

# Terms of Reference for the Review of the Treasury's Fiscal Policy Advice

November 2013

## Background

Almost twenty years have passed since the Fiscal Responsibility Act came into force in 1994, with the provisions of fiscal responsibility subsequently being absorbed into the Public Finance Act 2004, and further changes to the fiscal responsibility provisions recently being adopted. Our fiscal policy institutions have served us well through this period, and are well regarded internationally. In particular, the Government's fiscal accounts have come through the global financial crisis in better shape than many, largely reflecting the significant reduction in government debt during the previous decades and a relatively healthy banking sector. But there have been times when fiscal policy has been pro-cyclical during an economic upswing, putting upward pressure on domestic interest rates and the exchange rate, exacerbating macroeconomic imbalances. Thus, as the time is approaching when the government finances will return to surplus, we consider now to be a good time to review the way in which Treasury provides advice on fiscal policy.

## Goal

The goal of the review is to ensure that the fiscal policy framework and Treasury's fiscal policy advice within that framework are appropriate to the characteristics of the New Zealand economy and consistent with best international practice.

## Terms of Reference

The review will consider:

- 1 The information, frameworks and tools used by the Treasury in its provision of advice on fiscal policy.** The review will consider how data (including forecasts/projections) and fiscal indicators/tools are used to provide fiscal policy advice, including the interaction with the fiscal allowances.

- 2 **The coordination of fiscal policy with other elements of the economic policy framework.** The review will consider Treasury's processes for coordinating advice on fiscal policy strategy with other elements of the economic policy framework – including implications for the “mix” of macro-economic stabilisation policy (ie, the interaction with monetary policy), and the more structural dimensions of fiscal policy (the composition of revenue and expenditure policies). The review will also consider the different roles of the balance sheet and comment on whether fiscal policy advice adequately incorporates the implications of choices for the balance sheet.
- 3 **Treasury's advice on the fiscal policy framework.** The review will provide high-level comment on the extent to which New Zealand's transparency- and principles-based fiscal policy framework meets international best practice for fiscal policy, taking account of the characteristics of the New Zealand economy, and actual fiscal policy outcomes. The review should also consider Treasury's advice on the framework and tools/rules for implementing fiscal policy, including the balance between legislated targets and non-legislated operating targets. A more detailed review of the provisions in the Public Finance Act is out of scope.
- 4 **Treasury's understanding of and role in evaluating the drivers of government expenditure levels.** The review will bring an international perspective to considering the institutions and processes that Treasury uses to understand the drivers of government expenditure levels, and make suggestions for where improvements can be made, with the goal of improving the quality of expenditures and delivering better public services.
- 5 **Quality of Treasury's advice.** Drawing on the material discussed above, the review will comment on the overall quality of Treasury's fiscal analysis and policy advice. Practical suggestions will be made for how the quality of advice, and the monitoring, analysis and communication of fiscal policy, could be improved.

## Process

The reviewer will:

- 1 Obtain relevant expertise, including seeking views from other interested parties, and any other external bodies, as is considered desirable to assist in the examination of the areas detailed in these terms of reference.
- 2 Report to the Secretary to the Treasury and make recommendations for the future within the context specified above, based on the last decade's experience with the framework and the conduct of fiscal policy over that period, and from the international fiscal policy literature and emerging thinking.

Treasury will endeavour to provide the reviewer with copies of all written advice pertinent to this review, and to facilitate meetings with those who will be able to provide richer context to that advice.