Written evidence submitted by Pivotal, relating to the funding and delivery of public services in Northern Ireland inquiry (FPC0023)

Summary

A Budget for 2022-23 was not agreed by the Northern Ireland Executive before the First Minister resigned on 3 February 2022. The budgetary problems in 2022-23 came about through there being no Budget and no Executive, together with a very challenging external context of rising pay, energy and others costs. Some of these budgetary problems also had their roots in failures in decision-making in earlier years. Having an Executive in place would not have avoided all of these budgetary challenges, but it should have meant better financial management and reduced the likelihood of an overspend.

The short-term nature of budgetary management in 2022-23 was very damaging for strategic decision-making. On the most part, the focus for NI Departments and organisations funded by them was on survival only, since they lacked the stable budgets needed for any longer term planning of service delivery.

The Budget for 2022-23 set by the Secretary of State in November 2022 was balanced in a technical sense, but this was achieved in part by 'borrowing' £297 million from the funding allocation for 2023-24. This creates a peculiar V-shape in funding, with a fall of 6.4% in real terms in 2023-24 and then a rise of 1.9% in 2024-25. The Fiscal Council estimates that this means a real terms funding gap for NI of £808 million and £558 million respectively over the next two years. Moreover, the V-shaped profile of spending is very unhelpful for any longer term reform or workforce planning.

Northern Ireland starts 2023-24 with a bleak combination of no Executive, no ministers, no Budget (although it is due to be set soon), rising pay and other costs, and the requirement to repay £297 million out of this year's block grant. The funding settlements for Departments in 2023-24 look likely to be flat-cash at best, and less than this for most departments. Our view is that funding pressures over recent years mean that there is limited scope for further short-term efficiency savings. Longer term reform of public services could yield savings, but this requires stable budgets and planning, and will not be achieved in the short-term. Without any new revenue sources, cuts to services seem inevitable in the coming year, as we are seeing already for some Departments.

Meanwhile there is an urgent need for a strategic, long-term approach to all public services in Northern Ireland, including overdue reform. The last multi-year budget for Northern Ireland was for 2011-15.

The Barnett formula has prevailed for more than 40 years as the accepted method of allocating funding to Scotland, Wales and Northern Ireland, despite being introduced as a temporary measure. Until recently, Barnett had always provided NI with funding per head which was at least 25% above levels in England, but the 'Barnett squeeze' is gradually narrowing this premium. Consideration should be given to whether a 'floor' mechanism should be added to the formula for Northern Ireland, as is the case in Wales.

In the absence of additional funding from the UK Government, raising more revenue locally should be properly considered as a potential way to ensure that essential services can be funded. Northern Ireland's politicians have been very reluctant to look at these options in the past, but in our view there is a need for more realism about the budgetary challenges NI faces and the likelihood of increased funding for services coming from other sources. In particular, the lower charges paid by NI

households for rates and water stand out in comparison to what households pay in the rest of the UK. Looking further ahead, the Fiscal Commission has provided a thorough assessment of possibilities for increased devolution of tax raising powers, but these need to be considered over a longer time period and so do not provide any options for dealing with the immediate budgetary pressures.

Introduction

Pivotal is the independent public policy think tank for Northern Ireland. Pivotal aims to help improve policy in Northern Ireland, through promoting a greater use of evidence in decision-making and by involving a wider range of people in talking about policy issues. Pivotal is independent of political parties and political ideologies, and operates outside of government. We aim to promote and enable discussion about policy issues in Northern Ireland that is evidence-based, inclusive and accessible.

