



Fiscal Transparency and EU Independent Fiscal Institutions: Perceptions and Realities

Michal Horvath (University of York and Network of EU IFIs)

Main messages



1. Independent Fiscal Institutions (IFIs) ***are the fiscal transparency reform*** and not its alternative
2. A well set up IFI represents a **strong commitment to transparency** in medium-term-oriented budgetary processes
3. **Heterogeneity** in inputs and heterogeneity in outcomes
 - Some EU IFIs lack resources and have limited interaction with the executive and parliamentarians
 - **Some encouraging visible outcomes** in the transparency of forecasting and budgeting

Presentation outline



1. Independent fiscal institutions: theory and practice
2. Practical cases of IFIs making a difference
3. Challenges faced by IFIs



Independent fiscal institutions

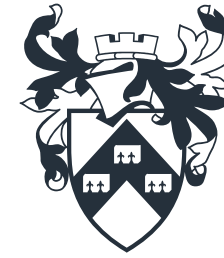
THEORY AND PRACTICE

IFIs: the rationale



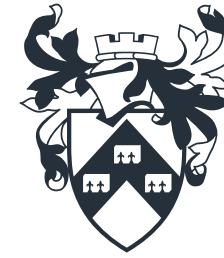
- **Good policy:** countercyclical, moderate debt, transparent
- **Actual policy:** often pro-cyclical with deficit bias and accounting tricks
- **IFIs:** a commitment device *through transparency*

How can IFIs help (in theory)?



- **Independent evaluation** of whether governments are keeping promises defined in fiscal rules
 - ✓ Asymmetric information, time inconsistency
- **Monitoring of the transparency** of accounts
 - ✓ Weak law enforcement, corruption
- Providing assessments of the **long-term consequences** of government policy
 - ✓ Intergenerational fairness, quality of public finances
- Providing **independent costing** of government measures
 - ✓ Common pool problem

IFIs: theory and practice



EU IFIS INTEGRATING TWO MODELS

THE ANGLO-SAXON MODEL

Institutions rather than rules
Oversight of the Executive
Reliance on trust and custom
Positive analysis
PBOs as a standard



THE “CONTINENTAL” MODEL

A rule-based model
IFIs guardians of the rules
Reliance on detailed processes
Need to take a stance on stance
Institutional diversity



COMBINATION OF ELEMENTS OF A VERY DIFFERENT NATURE

- Resource- and skill-intensive
- Need to build reputation quickly
- Need to develop effective stakeholder relations with a variety of institutions

