most of the Block Grant increase so far this year has had to be added to the centrally held pot for later allocation. This has increased it from £42 million at the Draft Budget (with the largest element being £13 million for Tackling Paramilitary Activity) to £303 million in the revised Draft Budget (compared to the £13,633 allocated to specific departments). Meanwhile the expected debt interest bill on past capital borrowing fell by £2 million to £43 million.

From the revised Draft Budget to the latest forecast

Table 2.1 shows that the latest forecast for the resource funding envelope is very slightly lower than in the revised Draft Budget at £13,964 million, reflecting a £15 million reduction forecast revenue from Regional Rates. The latest forecast for departmental spending of £14,571 million (made up of £14,557 plus the £14 million that continues to be held centrally) is £937 million higher than the sum allocated to specific departments in the latest budget position and £634 million higher than the sum allocated to departments or held centrally. (Taking the drop in expected revenue from the Regional Rates into account, this implies a £650 million shortfall against forecast available funding.) This is on the assumption that the funding held centrally in the revised Draft Budget is used to offset the forecast level of overspend by departments, rather than providing additional support to households and businesses in response to the rising cost of living. (Relative to the original Draft Budget published last year, departmental resource spending is forecast to be £1,043 million higher, reflecting the £393 million of additional funding incorporated in the revised Draft Budget and the £650 million of projected overspending against that position.)

The total projected overspend is slightly lower than the £661 million quoted in the Finance Minister's Written Ministerial Statement on 11 October 2022. This is because departments reduced their forecast spending by £27 million between the August Forecast Outturns (net of the £10 million emerging underspend on Victims pensions that had already been included) used by the Minister and the September returns we have been able to use, partly offset by the £15 million reduction in Rates revenue.

So where does the £634 million projected overspend against the indicative allocations in the revised Draft budget come from? Table 2.4 (and Chart 2.1 below) compare the latest forecast position for each department (and the centrally held pot) with those allocations.

Table 2.4 – Revised Draft Budget resource allocations and latest forecast position

	Revised Draft Budget	Latest Forecast Position	Overspend[1]	£ million Overspend (%)
Health	6,863	7,313	450	6.6
Education	2,447	2,715	268	11.0
Justice	1,125	1,211	86	7.7
Economy	861	829	-32	-3.7
Communities	819	879	59	7.2
Agriculture etc.	571	580	9	1.5
Infrastructure	447	552	105	23.5
The Executive Office	212	178	-34	-16.0
Finance	179	185	7	3.8
Minor departments	111	116	5	4.5
Departmental spending	**13,633**	**14,557**	**924**	**6.8**
Centrally held	303	14	-	-
Debt interest (RRI)	43	43	-	-
TOTAL SPENDING	**13,980**	**14,614**	**634**	**4.5**

Note:
[1] (-) represents an underspend

Source: Department of Finance

The Department of Health accounts for almost half the projected overspend against the revised Draft Budget allocations, which is not entirely surprising at is by far the largest component of the Executive's resource spending. In percentage terms, its projected overspend of 6.6 per cent is broadly in line with the average for all departments. In our recent Health Sustainability Report we estimated that Health spending per head of population in NI was 2.9 per cent lower than in England. The revised Draft Budget position has seen this deficit fall to 1.4 per cent. Health's forecast outturn would see NI spending 4.5 per cent higher than in England this year. Even if this level of funding could be found for Health (which is far from certain) it would provide only a temporary boost - in 2023-24 health spending is expected to again fall below that in England, by 2 per cent.

The highest rate of overspend is 23.5 per cent for the Department for Infrastructure followed by 11.0 per cent for the Department of Education. In cash terms the forecast overspend for the Department of Education is £268 million, but in response to an assembly question the Minister for Education said on 17 October 2022 that her department was facing *"a very significant overspend of up to c.£370 million"*, so the position may have further worsened.[8] Interestingly, within the Minor Departments the NI Assembly is forecasting a £1.1 million overspend against its Revised Draft Budget allocation even though it has not been sitting this year.

Two departments report that they expect to underspend against their revised Draft Budget allocations. In the case of The Executive Office this reflects the underspend on victims' pensions referred to in the Ministerial Statement. In the case of the

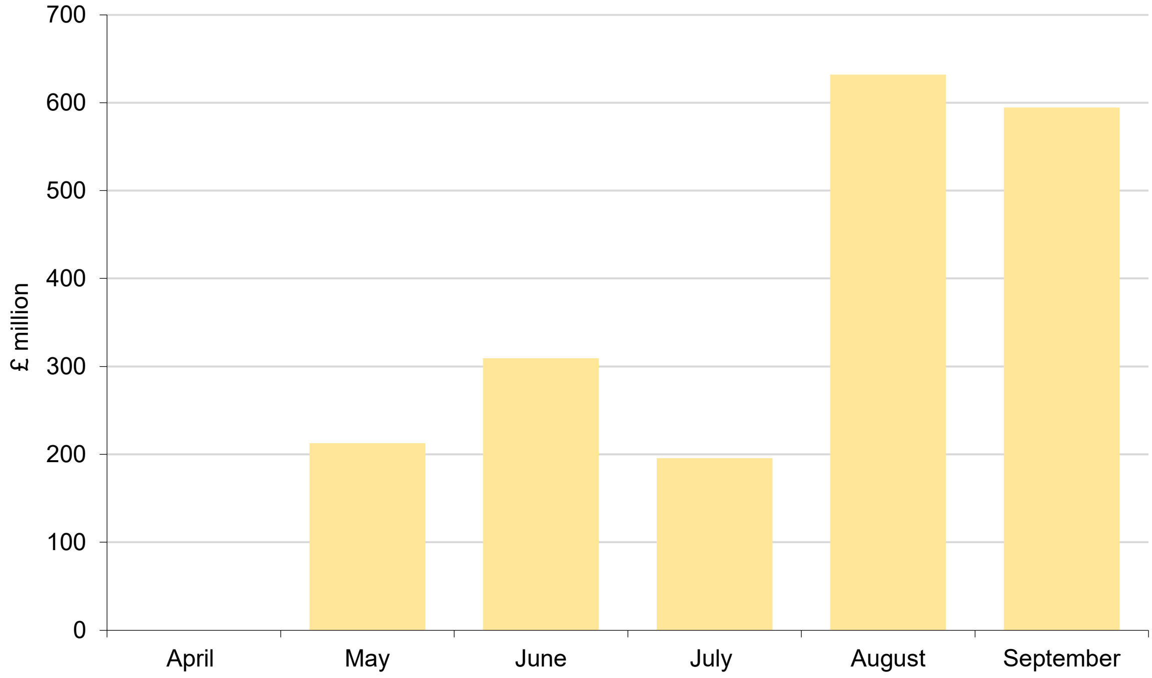
[8] AQW 4438 22-7 with a £390 million projected overspend reported in the response to AQW 3205 22-27 on 5 October 2022 http://aims.niassembly.gov.uk/questions/writtensearchresults.aspx?&qf=0&qfv=1&ref=AQW%204438/22-27

