ICAEW
REPRESENTATION 16/25

SPENDING REVIEW 2025

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ICAEW welcomes the opportunity to submit written evidence to HM Treasury on Phase 2 of the Spending Review 2025.

We welcome three-year spending reviews updated every other year

- This is a positive improvement to the financial planning process.
- We also welcome four-year capital budgets and the ten-year infrastructure strategy

Key principles we believe should be adopted within the Spending Review

- Clarity on the government's wider strategic objectives beyond the five missions.
- Digital first.
- Upfront investment to deliver sustainable efficiency improvements.
- Core capital investment programmes to provide funding certainty.
- Local government finance reform.
- Prevention as a genuine priority.

Specific suggestions for Spending Review 2025

- Planning reform must be leveraged to reduce time to build (e.g., East West Rail).
- Subsidy-reliant services need more sustainable financial models.
- Higher level apprenticeships are essential to develop the skills the UK needs.
- Investment in HMRC processes and responsiveness is essential to unlocking growth.

Effective financial management is key to delivering savings and maximising growth

- A clear line of sight is needed between multi-year spending reviews, annual budgets, supply estimates, in-year performance monitoring and end-of-year annual financial reports.
- Increase delegations of authority to encourage innovation and ownership of outcomes.
- End the huge volatility in capital expenditure within and between financial years.
- A portfolio approach is needed to manage overruns and underspends to reduce waste.
- Fraud prevention and detection capabilities should be enhanced.

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INTRODUCTION

1. ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of sustainable economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports, and regulates more than 175,000 chartered accountant members in over 146 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical, and ethical standards.
2. This submission has been prepared by ICAEW's Public Sector team. We support members working in and with the public sector to deliver public priorities and sustainable public finances, including over 14,000 in ICAEW's Public Sector Community.
3. ICAEW engages with policy makers, public servants, and others to promote the need for effective financial management, audit and assurance, financial reporting and governance and ethics across the public sector to ensure public money is spent wisely.
4. We draw your attention to ICAEW's Autumn Budget 2024 submission where we call for a long-term fiscal strategy, a business tax roadmap, making the UK the green finance capital of the world, supporting the skills needed for growth, and making it easier to start and grow a business.
5. We would be very happy to discuss our feedback in more detail if HM Treasury believe that would be of assistance.
6. For questions on this response please contact us at representations@icaew.com quoting REP 16/25.

KEY POINTS

WE WELCOME THREE-YEAR SPENDING REVIEWS UPDATED EVERY OTHER YEAR

This is a positive improvement to the financial planning process

7. We welcome the introduction of three-year spending reviews that are updated every other year.
8. When originally introduced, multi-year spending reviews proved to be beneficial to the quality of financial planning and hence the effectiveness of public spending. By providing departments and public bodies with the ability to plan ahead with reasonable certainty on the funding that would be available in the subsequent financial year or years, they were able to obtain better value for money when allocating resources, in workforce decisions, and in entering contracts with suppliers.
9. Unfortunately, these benefits were not available in the last year of each spending review as there is a 'cliff edge' in visibility until the subsequent spending review is completed. This flaw in the design of spending reviews removed the benefits of multi-year spending reviews in those years.
10. Over the past decade this has been exacerbated by decisions to postpone spending reviews, extending the lack of forward visibility for a further year. As a consequence, departments and public bodies entered 2014/15, 2015/16, 2019/20, 2020/21, 2021/22 and 2024/25, and will enter 2025/26, without assurance of funding availability beyond the end of those individual financial years.
11. The introduction of three-year spending reviews combined with an update every other year should eliminate this flaw in the previous process by ensuring that departments and public bodies should never enter a financial year without reasonable forward visibility of at least two years (and three for capital) in the funding available to fulfil their missions.

We also welcome four-year capital budgets, and the ten-year infrastructure strategy

12. We are delighted to see that the government has agreed with suggestions made by ICAEW and others for a longer time-horizon for capital budgets. Infrastructure and other programmes can take many years to deliver, and so stable and reasonable funding certainty is therefore important to be able to plan and deliver such projects efficiently and effectively.
13. Furthermore, we believe that basing infrastructure investment decisions on a coherent longer-term strategy will help deliver stronger economic growth.
14. We would encourage HM Treasury and departments to use the benefit of a longer time horizon for capital budgets to accelerate the timescales of multi-year capital investment programmes. Forward budget visibility should make it easier to set firm dates for the delivery of new assets, avoid delays in decisions about moving to the next phase, and reduce costs through the ability to enter into more multi-year procurement contracts.
15. While we think there might be some incremental benefits from five-year capital budgets in future spending reviews, the more important priority is to use the forward certainty that four-year capital budgets established by the Spending Review 2025 will provide to improve the planning, design and delivery of capital projects across government.