This response is set out in four sections to address each of the elements of the Inquiry:

1. Impact of the lack of an Executive on budgetary management and strategic decision-making across Northern Ireland Departments
2. Financial situation facing Northern Ireland's public services and consequences of budgetary pressures on the delivery of those services
3. Effectiveness of the Barnett formula in calculating the amount of money the UK Government makes available to Northern Ireland for providing essential services
4. Alternative options for increasing revenue in Northern Ireland which could be open to the Northern Ireland Executive or UK Government in bringing NI's finances on to a more sustainable footing

Throughout this response we have drawn extensively on recent reports from the Northern Ireland Fiscal Council and the Fiscal Commission NI. Their expert and independent analysis has been very valuable in providing data and assessment of current and future public finance challenges. The scrutiny and transparency these reports provide is particularly helpful given the current absence of normal budgetary processes by the Executive and Assembly.

1. Impact of the lack of a functioning Executive on budgetary management and strategic decision-making

Context – no Executive and no Budget for most of 2022-23

A Budget for 2022-23 had not been agreed by the Executive before the First Minister resigned on 3 February 2022. The budgetary problems in 2022-23 have come about through a combination of the absence of an agreed Budget and the lack of a functioning Executive, together with a very challenging external context of rising pay, energy and others costs.

A draft multi-year budget for 2022-25 had been discussed and put out for consultation in December 2021, but without the Executive parties' agreement to its content. This meant that Northern Ireland Departments began 2022-23 without definite funding allocations for the year. Although caretaker ministers were in charge of Departments until 28 October, it was not possible for them to agree a Budget since legislation says that this can only be done by an Executive.

In the absence of a Budget, the Department of Finance (DoF) provided indicative minimum allocations for 2022-23 for Departments based on the previous year's funding. Legislation allowed the DoF Permanent Secretary to authorise continued spending by Departments.

Implications for budgetary management

The lack of an Executive combined with the absence of a Budget for 2022-23 resulted in an estimated £660m projected overspend by end October 2022. We would make the following points about budgetary management during this period:

- Departments had no firm upper limit for their funding allocation for the year. Although given an indicative minimum allocation by DoF at the start of the year, all departments had an expectation of receiving further allocations during the year, so did not feel limited to this minimum allocation.
- Without a firm upper limit, caretaker ministers made commitments which pushed their projected spending for the year above their department's indicative minimum allocation, based on their priorities and maybe also their interpretation of what the Executive would have agreed had it been in place.
- There was a lack of collective responsibility for keeping within the overall available funding, since there was no Budget and no Executive taking an overview of the whole of spending. The Finance Minister and DoF urged caretaker ministers and departments to rein in spending commitments, but these requests had limited impact due to the absence of an agreed Budget or Executive.
- Civil servants did not have any formal power to constrain the decisions of caretaker ministers about spending. Around £320 million of spending was approved by caretaker ministers through Ministerial Directions, meaning that civil servants advised ministers that their decisions were not affordable. In addition, some of this spending was not approved by the Department of Finance. Note that there has been an absence of scrutiny of these Ministerial Directions since normally they would be reported to the Assembly's Public Accounts Committee.
- There were none of the usual in-year monitoring processes to review forecast spending formally and reallocate funding between departments.
- Without an Executive, there was no way to agree how to allocate additional funding received throughout the year, meaning that in-year Barnett consequentials (for example, from new 'cost of living' measures) could not be given out to Departments. Instead, these additions were added to the overall Northern Ireland block which was allocated in the Budget set by the Secretary of State. There was widespread concern in Northern Ireland that funding allocated in England to assist households with the rising cost of living was not able to be used for this purpose in NI.
- There was an absence of any transparency, scrutiny and accountability about budgetary issues because the Assembly and its Committees were not operating. Normally the Finance Committee plus each departmental Committee would scrutinise the draft Budget and consider its implications. There was no public consultation about the Budget after the consultation on the 2022-25 draft Budget was paused.

Would having an Executive have made a difference?

It is important to emphasise that having an Executive in place would not have removed all of the budgetary challenges experienced in 2022-23. Pay and other cost pressures and the tight overall settlement for Northern Ireland would still have been very difficult to manage and would have resulted in significant pressures on departments. However, with a clear agreed Budget and proper in-year monitoring processes, an overspend might have been avoided.

