STRENGTHENING THE CAPACITY OF THE DEPARTMENT OF FINANCE

REPORT OF THE INDEPENDENT REVIEW PANEL

December 2010

CONTENTS

3 December 2010

Mr Brian Lenihan TD,
Minister for Finance,
Government Buildings,
Dublin 2.

Dear Minister,

I am very pleased to provide the attached report which you commissioned in September to review the Department of Finance. The Panel has worked diligently to prepare this report and was assisted enormously by a very strong interest in our work within government, by all political parties, and by the broader public. There is a very wide recognition that Ireland needs a strong Department of Finance.

The Panel also received tremendous support from the Department and was very impressed by the commitment made to our work during these extremely busy times. We have been guided by your call, and that of your Secretary General Kevin Cardiff, for advice on how to improve the Department. We have been direct in our advice and believe that our recommendations warrant prompt action.

Finally, I want to emphasize how impressed I am with the staff already engaged in the Department. I would have been pleased to have had many of them serve on my team at the Department of Finance in Canada. But what I am most impressed with is the broad based understanding in the Department that it must use this occasion to substantially improve its capacity to serve you and Ireland better. I trust that our observations will help guide this effort.

Sincerely

Rob Wright

EXECUTIVE SUMMARY

1. The Panel was established by Minister for Finance Brian Lenihan on 10 September, 2010, to examine the Department of Finance's performance over the last ten years and advise how the Department might adapt to meet the challenges of the future. Ireland's economic challenges are substantial, and have become more starkly defined over the three month period of our review.

2. We had enormous support conducting our review. We met a large number of people from the political system, officials from the Department, individuals from the broader Public Sector and those with an interest in, and interaction with, the Department. We invited and received very useful submissions from the public. We enjoyed complete access to departmental personnel and records. We were impressed with the enthusiasm of the Secretary General and the Department for this exercise, at a time of unprecedented pressure.

3. The Irish economy was transformed in recent decades. A period of very strong growth in the 1990s was sustained by enhanced competitiveness and export growth. Pending membership of the single currency spurred inward investment. Despite predictions to the contrary, the Irish economy continued to grow substantially after 2000. However, the dynamic fundamentally changed. Exports no longer contributed significantly to growth, which was now driven by domestic developments, notably investment in building. Participation in EMU left interest rates too low for Irish circumstances. This fuelled the property boom as did financial market competition and interbank borrowing from Europe. Meanwhile, Irish competitiveness had deteriorated very significantly. The property bubble began to collapse from 2007 and the fallout was exacerbated by a significant deterioration in the external environment. The economic and fiscal challenge was, of course, severely aggravated by the failure of the Irish banking system.

4. The Government initiated two scoping reviews of the origins of the current crisis. Based on these reviews, the Government launched a Statutory Commission of Investigation into the Banking Sector, chaired by Mr Peter Nyberg. The Panel has been deliberate in ensuring that we did not overlap with the mandate of this statutory review.

5. To provide a focus for our review of departmental advice over the last ten years we examined three key questions:

- How appropriate was the Department's advice on the risk of pro-cyclical fiscal policy?
- Was the Department aware of the risks of overheating in the property sector and did it provide advice appropriate to the circumstances?
- Did the Department provide sufficient advice on the vulnerability of the tax system to an economic downturn?

6. The Panel reviewed in detail the annual June Memoranda to Cabinet on Budget Strategy. Generally speaking, we found that advice prepared by the Department for Cabinet did provide clear warnings on the risks of pro-cyclical fiscal action. These views were signed-off by the Finance Ministers of the day who would submit the Memoranda to Cabinet. The Department's advice was more direct and comprehensive than concerns expressed by others in Ireland, or by international agencies. With very few exceptions, however the quantum of spending and tax relief outlined in December Budgets was very substantially above that advocated by the Department and Minister in June.

7. We see three key reasons for this failure of fiscal policy. First, there were extraordinary expectations of Government in Ireland to create spending and tax initiatives to share the fruits of recent economic gains. These pressures were reflected in the political debate of the day where all political parties were eager to meet public expectations for more and better services. As well, the Irish economy was regarded by most as a model. The EU fiscal rules, the Stability and Growth Pact, were respected, debt fell and spending appeared to be well below EU levels. The underlying dangers were either missed or ignored.

8. Second, the Government's Budget process was completely overwhelmed by two dominant processes - Programmes for Government and the Social Partnership process. We recommend major changes to the budgetary process that would enhance ministerial accountability to Parliament, expand the release of detailed departmental analysis for consultation well before Budget time and provide oversight by some form of Fiscal Council.

9. Third, the Department of Finance should have done more to avoid this outcome. It did provide warnings on pro-cyclical fiscal policy and expressed concern about the risks of an overheated construction sector. However, it should have adapted its advice in tone and urgency after a number of years of fiscal complacency. It should have been more sensitive to and provided specific advice on broader macroeconomic risks. And it should have shown more initiative in making these points and in its advice on the construction sector, and tax policy generally.

10. We provide recommendations to formalise Department's records of Budget advice, to strengthen the rigour of the Department's policy advice and expand resources for tax policy and medium term economic planning.

11. The Panel recommends formalising in legislation the Department's accountability for assessing systemic macro-economy risks.

12. Turning to the issues arising from the structure and staffing of the Department; based upon our analysis, submissions from others, and consistent with views of Finance employees and managers we met, the Department:

- does not have critical mass in areas where technical economic skills are required;
- has too many generalists in positions requiring technical economic and other skills;
- is more numbers driven, than strategic;
- does not have sufficient engagement with the broader economic community in Ireland;
- often operates in silos, with limited information sharing;
- is poorly structured in a number of areas, including at the senior management level; and
- is poor on Human Resources Management.

13. We have been direct in our analysis and advice, but do not accept the notion that the Department is not fit for purpose. It has worked hard in response to the banking and economic crisis and must now apply the same determination to remake itself in the light of our observations in this report and the major challenges confronting Ireland.

14. The Panel recommends that the Department sharpen its focus on core business and then substantially strengthen its capacity to manage that core business. The Public Service Management and Development Division should be managed as a separate entity, as either a separate Department, or reporting directly to the Minister of State for Public Service Modernisation. The Minister and the Department of Finance should retain authority over the overall wage bill, negotiating mandates for new collective bargaining processes and manage a single window with other Departments to control public spending.

15. This change should help focus effort on the extraordinary opportunity provided by the Croke Park Agreement to modernise the capacity of the Public Service. We recommend two other processes to help – a fulltime Task Force from across Government to include individuals from the leading Departments and a Private Sector Advisory Board to help drive the process.

16. The Panel believes that the Sectoral Policy Division is a core function of the Department especially given the need to implement the economic recovery plan and the requirement for medium-term economic planning. The Department would be at risk of losing critical mass with any transfer of core functions.

17. To strengthen the remaining core Finance structure, we offer a set of recommendations to modernise management, reform existing organisation structures and add substantially more people with technical economic and other skills.

18. Working structures of the Department are less than optimal. We recommend removing a level of management from line management responsibilities. We also offer recommendations to reform working level structures and increase the effectiveness of the Department's Management Advisory Committee, including the creation of a Corporate Secretariat that would help enhance internal communications and outreach to the public.

19. On people, the Department needs to increase substantially its numbers of economists trained to Masters level or higher and add other technical capacity, especially accounting, banking and financial markets expertise. Over the next two years the Department should

double its number of economists trained to Masters Level. It should organise itself to engage more University recruits at that level every year.

20. On processes, the Department should commit to modernising the HR Management function. It should engage a professional Human Resources expert from outside Government to help develop HR systems. This should include performance management where dramatic improvements are necessary.

21. The Secretary General of Finance should lead this management renewal, presenting a change management plan to employees and reporting on progress in an annual accountability session with staff.

I. INTRODUCTION

1.1 This report was commissioned by the Minister for Finance, Brian Lenihan, following his commitment at the Oireachtas Joint Committee on Finance and the Public Service that a review would be carried out to assess the Department of Finance's policy advice and performance over the past 10 years and to make recommendations on how best the Department might adapt to meet the challenges of the future. The full terms of reference are at Appendix 1.

1.2 Composition of the Review Panel

On 10 September 2010, the Minister announced the composition of the Review Panel and its terms of reference. The members are:

- Mr. Rob Wright, Chairman of the Group
- Mr. Hans Borstlap and
- Mr. John Malone.

Mr Pat McArdle provided support and assistance to the Panel.

Further details on the members of the Panel are available at Appendix 2.

1.3 Work Programme

1.3.1 To discharge its task, the Panel drew up a work programme which involved:

- inviting submissions from the general public. We appreciated the responses that we received. A list of those who made submissions is attached at Appendix 3;
- a review of a wide variety of papers specifically prepared by the Department concerning the work done and advice tendered to Ministers;
- a lookback at a large number of files relating to the various areas of the Department so that we could form a view as to the nature and quality of the advice offered by officials during the period covered by our review;

- detailed discussions with a wide range of individuals including: the Taoiseach, Minister and former Minister, opposition finance spokespeople, social partners, current and former senior officials from the Department and from other Departments, Finance employees, current and former senior officials from institutions within the remit of the Minister for Finance and outside commentators on economic, taxation and other issues;
- familiarising ourselves with political, media and other commentary on the performance of the Department of Finance;
- familiarising ourselves with a number of recent studies on Ireland's economic challenges. These include: *The Irish Banking Crisis, Regulatory and Financial Stability Policy 2003-2008* by Governor Honohan of the Central Bank; *The Preliminary Report on the Sources of Ireland's Banking Crisis* by Regling and Watson; and the *Capacity Review of the Department of Finance* (2009). The Panel arranged meetings with the authors of those reports. During the course of our deliberations, the report of the Joint Committee on Finance and the Public Service: *Report on Macroeconomic Policy and Effective Fiscal and Economic Governance* was published.

1.3.2 The Panel's mandate is limited to the performance of the Department of Finance not other agencies of the State. A separate Statutory Commission of Investigation into the Banking Sector, chaired by Mr. Peter Nyberg, is providing a comprehensive assessment of all agencies involved in this issue and is due to report in March 2011. The Panel has been deliberate in ensuring that its work does not overlap with the work of this Statutory Commission.

1.3.3 The Panel would like to put on the record that we were impressed with the enthusiasm of the Secretary General of the Department and his staff for this exercise, at a time of unprecedented pressure.

1.4 Structure of the Report

The report is structured in five sections in addition to the Executive Summary and this Introduction. Section 2 sets out the context in which the Department operates, including the economic and fiscal context of the past ten years. Section 3 reviews the departmental policy advice on key issues over the past 10 years and makes recommendations arising therefrom. Section 4 analyses specific shortcomings in the organisation and Human Resources Management of the Department and recommends changes to address these issues. Section 5 provides conclusions; and a list of the recommendations is provided in Section 6.

2. BACKGROUND

2.1 Department's Mission

The Department's Statement of Strategy outlines its mission:

> *To support the achievement of the Government's economic and social objectives by promoting a sound, sustainable economic and budgetary environment, continuing improvements in the efficiency of public services, and an effective framework for financial services.*

2.2 Changing Responsibilities of the Department

2.2.1 There have been three major changes in the role of the Department over the years relating to Public Service Management, Economic Planning and Development, and Treasury Operations. These are reviewed below.

2.2.2 Responsibilities for issues relating to Public Service personnel, organisation and remuneration, previously with the Department of Finance, were assigned to a new Department of the Public Service in 1973. That Department was also charged with implementing the recommendations of the report of the Public Service Organisation Review Group (known as "the Devlin Report"), which sought to make significant structural changes to the Public Service. There was limited success in implementing these recommendations and the Department of the Public Service was abolished in 1987 and its functions re-absorbed into the Department of Finance.

2.2.3 A Department of Economic Planning and Development was established in 1977 and the following responsibilities were assigned to it:

- promoting and co-ordinating economic and social planning,
- identifying policies for economic and social development,
- assessing the plans and activities giving effect to such policies,
- reviewing the implementation of economic and social plans and reporting to Government thereon.

That Department was abolished in 1980 and its functions were transferred to the Department of Finance.

2.2.4 In 1990 the National Treasury Management Agency (NTMA) was established to discharge functions of borrowing for the Exchequer and managing the national debt which had been carried out by the Department of Finance. This represented a significant change for the Department, a loss of highly trained employees and a loss of a key function - treasury management - that typically resides with Departments of Finance. Since then, a growing number of functions have been assigned to the NTMA under a variety of governance structures.

2.3 The Department's Staffing and Organisation

The Department of Finance had 542 staff as of 1 November 2010 (in whole-time equivalent terms), reduced from 629 in December 2007. An organisation chart for the Department is attached at Appendix 4.

The Work of the Department is allocated across four Divisions:

1)	Budget, Taxation and Economic Division	(138)
2)	Financial Services Division,	(58)
3)	Sectoral Policy Division,	(129)
4)	Public Service Management & Development	(135)

In addition to which there are 82 other staff: the Secretary General, along with staff assigned to the Minister's Office, including Press Office (18), Corporate Services Division (54), administrative support (3) and seconded staff (6).

A detailed account of responsibilities of each Division is set out at Appendix 5 to this report.

2.4 The provision of advice by the Department

The Department advises the Minister in a variety of ways and on a wide range of issues. The most important function of the Department is providing the strategic look-forward in the context of the annual Budget. In addition to this, the Department provides policy advice:

- on a daily basis, in relation to significant current issues arising, which may relate to: major proposals from other Departments, issues on the horizon that may be of concern to the Minister, significant industrial relations issues;
- on a weekly basis, in relation to proposals brought forward for consideration by Cabinet either by Finance itself or by other Ministers;
- in relation to regular meetings of ECOFIN and other EU and international bodies attended by the Minister;
- at various strategic points throughout the year, for example, as key stages are reached in the budgetary/estimates cycle.

2.5 The Department's engagement with Europe

2.5.1 The relationship between the Department and the EU is of critical importance to the Department and to Ireland. The EU Commission consults committees of experts from member states – including Ireland – before drawing up new legislative proposals. Additionally, the Department interacts with EU bodies such as the Directorates-General for Economic and Financial Affairs, Taxation, EU Budget, Regional Policy, European Court of Auditors and OLAF (European Anti Fraud Office).

2.5.2 Dealing with EU issues involves attendance by the Minister and his officials at a large number of EU fora, notably:

- the Economic and Financial Council (Ecofin);
- the Eurogroup which meets on the eve of Ecofin;
- the Economic and Financial Committee (EFC) which, inter alia, prepares the work of Ecofin;

- sub-committees of the EFC – the Eurogroup Working Group which prepares the work of the Eurogroup Ministers; the Financial Services Committee, Sub-Committee on IMF and the Bills and Bonds Committee;
- The Department is also involved in developments specific to EMU which have increased in significance since the Lisbon Treaty.

2.5.3 The current difficulties facing Ireland will continue to intensify the relationship with the EU institutions; Ireland's Presidency of the EU Council in January 2013 will also increase the interactions between the Department and those institutions.