EU IFI mandates



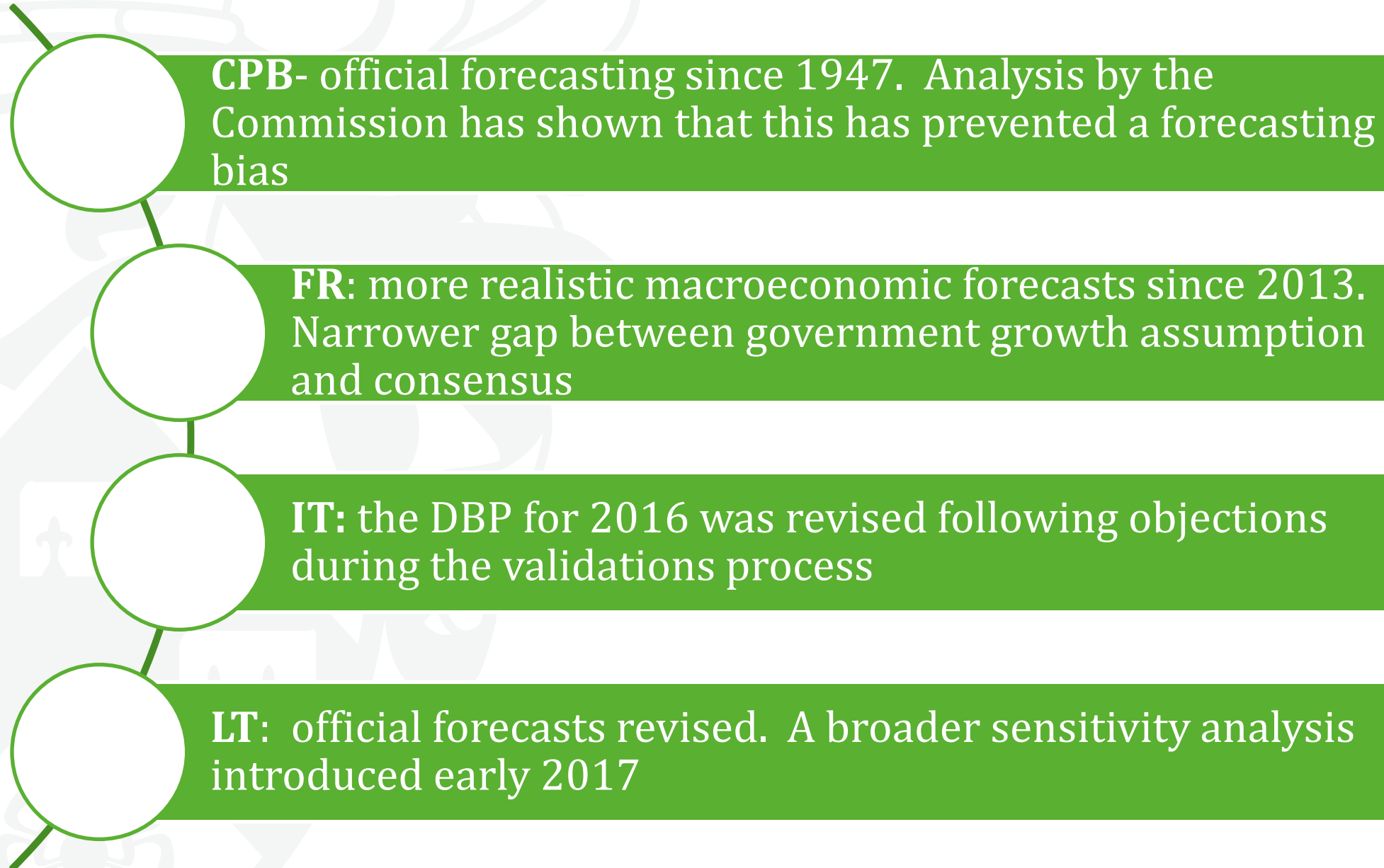
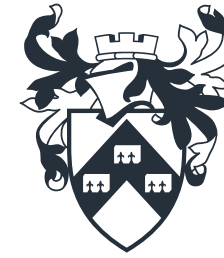
Task	Frequency
Assessment of draft annual budgets.	18
Endorsement/assessment of macroeconomic forecasts used for fiscal planning.	17
Endorsement/assessment of budgetary forecasts.	17
Ex ante fiscal rule assessment.	17
Assessment of Stability Programmes (or of national medium-term fiscal plans).	15
Promotion of fiscal transparency.	15
Ex post fiscal rule assessment.	14
Continuous monitoring of fiscal policy/budgetary execution.	14
Long-term sustainability assessments.	14
Involvement in the correction mechanism of the country's main fiscal rule	13
Research in public finance.	11
Monitoring of the budgets of sub-national government (incl. assessment of fiscal rules)	9
Quantification of short-term and long-term budgetary effects of envisaged policy measures and reforms	9
Research in other macroeconomic issues.	9
Normative statements/recommendations regarding fiscal policy.	7
Production of macro-economic forecasts used for fiscal planning.	4
Production of budgetary forecasts.	4



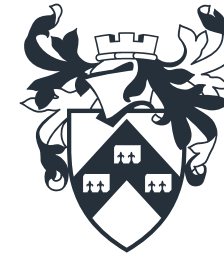
EU Independent Fiscal Institutions

MAKING A DIFFERENCE

Transparency in forecasting



Transparency in forecasting



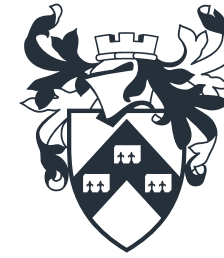
Strong legal backing

- **2011 Directive** on requirements for budgetary frameworks
- **2013 Regulation 473 of the 2 pack:** fiscal documents should be based on independent macroeconomic forecasts, and shall indicate whether the budgetary forecasts have been produced or endorsed by an independent body.

