Independent Fiscal Institutions in the European Union: Is Coordination Required?

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Motivation

• EU fiscal framework going national:
  • Fiscal rules
  • Independent fiscal “bodies” (≈ independent fiscal institutions / councils).

• Consistency with EU standards of fiscal discipline:
  • Required features for national fiscal rules (in EU law + IG Treaty)
  • Need for coordination among national “bodies” ? If so, what type?

• Paper analyzes coordination issue through three questions:
  #1 How do IFCs really influence fiscal policies? (Effectiveness)
  #2 Does answer to #1 point to specific coordination failures?
  #3 If so, what form of coordination and how?
IFCs to constrain fiscal discretion

• Constrained discretion = desirable policy regime → frameworks.
• Framework = rules ∩ independent institution.
• Rise of IFCs in fiscal frameworks.
How do IFCs influence fiscal policies?
IFCs' effectiveness

- No policy tool → IFCs can only work through:
  - Greater transparency → accountability (reputational/electoral costs)
  - Better fiscal information → more market discipline
  - Easier handling of common pool problems.
- Influence on fiscal decisions: through the public debate.
IFCs effectiveness

• Maximize signal/noise → presence in public debate + good COM.

• Golden rule: talk only when you must.

• Descriptive evidence on Google searches as metric for effective COM:
  • UK’s Office for Budget Responsibility
  • Netherlands Bureau for Economic Policy Analysis
  • [Spain’s Independent Fiscal Authority (AIReF)]
Talk only when you must: the OBR

Interest in OBR strongly correlated with key dates of the budget cycle.
Talk only when you must: the CPB

Peak interest around release of assessments of electoral platforms, ahead of general elections.

Average monthly pattern of interest concentrated around key forecast releases
Coordination failures
“Systemic” failure: little harmony

• Lack of convergence to leading practice.
  • Capacities to deliver appear to vary across countries (EFB, 2018)
  • Major differences in aspects that shape ability to deliver (Horvath, 2017).

Access to information (de jure guarantees, OECD)
“Functional” failure: cacophony

• Multiple assessments of the same fiscal position → cacophony.
• Sources of cacophony:
  • Information sets,
  • Priorities / perspectives,
  • Honest disagreements among experts (judgment and uncertainty involved).
• Effects of cacophony:
  • Undermines credibility of local IFC (agent of EC vs. dependent) → jammed signal.
  • Weakens EC traction at local level → runs against 2010 approach.
    → bad for new governance framework.
• Potential areas of conflict:
  • Forecasts, “other relevant factors,” recommendations.
Coordination and its forms
Hard vs. soft coordination

- National anchorage
- Independence (from EC and national politics)

Taming cacophony & benchmarking good practice → soft coordination
Information exchange and peer pressure

• Mitigate cacophony.
• Forge consensus on aspects of best practice critical to IFCs in EU framework.
• Vertical & horizontal:
  • Vertical: EC and national IFC (methods, judgments, timing),
  • Horizontal: developing good practice, benchmarking, peer pressure/reviews,
  • Overall consistency: IFCs as a group interact with EC on cross-country issues.
• Special case of recommendations: cost of cacophony higher (fiscal policy coordination at risk) → avoiding cacophony, e.g. through preset division of labor.
Coordination must be flexible

- IFCs are country-specific for (mostly) good reasons → modalities of vertical coordination tailored to each case. See Table 1.

<table>
<thead>
<tr>
<th>Fiscal illusion</th>
<th>Sustainability analysis</th>
<th>Low capacities</th>
<th>Funding guarantees</th>
<th>Centralized (Directive?)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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<td>No engagement</td>
<td>Effective comply/explain; hearings</td>
<td>Horizontal dialogue (peer pressure)</td>
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<td>Cacophony</td>
<td>Sharing information (data, models, etc)</td>
<td>Vertical dialogue</td>
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Coordination today

• Networks of IFCs: two networks / some differences in memberships.
  • Sui generis Network of EU IFIs: many aspects of horizontal information sharing (best practice, benchmarking), and elements of joint engagement with EC (fiscal governance reform, minimum standards for IFCs).
  • Official network of independent bodies: element of vertical dialogue of IFCs (as a group) with the center.

• European Fiscal Board:
  • Documents lack of harmony,
  • Identifies points of stress behind cacophony (information sets),
  • Encourages EC even-handedness → lower risk of cacophony.

• More coherence and clarity needed → proceed cautiously (independence is a sacred cow for new institutions).
Way forward

• Identify all the players in the game.
• Better align EFB on best practice IFC...
  • Independence cannot hinge too much on high-quality managerial appointments / staff.
  • Expanded role in coordination → resources + permanent managerial positions.
• Clear architecture:
  • IFC network with mandatory participation (build upon the positives of existing structures).
  • Upgraded EFB as an umpire of the network and enabler of vertical dialogue with EC.
Conclusions

• Risk of coordination failures: too little harmony, too much cacophony.

• Soft coordination is desirable: preserves IFC independence while more effectively promoting best practice in the EU context.

• Institutional architecture that remains flexible to accommodate tailoring of vertical dialogue and promotes harmony when required.

• EFB as an umpire and an enabler, but must get closer to best practice IFC to credibly play that role.