2.6 Economic and fiscal context

2.6.1 The Irish economy was transformed in recent decades. Income rose strongly, converging towards, and subsequently over-taking average European levels. In the early nineties, per capita income was around 70 per cent of the EU average. A decade later, Ireland had virtually caught up with the average.

2.6.2 This period of strong investment and growth was sustained by exports. The economy remained in broad balance and competitiveness, helped by a large devaluation of the Irish pound in 1992, was satisfactory. Pending participation in the single currency spurred inward investment and interest rates declined sharply.

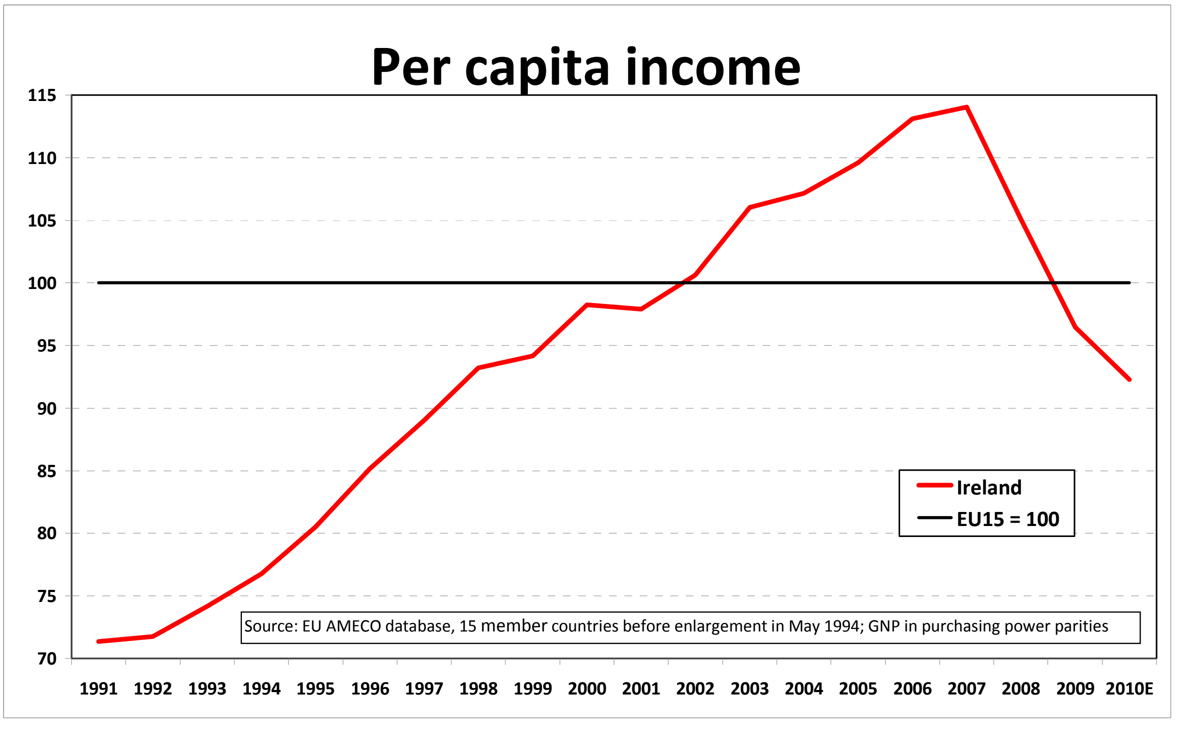
2.6.3 Despite predictions to the contrary, the Irish economy continued to expand after the Celtic Tiger period ended shortly after 2000. However, the dynamic changed. Exports no longer contributed significantly to growth which was now driven by domestic developments, notably investment in buildings.

2.6.4 Participation in EMU meant that monetary policy was set with regard to economic conditions in the euro area as a whole, with the result that nominal interest rates were too low for Irish circumstances. Combined with high inflation, real interest rates were negative for much of the period and the rate of credit growth increased rapidly.

2.6.5 The property boom was funded by cheap credit, increasingly sourced abroad in the form of interbank borrowing as the growth in domestic deposits failed to keep up with the explosion in credit. In some years, more than 80 per cent of the annual increment in credit went to fund a combination of house purchase and construction activity.

2.6.6 While there were occasional warnings, on the whole, both domestic and international commentators took a benign attitude towards the risks that were building up. The general view was that housing would experience a soft landing and there was no expectation that problems in the banking sector would have serious implications for the Exchequer or the economy generally.

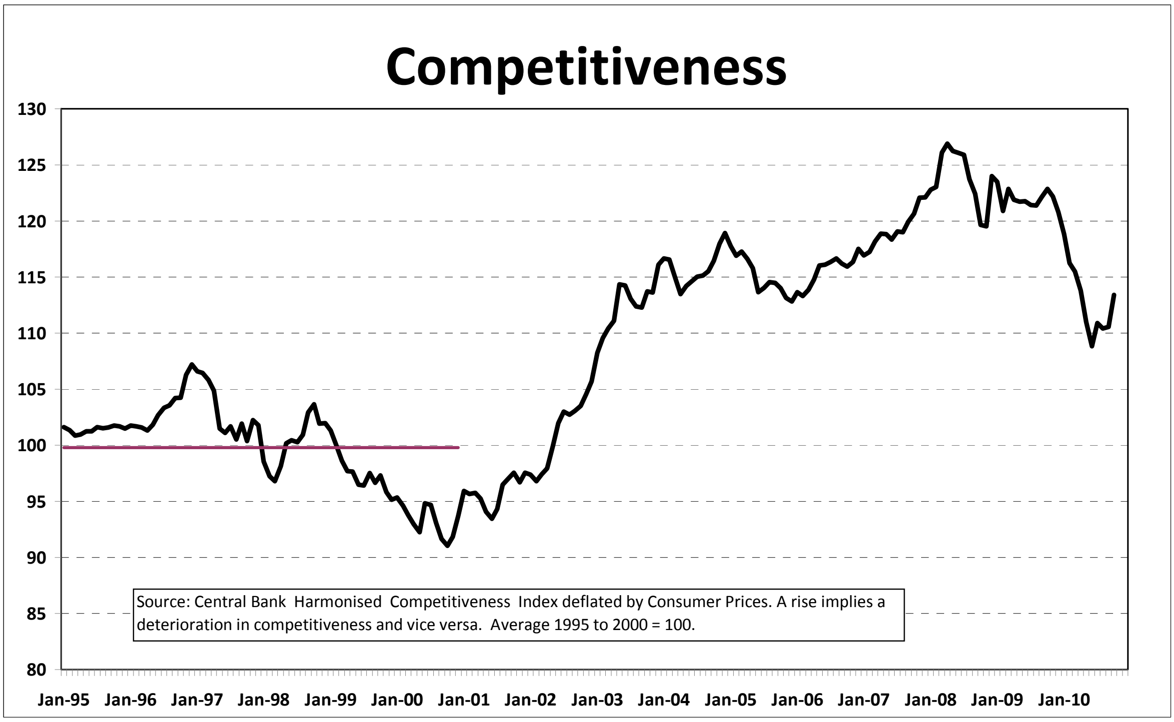
2.6.7 The upshot was a continued growth in per-capita incomes during most of the past decade. By 2003, Ireland had decisively moved above the EU average; in 2007 incomes peaked at 114 per cent of the EU average. Just two years later, Irish incomes were once again below the EU 15 average and in 2010 are estimated to be 8 per cent below the average with only Italy, Spain, Portugal and Greece recording lower levels of income. (GNP rather than the more usual GDP data are used for these comparisons as the Irish GDP data are inflated by multinational profits which accrue to non-residents thereby distorting the comparison). The pace of the downturn was particularly rapid.



2.6.8 From 2000 onwards, the Irish economy began to lose competitiveness. This reflected both currency movements and wage and cost developments. Because growth was driven by domestic factors, the loss of competitiveness did not register sufficiently with policy makers despite repeated warnings by the National Competiveness Council.

2.6.9 The cumulative loss in competitiveness, while difficult to measure accurately, was very considerable and by early 2008 the Central Bank's Harmonised Competitiveness Index had risen by 25 per cent above its 1995 base level and by even more when compared with the position at the turn of the century.

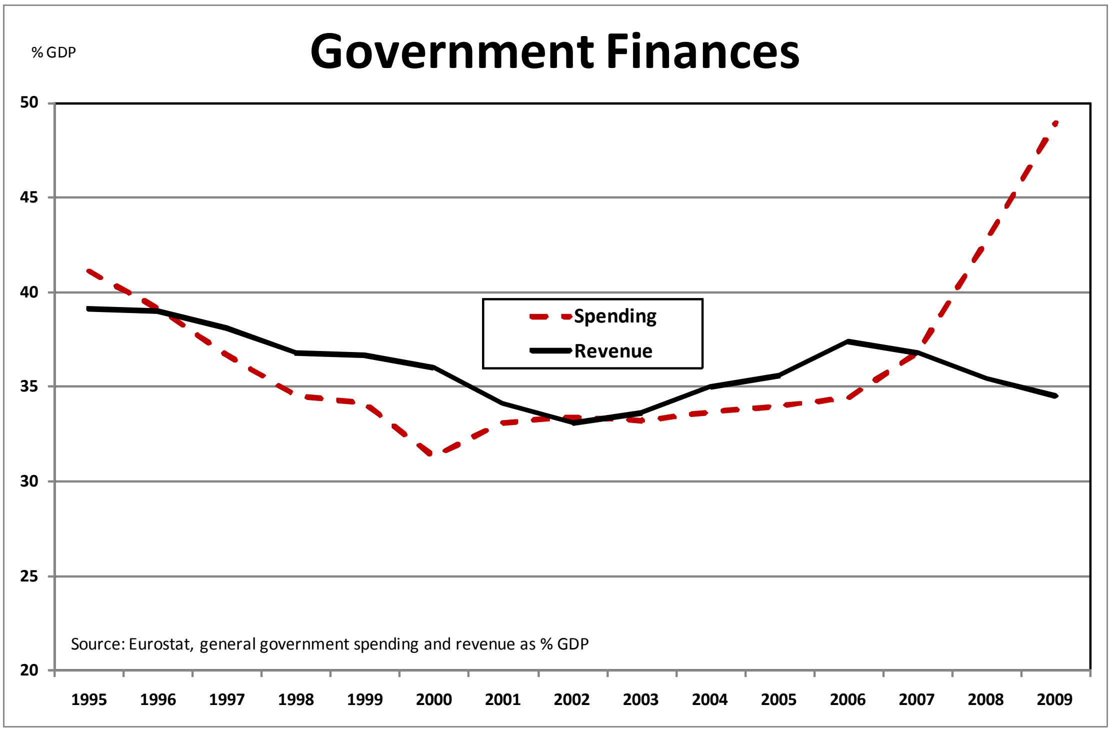
2.6.10 Recent developments have seen a substantial portion of this unwound as more favourable exchange rate movements and cost containment have helped move the index back to where it was in 2003. However, the competitiveness indicator is still about 13 percentage points above the average for 1995 to 2000.

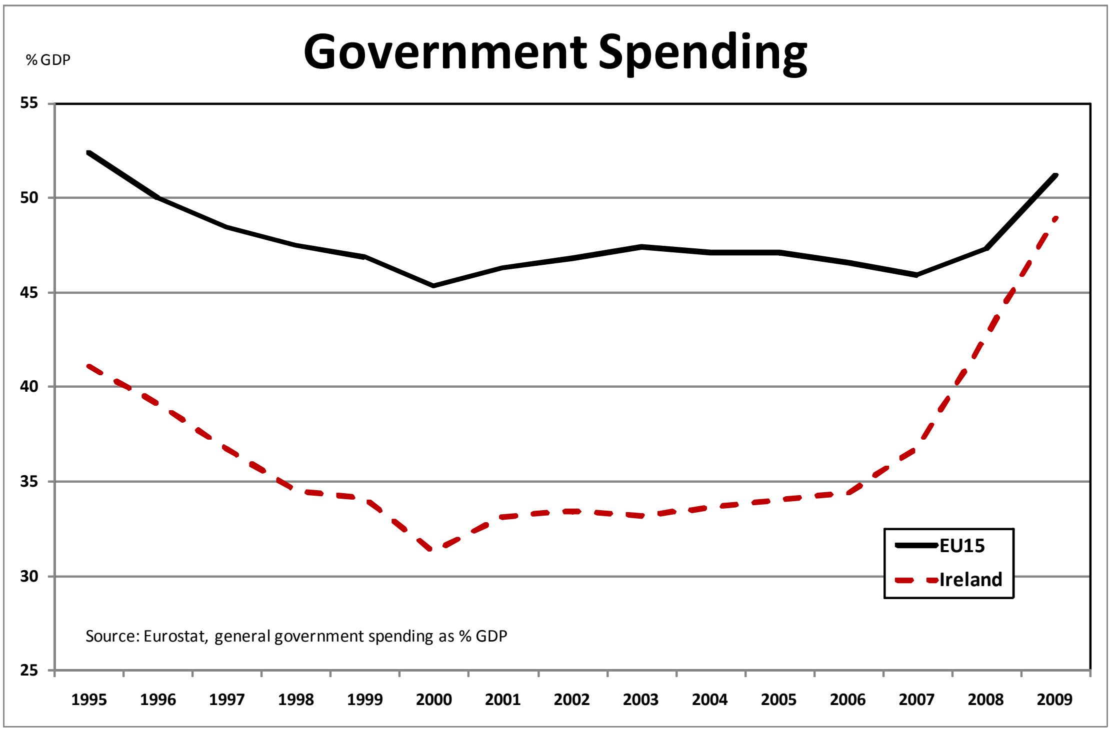


2.6.11 The steep growth in GDP from the mid-1990s onwards had a significant impact on the mindset of the Irish public and that of their politicians and brought with it pressures from a variety of quarters for major increases in public expenditure and reductions in taxation levels. Voted expenditure grew, on average, by about 11.5 per cent a year between 1998 and 2008 and major tax concessions were enacted throughout the decade.

2.6.12 The property bubble began to collapse from 2007 and the fall-out from this was exacerbated by significant deterioration in the external environment. Between 2007 and 2009, total general government receipts fell by 21 percent. While the yield on all tax heads fell, the declines in capital taxes (stamp duty, capital gains tax and capital acquisitions tax) were especially sharp.

2.6.13 Economic growth and a tax system geared to capture revenues from growth generated excesses in revenues over expenditure to 2007. From 2007 on, pressure on spending mounted, initially in the social welfare area as unemployment began to increase, and subsequently on debt interest. Despite the introduction of significant fiscal measures to curb spending and raise taxation, a large fiscal gap opened up.





2.6.14 In 2009, the deficit was 14.4 percent with an underlying fiscal deficit (i.e. excluding one-offs associated with the banking system) of about 12 percent of GDP. The situation in 2010 will be even more extreme and the overall deficit is estimated at 32 percent of GDP including emergency assistance to banks. Net of this, the underlying deficit will again be around 12 percent. Fiscal measures introduced to date, while considerable, have merely succeeded in stabilising the deficit at an elevated and unsustainable level.