A further important point is that many of the budgetary problems in 2022-23 had their roots in earlier years. There has not been a multi-year budget agreed by the Executive since 2011-15. There has not been an agreed Programme for Government since the same period. Departments have operated in silos with little collective ownership of issues. The Executive has often failed to prioritise between different issues and difficult decisions have been avoided. Possibilities for raising increased revenue locally have not been pursued. The absence of longer term planning has meant that the Executive has failed to take important decisions in the past that would have resulted in greater efficiency in the use of public funding, most notably in failing to take forward public sector reform.

Implications for strategic decision-making

The short-term nature of budgetary management in 2022-23 severely limited strategic decision-making. The emphasis was on survival rather than any consideration of longer term issues. In particular:

- Uncertainty about budgets prevented strategic decision making – a lack of clarity about budgets meant that departments and those organisations funded by them could only plan for the very short-term.
- Inability to plan for reform of public services – the absence of a clear budget for one year, let alone multi-years, meant it was almost impossible to plan any significant reform of how services were delivered.
- Very difficult to do proper workforce planning – not having a clear budget for one year, let alone multi-years, made it very hard to do workforce planning.
- Cuts to services have tended to be to programmes supporting some of the most vulnerable people, for example the Engage programme (educational recovery from Covid), school meals holiday payments and the Extended Schools programme. As well as the immediate impact on those who benefited from these programmes, in the longer term the absence of this support may lead to increased costs to public services.

Budget for 2022-23 set by Secretary of State in November

After the caretaker ministers ceased to be in post at end October 2022, the Secretary of State stepped in to set a Budget for 2022-23. This included working with departments to reduce the forecast overspend from £660 million to £297 million, mainly through paring back departments' spending commitments, but also helped by some additional Barnett allocations in the UK Budget in November. While the Secretary of State decided how the overall funding available to Northern Ireland would be divided between departments, it was left to civil servants to decide how this would be managed within each department.

The final £297 million overspend in 2022-23 was managed through a reserve claim from the Treasury which will be repaid by taking this amount from the 2023-24 block grant. This creates a peculiar 'V-shaped' budget profile, where real-terms funding for Northern Ireland Departments falls by 6.4% in 2023-24 and then rises by 1.9% in 2024-25. As a result, it is estimated that the total funding available is £808 million below what is needed in 2023-24 in real terms, and £558 million below what is needed in 2024-25 (see Fiscal Council NI report - the NI Executive's 2022-23 budget).

The following points about the Budget set by the Secretary of State are important:

- Some departments did much better than others in the Secretary of State's budget. Department of Health got around 90% of its overspend, Education, Justice and Infrastructure got 70-75%, and Communities got 57%. Given the immediate huge pressures in the health service, it is understandable that a decision to prioritise health was taken. However, this does mean much greater pressure on all other departments.
- While the immediate budgetary problems have been addressed in a technical sense (in that the budget was balanced for 2022-23), this has been achieved in some cases by cutting services and by a significant 'reserve claim' that has to be repaid in 2023-24. This 'loan' from 2023-24 may have been the only short-term solution to balance the 2022-23 budget, but it does just increase the number of difficult decisions needed the next year.
- While the Secretary of State decided the overall split of funding between departments, it was left to civil servants to decide how their department's allocation would be divided between different areas of spending. This means that civil servants had to make decisions about spending that would normally be taken by ministers, going far beyond the normal civil servant role and meaning decisions are being taken without democratic accountability.
- The shortfalls in available funding in 2022-23 and 2023-24 (£808 million and £558 million respectively in real terms) mean that there are huge further problems ahead.
- The 'V-shaped' profile of funding over the next two years is not conducive to effective planning of public service delivery, reform or workforce planning.

Will departments be able to manage spending within the funding available for 2023-24?

