5. CURRENT DOMESTIC FISCAL FRAMEWORK REFORMS ACROSS THE EU

5.1. INTRODUCTION

The Maastricht Treaty and the Stability and Growth Pact (SGP) impose budgetary obligations on Member States. In order to ensure the respect of objectives, they also stress the importance of *national rules and institutions* for budgetary discipline. The report on the SGP reform endorsed by the European Council on 22 March 2005 says that *national budgetary rules should be complementary to the Member States' commitments under the Stability and Growth Pact.* It also says that *national institutions could play a more prominent role in budgetary surveillance to strengthen national ownership, enhance enforcement through national public opinion and complement the economic and policy analysis at EU level*. This political orientation has been reiterated in subsequent Council conclusions and statements.

In the context of the current crisis, the role national fiscal frameworks may play in sustaining budgetary retrenchment is gaining more importance in the fiscal policy debate. For instance, the last year's EFC report on fiscal exit strategy acknowledges that *fiscal frameworks can provide suitable incentives and constraints for policy makers to commit to lasting fiscal consolidation and sustainable policies,* and recommends to further work on this issue. In the same vein, in the October 2009 Council Conclusions, the Ecofin stated that *important flanking policies to the fiscal exit will include strengthened national budgetary frameworks for underpinning consolidation strategies and support long-term sustainability.* In the same conclusions, the Council also recalled that *this should be reflected in the SCPs to be transmitted by Member States to the Commission by the end of January 2010.*

Against this background, the Commission has been carrying out a number of analyses and research projects in the area of fiscal governance over the latest years. For instance, recent past issues of the PFR include several analytical chapters dealing with different aspects of domestic fiscal frameworks. Most of this research is based on information provided directly by Member States, and has notably led to the dissemination of a comprehensive database on domestic fiscal rules, independent institutions and medium term budgetary frameworks across EU countries, which is now available at the external DG Ecfin website.([27]) The 2010 PFR also deals with these issues in the analysis included in Chapter 3 of Part II, which provides policy guidelines related to the appropriate and desirable institutional reforms more conducive to the strengthening of fiscal governance at national level.

This chapter also focuses on fiscal governance but from a different perspective. Specifically, it takes stock of recent and envisaged reforms of domestic fiscal frameworks that have been included by Member States in the last round of the SCPs, and presents and discusses the main features of these announced measures. In line with previous analyses, domestic fiscal frameworks are defined as the set of elements that form national fiscal governance, i.e. the overall system of arrangements, procedures and institutions that underlies the planning and implementation of budgetary policies. The main elements of domestic fiscal frameworks are numerical fiscal rules, independent public institutions acting in the field of budgetary policies, medium-term budgetary frameworks for multiannual fiscal planning (MTBFs) and budgetary procedures governing the preparation, approval and implementation of the budget.

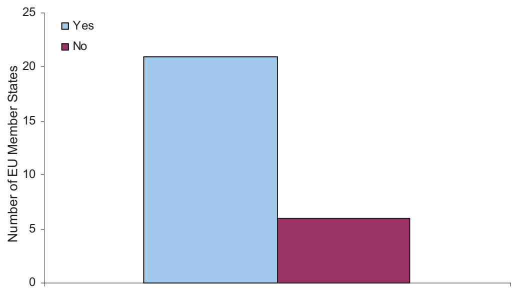
The chapter is structured as follows. Section 2 provides an overview of the informational content of the 2009-2010 SCPs as regards the reform of national fiscal governance. For those countries that included this information in their updates, Section 3 describes more in detail these measures according to the elements of domestic fiscal framework (i.e. rules, institutions, MTBFs and budgetary procedures). Section 4 focus on the link between the recommendations included in the Council Opinions and the policy initiatives announced in the SCPs. Finally, Section 5 summarises the main conclusions of this analysis.

