HM Treasury

Lord Wood of Anfield
Chairman, Economic Affairs Committee
House of Lords
London
SW1A OPW

24 June 2026

Dear Lord Wood,

I am writing to respond to the Committee's inquiry into the UK's fiscal framework. I would like to thank the Committee for the work that has gone into the report and for facilitating debate and discussion on such an important topic.

This government made significant reforms to strengthen the fiscal framework in 2024, including by:

- Setting fiscal rules that put debt on a sustainable path and prioritise investment to support long-term growth;
- Delivering the commitment to one major fiscal event a year to ensure stability for households and businesses while maintaining the transparency benefits of having two forecasts per year;
- Committing to hold regular multi-year Spending Reviews so that public services and departments have certainty on their funding;
- Introducing the fiscal lock to ensure that no government can sideline the Office for Budget Responsibility (OBR);
- Improving the transparency of spending information that the Treasury shares with the OBR;
- Committing to consider a wide range of metrics to inform a full assessment of the sustainability of the public finances and seek to improve sustainability over time;
- Requiring the OBR to report on the long-term economic impacts of capital investment and government policies in its forecast.

The fiscal framework supports delivery of the government's fiscal strategy to reduce borrowing while protecting investment. That strategy is working:

- Borrowing had been stuck at around 5% of GDP for 4 years – but because of the actions of this government, in 2025-26 borrowing fell by 1 percentage point to its lowest level for six years at 4.2%.

- Net financial debt is forecast to fall from 2028-29 and is forecast to be lower by 2029-30 than it is today.

- We are maintaining over £120 billion additional capital investment over the Parliament compared to the previous government’s plans, raising the level of GDP by over 0.4% after 10 years, and by 1.4% in the long run.

Our actions to repair the public finances have prepared Britain to better weather the conflict in Iran. At the Spring Forecast, inflation was at 3% and set to fall to target, a lower base than at the outset of the Russia-Ukraine conflict when inflation was high and rising, and borrowing was set to fall more over this Parliament than in any other G7 economy.

The annex to this letter responds to the full conclusions and recommendations detailed in the report, outlining the actions this government is taking to ensure the public finances remain on a sustainable path.

Torsten Bell

TORSTEN BELL MP
MINISTER FOR PENSIONS

HM Treasury

Annex (detailed response to recommendations)

The government welcomes the Committee's work on its report 'Fortifying the fiscal framework' and notes the conclusions and policy recommendations that the Committee has made. The Committee's conclusions and policy recommendations are set out below in bold as they appear in the summary of the report, with the government's response below each group of recommendations.

The fiscal rules

"1. We heard concerns that the current rules can be met without achieving a reduction in debt. The three-year target makes the challenge more pressing for the Government, and this is to be commended, but the fundamental point remains: the rules can be met every year and yet debt continue to rise. Moreover, the need to adjust to major shocks applies to all targets so need not rule out consideration of a fixed-year target.

2. Policy recommendation: The Government should set out an additional debt target which will show cumulative performance over three years such that in normal times debt in the third year is lower than in the first year. This will add credibility to the existing target."

The government has been clear that the fiscal rules are non-negotiable. The design of the fiscal rules strikes an appropriate balance between maintaining a clear medium-term anchor and allowing near-term adjustments in response to changing economic conditions before the three-year target. The IMF has welcomed the government's move to a three-year target, noting in their most recent Article IV report that "the common three-year horizon for the rules and the spending review will make fiscal plans more credible, while still allowing time for gradual adjustment in response to shocks." The alignment of the fiscal rules with Spending Review timelines means that the rules are met based on set departmental spending plans, as well as legislated tax policy.

The fiscal rules set a minimum constraint. In the most recent OBR forecast (March 2026), net financial debt (public sector net financial liabilities) is forecast to fall from 2028-29, a year earlier than mandated by the fiscal rules, then falls in every year, and is lower by 2029-30 than it is today.