Northern Ireland Departments begin 2023-24 with no Executive, no ministers, no Budget (although the Secretary of State has said he will set a Budget soon), ongoing pay and other cost pressures, and the need to repay the £297 million Reserve claim from 2022-23. The Fiscal Council has estimated that in real terms there is a £808 million shortfall in the funding available for 2023-24 (and £558 million for 2024-25).

This is an unprecedented situation. It would appear impossible to achieve the reduction in spending needed in 2023-24 without making cuts to services. While this is very difficult to assess, it would seem that most of the possible short-term efficiencies in departments' spending have been exhausted already given past years of tightened funding settlements. There remain significant potential savings from more structural reforms of how public services are delivered (most obviously in the health service), but these require multi-year budgets and long-term planning, and could not be achieved in the short-term. In the absence of efficiencies or new funding, it seems likely that cuts to services will be inevitable in 2023-24 (see next section).

Given the scale of the challenges and the likelihood of cuts to services in 2023-24, the case has been made by the FDA that the Secretary of State should take decisions about how spending will be cut within departments, rather than delegating these choices to civil servants. Without doubt such decisions would be taken by a minister had there been one in place, so it would seem appropriate for someone with political accountability to make them.

2. Financial situation facing Northern Ireland's public services

This section gives our assessment of the current financial position of Northern Ireland's public services. We start with some cross-cutting comments and then move to discuss specific sectors.

Cross-cutting comments

- All public services were already under serious financial pressure at the start of 2022-23.
- Many of the budgetary problems in 2022-23 had their roots in poor decision-making in earlier years.
- All public services face soaring pay, energy and other costs, and the block grant has not increased proportionately to cover these costs.
- The prioritisation of health (and to a lesser extent education and justice) in budgetary allocations in 2022-23 and 2023-24 means that other departments face huge falls in their budgets. The Department of Education has already announced cuts to certain programmes. Also of concern is the impact on investment in skills, which falls under the Department of Economy's remit for further education and higher education.
- Although it is difficult to assess this, our view is that funding pressures over recent years means that there is limited scope for further short-term efficiency savings by Departments. As a result, cuts to services seem inevitable.
- At present there is a serious risk that actions taken to manage budgetary pressures in the short-term result in greater costs to the public sector in the long-term. Many of the services or organisations at risk of having their funding cut are providing vital early intervention and prevention services.
- Northern Ireland has not had a functioning Executive for more than four out of the last six years. As a result, Departments and the organisations funded by them have had a succession of short-term, one-year budgets.
- There is a need for a co-ordinated, strategic, long-term approach to spending right across public services. The last multi-year budget for Northern Ireland was for 2011-15.
- Transformation is very much needed and overdue in many areas of public services. Opportunities have been missed because there has been unwillingness amongst politicians to take the necessary decisions.

Below are some headline comments on the financial situation in specific sectors.

Health

The Fiscal Council assessment of the 2022-23 Budget says that "Health arguably fared best among departments in the NIO [Secretary of State's] Budget [for 2022-23], having over 90 per cent of its projected overspend covered once we adjust for budget cover transfers. Education, Infrastructure and Justice had 70-75 per cent of their projected overspends covered and Communities 57 per cent."

The [Department of Health Permanent Secretary] has recently set out some very concerning implications from the budget for 2023-24 for services. He said that the best possible outcome for his Department is 'flat cash', and that even with efficiency savings this will mean a £300 million shortfall in the Department's budget in real terms. This would see per capita spending on health in Northern Ireland fall below England for the first time. Balancing the Department's budget under this scenario would require savings that he says would have a high impact on services.

The short-term nature of recent budget-setting has had a very damaging effect on the ability to plan for health service reconfiguration and for the future workforce. It is well known that reform of the health service in Northern Ireland is overdue, but there has been a reluctance amongst politicians to take the necessary decisions. The recent Fiscal Council report on sustainability of health spending highlighted higher unit costs per head for health provision in Northern Ireland, which is at least in part due to a failure to reconfigure how services are delivered. However, ongoing political instability and short-term budgeting leaves little or no opportunity to take the vital work of reform forward.