Department for the Economy, it reflects the reclassification of £55 million in research and development spending from resource to capital which also contributes to the large capital overspend for the Department set out in Table 2.6 below.

A large part of the expected overspend for most departments reflects public sector pay uplifts, but these settlements have not yet been agreed in the absence of an agreed NI Executive public sector pay policy. The rate of over (or under) spend for individual departments will depend on a range of factors, including the change in their budget plans compared with previous years, the proportion of spending accounted for by labour and energy costs, as well as the approach they take to controlling increasing costs and securing efficiency savings. However, the variation in the rates of overspend is greater than would be expected just from common cost pressures. We discuss other potential factors later in this paper.

The Department of Finance provides forecasts to the Treasury each month of the aggregate over- or under-spend against the Resource Departmental Expenditure Limit control total set by the Treasury, in effect what can be financed consistent with the Block Grant. As Chart 2.1 shows, the projected overspend fluctuated in the early months of the financial year to reach £196 million in July, but it then jumped to £632 million in August and £595 million in September following the UK pay review body recommendations, on the assumption that these would be implemented in NI. These overspends are smaller than the £661 million set out by the Minister for August and the £650 million set out by us for September, because the forecast submissions were based on the higher Block Grant that was anticipated before the Treasury withdrew the Barnett consequentials of the UK energy support package when it was decided that this would be delivered by the UK Government rather than by the devolved administration (See Table A.1).

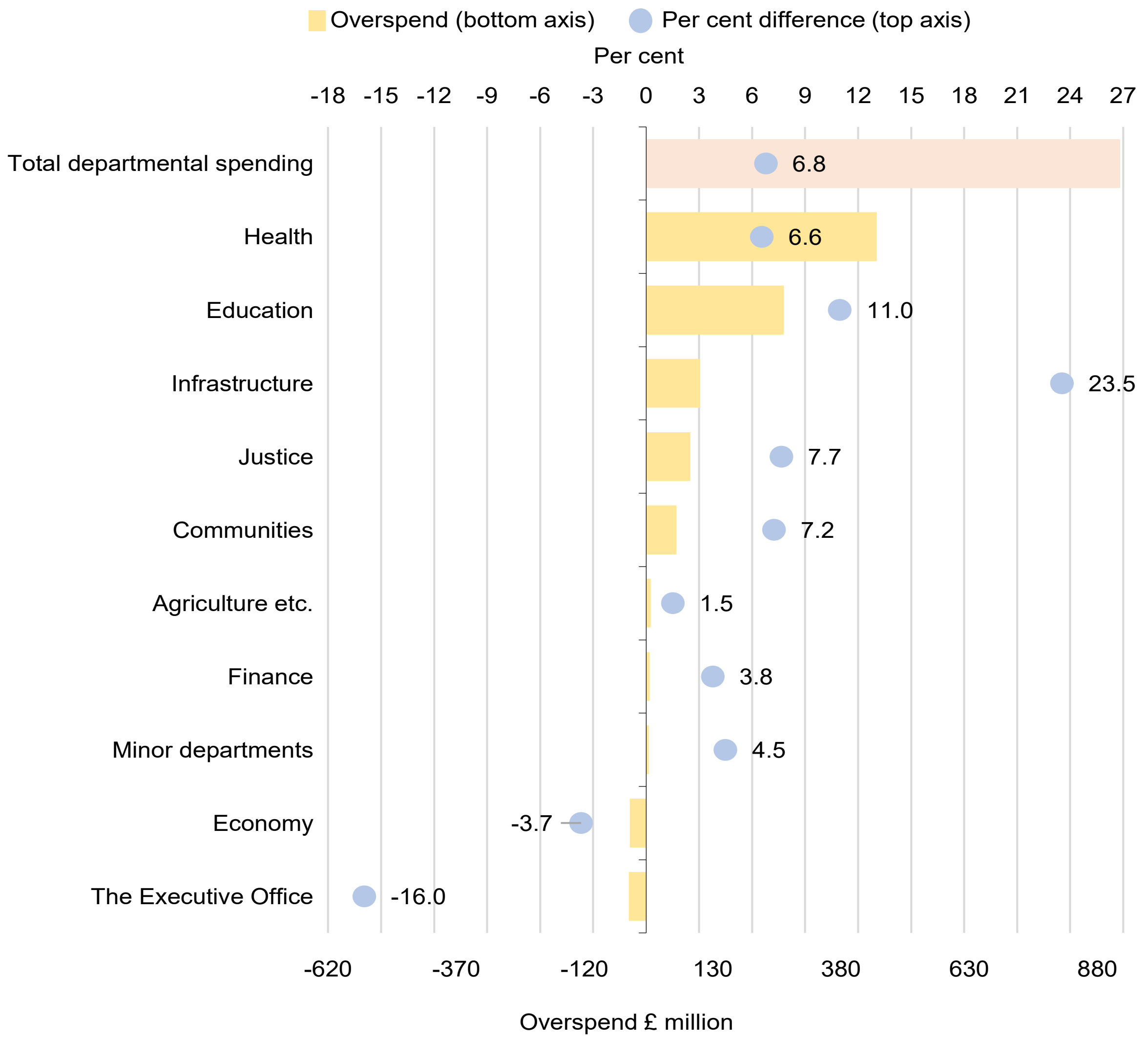
Chart 2.1 – Projected resource overspends in 2022-23 as reported to Treasury