Relatively low resource intensity (in case of endorsement)

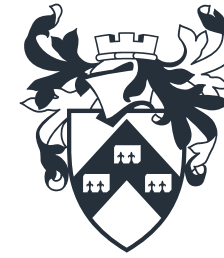
- Wide range of macro forecasts against which official forecasts can be evaluated
- Fairly standard statistical and econometric tools

Reducing information asymmetry



- Wide **dissemination policy of reports** and underlying technical info
- Efforts to **make documents accessible** to the general public
- **Institutional information** also published (annual reports, letters with MoF's, annual accounts)
- English versions: executive summaries at least
- Complemented with **active communication strategy**: press releases, briefings, interviews are frequent

Reducing information asymmetry



FR: publishing opinion on budget helpful for the Parliament.

CY: seminars for journalists resulting in better reporting on public finances.

SK: Eurostat changed the classification of important revenue items related to public enterprises.

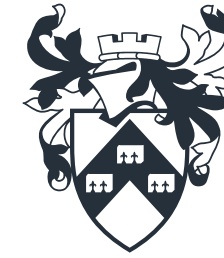
LT: improved reporting on disbursements from the budget programme “Funds for Unforeseen Events”.

ES: monthly data for the computation of the expenditure rule. Information on the methodologies and assumptions of official projections.

LU: IFI raised a debate on the appropriate level of the MTO.

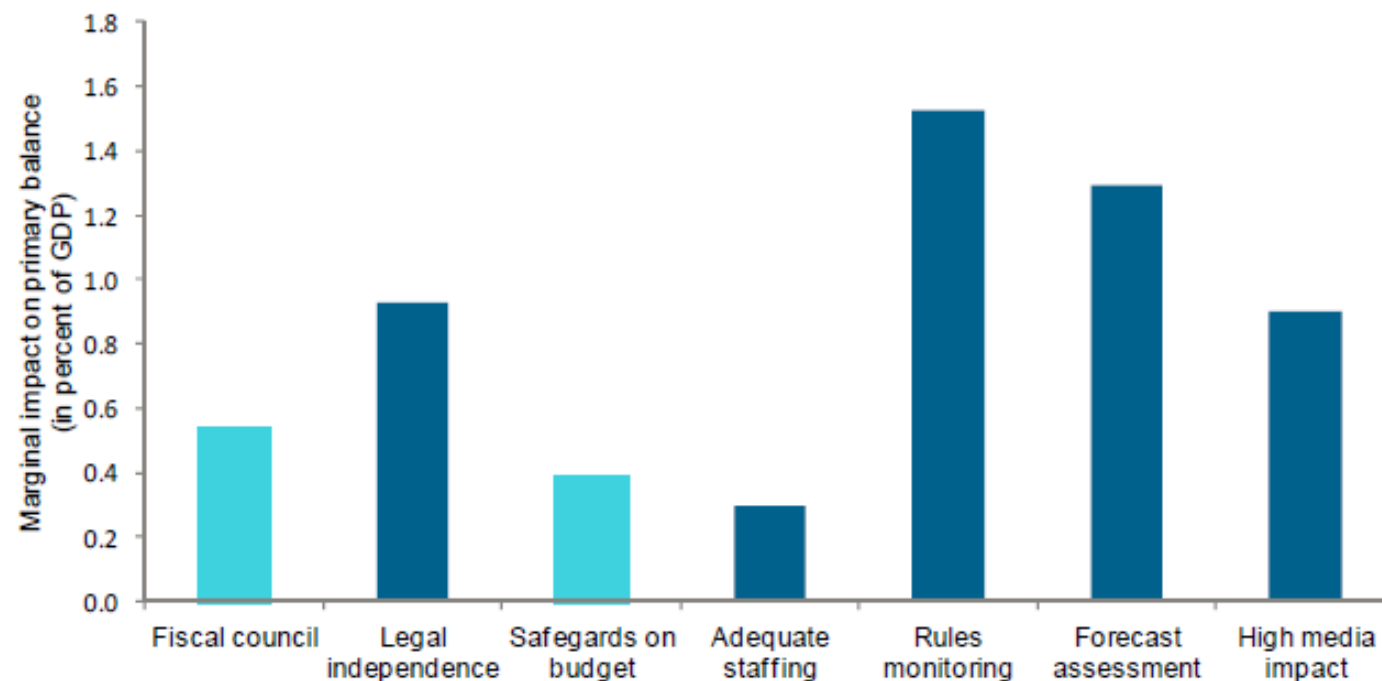
BG: MoF now publishes forecasts in a more transparent structure. Data for municipalities have become public.