Education

The Institute for Fiscal Studies highlight that spending per head in schools in Northern Ireland has fallen over the last ten years and is now the lowest of the four UK nations. On top of this, NI schools has been notified that the 2023-24 Budget is likely to result in a fall in funding for schools of 1.6%, meaning that the gap in spending per head will grow further. There has been strong opposition from education leaders and the Education Authority given the implications from this budget for funding cuts. In recent weeks, the Department of Education has announced it will no longer be able to fund some key programmes, including holiday hunger payments, mental health support in primary schools, Covid recovery support (Engage), the extended schools programme and free book bundles for babies.

The current budgetary pressures in education have roots going back many years. Funding for the Department of Education has been largely flat in cash terms over the last ten years (apart from Covid additions), generating growing pressures on budgets as pay and other costs rose. Importantly, the need for spending has increased due to growing numbers of children and increasing levels of Special Educational Needs. It seems unlikely that there are many efficiency savings left to be made in the short-term in the Department of Education budget, as borne out by the recent cuts to highly valued programmes.

Voluntary and community sector

At present, many voluntary and community sector (VCS) organisations have been given only short-term funding allocations by NI Departments for 2023-24, for example for one month or perhaps three months. This makes it extremely difficult to continue to deliver services, with many staff under the threat of redundancy.

Many organisations are facing serious financial difficulties as a result of the replacement of the European Social Fund (ESF) by the new Shared Prosperity Fund (SPF). Less funding was available in SPF for Northern Ireland than under ESF, and decisions on funding were made by the UK Government rather than NI Departments. Moreover, these decisions were not announced until the very last day of 2022-23. This seems to have been poorly handled by the UK Government, especially given that voluntary sector representatives in Northern Ireland had been raising the potential for problems since 2016.

Two headline implications are important about the current situation facing VCS organisations:

- VCS organisations support some of the most vulnerable people in Northern Ireland. In many cases, organisations do not have the financial resilience to continue delivering a service once funding is cut, leaving big gaps in provision. As well as the immediate social costs in terms of day-to-day wellbeing for service users, this will risk further costly problems in the future, for example health problems arising from isolation, lack of support and absence of stimulating activity.
- Financial problems risk eroding the ongoing capacity of the voluntary and community sector to deliver important services and support, since experienced staff members including leaders are either made redundant or choose to leave.

3. Effectiveness of the Barnett formula in calculating the amount of money made available to Northern Ireland

The Barnett formula provides Northern Ireland with funding additions calculated as a population-based proportion of funding increases in England (as is the case in Scotland and Wales). The 'additions' are added on to the baseline block grant, which is rolled forward each year. The formula has been used for Northern Ireland since 1979 after it was introduced as a temporary measure. It is an administrative arrangement without any statutory basis. The Fiscal Council provide a good explanation of the Barnett formula (see Public Finances in Northern Ireland, page 50) and the Institute for Government have published a useful paper.

The usual argument in favour of the Barnett formula is that it is an established and accepted method of deciding funding for Scotland, Wales and Northern Ireland (SW&NI), which for the most part avoids an annual negotiation about funding allocations (although there are annual discussions about baselines and some comparability factors). Since new funding is added on to the previous baseline, it provides some stability and predictability for SW&NI about their funding. For SW&NI, a strong argument in favour of the Barnett formula is that it continues to provide higher funding per head than in England.

The main argument against the Barnett formula is that it does not reflect relative needs across the UK. While 'additions' under the Barnett formula are based on population as a crude proxy for need, the baseline to which they are added is an historical amount rather than based on need. Questions have always been raised about the overall fairness of the formula, both about whether it provides sufficient funding to address needs in SW&NI, and also conversely whether it is fair to more disadvantaged areas in England which may have similar levels of need to SW&NI.

