

The Chief Pleas Government of Sark

The Colin Kniveton Papers

Produced by the Chief Secretary during his
period of consultancy

November 2012 until February 2013

Review of the Budget Preparation Procedures in Sark

A document for consideration, consultation,
discussion and comment

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Review of Budget Preparation Procedures

Introduction

In the light of proposed changes to the committee structure and supporting administrative team structure, the GP & A Committee has requested a paper setting out the manner in which a revised budget process might operate taking into account a perceived requirement to stimulate a greater level of economic activity in Sark and reflecting opportunities which may arise for the Government to play a more active role in the development of the economy.

Budgets – more than an exercise

On the Isle of Man (and in many other economies) the budget is government's most important economic policy tool. The annual budget process is almost a year long, and translates policies, political commitments, and goals into decisions on how much revenue to raise, how to raise it, and how to use these funds to meet the country's competing needs, from bolstering the economy to improving health care to alleviating poverty. A budget system that functions well is crucial to developing sustainable fiscal policies and economic growth. In many countries, economic problems are exacerbated by weak budget systems and faulty budget choices. Given its wide-ranging implications for a country's people, the budget should be the subject of significant scrutiny and debate.

While a government's budget directly or indirectly affects the lives of every one of its citizens, it can have the greatest impact on certain groups, such as the elderly, children, the poor and businesses. The well-being and prospects of these people can hinge greatly upon government decisions on raising and spending money.

Moreover, even when funds have been allocated to specific projects—whether for economic growth, young people, or the elderly or disabled—weak control or project management can result in funds never achieving the intended outcomes. The lack of political power among these marginalized people to hold their government accountable is another factor in poor budget execution (i.e., after the budget is passed, how money is actually raised and spent).

It is critical for organisations such as businesses, charities or local interest groups to engage in all stages in the budget cycle not only because they can contribute valuable technical skills to the process but they also have connections with the local community that enable them to bring critical information about the public's needs and priorities to budget debates. In addition to representing the concerns of marginalized people, these organisations can strengthen and support the ability of the poor and most vulnerable to participate in the budget process and make their voices heard.

The Budget Cycle

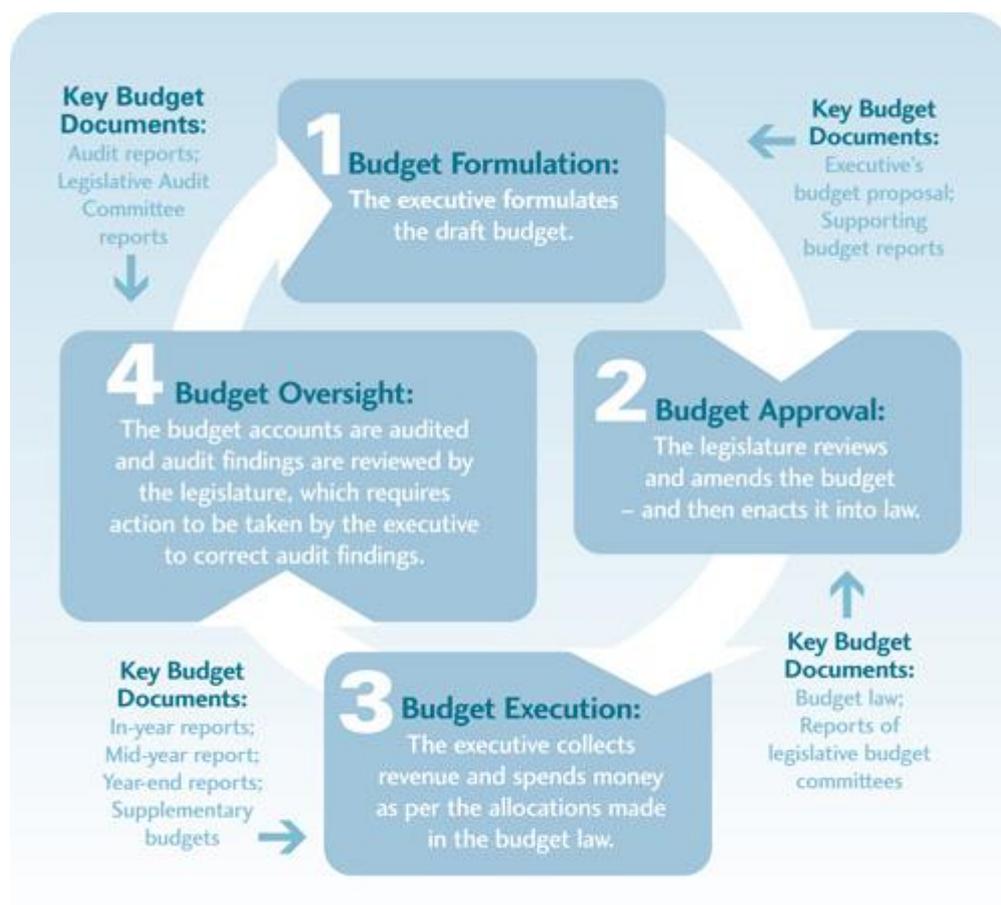
The budget should be more than just a single document—it is a year-long cycle whose different phases offer both government and the public varying access points to assess and possibly influence how public resources are raised and spent and, ultimately, the budget's desired outcomes.