2.6.15 For most of the past twenty years, the Irish economy was regarded as a model. Very few questioned this general consensus and those that did were ignored. The move from one of the poorest countries in the EU to one of the richest, in terms of annual income, fuelled expectations for increased spending towards levels in the rest of Europe. The EU fiscal rules, the Stability and Growth Pact, were respected, debt fell and spending appeared to be well below EU levels. The underlying dangers were either missed or ignored. Ireland was by no means unique in this, but the size of the hidden imbalances was greater and the subsequent correction more severe.

3. POLICY ADVICE OVER THE PAST TEN YEARS

3.1 Focus of Review

The Terms of Reference for our work task us to review the appropriateness of the Department's policy advice over the past 10 years, including its response to the current crisis. Given the range of work by the Department of Finance, it would be impossible to review in detail all of its advice over a ten year period, within our three month timeframe. Based upon its initial review of background documents and existing studies, the Panel decided to focus its efforts by reference to key observations from the Regling-Watson Report:

> "Fiscal policy heightened the vulnerability of the economy. At the macroeconomic level, it should have done more to dampen the powerful monetary and liquidity impulses that were stimulating the economy. Budgets that were strongly counter-cyclical could have helped to moderate the boom, and would also have created fiscal space to cushion the recession when it came. But budgetary policy veered more toward spending money while revenues came in. In addition, the pattern of tax cuts left revenues increasingly fragile, since they were dependent on taxes driven by the property sector and by high consumer spending. Ireland was also unusual in having tax deductibility for mortgages, and significant and distortive subsidies for commercial real estate development, yet no property tax." (page 5)

Consequently, our detailed review examined three key issues:

1. How appropriate was the Department's advice on the risk of pro-cyclical fiscal policy?
2. Was the Department aware of the risks of overheating in the property sector and did it provide advice appropriate to the circumstances?
3. Did the Department provide sufficient advice on the vulnerability of the tax system to an economic downturn?

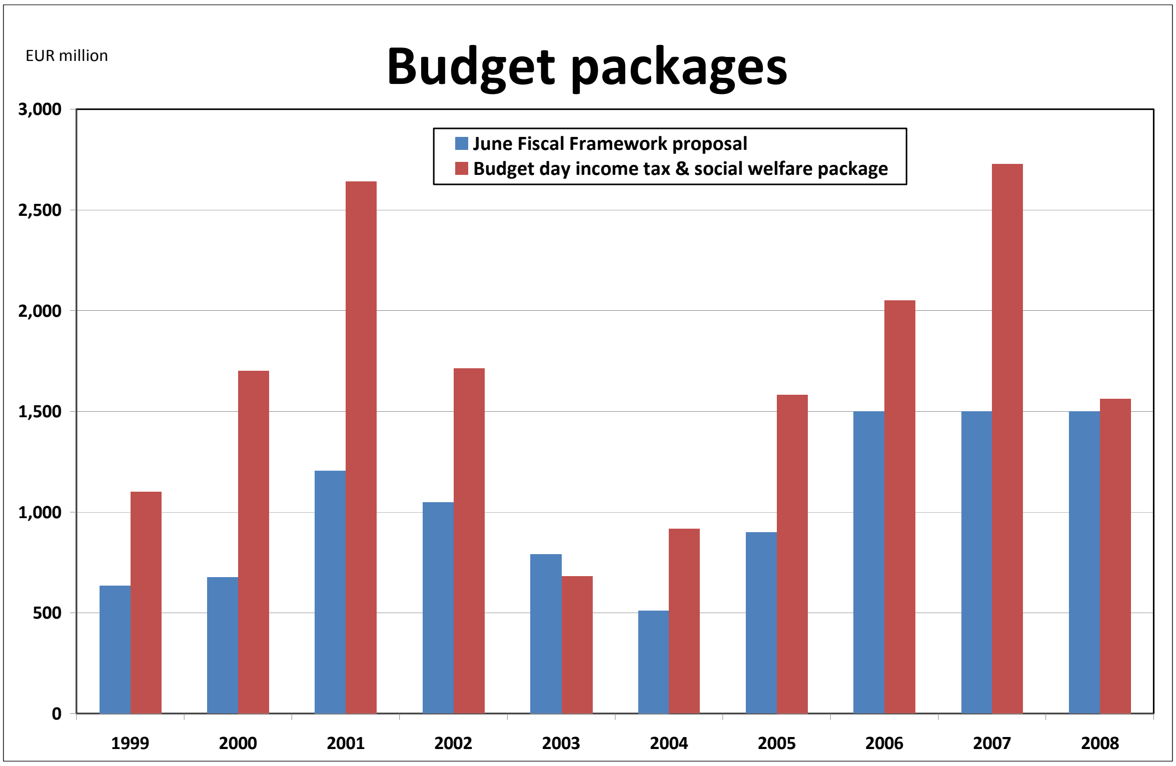
3.2 Pro-cyclical fiscal policy

3.2.1 The Panel reviewed international assessments of the risks of pro-cyclicality. A summary of commentary by the EC, OECD and IMF is at Appendix 6. These institutions frequently pointed to the risks of overheating prices and wages in Ireland, thereby decreasing its international competitiveness. Signals of overheating were especially loud in the early 2000s, when the Council gave an official warning to Ireland under article 99.4 of the Treaty, but became more muted as the global (and Irish) economy recovered from the burst of the ICT bubble. Nevertheless throughout the period, and especially from 2004 to 2008, these criticisms were leavened by favourable comment and even praise for Irish policy.

3.2.2 To review the Department's advice on the risk of pro-cyclical fiscal policy, the Panel began with a review of budgetary advice over the last ten years. The current budgetary process includes a number of stages. The Department consults other Departments, assesses the state of the economy, and works with the Minister to prepare a Memorandum to Cabinet on Budget Strategy in June of each year. That Memorandum projects economic and fiscal circumstances and outlines a quantum of spending and tax expenditure actions that are appropriate to the circumstances. Work to detail specific actions following this Cabinet discussion continues to the autumn. Since 2006, a Pre-Budget Outlook is usually issued in October to guide public dialogue up to the delivery of the Budget in early December. Significantly, final payments for previous year corporation tax and income tax payments by the self-employed yield critical information on the Government's current revenue position, well after the October Outlook and the initial Cabinet determination of Budget strategy in June.

3.2.3 The Panel reviewed in detail the annual June Memoranda to Cabinet on Budget Strategy. Generally speaking, we found that advice prepared by the Department for Cabinet did provide clear warnings on the risks of pro-cyclical fiscal action. These views were signed-off by the Finance Ministers of the day who would submit the Memoranda to Cabinet. Department officials do not, of course, participate in Cabinet discussion. This advice was more direct and comprehensive than concerns expressed by others in Ireland, or by international agencies.

3.2.4 With very few exceptions, however the quantum of spending and tax relief outlined in December Budgets was very substantially above that advocated by the Department and Minister in June. This can be seen in the chart following:



3.2.5 The differences between the position advocated in June and the outcome in December are stark but must be seen in the proper context. The Panel is conscious that the June quantum was seen as a starting point in the budgetary process. We present the chart simply to demonstrate that the June framework around which the Department's fiscal guidance was given was consistently and substantially exceeded. We examined why relatively prudent fiscal advice in June was systematically ignored in the Budget process. A number of factors contributed to this failure.

3.2.6 As noted earlier, very strong economic and fiscal performance in the 1990s created an extraordinary sense of optimism in Ireland. This fuelled enormous expectations of Government to create spending and tax initiatives to share the fruits of recent economic gains, even as the country's overall competitiveness degenerated substantially and revenues became unsustainable. These pressures were reflected in the political debate of the day where all political parties were eager to meet public expectations for more and better services. Consistently higher growth and revenue outcomes late in the Budget cycle further inflated expectations. Finally, the public and policy makers were insufficiently sensitive to the effects of extraordinarily expansive monetary conditions at the time, and to the fact that fiscal policy was the key potential counterbalance to this pressure.

3.2.7 Beyond a general sense of optimism, we review below two other aspects that contributed to this massive, sustained slippage from the June Fiscal Plans. First, a very poor budgetary process obscured ministerial and Government accountability to Parliament, and was overwhelmed by other spending processes – Programmes for Government and Social Partnership. Second, while departmental advice in June was generally appropriate, we have a number of observations as to how departmental advice could have been more effective over the entire budgetary cycle. We review these factors below.

3.3 Budgetary and other processes

3.3.1 All parties establish a platform going into an election. A vital part of coalition Government is the preparation of a joint Programme for Government by governing coalition partners. Such agreements are core to the political stability of the governing coalition and often include very specific spending and tax expenditure commitments. These initiatives are presented as given, without a full economic or fiscal analysis by the Department of Finance.

3.3.2 The process leaves the Department to debate the pace of delivery of new spending and tax initiatives but not the Government's commitment to these important fiscal matters. The Department could, and did, argue for reallocation of existing spending to offset new commitments in a Programme for Government. But this proved increasingly difficult, and ineffective, given the magnitude of Programme for Government commitments and the availability of resources. Included below is an excerpt from the 2002 Programme for Government that illustrates the specificity of these commitments.

> The parties remain committed to the achievement of the taxation objectives set out in Action Programme for the Millennium. Over the next five years our priorities with regard to personal taxation will be:
>
> – to achieve a position where all those on the national minimum wage are removed from the tax net, and
> - to ensure that 80% of all earners pay tax only at the standard rate.
> – to use the potential of the tax credit system to effectively target changes and to pursue further improvements in the income tax regime if economic resources permit.
>
> • We will complete the reduction of the standard rate of corporation tax to 12.5% in 2003.
> • We will increase Capital Gains Tax exemption limits.
> • We will examine the tax treatment of share options.
> • We will keep down taxes on work in order to ensure the competitiveness of the Irish economy and to maintain full employment.
> • We will vigorously pursue actions to ensure that that everyone is tax compliant.

3.3.3 The 2002 Programme for Government, like others, undertook to achieve these changes while promoting "low inflation" and "responsible fiscal policies" and maintaining the "public finances in a healthy condition". However, the dominant impact of Programmes for Government was to create a ready list of politically driven spending and tax initiatives to insert into Budgets, including to the extent of any last minute revenue availability.

3.3.4 The Social Partnership process was also a major driver of spending. Initiated in the 1980s, this process led to a number of national social and economic agreements between 1987 and 2009, which included pay settlements in the private and public sectors. The 1987 agreement and agreements in the 1990s tended to trade-off wage moderation for lower personal tax rates, with the effect of increasing take home pay. In the negotiations leading up to these agreements, the general levels of increases were effectively settled between the private sector employers and trade unions, with the increases applying by extension to the public service.

3.3.5 This process was extremely important to Ireland emerging as an economic growth leader in Europe. Wage costs were set at competitive levels. The process also created a climate of labour harmony that further enhanced the investment climate.

3.3.6 However, the process helped to generate profoundly different outcomes after 2000. An over-heated economy generated labour shortages and high wage demands. These pressures overwhelmed private sector wage negotiations and, through the Partnership Process, also inflated public sector outcomes. Such demands were difficult to deny given the burgeoning revenues generated by an over-heated economy. Economic overheating, along with the Social Partnership Process, led to a major deterioration in competitiveness in the Private Sector and to very high Public Service wages, especially relative to international partners. Primary School teacher salaries, for example, rose from seventh of ten countries in the OECD comparator group in 2002 to third, behind only Germany and Switzerland by 2008.

3.3.7 As the representative of the Public Service employers, the Department of Finance had an important input to the Partnership Process, and consistently warned of growing threats to competitiveness. But it did not drive the process, and was reluctant to oppose packages that included outcomes that retained labour peace for the economy as a whole.

3.3.8 Over the ten year period of review, the Programme for Government and Social Partnership Processes helped overwhelm the Budget process. Instead of providing an appropriate fiscal framework for prioritisation of competing demands on the Government's overall agenda, the Budget essentially paid the bills for these dominant processes. Relatively clear advice to Cabinet in June on the risks of excessive spending and tax reductions was lost by the time of December Budgets.

3.3.9 Spending pressures of this magnitude could have been resisted even within the established Budget process. However, the chance of success would be substantially enhanced by modernizing the budgetary process to protect the Government's annual fiscal framework.

3.3.10 In the current budgetary process, the period for public dialogue on economic and fiscal challenges facing the economy is far too short. Departmental advice on the economic outlook and sectoral challenges, for example, should be subject to more public and external scrutiny before Budgets are finalised. The process must also support a more rigorous commitment to the planned quantum of fiscal action. The objective of a renewed budgetary process should be to enhance ministerial accountability to Parliament, and the public by:

- creating a meaningful consultation period, and seeking broad feedback on the Government's fiscal plan,
- releasing more departmental analysis to inform public debate, and

- providing for third party validation of departmental analysis and the Government's fiscal plan through some form of Fiscal Council.

3.3.11 *Recommendations:*

1) *After Cabinet review of Budget strategy in June, and consistent with its April submission to the European Commission, the Government should release for public and parliamentary review:*

   - *the Department's economic and fiscal forecast,*
   - *the Department's assessment of the economic and fiscal risks to this outlook,*
   - *related sectoral analysis by the Department and*
   - *the Government's proposed quantum for fiscal action in new spending and tax expenditures.*

   The Minister and the Department should consult widely on this framework, particularly with the relevant Oireachtas Committee.

2) *Departments would not seek spending enhancements beyond the spring consultations leading to the Budget review at Cabinet.*
3) *To the extent that November tax results surprised to the upside, such revenue should be used for debt reduction, not new spending or tax relief.*
4) *The Panel supports the establishment of a Fiscal Council to review and publish commentary on the Department's analysis and the Government's proposed quantum for fiscal action. The Panel believes that such a Fiscal Council must be independent of Government, have qualified membership, a straight forward role and the ability to report in a timely manner. For example, following a June release of the Government's fiscal plan, the Fiscal Council could review:*

   - *the Department's economic and fiscal outlook,*
   - *the Department's risk assessment,*
   - *whether the proposed fiscal framework, including provision for new Government budgetary action, entails acceptable risks for the economy.*

5) *To the extent the December Budget exceeds the quantum of action identified in June, the Fiscal Council should reassess the risks of these further actions for the economy.*
6) *The Fiscal Council could also usefully assess the impact of future Social Partnership wage and fiscal provisions on Ireland's economic competitiveness.*

3.4 Economic and Fiscal Forecasting

3.4.1 The Department's economic and fiscal forecast is critical to the budgetary process. It helps to guide choices on economic and fiscal policy. The Panel's terms of reference specifically directed us to review the Department's record on economic and fiscal forecasting. The Department works closely, but informally, with colleagues in the Central Bank, ESRI and Revenue Commissioners to prepare its economic and fiscal forecasts. All those who discussed forecasting with the Panel judged the Department's work to be as good as any other institution making forecasts of the Irish economy. However, the recent past also demonstrates that it is extremely difficult to project "turning points" particularly in a rapidly growing economy.