Northern Ireland has benefited from some significant extra funding allocations outside of the Barnett formula, which has not been the case in Scotland and Wales. These extra allocations have been linked to the particular challenges facing Northern Ireland and have often been associated with the restoration of devolution, for example the agreements at St Andrews (2006), Fresh Start (2015) and New Decade, New Approach (2020). Extra funding for Northern Ireland was also allocated as part of the Conservative Party's 'Confidence and Supply' agreement with the DUP (2017).

How does funding per head in Northern Ireland compare to the rest of UK?

The Fiscal Council provide the figures in Table 1 below for the 'premium' of recent block grant allocations to Northern Ireland compared to equivalent UK spending. The NI block grant in these figures includes some significant non-Barnett additions (as mentioned above). Note the marked decline in the 'premium' from 2018-19 over time, which is attributable to the 'Barnett squeeze' (discussed further below) and the absence of any extra funding allocations to Northern Ireland outside of the Barnett formula.

Table 1: NI block grant per head compared to England

Year	NI block grant 'premium' in spending per head above England
2016-17	37.6
2017-18	38.1
2018-19	40.3
2019-20	37.3
2020-21	33.8
2021-22	30.4
2022-23	29.0
2023-24	24.8
2024-25	24.9

Source: Fiscal Council NI sustainability report 2022

Is the Barnett formula fair to Northern Ireland?

Discussions about the fairness of funding allocations to SW&NI hinge on how much 'need' is greater in SW&NI compared to England, on the basis of issues like demographics, health, social disadvantage, geography and economies of scale. 'Need' is very difficult to assess, with the results being open to challenge and inevitably disputed. The Fiscal Council's recent Sustainability Report provided a list of historical assessments of how much need in Northern Ireland exceeded need in England (see Table 2), concluding that need at present is around 20% higher in NI than in England. They found that the premium in block grant funding per head in Northern Ireland in 2024-25 will be around 25%, concluding therefore that at present the additional funding per head for Northern Ireland does broadly account for need. Others however would judge that need in NI is higher and so would dispute this assessment. Importantly, the 'Barnett squeeze' (discussed below) means that funding per head will not remain at this higher level, which raises serious concerns about the sustainability of NI's public finances in the coming years.

Table 2: Assessment of need for public spending in Northern Ireland compared to England

Assessment of need	**How much is need greater in Northern Ireland?**
HM Treasury 1978-79	31%
HM Treasury 1994	22%
Northern Ireland Executive 2002	25%

Holtham Commission 2008	21% (indicative)

