An Roinn Caiteachais Phoiblí
agus Athchóirithe
Department of Public
Expenditure and Reform

DPE053/001/2013

30 September 2013

Circular 15/13:

**Medium-Term Expenditure Framework:
Application to Current Expenditure**

1. The purpose of this Circular is to set out for Departments/Offices the rules and procedures in relation to three year ceilings for Exchequer voted current expenditure. The Circular explains the broader expenditure control context in which these ceilings fit and sets out the arrangements for planning and managing current[1] expenditure within the new fiscal structures put in place at a European level through the reforms to the Stability and Growth Pact (SGP), and at a domestic level through the *Fiscal Responsibility Act 2012* (FRA 2012) and the *Ministers and Secretaries (Amendment) Act 2013* (MSAA 2013).

2. The detailed rules and arrangements for the management of Government Expenditure Ceilings and Ministerial Expenditure Ceilings[2] are set out in sections I to VI (paragraphs 3 to 19) of this Circular, and a brief overview of Ireland's obligations under the reformed SGP and the new domestic fiscal framework are set out for information in section VII (paragraphs 20 to 25).

I. Three-year Government Expenditure Ceilings and Ministerial Expenditure Ceilings

3. The *Comprehensive Expenditure Report 2012-2014* (CER) of 5 December 2011 introduced a new model of multi-annual budgeting called a Medium Term Expenditure Framework (MTEF). The MTEF model is centred upon the principles of *transparency and openness* in regard to the setting and review of Departmental spending priorities, and upon the necessity for *clear medium-term planning* so that available resources are deployed, managed, and re-allocated (as appropriate) to best effect. A major feature of the MTEF is the move from the previous system of annual budgeting to a system of preparing three year parameters for current expenditure for Government Departments and Offices. The new arrangements were initiated on an administrative basis and now, following recent enactment of the MSAA 2013, have a statutory basis with statutory provision for Government Expenditure Ceilings and Ministerial Expenditure Ceilings being made in section 1 of the MSAA 2013. In keeping with the administrative arrangements that were published in the CER, section 1 of this Act provides for fixed spending ceilings for each Ministerial Vote Group for a rolling three year period.

4. The Government Expenditure Ceilings and Ministerial Expenditure Ceilings will be decided by Government and set on a nominal gross expenditure basis. These expenditure

[1] The existing arrangements with regard to capital envelopes as set out in Circular 06/2013 will continue to apply within the context of the overall MTEF.
[2] Definitions of Government and Ministerial Expenditure Ceilings are set out in the Glossary of Terms.

Tithe an Rialtais,
Sráid Mhuirfeán Uacht,
Baile Átha Cliath 2,
Éire.

Government Buildings,
Upper Merrion Street,
Dublin 2,
Ireland.

T: +353 1 676 7571
F: +353 1 678 9936
www.per.gov.ie

ceilings will operate as upper limits on expenditure for each year within the three-year period. The MSAA 2013 provides that the Estimates for Public Services for a financial year, together with estimated expenditure from the Social Insurance Fund and the National Training Fund for the same financial year, shall not exceed the relevant Government Expenditure Ceiling for each financial year of the three year period. It will be a matter for Ministers and Heads of Departments/Offices to devise plans and policies to ensure adherence to the Ministerial Expenditure Ceilings. In this regard, the *Public Spending Code* (http://publicspendingcode.per.gov.ie), including the provisions for expenditure appraisal, management and review, will be of use to Departments/Offices in ensuring that the limited resources available to them are allocated and utilised to best effect.

5 Following Government Decision, these ceilings will be published in the Expenditure Report issued by the Department of Public Expenditure & Reform in October of each year and will be reported upon in the Stability Programme Update published by the Department of Finance in April of each year. Any changes to existing ceilings will be reconciled fully (see paragraph 11).

II. Rolling Nature of the Ministerial Expenditure Ceilings

6. In the context of the Budget and Estimates each year, the three-year frame of reference of the MTEF will be extended to include a new, outer (i.e. third) year. For that new year, the Government will agree its aggregate fiscal position in accordance with the fiscal rules provided for in the FRA 2012, and in this context the Government will agree a Government Expenditure Ceiling for each year.

7. Once the Government Expenditure Ceiling is determined for that new incoming year, the Department of Public Expenditure & Reform will make proposals for the indicative technical allocation of this aggregate ceiling into Ministerial Expenditure Ceilings for that year. (The previously-set Ministerial Expenditure Ceilings for the earlier two years in the frame of reference will not be adjusted in this context, except on the basis provided for under section III below.) These proposed allocations will form the technical basis for subsequent discussions to enable the Minister for Public Expenditure and Reform to bring forward proposals to Government in relation to revised Ministerial Expenditure Ceilings.

