



**EU INDEPENDENT  
FISCAL INSTITUTIONS**

# **EU FISCAL AND ECONOMIC GOVERNANCE REVIEW: A CONTRIBUTION FROM EU IFIS**

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23 NOVEMBER 2021

# BACKGROUND

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- **National independent fiscal institutions (IFIs) are independent official bodies with mandates to monitor and assess different aspects of fiscal policy.**
- The European Commission relaunched its **review of the economic and governance framework** in October 2021. It will consult the IFIs.
- **The Network of EU IFIs is an independent group** of 32 national IFIs that provides a platform to exchange views, expertise and pool resources in areas of common concern.

*This paper was prepared by the Secretariat of the Network of EU IFIs and an ad hoc Working Group of the Network of EU IFIs; the paper is published under the responsibility of the Leadership of the Network. It does not represent the views of each institution individually.*

# HOW CAN IFIs STRENGTHEN FISCAL GOVERNANCE?

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- IFIs can help to produce **more accurate and less biased** fiscal forecasts (Beetsma et al, 2018).
- By improving monitoring and transparency, IFIs can **improve compliance** with fiscal rules (Lledo, 2018).
- IFIs can help to make the case for **sound fiscal policies** (Beetsma et al. 2017) and to contribute to **deficit reduction** (Capraru et al, 2020).
- IFIs have an ability to **engage with the public** through national media (EC, 2021).

# WHAT DO IFIs BRING TO THE DEBATE?

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- National IFIs have substantial experience and expertise in **fiscal policy in EU countries** and in the **application of EU fiscal rules**.
- This paper draws on those experiences, knowledge of national conditions and our economic expertise as a contribution to the wider debate.
- This paper focusses on the **EU fiscal framework**.
- There are wider and fundamental questions around EU economic governance that are beyond the scope of the work of the Network of EU IFIs and the IFIs' mandates – these need to be addressed on a political level.

# KEY MESSAGES

- **The current EU governance framework suffers from weak compliance, procyclicality and excessive complexity.**
- **The fiscal governance framework that will be applicable as of 2023 needs to be clarified.**

Rules

- **A simple and transparent multi-year approach to enforceable numerical fiscal rules should be prioritised.**
- **The focus should be narrowed to fewer numerical rules, while detailed implementation should be streamlined.**

IFIs

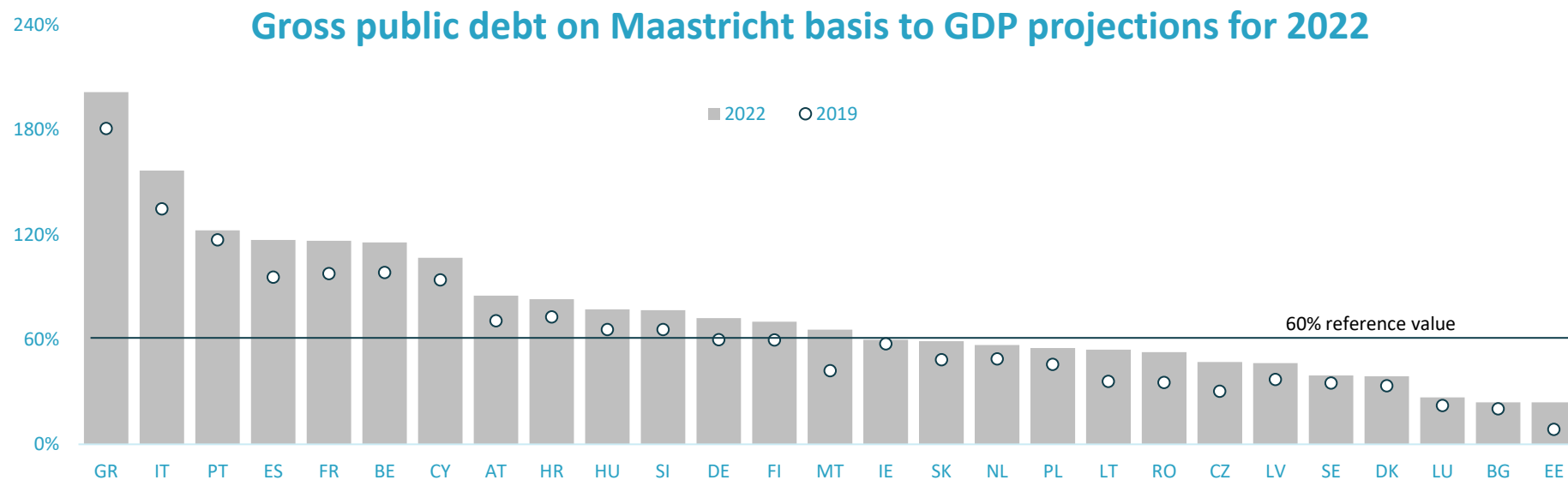
- **The role of national IFIs in supporting sound fiscal policy should be enhanced.**  
National IFIs are well-placed to carry out assessments of fiscal developments and sustainability at national level.
- **There should be an obligation on the EU institutions to take these assessments into account.**  
National IFIs should retain their independence, receive timely access to information and receive an adequate level of resources in order to continue providing objective assessments.
- **The effective functioning of IFIs should therefore be supported by minimum national framework standards in EU Member States. This may require a broadening of national IFI mandates in some cases.**