KEY PRINCIPLES WE BELIEVE SHOULD BE ADOPTED WITHIN THE SPENDING REVIEW

Clarity on the government's wider strategic objectives beyond the five missions

16. We believe that business planning works best when aligned with the mission, vision, and strategic objectives of the organisation concerned.
17. We therefore concur with the approach of aligning the relevant parts of the Spending Review 2025 with the government's five missions to kickstart economic growth, build an NHS fit for the future, safer streets, break down barriers to opportunity, and make Britain a clean energy superpower, and with the foundations of economic stability, national defence, and secure borders.
18. However, these missions and foundations do not encompass the full range and scope of the government's ambitions and the range and scope of the public services it delivers.
    We therefore believe that Phase 2 of the Spending Review needs to be aligned with the government's wider strategic objectives in order to provide coherence to the rest of government not directly affected by the five missions.
19. The government appears to have already identified several strategic objectives beyond its five missions that are informing its policies and the Spending Review 2025. From our understanding of public statements by government ministers these appear to include:
    - Long-term sustainable public finances.
    - Higher living standards.
    - Digital first public services (not just in the NHS).
    - 1,500,000 new homes over five years.
    - Devolution to, and more effective, regional and local government in England.
    - Prevention over remediation.
    - Rebuilding the trust of the public in government, and its ability to deliver on their priorities.
20. We cannot speak for the government as to whether the above list is accurate or complete, and so we believe it would be helpful if the government's wider strategic priorities were to be explicitly set out in the Spending Review 2025 document when it is published.
21. Doing so would provide clarity to ministers, Parliament, public servants, and the public on the basis for the resource allocation decisions that the government is making. It would also help guide decision makers as to the strategic priorities they should be following as budgets are cascaded within departments and turned into operational plans.

Digital first

22. Using technology to transform public service is a long overdue reform that is an essential component of improving their quality, efficiency and effectiveness.
23. The government has recognised the necessity of this shift within the NHS, and its 10-year Health Plan sets out three strategic principles: to shift from hospitals to communities, from analogue to digital, and from sickness to prevention.
24. A similar approach is needed for other public services, including a digital first principle for all services that the government provides.
25. It is of course extremely important that in moving to a digital first principle that there is provision to support the ‘digitally disadvantaged’. However, this should not be used as an argument for not making or delaying the transition. In practice the efficiency gains of a digital first process will benefit all users of public services, including those who need support or alternative means to access digital services.
26. An example is the Passport Service, where a digital first approach has led to significant benefits for all users, including those who are unable to or find it difficult to access the internet.

Upfront investment to deliver sustainable efficiency improvements

27. Sustainable efficiency gains do not happen by magic.
28. While cutting budgets can result in public bodies innovating to operate with fewer resources initially, the result can often be counterproductive. A lack of resources can mean that there is no capacity to reform inefficient processes, develop new technology solutions, maintain equipment and buildings adequately, or to train staff effectively. Backlogs emerge, maintenance is foregone, problems arise in other public services, and the overall cost to the taxpayer ends up being much higher in the long-term.
29. Our experience, and that of our members working in both the private and public sectors, is delivering improvements that permanently reduce the cost and improve the quality of outputs often requires significant upfront investment. This is likely to include as much, if not more, revenue investment in re-engineering processes and in enhancing the skills and expertise of people, as it does in capital investment in technology or facilities.
30. A key test of the Spending Review 2025 will be whether departments have the revenue budgets for transformation that will be needed alongside the capital budgets for technology investment.

Core capital investment programmes to provide funding certainty

31. Uncertainty around the continued commitment to and future funding for multi-year capital programmes makes it very difficult for projects to be delivered in the most efficient way possible.
32. The benefit of a multi-year spending review is that departments will have forward certainty of their overall capital budgets, and this will benefit their overall planning of capital investments.
33. Unfortunately, there will be a temptation to retain as much flexibility at a departmental or directorate level, resulting in insufficient visibility of funding at the project or project portfolio level.
34. One way of obtaining this benefit would be to categorise between 60% and 80% of projects or project portfolios as ‘core projects’ with accompanying forward certainty of funding. Such an approach would benefit from providing the assurance that project teams need to effectively deliver core capital investment programmes, while retaining sufficient flexibility at a departmental and directorate level to adapt to circumstances and emerging priorities over the course of each spending review period.