3.4.2 More critical comments were made on the issue of whether the Department and Government could not have been more active in publishing alternative forecast scenarios. Given the record of advice and concern on pro-cyclical fiscal policy in the Department, a forecast scenario of a major correction could have been very informative, in retrospect. An improved budgetary process overall would also strengthen the forecasting function. The Panel believes that this function would be further strengthened by a more robust engagement with outside economists.

3.4.3 *Recommendations:*

7) *Forecasts in Budget Memoranda to Cabinet and for public consultations should include well articulated scenarios of alternative outcomes, consistent with the Department's risk analysis.*
8) *In addition, the Department should provide a public work-shop, with private sector and academic interests, once a year so that the assessment of the economic and fiscal challenges can be debated before the Department finalises its forecasts.*

3.5 Departmental Advice

Had departmental and ministerial advice to Cabinet at the start of the budgetary cycle been accepted and sustained, Ireland would have been better positioned to deal with the current economic challenges. We have reviewed some systemic reasons for this failure. The Department should have done more to avoid this outcome. It should have adapted its advice in tone and urgency after a number of years of fiscal complacency. It should have been more sensitive to, and provided specific advice on, broader macroeconomic risks. And it should have shown more initiative in making these points and in its advice on the construction boom and tax policy generally. These points are infinitely easier to make in retrospect, in a profoundly different public and policy context than during the exuberance of the last decade. We make them not to judge; but to guide our advice on how to improve the Department of Finance for the future.

3.6 Advice over the Budget Cycle

3.6.1 The Department did not adapt the tone of its advice against pro-cyclical action over time. As noted earlier, the Budget Memoranda to Cabinet from 2000 to 2008 generally provided appropriate advice to maintain a prudent fiscal stance. Despite this, Government action in subsequent Budgets was successively above levels recommended by the Minister and Department in June. There are a number of reasons for this which could have been surmised for any one year in question. But after several years of fiscal action well above that clearly recommended by the Department, one would have expected the tone, and shape, of advice on the risks of this path to increase vigorously. We would have expected more initiative to make these points in new ways. This did not happen.

3.6.2 The Panel must also report a limited amount of formal analysis and advice on fiscal risks outside of the June Memoranda to Cabinet. In part, this reflects a focus on the established budgetary process. But given the impact of spending pressures on Budget outcomes, one would have expected a stronger stream of cautionary advice on the risk of pro-cyclicality, especially as spending and tax relief initiatives outpaced amounts recommended to Cabinet in June by a large amount.

3.6.3 There are examples of where such advice was tendered in writing. We have also been advised of some important oral briefs that reinforced the Department's concern about pro-cyclicality. But these are not part of the official record. It is not unusual for Finance Departments worldwide to provide much of their background briefing orally. But it is best practice to maintain a formal written record. This ensures that Ministers are provided with the best possible advice from their officials. A written record enhances the accountability of officials to provide advice and forces clarity of thought. It helps to ensure clear internal communications between different areas of the Department. A record also establishes clear accountability for advice not taken. The lack of a coherent record of budgetary advice represents a major shortcoming in the systems of the Department of Finance.

3.6.4 Under Ireland's Freedom of Information law, policy advice tendered outside of Cabinet consideration is subject to public disclosure. A public airing of serious policy differences between a Minister for Finance and his advisors could have serious implications for financial markets. At a minimum, it would strain relationships between the Minister and his officials and this would be very damaging to the budgetary process.

3.6.5 Our review has established that possible Freedom of Information release does limit the written record of non-consensual advice. Secretary Generals of other Departments have noted this. And it certainly appears to be the case in the Department of Finance. This is a paradox – a law introduced to provide greater public access to information has not done so, but has instead helped substantially to limit vital public records. The Panel supports the maximum possible public access to official records. Indeed, we believe there should be greater access to economic analysis generated by the Department of Finance. But, we believe that there should be an exception in the case of Budget policy advice to the Minister. It should not be accessible given market sensitivity and other factors outlined above. It should be noted that the Comptroller and Auditor General already has access to all such files and can report, as needed, on issues of concern.

3.6.6 *Recommendations:*

9) *The Department of Finance should keep a written record of advice tendered and decisions taken as part of the budgetary process.*
10) *The Panel strongly supports the public release of substantially more economic analysis by the Department. However, policy advice to the Minister for Finance in*

the preparation of the Government's Budget should not be subject to release under Freedom of Information for at least five years.

3.7 Macroeconomic Risks

3.7.1 The Department paid insufficient attention to broader macro-economic risks. While suitably direct on the risks of excessive spending and tax relief, annual departmental advice to Cabinet generally did not consider the broader set of macroeconomic risks. It did not, for example, consider the risks related to the extraordinarily expansive monetary conditions, which substantially heightened the risks of pro-cyclical fiscal action identified by the Department. This too, represents a significant deficiency. In part, this was due to insufficient oversight of the various agencies tasked with contributing to Ireland's financial stability. It was also due, at least in part, to a shortage of highly-trained economists and financial market experts in the Department. The Department also appeared to have had too limited a view of its own responsibilities to monitor the comprehensive set of macroeconomic risks to Ireland.

3.7.2 In times of economic need the country turns to its Minister and Department of Finance to play a key role in managing the situation. The recent banking crisis in Ireland demonstrates that, even where the Department does not bear a direct accountability for the problem at hand, it is called upon to contribute to a solution. It is also uniquely well placed to provide the Government with a regular assessment of overall fiscal and economic risks to the country through its Budget process. A key lesson from Ireland's recent banking regulatory failure was that the Department needs to be enabled, and clearly accountable, to report on broader risks to the economy. This must include new activities such as NAMA. The role of the Department would not be to manage this initiative but to be in a position to assess and report on systemic risk.

3.7.3 *Recommendations:*

11) *The Panel recommends that the Department prepare comprehensive macroeconomic risk assessment for Ireland as part of its annual advice to Cabinet.*

12) *The Department should establish sufficient formal arrangements with the Central Bank, including its Financial Regulation function, the NTMA and NAMA, and establish sufficient technical capacity internally to manage this process.*
13) *The Government should introduce legislation to establish a co-ordinating committee of these financial agencies, chaired by the Secretary General of the Department of Finance, which would require the full exchange of any information that could entail fiscal or economic risks to the country, among the above agencies.*

3.8 Construction Policy

3.8.1 As part of the annual Memorandum to Cabinet on Budget preparations, and separately, the Department did provide advice on the risks of on overheated construction sector as far back as 1999. The Department's assessments of the risks from the Irish housing bubble were at least as strong as any public analysis over the period. However, there were countervailing views at the time and even demands for substantial additional tax incentives for construction which, thankfully, were rejected by the Government.

3.8.2 Based on departmental advice, the Government took some limited action to moderate tax incentives for construction early in the decade and again eventually in 2006/2007. However this action was not sustained and was too little and too late to moderate construction activity sufficiently.

3.8.3 Despite repeated expressions of concern over the construction sector in Budget Memoranda to Cabinet and elsewhere, the Department did not organise a strategic response to the problem, or identify a full range of options to moderate activity in the sector. The Department also lacked coherence across its divisions in dealing with the issue. An example of this was the Department's response to concerns elsewhere in Government, and in some areas of the banking sector, about the introduction of 100 percent mortgages. Admittedly, the Department would have had a hard time fighting 100 percent mortgages given the Government's strong concern about home affordability for first-time buyers. Once the Financial Regulator, who is accountable for such authorisations, declared himself to be fully satisfied with the introduction of these instruments, the Department stopped considering the issue. This was an opportunity lost.

3.8.4 *Recommendation:*

14) *The Department should include sectoral assessments in its annual economic analysis and forecast that is released for public consultation.*

3.9 Tax Policy Advice

3.9.1 The panel reviewed whether the Department adequately advised on the vulnerability of the tax system to a downturn. First, the Department was very clear on the risks to the Exchequer of a downturn in the construction sector, providing specific estimates of the fiscal risks, and clear advice on the dangers of relying on related tax revenues.

3.9.2 However, there was no analysis or advice on the broader risk to the tax system from a more general downturn in economic activity from levels created in part by pro-cyclical fiscal policy. This lack of policy initiative is again disappointing, given the very active tax agenda of the Government over the last ten years. In fairness, the Government's tax agenda was effectively defined at the political level, as part of the Programme for Government. For example, Programmes for Government limited the income tax base by removing minimum wage earners from the tax net and committing to keep 80 per cent of taxpayers at the lowest rate of taxes. These were effective political messages for the electorate, but not good tax policy. Once established as Government policy, there was no market for departmental advice on the suitability of such commitments. But such analysis should have been provided and communicated forcefully to the Minister for Finance and the Government.

3.9.3 The result was the narrowing of the tax-base to an unsustainable degree and commitment to major tax expenditures. The narrowness of the tax base and the complexity of the tax system suggest to the Panel that there is need for a review of the entire system.

3.9.4 *Recommendation:*

15) *The Department should substantially increase its analytical capacity in the tax policy area.*
16) *The Department should organise itself to consult with tax and financial experts and prepare advice that is most appropriate to an efficient tax regime for Ireland.*

3.10 Department's Response to the Crisis

3.10.1 The Panel reviewed the Department's support to the Government since the banking crisis broke. The Department played a key role on the banking side by using the Domestic Standing Group to organise a whole of Government assessment of the situation at the early stages of the crisis. The Department also played a lead role in managing the Government's fiscal response to the crisis, including several major policy packages:

- major fiscal action in Budget 2009,
- again in the supplementary 2009 Budget,
- in Budget 2010, and
- in the Public Service Agreement, 2010-2014 (the Croke Park Agreement).

3.10.2 These actions reflect a marked enhancement in leadership from an organisation not called upon to lead for much of the previous decade.

3.10.3 Every party that worked with the Department over this period commented positively on the quality of effort and professionalism displayed during this period of need. At the same time, the extraordinary pace of activity has exposed some major shortcomings in the Department's capacity. When the banking crisis broke, the Department had neither the time nor the resources to conduct in-depth investigation of issues. This reflected shortages of skills in the requisite disciplines and inadequate knowledge of underlying developments in the sector.

3.11 Medium Term Analysis

3.11.1 Any Finance Ministry should have a medium-term economic planning capacity. Economic planning and analysis are specific elements of the Department's statutory functions since the Department of Economic Planning and Development was merged with the Department of Finance in 1980. The Department has developed the *National Recovery Plan 2011-2014* and will monitor its implementation over the coming years.

3.11.2 The Panel is aware that the Department did carry out medium-term economic analysis, including demographic analysis, in the past. The Department is to be commended for the preparation of its demographic study in 1998 which was released for public consultation and led to the establishment of the National Pension Reserve Fund. It is unfortunate that a similar study in 2003 was not released for public consultation.

3.11.3 The rigour of the Department's economic planning activities will be significantly enhanced by active engagement with other economic analysts both inside and outside of the Government sector.

3.11.4 *Recommendation:*

17) The Government should commit to the preparation of regular medium- term economic plans for Ireland at least every five years.

4. STRENGTHENING THE DEPARTMENT OF FINANCE

4.1 Ireland needs a strong Department of Finance as it faces some extraordinary challenges including:

- the implementation of recently launched *National Recovery Plan 2011-2014*;
- A significantly different relationship with international institutions including: the European Commission, IMF, OECD and international rating agencies.
- The need for an enhanced relationship with other institutions within the portfolio of the Minister for Finance, including the Central Bank and its Financial Regulation function, the National Treasury Management Agency and NAMA.
- The need for major progress on Public Service Modernisation.

To meet these challenges the Department needs to be substantially strengthened in its core functions.

4.2 Readiness of the Department for future challenges

4.2.1 Based upon our analysis, submissions from others, and consistent with views of Finance employees and managers we met, the Department:

- does not have critical mass in areas where technical economic skills are required;
- has too many generalists in positions requiring technical economic and other skills;
- is more numbers driven than strategic;
- does not have sufficient engagement with the broader economic community in Ireland;
- often operates in silos, with limited information sharing;
- is poorly structured in a number of areas, including at the senior management level; and
- is poor on Human Resources Management.

4.2.2 We have been direct in our analysis and advice, but do not accept the notion that the Department is not fit for purpose. It is. It has worked hard in response to the banking and economic crisis and must now apply the same determination to remake itself in the light of the above observations and the major challenges confronting Ireland. We provide some specific advice on how it can begin to do so, looking at structures, people, and processes. But we begin with a discussion of Public Service Management before we turn our attention to the core Finance functions.

4.3 Department's Interface with Other Departments

4.3.1 Many Secretaries General from other Departments expressed frustration at the insufficient coordination between the "two sides" of Finance – Public Service Management and Development, and Sectoral Policy, in particular in relation to control of Public Service numbers. Others observed that the Department lacked a critical mass, or interest in a strategic interface with line Departments. Observers within the Department identified this as a problem that must be addressed, as they did with the 2009 Capacity Review.

4.3.2 The Panel believes that combining the Public Service numbers control function with the Sectoral Policy area will assist the Department in making the right choices in relation to spending and personnel issues. Given the well articulated need for medium-term economic planning, such a fusion would also help the Department in its interface with other key Departments and agencies.

4.3.3 *Recommendations:*

18) *The Department should integrate those sections of Public Service Management and Development Division dealing with administrative budgets into Sectoral Policy Division to create a "single window" interface with line Departments.*
19) *Activities could be organised immediately under the Assistant Secretary level in the Sectoral Policy Division. The longer-term objective should be to establish Principal positions responsible for the interface of all activities with outside Departments.*

4.4 Public Service Management and Development

4.4.1 When the Public Service Management function returned to the Department in 1987 it did not reintegrate. It still has a separate Secretary General who participates in the Finance Management Committee. Industrial relations activities and collective bargaining advice warrant such a senior level oversight; Public Service Reform warrants such oversight even more so. But the Division needs either to integrate more fully into the Finance structure or become clearly established as a distinct entity.

4.4.2 Other reviews have considered moving Public Service Management out of the Department of Finance but refrained from doing so because of the major impact of public sector wage negotiations on the fiscal framework. Given the economic and fiscal challenges of the next several years, the Minister and Secretary General of Finance should not be distracted by non-core issues. As well, there is an extraordinary opportunity afforded by the Croke Park Agreement to accelerate dramatically Public Service modernisation at this time. We are convinced that the public service function should be managed as a distinct entity. New structures must be considered to energise this effort, including a separate Department or direct relationship with the Minister of State for Public Service Modernisation.

4.4.3 If Public Service Management is structured as a separate Department, the Department of Finance should control the wage bill, the quantum for wage settlements and manage the single window on personnel and financing controls for line Departments. It should also have an important say on how collective bargaining should be managed. But it should not manage industrial relations, common services, collective bargaining processes or Public Service Modernisation.

4.4.4 *Recommendations:*

20) *Public Service Management and Development Division should be established as a separate entity, either as an entirely separate Department or reporting directly to the Minister of State for Public Service Modernisation.*
21) *The Secretary General of the Department of Finance and Minister for Finance should retain authority over the overall wage bill, negotiating mandates for new*

collective bargaining processes and manage a single window on departmental control functions.

