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Effective Legislative Scrutiny

This Note provides some detail on best practices put forward by international organisations in relation to scrutiny of budgets and financial information. It also raises some issues facing parliamentary scrutiny in the wake of the international financial crisis. Finally, some case studies highlight the value of scrutiny in practical terms.

1. Introduction

This Briefing Note is intended to provide useful source information to support the Committee for Finance and Personnel's discussion paper on the Executive's Review of Financial Process.

The Note begins by briefly outlining the principles and purpose behind financial scrutiny in the legislature. It also discusses by whom scrutiny should be conducted, and at what stage in the budgetary process. Section 3 presents some discussion of the imperatives and challenges raised for scrutiny by the recent financial crisis. Section 4 presents some case study examples of where scrutiny has been effective.

2. Best practice

This section discusses why parliamentary bodies should be conducting financial scrutiny. It then looks at which part of the legislature is best placed to conduct scrutiny effectively.

Why conduct scrutiny?

Material produced for the World Bank's Parliamentary Staff Training Program *Effective Financial Scrutiny: The Role of Parliament in Public Finance* states that:

> *Improvised budget cuts tend to adversely affect vulnerable groups that have a weak political voice, and who are most dependent on government initiatives.*

This points to one fundamental of effective legislative scrutiny: its purpose is to ensure that the executive branch of government effectively **plans** its budgets, rather than improvises them. The point is further developed:

> *Frequent adjustments to budgets can reflect the uncertainties that are characteristic of the macroeconomic environment, but 'continuous' or 'repetitive budgeting' is also a symptom of a weak and ill-disciplined budget system. To ensure that its authority is not undermined by excessive adjustments, the legislature might find it useful to keep a close eye on implementation through scrutiny of actual spending during the fiscal year. Any significant adjustments to the budget should be captured in adjustment or supplemental appropriations that are tabled in the legislature for approval. In-year adjustment decisions need to be made in a transparent manner and should be subject to the same scrutiny carried out at the budget formulation stages.*[1]

[1] World Bank (undated) 'Effective Financial Scrutiny: The Role of Parliament in Public Finance' available online at: http://siteresources.worldbank.org/PSGLP/Resources/budgetall.pdf (accessed 12 April 2012) (see page 29)

Secondly, then, there is an imperative for the legislature to focus on in-year changes and adjustments (in Northern Ireland this is achieved through monitoring rounds) and not only on plans at the time of budget preparation and approval. This should help ensure that the executive arm of government is not adjusting the budget 'on the hoof' and that there are justifications and explanations for changes made in-year.

In-year budgetary review is also supported by experts at the International Monetary Fund (IMF):

> *A good budgetary practice is to require a formal midterm review of budget execution by the legislature, which may, if necessary, adopt a revised annual budget law to accommodate necessary changes.*[2]

The Organisation for Economic Cooperation and Development (OECD) also advocates provision of in-year information by the executive to the legislature. This is to enhance budget transparency, and also clearly facilitates scrutiny:

> *The mid-year report provides a comprehensive update on the implementation of the budget, including an updated forecast of the budget outcome for the current fiscal year and, at least, the following two fiscal years. The report should be released within six weeks of the end of the mid-year period.*[3]

Writing in 2003 (some years before the recent global financial crisis), one expert noted that:

> *While there is a renewed global emphasis on fiscal sustainability, many parts of the world face massive development challenges. In such circumstances, the issue of how to put public resources to optimal use becomes paramount, and* ***the contribution of parliament to sound financial governance through effective scrutiny cannot be underestimated****.*[4] *[emphasis added]*

This is a powerful point: the legislature can make an important contribution to ensuring financial governance is sound. In turn, this may reduce the likelihood of spending scandals occurring and being highlighted in retrospect by the Public Accounts Committee. There is, then, an incentive for the executive arm of government to facilitate scrutiny.

Who should conduct scrutiny?