([27]) http://ec.europa.eu/economy_finance/db_indicators/fiscal_governance/index_en.htm

5.2. OVERVIEW OF THE INFORMATION CONTAINED IN THE 2009-2010 SCPS

A majority of Member States included in their 2009-2010 SCPs information related to the reform of national fiscal frameworks.(28) Specifically, 21 countries have already implemented and/or envisage to implement changes in their respective systems of fiscal governance, which can only be considered a positive feature of the last round of SCPs (see graph I.5.1).(29) As for those countries that do not foresee any substantial reform of the fiscal framework in the coming years, most of them declare to stick to the prevailing fiscal framework to redress the current fiscal imbalances (e.g. BE, DK and ES) while others announce future reform or strengthening measures but no details are provided (e.g. LU, MT and FI).

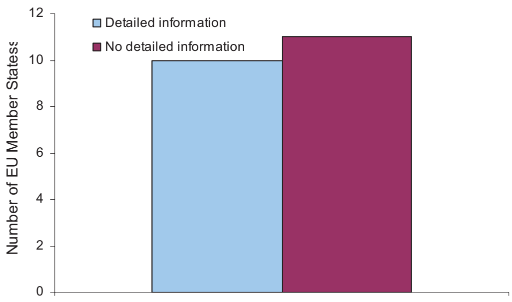
Graph I.5.1: **Information on national fiscal frameworks included in the 2009-2010 updates of the SCPs**



Source: Commission services, 2009-2010 updated SCPs.

However, both the level of detail of this information and the stage of implementation or the degree of advancement of reform plans vary widely across countries (see graph I.5.2 below). Thus, only 10 Member States included detailed information in terms of concrete measures and calendars. While the updates of DE, EE, IT, HU, NL, AT, PL SI, SE and UK contain exhaustive information about ongoing and future reforms, the programmes of BG, CZ, IE, EL, FR, CY, LV, LT, PT, RO, and SK only provide scant and generic information.

Graph I.5.2: **Detailed information on reform plans included in the 2009-2010 updates of the SCPs**



Source: Commission services, 2009-2010 updated SCPs.

Arguably, the level of detail provided in the SCPs is somewhat related to the degree of implementation. Indeed, among the 10 Member States giving comprehensive information only one of them (NL) reports the introduction of reform measures from 2011 onwards, while all the remaining countries have already put into operation (at least partially) the announced policy initiatives between 2009 and the 1st quarter of 2010. By contrast, most of Member States reporting a limited amount of information announce the introduction of their reform actions only from 2010 or 2011 onwards.

5.3. TYPE OF MEASURES ACCORDING TO THE MAIN ELEMENTS OF DOMESTIC FRAMEWORKS

As said in the previous section, 21 Member States report recent and/or future changes to their national fiscal frameworks. These measures address the reform of different elements of these frameworks, namely rules, independent institutions, MTBFs and budgetary procedures.

According to this classification, changes to the existing budgetary procedures are the most frequent policy initiatives and are foreseen by 19 Member States. These are closely followed by the reform and/or introduction of numerical fiscal rules in 13 EU countries.(30) Finally, reforms to

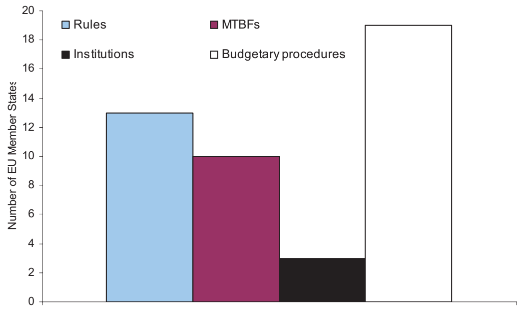
(28) This note is based on the programmes submitted by the 27 Member States of the EU.

(29) Changes in national fiscal frameworks reported in the SCPs represent all innovations relative to the information set in the DG Ecfin fiscal governance database that currently covers effectively implemented reforms up to 2008.

(30) In 2 of these 14 Member States (SK and UK) two additional rules are planned to be introduced. In the case of the UK, these two new rules replace the former golden and debt rules. As for PL and RO, according to their SCPs, they plan to introduce 4 and 3 new fiscal rules. Specifically, RO plans to implement 1 budget balance and 2 expenditure

MTBFs and institutions rank more distantly with 10 and 3 Member States envisaging changes, respectively (see graph I.5.3 below).

Graph I.5.3: **Type of reforms according to the main elements of domestic fiscal frameworks**



Source: Commission services, 2009-2010 updated SCPs.