Statistics

- **Fiscal rules should be supported by better data and other information**

# CHALLENGES TO THE CURRENT FRAMEWORK

- Covid-19 pandemic has created new challenges for the EU fiscal framework
- There is a need to ensure **debt ratios are reduced** over time to safer levels, despite lower interest rates

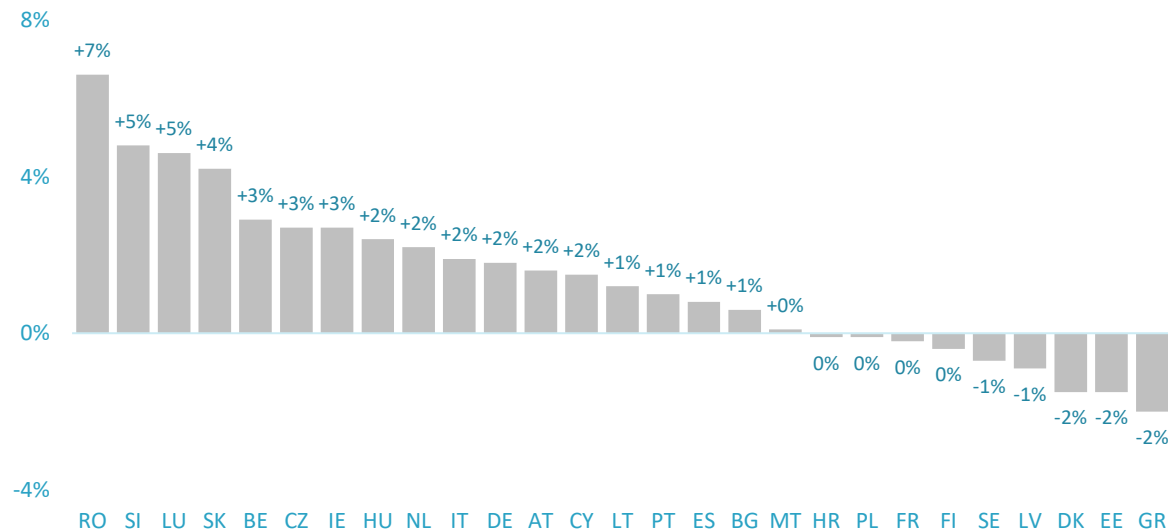


Source: 2021 Spring forecast ([EC, 2021](#))

