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Institutional Reforms and Fiscal Adjustment

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18.1 Introduction

As current debt dynamics call for significant fiscal retrenchment over the medium term, present governments must credibly anchor future fiscal policy in some trajectory deemed consistent with a sustainable debt. Absent credibility, a vicious cycle of large frontloaded consolidations followed by financial market bets on the self-defeating nature of these adjustments is a real possibility (IMF 2012a). This is where a central lesson from the 2008 to 2009 crisis meets the precondition to a successful exit from crisis policies: sound fiscal governance must ensure that fiscal policy is predictable, stabilizing, and financially sustainable.

Clearly, the institutional arrangements governing fiscal policy prior to the crisis could not prevent some of the imbalances that magnified its effects. In particular, in many EU and euro area countries, fiscal buffers had not been built up as envisaged during the relatively prosperous pre-crisis years owing to weak implementation of the Stability and Growth Pact obligations. Exceptions were largely those EU countries that followed national fiscal rules that complemented the supranational rules. Outside the European Union, the disciplining role of fiscal institutions was also mixed, although pre-crisis institutional reforms had helped a number of emerging economies to create sufficient space to stabilize the economy.

Thus strengthening fiscal institutions has naturally emerged as an essential element to address the fiscal legacy of the crisis. This applies to governance reforms at the national level as well as the supranational level in the euro area and the EU, where implementation of the reformed Stability and Growth Pact is aimed to close the pre-crisis gaps. Outside the European Union, many countries have started or are considering reforms by anchoring fiscal policy over the medium term, strengthening budgetary planning, reporting, analysis, and execution, and improving risk management. In addition to specific measures in public financial management, reforms center on rules-based fiscal frameworks and nonpartisan fiscal agencies, which will be at the center of this chapter.

The rest of this chapter is structured as follows. Section 18.2 analyzes pre-crisis shortcomings of fiscal governance, in particular in the European Union. It also reviews the limits of fiscal institutions that were exposed by the crisis. Sections 18.3, 18.4, and 18.5 summarize key aspects of recent institutional reforms related to numerical fiscal rules, nonpartisan fiscal agencies, and major public financial management features, respectively. All three sections cover also governance reforms at the EU level. Section 18.6 concludes and summarizes several governance challenges.

18.2 Fiscal Institutions before and during the Crisis

We use the term fiscal institutions to designate processes or arrangements intended to favor the conduct of sound fiscal policies, through adequate constraints on policy discretion, including measures that enhance transparency and democratic accountability. At the macroeconomic level they aim at addressing the deficit and procyclicality biases that often affect discretionary fiscal policies. Two institutional approaches have frequently been advocated: the first approach sets policy boundaries, the second relies on self-discipline by raising transparency and reputational costs. In particular, fiscal rules impose long-lasting constraints through numerical limits on budgetary aggregates. External surveillance arrangements, including fiscal watchdog bodies, foster democratic accountability through analysis, information, and advice. These two approaches are increasingly used in combination. Effective implementation of fiscal rules is supported by sound public financial management systems, including reliable, comprehensive, and timely reporting systems, good forecasting and medium-term planning capacity (including through medium-term fiscal frameworks), top-down budgeting, and strong budget execution.[1]

In the past, institutional fiscal reforms often followed episodes of fiscal stress, allowing many of the countries that implemented such reforms to face the current crisis with better starting positions. As regards the adoption of national numerical fiscal rules, a first surge occurred in advanced economies in the early and mid-1990s. This was in part in response to bank and debt crises of the 1990s (e.g., Finland and Sweden) as well as consolidation needs to qualify for the euro area (e.g., Belgium). In emerging economies, fiscal rules spread from the early 2000s. Many adopted rules-based fiscal frameworks in response to experience with fiscal excesses and overhauled budget procedures, often reflected in the adoption of fiscal responsibility laws (e.g., Brazil, Colombia, Panama, Peru, and Sri Lanka). Before the crisis more emerging than advanced economies had national fiscal rules in place, often combined with relatively strong fiscal positions (figure 18.1).

Despite supranational budgetary limits, many EU countries entered the crisis with insufficient fiscal buffers. In the pre-crisis years, public finances improved in

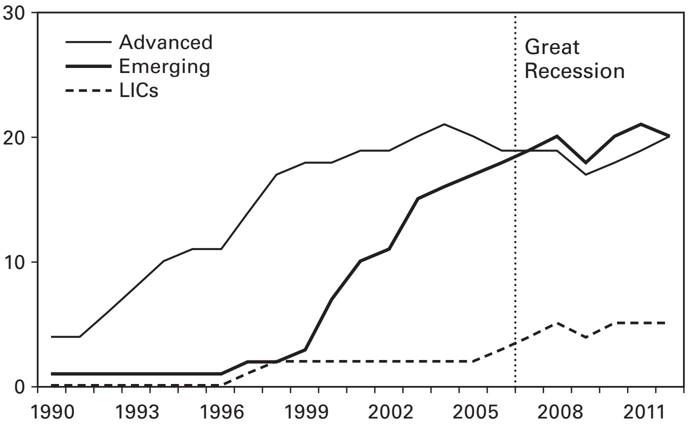

Figure 18.1
Number of countries with national fiscal rules. Based on fiscal rules in effect by end-March 2012.
Source: Schaechter et al. (2012)