Source: Fiscal Council NI sustainability report 2022

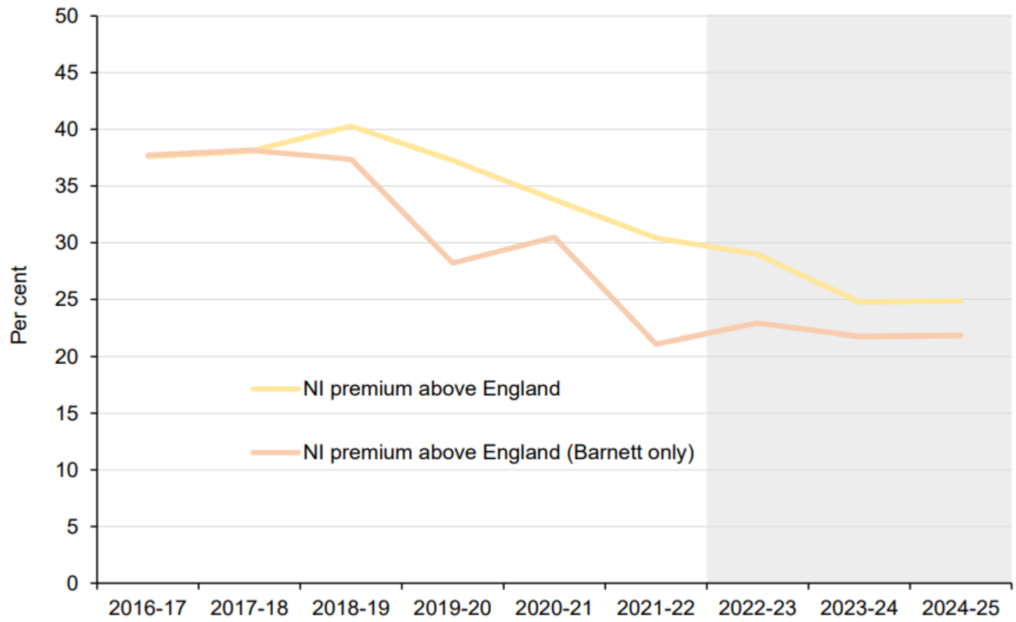
<u>'Barnett squeeze'</u>

A growing issue in Northern Ireland is the impact of the 'Barnett squeeze'. This arises because, under the Barnett formula, only <u>additions</u> to NI's block grant are proportionate to how much funding increases in England. So the percentage increase in <u>total</u> funding in NI will be lower than the percentage increase in England, since NI's baseline funding per head is higher than England's. This means funding per head in Northern Ireland (and Scotland and Wales) will grow more slowly than in England. As an example, the growth rate of UK DEL funding between 2019-20 and 2024-25 will be 6.0% per year, while the growth rate for the NI block grant will be only 3.6% per year (with annual growth rates of 5.1% in Scotland and 4.9% in Wales).

The 'Barnett squeeze' means that funding per head in NI is gradually converging towards funding per head in England (with a similar 'squeeze' happening in Scotland and Wales). In Northern Ireland, this 'squeeze' over time has been partly offset by the non-Barnett funding additions mentioned above.

Chart 1 below from the Fiscal Council demonstrates the impact of the 'Barnett squeeze'. It shows the premium in spending per head in Northern Ireland at 38% in 2017-18, rising slightly in 2018-19 because of extra non-Barnett funding allocations, but then falling markedly to 25% in 2024-25.

Chart 1: Percentage 'premium' in Northern Ireland block grant per head above England



Source: Fiscal Council sustainability report (2022)

Projections by the Fiscal Council show this trend continuing, with the premium falling below 20% in the early 2030s and to 10% in the late 2040s. This assumes that the 'squeeze' is not offset by any non-Barnett additions in funding for Northern Ireland.

Given the impact of the 'Barnett squeeze', in Wales a funding floor was agreed following the Holtham Commission in 2008. This floor makes an adjustment to the Barnett formula so that funding per head in Wales does not fall below 115% of funding per head in England. Given there is nothing to stop the Northern Ireland premium falling below the 120% level that might be said to represent higher need, it would be appropriate to consider the case for introducing a similar 'floor' mechanism for NI. There would obviously be a lot of debate about the level at which a NI floor should be set. Note also that such a mechanism might reduce the opportunities for NI to argue for extra funding additions above it.

4. Alternative options for increasing revenue in Northern Ireland

To address shortfalls in Northern Ireland's budget, in broad terms there are four options:

a) Make efficiency savings within public services ('do more for less')
b) Reduce or stop some public services
c) Seek more funding from Westminster via the block grant
d) Raise increased revenue within Northern Ireland

Northern Ireland Departments are currently focussed on a) and b) as they seek to keep spending within the funding available for 2022-23 and 2023-24. This has been extremely challenging to date and the prospects for 2023-24 are even worse, as demonstrated in multiple warnings from NI Departments and organisations funded by them about budget shortfalls, along with recent cuts to key spending programmes.