# CHALLENGES TO THE CURRENT FRAMEWORK

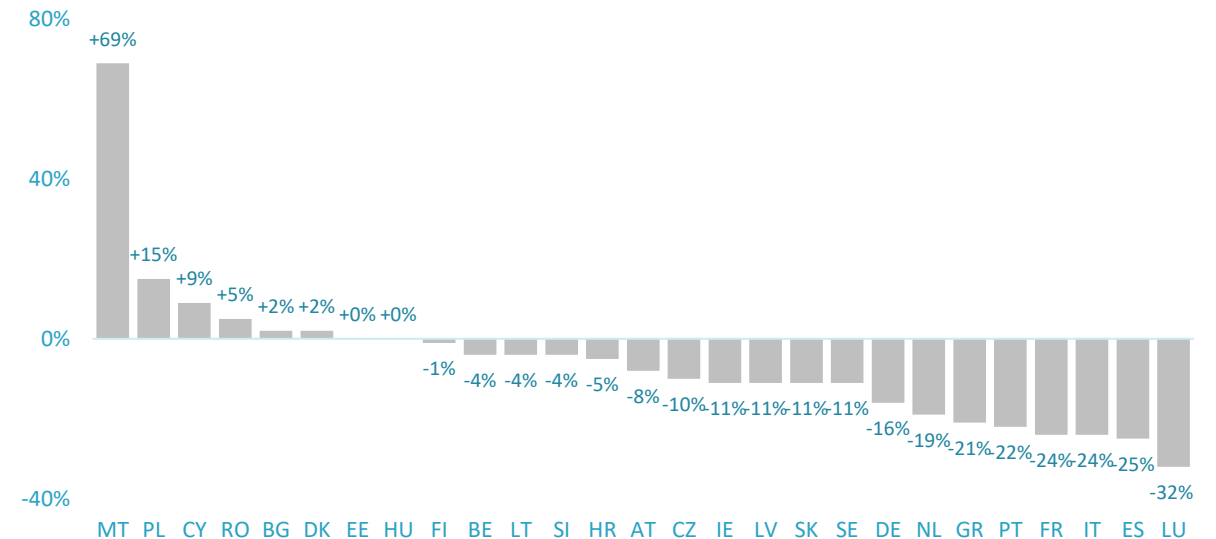
- There is a need to **raise productivity and achieve climate and social objectives**, in part by ensuring that adequate levels of public investment are undertaken to support these objectives

Total change in gross public pension expenditure over 2019-45 (%/pps of GDP)



Source: 2021 Ageing report (EC, 2021)

Change in national contribution to the EU target of 2030 final energy consumption reduction (% of 2005 targets)



Source: Economidou et al, 2020

# PROBLEMS WITH THE CURRENT FRAMEWORK

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- National fiscal policies should ensure long-run fiscal sustainability, while pursuing appropriate counter-cyclical policies and contributing to sustainable growth, social and climate objectives.
- While experience differs widely, weak outcomes in many countries:
  - **Government debt ratios have been rising** in recent decades, despite declining interest rates.
  - **Long-term fiscal pressures** have increased.
  - **Failure to run appropriate countercyclical policies** or to save sufficiently during economic expansions.
- Current fiscal framework suffers from 3 main problems:
  - **Weak compliance.**
  - **Procyclicality.**
  - **Excessive complexity.**



# DESIGN OF FUTURE FISCAL FRAMEWORK

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- The approach to the future EU fiscal framework in this paper is based on **three pillars**:



- **A new governance framework should be in place from 2023** once the General Escape Clause is deactivated.

# (1) FISCAL RULES

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- The Network does not take a position on the exact set-up of the EU fiscal rules.
- Numerical rules should remain core part of the overall framework but need to be better designed.

**Simpler**

**More  
transparent**

**Less  
procyclical**

**Multi-  
annual**

- The **complexity of the rules could be addressed** through:
  - reducing the number of rules that are the focus of enforcement.
  - streamlining details of existing rules.