Source: Department of Finance

The Finance Minister said in his Statement that the budget position was "*hugely concerning*" and that "*steps must be taken now to ensure an incoming Executive is not faced with a scenario where it cannot manage its budget within Treasury control totals*". However, he also advocated additional allocations for public sector pay and the Departments of Communities, Health, Education and Justice, but did not suggest where the near-term economies necessary to balance the budget should come from.

Chart 2.2 – Forecast overspends against the latest budget position for resource spending



Source: Department of Finance

Other spending categories

While the main focus of the Executive's Budget is on non-ringfenced resource spending, the Treasury also sets control totals for: conventional capital (investment in infrastructure, plant, machinery and the like); FTC (which can only be used to make loans or investments in the private sector); and Ringfenced Resource spending (which covers depreciation and impairment of existing assets).

In this section we summarise the evolution of the first two categories from Draft Budget to revised Draft Budget to the latest forecast position. We omit Ringfenced Resource as this is a 'non-cash' number and unlikely to require urgent policy decisions by the Secretary of State or a restored Executive.

Conventional capital spending

Table 2.5 shows that Draft Budget made provision for £1,991 million of capital spending in 2022-23, mostly financed by the Block Grant but also partly from £140 million of planned capital borrowing under the Reinvestment and Reform Initiative (RRI) and £7 million of Irish Government funding for the A5 road project. Of this, £1,976 million was allocated to departments and £15 million held centrally.

In the revised Draft Budget, the total funding for capital spending has fallen by £125 million to £1,866 million. This is more than explained by the fact that the £140 million of capital borrowing planned at the Draft Budget cannot take place in the absence of an Executive and that the £7 million of Irish Government support for the A5 road project will not now be needed this year. Partially offsetting these developments, the Block Grant has increased by £22 million to £1,866 million with additional funding in respect of IFRS 16 change in the accounting treatment for leases and the carrying forward of a £25 million underspend in 2021-22 through the Budget Exchange scheme partly offset by lower earmarked funding.

However, the amount allocated to departments in respect of the IFRS 16 is £9 million less than the funding being provided by Treasury and it is assumed that this will be returned to Treasury with an associated reduction made to the Block Grant to £1,857 million.

On the spending side, the revised Draft Budget allocated a net additional £23 million to departments and no longer kept £15 million in the central pot – giving an overall increase of £8 million. The Department of Health's indicative allocation increased by £25 million, but Department for Infrastructure's fell by £14 million.

Table 2.5 - Conventional capital spending and financing

				£ million
	Draft Budget	Revised Draft Budget[1]	Latest forecast position	Change from Draft Budget
FINANCING				
Block Grant	1,844	1,866	1,857	13
Capital borrowing RRI	140	0	0	-140
Irish Government funding for A5	7	0	0	-7
TOTAL FINANCING	**1,991**	**1,866**	**1,857**	**-134**
pays for				
SPENDING				
Departmental spending	1,976	1,999	2,043	67
Held centrally/unallocated Block Grant funding	15	0	0	-15
TOTAL SPENDING	**1,991**	**1,999**	**2,043**	**52**
NI Executive Underspend (+)/Overspend (-)	*0*	*-133*	*-187*	*-187*

Note:

[1]Assumption is that all funding held centrally will be used to offset departmental overspend

Source: Department of Finance

In their September returns, departments forecast that they would overspend their indicative allocations by £45 million (or 2.2 per cent). Factoring in the absence of planned capital borrowing and the A5 money, this implies an overspend against available funding of £187 million – proportionately higher than for resource.

Table 2.6 shows that the biggest projected capital overspend is by the Department of the Economy at £66 million or 36.3 per cent of its latest budget position. But this reflects a reclassification of research and development spending from resource to capital which (as noted above) also explains why the Department is projecting an underspend on resource. The second biggest projected over-spender is Infrastructure at £26 million, but as the largest capital spender this amounts to only 3.4 per cent of its latest funding position. Health, Education and Justice all expect to underspend against their revised Draft Budget allocations.

Table 2.6 - Revised Draft Budget capital allocations and latest forecast position

				£ million
	Revised Draft Budget	Latest Forecast Position	Overspend[1]	Overspend (%)
Infrastructure	753	779	26	3.4
Health	375	360	-15	-3.9
Communities	229	236	6	2.8
Education	200	184	-15	-7.6
Economy	183	250	66	36.3
Justice	106	83	-22	-21.2
Agriculture etc.	92	101	9	9.8
Finance	37	35	-3	-7.4
The Executive Office	16	10	-6	-37.6
Minor departments	8	6	-2	-22.8
Departmental spending	**1,999**	**2,043**	**44**	**2.2**
Centrally held	15	0	-	-
TOTAL SPENDING	**2,014**	**2,043**	**29**	**1.4**

Note:
[1] (-) represents an underspend

Source: Department of Finance

In setting a Budget, the Secretary of State for Northern Ireland (or a restored Executive) will have to decide whether to undertake the planned level of borrowing or perhaps even to increase it to manage the projected overspend (which would be achievable within the £200 million annual limit on borrowing agreed with the Treasury in 2002). The UK Government has tended not to borrow when it is setting the NI Budget, except to cover redundancy payments that were already agreed.