Table I.5.1 provides a general overview of the measures considered by Member States in their respective Stability and Convergence Programmes. These policy actions are classified both according to the elements of the fiscal framework and by country.

Subject to the comprehensiveness of the information submitted by Member States, the next sub-sections describe more in detail these reform measures for each building block of domestic frameworks.

5.3.1. Reforms of numerical fiscal rules

Measures addressing reforms in the field of fiscal rules are primarily implemented through the establishment of 19 new rules constraining the conduct of fiscal policy, whereas only 2 of the

rules, while PL announces the establishment of 1 budget balance rule, 1 debt rule and 2 expenditure rules.

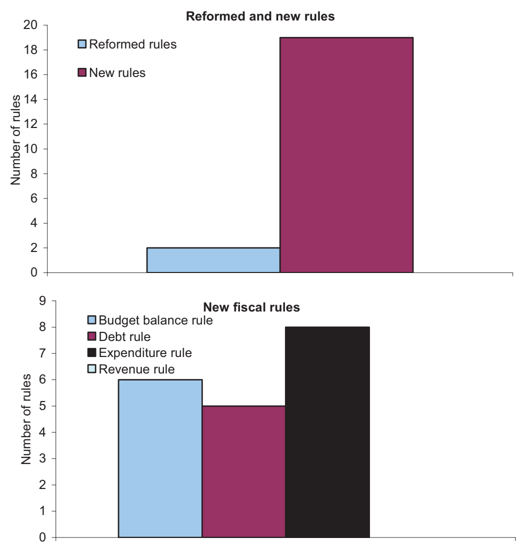
Table I.5.1: **Measures included in the 2009-2010 SCPs to reform domestic fiscal frameworks**

	Numerical rules			MTBF			Independent institutions			Budgetary procedures		
	Number of rules in 2008	Reform existing rules	New rules	Already in place in 2008	Reform existing MTBF	New MTBF	Number in place in 2008	Reform current bodies	New bodies	Measures upgrading procedures	of which higher centralisation	of which top-down budgeting
BE	4	0	0	Yes	No	No	2	No	No	No	–	–
BG	2	0	0	Yes	No	No	0	–	No	No	No	–
CZ	2	0	0	Yes	No	No	0	–	No	Yes	No	No
DK	3	0	0	Yes	No	No	1	No	No	No	–	–
DE	5	0	1[(4)]	Yes	No	No	4	No	No	Yes	**No**	**Yes**
EE	2	1	0	Yes	No	No	1	**No**	No	Yes	No	**No**
EI	3	0	0	Yes	No	No	0	–	No	Yes[(5)]	–	–
EL	0	–	–[(1)]	No	–	–[(2)]	1	No	–[(3)]	Yes	**Yes**	Yes
ES	4	0	0	Yes	No	No	2	No	No	No	–	–
FR	5	0	1	Yes	No	No	2	**No**	No	Yes	No	**No**
IT	4	0	1	Yes	Yes	No	1	**No**	No	Yes	Yes	No
CY	0	–	0	No	No	Yes	0	–	No	Yes	**No**	No
LV	2	0	0	Yes	No	No	0	–	No	Yes	**No**	**No**
LT	4	0	0	Yes	No	No	1	**No**	No	Yes	Yes	**No**
LU	3	0	0	No	–	–	1	**No**	No	No	–	–
HU	2	0	1	No	–	Yes	1	No	Yes	Yes	**Yes**	No
MT	0	–	0	Yes	No	No	0	–	No	No	–	–
NL	2	0	1	Yes	No	No	1	**No**	No	Yes	No	**No**
AT	1	0	1	Yes	No	Yes	3	**No**	No	Yes	No	No
PL	1	1	4	Yes	Yes	No	0	–	No	Yes	**No**	No
PT	3	0	1	No	–	Yes	2	No	No	Yes	**No**	**No**
RO	2	0	3	Yes	No	Yes	0	–	Yes	Yes	No	**No**
SI	2	0	1	Yes	No	No	1	**No**	Yes	Yes	No	No
SK	2	0	2	Yes	Yes	No	0	–	No	Yes	**No**	No
FI	4	0	0	Yes	No	No	0	–	No	No	–	–
SE	3	0	0	Yes	Yes	No	2	**No**	No	No	–	–
UK	2	0	2[(6)]	Yes	No	Yes	1	**No**	No	Yes	No	No
Total	67	2	19	22	4	6	27	0	3	19	4	2