4.5 Public Service Modernisation

4.5.1 Some significant strides have been made in the area of Public Service Modernisation, particularly on improved electronic and other services to the public. However progress on Public Service Modernisation generally has been very disappointing. The Department of Finance must bear its share of the responsibility for this. The Department has not prioritised Public Service Modernisation, and has devoted limited resources to the area.

4.5.2 The Irish Public Service confronts much greater rigidity in managing change than do other EU and OECD countries. During the Celtic Tiger years, with an abundance of resources, the need to improve the efficiency of the public service was not as clearly seen as a priority as it is now. As well, the Partnership Process was not supportive of dramatic reform in the Public Service. The terms of the Croke Park Agreement signal that this is no longer the case.

4.5.3 Ireland is clearly entering a period of prolonged fiscal restraint. In this environment, major public service reforms are essential to help facilitate adjustment in public administration and minimise service reductions to the public. That is the commitment of Croke Park – to manage change much more efficiently for the public good. A process is well under way to have Departments identify the flexibilities needed to adapt efficiently to spending constraints about to be identified in the Budgets for 2011 and beyond.

4.5.4 More work is needed to enhance the transparency of this process and to identify other reforms that are possible on central human resource policies. Much less work is underway on this latter issue, but it is equally important. The Panel's work on the Department of Finance's critical shortage of technical skills, leads us to conclude that major reforms must also be instituted on these central human resource policies, especially staffing.

4.5.5 The challenge of current Public Service Modernisation is relatively well defined. What is missing is a strong organisation for effective implementation. We believe that establishing the Public Service Management Division as a distinct entity would help. It should be supplemented with two other initiatives: a private sector board to help drive real change and an inter-Governmental task force on implementation.

4.5.6 To maximise the opportunities of Public Service Reform, greater co-ordination of effort with major Departments overseeing Public Service Modernisation in their respective sectors, is also required. A full-time Task Force involving key players from these Departments, together with private sector expertise, should be established to drive forward the reform initiative and ensure its implementation. The duration of the Task Force would be coterminous with that of the Croke Park Agreement. In addition, there is a need to recruit expertise in the area of change management and business process re-engineering.

4.5.7 The Task Force should have a team-leader who would have direct access to the Minister of State responsible for Public Service Modernisation.

4.5.8 *Recommendations*:

22) *The Panel strongly supports the creation of a Private Sector Advisory Board which it understands is under consideration by the Departments of the Taoiseach and Finance.*
23) *A full-time Task Force should be established and assigned responsibility for driving forward the reforms under the Croke Park Agreement.*
24) *The Task Force would comprise existing staff from the Modernisation Unit of the Department. The Task Force would also include key individuals from the leading Departments along with expertise in the area of change management on secondment from the private sector.*
25) *The Task Force's Team leader should have direct access to the Minister of State responsible for Public Service Modernisation.*
26) *In addition, there is a need to recruit expertise in the areas of change management and business process re-engineering.*

4.6 Core Finance Functions

4.6.1 Excluding Public Service Management and Development Division reduces the Finance staffing level to some 400 people. Given current economic challenges, some have argued for the creation of new budgetary and analytical agencies reporting to Parliament. Others have argued that the Sectoral Policy Division of Finance be transferred to a separate Department with Public Service Management functions. These ideas all contribute to an important public debate on how to strengthen Ireland's capacity to manage its financial and economic affairs.

4.6.2 Reflecting on these ideas, we believe the top priority should be to strengthen the core functions of the Department of Finance. This will be a major undertaking. The Department will not be able to lead on the *National Recovery Plan 2011-2014* without its Sectoral Policy Division. And the function could not be created elsewhere to have effect for a considerable time. Its effectiveness would be highly questionable without a link to the Department and the Minister for Finance. Consequently, we do not support the suggestion that the Sectoral Policy Division be removed from the Department of Finance.

4.6.3 A substantially improved budgetary process that would enhance ministerial accountability to Parliament, as recommended above, would in our view be more effective than the creation of new agencies of Parliament. Resources to enhance economic analysis could be more effective if assigned to the Department of Finance than to new agencies.

4.6.4 The transfer of treasury operations to the NTMA helped create a very capable institution with a very broad remit. However the change weakened the skills set in the Department of Finance on finance and banking. This impaired the Department's capacity to respond to the banking crisis.

4.6.5 *Recommendation:*

27) *With the possible exception of the Public Service Management and Development Division, no other core functions should be moved out of the Department of Finance.*

4.7 Structure

4.7.1 The Department of Finance is unique among Civil Service Departments in that Assistant Secretaries do not report directly to the Secretary General. There is an additional level of management – Second Secretary General[1] - between the Secretary General and the Assistant Secretaries in the Department of Finance. This arrangement blurs accountability, under-utilises the expertise of Assistant Secretaries and helps to inhibit effective internal communications.

4.7.2 It is our view that the existing and future needs of the Department require changes to the roles and responsibilities of the Second Secretary grade. It is simply not possible for the Secretary General to deal with the large number of high-level, pressing issues confronting the Department without this senior level of support. However, removing Second Secretaries from their responsibilities as managers of large Divisions would free them up to play a more strategic support role than is possible at present.

4.7.3 *Recommendations:*

28) *Assistant Secretaries should report directly to the Secretary General of Finance.*
29) *Second Secretaries should cease to have divisional line management responsibilities, but should be able to call upon resources across the Department as and when necessary.*
30) *The Second Secretary currently responsible for Sectoral Policy Division should be designated as Chief Operating Officer for the Department. The function of this post would be to lead the co-ordination across the Department of major issues, for example, to lead the interaction between the Budget and expenditure sides of the Department, and otherwise to help ensure the entire Department is connected to key policy and management issues.*
31) *The Second Secretary post leading the Budget, Tax and Economic Division could focus primarily on the increasingly important role of interacting with the institutions of the European Union and other international institutions.*
32) *The Second Secretary responsible for Financial Services should retain responsibility for this function until such time as the banking crisis is considered to*

[1] One of the positions at the second level is graded as Secretary General, and is in charge of Public Service Management and Development Division.

have abated sufficiently. At that time the post should be abolished. That Second Secretary could draw on the support of the Assistant Secretaries currently in that Division as necessary, but they would report directly to the Secretary General.

4.8 The Management Advisory Committee (MAC)

4.8.1 The Department's MAC does not play a meaningful role in ensuring that senior management debate all major policy issues of concern to the Department. We understand that the MAC structure is used, in the main, for exchange of information. While that function can be useful, the Panel feels that the essential role for a MAC should be to act as a clearing house for major policy and management issues.

4.8.2 The Department's MAC is also unique in not having the Department's Assistant Secretaries as permanent members. Assistant Secretaries now attend the MAC on a rotational basis, but are not formally briefed on meetings they miss. It would be essential that a MAC with a broader remit, as recommended by us, would not be deprived of the invaluable intelligence, experience, insights and expertise that the Assistant Secretary grade has to offer.

4.8.3 *Recommendations:*

33) *The remit of the MAC should be broadened to include discussion of major strategic challenges confronting the Department.*
34) *All those that report to the Secretary General should attend MAC meetings. Given the pace of change underway, MAC meetings could usefully include a brief report by Assistant Secretaries on key issues in their area, where appropriate, as well as Secretary General and Second Secretary reports on high level issues.*
35) *Attendees at MAC should, as a matter of course, brief their own direct reports on outcomes from these meetings.*
36) *The MAC should meet more often at Budget time and during periods of major change to enhance internal communication and connect all employees to emerging issues. It should schedule regular meetings on key policy issues.*

4.9 Corporate Secretariat

4.9.1 There is no corporate affairs function in the Department of Finance where staff work at a very intense level and where a lack of coordination can present major challenges. In most large organisations, corporate secretariats are seen as providing a key support to management and as presenting the organisation to the outside community. In the Department of Finance, such a function would help to ensure that management and staff were apprised of emerging issues affecting their areas of responsibility and that the Department presented a clear and consistent message to the public and to the media. It would interface with the Minister's Office and provide a focus for the Department's outreach efforts. The Panel believe that such a secretariat, properly staffed and with a clear mandate, could bring enormous benefits to the Department, both internally and externally.

4.9.2 *Recommendation:*

37) A Corporate Secretariat, which should be headed by a Principal who would report directly to the Secretary General, should be established. It would bring together and enhance a number of functions which are located in different areas of the Department. The functions of the Secretariat would be to:

- *manage the interface with the Minister's Office;*
- *co-ordinate briefs and draft speeches for the Minister to ensure consistency and quality;*
- *help ensure effective internal communications;*
- *manage departmental outreach and the Department's profile;*
- *co-ordinate, on a regular basis, the preparation of a brief for MAC on all major live issues and an early warning on significant emerging issues;*
- *help co-ordinate major departmental initiatives;*
- *co-ordinate departmental strategy statements;*
- *manage the activities of the Department's Press Office; and*
- *manage the Freedom of Information function in the Department.*

4.10 Structure at the Working Level

4.10.1 We have recommended that the management role of Assistant Secretaries should be clarified and enhanced. We are also aware that there is a tendency in the Department for work and responsibility to be retained at senior management levels when it could, more appropriately, be delegated. Each Assistant Secretary should look at his/her responsibilities with a view to devolving work to Principals. Principals should also ensure that they have devolved work appropriately to their Assistant Principals.

4.10.2 The Panel also has concerns about the spread of responsibilities at the level of Principal and at the basic work unit in the Department below Principal, i.e. the section led by an Assistant Principal. We noted that, across the Department, the ratio of Principals to Assistant Principals is currently approximately 1:2.5, while the number of Assistant Principals is almost equivalent to the number of Administrative Officers (AOs) and Higher Executive Officers (HEOs) reporting to them. The situation varies in some areas, with some supervisors having more or less than the average. This narrow reporting structure is unlikely to foster horizontal thinking on the part of either Principals or Assistant Principals. Equally, it deprives staff of the benefits of working as part of a wider team. Finally, it could be wasteful of resources. It is our view that this structure should be changed to enhance teamwork and broaden the span of responsibility and supervision at Principal and Assistant Principal levels.

4.10.3 *Recommendation:*

38) The Department should examine working level structures and the devolution of responsibilities to ensure the delegation of more responsibilities to middle management levels and to create larger teams throughout the organisation.

4.11 Enhancing the Department's technical skills

4.11.1 In its cadre of 542 staff, the Department has only 39 economists trained to Masters level or higher. Many of these individuals are public servants of the highest calibre and excellent practitioners of applied economics. Many other staff who have less formal economic training have also distinguished themselves over the period of our review.

However, 39 economists in the Department of Finance is extraordinarily low by international standards. Even excluding the public service cadre of 135 people, this represents less than 10 percent of the total staff complement in the core of Finance. In contrast, 60 percent of the Canadian Department of Finance are economists trained to Masters level or higher; and about 40% of staff in the core areas of the Dutch Finance Ministry are trained to Masters level or higher.

4.11.2 The Department does not need 60 percent of its staff to be economists. But it must make an urgent and sustained effort to boost its number of economists and other skilled staff. Management should define the technical needs of positions and hire the best person for the job whether from within Government or otherwise.

4.11.3 *Recommendations:*

39) *Even in this period of restraint, the Department must find a way to increase substantially the numbers of economists and other staff with relevant technical qualifications.*
40) *The Department should double the number of economists, appointed through open, public competition and trained to Masters level or higher, over the next two years. These appointees should comprise a mix of recent university graduates and experienced individuals and be assigned to positions throughout the organisation. The Department should organise itself to maintain a regular inflow of new university recruits.*
41) *The Department should work to establish a welcoming professional environment for new economists. Economists at Masters level and above should be identified and their numbers reported on annually; a champion for establishing and promoting this "community of interest" should be named.*
42) *The economic seminars by external economists, which were recently introduced by the Secretary General, should be made permanent; the Department should permit the publication of professional economic analyses, by staff in the Department, that are clearly identified as not the views of the Department.*
43) *The Department should expand its complement of skilled staff in other disciplines, especially accounting, analysis, banking and financial markets.*
44) *The Department should immediately seek the secondment of skilled personnel on a two-year rotation from the Central Bank, NTMA, ESRI and other relevant bodies.*

45) *The Department should also promote exchange agreements with other Finance Departments internationally.*

4.12 Enhanced HR function

4.12.1 Human Resource Management is currently a low priority for the Department of Finance. The importance of this function tends to be crowded out by the daily churn of urgent issues. The consequences of the neglect of this area are evident in a number of ways: insufficient commitment across the Department to performance management, skills shortages in critical areas and reporting structures at senior and middle-management levels that are far from ideal.

4.12.2 If this function is to be enhanced, and to contribute proactively to the essential development of the Department, it must be lead by an appropriately qualified, dynamic HR specialist, ideally with relevant experience in the private sector. The HR specialist would be given a small number of high-level targets to be achieved over a three year period. In order to give the Department more freedom with regard to the contract of the appointee and to stress the results-driven nature of the post, consideration might be given to making the appointment on a short-term contract, initially for three years.

4.12.3 The majority of staff at the Department are well suited to the needs of their position. As in any organization, some are not, and conspicuously underperform. This is a serious morale issue for other employees and a material impediment to departmental performance, particularly in a period of restraint. Performance management is a challenge to deal with in any organization. The Department also currently lacks the tools to deal with the issue, and must substantially upgrade its performance assessment process and practices and establish broader support mechanisms to help managers confront under-performance.

4.12.4 The Department of Finance should become a centre of excellence in the area of performance management and act as an example to other areas of the Public Service in this regard. We are aware that this issue is of concern to employees and the senior management in the Department. We would like to see a clear articulation from top management of the necessity for a properly-functioning performance management system where issues of under-performance are addressed effectively.

4.12.5 *Recommendations*:

46) *A senior HR specialist should be appointed to the Department initially, at any rate, on a short-term contract. The post would be advertised and preference would be given to an individual who had managed a dynamic HR function in the private sector.*
47) *The Department should reinforce its performance review process and require the identification of under-performance and an individualised plan to deal with problems identified.*
48) *Once each year, the MAC should take a full day to review individual performance in the Department. It should identify, of all supervisors, the top 20% on people management – those who recognise high performance and deal with poor performance. This process should also identify the bottom 20% - those supervisors who are not performing well in this area and those who are not taking a proactive approach to this issue. Plans to address under-performance should be required. A supervisor's performance in "people management" should have a material impact on consideration for promotion.*

4.13 Change Management

4.13.1 Collectively, the recommendations of the Panel represent major change in the Department of Finance. The Panel believes this change agenda will be embraced by the Department and its Secretary General. The Secretary General will need personally to lead this renewal process but will require support.