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[2] IMF (2010) 'Reforming Budget System laws' available online at: http://www.imf.org/external/pubs/ft/tnm/2010/tnm1001.pdf (accessed 12 April 2012) (see page 15)

[3] OECD (2002) 'OECD Best Practices for Budget Transparency' available online at: http://www.oecd.org/dataoecd/33/13/1905258.pdf (accessed 12 April 2012) (see page 10)

[4] Wehner, J (2003) 'Principles and Patterns of Financial Scrutiny: Public Accounts Committees in the Commonwealth' in Commonwealth and Comparative Politics Vol 41, No.3, pages 21-36 (see page 22)

If mistakes and scandals are to be avoided, scrutiny needs to be conducted by the appropriate actors, at the appropriate time. The literature identifies three overall objectives of scrutiny:

- Aggregate fiscal discipline, or affordability. In other words, to look at the big picture of total revenue and expenditure, and whether these are appropriately balanced;
- Allocative efficiency, or prioritisation. In other words, whether the division of allocations between different sectors/programmes is justifiable and coherent; and,
- Operational efficiency, or value for money. Essentially, are public bodies spending their allocations well.[5]

According to one expert:

> *This suggests that comprehensive financial scrutiny is achieved when parliament safeguards and makes a purposeful contribution towards meeting each of these objectives.*[6]

To make such a contribution, the legislature must engage at different times – **before** expenditure is committed, at the policy development/budget planning stage (*ex ante*), and **after,** at the financial reporting stage (*ex post*). (see table 1)

TABLE 1
PARLIAMENTARY ENGAGEMENT WITH KEY ISSUES IN PUBLIC SPENDING

	Affordability	Prioritisation	Value for money
Ex ante	X	X	
Ex post			X

Source. Wehner 2003

The table shows the importance of not leaving all scrutiny to the Public Accounts Committee (PAC), which by its nature only engages *ex post*. Two of the three elements need to be conducted *ex ante*, and this is where the Assembly's statutory committees' role become important.

This point is further highlighted in the World Bank training material:

> *If a legislature decides to engage with aggregate and allocational decisions,* ***it will have to do so through ex ante scrutiny during the approval stage of the budget process****… In other words, ex ante scrutiny focuses*

[5] See Schick, A (1998) 'A Contemporary Approach to Public Expenditure Management' available online at: http://www.5m.com.tr/en/kaynaklar/AcontemporaryApproachtoPublicExpenditureManagement.pdf (accessed 13 April 2012)

[6] Wehner, J (2003) 'Principles and Patterns of Financial Scrutiny: Public Accounts Committees in the Commonwealth' in Commonwealth and Comparative Politics Vol 41, No.3, pages 21-36 (see page 23)

on the content and direction of budget policy, and ex post scrutiny on the quality of its implementation.[7] *[emphasis added]*

It is also important to emphasize that **it is in committees**, **rather than in plenary, that this scrutiny should take place**. Again, this is highlighted in World Bank training material:

> *Committees are the 'engine room' of the legislature […]. It is here that in-depth and technical debate can take place, away from the political grandstanding that often characterizes proceedings in the chamber.* ***When discussion takes place mainly on the floor of the house the budgetary influence of the legislature tends to be weak.***[8] [emphasis added]

3. Challenges for financial scrutiny

The recent financial crisis has resulted in considerable fiscal pressures on many developed industrialised states. The Centre for Public Scrutiny (CfPS) noted that there is potential for austerity measures to put pressure on scrutiny:

> *…with a macroeconomic storm raging, and with national governments and international bodies struggling to cope, it might seem overoptimistic to suggest that those involved in audit, inspection and scrutiny – the "fourth arm" of government, with no formal decision making powers – can exert any real influence.*[9]

At the same time, however, it has been argued in a recent study by the Association of Chartered Certified Accountants (ACCA) that:

> *Parliamentary financial scrutiny on its own may not prevent the next financial crisis, but* ***it is a vital part of a nation's governance*** *and if done well it may help manage the risks of future financial crises.* [10] *[emphasis added]*

The ACCA study looked at four countries (Australia, Canada, Ireland and the UK) and found that in each of the countries there had been a growth in Independent Fiscal Institutions (such as the Office of Budget Responsibility in the UK). But these institutions do **not** perform a legislative scrutiny role. It also found there has been little improvement in parliamentary financial scrutiny.