While the NI Act precludes overcommitment of the Block Grant, projected capital overspends are not unusual at a departmental level at this point of the year and almost one quarter of all capital spending in the current financial year is projected to occur in March 2023. If this year-end surge were to be tempered, the need to borrow would be reduced.

Financial Transactions Capital spending

As we have discussed in previous publications, Block Grant funding for Financial Transactions capital (FTC) spending arises largely from the Barnett consequentials of UK Government measures to support the housing market and neither the Executive nor the other devolved administrations have found it easy to spend as it is not a particularly convenient way to address their investment priorities.

Table 2.7 shows that the Draft Budget anticipated £163 million of Block Grant funding for FTC spending this year, with only £56 million allocated to departments and the rest held centrally. In the revised Draft Budget the funding had increased by a further £62 million to £225 million, which was added to the centrally held pot.

Table 2.7 - Financial transactions capital spending and financing

				£ million
	Draft Budget	**Revised Draft Budget[1]**	**Latest Forecast Position**	**Change from Draft Budget**
FINANCING				
Block Grant	163	225	225	62
TOTAL FINANCING	**163**	**225**	**225**	**62**
pays for				
SPENDING				
Departmental spending	56	56	44	-12
Held centrally for later allocation/unallocated Block Grant funding	107	169	0	-107
TOTAL SPENDING	**163**	**225**	**44**	**-119**
NI Executive Underspend (+)/Overspend (-)	*0*	*0*	*181*	*181*

Note:
[1]Assumption is that none of the funding held centrally w ill be spent

Source: Department of Finance

Table 2.8 shows that Communities and (to a far lesser extent) Economy are the only departments allocated FTC funding and they both expect to underspend against their revised Draft Budget allocations by significant margins. With the central pot likely to be unspent as well, FTC spending is forecast to be only £44 million compared to available funding of £225 million. With the Treasury maintaining separate control totals, some of this underspend could be carried forward to next year but it cannot be used to offset the projected resource and conventional capital overspends.

Table 2.8 - Revised Draft Budget FTC allocations and latest forecast position

	Revised Draft Budget	Latest Forecast Position	Overspend[1]	£ million Overspend (%)
Communities	52	38	-14	-26.5
Economy	3	2	-1	-40.4
Agriculture etc.	0	0	0	0
Education	0	0	0	0
Finance	0	0	0	0
Health	0	0	0	0
Infrastructure	0	0	0	0
Justice	0	0	0	0
The Executive Office	0	3	3	0
Minor departments	0	0	0	0
Departmental spending	**56**	**44**	**-12**	**-21.4**
Centrally held	169	0	-	**-**
TOTAL SPENDING	**225**	**44**	**-181**	**-80.4**

Note:
[1] (-) represents an underspend

Source: Department of Finance

3 How did we get here?

In the previous chapter, we described how the Department of Finance has updated the indicative spending allocations provided to NI departments in the Draft Budget in the limited fashion permissible in the absence of an Executive. But departments now expect to overspend these allocations and the available funding by unusually significant sums for both resource and conventional capital, but (as is usually the case) they do not expect to spend the funding available for FTC spending

So why have the projected overspends for resource and conventional capital spending emerged? In this chapter we explore two main explanations;

- **Inflation and pay pressures** faced by all NI departments (and indeed their counterparts in Whitehall and in the other Devolved Administrations).
- The **weakening of budgetary control and management mechanisms** specific to NI when there is no functioning Executive and Assembly.

Inflation and pay pressures

When we commented on the 2022-25 Draft Budget in January 2022, we noted that the spending plans were covered by anticipated funding and permitted borrowing (thereby balancing the budget in that sense) but that upward pressures on spending from higher inflation could unbalance it again. That risk has now crystallised.

Inflation affects the running costs of the public sector through the direct cost of inputs (such as energy), through upward pressure on pay settlements (to limit the squeeze on public sector workers' living standards) and through the costs of procured goods and services (which themselves reflect these same pressures).

Inflation and average earnings growth are both running much more strongly than the Treasury and the NI Executive anticipated when the Block Grants and Draft Budget spending plans for 2022-25 were set. The average independent forecasts made in the preceding 3 months for CPI inflation through 2022 and average earnings growth in 2022 were 10.4 and 5.8 per cent respectively in October, compared to 3.1 and 4.0 per cent respectively in December 2021.[9] Energy costs have risen particularly strongly, with the price of heating oil rising by 89 per cent in the year to October. [10]

The main cost of delivering public services is staff costs, where higher inflation is putting upward pressure on settlements. The 2022 UK pay review body recommendations for NHS staff (expected to be the subject of industrial action) are

[9] https://www.gov.uk/government/collections/data-forecasts#2022
[10] 20 October 2022 price of 900 litres of £888.20 compared with 21 October 2021 price of £469.93 https://www.consumercouncil.org.uk/homeheatingoilpricechecker/tool/archive

expected to increase the pay bill by around 4.8 per cent across the UK,[11] with a 4.5 per cent increase in salary scales recommended for doctors.[12] Other pay review bodies have recommended a 5 per cent increase in pay costs for police officers[13] (England & Wales only) and a 5 per cent increase in pay and allowance ranges for teachers (England only).[14]

The spending forecasts submitted by NI departments in the wake of these recommendations appear to assume their implementation in NI, hence the jump in the projected overspend reported to the Treasury between July and August that we referred to in the previous chapter. But the Finance Minister noted in his 11 October 2022 Written Ministerial Statement to the Assembly that "*…public sector pay policy needs to be put in place before pay awards can be progressed*". In the absence of an Executive, he indicated that this was not possible. If and when the Executive is restored, "*to provide a pay award to staff it would be necessary to reduce spending in other areas*." But there is no sign that departments have identified other economies to help fund higher pay settlements. In the absence of an Executive, Ministers have not been in a position to reach a collective judgement on the trade-off between the amount that public sector workers can be paid and the number of them that can be employed within a given pay-bill or overall budget envelope.