4.13.2 *Recommendations:*

49) *The Secretary General should present a Change Management Plan to employees and report on progress in an annual accountability session to all staff.*
50) *He should be supported by all managers, by a champion for change management at Assistant Secretary level and by the newly recruited professional HR specialist.*

5. CONCLUSIONS

5.1 In virtually all countries, responsibility for monetary policy is delegated to a Central Bank that is independent of the political process. This occurs because it has proven to be virtually impossible for the political process in any democracy to sanction explicitly action to restrain economic growth early enough in the business cycle to avoid dangerous overheating of the economy. As a relatively small nation now within a large monetary union, the Irish Central Bank has fewer tools available to constrain monetary conditions. This puts much more onus on fiscal policy to constrain spending and tax expenditures to levels that are sustainable from the underlying growth of the economy.

5.2 Ireland failed this test of prudent fiscal management. One could have hoped for a relatively soft landing of the domestic economy in the absence of unanticipated global upheaval and domestic bank failures. But fiscal management should provide greater capacity to manage such unanticipated outcomes.

5.3 The country does not need this report to recognize this failure. But in recovery from its current circumstance, the country must constrain its ambitions for Government supports to sustainable levels.

5.4 We believe that Government must substantially improve budgetary processes, enhance ministerial accountability to parliament and publicly release substantially more departmental analysis for public consultation.

5.5 The Department needs to be more effective and needs to remake itself. This requires a series of changes of structure, professional capacity and internal working methods, together with a more outward looking attitude. These issues need to be addressed urgently.

5.6 Our hope is that the recommendations in this report will help the Department in this endeavour.

6. RECOMMENDATIONS

Budgetary and Other Processes:

1) *After Cabinet review of Budget strategy in June, and consistent with its April submission to the European Commission, the Government should release for public and parliamentary review:*

   - *the Department's economic and fiscal forecast,*
   - *the Department's assessment of the economic and fiscal risks to this outlook,*
   - *related sectoral analysis by the Department and*
   - *the Government's proposed quantum for fiscal action in new spending and tax expenditures.*

   The Minister and the Department should consult widely on this framework, particularly with the relevant Oireachtas Committee.

2) *Departments would not seek spending enhancements beyond the spring consultations leading to the Budget review at Cabinet.*
3) *To the extent that November tax results surprised to the upside, such revenue should be used for debt reduction, not new spending or tax relief.*
4) *The Panel supports the establishment of a Fiscal Council to review and publish commentary on the Department's analysis and the Government's proposed quantum for fiscal action. The Panel believes that such a Fiscal Council must be independent of Government, have qualified membership, a straight forward role and the ability to report in a timely manner. For example, following a June release of the Government's fiscal plan, the Fiscal Council could review:*

   - *the Department's economic and fiscal outlook,*
   - *the Department's risk assessment,*
   - *whether the proposed fiscal framework, including provision for new Government budgetary action, entails acceptable risks for the economy.*

5) *To the extent the December Budget exceeds the quantum of action identified in June, the Fiscal Council should reassess the risks of these further actions for the economy.*
6) *The Fiscal Council could also usefully assess the impact of future Social Partnership wage and fiscal provisions on Ireland's economic competitiveness.*

Economic and Fiscal Forecasting:

7) *Forecasts in Budget Memoranda to Cabinet and for public consultations should include well articulated scenarios of alternative outcomes, consistent with the Department's risk analysis.*
8) *In addition, the Department should provide a public work-shop, with private sector and academic interests, once a year so that the assessment of the economic and fiscal challenges can be debated before the Department finalises its forecasts.*

Advice over the Budget Cycle:

9) *The Department of Finance should keep a written record of advice tendered and decisions taken as part of the budgetary process.*
10) *The Panel strongly supports the public release of substantially more economic analysis by the Department. However, policy advice to the Minister for Finance in the preparation of the Government's Budget should not be subject to release under Freedom of Information for at least five years.*

Macro-economic Risks:

11) *The Panel recommends that the Department prepare comprehensive macroeconomic risk assessment for Ireland as part of its annual advice to Cabinet.*
12) *The Department should establish sufficient formal arrangements with the Central Bank, including its Financial Regulation function, the NTMA and NAMA and establish sufficient technical capacity internally to manage this process.*

13) *The Government should introduce legislation to establish a coordinating committee of these financial agencies, chaired by the Secretary General of the Department of Finance, which would require the full exchange of any information that could entail fiscal or economic risks to the country, among the above agencies.*

Construction Policy:

14) *The Department should include sectoral assessments in its annual economic analysis and forecast that is released for public consultation.*

Tax Policy Advice:

15) *The Department should substantially increase its analytical capacity in the tax policy area.*
16) *The Department should organise itself to consult with tax and financial experts and prepare advice that is most appropriate to an efficient tax regime for Ireland.*

Medium Term Analysis:

17) *The Government should commit to the preparation of regular medium- term economic plans for Ireland at least every five years.*

Department's Interface with Other Departments:

18) *The Department should integrate those sections of Public Service Management and Development Division dealing with administrative budgets into Sectoral Policy Division to create a "single window" interface with line Departments.*

19) *Activities could be organised immediately under the Assistant Secretary level in the Sectoral Policy Division. The longer-term objective should be to establish Principal positions responsible for the interface of all activities with outside Departments.*

Public Service Management and Development:

20) *Public Service Management and Development Division should be established as a separate entity, either as an entirely separate Department or reporting directly to the Minister of State for Public Service Modernisation.*
21) *The Secretary General of the Department of Finance and Minister for Finance should retain authority over the overall wage bill, negotiating mandates for new collective bargaining processes and manage a single window on departmental control functions.*

Public Service Modernisation:

22) *The Panel strongly supports the creation of a Private Sector Advisory Board which it understands is under consideration by the Departments of the Taoiseach and Finance.*
23) *A full-time Task Force should be established and assigned responsibility for driving forward the reforms under the Croke Park Agreement.*
24) *The Task Force would comprise existing staff from the Modernisation Unit of the Department. The Task Force would also include key individuals from the leading Departments along with expertise in the area of change management on secondment from the private sector.*
25) *The Task Force's Team leader should have direct access to the Minister of State responsible for Public Service Modernisation.*
26) *In addition, there is a need to recruit expertise in the areas of change management and business process re-engineering.*

Core Finance Functions:

27) *With the possible exception of the Public Service Management and Development Division, no other core functions should be moved out of the Department of Finance.*

Structure:

28) *Assistant Secretaries should report directly to the Secretary General of Finance.*
29) *Second Secretaries should cease to have divisional line management responsibilities, but should be able to call upon resources across the Department as and when necessary.*
30) *The Second Secretary currently responsible for Sectoral Policy Division should be designated as Chief Operating Officer for the Department. The function of this post would be to lead the co-ordination across the Department of major issues, for example, to lead the interaction between the Budget and expenditure sides of the Department, and otherwise to help ensure the entire Department is connected to key policy and management issues.*
31) *The Second Secretary post leading the Budget, Tax and Economic Division could focus primarily on the increasingly important role of interacting with the institutions of the European Union and other international institutions.*
32) *The Second Secretary responsible for Financial Services should retain responsibility for this function until such time as the banking crisis is considered to have abated sufficiently. At that time the post should be abolished. That Second Secretary could draw on the support of the Assistant Secretaries currently in that Division as necessary, but they would report directly to the Secretary General.*

Management Advisory Committee (MAC):

33) *The remit of the MAC should be broadened to include discussion of major strategic challenges confronting the Department.*
34) *All those that report to the Secretary General should attend MAC meetings. Given the pace of change underway, MAC meetings could usefully include a brief report by Assistant Secretaries on key issues in their area, where appropriate, as well as Secretary General and Second Secretary reports on high level issues.*
35) *Attendees at MAC should, as a matter of course, brief their own direct reports on outcomes from these meetings.*
36) *The MAC should meet more often at Budget time and during periods of major change to enhance internal communication and connect all employees to emerging issues. It should schedule regular meetings on key policy issues.*

Corporate Secretariat:

37) *A Corporate Affairs Unit, which should be headed by a Principal who would report directly to the Secretary General, should be established. It would bring together and enhance a number of functions which are located in different areas of the Department. The functions of the Unit would be to:*

    - *manage the interface with the Minister's Office;*
    - *co-ordinate briefs and draft speeches for the Minister to ensure consistency and quality;*
    - *help ensure effective internal communications;*
    - *manage departmental outreach and the Department's profile;*
    - *co-ordinate, on a regular basis, the preparation of a brief for MAC on all major live issues and an early warning on significant emerging issues;*
    - *help co-ordinate major departmental initiatives;*
    - *co-ordinate departmental strategy statements;*
    - *manage the activities of the Department's Press Office; and*
    - *manage the Freedom of Information function in the Department.*

Structure at the Working Level

38) *The Department should examine working level structures and the devolution of responsibilities to ensure the delegation of more responsibilities to middle management levels and to create larger teams throughout the organisation.*

Enhancing the Department's technical skills:

39) *Even in this period of restraint, the Department must find a way to increase substantially the numbers of economists and other staff with relevant technical qualifications.*
40) *The Department should double the number of economists, appointed through open, public competition and trained to Masters level or higher, over the next two years. These appointees should comprise a mix of recent university graduates and experienced individuals and be assigned to positions throughout the organisation. The Department should organise itself to maintain a regular inflow of new university recruits.*
41) *The Department should work to establish a welcoming professional environment for new economists. Economists at Masters level and above should be identified and their numbers reported on annually; a champion for establishing and promoting this "community of interest" should be named.*
42) *The economic seminars by external economists, which were recently introduced by the Secretary General, should be made permanent; the Department should permit the publication of professional economic analyses, by staff in the Department, that are clearly identified as not the views of the Department.*
43) *The Department should expand its complement of skilled staff in other disciplines, especially accounting, analysis, banking and financial markets.*
44) *The Department should immediately seek the secondment of skilled personnel on a two-year rotation from the Central Bank, NTMA, ESRI and other relevant bodies.*
45) *The Department should also promote exchange agreements with other Finance Departments internationally.*

Enhanced HR function:

46) *A senior HR specialist should be appointed to the Department initially, at any rate, on a short-term contract. The post would be advertised and preference would be given to an individual who had managed a dynamic HR function in the private sector.*
47) *The Department should reinforce its performance review process and require the identification of under-performance and an individualised plan to deal with problems identified.*
48) *Once each year, the MAC should take a full day to review individual performance in the Department. It should identify, of all supervisors, the top 20% on people management – those who recognise high performance and deal with poor performance. This process should also identify the bottom 20% - those supervisors who are not performing well in this area and those who are not taking a proactive approach to this issue. Plans to address under-performance should be required. A supervisor's performance in "people management" should have a material impact on consideration for promotion.*

Change Management:

49) *The Secretary General should present a Change Management Plan to employees and report on progress in an annual accountability session to all staff.*
50) *He should be supported by all managers, by a champion for change management at Assistant Secretary level and by the newly recruited professional HR specialist.*

APPENDIX 1

Terms of Reference of the Review

The Independent Review Group will undertake a comprehensive evaluation of the systems, structures and processes of the Department of Finance relating to those elements of budgetary, economic, financial and public service management that are relevant to its role.

In this regard the review will assess the Department's

- Performance in the past 10 years,
- Advice (appropriateness and quality), forecasts, risk analysis (including of non-consensual opinion) and communications strategy, and,
- Development and management of responses to the current crisis.

This assessment should have regard to the policy, legal and institutional framework within which the Department worked during this period.

The Group will, based on the conclusions and lessons drawn from this assessment, make recommendations for the future development, structure and resourcing of the Department.

In making its recommendations the Group will have regard to best practice regarding the organisational structures, skills, training, staff mix and levels required by a modern Finance Ministry in order that it can best fulfil its role in relation to (i) economic and financial management; (ii) policy analysis, development, advice and implementation; and, (iii) communication, transparency and accountability.

The Group will provide its full report and recommendations within three months.

APPENDIX 2

Membership of the Panel

Mr Rob Wright is Chairman of the Group. He has 35 years of economic policy and management experience in the Public Service of Canada, over twenty years of which was at the Deputy Minister (Secretary General) level, most recently as Deputy Minister of Finance.

Mr Hans Borstlap, was Director-General at the Ministry for Social Affairs and Employment and for many years a member of the Central Economic Commission. He was the first Chairman of the Employment and Labour Market Committee of the EU. He is currently a member of the Council of State and provides advice to the Government on the annual Budget in this role.

Mr John Malone is a former Secretary General of the Department of Agriculture and Food.

Mr Pat McArdle is an economist and provided support and assistance to the Panel.

APPENDIX 3

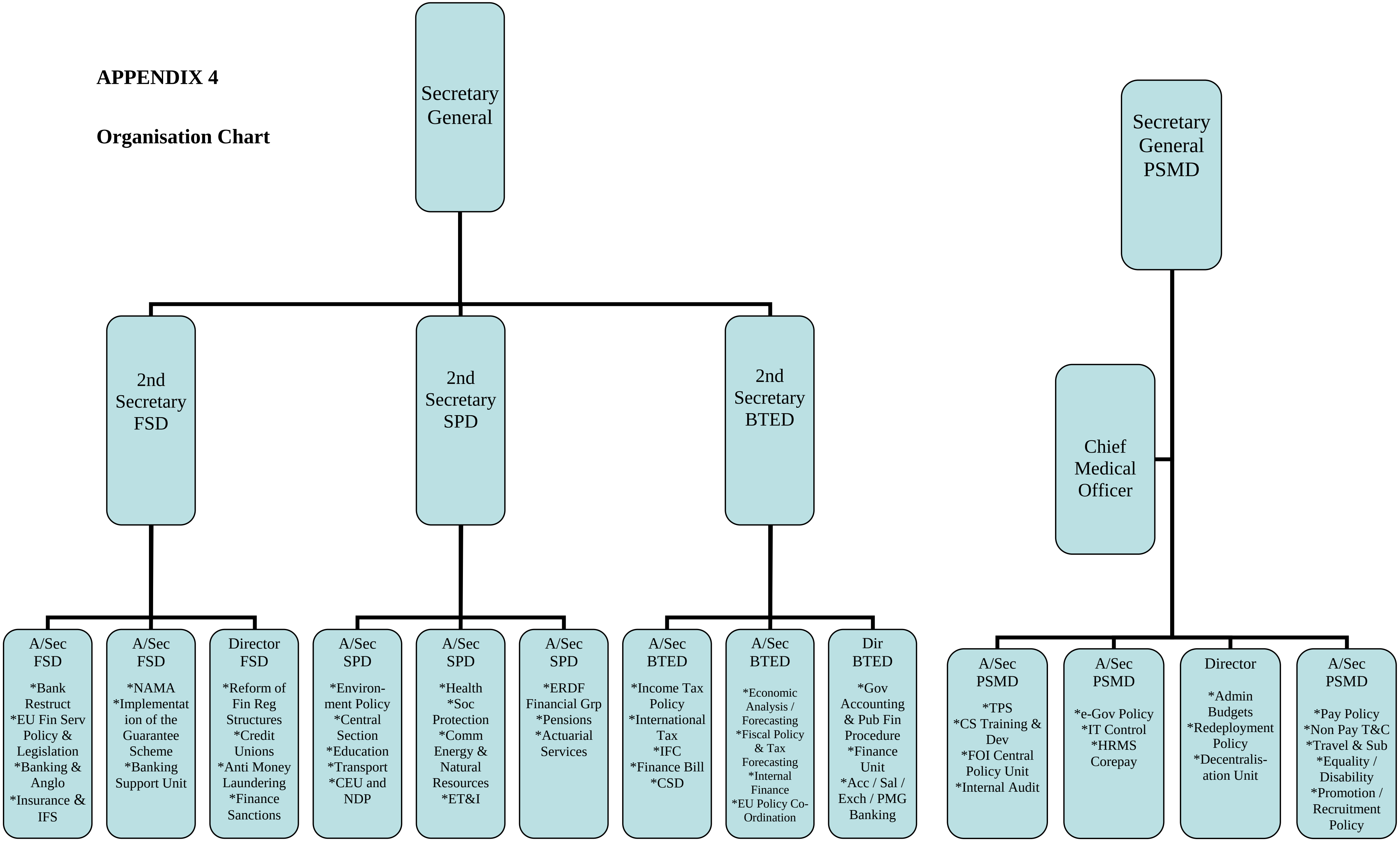
Submissions received in <u>Review@finance.ir</u> Mailbox

