Feature

What is a Charter of Budget Honesty? The Case of Australia

It is now nearly 20 years since Australia introduced a prominent piece of legislation known as the *Charter of Budget Honesty Act (1998)* to improve the transparency and the discipline of its budget process. This article examines the success of the charter, as well as its limitations, in the context of Australian budget process, including an analysis of its most pertinent components, so as to then reflect more broadly on the impact of budget honesty mechanisms for parliaments with a similar structure and history, including Canada.

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In our time, most Parliamentary democracies in the world are faced with the question of how to maintain budget discipline, particularly with respect to three overarching concerns: a long-run reliance on deficits; the ability to manage unforeseen economic shocks; and the level of transparency and accountability in the budget process. Following the economic crisis of the past decade, more parliaments are finding themselves debating questions of fiscal discipline and fiscal transparency at ever more frequent intervals. Some legislatures have tried to give a more concrete form to their beliefs in budget discipline and budget transparency by enshrining them into charters or acts.

Among such budget-discipline enshrinements, the one that has gained the most prominence in its local legislative budgeting context is Australia's *Charter of Budget Honesty* ([Charter], 1998).[1] Since its promulgation, the Charter has come to occupy a central role in the national budget process, creating a system of processes that *inter alia* involve Parliament, the Treasury, the Department of Finance, and the Parliamentary Budget Office (PBO). The Charter has also initiated a set of rituals which are now considered core aspects of the annual budget, and which much of the Australian public has come to consider standard political and economic practice.

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To understand the evolution of such an important document, it is worth quickly visiting the historical context in which the need for such a Charter emerged. Australia has had a long history of fiscal rules at a subnational level: in the 19th century, the Australian colonies passed legislative debt-limits and balanced-budget requirements; and some of those provisions are still in place today.[2] That being said, it was not until the latter half of the 20th century that a significant consensus arose in Australia for budget discipline and transparency at a level underwritten by national fiscal rules. This thinking was in large part inspired by reforms that were pioneered in neighbouring New Zealand, which in 1994 promulgated the *Fiscal Responsibility Act* that placed explicit importance on improving budget transparency. The intent of New Zealand's law was to consolidate the finances of government (debt and deficit), which had accumulated over the 1980s and 1990s; and the promulgation of the Act should be seen in the context of the movement in most anglophone societies at that time towards reducing the size of government and "rolling back the state".[3]

Both the United Kingdom and Australia drew from these reforms in New Zealand, and by 1998, both countries had enacted some form of law addressing financial discipline and transparency. In the UK, this law was called the *Finance Act* (1998) which included a *Code for Stability* of national finances; and in Australia, it was the *Charter of Budget Honesty* (1998). It can be said that some of the important common factors shared by these laws include: guidelines and guiding principles for fiscal policy; an emphasis on clear statement of fiscal objectives; a fairly demanding set of requirements for reporting fiscal statements to the public; and an emphasis on long-term orientation towards fiscal policy.

At the time that it was instituted, the Charter represented the very best in fiscal policy legislation, both in terms of scope and rigour. The stipulated purpose of the Charter is to provide "to improve fiscal policy outcomes," and it provided for this "by requiring fiscal strategy to be based on principles of sound fiscal management and by facilitating public scrutiny of fiscal policy and performance." In order to meet these outcomes, the Charter was comprised of several important moving parts that were to work in concert to collectively push for fiscal discipline and transparency.

The Moving Parts of the Charter

Within the Charter, the most important documents that collectively give it force as budget legislation include:

- a Fiscal Strategy Statement (FSS)
- a Mid-Year Economic and Fiscal Outlook report (MYEFO)
- a Budget Outcome Report (BOR)
- an Intergenerational Report (IR), and;
- a Pre-Election Fiscal Outlook (PEFO).