(1) The programme announces the introduction of new rules but neither the number nor their features are specified. (2) The programme does not specify whether some multiannual measures strengthening fiscal planning and monitoring constitute the basis for introducing an effective MTBF. (3) The programme does not clarify whether a new body to be implemented in the next future can be considered an independent fiscal institution. (4) The existing golden rule for the Federal Government was abolished in 2009 and replaced by a new cyclically adjusted balance rule. (5) Inclusion of multiannual budgetary targets in the annual budgetary documentation. (6) The two prevailing fiscal rules in 2008 were replaced as of 2010 by binding balance and debt targets over the period from 2009 10 to 2010 16. As a result, the total number of fiscal rules in place remains unchanged between 2008 and 2010.
Source: 2009 2010 SCPs

prevailing rules are expected to be reformed (see graph I.5.4 below) ([31]).

Graph I.5.4: **Reformed and new fiscal rules**



Source: Commission services, 2009-2010 updated SCPs.

The degree of implementation of these reforms diverges across Member States. For instance, DE and HU have already introduced, respectively, a budget balance rule on a cyclically-adjusted basis for the Federal government and the Länders; and a debt rule defined in real terms for the central government. In both cases, not only the target definition and the coverage of the rules are known but also their monitoring mechanisms. By contrast, FR announces its intention of establishing a new budget balance rule on a multiannual basis for the whole of the general government sector. A working group, analyzing and assessing various forms of rules, has been established in order to adopt this new rule over the next years. This working group is expected to provide its report by next summer. Similarly to FR, SK announces the introduction of expenditure limits and a debt brake with a strong legal basis but no further information on these policy initiatives is contained in the update. Finally, other countries such as EL also envisage the introduction of fiscal rules in the short-term but neither details nor calendars are provided.

By type of rule, 8 out of the 19 new numerical fiscal rules are expenditure rules, whereas new budget balance and debt rules amount to 6 and 5, respectively. No new revenue rule obliging the government to allocate higher-than-expected revenues to debt reduction is announced (see Graph I.5.4 below).

Finally, two countries, PL and EE, plan to reform their existing fiscal rules. In the case of PL, the reform of the existing debt rule for the general government through more stringent corrective mechanisms is accompanied by the establishment of 4 new rules according to the update: a budget balance rule and a debt rule both for local governments to be implemented in 2011 and 2014 respectively, and two expenditure rules constraining non-mandatory expenditure.([32])

5.3.2. Reforms of medium-term budgetary frameworks (MTBFs)

In 2008, a large majority of Member States declared to have in place a domestic MTBF for fiscal planning, and only EL, CY, LU, HU and PT reported not to have such fiscal arrangement in their respective fiscal governance systems.

According to the information provided in the 2009-2010 SCPs, 10 Member States report changes to their national MTBFs. Specifically, in 4 Member States the existing MTBF is being reformed while in the remaining 6 countries a new framework is announced (see Graph I.5.5 below).

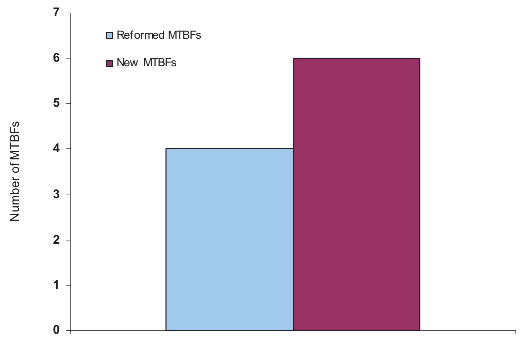
In 3 cases (AT, RO and UK), newly introduced MTBFs replace the existing frameworks. In the case of HU, by contrast, a new MTBF has been set for the first time in the form of a fiscal responsibility law introducing medium-term fiscal plans covering at least three years. This is also the case for CY and PT, which did not have such fiscal arrangement in place and now announce its implementation. By contrast, neither EL nor LU envisage the establishment of a domestic MTBF.