“3. When the Government operates with a small fiscal buffer, the potential for non-compliance with the fiscal rules increases, leading in turn to speculation about policy measures to ensure compliance; this encourages a pre-occupation with the headroom figure itself. We also note that setting a larger fiscal buffer at the start of the fiscal period would make it more likely to achieve an actual reduction in debt. The previous reductions in the size of the buffer are, we believe, a cause of substantial policy volatility. Whilst recent increases in this buffer are welcome, they are insufficient.

4.Policy recommendation: The Government should commit to operating with substantially larger buffers that reflect the unavoidable forecast errors in the OBR’s projections used to assess compliance with the fiscal rules.”

At Budget 2025, the government took the responsible decision to build more headroom against the stability rule to the highest level in four years, to provide the buffer to weather shocks and the flexibility we need to respond to them, enabling more policy certainty and stability for households and businesses.

The OBR did not assess performance against the fiscal rules at Spring Forecast – however their forecast showed headroom against the stability rule had increased since the Budget from £21.7bn at the Budget to £23.6bn in 2029-30, with headroom against the investment rule also higher at £27.1bn. The OBR noted in their analysis at Spring Forecast that this “slightly exceeds the average absolute pre-measures forecast-to-forecast deviation in our most recent 10 forecasts”. The OBR’s forecasts are central, which means that they are an estimate of the middle of a range of possible outcomes, and the OBR note that risks are “broadly evenly balanced to the upside and downside”.

Furthermore, the government has made changes to support one fiscal event a year, while maintaining the transparency of having two forecasts per year. In line with recommendations made by the IMF, the government has legislated so that the OBR will now only assess the fiscal rules once per year at the Budget, when the government will set out its fiscal strategy. This will help to further strengthen stability.

More broadly, the government’s approach to fiscal policy is determined by the Treasury’s objectives for fiscal policy as set out in the Charter for Budget Responsibility, to support sustainable economic growth and the provision of high-quality public services and investment across the UK, through the effective management of the public finances and sustainable taxes and borrowing. This involves:

- taking decisions that support fiscal sustainability and safeguarding intergenerational fairness through a strong balance sheet;
- prioritising investment to support long-term growth and funding high-quality public services while delivering value for money for the taxpayer;

- a clear commitment to fiscal transparency and strong institutions through affirming the independence of the OBR and ensuring that fiscal policy is supportive of monetary policy.

"5. Repeated changes to the fiscal rules over the years have undermined the credibility of the fiscal framework and irrespective of their merits, further modifications must be seriously considered within this context. A target that can be met so long as debt is falling in a final year compared to the penultimate year, even when debt ends up higher than in the present year, remains a serious flaw in the fiscal framework and its retention will only serve to detract from the all-important perception that the Government means what it says. In view of the challenges of net zero, an ageing population, a commitment to increased defence spending and stagnating productivity growth which are already upon us, this matters more than ever. As such, the rules must encompass a stipulation that debt should fall in the immediate years ahead to allow appropriate headroom.

6. <u>Policy recommendation:</u> Any new rules should be formulated as part of a concerted, in-depth consultation exercise conducted in a period where there is no formal political campaigning."

The Chancellor has been clear our fiscal rules are non-negotiable.

The government considers that it is right that fiscal rules are set by the Chancellor, in line with the government's economic priorities and fiscal strategy. The government's economic priorities and fiscal strategy were set out in its manifesto, prioritising investment within a robust fiscal framework.

HM Treasury regularly engages relevant stakeholders and experts, as well as those from other countries. The government's fiscal rules are legislated for through the Charter for Budget Responsibility, which is voted on by the House of Commons, providing an opportunity for Parliamentary debate and scrutiny.