Under the Charter, the government outlines its budget strategy in an overarching Fiscal Strategy Statement (FSS), which is tabled by the Treasurer and publicly released with each annual budget. According to the Charter, the purpose of the FSS is to "increase public awareness of the Government's fiscal strategy and to establish a benchmark for evaluating the Government's conduct of fiscal policy." It outlines the general procession of the budget and its policy priorities at the current time. In the 2015-16 budget, for example, the FSS highlighted the government's priority on "job growth", and "budget repair" in light of falling iron ore prices which had a large detrimental impact on the revenue side of the national budget.[4]

The Mid-Year Economic and Fiscal Outlook report (MYEFO) acts as an update and a progress report to the annual budget half-way (November) through the fiscal year (beginning May). It apprises the public, the legislature, and the executive branch of any outstanding events or changes that may affect the budget's trajectory. As an example, in the 2015-16 budget, the 250-page MYEFO adjusted the future projected price of iron ore downwards from $48 to $39, and revised other line items to reflect lower revenues in the budget accordingly.[5]

The Budget Outcome Report (BOR) is published by the Department of Finance within three months of the budget's passing (usually by August), and summarizes the post-budget financial statements.

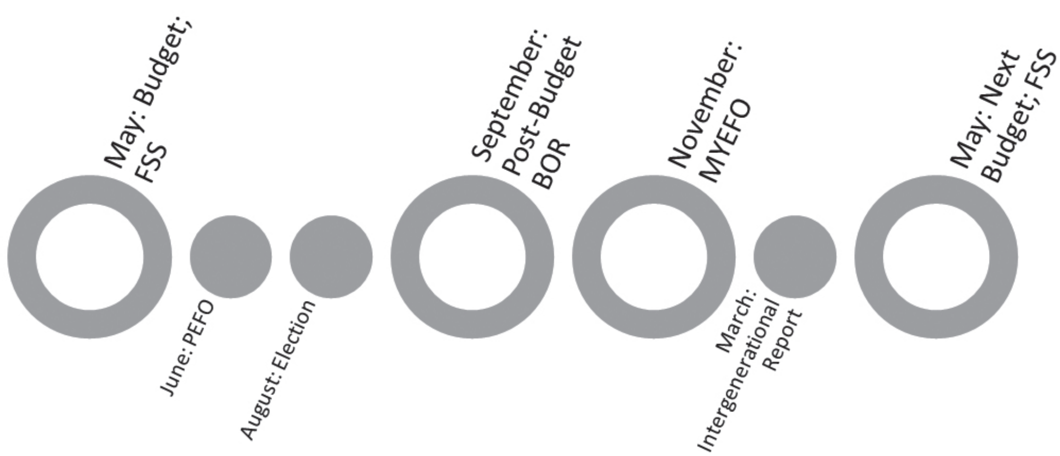
To provide a long-term aspect to the fiscal discipline objectives of the Charter, the Treasury produces an Intergenerational Report (IR) at least once every five years, usually releasing it in the month of March. The purpose of this report is to show how changes to Australia's population size and age profile may impact its economic growth, its workforce, and its public finances over the next 40-year period. For example, the 2015 Intergenerational Report draws attention to the rapid aging of Australia's population, which when coupled with low fertility rates (less than 2.0 children per woman), means that greater stresses will be incurred by public finances over the next 40 years, particularly with respect to healthcare and aged-care provision.[6]

In an election year, there are additional procedures stipulated by the Charter. A Pre-Election Fiscal Outlook (PEFO) is produced two months before the election in which budget estimates are updated by Treasury and the Dept. of Finance. PEFO also divulges to the public any decision of government since the last economic update was published, which ensures that the government, the opposition, the parliament and the public know the country's fiscal position before the election. The year 2016 is an election year in Australia, and the PEFO was released in late May, two months prior to the July 2 election date.

There are some additional clauses in the Charter which do not follow a timetable but which are triggered by significant changes to national financial statements. As an example, in certain cases where the face value of the stock and securities issued by the government increases by $50 billion or more since a previous Charter-related report or statement has been issued, then the Treasurer is expected to table a statement setting out reasons for the increase.