Politicians and others will frequently make the case for increased funding from Westminster via the block grant (option c) above). This may be justified, particularly as the 'Barnett squeeze' means convergence in spending per head over time. However, in Pivotal's view there is also a need for a realistic consideration of increased revenue raising within Northern Ireland (option d) above). There has been a tendency to close down discussion about such possibilities in the past, in favour of seeking additions to the block grant from the UK Government. We suggest that a well-informed public conversation is needed about the options for increased local revenue raising and the potential funding that is foregone by choosing not pursue these options.

Increased revenue raising within Northern Ireland could be either through a greater use of existing revenue raising powers, or in the longer term through the devolution of increased fiscal powers. These options are considered briefly below.

<u>Raising more revenue using existing powers</u>

Most of the revenue raised by the Northern Ireland Executive comes via the regional rates on domestic and non-domestic properties. Increased revenue could be raised by this route, but in the past the Executive has focussed on keeping the regional rate low in order to minimise the costs for households and businesses. For example, the Executive only made very small increases in the domestic regional rate between 2007 and 2017, although the non-domestic regional rate increased more sharply. Pivotal's view is that greater consideration should be given to using the domestic rates system in particular to generate increased revenue to fund essential public services, but doing so in a way that protects lower income households.

Northern Ireland households do not pay for water in the same way as households in the rest of the UK. The Executive foregoes a potential £345 million of income each year by not having water charges. Water charges have been considered at various times in the past, but there is significant political opposition to their introduction. The comparison in the table below of costs faced by households across the UK would question whether this is justified (see Fiscal Commission final report).

Table 3: Comparison of household charges across the UK (rates/council tax & water/sewage)

	Average Bill (Council tax or rates)	Water and sewage	Total household bill
Northern Ireland	£1,036	£0	£1,036
England	£1,428	£408	£1,836
Wales	£1,544	£408	£1,952
Scotland	£1,198	£383	£1,581

Source: Department of Finance – Land and Property Services (LPS), Presentation to Fiscal Commission – May 2021

There are a number of other areas where the Northern Ireland Executive chooses to offer more generous provision than in the rest of the UK (often called 'super-parity' measures). These include lower student fees, welfare reform mitigations, free prescriptions and concessionary travel. Together these total to around £600-700 million of revenue foregone in 2020-21, that could be used for other spending on public services. In Pivotal's view, there should be a full consideration of whether the revenue foregone by these policies is justified, given it means less is available to spend on other public services.

Note there are also some 'sub-parity' policies, where Northern Ireland offers less than the rest of the UK, the most notable being the much lower amount of free pre-school childcare in NI.

Any introduction of increased rates, water charges or other revenue raising would need to fully consider the implications for households on lower incomes, particularly given the ongoing pressures on the cost of living.

Raising increased revenue through devolution of more fiscal powers

The Fiscal Commission final report gives a thorough and valuable assessment of the potential for increased fiscal devolution to Northern Ireland. Note that the options examined in this report would all involve significant policy change and need time for implementation, and so they do not offer a solution to the current budgetary problems in the short-term.

The Fiscal Commission report concluded that in principle there was a strong case for increased devolution of some tax-raising powers to Northern Ireland, since it would put more responsibility and accountability into the hands of local politicians and allow them to tailor taxes for the local situation. After reviewing the full range of taxes, the report suggested partial devolution of income tax, plus stamp duty land tax, landfill tax and Air Passenger Duty. The Fiscal Commission emphasised that this should be a long-term process requiring detailed consideration, including of the risks.

Pivotal's view is that these options for fiscal devolution should be fully considered, including a well-informed public conversation. We note however that the Fiscal Commission's report said that almost all consultees questioned the Northern Ireland Executive's capacity to take on the devolution of fiscal powers, both in terms of its stability and its ability to reach coherent and consistent policy decisions. It is notable also that the Treasury has said that getting Northern Ireland’s public finances onto a sustainable footing is a pre-condition of any devolution of corporation tax powers.

April 2023