From this fiscal year (2026-27), the fiscal rules target the third year of the forecast, which binds near-term decisions while still providing space for macroeconomic adjustment and the operation of the automatic stabilisers in the first two years of the forecast. The rationale for moving to a rolling rule rather than a fixed rule is that it avoids the need to make sharp policy adjustments in response to small changes in the forecast or economic shocks. With a fixed rule, as the target grows nearer, adjustments like in-year savings or tax rises become more challenging and economically damaging. A rolling target instead provides a medium-term anchor to support stability and sustainable public finances.

The fiscal council

"7. The OBR is a valuable component of the UK's fiscal framework. They substantially enhance the transparency of fiscal policy. Their role is that of an impartial judge of the

Government's compliance with its own rules, not a policy decision maker. We commend the Government's continued commitment to the independence and value of the OBR and its role within the fiscal framework. While it is not within our remit to investigate the recent pre-Budget process, the OBR's independence should not prevent a close and continuous working relationship between the OBR and the Government and efforts should be made to ensure this proceeds more smoothly.

8.The OBR does not set the fiscal rules. Their role is to produce forecasts and those forecasts are used to assess the Government's compliance with its own fiscal rules. This compliance is an entirely self-imposed constraint that the Government is free to set aside. They can reject the OBR's forecast and claim compliance with the rules based on their own assessment of the future path of the public finances, or they can reject compliance with the rules themselves (as was done following the 2008 global financial crisis). The perception that the OBR prevents the Government from making autonomous decisions is mistaken."

The OBR's independent scrutiny, via its economic and fiscal forecasts, underpins the credibility of the government's fiscal policy. The government values the OBR's vital role in ensuring we have a robust and transparent fiscal framework which is why the first piece of legislation passed by this government introduced the fiscal lock, ensuring no government can sideline the OBR. The OBR has been widely recognised as reducing forecast bias.

As set out in the Charter for Budget Responsibility, the government has adopted the OBR's fiscal and economic forecasts as the official forecasts for the Budget Report. The government sets its fiscal strategy and policy, underpinned by the fiscal rules, based on the government's objectives for economic stability, growth and public services.

"9. Policy recommendation: In line with international best practice, the OBR should continue to carry out two forecasts per year. Although doing so will increase the likelihood of pressure on the Government to make fiscal policy announcements in response to assessments of failure to comply with the rules or minimal headroom, this is counteracted by the increased likelihood of greater changes in assessment between forecasts if they are carried out only once a year. The balance of considerations favours two forecasts with one fiscal event.

10. Policy recommendation: The Government should change the timing of the Spring forecast so that the length of time between the two forecast events is closer to six months. This would reduce the pressure to announce policy in the Spring Statement when there is more than six months until the Budget."

The government welcomes the Committee's support for the government's policy to hold one major annual fiscal event, while maintaining the transparency benefits of having two official forecasts in each year. We value the OBR's vital role in ensuring economic and fiscal transparency, and the OBR will continue to publish two forecasts a year.

In line with recommendations made by the IMF, the OBR will now only assess the fiscal rules once per year at the Budget, when the government will be setting out its fiscal strategy. This will help create a more predictable framework and strengthen stability – giving businesses and households greater certainty to plan and invest.

Decisions on the timing of Budget and Spring forecasts are taken by the Chancellor based on a range of considerations. The government does not comment on the specific dates for OBR forecasts until they have been announced to Parliament and the OBR has been appropriately notified.

"11. We do not think it is justified to criticise the OBR based on its overall forecasting record. While there is a strong case that the OBR should have made an earlier correction to its over-optimistic productivity forecast, the productivity growth error is merely one of the factors, alongside external shocks and changes to government spending plans, that explains the forecast error. The OBR has an estimable track record of reviewing its own forecast performance and we see no reason to change its current approach.

12.As with many of the issues considered over the course of this inquiry, the concern with the OBR's track record is a function of the Government's decision to operate with very little headroom. Were this not the case, the consequences of changes to the OBR's forecast would be minimal.