Following the lead of the United States (1974) and Canada (2006)[7], Australia also decided to instate a Parliamentary Budget Officer (PBO) in 2011 to advise legislators, particularly those of the opposition parties, on matters pertaining to the costing and analysis of budget policy. When this office was created, the Australian government amended the Charter of Budget Honesty to incorporate a role for the PBO within the annual budget process.[8] The Australian PBO is mandated to "inform the Parliament by providing independent and non-partisan analysis of the Budget cycle," which is

Figure 1: A Simplified Timetable of the Charter's Components With Respect to the Budget Process in Australia



The diagram above supposes (1) an election in the month of August; and (2) an intergeneration report is issued in that year. The larger dots represent fixed annual events, while the smaller dots represent contingent events.

similar to the stipulated role of the Canadian PBO,[9] but in order to effectuate this work, the Australian PBO has the benefit of several Memoranda of Understanding (MoUs) which enable it to collaborate with, and access information from, various government departments.

The Canadian PBO does not have similar or as strict MOUs with departments, but in terms of collaboration and access to information, its legislation provides that "the PBO is entitled, by request made to the deputy head of a department…to free and timely access to any financial or economic data in the possession of the department that are required for the performance of his or her mandate." [s. 79.3 (1) of the *Parliament of Canada Act*.] Furthermore, the Canadian legislation also stipulates that the "PBO may, in the performance of his or her mandate, enter into contracts, memoranda of understanding or other arrangements in the name of his or her mandate." [s.79.5(1) of the P*arliament of Canada Act.*] In Canada, the past issues related to access to information ended in Court in 2013, but the Court didn't conclude with a formal decision. Instead, a parliamentary remedy was suggested by the Court and was pursued. It culminated with a motion adopted in 2015 by the Joint Committee on the Library of Parliament.

With respect to the Charter's requirements, the Australian PBO is mandated to cost proposed budget policies for the opposition. In this sense, it serves as an instrument to level the playing field between government and opposition, since government already has the tools of Treasury and Department of Finance at its behest. Documentation from these departments includes costing details, while the PBO independently and separately costs the policies as well. In case of discrepancies, department officials and PBO staff may be summoned to parliamentary inquiries to explain the differences. This has happened on various occasions.[10]

These moving parts together build a more cohesive fiscal discipline framework. Collectively, they help to increase transparency by creating a regular stream of government reports that apprise the public, the legislature, and other government branches, of movements in the national fiscal balance. Some of these are event specific (e.g. PEFO), while others are short term in nature (MYEFO), while still others are very long-term by design (IR).

Many proponents argue that this integrated set of statements on budgeting, as demanded by the Charter, helps to foster a more democratic space that is conducive to the driving principle of the Charter: "sound fiscal management." However, in order to appreciate the ability of the Charter to achieve this idealized goal, it is important to first understand just what is meant by "sound fiscal management."

What is "sound fiscal management"?

The Charter defines the principles of "sound fiscal management" as comprising several components. Above all, it considers the management of financial risks faced by the nation in a prudent manner, "having regard to economic circumstances, including by maintaining […] government debt at prudent levels." This is supported by an expectation that fiscal policy contributes to (1) adequate national saving, and (2) to "moderating cyclical fluctuations in economic activity, as appropriate, taking account of the economic risks facing the nation and the impact of those risks on the Government's fiscal position", while (3) pursing taxation and spending in a manner "consistent with a reasonable degree of stability and predictability in the level of the tax burden; [while maintaining] the integrity of the tax system." These decisions are to be made with "regard to their financial effects on future generations."

When discussing the "financial risks" that must be managed in a prudent manner, the Charter specifically mentions certain groups of risks that it must target, including: risks arising from excessive net debt; commercial risks arising from ownership of public companies; risks arising from an erosion of the tax base; and risks arising from the management of national assets and liabilities.