The impact of higher energy and pay costs on the NI budget depends in part on how the UK Government responds to them in the forthcoming Autumn Statement on 17 November 2022. Given that public services are confronting the same cost pressures in England, the Treasury might decide to provide more money for public services this year (presumably followed by greater savings in later years). This would ease the immediate budget pressures in NI by increasing the Block Grant through the operation of the Barnett Formula. But so far it has indicated no desire to do so. NI has more public sector workers per head of population than England, which means that any additional Barnett consequentials are unlikely to be sufficient to address the full cost of implementing the same pay award in NI as in England.

Weak budget control in NI without an Executive

In previous chapters we have mentioned various ways in which the processes of budget control, management and scrutiny have been affected by the failure of the outgoing Executive to agree a budget, its subsequent collapse and the role of caretaker ministers and senior civil servants in taking spending decisions. We have noted in other reports that even in normal times the Department of Finance is in a less powerful position than the Treasury to control departmental spending. A strong case can be made for saying that spending control is even weaker under the current political and constitutional circumstances than in normal times – something that the NI Executive and UK Government might both wish to think about before they arise again. In this section we consider a few potentially contributing factors.

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[11] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1092270/NHSPRB_2022_Accessible.pdf
[12] https://www.gov.uk/government/publications/review-body-on-doctors-and-dentists-remuneration-50th-report-2022
[13] https://www.gov.uk/government/publications/police-remuneration-review-body-report-2022-england-and-wales
[14] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1092278/STRB_32nd_Report_2022_Accessible.pdf

Statutory constraints on departmental spending

The Budget process sets administrative limits on departmental spending, but the legislative authority to spend is conferred through the Estimates process and Budget Acts which set limits in terms of Net Resource and Net Cash required.

The issue of funds from the Consolidated Fund at the beginning of the 2022-23 financial year was provided for under the Vote on Account and Spring Supplementary Estimates, reflected in the Budget Act (Northern Ireland) 2022.[15] This was passed before the Assembly collapsed on 8 March 2022, with Royal Assent received on 24 March 2022. The Act authorised spending of up to 45 per cent of the total voted provision for 2021-22, namely £11,091 million in terms of the Net Resource requirement and £9,822 million Net Cash required.[16] The spending approved as part of the Estimates process also includes Annually Managed Expenditure (mostly on pensions and social security benefits) which equates to 45 per cent of NI Executive Total Managed Expenditure in 2022-23. So this cannot be directly compared with the Draft Budget estimates and forecasts discussed earlier.

In the absence of a subsequent Budget Bill and an Assembly to pass it, the power to issue funds passed in July under emergency powers to a designated officer[17] of the Finance Department (in practice the Permanent Secretary, albeit still under the direction of his caretaker minister until 28 October 2022). These powers were first used on 24 August 2022, authorising departments to spend up to 60 per cent of the provision for the previous year (later increased to 65 per cent). But Section 59(4) of the NI Act and Section 7 of the Government Resources and Accounts Act (Northern Ireland) 2001 allows the Permanent Secretary to increase this up to 95 per cent in advance of a Budget Bill being passed.

The autonomy of caretaker Ministers

The NI Act 1998 makes it clear that a Budget cannot be agreed in the absence of a functioning Executive.[18] But for as long as caretaker Ministers remain in place under the NI (Ministers, Elections and Petitions of Concern) Act 2022 (MEPOC), they can still direct their Accounting Officers (their Permanent Secretaries) to spend on areas where Executive agreement is not needed.

Managing Public Money Northern Ireland (MPMNI)[19] – which *"sets out the main principles for dealing with resources used by public sector organisations"* – requires Accounting Officers to ensure that spending (and other) decisions are not irregular, improper or offer poor value for money. It says that Accounting Officers should bring any conflict or concerns that arise between their Minister's instructions and

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[15] https://www.legislation.gov.uk/nia/2022/6/enacted#:~:text=Budget%20Act%20%28Northern%20Ireland%29%202022%202022%20CHAPTER%206.,years%20ending%2031%20March%202022%20and%202023%3B%20to
[16] https://www.finance-ni.gov.uk/sites/default/files/publications/dfp/NI_estimates_vote_on_account_2022-23.pdf This places limits by Request for Resources (i.e., by department and main pension schemes) in terms of Net Resources required on account and Cash required on account.
[17] Section 59 of NI Act 1998: https://www.legislation.gov.uk/ukpga/1998/47/contents
[18] https://www.legislation.gov.uk/ukpga/1998/47/section/64
[19] https://www.finance-ni.gov.uk/sites/default/files/publications/dfp/managing-public-money-ni-chapters.pdf section 3.4

their own duties to the attention of their Minister.[20] If, despite their advice, the Minister decides to continue with a course of action, the Minister can issue a formal Ministerial Direction instructing the Accounting Officer to proceed. (Accounting Officers – not just in NI – sometimes seek Directions for decisions that they themselves regard as sensible and appropriate but want formal cover for.)

As Table 3.1 shows, Ministerial Directions have been issued for spending decisions worth £345.4 million so far this financial year, the vast majority by the Minister of Health – who presides over the biggest spending department.

Table 3.1 – Ministerial Directions requested and approved in 2022-23

		£ million
	Requested	**Approved**
Health	280.3	-
Communities	22.6	-
Education	20.9	20.9
Justice	20.0	-
Agriculture etc.	1.6	1.6
Total	**345.4**	**22.5**

Source: Department of Finance

On receiving a Ministerial Direction, the usual course of action is for approval to be sought from the Finance Minister or the Executive. If confirmed, the Accounting Officer then informs the Comptroller and Auditor General, who brings it to the attention of the Public Accounts Committee (PAC). Following discussion at PAC, Ministerial Directions are published. In the absence of an Executive, Directions were submitted to the Finance Minister but he had approved only £22.5 million of them before he and the other caretakers left office on 28 October 2022. In the absence of a functioning PAC, those he has approved have not been discussed or published.