most EU economies such that all excessive deficit procedures were abrogated (except in Hungary and the United Kingdom). However, these improvements came on the back of strong economic growth and asset price booms in some economies which pushed overall balances below the 3 percent deficit threshold, while structural deficits remained high in many economies and considerably above the country-specific medium-term budgetary objectives. The focus of the Stability and Growth Pact (SGP) on its corrective arm (the headline deficit limit) with no enforcement of the preventive arm (the structural deficit) and the debt limit, combined with a lack of governance and policy convergence outside the fiscal area, emerged as considerable weakness of EU fiscal governance which left many EU economies ill-prepared for the crisis. In contrast, EU countries with strong national rules in place fared better. For example, the Netherlands and the Nordic countries, with their traditions of rules-based medium-term fiscal policy-making, realized small structural deficits or surpluses on average in the six pre-crisis years and were among the few to meet their medium-term budgetary objectives (figure 18.2).

While financial markets did not differentiate euro area sovereign risk in the run up to the crisis, countries with stronger fiscal institutions—and especially fiscal policy rules—largely escaped the panic sell-offs that followed the Greek debt crisis. Although a careful econometric analysis would be required to identify causation, figure 18.3 depicts the dramatic contrast between the government bond yields in countries with strong national fiscal rules and those with weaker or no rules.

While rules can help anchor medium-term expectations, the crisis has exposed their limits when faced with extreme shocks. The ability to provide countercyclical

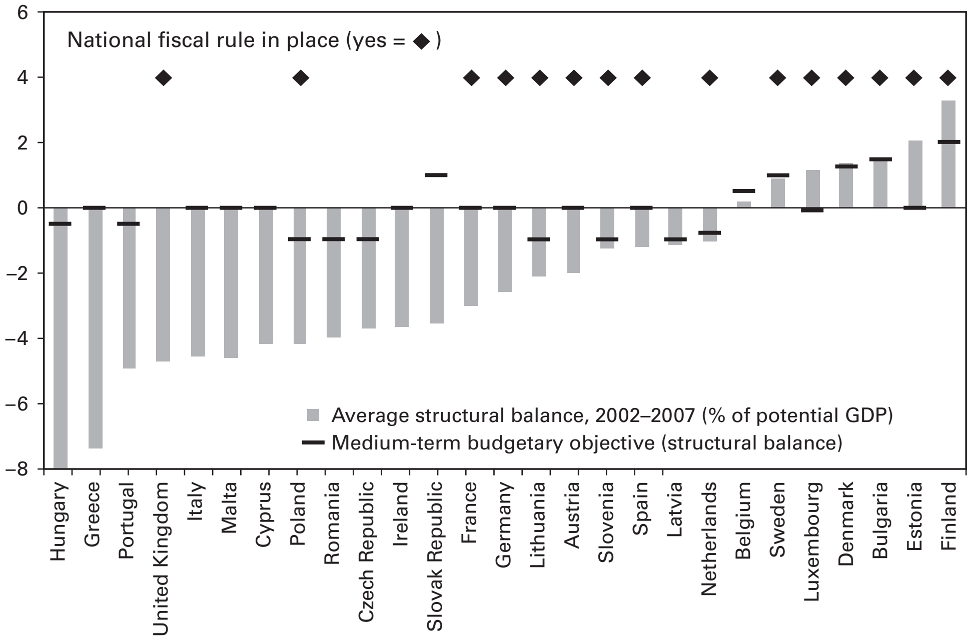

Figure 18.2
EU countries: Pre-crisis fiscal performance and national fiscal rules
Sources: IMF, *Fiscal Monitor*; IMF staff assessment

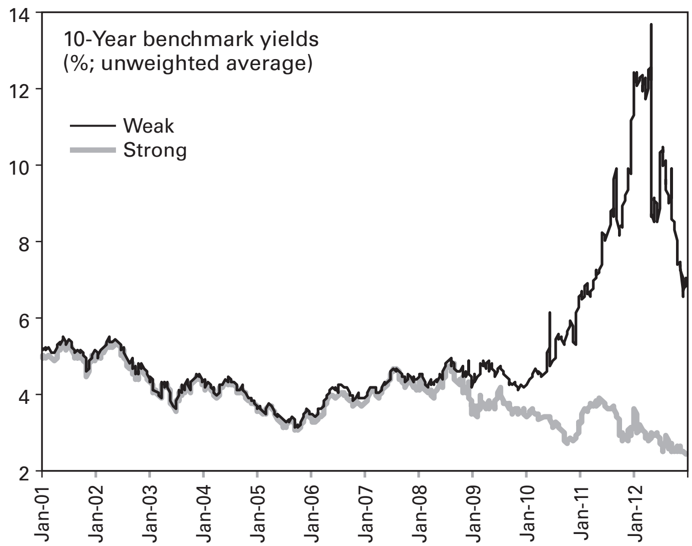

Figure 18.3
Euro area economies: Evolution of yields and strength of national fiscal rules. Countries classified as "strong" are those where the fiscal rule strength index from Schaechter et al. (2012) is above the pre-crisis (2007) median (Austria, Finland, France, Germany, Netherlands, and Spain); in countries classified as "weak" the index is below the median (Belgium, Greece, Ireland, Italy, Portugal, and Slovenia).
Sources: Bloomberg; IMF staff estimates

