
Report: Review of the arrangements between the Office for Budget Responsibility and the Welsh Government for the production of Welsh tax forecasts in the first operational year 2019-20

Introduction

1. This report provides the detail of the review of the arrangements between the Office for Budget Responsibility (“the OBR”) and the Welsh Government for the production of Welsh tax forecasts. The requirement to review was agreed by both organisations and is provided for in the *Terms of Reference*,¹ which also set out the detail of their arrangement.
2. At the time of the review (summer 2020) one complete annual cycle of the new forecasting arrangements had been undertaken.

Background to the current arrangements

The fiscal framework

3. The requirement to establish independent arrangements for the provision of Welsh tax forecasts is provided for in *The agreement between the Welsh Government and the United Kingdom Government on the Welsh Government’s fiscal framework*² (“the fiscal framework”). For the first two years of devolved/Welsh tax forecasts (for the budgets relating to 2018-19 and 2019-20) the Welsh Government temporarily produced its own forecasts which were independently assured by Bangor University. However, the fiscal framework required that a forecasting arrangement be established with an organisation independent of the Welsh Government and so the Welsh Government and the OBR entered into a formal arrangement for the provision of Welsh tax forecasts for the 2020-21 budget onwards.

Governing documentation

4. The arrangements for the production of Welsh tax forecasts are governed by the following three documents:
 - *The Memorandum of Understanding between the Welsh Government and the OBR*³ (“the MoU”) - this provides for the overarching arrangements. This agreement was already in place following tax devolution but was reviewed once specific forecasting arrangements between the two organisations were established. This document was originally produced by the OBR in full consultation with the Welsh Government
 - *The Terms of Reference for the provision of Welsh tax forecasts by the Office for Budget Responsibility for the Welsh Government*⁴ – this document was co-produced by the two organisations and sets the detailed requirements of the tax forecasting arrangements that took effect from 2019-20
 - *Financial framework between the Welsh Government and the OBR*⁵ (“the financial framework”) – this document was produced by HM Treasury in consultation with the OBR and the Welsh Government. It details the financial settlement between the two organisations to cover the costs of the production of Welsh tax forecasts

¹ The Terms of Reference for the provision of Welsh tax forecasts by the Office of Budget Responsibility for the Welsh Government see <https://obr.uk/download/terms-reference-welsh-government-obr/>

² Paragraph 52 [The agreement between the Welsh Government and the United Kingdom Government on the Welsh Government’s fiscal framework \(December 2016\)](#)

³ [The Memorandum of Understanding between the Welsh Government and the OBR](#)

⁴ Available at; <https://obr.uk/download/terms-reference-welsh-government-obr/>

⁵ [Financial framework between the Welsh Government and the OBR](#)

5. This review concluded that the arrangements had coped well during an unusual first year of operation. It recommended modest changes to the terms of reference and financial framework that have been adopted.”

Operational context 2019-20

6. The *Terms of Reference* were developed and agreed with the expectation that a typical fiscal year in Wales would see a Draft Budget published in early autumn, at least eight weeks of scrutiny by the Senedd, followed by a Final Budget published in early winter. The UK Government Autumn fiscal event would usually take place in between the Welsh Government’s publication of its Draft and Final Budgets.
7. The first year of operation under these *Terms of Reference* was not a typical year. There was a great deal of uncertainty around the timing of the publication of the Welsh Government’s 2020-21 Draft Budget last year due to three unusual features of the fiscal year:
- the UK Government one-year Spending Round in September;
 - the UK General Election in December; and
 - consequently, no UK Government Autumn Budget or updated macro-economic forecast.
8. Welsh Ministers delayed the publication of the Draft Budget until after the Spending Round and then the election in the hope that the UK Government would publish its Budget and macro-economic forecast, providing a more up to date Welsh fiscal position. The lack of an autumn UK fiscal event meant that the publication of the Welsh Government’s Draft Budget was delayed until December 2019, with the forecasts based on economic determinants from March 2019. This meant that the Welsh Government had to complete a whole Budget cycle without an updated macro-economic forecast.
9. The unusual timetable also affected the OBR’s activities through the year, including the key deliverables from the OBR under these terms of reference – the two *Welsh Taxes Outlook*⁶ reports – which were required at different points in the calendar year and with different inputs to those expected when the terms were agreed. The OBR was able to fulfil its responsibilities in these circumstances, publishing its first *Welsh Taxes Outlook* alongside the Welsh Government’s Draft Budget, and an update alongside the Final Budget, as required.