# DIFFERENT APPROACHES

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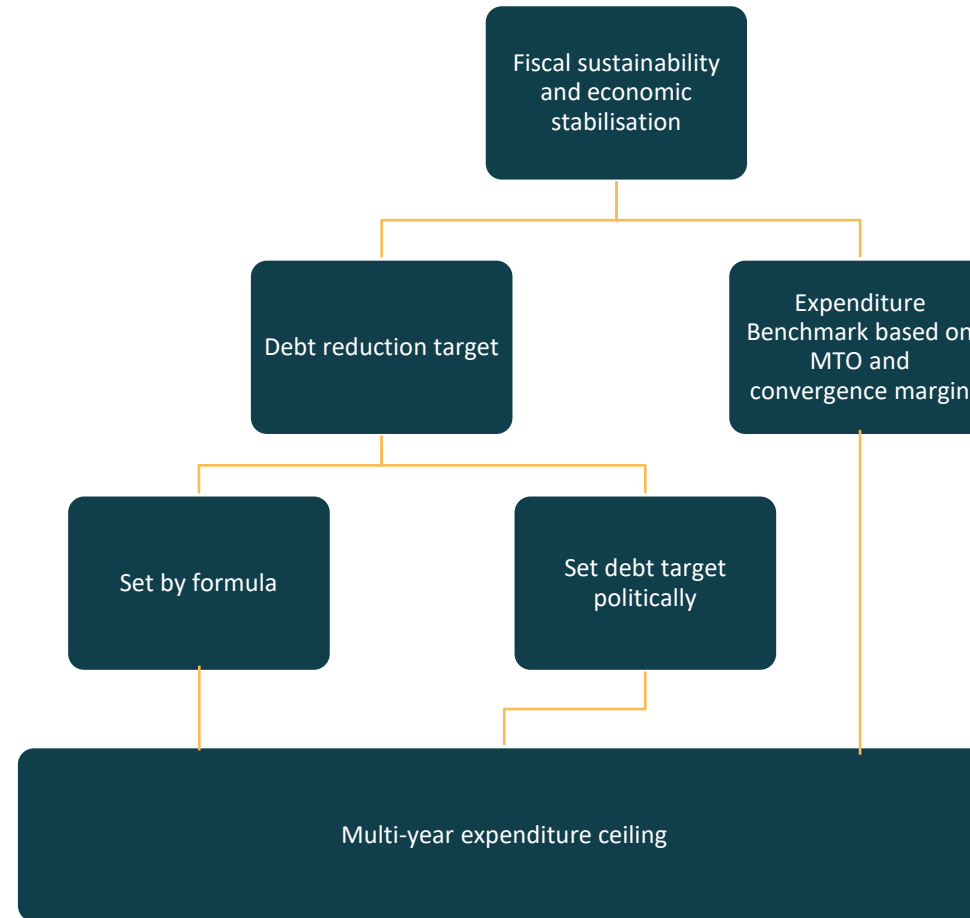
- **Two main approaches** have been proposed for future EU fiscal rules:
  - Debt anchor, expenditure ceiling.
  - Modifying the existing EU SGP framework.
- In theory, the two main proposed approaches can be viewed as two ways of **achieving a similar outcome for the public finances.**
- In practice, there may be **advantages and disadvantages** to how each functions and this will depend on **specific design features of their implementation.**

# DIFFERENT APPROACHES MAY CONVERGE

High-level goal

Intermediate goals

Operational goal



# WELL-DESIGNED MULTI-YEAR CEILINGS

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- **Multi-year expenditure ceilings** could help as operational requirement to achieve fiscal objectives.
- **Several design issues** must be considered in setting the expenditure ceiling:
  - Setting the medium-term **multi-annual** spending path.
  - Spending should be measured using a **modified measure** that allows to run steady budgetary policies without distortions due to one-off factors.
  - Accounting and variables used to determine the expenditure ceiling should be **harmonized**.
  - Spending should **adjust for discretionary revenue measures**.
  - Deviation from the rule should be allowed in **specific circumstances** (e.g. adjustment margin for overruns or a rainy-day fund) and subject to **oversight by IFIs**.