III. Fixed Nature of the Ministerial Expenditure Ceilings

8. The Ministerial Expenditure Ceilings will be binding over the three year period and the annual Estimates of Expenditure for each year will be set in accordance with those Ceilings as decided by Government.

9. The Government may decide to vary the Government Expenditure Ceiling in the following limited circumstances and subject to compliance with the overall fiscal rules (set out in Section VII):-

- (i) If specified *exceptional circumstances (as defined in FRA 2012)* (e.g. severe macroeconomic shocks etc.) occur that may necessitate breaching the ceiling;
- (ii) If compensatory discretionary measures are introduced, e.g. through changes to tax policy resulting in increased revenues in a year. This would allow for the

Government Expenditure Ceiling to be increased without affecting General Government Balance targets;

(iii) Section IV details the special arrangements to be made for cyclical expenditure and certain other expenditure categories.

10. The Government may decide to vary the Ministerial Expenditure Ceilings in the following limited circumstances:-

(i) Following on from a decision by Government to vary the Government Expenditure Ceiling for any year, the Ministerial Expenditure Ceilings may be varied and re-allocated, on the basis of proposals brought to Government by the Minister for Public Expenditure & Reform.

(ii) If the Government has conducted a Comprehensive Review of Expenditure as outlined in section VI of this Circular, the Minister for Public Expenditure & Reform may bring forward proposals for new Ministerial Expenditure Ceilings, replacing some or all of the previously-set Ceilings, to take account of the results of that Review.

(iii) If the Government considers that there are good and pressing reasons of public policy for allowing reallocation of resources among Ministerial Expenditure Ceilings, whether to take account of the views of Oireachtas Committees, the views of the EU institutions, the transfer of functions between Departments, or for any other reason, then the Minister for Public Expenditure & Reform may bring forward proposals to Government for new Ministerial Expenditure Ceilings, replacing some or all of the previously-set Ceilings. In any such circumstance, the Minister for Public Expenditure & Reform will make arrangements to explain to the Oireachtas the reasons for such a varying of the Ministerial Expenditure Ceilings.

(iv) If an adjustment of one or more individual Ministerial Expenditure Ceilings becomes necessary arising from a failure of one or more Departments/Offices to comply with their Ceilings for the current year, the adjustments will be made by the Government on foot of a proposal from the Minister for Public Expenditure & Reform. In any such circumstance, the relevant Minister will be required to seek a Supplementary Estimate under the provisions currently set out under the *Public Financial Procedures*.

(v) Section IV of this Circular details the special arrangements to be made for cyclical expenditure and certain other expenditure categories.

(vi) If a Department has carried over funds from one year to the next as detailed in Section V of this Circular.

11. The multi-annual Government Expenditure Ceiling and Ministerial Expenditure Ceilings will be notified to Dáil Éireann as set out in Section 1 of MSAA 2013 and will be re-stated publicly on an annual basis. This restatement will involve a reconciliation with the last published ceilings for the same period, accompanied by explanations of all significant deviations. The reconciliations will be conducted under a number of categories, such as technical adjustments and discretionary policy changes, rather than on an item-by-item basis (except where specification may be required as indicated below).

IV. Special Arrangements for certain expenditure categories

12. Special arrangements will apply to expenditure categories which are internationally recognised as being very closely related to the economic cycle and which consequently are less amenable to the normal forms of multi-annual planning and control. The main category of expenditure subject to special arrangements is unemployment-related payments, such as Jobseekers Allowance and Jobseekers Benefit.

13. If the final outturn for the year is less than the allocated amount on these cyclically-sensitive payments, the difference will automatically accrue to the benefit of the Exchequer, rather than be transferred across to fund the expansion of other (non-cyclically-sensitive) services. Effectively these cyclically-sensitive areas are ring-fenced. However, these areas are not excluded from the scope of expenditure reductions or expansions that may be considered by the Government from time to time. The principal difference is that the cyclically-sensitive allocations must be re-visited each year in light of updated economic forecasts, whereas the non-cyclical expenditure elements that form the core of the Ministerial Expenditure Ceilings would not normally be re-visited or adjusted over the 3-year timeframe.

14. A further expenditure category that is subject to these special arrangements is European co-funded payments. Expenditure in this category will be re-visited each year in light of EU budgetary developments.