([31]) In the case of Greece, the update announces the implementation of new fiscal rules in 2010. However, no details about the type of rules and calendar implementation are provided. As a result, Greece has not been included in graph 4 of this sub-section.

([32]) For these two expenditure rules, however, the programme does not provide a concrete calendar and is not fully clear whether the rule is applied to the general government sector or only to the State budget.

As a result, the total number of domestic frameworks is expected to increase from 22 in 2008 to 25 at present.

Graph I.5.5: **Reformed and new MTBFs according to the SCPs**



Source: Commission services, 2009-2010 updated SCPs.

Finally, the 4 reforms of the existing frameworks (IT, PL, SK and SE) mainly consist of the reinforcement of the binding nature of fiscal targets and the extension of the period covered by the framework. The latter applies particularly to SE, which has recently set a legally binding three-year period for the existing framework.

5.3.3. Reforms related to independent public institutions

The resort to independent public institutions acting in the field of fiscal policy is by far the less popular policy option to reform national fiscal governance. Thus, only 3 new independent bodies have been (or will be) set up compared to the situation prevailing in 2008, when the number of these institutions in the EU amounted to 27. Besides, no reforms of the existing institutions in 2008 are announced in the 2009-2010 SCPs.

The newly introduced independent bodies have been established in HU and SI. In HU, the new body has been entrusted with the mandate of assuring the transparency of fiscal planning and is supported by a secretariat. In turn, the new institution in SI acts as a consultative body for the assessment of fiscal policy and budgetary developments as well as structural reforms (see the country specific annex for further information). Finally, the recently approved Fiscal Responsibility Law in RO will entail the establishment of a new independent institution.

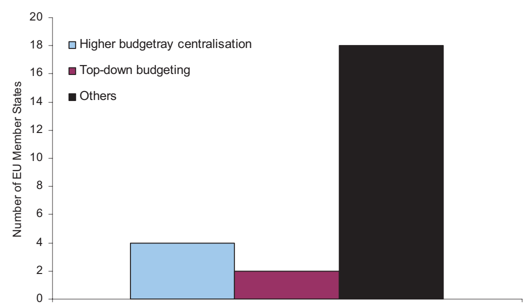
Overall, these 3 new institutions help rebalance to some extent the earlier uneven distribution of these bodies across the EU. In 2008, the 27 existing institutions were spread across 17 EU countries, of which 13 belonged to the former EU15. At that time, SI was one of the four new Member States having already introduced an independent body (i.e. the IMAD, which notably provides independent forecasts for the budget preparation).

5.3.4. Changes to domestic budgetary procedures

Changes to domestic budgetary procedures account for the largest number of measures addressing the reform of national fiscal governance, particularly at the planning stage.([33]) According to the 2009-2010 SCPs, 19 Member States have already implemented, or will do it in the next future, policy measures targeting the upgrading of the current budget process.

However, only a limited number of countries report having designed and/or implemented measures strengthening the centralisation of the budget process or the introduction of top-down budgeting (see graph I.5.6). These are the two elements of domestic budgetary procedures most conducive to fiscal discipline as they act to address the common-pool problem. Finally, the other reported measures aim mainly at performance and programme budgeting and, to a lesser extent, the reinforcement of monitoring mechanisms and the improvement of reporting procedures to increase transparency.

Graph I.5.6: **Reforms of budgetary procedures in the SCPs**



Source: Commission services, 2009-2010 updated SCPs.

([33]) The other two dimensions of the budget process are the approval and the implementation stages.