The review: summer 2020

Review activity

The following is a summary of the activities which have led to the publication of this report.

- Welsh Government and the OBR agreed the scope of the review
- Both organisations held separate team discussions to respond to the scope questions
- The written outputs of these discussions were shared between organisations
- The data captured for these discussions was used to draft the review document
- The draft review document was shared with both organisations for factual checking and to ensure views were captured and reflected fairly

⁶ [Welsh Taxes Outlook](#) (OBR) (December 2019) and update (February 2020)

- The existing governing documents were reviewed to ensure that they remain relevant and suggested amendments made if necessary
- Final versions of the report and the amended governing documents were considered and cleared by the OBR's Budget Responsibility Committee and the Welsh Government

Scope

10. The following specific questions and areas for consideration were agreed by both the Welsh Government and the OBR to be within the scope of the review:
- A. Did the cost of the arrangements reflect the activity undertaken?
 - B. Were suitable engagement activities identified and undertaken?
 - C. Did the process of forecasting and challenge run smoothly?
 - D. Are the documents underlying the arrangements fit for purpose (the MoU, Terms of Reference and the financial framework)? Are there any scenarios where the documents would not provide the framework needed and if so, how should they be amended?
 - E. Quality of the two publications (the *Welsh Taxes Outlook* documents)
 - F. Reflections on the content of future *Welsh Taxes Outlook* publications, what these should include?
 - G. Future plans for evaluating forecasts, including considering where these should be published.
 - H. Lessons for future years including any scenario planning.
 - I. What value or benefits (beyond the Terms of Reference) gained from the arrangement?

Response to the areas for review

11. This next part of the document sets out the responses of both the Welsh Government and the OBR to each of the review questions/topics.

Costs

12. Provision for setting and recovering costs are set out in the financial framework. The key elements of which are that:
- the Welsh Government and the OBR will agree the precise costs of funding every year – *the Minister for Finance wrote to the OBR in March 2020 confirming funding of £100k for the services being provided by the OBR in the financial year 2020-21. A copy of this letter is at **Annex A***
 - the Chair of the OBR writes to the Welsh Government 'Cabinet Secretary for Finance' setting out how the funding from the Welsh Government has been used by the OBR – *a copy of this letter dated February 2020 for the financial year 2019-20 is at **Annex B***
 - The Welsh Government will fund the OBR via a Budget Cover Transfer to HM Treasury ahead of the start of the financial year in which the services are to be provided

A. *Did the cost of the arrangements reflect the activity undertaken?*

13. Both teams felt that the OBR had fulfilled its requirements and that the costs accurately reflected the services provided as described in the letter at **Annex B**.

14. In addition, the Welsh Government felt that the value achieved from the arrangements was high. This is reflected in the response to question 'I'

Recommendation:

15. No recommendations based upon the feedback from either organisation but a review of the financial framework document suggests that the document should:
- be updated to include the amended title of the Welsh Government Minister for Finance & Trefnydd
 - be updated to include the new name of the Senedd
 - be reviewed to ensure that the description of the costs in its Annex is flexible enough to cover the circumstances of any given operation year