The spending for which Directions have been sought is equivalent to around half the projected resource overspend. The £22.5 million of spending for which the Finance Minister has agreed to the Direction was presumably included in departments' September Forecast Outturns. But it is impossible to know how much more was – and therefore how much of the remaining spending for which approval has been sought is a contributor to the projected overspend and how much is an additional risk on top. As we describe below, Ministers have been told not to include *"aspirational"* spending in their forecasts even if they regard it as a priority.

[20] Examples where it is appropriate to seek Ministerial Direction include where there are concerns or conflicts around Regularity (where the proposal is outside the legal powers, delegations or agreed budgets), Propriety (where the proposal would breach Assembly control procedures), Value for Money, and / or Feasibility (where there is doubt around the proposal being implemented accurately, sustainably and within intended timeframe)

Guidance from the Department of Finance

As part of its on-going management of the NI public finances, departments provide the Department of Finance with monthly reports on their expected spending for the whole financial year - the Forecast Outturns to which we have already referred.

Ordinarily departments are prohibited from forecasting higher spending than they have been allocated. In other words, they have to determine how to live within their allocations, by reallocating internally and, where necessary, by bidding for additional resources at the In-Year Monitoring Rounds which normally take place three or four times a year. Without formal allocations to hold departments to, this discipline is absent as the Department of Finance's guidance on reporting reflects.

The Department of Finance issues (and indeed publishes) reporting guidance to departments at the beginning of each financial year. That for 2021-22 stated;

> *"Departments must treat all allocations set in the course of the Budget process as ceilings, and should seek to manage their activities to contain spending within those ceilings, unless and until any increase is agreed by the Executive.*[21]

The guidance for 2022-23 was sent to departments in April this year (but not published) and then updated on 15 August 2022. Rather than instructing departments not to forecast breaches of the indicative resource, capital and FTC allocations in the updated Draft Budget, it said that forecasts *"should be based on your current spending trajectory but must not include any aspirational spend i.e. expenditure which will be incurred only if additional funding is secured. This is important even if this aspirational expenditure is a Ministerial priority."* Compared to the recording of expenditure against what previously represented a hard budget constraint for each department - their budget allocations - we see a much weaker position reflected in the guidance this year. The guidance also explained that:

> *"The Finance Minister has emphasised the importance of not making decisions to cease services where there is a reasonable expectation that the department will receive further funding later in the financial year once a Budget is put in place. This must however be balanced not committing to expenditure which would put the department on a spending trajectory that would pose a risk to the Block."*

The absence of In-Year Monitoring Rounds itself weakens budget control by removing an opportunity for systematically reprioritising and redistributing resources between departments in response to emerging pressures or changing priorities. In the absence of an Executive, the Finance Minister cannot carry out Monitoring Rounds unilaterally as Section 2.4 of the Ministerial Code[22] places a duty on Ministers to bring to the attention of the Executive Committee any matters that cut across the responsibilities of two or more Ministers, require agreement on prioritisation or requires the adoption of a common position.

At the same time, the Draft Budget proposals did not represent a material change in the prioritisation of funding between departments that had been made in previous years and they would have been aware how much additional Block Grant funding

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[21] https://www.finance-ni.gov.uk/sites/default/files/publications/dfp/2021-22%20In-Year%20Monitoring%20of%20Public%20Expenditure%20-%20Guidelines.pdf
[22] https://www.northernireland.gov.uk/topics/your-executive/ministerial-code

had become available subsequently. On that basis, departments should have had a reasonable idea of the funding that they would have received if a Final Budget had been agreed and legislated for, which might have been expected to inform their spending decisions throughout the year. But the level of expenditure currently being forecast does not appear to reflect a reasonable estimate of the resources likely to be available. For example, the overspend forecast by the Department of Health is more than all the unallocated funding available to the NI Executive.

Lack of Assembly scrutiny

One of the consequences of the parties not electing a Speaker to the Assembly, is that Assembly Committees could not be formed. The overall Forecast Outturn position is usually presented monthly to the Finance Committee and published by the NI Assembly on its website. The individual committees also regularly review the position for each department. In the absence of the Finance Committee, the monthly Forecast Outturn is not currently scrutinised or published by the Assembly. This lack of scrutiny may at the margin help explain how the projected overspend has escalated to the surprising levels set out by the Finance Minister and updated here.

4 What happens next?

With NI departments on course for a significant overspend against available funding, the caretaker ministers now removed from office and an Assembly election looming at some point in 2023, what happens next? In this chapter we examine:

- How the budget for the **rest of this year** may be managed and legislated for; and

- The potential implications of this year's overspend for **future years**.

A belated Budget for 2022-23

Because of the continuing absence of an agreed Budget for 2022-23, there has been no legislative authority for spending since the Vote on Account was passed late in the last financial year apart from through the use of emergency powers (discussed in the last section). There are no full year Estimates in place to give departments formal allocations (with spending ceilings) to manage, monitor and forecast against.

Emergency powers can only provide authority to spend up to 95 per cent of last year's provision (with the current authorisation at 65-67 per cent). Legislative intervention is needed to go above this level, which might well be necessary. Some hint of the consequences of these limits being reached is provided by government shutdowns in the United States, most significantly in 1995-96, 2013 and 2018-19, when an appropriation (Budget) bill was not agreed before the start of the fiscal year and federal employees were furloughed. The consequences would be more serious for NI given that more services are provided by the public sector.

We assume that the Northern Ireland Office (NIO) will intervene to regularise this position, in effect taking on the task of setting and legislating for the Budget that the Stormont institutions have not been in place to fulfil. The most likely first step will be for the Secretary of State to announce a set of budgetary allocations via a Written Ministerial Statement. This happened in March 2018, when the then Secretary of State issued a statement which set out departmental allocations for 2018-19.[23] The NIO is already gathering information from departments to prepare for this.