V. Carryover of Current Spending, Recoupment of Overruns and Departmental Continuity Reserves

15. As a general principle, Departments will be allowed to carry over savings against the original estimates from one year to increase the current expenditure ceilings for the next year only. Such carryover will be subject to the approval of the Minister for Public Expenditure & Reform and must comply with the overall fiscal rules. In particular, it should be noted that if the level of savings proposed for carryover into the following year, across all Departments/Offices, poses a risk to the overall Government Expenditure Ceiling and/or the Government targets for the public finances, then the carryover may have to be capped. The purpose of the carryover facility is to offer Departments/Offices, who succeed in managing within their expenditure ceiling in any given year, the possibility of carrying over some proportion of that current expenditure saving to augment their previously-set expenditure ceiling for the following year. In addition to the overall cap that may be applied by the Minister for Public Expenditure and Reform the following safeguards also apply:-

i. A Department may be authorised to carry over up to:

a) 100% of its savings up to 2% of the gross current allocation;
b) 2/3 of its savings between 2% to 6% of the gross current allocation (with the remainder accruing to the Exchequer); and
c) Savings above this level will be examined on a case by case basis by the Department of Public Expenditure & Reform and will in any event be subject to an overall cap to balance the need to ensure that the Exchequer realises a benefit from savings that arise with the principle that prudent and proactive stewardship of public funds should be incentivised.

ii. The carried-over funds can be spent on any once-off projects or structural measures approved by the relevant Minister (and subject to sanction from the Department of Public Expenditure & Reform in the normal way), but may not be used to create an ongoing liability to the Exchequer. This applies to both pay and non-pay savings, but any proposals for carryover of pay savings should be consistent with pay expenditure limits and must be approved by the Department of Public Expenditure & Reform.

16. In order to facilitate the inclusion of the total proposed amount of the carryover by Vote in the Budget Estimates, each Department/Office is required to provide the Department of Public Expenditure and Reform with its indicative statement of proposed current carryover amounts by Vote along with a business case in support of its proposal in a timely manner in the context of the Estimates. Precise deadlines will be advised as part of the normal Budget preparations each year.

17. In order to ensure compliance with Ministerial Expenditure Ceilings the following control measures will apply:

(i) Where a Department is found to be in excess of its profiled expenditure for two months **and/<u>or</u>** where the Department of Public Expenditure and Reform has identified a substantive risk to the end-year expenditure outturn, the Minister for Public Expenditure and Reform will report on this to Government as part of the routine monthly Expenditure Management Report. Unless the Minister for Public Expenditure and Reform is satisfied that the overspend is due to timing and not deemed to be a substantive risk to the end-year expenditure position, the Minster for Public Expenditure and Reform will seek a decision by Government requiring the Department to provide monthly reports to Government detailing how the expenditure overrun occurred; steps being taken to address the issue; and an overall update on the expenditure position.

(ii) If after two months of reporting to Government the expenditure overrun has not been corrected the Minister for Public Expenditure and Reform will seek a decision by Government to authorise a formal review led by the Department of Public Expenditure and Reform to identify areas where savings and efficiencies can be made to ensure adherence to the end-year expenditure ceiling. The outcome of this review is to be reported to Government, within a month of the Government Decision authorising the review, and will provide recommendations to Government which, following Government agreement, the Department will be required to implement to address the overrun. Any incremental costs arising from the production of this report will accrue to the Department whose expenditure is under review.

(iii) Finally, if the Department fails to implement the Government Decision and breaches the expenditure ceiling, on foot of a proposal from the Minister for Public Expenditure and Reform, the Government may require that the Department “repay” the overrun in the next year. In such circumstances, the Department will be subject to an offsetting adjustment in the Ministerial Expenditure Ceiling for the following year and will be required to devise policy measures to live within the reduced allocations. In circumstances where the Department cannot absorb the full required adjustment in the following year's expenditure ceiling, the Government can decide that it may be necessary either to spread the adjustment over two or more years or, in circumstances where the overall Government Expenditure Ceiling and/or the Government targets for the public finances do not allow such an approach, to allocate the balance of reductions across other Departments so that the overall expenditure path remains on target. This will require re-prioritisation of resources within each Ministerial envelope.

18. The introduction of Departmental Continuity Reserves is under consideration and may be introduced at a later date. The continuity reserves would provide Departments with a buffer to protect against fluctuations around their spending limits.

VI. Periodic Review of Priorities: the Comprehensive Review of Expenditure

19. A Comprehensive Review of Expenditure (CRE) exercise will be conducted approximately every 3 years subject to the agreement of the Government. This exercise will allow the multi-year Ministerial Expenditure Ceilings to be re-considered and re-set to reflect developing Government priorities. The CRE will make use of the developing corpus of VFM & Policy Reviews and Focused Policy Assessments conducted in line with the Public Spending Code, as well as targeted cross-governmental analyses to ensure that the entire base of expenditure is evaluated against the priorities of Government.

VII. Fiscal Parameters

20. The MTEF and the Ministerial Expenditure ceilings operate within the broader expenditure control context arising from the reforms of the SGP.

21. FRA 2012 imposes a duty on the Government to ensure compliance with the budgetary rule and the debt rule, which are provided for in the FRA 2012. The budgetary rule requires that the budgetary position of general government must be either:

- In balance or in surplus and that this will be satisfied if the annual structural balance is at the medium-term budgetary objective (MTO); or

- If it is not at the MTO target, it is on the adjustment path towards adhering to the MTO as set in accordance with the SGP.