5.4. THE ASSESSMENT OF THE DOMESTIC FISCAL FRAMEWORKS REFORMS

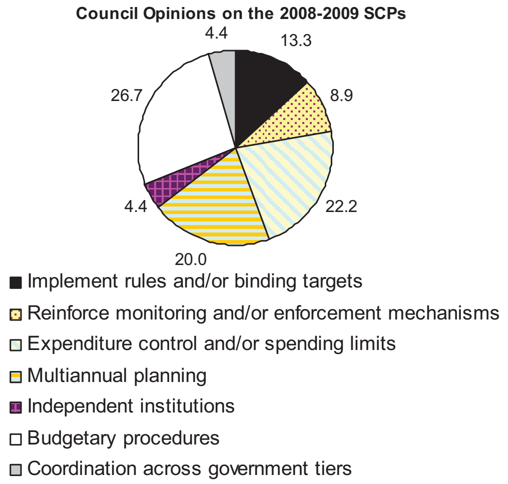
This section summarises key features of the assessment on the domestic fiscal frameworks reforms. It does so, first, by comparing policy invitations in the Council Opinions (COs) made on the two last rounds of SCPs. It then compares the reforms reported in the 2009-2010 SCPs with the policy invitations issued by the Council on the previous round of SCPs. Finally, it briefly comments the Commission services' Macro Fiscal Assessments.

5.4.1. Last year's COs and the current COs on the 2009-2010 SCPs

This sub-section looks at the nature of the policy invitations issued by the Council on the last two rounds of SCPs. Graph I.5.7 shows how the policy invitation issued last year, on the 2008-09 SCPs, were distributed by type of measure. Overall, the graph shows that over 25% of the invitations concerned weaknesses in domestic budgetary procedures. These policy invitations mainly referred to concerns about the transparency, the performance and programme budgeting and the level of centralisation of the budgetary process. 20% of the invitations concerned multi-annual planning while 22% of the invitations related to issues of expenditure control and/or expenditure limits. Grouping together the invitations concerning expenditure with those on the implementation of rules and binding targets and those on the reinforcement of monitoring and/or enforcement mechanisms, shows that 45% of the advice given was directly concerned with fiscal discipline.

Graph I.5.8 shows the distribution of policy invitations issued on the current round of SCPs, by type of measure. Compared with the previous year, there is a significant increase in the share of invitations concerning a reinforcement of the monitoring or enforcement mechanisms (from 9% to 17%) and the coordination across government tiers (from 4% to 10%). There is a countervailing decrease in the share of recommendations requesting a strengthening of budgetary procedures and those concerning multiannual planning. However, in absolute terms, the number of invitations falling in these two categories remained roughly the same between last year and this.

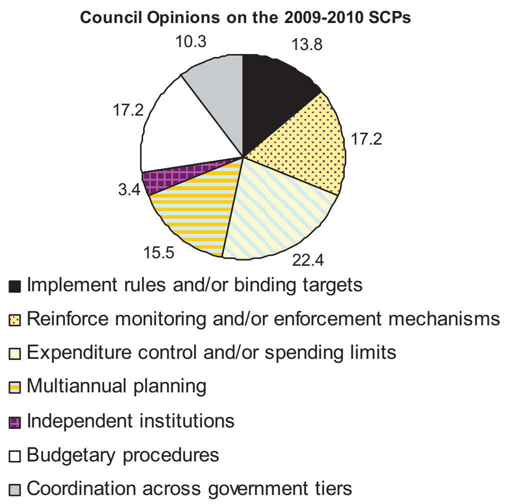
Graph I.5.7: **Council policy invitations on last year's SCPs by type of measure (as a % of total measures)**



Source: Commission services, 2009-2010 updated SCPs.

The group of measures addressing fiscal discipline more directly, i.e. the invitations on rules, monitoring and enforcement procedures and the overseeing of public spending developments, increased further. In this year's round, 55% of the advice given covered these issues, compared with 45% last year.

Graph I.5.8: **Council policy invitations on this year's SCPs by type of measure (as a % of total measures)**



Source: Commission services, 2009-2010 updated SCPs.

5.4.2. Last year's COs and policy initiatives contained in this year's SCPs

A relevant question when analysing and assessing the reform measures included in the 2009-2010 SCPs is to what extent they follow the policy invitations issued by the Council in last year's COs.

Last year, 19 Member States received a policy invitation relating to the reform of fiscal frameworks.([34]) Of these, 7 Member States included measures in the 2009-2010 SCPs which follow (at least partly) their policy invitations, while the initiatives of the remaining 12 Member State are not in line with the recommendations.

In conclusion, in spite of the significant number of invitations addressing the reform of domestic fiscal frameworks, the fulfilment of the policy invitations included in the previous round of Council Opinions is rather limited.