IFIs and fiscal performance



IMF (2013): "The econometric analysis suggests that certain characteristics of fiscal councils are associated with stronger fiscal performance, but that the mere existence of a council is not."

Figure 8. Fiscal Councils and Fiscal Performance



Source: IMF staff estimates (Appendix I).

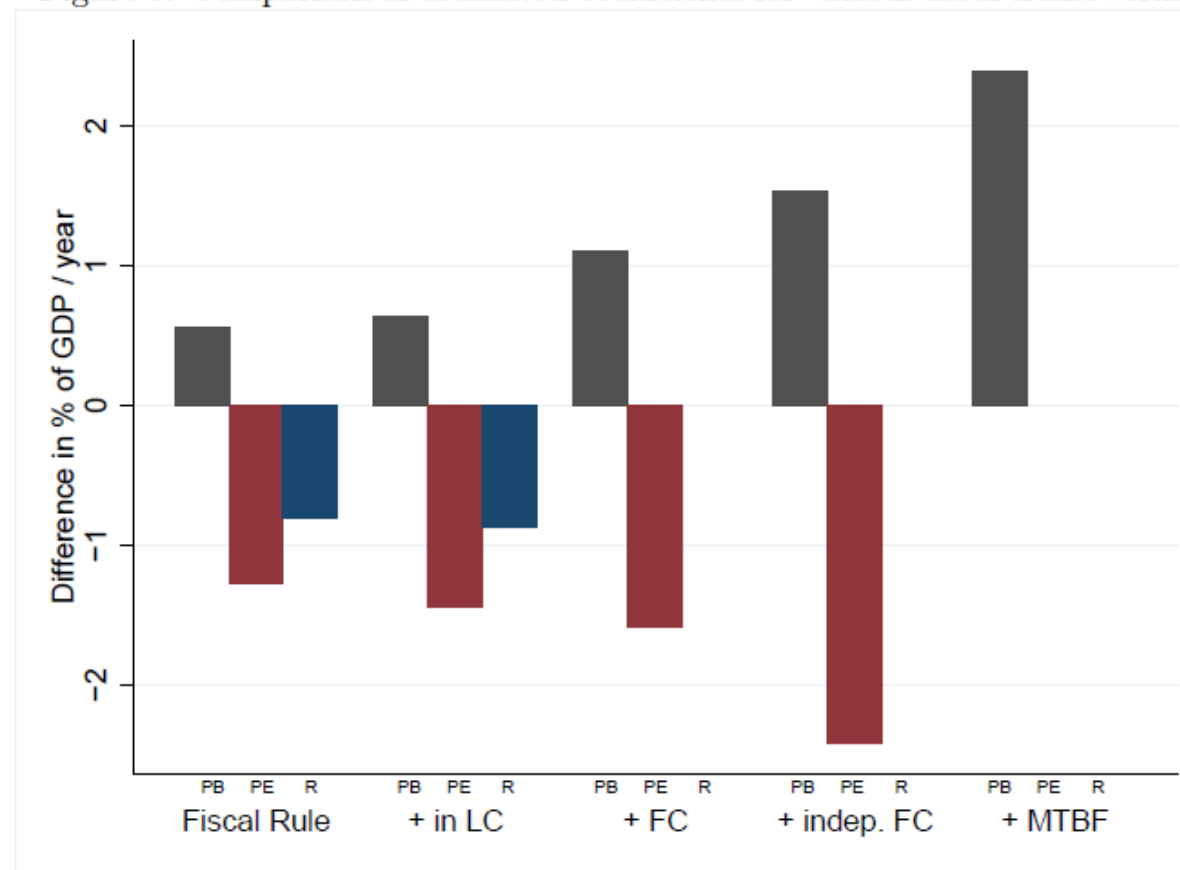
Note: light-colored bars indicate that the estimated marginal impact of the binary variable is not statistically different from zero.