Engagement

16. Increasing awareness of the fiscal context and building Welsh expertise is vital to the devolution process. Engaging in Wales to assist with this is a key requirement placed on the OBR as set out in paragraph 21 of the *Terms of Reference*. The OBR is required to engage with appropriate individuals and organisations (including the Senedd's Finance Committee) twice during the financial year: once in the summer following the UK Government's Spring Statement; and second, following the UK Government's Autumn Budget, where for both events they provide an update on their latest forecasts.
17. In response to the engagement provision, the following activities were undertaken by the OBR in Wales:
- Technical briefing given in the Senedd, offered to all MS and their staff (January 2020)
 - Attendance at Finance Committee (June 2019 and January 2020)
 - Attendance and presentation given at the first annual Welsh Taxes Conference (July 2019)
 - Meet and greet/information exchange meeting with officials from the Welsh Government (July 2019)
 - Presentation at a Wales Governance Centre event (July 2019)

B. Were suitable engagement activities identified and undertaken?

18. Both teams believe that the engagement requirements in the *Terms of Reference* were clear and that the engagement effort in the first year of operation was appropriate. Officials from both organisations also regularly engage with each other both formally and informally to deliver the Welsh tax forecasts and a good working relationship has been developed. Additionally, Welsh Government officials were pleased with both the willingness of the OBR to engage in Wales, and the breadth of the engagement, which was excellent.

Recommendation:

19. The willingness of the OBR to engage in Wales and the quality of the engagement is an important part of developing tax and forecasting capability in Wales. The review concluded that the engagement objective was well-achieved in the first year of operation, the quality was high and the number of opportunities exploited exceeded expectation.
20. Circumstances surrounding this current (second) year of operation are very different and the ability to engage in Wales has obviously been significantly diminished by the Covid-19 crisis. The Chair of the OBR attended the Senedd Finance Committee in September 2020, and Andy King, the Budget Responsibility Committee fiscal expert, presented at the annual Welsh Taxes Conference in October 2020.

21. In order to fulfil the requirements set out in the *Terms of Reference* and to ensure value for the funding already provided to the OBR, it is recommended that the Welsh Government and the OBR continue with the virtual approach to engagement. It will also be important to ensure the new Chair of the OBR has sufficient early engagement activity to provide him with the necessary background on the fiscal, economic, and institutional situation in Wales.

Producing the forecasts

C. Did the process of forecasting and challenge run smoothly?

22. Both organisations felt that the forecasting process and the associated challenge meetings worked well. The OBR noted that Welsh Government analysts provide high quality forecast returns for the fully devolved taxes. The process is an iterative one, with the OBR providing updated determinants and the Welsh Government returning revised revenue forecasts over a number of rounds. The challenge meetings are an opportunity to discuss aspects of the forecasts and, in the light of these discussions, for the OBR to make forecasting judgements where necessary. This process allows the OBR to quality assure the forecasts, make refinements and address issues in a timely fashion. They also found it useful to review forecast models and make judgements during the quieter summer months. Both organisations felt that regular engagement, provision of information at the right time and good communication supported the smooth running of the process.

23. Welsh Government officials also cited the willingness to incorporate flexibility into the process was vital during what was an unpredictable year.

Recommendation: see 'D'

Governing documentation

D. Are the documents underlying the arrangements fit for purpose (the MoU, Terms of Reference and Financial Framework)? Are there any scenarios where the documents would not provide the framework needed and if so, how should they be amended?

24. Both organisations reported that the governing documentation provided an adequate framework for operations. It was noted by the Welsh Government that although there were no issues with the documentation, their existence had not resolved operational issues during the first year. Instead the successful completion of the process had relied on the good working relationships in place to get things done under unusual circumstances. If there had been a reliance on the *Terms of Reference* in particular then some difficulties may have been experienced, but this is an untested area after the first year of operation.

Recommendation:

25. 2020-21 will be another atypical year. Flexibility will be needed again to deliver the two *Welsh Taxes Outlook* publications, making use of the good working relationships in existence between the two organisations rather than the stated requirements in the *Terms of Reference*. Without the preferred situation of fixed dates for UK fiscal events to plan around, it is recommended that the *Terms of Reference* be adjusted to ensure the requirements placed on either organisation are flexible enough to account for atypical years. This would be of particular

importance if it were not possible to rely on positive working relationships. The amendments proposed to the financial framework document are covered in paragraph 15 above.