This “budget cycle” can be broken down into four major events or stages:

- **Formulation**—when the relevant authority puts together the budget plan
- **Approval**—when the legislature debates, alters (or rejects), and ultimately approves the budget plan
- **Execution (implementation, monitoring, and control)**—when the government implements the policies in the budget
- **Oversight (auditing and legislative assessment)**—when the relevant body assess the expenditures made under the budget to ensure compliance with agreed limits

In order that Chief Pleas, (through the relevant committees) can influence budget decisions and provide effective independent oversight throughout the process, there are a set of documents that should be produced and circulated at each stage. The information in these documents should be comprehensive and accessible, and they should be made available in a timely way to support effective participation by stakeholders.

The following table summarises these documents and the relationship between them:



Current situation in Sark

The current budget process in Sark is simple and in circumstances where little changes from year to year, works relatively smoothly, providing no situations arise that require a significant deviation from previous years.

Budgets are prepared by individual committees during August and submitted to the Michaelmas sitting of Chief Pleas for agreement as to both expenditure and income proposals. Some committees appear more scientific than others when preparing their submissions. Some submissions are based almost exclusively on previous year's activities, with adjustments for inflation, while others involve a more comprehensive review of existing and potential expenditure.

The role of the Finance and Commerce Committee, (FCC) who present the budget to the Chief Pleas, is a difficult one, as it appears to have responsibility without authority in terms of setting budget parameters.

As such, the FCC has to adjust income to meet planned expenditure, as opposed to setting spending parameters within such limits as it believes is prudent to afford. Such a situation was illustrated in respect of the debate which arose with regard to the funding of the current Temporary Chief Secretary, in which proposals to fund the expenditure by means of an increase in various taxes were not fully agreed, resulting in a difficult situation within Chief Pleas.

Although a solution was reached relatively quickly, the manner of the way in which the budget was settled does not inspire confidence that the budget outcome was the result of a properly conceived and implemented economic strategy.

Areas for Consideration

Although Sark's finances should be regarded as being relatively straightforward, the principle of using the budget as an economic tool is still valid. The annual budget should not be regarded as being a "one-off" exercise. It should form a part of a longer term plan, aimed at shaping the economy in accordance with the objectives of the economic strategy that should guide the preparation of the budget.

As such, there should be themes that determine the shape of the budget. As an example, the most recent Isle of Man budget set out the following points to demonstrate the manner in which the budget was prepared to support overall economic strategy:

- *"To rebalance the budget so that there is no requirement to utilise reserves for ongoing spending commitments by the end of 2015-16. A revised four year plan is outlined this year.*
- *To ensure 90% delivery of a smaller capital programme in order that a constant level of work flows to the construction industry. Projected delivery in 2011-12 is 75%, some 8% below the 83% achieved last year.*
- *To achieve the statutory annual surplus of receipts over payments. The surplus is estimated to be £16 million for 2011-12, and negligible (after transfers) for 2012-13.*

- *To remove the requirement for Government subvention to the MEA. No MEA subvention for 2012-13. Capital advances still made and repayments of previous borrowings.*
- *To facilitate sustainable economic development and diversification.*
- *Continued provision for Department of Economic Development, Economic Development Fund and Regeneration.*
- *To simplify the corporate and personal taxation regimes. Alimony and maintenance relief withdrawn.*
- *To ensure fairness in the raising of taxation and charges, and to understand the aggregate impact of these on different groups. Restriction of Allowances to basic rate of tax. Increase in Income Tax Cap. Reviews of universal benefits and student tuition criteria.*
- *To manage the growing pension liability by use of reserves, employee contributions and by implementing a revised pension scheme.”*

If the economic strategy has previously been debated and agreed, the contents of the annual budget are a logical consequence of such a policy. This is a similar situation to that which resulted in the production of A Vision for Sark, which is a consequence of the residents’ survey. As such, while all the above points would not be applicable to Sark, issues such as:

- *To rebalance the budget so that there is no requirement to utilise reserves for ongoing spending commitments by the end of 2015-16.*
- *To ensure 90% delivery of a smaller capital programme in order that a constant level of work flows to the construction industry.*
- *To facilitate sustainable economic development and diversification.*
- *Continued provision for Department of Economic Development, Economic Development Fund and Regeneration.*
- *To ensure fairness in the raising of taxation and charges, and to understand the aggregate impact of these on different groups.*

are all economic objectives that might sit very properly within a Sark Annual Budget with appropriate adjustments to suit local conditions.