IFIs and fiscal performance

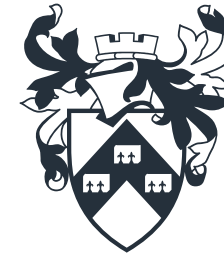


Nerlich and Reuter (2013): "We find strong support that numerical fiscal rules help to improve the primary balance, and that the budgetary impact can be further strengthened when supported by independent fiscal councils and an effective medium-term budgeting framework."

Figure 3: Comparison of estimated coefficients for various fiscal frameworks



IFIs and fiscal performance



FR: In 2015 and 2016 government did not answer to HCFP pointing out that structural adjustments were less than required by EU rules.

SK: government did not react to the identified significant deviation from targets in 2016

CY: Finance Ministry disagreed with IFI and COM figures, promoting methodological changes at EU level

ES: no reaction to deviations or risks of deviations from targets and requests for preventive or corrective action at the regional level



Challenges

RESOURCES AND STAKEHOLDER RELATIONS

IFIs as a litmus test



ARE GOVERNMENTS SERIOUS ABOUT TRANSPARENCY?

- To promote better fiscal policy through transparency, IFIs need
 - Financial and human resources
 - Information
 - Constructive dialogue with the executive
 - Links with parliamentarians
 - Effective communication with the public
- Some of these factors directly controlled by governments
- In practice, we observe a **continuum from “designed-to-work” to “designed-to-fail” IFIs**

IFIs as a litmus test

AN INDEX OF POTENTIAL EFFECTIVENESS



Horvath (2017): 'EU Independent Fiscal Institutions: An Assessment of Potential Effectiveness', *Journal of Common Market Studies* (forthcoming)

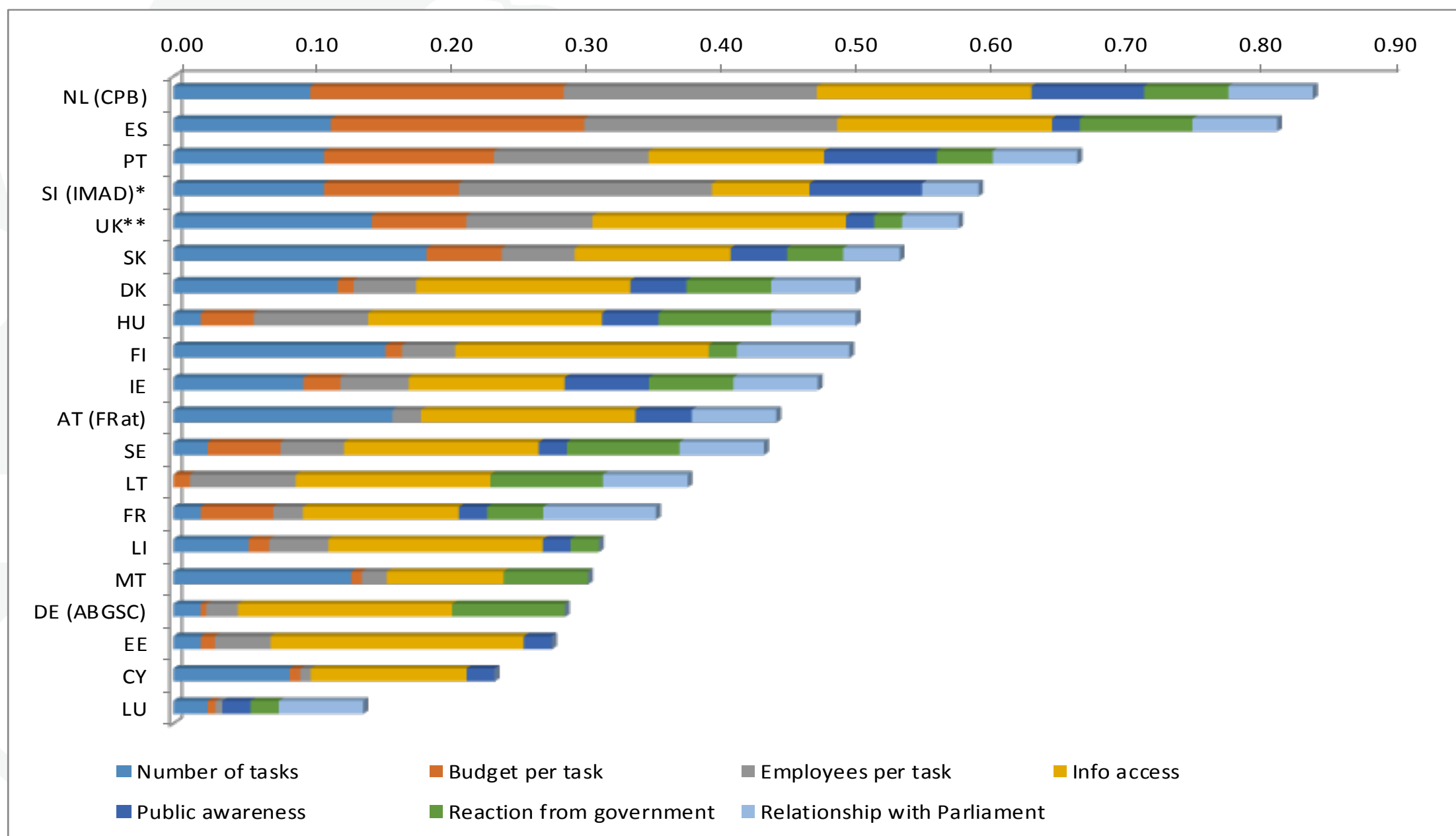
Measure	Weight
Breadth of mandate	75%
Financial resources	
Human resources	
Access to information	
Public awareness	25%
Reaction from government	
Relationship with parliament	