# REDUCING COMPLEXITY

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- **The number of rules that are the focus for enforcement could be reduced.**
- **The *interpretation* of the rules could be simplified and strengthened:**
  - “Investment” and “Structural Reform” clauses should be **conditioned on a full economic assessment** rather than numerical criteria only, including an assessment by the national IFI.
  - Key concepts (e.g. DRMs, one-offs, structural balance etc.) should be set out in a **simple way based on clear principles** and with examples, but without trying to cover every possibility.
  - **A single escape clause** could increase simplification and transparency of the current EU fiscal framework.
- **Surveillance of the compliance with the fiscal rules should also make more use of IFIs’ assessments of fiscal policy.**

# OTHER KEY RULES ISSUES


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- Investment may warrant **special treatment and recognition in the design of the rules**. The advantages and drawbacks of this would need to be carefully weighed.
- Rules should be **tested prior to the implementation** and implications of proposed rules should be fully developed based on current forecasts for all Member States.


# (2) THE ROLE OF IFIs SHOULD BE ENHANCED

- IFIs bring a detailed, objective understanding of national circumstances.
- Their roles include macroeconomic analysis and forecasting, budgetary analysis and projects; wider assessment of policy.
- Multiple studies point to substantial positive impacts of the EU IFIs on fiscal transparency and sustainability.


**LATEST IFIs PUBLICATIONS**



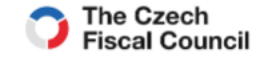
[The Austrian Fiskalrat's report on fiscal sustainability](#) provides an assessment of the long-run sustainability of the Austrian public finances. [Read here](#)




[The Spanish AIReF announced the addition of a new public spending evaluation division](#) which strengthens the institution's permanent review capabilities. [Read here](#)



[The Italian UPB's overview of public finance strategies in the 2021 Stability and Convergence Programmes of EU countries](#) compares public finance outcomes and strategies among the EU countries. [Read here](#)



[The Czech Fiscal Council's opinion concerning the development of public sector finances and the set-up of fiscal and budgetary policy](#) identifies risks and threats that may have an adverse impact on public budget stability. [Read here](#)



[The Dutch Raad van State's opinion on the 2022 Budget Memorandum and the 2021 September Report on Fiscal Monitoring](#) related to its mandate to provide independent fiscal monitoring. [Read here](#)



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# STRENGTHENING THE ROLE OF IFIs IN THE EU FRAMEWORK

There should be a **requirement** at EU level to take into account assessments in:

Assessment of **compliance** with national fiscal rules that mirror EU requirements.

Assessment of **specific measurement issues** (e.g. one-offs, DRMs, potential output, etc.).

Assessment of **fiscal sustainability** and the overall **fiscal position** on a regular basis.

However, EU institutions must remain responsible for their decisions and any potential conflict between the European Commission's and IFIs' assessments should be avoided.

National IFIs must retain their independence and have other roles.

# STRENGTHENING IFIs

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- **Minimum institutional requirements** for IFIs should be set:
  - Mandate to **address government** and parliament and to publicly disclose reports and recommendations.
  - Good and timely **access to information**.
  - **Effective implementation** of the “Comply or Explain” principle.
  - Adequate **level of resources** and management flexibility.
  - Sufficient **safeguards** to political pressures.

## (3) DATA AND OTHER INFORMATION

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- Member States should be required to produce **credible medium-term fiscal projections covering at least 4 years** in all national official macro-fiscal documents.
- Simplification, increased transparency and methodological improvements are required in the **assessment of output gap estimates**.
- **Improved treatment of “one-off” measures** (incl. more guidance on classification) to improve the monitoring of the underlying fiscal position.
- Better **measurement of the discretionary-revenue measures (DRMs)** to enhance fiscal monitoring.

# DATA AND OTHER INFORMATION

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- More transparency with regards to the **disbursement and usage of the EU funds**.
- Requirement to **produce debt sustainability analysis** at national level, either by governments subject to national IFI oversight or by national IFIs.
- **Net debt and net worth statistics** and projections should be measured and published to enhance the assessment of public debt stocks.
- **Gross and net financing needs** should be projected and published to enhance the assessment of public debt flows.

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# CONTACT US

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