[7] World Bank (undated) 'Effective Financial Scrutiny: The Role of Parliament in Public Finance' available online at: http://siteresources.worldbank.org/PSGLP/Resources/budgetall.pdf (accessed 12 April 2012) (see page 84)

[8] World Bank (undated) 'Effective Financial Scrutiny: The Role of Parliament in Public Finance' available online at: http://siteresources.worldbank.org/PSGLP/Resources/budgetall.pdf (accessed 12 April 2012) (see page 89)

[9] CFPS (2009) 'global challenge, local solutions: the role of scrutiny, audit and inspection in tackling the recession' available online at: http://www.cfps.org.uk/publications?item=6959&offset=0 (accessed 13 April 2012) (see page 1)

[10] ACCA (2011) 'Parliamentary financial scrutiny in hard times' available online at: http://www2.accaglobal.com/pubs/general/activities/library/public_sector/ps_pubs/tech-tp-pfs.pdf (accessed 13 April 2012) (see page 1)

Key findings of the report include:

- The focus of financial scrutiny needs to be realigned with the budget, spending plans and resource accounts, rather than with the technical detail of the estimates. ACCA argues this requires structural and cultural reform;
- Parliamentary committees have a number of strengths (including the ability to facilitate technical debate and scrutiny), but they also have weaknesses (such as a general lack of skills and a lack of follow-up on recommendations made in reports);
- Governments making data widely available should **not** be seen as a substitute for effective financial scrutiny by parliaments;
- As public spending cuts are undergone, it is important that resources such as support for committees of the legislature are safeguarded from “unreasonable cuts” and that a clear and coherent policy to improve scrutiny is developed at an institutional level;
- There is a risk that governments may use the financial crisis to reduce scrutiny rather than enhance it. For example, in Australia there is a perception that the budget process has become **less** transparent as the Federal governing party “plays on popular fears that the economy is faltering and needs urgent attention.”[11] and,
- It is perceived by some commentators that current parliamentary scrutiny is lacking and policy initiatives are rushed through to prop up the economy without proper debate or consultation.

Among other things, these findings led ACCA to conclude that:

> *In the middle of the largest financial crisis that the world has seen, parliaments and governments should not waste the opportunity to reform how they go about scrutinising public funds and taxation policies. […]* ***The arguments for improving financial scrutiny are more compelling than those against greater parliamentary involvement.***[12] *[emphasis added]*

Particular recommendations from the study are:

- Legislatures and executives need to approach scrutiny in the right way and use the financial crisis as an opportunity to have a fundamental re-think about how to improve financial scrutiny and make it strategically important;
- Politicians need to embrace training and improve their performance; and,
- Parliaments need to address the limitations of the committee system (influencing government and following up on recommendations.

[11] ACCA (2011) ‘Parliamentary financial scrutiny in hard times’ available online at: http://www2.accaglobal.com/pubs/general/activities/library/public_sector/ps_pubs/tech-tp-pfs.pdf (accessed 13 April 2012) (see page 2)

[12] ACCA (2011) ‘Parliamentary financial scrutiny in hard times’ available online at: http://www2.accaglobal.com/pubs/general/activities/library/public_sector/ps_pubs/tech-tp-pfs.pdf (accessed 13 April 2012) (see page 8)

4. What scrutiny can achieve

The CfPS is a small charity whose principal focus is on scrutiny, accountability and good governance, both in the public sector and amongst those people and organisations who deliver publicly-funded services. The bulk of its work focuses on local government and the wider localism agenda. It also works extensively with and for health and social care bodies, and others such as police, park and fire authorities, housing associations and other housing management organisations, universities, regulators, Parliament and select committees and government departments.[13]

In its report *global challenge, local solutions*[14] CfPS identified a number of examples of where scrutiny has delivered benefits to public bodies. Note that whilst the examples provided here are from local government in England, the **functions** to which they relate are delivered by central government departments in Northern Ireland. They are, therefore, comparable with some of the issues which the Assembly's statutory committees may scrutinise.