IFIs as a litmus test

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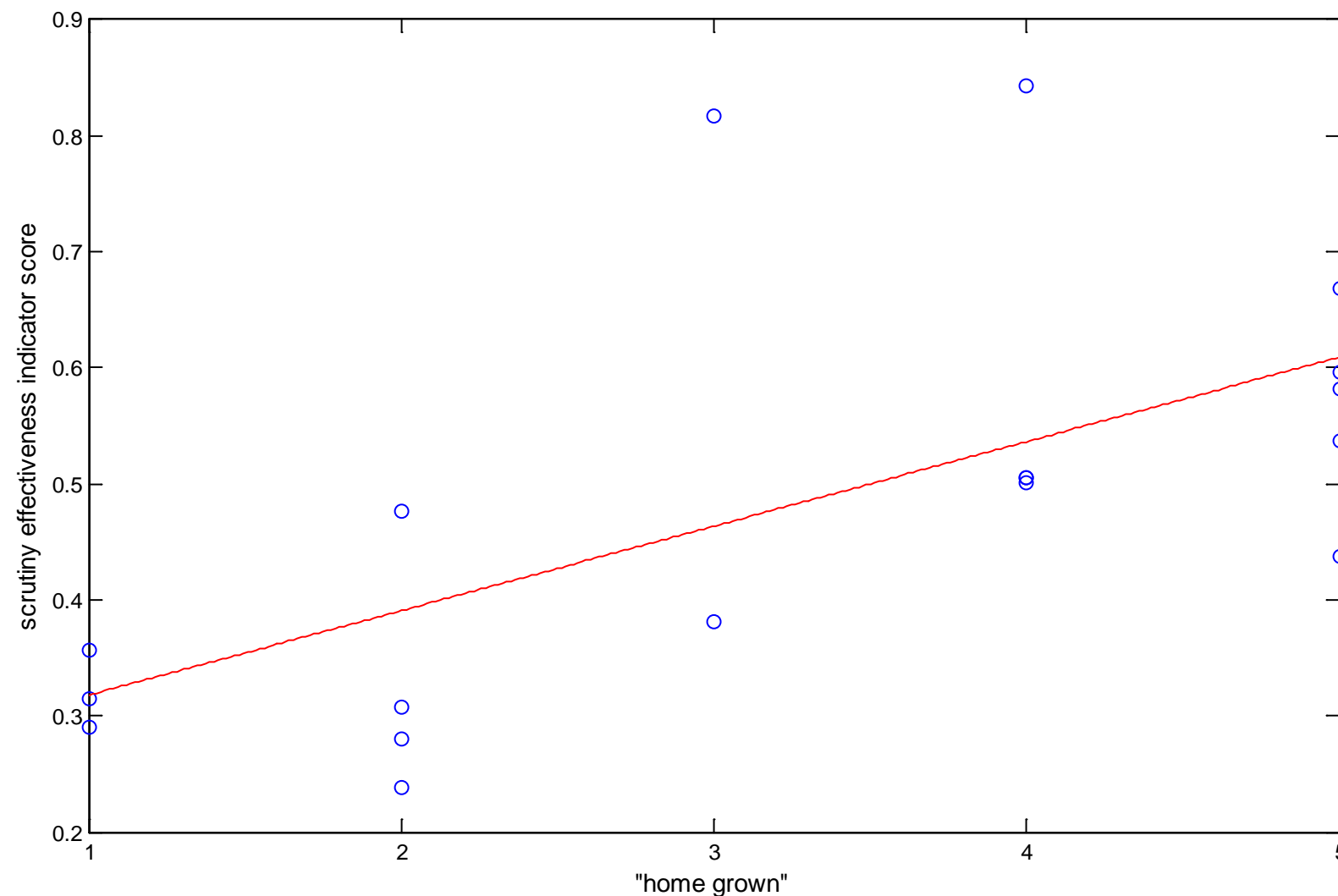