Is this definition of "sound fiscal management" correct, comprehensive, or sufficient? Today, many Australian budget scholars seem to think that, in the broader scope of things, the Charter's definition is still insufficient because the document remains prone to "interpretive approaches", with high levels of subjectivity about various aspects of the abstract notion of "budget honesty", not least with respect to the definition of "sound fiscal management."[11] Furthermore, a sizeable consensus among budget scholars would seem to assert that the Charter could benefit from greater precision if it were to contain some form of concrete benchmarking against which to gauge government budgetary performance. Such benchmarks are sometimes referred to as "fiscal rules", and are more prevalent in European countries.[12] Nonetheless, it is important to remember in this regard that, as one budget scholar recently noted: "it would be a serious mistake to assume that there is, or could ever be, a set of accounting measures capable of giving precise, unambiguous and readily verifiable expression to given fiscal responsibility principles. Accounting measures are, by their very nature, imprecise and ambiguous."[13]

Assessing the success of the Charter

In the nearly 20 years since the promulgation of the Charter, various budget scholars, government officials, and parliamentarians have had different opinions on the adequacy of the Charter to serve its purported objectives of fostering greater budget discipline and stronger budget transparency, through the pursuit of the "sound fiscal management."

One poignant criticism arises from the logic that "less is more", whereby the surfeit of budget data produced in order to adhere to the Charter does not significantly increase transparency in the budget process. Rather, it results in an overproduction of fiscal data which in fact restricts the ability of decision-makers to conduct oversight. This point has been voiced in various parliamentary committee reports,[14] and it speaks to a long-standing debate among scholars of accounting and budgeting, that fiscal documentation adheres more to form rather than function; to the letter rather than the spirit, of transparency. To this point, former Australian Senator Andrew Murray conducted a review of the Charter in 2008 as part of the Kevin Rudd government's ''Operation Sunlight'' reforms. His review highlighted various shortcomings of Australia's existing fiscal responsibility legislation, most of which pertained to the idea that the Charter only requires governments to pay "lip service to principles of fiscal soundness, but is otherwise non-prescriptive about fiscal policy outcomes".[15]

A second criticism has been that the Charter is restricted, in that it cannot influence what are constitutionally defined parameters for parliamentary involvement in the budget process. As an example, in Australia, Section 53 of the Constitution prevents the Senate from amending bills for the "ordinary annual services" of government, which represents the majority of annual appropriations.[16] The Charter therefore operates within an existing budget ecosystem, and thus does not change existing legislative powers that are constitutionally enshrined. In other words, the Charter does not override existing parameters for legislative engagement in budgeting.

A third criticism comes from the practitioner experience of other countries and states, and it asserts that regulation of a "balanced budget" or fiscal discipline cannot, on its own, be the full guarantor of sound fiscal management. As evidence, the criticism points to the fact that states with balanced-budget laws have defaulted in the past; for example, New York defaulted in 1974 despite its constitutional balanced-budget requirement. However, this argument is more flimsy because it doesn't address the counterfactual: how many more states *would have* defaulted if they *didn't* have balanced-budget legislation? Simply because balanced-budget legislation cannot *compel* actors to meet fiscal targets, does not mean it cannot encourage them to exercise fiscal restraint. Furthermore, the fact that states are encouraged to adhere to fiscal prudence, rather than compelled to do so, is an inherent trade-off between the flexibility of governments to act and the discipline they must exercise. There are greater value judgments associated with this perspective. Looking at this from a more theoretical perspective, for fiscal legislation such as the Charter to work in a manner that *compels* as opposed to encourages discipline, there would need to be some additional elements present, including: clear and unambiguous fiscal targets; strong internal and external oversight of budgets to assess levels of compliance; and a strong coherence between the letter of the law and the spirit.[17] What makes these conditions very difficult to meet is that there is always a high degree of uncertainty about the future path of economic growth, particularly with respect to unforeseen economic shocks. Furthermore, there is no consensus among economists on what an ideal fiscal target is, which means that the fiscal discipline goals set into laws are based on the arbitrary nature of what target should be followed. Political parties differ in their fiscal philosophy: some emphasize balanced budgets, while others view the flexibility to run planned deficits as good fiscal policy.[18] Therefore, while balanced budget laws may be in place, they ought not to be a precursor for Charters of Budget Honesty. To address this, a Charter of Budget Honesty should explain how a government plans to meet whatever targets it sets, premised on its own fiscal agenda. Beyond this, It is also difficult to get the timing right on fiscal policy interventions to smooth out the economic peaks-and-troughs, and so many scholars have found that fiscal interventions can sometimes actually make things worse.[19]