Some brief case studies are presented below. Case study 1 looks at the impact of scrutiny in relation to economic development in Newcastle under Lyme. Case study 2 relates to consumer debt in Yorkshire. Case study 3 relates to worklessness in Burnley.

[13] http://www.cfps.org.uk/about-us

[14] The full report containing many case studies is available online at: http://www.cfps.org.uk/publications?item=6959&offset=0 (accessed 13 April 2012)

Case study 1: economic development in Newcastle under Lyme

Newcastle under Lyme

This authority concluded, in May 2009, a review entitled "Encouraging economic development in uncertain times". The work deliberately set out not to provide conclusive answers, but to establish a sound evidence base for further research.

What happened (methodology)	What was achieved (outcomes)
Detailed mapping exercise of work being carried out by the authority and others (including the county council and regional bodies).	Recommendations for more effective procurement between and the council and its partners, and better use of the council's general power to enhance the wellbeing of the area – and use of the powers under the Sustainable Communities Act.
Evidence gathered from local business.	Recommendations for a borough-wide strategy for helping local business, with sign-up from all relevant partners; this will include enhanced business support services from the council.
On the basis of the above evidence, an analysis of where gaps in provision lay.	Recommendations which focused on areas where the council and its partners needed to plug gaps in provision.
Overall outcome	
The review provided some clear direction for the council in using partnership arrangements much more effectively.	

Case study 2: consumer debt in North Yorkshire

North Yorkshire – the council carried out detailed work into the nature of consumer debt in the county, based on intelligence from community groups that, while local people wanted to reduce the dependency on doorstep lending and loan sharks, the area was a "credit union desert", with no single community based source of low cost credit for the financially excluded.

What happened (methodology)	What was achieved (outcomes)
Evidence was gathered from local people about the impact of financial exclusion on the population.	The need, and appetite, amongst the wider community to establish a credit union to allow those on a low income to access credit responsibly could be clearly identified. The relationships built as a result of this exercise helped to bring about the review's more general outcomes.
A feasibility study was carried out to assess the realism of establishing a pan-county credit union.	Scrutiny was able to develop findings and recommendations founded on evidence, as an independent body, so reaching an objective opinion unencumbered by any perception of vested interests.
Recognising the unwillingness of the council and its partners to embark on such as venture, other solutions were considered which would minimise the risk to the authority.	A solution was developed whereby a county-wide credit union could be grown out of an existing, smaller, union – a much more cost-effective technique than establishing a new body.
Overall outcome	
The main outcome of the review was the successful establishment of a credit union for the whole of North Yorkshire.	

Case study 3: the Working neighbourhoods Fund and worklessness in Burnley

Burnley

This Economy Scrutiny Committee examined how the authority used funds made available through the Working Neighbourhoods Fund (WNF).

What happened (methodology)	**What was achieved (outcomes)**
Regional comparative research with other authorities in receipt of WNF funding.	Findings that Burnley's direct spend of worklessness and related issues was significantly less than other authorities, giving rise to concerns about the effectiveness of the projects being undertaken to support this area of policy.
Research into the national guidance provided on the WNF.	A clear picture of the objectives of the fund, leading to a judgment on whether the projects being undertaken in Burnley were effective in the light of the intended outcomes set for WNF by government.
Research into the commissioning process for projects being funded by WNF.	Detailed recommendations on improvements for commissioning, to ensure that priorities were more robust.
Overall outcome	
The review provided a clear view on whether the authority's WNF spend was "value for money", and highlighted the potential, when considering value for money issues such as this, decisions often rest of subjective interpretations of where money is and is not being spend most effectively. This understanding has helped to inform a more robust bcal approach to the spending of funds such as the WNF.	

5. Concluding remarks

This Note has shown that there is considerable support for the concept of scrutiny in the guidance issued by international financial institutions. It has also highlighted some current challenges (and opportunities) for effective scrutiny. In addition, it has demonstrated that there is practical evidence that scrutiny can be an effective tool for improving governance.