In the event of exceptional circumstances as defined under the SGP this rule may not apply.

22. If there is a failure to comply with the budgetary rule and there is a significant deviation from the MTO or the adjustment path, then the Government will be required to implement the correction mechanism and introduce a plan to restore compliance.

23. Furthermore reforms to the SGP introduced a complementary expenditure measure known as the Expenditure Benchmark that aims to link the changes in expenditure with growth in the economy. Through application of the Expenditure Benchmark, which takes into account decisions in relation to discretionary revenue measures, a multi-annual upper limit on General Government expenditure is determined.[3]

24. Once the limit on General Government expenditure has been determined the Government Expenditure Ceiling, as defined in the MSAA 2013, can be derived as outlined below:

i. The expenditure from own resources of the Local Government Sector and Central Government Bodies (including Extra Budgetary Funds) outside the Exchequer must be calculated. In line with the agreed Protocol for the control and monitoring of local authorities contribution to the General Government Balance, the Local Government Sector will finalise their key budgetary parameters (current and capital receipts and expenditure) in order to facilitate the change in the budgetary timetable under the "two-pack" reforms.

ii. All other non-voted Government expenditure must also be removed in order to establish an overall upper limit on the aggregate cash-based Government Expenditure Ceiling referenced in the MSAA 2013.

25. Essentially, the Government Expenditure Ceiling is equivalent to total gross voted expenditure. The MSAA 2013 provides that, upon a proposal of the Minister for Public Expenditure & Reform, the overall Government Expenditure Ceiling shall be apportioned into individual Ministerial expenditure ceilings for both current and capital expenditure for the next three financial years.

26. **Dissemination and Implementation**

You are requested to bring this Circular to the attention of all staff in your Department/Office involved in planning and controlling public expenditure and also to relevant public bodies under the aegis of your Department/Office. Any queries in relation to this Circular should be addressed to John Kinnane email: john.kinnane@per.gov.ie in Central Section, Department of Public Expenditure and Reform.

27. The Department of Public Expenditure and Reform will keep the operation of the Circular under review to ensure that its implementation contributes effectively towards continuing fiscal structural reform.

____

Deirdre Hanlon
Assistant Secretary
30 September 2013

[3] For more details on the translation of the MTO to the expenditure benchmark, please see the *Vade Mecum on the Stability and Growth Pact*, available at http://ec.europa.eu/economy_finance/publications/occasional_paper/2013/op151_en.htm

Glossary of Terms

Expenditure Benchmark

The 'expenditure benchmark' has been introduced as part of the suite of EU fiscal reforms (in EU Regulation number 1466/97, which forms part of the so-called "six-pack") designed to enhance European fiscal surveillance and complement analysis of the structural balance. This benchmark is related to the medium-term budgetary objective (MTO) and limits the growth of overall General Government expenditure, which includes the expenditure of Local Authorities. It is linked to the potential real growth rate of the economy and is used to calculate the overall limit on the growth of General Government expenditure, unless financed through additional discretionary tax/revenue increases. Debt interest expenditure and certain other expenditure related to the economic cycle are excluded from the base in this assessment as the aim is to focus on policy choices which have an effect on the structural balance. The reference rate for the 'expenditure benchmark' is fixed for three years in line with the current practice for MTO's.

Medium-Term Budgetary Objective (MTO)

The MTO is a key element of Stability and Growth Pact and represents a structural budgetary position that safeguards against the risk of breaching the 3% of GDP threshold and ensures the long-term sustainability of public finances and a core element of the Stability & Growth Pact and Fiscal Compact. It is set by Member States subject to a minimum set by the EU Commission. The MTO is updated every three years, taking account of any economic or budgetary policy changes that may occur. It can also be updated more often, if new structural reforms with major impacts on the sustainability of the public finances are implemented.

Exceptional Circumstances

FRA 2012 provides that exceptional circumstances mean: a period during which an event outside the control of the State has a major impact on the financial position of the general government, or a period of severe economic downturn, within the meaning of the Stability and Growth Pact.

Government Expenditure Ceiling

As set out in Section 1 MSAA 2013 Government Expenditure means the sum of money which is met out of:

- money supplied out of supply grants and appropriations-in-aid in respect of supply services,
- money paid out of the Social Insurance Fund, and
- money paid out of the National Training Fund.

The MSAA 2013 provides that each year the Government shall make a decision approving an upper limit on Government Expenditure for the following three year period.

Ministerial Expenditure Ceiling

Subject to the Government Expenditure Ceiling, and following a proposal from the Minster for Public Expenditure and Reform, the Government shall make a decision approving the amount of Government expenditure to be apportioned to the area of responsibility of each Minister. These amounts shall constitute the Ministerial Expenditure Ceilings for each of the three financial years concerned.