13. <u>Policy recommendation:</u> Assuming the Government keeps to its commitment to holding one fiscal event a year, revisions to the OBR's approach to forecasting should be made in advance of the Economic and fiscal outlook produced for the Statement to Parliament. This will decrease the potential for policy volatility by allowing the Government sufficient time to reflect upon the impact on compliance with the fiscal rules."

As the government's independent forecaster, the OBR has full discretion over the judgements underpinning its forecasts. All forecasts are uncertain and there are inherent difficulties in making accurate predictions in a complex environment and especially in the face of shocks. The OBR is required by law to annually assess the accuracy of its previous economic and fiscal forecasts compared to data outturns, which it does in its Forecast Evaluation Reports. This serves to identify lessons for future forecasts, to improve forecasting accuracy and ensure transparency in the OBR's judgements and methodologies.

These reports have shown that the OBR's forecasting accuracy has been comparable to that of external forecasters and more accurate than the forecasts produced by HM Treasury before the OBR was established.

“14. Policy recommendation: The OBR should continue to take the Government’s word on the policies it will implement in its main forecast. That said, the OBR should in its analyses make clear its assessment of the uncertainties around the impact of stated policies and refer to the established history of governments failing to follow through with announced policy (as it has, for example, in its analysis of fuel duty). We welcome this work of setting out forecast sensitivities to previous history.”

The government agrees the OBR should continue to take government policy as stated. The Budget Responsibility and National Audit Act (2011) sets out that the OBR “may not consider what the effect of any alternative policies would be”. The Charter for Budget Responsibility requires the OBR forecasts to contain an analysis of the risks surrounding the economic and fiscal outlooks.

“15. Dynamic scoring is a useful tool for the OBR in the production of its forecasts and we welcome its recent guidance on its approach to scoring the impact of government policy. Despite understandable frustrations at the OBR’s claims that some policy proposals fail to meet the threshold, the OBR should be commended for its commitment to evidence-based analysis. We recognise that there will always be those who disagree with the assumptions in the OBR’s model, but it is for the government of the day to make its case. Such differences are unlikely to have an impact in a three-year timeframe. Further, the fact that the OBR does not score a policy should be no barrier to the Government adopting it. If it proves to be more beneficial than could be evidenced at the time of implementation, this is all to the good and will eventually be reflected in the OBR’s projections.

16.Once again, controversy over such disagreements is only heightened when the OBR’s decisions in this regard have an impact on governments’ compliance with the fiscal rules. If they operated with a greater buffer, there would be no immediate difficulty to be faced should the OBR disagree with the Government on the positive impact on potential output of a given policy. This further strengthens the conclusion that the Government should operate with an increased buffer.

17.There is a clear case on the grounds of objectivity and legitimacy for the OBR continuing to construct the forecasts.

18. Policy recommendation: Responsibility for producing the forecast should remain with the OBR. However, we do not believe it necessary for dialogue with the Government to be restricted in order to preserve independence and both the OBR and the Government should continually work to improve cooperation between relevant teams. The OBR is mandated to publish its own view at the end of the forecast process and should be able to resist any pressure from the Government for a different outcome.”

The government agrees with the Committee’s conclusion that the economic and fiscal forecast should be produced independently by the OBR, rather than the Treasury. HMT has a close, collaborative working relationship with the OBR at ministerial and official level and while we support them in fulfilling their duties, their independence is respected at all times. The OBR have also described the relationship as “highly collaborative”. HMT will continue to work closely with the OBR to ensure that it has the information it needs to produce its forecasts. In recent forecast publications, the OBR have stated “We have been provided with all the information and analysis that we requested and have come under no pressure from Ministers, advisers, or officials to change any of our conclusion”.

The government values the OBR’s vital role in ensuring we have a robust and transparent forecast. Credible, independent analysis helps ensure that the government has sustainable and credible economic and fiscal plans. The government considers that it is right that the official forecasts are produced independently by the OBR to avoid any perception of bias, but the Chancellor has been clear that these forecasts are not our destiny.