The call for submissions published in the Irish Times and Irish Independent asked that submissions be sent to the review@finance.ie mailbox by Friday, 15th October. However, submissions received after that date were considered by the Review Panel

	Date received	**From**	**Organisation**
1	13 September 2010	Mr. Peter Duffy	Individual Capacity
2	1 October 2010	Mr. Peter Stafford	Society of Chartered Surveyors
3	10 October 2010	Mr. Robert Pye	Individual Capacity
4	14 October 2010	Deputy Joan Burton	Labour Party
5	15 October 2010	Fr. Seán Healy	Social Justice Ireland
6	15 October 2010	Mr. Martin Newell	Individual Capacity
7	15 October 2010	Mr. Gerry Murray	Individual Capacity
8	15 October 2010	Mr. Donal Ó Brolcáin	Individual Capacity
9	17 October 2010	Mr. Edmund Honohan	Individual Capacity
10	21 October 2010	Mr. Myles Duffy	Individual Capacity
11	22 October 2010	Mr Dónal de Buitléir	Individual Capacity
12	15 November 2010	Mr. Stephen Boyd	Impact Professional Accountants Branch

APPENDIX 4

Organisation Chart



APPENDIX 5

Divisional Responsibilities in the Department of Finance

Budget, Taxation and Economic Division is headed up by a Second Secretary General. The work of the division can be divided into three broad areas: Budget and Economic Policy Area, Tax Policy Area and the Finance Directorate:

i. The core focus of the Budget and Economic Policy Area of this Division is to provide macro- economic and fiscal analysis and policy advice to the Minister and Government on domestic and international developments. A central part of the work of this area is the regular production of macroeconomic and fiscal forecasts, interpretation and analysis of economic and tax trends, debt sustainability and provision of economic and budgetary commentary and advice on a variety of macro-issues as required to senior management/Minister as well as the Taoiseach and other Government members. In this regard the annual budget represents a key outcome. The Unit has a central role in the work of the Department and plays a significant part in driving the policy agenda along with other key stakeholders. There is a significant international aspect to its work, mainly through EU, OECD and IMF obligations. Much of this is through attendance at various international Councils, Committees, Working Groups and other meetings. Engagement with various other international bodies such as the EIB/EBRD/World Bank/Asian Development Bank and Council of Europe, briefing visiting foreign delegations and Rating Agencies are also a key part of the workload. The formulation and delivery of the Department's policy advice in relation to economic and fiscal matters that arise in relation to meetings of the Economic and Financial Affairs Council (Ecofin) and the Eurogroup is also a key responsibility of this area.

ii. The role of the Tax area is to develop, innovate and manage the tax policy input to the Budget and to provide detailed policy proposals for the Finance Bill. The strategic tax policy objective is to have an efficient, balanced and equitable taxation system that provides economic and social progress while generating the resources necessary to fund public services. There is a significant EU and international dimension to the work which both defends Irish interests and promotes understanding and confidence in Irish tax policy. These functions are delivered with the support of the Revenue

Commissioners. There is a very close and effective working relationship between the Department and the Revenue Commissioners with mutual recognition of the distinctive roles assigned to each organisation.

The Finance Directorate has responsibility for Government Accounting, Accounts/ Exchequer/ Pay Master General (PMG) Banking and Salaries/ PMG Pensions. The objectives of the Directorate are to promote best practice in public financial procedures and Government Accounting and to ensure that ongoing and annual aggregate outputs are timely and accurate. These include: payroll for employees and pensioners, transfers in support of departmental payment systems, clearance of payable orders within two days, payments to suppliers and programme beneficiaries, Exchequer Statements, Appropriation Accounts, Finance Accounts, various Fund Accounts and liaison with the PAC. The Finance Unit is responsible for the Annual Estimates process and Financial Management in respect of the Department itself.

Financial Services Division is headed by a Second Secretary General. This Division is responsible, working closely together with the Central Bank, including its Financial Regulatory function, and the NTMA for advising the Minister and Government on strategy for addressing the domestic impact of the global financial turmoil. It also has overall responsibility for the legislative and policy framework for financial services and financial regulation in Ireland. The Division's key objectives currently include securing the objectives of the Banking Guarantee Scheme and those of the Government's Recapitalisation Programme. There is a very strong EU and international dimension to the Division's work. Financial regulation in Ireland is largely based on a detailed and comprehensive EU-wide template. Consequently, a particular priority for the Department is to seek to ensure that the evolution of EU financial services policy is aligned with national goals and objectives. In that context, a particular focus of attention is the proposed reform of EU financial regulation and supervision and a range of EU financial services initiatives introduced in response to the international financial crisis. The Division is also responsible for supporting the appropriate development of international financial services in Ireland which have been a major contributor to growth and employment.

Sectoral Policy Division (SPD) is under a Second Secretary General. This division is responsible for formulating and promoting sectoral policies and expenditure allocations which support and promote the Government's economic, social and environmental objectives, in conjunction with spending departments. This involves:

- monitoring public expenditure,
- developing and evaluating sectoral policy issues,
- contributing to the development of a Department-wide approach to climate change policies,
- promoting a VFM culture across Departments, through the work of the Central Expenditure Evaluation Unit (which has responsibility for the mid-term evaluation of the National Development Plan and for monitoring the spot checks that Departments are required to carry out on their own capital expenditure),
- taking a lead role in relation to EU structural funds,

co-ordinating and promoting a whole-of-Government view of pension policy across the economy: national pensions policy, Public Service pensions and civil service pensions. SPD plays a lead role in the areas of development and implementation of public pensions policy and civil service pensions administration, policy and disputes resolution.

Public Service Management Division (PSMD) is headed up by the Secretary General, Public Service Management and Development. It is sub-divided into three main areas:

i) Personnel and Remuneration (P&R): this area is responsible for pay policy and IR issues across the Public Service. P&R also has responsibility for conditions of service in the civil service, including recruitment, promotion and equality as well as for the Public Service decentralisation programme. P&R is also responsible for the management of staffing levels and administrative budgets in the civil service in line with government policy and for redeployment issues.

ii) Public Service Development (PSD) deals with modernisation issues across the Public Service, Civil Service organisational issues, staff training and development, ethics, Freedom of Information, and relations with the Ombudsman. It supports the work of the Minister of State and Cabinet Committee on Transforming Public Services and works with other divisions of the Department, notably Personnel & Remuneration Division (PRD), the Centre for Management, Organisation & Development (CMOD) and Sectoral Policy Division (SPD) on the implementation by the Department of

Finance of key elements of the Transformation agenda, HR policy, eGovernment and the application of information technology, performance budgeting, public procurement, the reform of State agencies and the implementation of the *Public Service Agreement 2010-2014*. It is responsible for the development of shared services initiatives and business process re-engineering in the Public Service.

iii) Centre for Management and Organisation Development (CMOD): the role of CMOD is to provide advice and assistance to public bodies in relation to technology issues, to assess and approve proposals for ICT expenditure from public bodies, to monitor progress of significant ICT projects, to undertake national procurement on behalf of public bodies and to manage shared multi-supplier framework contracts for hardware and telecommunications, to provide shared ICT services such as Government Networks, a shared HR Management System and common payroll software for the civil service, to manage the development of eGovernment policy, to provide central eGovernment services, event publication systems for public bodies etc. and to provide internal ICT services for the Department of Finance.

Corporate Services Division (CSD): CSD provides support for the activities of the Department in the areas of staff provision, welfare, management and training, accommodation and also a range of departmental functions which are serviced or co-ordinated centrally. The Division reports to the Secretary General, Public Service Management and Development.

APPENDIX 6

Summary of International Reports on the Irish Economy

The reports summarised below are from three sources: the European Commission (EC), the IMF and the OECD. This Appendix is structured as follows. First, the conclusions of the EC's recommendations to the Council on the Irish stability programmes from 1999 to 2010 are summarised. Second, the OECD's economic surveys of 2003, 2006 and 2008 (these are published roughly every two and a half years) are summarised. Finally, the Executive Directors' conclusions from the bilateral article IV consultations procedure of the IMF are summarised.

EC Reports

1. EC recommendation to Council of 12 January 1999:
    i. budget projections for 1999-2001 were realistic and in line with the Stability and Growth Pact (SGP);
    ii. the expected decrease of the debt ratio from 60% in 1998 to 43% by 2001 was welcomed;
    iii. the authorities were warned that the favourable economic situation was not without risks, in particular from rising wages and inflationary pressures;
    iv. a tighter fiscal policy would help contain these pressures;
    v. welcomed the planned increase in public investment to meet infrastructural needs and to replace EU structural funds.
2. EC recommendation to Council of 18 January 2000:
    - roughly the same as a year before.
3. EC recommendation to Council of 24 January 2001:
    i. an official warning was given under article 99.4 of the Treaty, as fiscal policies were not in line with the 2000 Broad Economic Policy Guidelines (BEPG);
    ii. the expansionary nature of the 2001 Budget constituted a major risk;
    iii. the direct and indirect tax cuts and very large increases in current and capital expenditure would worsen the overheating problem;
    iv. the fiscal loosening planned for 2001 was inappropriate for an economy operating above potential – GDP was forecast to grow by nearly nine percent.

4. EC recommendation to Council of 30 January 2002:
   i. concerns were expressed that the previous budgetary strategy of maintaining high surpluses and further reducing the debt ratio, which had been endorsed by the Council, were no longer being followed;
   ii. the fiscal targets implied that Ireland could cease to comply with the "close to balance" requirements of the SGP by 2003 but would still avoid breaching the 3 percent of GDP threshold;
   iii. regretted that the new update did not present any plans to introduce a medium-term framework to guide public spending or to improve expenditure control as requested in the BEPGs agreed for 2001;
   iv. noted with satisfaction the broad-based strategy to prepare for ageing population;
   v. warned that recent rates of increase in current and capital spending, motivated by a desire to tackle infrastructural needs and public sector deficiencies, could not be sustained without action on the revenue side.
5. EC recommendation to Council of 30 January 2003:
   i. although the 2002 budget was judged to be expansionary, in the event, policy was expected to be neutral in 2003 as a result of (1) a cut in capital expenditures, (2) a marked reduction in the growth rate of current expenditures and (3) an overall stabilisation of the tax burden;
   ii. the targets in the programme respected the safety margin against breaching the 3% of GDP threshold for the deficit ratio;
   iii. although Ireland was in a relatively good position considering its low debt level and gradual build-up of assets in the National Pensions Reserve Fund, the deficit position envisaged for 2005 did not seem to be ambitious enough.
6. EC recommendation to Council of 28 January 2004:
   i. while there was little or no improvement in the budgetary position between 2004 and 2006, Ireland was on a sustainable path with some long-term risks;
   ii. future age-related spending might become a problem, although the debt ratio was quite low and there was a gradual build-up of assets in the National Pensions Reserve Fund;
   iii. commended the Irish authorities for the extension of multi-annual budgeting system to all capital spending.
7. EC recommendation to Council of 2 February 2005:

i. the macroeconomic scenario appeared plausible;
ii. the budgetary stance seemed to be sufficient to maintain the SGP's medium-term objective of being close to balance or in surplus;
iii. the risks attached to budgetary projections appeared broadly balanced as forecast receipts seemed plausible, contingency provisions were quite high, and Ireland had made encouraging progress in adhering to expenditure targets;
iv. Ireland appeared to be in a relatively favourable position with regard to the long-term sustainability of its public finances with low debt ratios and accumulating reserves in the pension fund;
v. overall, economic policies were in line with 2003-2005 BEPG.

8. EC recommendation to Council of 22 February 2006:
   i. budgetary position was sound and the budgetary strategy provided a good example of fiscal policies in compliance with the SGP;
   ii. the EC invited Ireland to continue to implement measures to address the long-term budgetary implications of an ageing population.
9. EC recommendation of 7 February 2007:
   i. medium-term budgetary position was sound and, provided the fiscal stance in 2007 did not prove to be pro-cyclical, the budgetary strategy provided a good example of fiscal policies conducted in compliance with the SGP;
   ii. it would be prudent to maintain room for manoeuvre against any reversal of the current growth pattern which had been led by strong housing sector developments;
   iii. Ireland was invited to continue to implement measures to improve the long-term sustainability of its public finances.
10. EC recommendation of 19 February 2008:
   i. Ireland was facing several macroeconomic challenges in its transition to a period of lower economic growth (mainly the return to more sustainable activity in the housing sector);
   ii. slowing domestic demand had been accompanied by losses in recent years in export market shares as a result of price competitiveness challenges;
   iii. a notable deterioration of the fiscal position to a deficit over the period 2007-2008 was envisaged;

iv. the risks attached to the budgetary projections were broadly neutral in 2008, but, from 2009 onwards, outcomes could be worse than projected due to insufficient expenditure containment;

v. as the public debt was low, Ireland was at medium risk because of the projected impact of population ageing on pension expenditure;

vi. Ireland was invited to keep firm control over expenditures and to implement further pension reforms to improve long-term sustainability of public finances.

11. EC recommendation to Council of 18 February 2009:

i. following a very sharp deterioration in 2008, the general government deficit would widen further in 2009, to 9.5% of GDP;

ii. measures adopted in response to the economic downturn were welcome and adequate given the high deficit and sharply increasing debt position and were in line with the European Economic Recovery Plan;

iii. a reduction of the deficit was envisaged to below 3% of GDP by 2013, while debt would breach the 60% reference value from 2010;

iv. budgetary outcomes were subject to downside risks mainly due to lack of information on the envisaged consolidation measures after 2009 and the optimistic macroeconomic outlook especially in later years;

v. further risks resulted from measures to support the financial sector (bank guarantees, possibility of further capital injections or nationalisations of banks);

vi. Ireland was invited to (1) limit the widening of the deficit and rigorously implement a substantial broadly-based fiscal consolidation in 2010 and beyond; (2) strengthen the medium-term budgetary framework as well as closely monitor adherence to the budgetary targets; and (3) improve long-term sustainability of public finances by implementing further pension reform measures in addition to pursuing fiscal consolidation.