The reports

E. Quality of the two publications (the Welsh Taxes Outlook document)

26. The quality of the publications was deemed to be excellent by the Welsh Government officials and any feedback received by them from stakeholders has been positive. The OBR were happy with the quality of their reports and welcomed the assistance of the Welsh Government in helping to assure this.

F. Reflections on the content of future Welsh Taxes Outlook publications, what these should include

27. The OBR stated that the main focus of the *Welsh Taxes Outlook* would continue to be the devolved taxes but that the reports would reflect current forecasting issues as they arise, including key determinants and may include bespoke analysis if required. The reports will also consider the performance of past forecasts against the outturn data. The OBR and the Welsh Government are considering the possibility of expanding the *Welsh Taxes Outlook* in the future to include non-domestic rates.

G. Future plans for evaluating forecast including considering where these should be published

28. The OBR and the Welsh Government have discussed forecast evaluation. OBR will review its 2020-21 forecasts for the fully devolved taxes in its 2021 *Welsh Taxes Outlook* publication. OBR will only be able to evaluate its forecast for the Welsh rates of income tax in 2020-21 after outturn information is published in the summer of 2022.

29. In the meantime the Welsh Government will publish an evaluation of its own forecasts for 2019-20, as assured by Bangor University.

30. A more general evaluation note on the forecast process for 2020-21 was made by the Welsh Government. They stated that the biggest impact of the disruption to normal processes had been that a whole Budget setting process had been experienced without an updated macro-economic forecast, because of the UK election and absence of an Autumn Budget in 2019. The forecast was adjusted in the Welsh Government's 1st Supplementary Budget of 2020 to take into account the OBR's March 2020 *Economic and Fiscal Outlook*.

Lessons and benefits

H. Lessons for future years including scenario planning

31. The OBR stated that their main challenges during the first year of operation arose from the shifting UK Government fiscal event timetable. Having a clearer and more certain timetable for UK fiscal events would enable the OBR and Welsh Government to plan more easily and would have ensured a smoother and more efficient process. The other challenge, in part caused by the uncertain timings, was around the lead times required translating a technical document into Welsh. The lessons learned will be used to minimise risks around future publications, although it should be noted that any issues experienced by the OBR did not affect the publication

requirements.

32. The Welsh Government was in full agreement that uncertainties around the UK Government's timetable for fiscal events presented the biggest challenges in this first year. The flexible approach adopted by both organisations and good levels of communication ensured that the process was completed successfully. In light of the timing uncertainties, it might be better for requirements in the *Terms of Reference* to be aligned to events rather than specific dates. It might be necessary to review the arrangements again in future, given the unusual circumstances in the first year of operation and the fact that Covid-19 means that the second year of operation will be unusual too.

1. What value or benefits (beyond the Terms of Reference) do you gain from the arrangement?

33. Both organisations identified significant benefits to their respective organisations as a consequence of entering into the tax forecasting arrangements.

34. The benefits identified by the OBR were:

- it has strengthened and enhanced their understanding of issues related to Welsh devolved tax forecasting. Engaging with Welsh Government has given them greater insight into related issues such as the cross-border effects that might arise if the Welsh rates of income tax deviated from those set by the UK Government.
- there have been spill-over benefits to other OBR publications, for example the framework that they developed for the income tax chapter of the *Welsh Taxes Outlook* will be used in their *Devolved tax and spending* report.
- they have gained from exposure to a broader set of stakeholders. Their engagement in Wales, particularly at the Welsh taxes conference, raised the profile of their work but also enhanced their understanding of Welsh-specific economic and fiscal issues.

35. The benefits identified by the Welsh Government were:

- being able to tap into the experience of established and highly respected forecasters and the sharing of that experience and knowledge is invaluable. It allows the Welsh Government to access what is arguably the biggest centre of fiscal expertise in the UK, one which is also plugged into the UK system and other devolved nations
- it has strengthened relations with UK Government counterparts, as Welsh Government officials attend the same meetings and challenge process with OBR that other government departments involved in tax forecasting do.
- their cultures are similar – the OBR understand government deadlines and are used to prioritising and being flexible – this was hugely important last year when the timings of fiscal events were not as expected
- as the UK's official independent watchdog, forecasts from the OBR carry considerable credibility and independence

Conclusion

- The first year of operation was a successful one, despite the uncertainty arising from the timing of UK fiscal events.