Local government finance reform

35. Successive governments have deferred reform of local government funding in England for far too long. A large number of different funding streams have arisen, many of which are complex and complicated, based on out-of-date demographic and other assumptions, and require excessive involvement from Whitehall in often the smallest of local decisions, such as where to locate a public convenience.
36. At the same time, demand for social care, homelessness, special education needs and other welfare provision has put significant pressure on council budgets.
37. The result has been a significant mismatch between resources and need in many areas, a deterioration in the quality of local public services, and financial difficulties for many local authorities, including an increasing number issuing section 114 ‘bankruptcy’ notices.
38. While multi-year awards for regional and local government in England will provide many benefits, what is also required is a clear strategy for reforming funding streams over time.
39. In doing so, we believe there would be a benefit in separately identifying and managing council tax precepts and central government funding streams for local public services from those for local welfare services including children and adult social care, homelessness, housing support, and special educational needs provision. This would make it easier to share the costs of local welfare provision across wider geographies, perhaps at a regional level, while providing greater transparency to the public on the amount of their council tax bills that is actually spent on local public services.

Prevention as a genuine priority

40. Prevention has many benefits in that it is often much cheaper than dealing with problems when they occur, as well as providing better outcomes. This is clear in the health sphere but is also the case in many other public services and welfare programmes, ranging from education to the criminal justice system.
41. Unfortunately, prevention budgets are often the first to be cut when attempting to deal with financial pressures. They appear discretionary, but many of the financial pressures being experienced today are the result of not having invested sufficiently in prevention in previous times.
42. This is on top of the adverse consequences for the people involved.
43. Breaking this cycle will be difficult, but it starts by making prevention a key priority driving resource allocation decisions, with reform to how performance is monitored and the incentives for departments to genuinely focus on prevention in order to improve outcomes and reduce costs in the future.
44. It will also involve a much better understanding and management of the wider cost implications of individual decisions across central and local government. Investment in prevention that benefits the overall public finances should be prioritised even if there is a hit to the bottom line of the individual public body concerned.

SPECIFIC SUGGESTIONS FOR SPENDING REVIEW 2025

Planning reform must be leveraged to reduce time to build (e.g., East West Rail)

45. The planning reforms proposed by the government should in theory enable future infrastructure assets to be planned, designed and built much more quickly than they have in the past.
46. However, we don’t think the government should sit back and hope that future projects will benefit in this way. One test of these reforms will not just be about how the rate of housebuilding can be increased, but about how quickly infrastructure projects can be delivered.
47. An example is the East West Rail project designed to link Oxford and Cambridge that is still a decade or so away from being completed. Planning reform should enable this and numerous

other infrastructure projects to be delivered within a much shorter timeframe, unlocking the economic growth they are designed to support that much more quickly.

Subsidy-reliant services need more sustainable financial models

48. Services such as the railways, higher education, heritage, and the arts are funded through a mixture of user charging and taxpayer subsidies. The funding models for these, and other similar activities, have come under significant pressure in recent years, with demands for higher subsidies either taking away money from other priorities or resulting in cuts in the quality or scope of services.
49. We believe there is a need for a fundamental review of the funding models for these and other services to reduce the reliance of these services on the long-term ‘capriciousness’ that is inherent in relying on taxpayer subsidy decisions and provide a more secure funding approach.
50. This should include re-evaluating the mix between fixed and variable charging to better match the economics of the services concerned (e.g., the railways with its high fixed base), the structure of the student loans system, and opportunities to establish a greater level of endowment funding for heritage and arts organisations.

Higher level apprenticeships are essential if we are to develop the skills the UK needs

51. We support the governments’ plans to introduce a Growth and Skills Levy to replace the Apprenticeship Levy. Investment in the skills of the future is essential if productivity is to be improve and growth accelerated.
52. However, we are deeply concerned that the proposed removal levy funding for Level 7 apprenticeships would damaging for professional and technical skills in the UK economy and have a far-reaching impact across accountancy and other growth-driving sectors.
53. The unintended consequences include the loss of highly-skilled domestic training roles to offshoring – which our members and employers tell us is a very real possibility – a widening skills gap and reduced social mobility. All these factors risk diminishing the ability of UK businesses of all sizes to help achieve the fastest growth in the G7.

Investment in HMRC processes and responsiveness is essential to unlocking growth

54. More investment in HMRC processes and digital services is needed to minimise the time individuals, businesses and agents spend on compliance and maximise the time they spend on generating wealth and hence taxes to pay for public services. Traditional telephone and post services will continue to be required and support through these channels must be maintained, particularly during the transition to digital services.