Growth is the central mission of the government, and the government prioritises this in policymaking. Forecast judgements on the impacts of policy on growth are made by the independent OBR, and where impacts are not scored this does not prevent the government taking policies forward. There are clear examples of growth-supporting policies that have not been scored by the OBR, for example action to reduce elective surgery waiting lists, and aspects of planning and infrastructure reform. These have nonetheless been pursued, demonstrating that OBR scoring does not determine whether a policy proceeds.

The government must also take a longer-term view of economic policy, including impacts that extend beyond the OBR’s five-year forecast horizon. The updated Charter introduced by this government requires the OBR to analyse and report on the impacts of capital investment or other new policies beyond the forecast horizon where these may be material.

“19. Policy recommendation: Given that a number of organisations already assess General Election manifestoes, we do not think the OBR should score manifestoes. The most recent fiscal forecast and the report on longer term fiscal risks and sustainability should however provide a framework for economic debate during the election period.”

The government agrees with the Committee’s conclusion that the OBR should not take a greater role in scoring manifestos.

Successive independent external reviews including the 2025 External Review and the OECD review in 2020 have highlighted the OBR’s clearly defined remit as a core strength and have cautioned extending this into politically contentious areas such as costing opposition policies. Doing so could risk the OBR’s credibility and undermine confidence in its impartiality.

“20. The *Fiscal risks and sustainability* report is as important as the Economic and fiscal outlook. The primary reason for assessing compliance with the fiscal rules is to improve the long-term prospects of the public finances. We are disappointed by the insufficient attention given to the report, as shown by the decline in length and detail of the Government's response and the lack of any formal parliamentary time set aside for debating its findings and the Government response.

21. Policy recommendation: The Government should commit to responding fully and adequately to the Fiscal risks and sustainability report. It should also set aside Parliamentary time for debate introduced by the Chancellor on the report and the Government's response."

The government takes sustainability seriously, and fiscal sustainability is central to the Treasury's objectives for fiscal policy, as set out in the Charter for Budget Responsibility.

The government recommitted to publishing a full response to the Fiscal Risks and Sustainability (FRS) report within a year in the updated Charter published in 2024, underlining the government's commitment to provide a full response to increase the transparency of the decisions taken to manage risks to the public finances, improving accountability to Parliament and the public.

The government set out its initial response to the OBR's 2025 FRS to Parliament via a Written Ministerial Statement at the time of publication. The government's full response to the 2025 FRS was published alongside Budget 2025, setting out the actions being taken to improve fiscal sustainability over time. Printed copies were made available to Parliament, as well as digital copies being accessible on gov.uk. The response sets out the policy decisions taken that this government has taken to address long-term sustainability challenges. For example, at Budget 2025 the government strengthened the tax base by introducing eVED to respond to the long-term decline in fuel duty receipts, which the OBR previously noted is the "single-largest component of the fiscal cost of net zero across both tax and spending".

Taken together, the FRS and the government's response are an important part of the government's fiscal risk management framework and ensure that the UK remains at the forefront of best practice in managing and monitoring long-term risks to the public finances.

The government welcomes that your Committee and the Treasury Committee help to bring attention to the FRS through your scrutiny of the OBR and the FRS following the report's publication and welcomes debate. The scheduling of parliamentary business is a matter for the business managers and Parliament.

"22. Policy recommendation: As the OBR has a degree of discretion as to the content of the Fiscal risks and sustainability report, it should continue its ongoing efforts to generate greater interest in the report. Its recent analysis of the long-term pressures of pensions spending is a laudatory example."

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The government notes the Committee's recommendations for the OBR on the content of the FRS report.

As set out in legislation, the OBR has full discretion on how it prepares its reports. The government welcomes the OBR's focus on long-term issues and looks forward to continuing to engage with its analysis.