In order to achieve a more structured budget process, the responsible committee must play a more dominant role in the overall preparation of estimates for both income and expenditure and define the parameters that individual committees should adhere to. At present, the FCC appears unable to effectively oversee the process due to its limited mandate. If implemented, the proposals for a revised committee structure would see responsibility for the budget vested in the Finance and External Affairs Committee, with a significantly enhanced role in respect of financial control, led at officer level by an experienced Treasurer. Input would also be derived from the Chairman’s Committee, who would have overall responsibility for ensuring that the budget conformed with the economic strategy and that all initiatives planned by committees would be designed to be in keeping with such a strategy.

In this manner, the economic objectives might require for enhanced expenditure of a capital or revenue nature, which might require increased revenues. Alternatively, economic circumstances

might dictate that expenditure has to be reduced to ensure that the budget is balanced, especially where estimates of income suggest that a deficit might arise.

Other issues that should be reviewed are the use of the Guernsey RPI as an automatic basis for increasing, amongst other cost headings, public sector pay, which is misguided and should be reviewed. It is highly unlikely that inflation on Sark will be equivalent to that in Guernsey due to the absence of significant factors such as mortgage costs and vehicle expenses.

Many jurisdictions do not award annual inflation increases due to pressures to keep costs down. Sark should review annual pay awards to its public sector staff on the basis of what can be afforded and the appropriateness of current levels of pay.

All public sector staff should have their terms and condition reviewed annually to ensure they remain appropriate. There may be instances where the scale of work increases or decreases, requiring some form of adjustment to the resources available to be made.

Sark should consider allocating funds to specific purposes, to create a number of specified reserve accounts that can be increased or called upon when economic circumstances warrant such action. Headings such as Marketing Initiatives, Economic Development, Legal Reserve, IT Infrastructure are all examples of areas where funds can be segregated as a part of the budget process and utilised speedily when opportunities arise. It is possible to set limits which would require any spending proposals over a *de minimis* limit to be referred to Chief Pleas for authorisation, while delegating authority for smaller amounts to be vest in the Chairman's Committee.

Conclusion and Recommendations

The manner in which the 2013 Budget process was debated and ultimately agreed at the 2012 Michaelmas sitting of Chief Pleas did not inspire confidence. The specific way in which any item of exceptional or non-recurring expenditure is accounted for should be agreed and subsumed into a budget process well in advance of the budget debate, supported by sound accounting principles. It is always preferable that a country is able to demonstrate a united front when presenting its economic and financial strategies. This in turn reassures both businesses and individuals that its political leaders are working towards unified aims and objectives.

As such, the presentation of the budget at the appropriate sitting of Chief Pleas should contain few, if any surprises to those who will be deciding its outcome. Under the overall responsibility of the Treasurer (whose revised job specification is set out in a previous paper) the process of drawing up the budget proposals should commence at a committee stage, with overall parameters for expenditure being confirmed and opportunities for raising income being considered. It should be possible to advise Chief Pleas of the broad expenditure and income headings of the budget in July, prior to seeking approval for the complete package in October.

Prior to the October sitting, Conseillers may be given a confidential briefing as to the detailed contents of the budget. While the maintenance of confidentiality is always a difficult proposition on a small island, Conseillers should be given the opportunity to reflect upon the provisions of the

budget in good time. However, confidentiality is required because the budget may contain amendments to fiscal policies which if made known too early, may present opportunities for tax planning or some other form of manipulation of affairs that would negate the impact of the changes.

If Sark's economy is to be developed, non-recurring items of expenditure will become the norm as opposed to the exception. The budget process must be able to cope with such items and adapt to their existence, while maintaining the overall set of principles determined by the economic strategy. Such a process will be made more manageable by the existence of a revised committee structure which will deliver the authority to the relevant committee to bring about a more structured budget process, which will have as its principal objective, the delivery of an agreed economic strategy.

If such an arrangement cannot be reached, it is recommended that the FCC puts forward proposals for a revised mandate that will see its powers to oversee and scrutinise both future financial proposals and the effectiveness of expenditure established or enhanced.

It is further recommended that a review is undertaken with regards to the manner in which annual adjustments to public sector salaries and wage rates are determined, to remove the automatic reference to Guernsey RPI and replace the current practice with a more market based review of terms and conditions, taking into account performance, workload and specific factors that may impact upon the status and the appropriate level of remuneration for the position.