One important decision will be whether to wait for the UK Government Autumn Statement on 17 November 2022 before setting a budget. If the Treasury decides to increase public services spending in the short term to address inflation and pay pressures (while almost certainly announcing cuts over the longer term), this could generate Barnett consequentials and increase the Block Grant – thereby reducing the projected overspend against available funding (Based on the allocations at the 2021 Spending Review the Chancellor would need to increase UK government equivalent resource spending by £6.5 billion or 2.1 per cent to generate £200million in additional Barnett consequentials for the Executive in 2022-23).

[23] https://www.gov.uk/government/news/written-ministerial-statement-northern-ireland-finances

To provide the legal authority for spending against his announced allocations, the Secretary of State is then likely to introduce NI Estimates and Budget legislation at Westminster.[24] In 2018, the Secretary of State announced a 2018-19 Budget by Written Ministerial Statement,[25] and the Department of Finance published some explanatory material in a Press Release[26] and tables containing departmental allocations.[27] The Secretary of State may also introduce legislation to confirm the powers of NI Permanent Secretaries to take decisions, as in previous periods of political uncertainty.[28] Without such legislation, the 'Buick judgment'[29] (No. [2018] NICA 26) in July 2018 by the NI Court of Appeal (in the case of a decision made by a NI Permanent Secretary to approve a planning application for a major waste treatment centre and energy from waste incinerator) makes it clear that Permanent Secretaries cannot exercise the powers of Ministers in their absence.

In setting a Budget, the Secretary of State will have to address various outstanding issues that would normally require the Executive to exercise collective authority:

- **Public sector pay** remits would usually be set by the Executive, in many cases on the basis of recommendations by independent pay review bodies often at the UK level. As we have discussed, the assumption that NI departments will implement these recommendations is the major reason why the projected resource overspend jumped in the summer. The Secretary of State will have to decide whether to reflect these in his allocations.

- The absence of the Executive has meant that **in-year additions to the Block Grant** have not formally been allocated to departments. (Indeed, in the absence of a Budget, no formal allocation of funding has been possible.) But the Finance Minister made clear in his Statement what some of his priorities would be when it did become possible to allocate the funding. In setting his allocations, the Secretary of State will have to judge his own priorities.

- NI departments cannot undertake **capital borrowing** under RRI without an Executive decision. In the absence of this borrowing the projected capital overspend against available funding rises from £47 million to £187 million. In the past, the UK Government has been reluctant to borrow in the absence of the Executive (because of the future calls it makes on the Executive's resources). But the Secretary of State may feel it is appropriate to do so this year because of the overspend position. Treasury rules normally allow capital borrowing of up to £200 million in any single year.

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[24] See for example, the NI Budget Act 2019 https://www.legislation.gov.uk/ukpga/2019/30/enacted which authorised the issuing of cash and resources from the NI Consolidated Fund.
[25] https://www.gov.uk/government/news/written-ministerial-statement-northern-ireland-finances
[26] https://www.finance-ni.gov.uk/news/ni-budget-2018-19-announced
[27] https://www.finance-ni.gov.uk/publications/2018-19-northern-ireland-finances
[28] Among other things the Northern Ireland (Executive Formation and Exercise of Functions) Act 2018 clarified that a senior officer of a Northern Ireland department is not prevented from exercising a function of the department during the period for forming an Executive if they are satisfied that it is in the public interest to do so https://www.legislation.gov.uk/ukpga/2018/28/contents/enacted
[29] No. [2018] NICA 26 https://www.judiciaryni.uk/judicial-decisions/2018-nica-26 The judgment was also discussed in the Commons during the passage of the NI Budget (no.2) Act 2018 https://hansard.parliament.uk/Commons/2018-07-09/debates/01CFB877-FEB8-4CD2-BD6E-965DFFF1E0FD/NorthernIrelandBudget(No2)Bill

The future financial impact of an overspend this year

In the event that the current projected overspends on resource and capital come to pass, the Treasury's *Statement of Funding Policy* states that:

> "*Breaches by the devolved administration of their control totals would represent serious financial mismanagement. The presumption is that the following year's block grant would be reduced by an amount equivalent to the breach. The same rule applies to departments of the UK Government.*" [30]

Table 4.1 shows the impact of recouping a £650 million resource overspend by reducing the Block Grant by the same amount in 2023-24 or by reducing it by half that amount in both 2023-24 and 2024-25, to smooth the impact. The forecasts of continued above average inflation will exacerbate these Block Grant reductions.

The original plans from the 2021 Spending Review were for the NI Executive Resource Departmental Expenditure Limit (and therefore the Block Grant) to increase by 1.7 per cent in 2023-24 and 3.2 per cent in 2024-25 compared with 2022-23. Since the Spending Review, the Block Grant this year has increased by £448 million (£58 million of earmarked funding had been incorporated into Draft Budget) reflecting the Barnett consequentials of increases in UK Government plus some non-Barnett additions. So the latest Block Grant plans imply a drop of 1.7 per cent in 2023-24 followed by a 1.5 per cent rise in 2024-25.

If the £650 million overspend is fully recouped in 2023-24 this would see the Block Grant fall by 6.6 per cent next year and rise by 6.8 per cent in 2024-25. This would certainly 'punish' departments for overspending this year, but at the price of introducing greater volatility into their funding stream that is unlikely to help with service planning and management. If the overspend was recouped over two years, the Block Grant would fall by 4.1 per cent in 2023-24 and rise by 1.5 per cent in 2024-25 (to a level 2.7 per cent below 2022-23, rather than 0.2 per cent below if the pain was concentrated in next year alone).