12. EC recommendation to Council of 22 April 2010:

i. regarded Ireland's response to counter the widening of the government deficit as swift and determined;

ii. General Government Deficit was expected to stabilise in 2010 at 11.6% of GDP and a back-loaded reduction was envisaged to below the 3% of GDP reference value by 2014;

iii. the budgetary outcomes could be worse than targeted mainly due to (1) lack of specifics on post-2010 consolidation efforts (2) the forecast favourable macroeconomic outlook after 2010 and (3) the risk of expenditure overruns in 2010 and beyond to the extent that the still to be spelled out strategy should rely on expenditure restraint;

iv. although the size of the 2010 savings package was broadly in line with the Council recommendation of 2 Dec 2009, it would be important to address the risks identified by spelling out the measures underlying the consolidation strategy and adopting additional measures if growth disappointed or spending slipped;

v. there was a need to regain competitiveness through measures enhancing productivity growth and adequate wage policies, and to support the re- and up-skilling of the newly unemployed to prevent them from turning into long-term unemployed;

vi. further reforms to the pension system were important to improve the long-term sustainability of the public finances;

vii. Ireland was invited to (1) implement rigorously the Budget for 2010 and back up the envisaged consolidation packages for the following years with concrete measures, while standing ready to adopt further consolidation measures should this prove necessary, (2) improve the long-term sustainability of public finances by implementing further pension reform measures, (3) limit risks to the adjustment, strengthen the enforceable nature of its medium-term budgetary framework as well as closely monitor adherence to the budgetary targets throughout the year.

OECD reports:

1. 2003 Economic Survey conclusions:
   a. the 2001 economic slowdown in Ireland was closely linked to the bursting of the ICT bubble, but also reflected a deterioration in Irish cost competitiveness due to strong inflation in the sheltered sector of the economy, reflecting the combined influence of large wage gains emanating from the tradable sector, low productivity growth in the sheltered sector and the generally expansionary effects of very low real interest rates since Ireland joined the EMU;

b. the policy challenge in the short term was to ensure that both income expectations and public finances adjusted to a slower growth environment, so as to safeguard against deterioration in international competitiveness and ensure fiscal sustainability and the maintenance of a growth-supportive tax environment;
c. over a longer term, the broad aim of the authorities should be to ensure that the economy continued to grow at a reasonably high rate and policies should be more clearly oriented towards protecting the interests of consumers rather than producers;
d. although GDP growth remained high at 6% in 2002, GNP growth was significantly lower (2%), since much of the growth accrued to foreign owners in the biomedical and pharmaceutical sectors;
e. the economy had lost momentum since late 2002 with a further slowdown in exports and a substantial weakening in business confidence;
f. demand for labour had slackened, leading to a rise in the unemployment rate;
g. a weak trend was expected to prevail in 2003, but was forecast to give way to modest acceleration in 2004 on the assumed recovery in export markets. Construction activities were likely to remain a major source of buoyancy due to rapid development of the physical infrastructure and continuing strong demand for housing;
h. while the 2001 and 2002 Budgets had substantially overestimated revenues and underestimated spending pressures, the 2003 budget seemed to be more consistent with slower underlying growth in the tax base: it relied on increased taxation and allowed for a smaller increase in spending that was allocated selectively to priority areas.

2. 2006 Economic Survey conclusions:
    a. as one of OECD's most open economies, Ireland was particularly exposed to external risks (declining exports and FDI);
    b. domestic risks were important too, of which the most prominent was the risk of overshooting housing prices. Although a soft landing was considered the most likely scenario, a sharper fall could not be ruled out;
    c. the Irish Government should balance its Budget or even run a surplus, curtail tax breaks (especially in the housing sector) and push ahead with public management reforms to get better value for money from public expenditure;

    d. to prepare better for negative fiscal shocks the authorities should adopt a more top-down budgeting approach to help expenditure planning and control.

3. 2008 Economic Survey conclusions:
    a. economic fundamentals remained strong;
    b. in the short run, wage restraint and labour market flexibility were important to continue to attract FDI and to encourage foreign demand to offset the slowing down of domestic activity;
    c. in the longer run, stronger productivity growth, and continued increases in participation rates, would be needed to sustain a fast pace of real income growth;
    d. easing of activity had led to a slowdown in Government revenues and a sharp drop in the fiscal surplus; at the same time Government was committed to a large infrastructure investment programme and there was a strong demand for better public services;
    e. public finances faced serious pressures from the ageing of the population in the long run;
    f. Ireland was sensitive to weak US and UK demand for its exports and to lower FDI flows;
    g. although Irish finances were in a relatively good position as the country had achieved high growth rates in the past decade and a half, debt had diminished and the reserves in the pension fund had increased, public spending could increase and revenue growth had slowed down; therefore the Irish should commit to a more balanced fiscal policy.

IMF reports

1. 2000 Article IV Consultation conclusions:
    a. Commended the authorities for the performance of the economy over the past decade;
    b. signs of overheating had become more pronounced (rapid price increases in non-tradables, labour shortages, physical bottlenecks, rising property prices and rapidly growing private sector credit);
    c. expressed concern that rapid inflation could cause the social consensus underlying the wage agreement to erode and could lead to a difficult adjustment later, if the euro were to appreciate;
    d. increasing public investments in infrastructure, tax reforms to improve labour participation and deregulation and privatization to foster competition were needed while a tighter fiscal policy would help dampen excess demand;
    e. Directors called on the authorities to resist tax reductions above those in the national wage agreement;
    f. the planned benchmarking exercise was welcome although this should not come at the expense of overall public sector wage restraint;
    g. although Ireland had a sound and highly developed financial system, risks to financial sector stability could arise from rapid lending growth, in particular related to the domestic property boom;
    h. Directors expressed their concern that, after several years of rapid property price increases, housing demand might increasingly be driven by expectations of further price increases, a trend that could be abruptly reversed.
2. 2001 Article IV Consultations conclusions:
    a. Directors commended the authorities for Ireland's outstanding economic performance;
    b. the economic outlook remained broadly favourable, but authorities faced a number of challenges as growth adjusted to a lower, more sustainable, trajectory;
    c. the deterioration in the global outlook (especially for the technology sector) posed considerable downside risks;

d. Directors stressed the difficulty of managing a counter-cyclical fiscal policy in a small open economy and considered that the authorities should aim for a neutral policy in 2002;
e. Directors welcomed the efforts to improve the tax structure;
f. a number of structural reforms were considered desirable to help secure continued vigorous growth over the medium term:
    i. wage reforms, private sector wages should be market-determined and public sector wages aligned with those in comparable private sector jobs;
    ii. strengthening competition through privatization and deregulation;
g. Directors called for further progress to improve the coverage and timeliness of data necessary to monitor short-term developments.

3. 2002 Article IV Consultations conclusions:
    a. again commended the authorities for the impressive economic performance;
    b. the Irish economy appeared to have weathered the global slowdown relatively well;
    c. the economic outlook was broadly favourable;
    d. continued appreciation of the euro, combined with relatively high inflation and labour costs could adversely affect Ireland's competitiveness and strength of recovery; these factors could also pose a risk – albeit likely to be a manageable one – to the financial sector;
    e. Directors expressed concern about the sharp deterioration in the structural fiscal balance in 2001, but agreed that measures to unwind the stimulus for 2002 were not advisable at that time;
    f. the fiscal position for 2003 should, at a minimum, be kept neutral;
    g. capitalization of the banking system appeared to provide an adequate cushion against possible risks to asset quality, but supervisory authorities should ensure that capital and provisions remained adequate in the event of a deterioration in unemployment, company finances or property prices.

4. 2003 Article IV Consultations conclusions:
    a. Directors commended the Irish authorities for their exemplary track record of sound economic policies, but saw signs of sustained slower growth in the period ahead calling for a sharper policy focus on reducing inflation and improving competitiveness;

b. Directors noted that there was a significant risk that house prices could be overvalued, although financial sector risks appeared to be manageable;
c. Directors stressed the need for continued supervisory vigilance to ensure stability of the financial system;
d. While high levels of capitalisation and profitability had strengthened bank balance sheets, credit risks related to investor-owned housing properties, concentration of commercial property exposure among a few institutions and the health of the insurance industry merited close attention;
e. Directors emphasized the need of wage growth moderation in order to preserve external competitiveness and to avoid risks to employment;
f. Directors welcomed the somewhat contractionary fiscal stance envisaged for 2003, stressed that spending should be held to budgeted levels and that any revenue shortfalls be offset by restraint with respect to the wage bill and transfers, whereas capital spending should be protected;
g. Directors agreed that the authorities' medium-term fiscal target of overall structural balance was appropriate, but the authorities should not rely on continued strong output growth to eliminate the deficit.

5. 2004 Article IV Consultations conclusions:
   a. again commended Ireland's impressive performance which was based on sound economic policies providing useful lessons for other countries;
   b. economic recovery was expected to become stronger and broad-based in the short term, supported by external demand and a continued rebound in business investment;
   c. core inflation was expected to remain moderate;
   d. the main risks to this outlook stemmed from the potential for further euro appreciation and the possibility of an abrupt unwinding of the housing boom;
   e. in the medium term, Directors expected growth to be markedly lower, as many of the factors that accounted for the 1990s boom were one-off in nature;
   f. growth would still remain high by international standards;
   g. the transition to slower growth would require adjustments in expectations in labour and housing markets and also in fiscal policy;
   h. although inflation had decelerated –suggesting that expectations had adjusted to lower growth – the level of competitiveness had deteriorated;

i. Directors called for an extended period of wage restraint as well as increased wage flexibility within the social partnership;
j. while an abrupt unwinding of the housing boom was unlikely to cause concern about financial stability, the impact on employment and consumer spending could be significant;
k. many Directors warned against providing additional incentives in the form of subsidies to home ownership and urged the removal of interest-deductibility of mortgage payments on primary dwellings, as well as the introduction of a wealth tax on property;
l. although the overall outturn for 2003 and early returns in 2004 were better than expected, Directors noted that this performance was in part due to one-off factors.

6. 2005 Article IV Consultations conclusions:
    a. commended Ireland's continued impressive economic performance;
    b. Directors concluded that economic growth was expected to be strong in the short term, driven by an acceleration of consumption and continued robust business investment;
    c. with a gradual cooling of the housing market, residential investment would likely decline modestly starting in the following year;
    d. the main risks to the outlook were considered to be: (1) a further rise in oil prices, (2) an abrupt slowdown in global economic growth, (3) a sharp decline in the housing market and (4) rapid growth of aggregate demand giving rise to wage pressures, thereby undermining external competitiveness;
    e. Directors noted that the 2005 Budget imparted a considerable fiscal stimulus while euro area monetary policy was very accommodative for Ireland;
    f. Directors underscored the importance of building a fiscal cushion in good times, in the event of downside risks materialising;
    g. the conduct of Ireland's fiscal policy had been laudable over the years and, while an enhanced public debate could help, any Directors did not see a case for a fiscal council.

7. 2006 Article IV Consultations conclusions:
    a. Ireland was again commended though growth had become increasingly unbalanced;

b. Directors expected economic growth in 2006-07 to remain strong, driven by domestic demand and accompanied by a widening current account deficit and continued rapid credit growth;
c. while the contraction of the construction sector to a more sustainable size over the medium term was likely to be smooth, Directors noted that an abrupt correction could not be ruled out;
d. while recognizing that Ireland's fiscal position was sound, most Directors considered that a modest fiscal tightening would be desirable in 2007, given the strength of domestic demand, potential risks of a hard-landing and the need to prepare for population ageing, although a number of Directors saw less merit in fiscal tightening at that juncture, pointing to the need for further spending to achieve social goals and the recent tightening of euro area monetary policy;
e. Directors considered that continued wage moderation and labour market flexibility were essential to support competitiveness and broadly welcomed the new social partnership agreement.

8. 2007 Article IV Consultations conclusions:
   a. commended Ireland's continued impressive economic performance, characterised by one of the highest growth rates of GNP per capita among advanced countries, underpinned by prudent fiscal policy, low taxes and labour market flexibility;
   b. Directors expected economic growth to remain robust over the medium term, but urged that careful attention be paid to of a number of downside risks: i.e. inflationary pressures, declining competitiveness, a widening of the current account deficit, a deterioration in global financial market conditions, the growth outlook of the US and the adjustment to a cooling of the housing market;
   c. while the slowdown of the housing sector had been gradual so far, a sharper correction in house prices could significantly slow economic growth;
   d. Ireland's medium-term fiscal discipline was commended, but many Directors saw the planned reduction in the 2007 fiscal surplus as an undesirable pro-cyclical fiscal stimulus;

e. Directors encouraged the authorities to restrain current expenditure growth and to continue to focus on improving the quality of public spending through cost-benefit analysis;
f. Directors concurred that Ireland was well-placed to meet the fiscal challenges of increasing age-related spending over the long term;
g. although Directors welcomed the indicators including stress tests that confirmed the soundness of the Irish banking system, financial sector vulnerabilities required continued supervisory vigilance;
h. Directors stressed that preserving and enhancing Ireland's external competitiveness through wage moderation would be key to underpinning future growth prospects.

9. 2009 Article IV Consultation conclusions:
    a. Directors noted that Ireland had been hit particularly hard by the global economic and financial crisis and that critical macroeconomic imbalances had emerged as credit supply accommodated an unsustainable rise in property prices;
    b. Directors commended the scale and speed of the authorities' response, while noting that such efforts needed to be sustained over an extended period of time;
    c. Directors supported the efforts to restructure the financial sector, including the decision to establish NAMA and urged risk-sharing in the pricing of distressed assets;
    d. Directors welcomed the fiscal measures already taken, including significant, and politically difficult, cuts in public sector wages.
10. 2010 Article IV Consultation conclusions:
    a. Directors considered that the authorities' decisive measures to support the banking sector and advance fiscal consolidation had helped gain policy credibility and stabilize the economy, and encouraged them to sustain these efforts;
    b. Directors noted that vulnerabilities remained high and required effective mechanisms for oversight and transparency to minimize risks and sustain market confidence;
    c. Directors concurred with staff's analysis that the speed of the recovery was likely to be moderate with relatively limited growth and high unemployment,

and noted in this context, that structural reforms aimed at regaining competitiveness and boosting potential output were necessary to put the recovery on a sustainable track;

d. Directors observed that a sizeable agenda remained to strengthen the banking sector;

e. Directors emphasized the need to strengthen the financial stability framework;

f. Directors underscored the importance of adhering to the further consolidation targets going forward and agreed that the consolidation plan would benefit from greater specificity;

g. Directors encouraged the authorities to move further towards a medium-term Budget framework and to adopt a fiscal rule and establish a fiscal council to advise on risks underlying public finances.