- A clear timetable for UK fiscal events would enable the arrangements to operate in a smoother and more efficient way.
- The success in the first year can be attributed to good working relationships, a willingness to engage and a flexible approach.
- Benefits accrued to both organisations beyond the deliverables required by the *Terms of Reference*.
- In the absence of a settled timetable for UK fiscal events, there may never be a typical year and therefore successful future forecast delivery will be contingent on a continuing flexible approach and good communication.

Annex A – MFT funding letter

Rebecca Evans AC/AM
Y Gweinidog Cyllid a'r Trefnydd
Minister for Finance and Trefnydd



Llywodraeth Cymru
Welsh Government

Ein cyf/Our ref RE/00048/20

Robert Chote
Chairman
Office for Budget Responsibility

c/o: Marcus.Hanson@obr.uk

18 March 2020

Dear Robert,

Thank you for your letter setting out the detail of the costs incurred in 2019-20 by the Office for Budget Responsibility in fulfilling its role as provider of independent tax forecasts for the Welsh Government.

As agreed, the Welsh Government will provide the same budget of £100,000 for the coming financial year. We are also due to review the arrangements this summer, in the light of our experiences of the first year. It may be difficult to draw firm conclusions at this stage, given the unusual context and non-standard scheduling of fiscal events over the last year. However, there will still be lessons to be learnt. Thanks to your organisation's ability to adapt to shifting circumstances, we have good evidence that the system is flexible enough to deal with unexpected changes.

I would like to thank you and your colleagues for your part in making the new arrangements a success, including your engagement work in Wales and the excellent first *Welsh Taxes Outlook* report.

I look forward to the continued smooth running of the independent forecasting arrangements.

Yours sincerely,



Rebecca Evans AC/AM
Y Gweinidog Cyllid a'r Trefnydd
Minister for Finance and Trefnydd

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Rydym yn croesawu derbyn gohebiaeth yn Gymraeg. Byddwn yn ateb gohebiaeth a dderbynnir yn Gymraeg yn Gymraeg ac ni fydd gohebu yn Gymraeg yn arwain at oedi.

We welcome receiving correspondence in Welsh. Any correspondence received in Welsh will be answered in Welsh and corresponding in Welsh will not lead to a delay in responding.

Annex B – OBR costs letter



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18 February 2020

Dear Rebecca

The OBR's funding from the Welsh Government

As required by the Financial Framework between the Welsh government and the OBR, I am writing to set out how the funding from the Welsh Government for 2019/20 has been used by the OBR to deliver the requirements of the Terms of Reference.

A breakdown of the £99,727 spent within the £100,000 budget allocated to the OBR by the Welsh Government is set out in the table below. The largest cost was staff time at £77,659, with the production of the *Welsh Taxes Outlook* and our engagement trips to Cardiff occupying significant amounts of staff time across the paygrades.

Our next biggest cost was the leasing of office space for our new analyst at £9,667, whilst the translation and printing of the report totalled £6,739. Travel to and from engagements in Cardiff, along with hotel accommodation, added a further £2,562. These together accounted for the vast majority of our spending, with the remaining funding spent on new IT equipment, dedicated on-the-job training for our new analyst and the development of new pages on our website in both English and Welsh.

	Estimated cost, £	Actual cost, £
Total staff costs	72,300	77,659
Non-staff costs	27,700	22,068
Office costs	11,100	10,867
of which		
Lease of office space		9,667
Cost of IT equipment		1,200
Printing, website and translation	11,000	7,639
of which		
Printing and Welsh translation		6,739
Website development		900
Travel and accommodation	3,600	2,562
Training and development	2,000	1,000
Total costs	100,000	99,727

Best regards, Robert

Robert Chote
Chairman