EFFECTIVE FINANCIAL MANAGEMENT IS KEY TO DELIVERING SAVINGS AND MAXIMISING GROWTH

A clear line of sight is needed between multi-year spending reviews, annual budgets, supply estimates, in-year performance monitoring, and end-of-year annual financial reports

55. There is no clear line of sight between the total amount of money allocated by the government and authorised by Parliament, and the amounts going to individual public services. This hampers both effective financial management and accountability.
56. We believe there should be a consistent reporting approach that enables decision makers and those to whom they are accountable to, see the amounts allocated to individual or groups of public services in multi-year spending reviews, annual budgets and supply estimates and to follow those through to in-year performance monitoring reports and end-of-year annual financial reports.

Increase delegations of authority to encourage innovation and ownership of outcomes

57. One of the major obstacles to innovation can be excessive bureaucracy that requires even very small expenditures to be approved at too high a level in an organisation. This can make it difficult to incur relatively small expenditures even if doing so will reduce costs overall.
58. One of the reasons for this is that while delegated authorities for expenditure set too high can present excessive risk, if they are set too low, they can constrain the ability of organisations and teams to make rationale financial decisions. A balance is needed between providing directors and managers with the tools they need to do their jobs effectively and the appropriate level of constraints over their freedom of action.
59. As an example, a team manager might find it easier to recruit an additional staff member (because they have capacity within their budget) instead of incurring a much smaller expenditure that would save money overall but requires formal approval by several levels of management above them (with associated bureaucratic hurdles). Multiplied across government this can add up to a lot of wasted expenditure as managers find it easier to retain an inefficient cost structure because of the obstacles they would need to overcome if they were to seek to reform it.
60. We believe that HM Treasury and departments should review delegated authorities across government to ensure that there is a better balance between empowering teams to innovate and ensuring that larger expenditures are appropriately controlled.

End the huge volatility in capital expenditure within financial years

61. According to public sector finance statistics, more than a quarter of capital investment is incurred in the final two months of each financial year.
62. This is despite the ability of budget holders to carry forward unspent capital amounts to subsequent years and management processes intended to prevent a rush to get projects out the door at the end of each financial year.
63. There are several reasons for this sub-optimal approach to capital budgeting and the delivery of capital programmes. The lack of forward certainty that multi-year spending reviews should ideally address is one key reason, but other reasons include the lack of long-term capital and maintenance plans in many departments, the lack of standardised building and equipment designs, an annual budgeting cycle that means that projects often only receive final approval in the second half of a financial year, and the lack of rolling programmes of capital investment that enable expertise to be built up and more effective capital procurement.
64. Spending Review 2025 provides an opportunity for departments to develop such plans and to revise their approach to capital investment planning to drive better value for money.

A portfolio approach is needed to manage overruns and underspends to reduce waste

65. One of the ironies of the comparatively low level of public investment compared with many other developed countries is that departments frequently do not spend all of their capital budgets. This is despite the poor state of hospitals, schools, and many other public buildings that urgently require replacement and are costly to run, and the need for much greater investment in technology to improve the delivery of public services.
66. At the same time, the public sector has a history of going significantly overbudget on major projects, causing embarrassment to the departments concerned and – even more unfortunately – the descoping or deferral of those projects (or in many cases other projects), often significantly reducing the public benefits that were originally envisaged.
67. Some of the reasons for these overruns relate to operational and financial management capabilities, ranging from the quality of cost estimates and the effectiveness of procurement to the management of project risks. These can be addressed by strengthening finance teams within government.
68. Others relate to delays in planning approvals and compliance requirements that the government also has plans to address.

69. Despite these improvements, there are always likely to be projects that go overbudget and there is a need for change in how overruns are managed within and between departments and between financial years.

70. A portfolio approach would help avoid situations where teams within departments deliberately plan to underspend their capital budgets 'just in case' some projects go over budget. It would also help prevent the current practice of descoping or deferring other projects to avoid overspends in one part of a department or in a department even where there is budget capacity available elsewhere.

Fraud prevention and detection capabilities should be enhanced

71. The National Audit Office estimates that fraud and error cost the taxpayer between £51bn and £81bn in 2023/24. As a consequence, preventing and detecting fraud and error is one of the most productive activities that government can undertake to increase the resources available for its priorities.

72. We welcome the work that the Public Sector Fraud Authority has already done to improve the government's work in this area. However, more can and should be done.

73. We believe the Spending Review should increase the resources allocated to preventing fraud and error given the significant returns that will be generated by doing so.

74. Preventing fraud and error goes beyond compliance and investigation to address the underlying issues that make it too easy for fraud to be perpetrated and errors to be made. There is a need for a systemic effort over the Spending Review period to simplify, streamline and digitalise complex and overcomplicated rules and processes across government, especially in the tax and benefit systems.