Table 4.1- Impact on the Block Grant of recouping a resource overspend

Scenario		2022-23	2023-24	£ million 2024-25
	Latest value of RDEL			
No change	RDEL	13,384	13,155	13,351
	% change on previous year	-	-1.7	1.5
£650 million deducted from 2023-24	RDEL	13,384	12,505	13,351
	% change on previous year	-	-6.6	6.8
£325 million deducted from 2023-24 and 2024-25	RDEL	13,384	12,830	13,026
	% change on previous year	-	-4.1	1.5

Source: Department of Finance and NIFC calculations

[30] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1030043/Statement_of_Funding_Policy_2021_-_FINAL.pdf Paragraph 8.14

As the Statement of Funding Policy says, the recouping of any overspend is a *"presumption"* rather than being written in stone. And the Treasury has dealt with actual or potential overspends in different ways in the past:

- Pressure on the resource budget can be eased by permitting a **capital to resource switch**. For example, the March 2018 UK Budget included "*£100m in flexibility [for NI] to enable existing capital funding to be used to address public services resource pressures in 2018-19*".[31] This is an unusual approach because the Block Grant for capital spending is supposed to be investment in public assets rather than meeting day-to-day pressures. But, by reducing the resource overspend, it would limit the volatility created by clawing it back – albeit at the price of increasing the overspend on capital.

- The Treasury agreed a **one-off loan** to the Executive in the 2014-15 financial year[32] and later the Stormont House Agreement included provision for it to be repaid from asset sales and capital budget.[33] Phasing the clawback of any overspend (as shown above) would deliver a similar outcome.

- The Treasury could agree **additional ad hoc funding**, either as part of the Autumn Statement or Budget, or as financial support for a deal to restore the Executive. The Secretary of State announced in February 2019 that the NI Budget for 2019-20 included £140 million of additional funding for NI from the Treasury, as well as flexibility for a capital to resource switch of up to £130 million, in order to balance the books. This was on top of additional funding from the financial annex to the Confidence and Supply agreement.[34]

- We discussed in our Sustainability Report the approach adopted by the UK government of agreeing a **Barnett floor** for Wales. The NI Executive would have received £75-150 million more in Block Grant funding in 2022-23 if its Barnett consequentials included the same form of additional needs adjustment as that applied to the funding for the Welsh Government. (We have used figures of 5-10 per cent for NI compared with 5 per cent transitional rate for Wales, reflecting the higher levels of need in NI).

[31] https://questions-statements.parliament.uk/written-statements/detail/2018-03-08/HCWS527
[32] https://www.bbc.co.uk/news/uk-northern-ireland-29562432
[33]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/390673/Stormont_House_Agreement_Financial_Annex.pdf
[34] https://questions-statements.parliament.uk/written-statements/detail/2019-02-28/hcws1370

5 Concluding reflections

The NI Executive finances a very high proportion of its spending from the Block Grant that it receives from the UK Government and its ability to top this up with borrowing and revenue from the Regional Rates and fees and charges is very limited. The Treasury's *Statement of Funding Policy* makes it clear that "*Devolved administrations, like UK Government departments, must live within these Block Grant allocations (plus their own resources) and absorb unforeseen pressures, managing as necessary by using the tools available to them...*".

In a normal year, it can often be the case that one NI department or another appears during the year to be on course to overspend. Usually, either the pressures turn out to be not as severe as first feared or the Executive agrees that additional funding can be provided as part of the In Year Monitoring process. At the end of the year, individual departments and the Block Grant as whole remain within budget.

The 2022-23 financial year is different both in terms of the number of departments projecting an overspend and the overall scale of the budget gap. With the exception of Economy and The Executive Office, all the main NI departments expect to overspend against their Resource DEL budget position and the available funding. Based on their latest forecasts, in September, departments expect to overspend their latest indicative budget allocations by £924 billion, of which funding still held centrally could absorb only £274 million. This leaves an overall projected overspend against available funding – the *"Block Grant allocations (plus their own resources)"* referred to above – of £650 million or 4.7 per cent. The projected overspend is smaller for capital, in cash terms, but this implies limited scope to switch funding between the two as on occasion in the past.

Coming on the heels of the challenges posed by the Covid-19 pandemic, the increase in inflation and pay pressures during 2022-23 has placed considerable pressure on departmental budgets. There is little evidence that departments have sought to control or offset cost increases or to secure efficiencies on the scale needed to address the projected overspends. Ministers have continued to make funding commitments at the same time as indicating that they were going to overspend.

Having been charged with scrutinising how the Executive balances its budget, the Fiscal Council views these developments with obvious concern – barring corrective action and/or additional funding from the UK Government, the budget is no longer on course to be balanced. And if it is not, the Treasury would expect to reduce the Executive's Block Grant next year making an already tight squeeze even tighter.

Although some cost pressures are largely unavoidable, the arrangements put in place for spending control and budget management in the absence of an Executive currently seem to be making a bad situation even worse. Caretaker Ministers and officials are both exercising some legal powers in parallel, and they face little accountability in the absence of an Executive and Assembly. In addition to addressing the immediate fiscal challenges that confront NI departments over the rest of this year and coming years, Stormont and Whitehall should both given serious thought to how such a situation could better be managed in future.

Appendix

Table A.1- Changes to Resource DEL Block Grant for 2022-23 since 2021 Spending Review

	£ million
Spending Review (October 2021)	**12,936.1**
Committed Earmarked funding included in Draft Budget allocations to NI departments	58.1
Draft Budget (December 2021)	**12,994.2**
Spring Statement Barnett allocations (including Energy Support)	183.8
Main Estimates Barnett allocations	87.6
Main Estimates Earmarked and Non-earmarked (£100m) Non-Barnett Allocations	168.0
DEL position reported in 2022 PESA (July 2022)	**13,433.5**
Reversal of Energy support Barnett allocation	-164.8
Provisional Outturn Carryforward of 2021-22 underspend	101.6
Additional Barnett allocations	14.0
Latest DEL position (October 2022)	**13,384.3**
Change in Resource DEL from Draft Budget	**390.1**
Allocation of Earmarked funding to NI departments	74.2
Department of Health allocation	50.0
Ringfenced deduction for NI Assembly election cost	-6.3
Unallocated Resource DEL funding	**272.2**

Source: Department of Finance