5.4.3. The 2009-2010 SCPs and the Commission's assessments

Finally, an additional interesting exercise consist of looking at the Macro Financial Assessment of the last round of SCPs to see how the Commission has evaluated the reforms announced in the updates.([35])

The assessment is somewhat negative (or mixed in same cases) with respect the measures included in the SCPs of 10 Member States. For instance, the assessment of the recent initiatives in BG points to likely counterproductive effects in terms of transparency. While in the case of BE, ES and MT the update does not foresees major reforms, the assessment underlies the need for further improvements in their national fiscal frameworks. As for CZ, EI, EL, FR, LV and UK the assessment considers that progress has been made recently. However, in all these countries there is significant room for additional improvements and the assessment puts forward some policy proposals to strengthen the current framework.

Although there is still margin for further progress to effectively strengthen fiscal governance, the Commission concludes that important improvements have been achieved (or can be achieved if the envisaged measures are implemented) in 10 Members States (i.e. DE, EE, IT, HU, AT, LT, PL, RO, SI, and SK).

Finally, no significant weaknesses are identified in the case of DK, LU, NL, FI and SE.

5.5. MAIN CONCLUSIONS

Following the 2009 Council Conclusions, a majority of Member States have included in their respective SCPs information related to the reform of domestic fiscal frameworks. Specifically, 21 EU countries report recent and/or future changes to be implemented in the next years. However, detailed information on the scope of these measures and/or an implementation calendar is only provided in 10 cases.

By type of measure, changes to the existing budgetary procedures are the most frequent policy initiatives and are foreseen by 19 Member States. As for reforms related to numerical fiscal rules, they are envisaged in 13 SCPs, and the amendment of MTBFs or the introduction of new frameworks is reported by 10 countries. Finally, policy initiatives in relation to independent institutions are limited to 3 Member States.

Most of the measures targeting the upgrading of the existing budgetary procedures are related to transparency issues, programme and performance budgeting and monitoring mechanisms. By contrast, those elements of the budget process most conducive to fiscal discipline (i.e. the centralisation of the budget process and the use of top-down budgeting) are hardly addressed.

The announced reforms of fiscal rules are for the most part based on the introduction of 19 new rules, while only 2 countries announce the reform of existing rules. 8 of these new rules establish constraints on expenditure developments while new budget balance and debt rules amount to 6 and 5, respectively. No new revenue rules are foreseen.

Changes to MTBFs consist of both the reform of the existing frameworks and the introduction of

([34]) Those Member States that did not receive any policy recommendation in the field of fiscal governance were CZ, DK, ES, CY, LU, NL, FI and SE.

([35]) At the time this chapter was being prepared, the assessments of the updated programme of Portugal and Cyprus were note yet available.

new ones (4 and 6 Member States respectively). Three countries not having in place a MTBF in 2008 announce now the introduction of a new framework. Overall, the total number of MTBFs currently amounts to 25.

The resort to independent fiscal institutions is by far the less frequent policy initiative according to the updates. In only 3 Member States the introduction of such bodies acting in the field of fiscal policy is announced.

Similarly to the previous round of the Stability and Convergence Programmes, the draft Council Opinions on the 2009-2010 SCPs continue to show a majority of policy invitations targeting the improvement of the prevailing budgetary procedures. However, there has been now a significant increase in recommendations requesting a reinforcement of monitoring and enforcement mechanisms of fiscal targets. In addition, the sum of those policy invitations more directly linked to fiscal discipline (i.e. rules, monitoring and enforcement procedures and the overseeing of spending developments) represents by far the main area of this year's policy invitations.

In spite of the significant number of recent or announced reforms of domestic fiscal frameworks, compliance in relation to the last year's policy invitations is rather limited. Only in 7 cases the measures contained in the 2009-2010 SCPs follow (at least partly) last year's policy invitations.

To conclude, the Macro Financial Assessments of the programmes are somewhat mixed with respect the measures included in the SCPs of 10 Member States. By contrast, the evaluation of the recently implemented or envisaged measures is rather positive in other 10 EU countries. However, the Commission considers that supplementary policy initiatives would be needed with a view to effectively strengthening fiscal governance. Finally, only in 5 countries, the existing frameworks do not seem to present major weaknesses. The assessments for CY and PT were not yet ready at the time this analysis was conducted.