IFIs as a litmus test

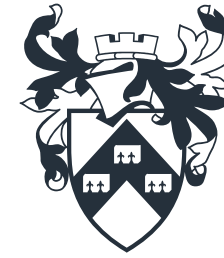


THE IMPORTANCE OF LOCAL OWNERSHIP

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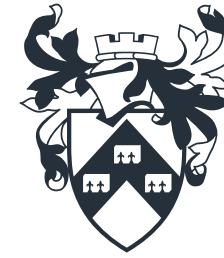
IFIs as a litmus test



EFFECTIVENESS OF COMPLY-OR-EXPLAIN MECHANISMS

- “Comply or explain” following recommendations
 - Envisaged in Fiscal Compact in relation with compliance with rules, IFIs tend to think more broadly
 - Exact implementation left to member states
- Potential approaches by governments
 - A. **Omission strategy:**
 - ❖ Silence in response to the report or direct communications
 - B. **Belligerence strategy:**
 - ❖ Limiting the scope of the recommendations by making the most restrictive interpretation of an IFIs mandate or the object of the report
 - C. **Evasive strategy:**
 - ❖ Stating neither an intention not to comply nor a general commitment to comply
 - D. **Actual application of the principle:**
 - ❖ Compliance within a reasonable time limit
 - ❖ Explanation of the reasons for departing from the recommendations

IFIs as a litmus test



EFFECTIVENESS OF COMPLY-OR-EXPLAIN MECHANISMS

‘not sufficiently detailed in the **legislation** or in any other documentation’

‘legislation does not detail the **content / extent of the response**’

‘[the law] does not specify any **consequences** for not publishing the opinion or for publishing it without any relevant information’

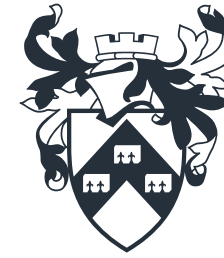
‘situations when the principle should be applied are well defined; less clear is the **timing**’



Concluding remarks

SUMMARY AND IMPLICATIONS

IFIs and transparency



- **IFIs and fiscal transparency go hand in hand**
 - IFIs exert influence through enhancing transparency
 - Executives serious about IFIs will set up an effective IFI (as well as reform their own institutions)
- Willingness to provide resources, information and to act as a **constructive partner to IFIs** is a good indicator of **how serious governments are about transparency**
- The EU **evidence on this is mixed** and there is room for
 - Defining and enforcing minimum standards
 - Peer pressure/support at the international level
 - More detail and formalisation on some “Anglo-Saxon” elements