Concluding Remarks

In sum, although there are some poignant criticisms of the Charter, it has come to form a cornerstone of Australia's national budget process. So, would such a Charter be suitable for other parliaments? The answer would seem to depend on what the goal of the charter would be. If, on one hand, the objective is to ensure full and rigorous fiscal transparency and discipline, then such a charter, or any other budget honesty mechanism for that matter, would be an insufficient piece of legislation on its own. If, on the other hand, the objective is to incrementally enhance the Parliament's fiscal engagement and budgeting rigour as part of a broader and more abstract commitment to "fiscal prudence", then the charter of budget honesty could be one component within that broader commitment.

Notes

1 The Charter of Budgetary Honesty (1998). Parliament of Australia. Canberra.

2 Robinson, Mark (1996). Can Fiscal Responsibility Legislation be Made to Work? *Agenda: A Journal of Policy Analysis and Reform*, Vol. 3, No. 4, pp. 419-430.

3 Kopits, George (2001). Fiscal rules: useful policy framework or unnecessary ornament? *IMF Working Paper Series*. 01/145. International Monetary Fund: Washington.

4 Government of Australia (2016). *Fiscal Strategy and Outlook*. Budget Papers Vol. 1. Canberra: Australia.

5 Government of Australia (2015). *Mid-Year Economic and Fiscal Outlook*. Canberra: Australia.

6 Australian Treasury (2015). *Intergenerational Report*. Canberra: Australia.

7 Chohan, Usman W. and Jacobs, Kerry (2016). The Presidentialisation Thesis and Parliamentary Budget Offices. *Parliamentary Affairs.*

8 *Parliamentary Service Amendment* (Parliamentary Budget Officer) *Act* (2011). Parliament of Australia. Canberra.

9 Chohan, Usman W, (2013). Canada and the Global Network of Parliamentary Budget Offices. *Canadian Parliamentary Review*. Vol 36. No. 3. Pp. 17-21.

10 Chohan, UW (2016). Business Briefing: How does Australia's policy costing body, the PBO, compare? *The Conversation Australia*. Interview. June 8.

11 Wanna, John (2010). Australia after Budget Reform: a lapsed pioneer or decorative architect? In Wanna, J., Jensen, L., and de Vries, J. (eds.) *The Reality of Budget Reform in OECD Nations*. Edward Elgar Publishing: Gloustershire.

12 Kopits, George (2001). Fiscal rules: useful policy framework or unnecessary ornament? *IMF Working Paper Series*. 01/145. International Monetary Fund: Washington.

13 Robinson, Mark (1996). Can Fiscal Responsibility Legislation be Made to Work? *Agenda: A Journal of Policy Analysis and Reform*, Vol. 3, No. 4, pp. 419-430.

14 Examples include the *Joint Committee of Public Accounts and Audit report on Accrual Budget Documentation* (2002), and the Australian Senate's *Standing Committee on Finance and Public Administration* (2007), titled "Transparency and accountability of Commonwealth public funding and expenditure".

15 Kirchner, Stephen (2011). Reforming Fiscal Responsibility Legislation. *Economic Papers of the Economic Society of Australia*. Vol. 30, No. 1, pp. 29–32.

16 *Commonwealth of Australia Constitution Act* (1901).

17 Robinson, Mark (1996). Can Fiscal Responsibility Legislation be Made to Work? *Agenda: A Journal of Policy Analysis and Reform*, Vol. 3, No. 4, pp. 419-430.

18 Chohan, Usman W. and Jacobs, Kerry. Public Value in Politics: A Legislative Budget Office Approach. *International Journal of Public Administration.*

19 See Robinson (1996) and Hemming (2003) for discussions.