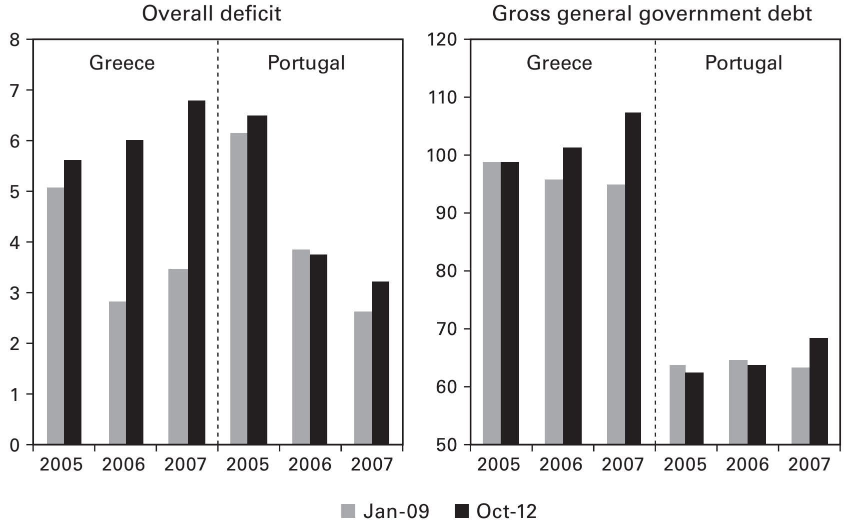

Figure 18.4
Revision of historical fiscal variables over time: Greece and Portugal (percent of GDP)
Sources: IMF, *World Economic Outlook*, January 2009 and October 2012

policy support within the rules-based framework was notable in those national rules that account for the cycle (e.g., Australia and Switzerland) or include escape clauses (e.g., Brazil and Spain). The supranational arrangements in monetary unions all have the option to extend the time frame for adjustment in case of deviations from the rule for the case of severe recessions. Most national rules, however, did not have this flexibility built in and were thus put into abeyance during the crisis. Experiences with formulating transition paths back to the rules' budgetary limits differ across countries, often linked to the capacity for formulating medium-term plans and the degree of economic uncertainty.

Other fiscal institutional weaknesses were revealed by the crisis. Reporting shortcomings led to significant upward revisions of key fiscal variables (figure 18.4). The Greek budget deficit for 2007 turned out to be nearly twice as large as reported earlier and was revised up from 3.5 percent (reported in January 2009) to 6.8 percent of GDP (in the October 2012 WEO). At the same time, accounting stratagems have sometimes been used to meet fiscal targets—thereby sidestepping the need for true adjustment (see Irwin 2012). Examples include currency swaps to hide a debt build-up (e.g., Greece), assumption of long-term pension obligations in exchange for short-term revenue (e.g., Portugal, Hungary, and other Eastern European countries), and use of public-private partnerships to defer the recognition of investment spending (e.g., Portugal).

Table 18.1
Type of recently adopted national fiscal rules since 2010

Type of rule	Countries
Budget balance rule[a]	Austria, Colombia, Croatia, Italy, Jamaica, Portugal, Serbia, Spain, United Kingdom
Pay-as-you-go rule[b]	Japan, United States
Debt rule	Croatia, Hungary, Serbia, Slovak Republic, Spain, United Kingdom
Expenditure rule	Croatia, Ecuador, France, Israel, Japan, Namibia, Poland, Romania, Russia, Spain, United States
Revenue rule	France

Sources: National authorities; IMF staff assessments.
Note: Rules include those that have been adopted but have not yet taken effect. See table 18.2 for more details.
a. All of these budget balance rules account for the economic cycle, except in Jamaica.
b. The pay-as-you-go rules are considered procedural rather than numerical rules and thus not counted in the dataset.

18.3 "Next-Generation" Fiscal Rules

18.3.1 National Fiscal Rules

Many countries adopted new rules or overhauled existing ones in response to the crisis (tables 18.1 and 18.2). Multiple motivations were typically behind these decisions: reassuring markets about the sustainability of fiscal policy and public finances; committing to and locking in sustained adjustment efforts; guiding expectations about the medium-term fiscal stance.

While many reforms concern European countries hardest hit by the crisis, the trend is broader as the below examples show (table 18.2).

- A few countries could build on their pre-crisis institutional reform efforts. Germany enshrined a structural budget balance rule in its constitution in 2009. After a transition period, starting in 2011, the structural deficit ceiling of 0.35 percent of GDP for the federal government will take full effect in 2016, and the states will need to maintain structurally balanced budgets from 2020. France sets binding multiyear expenditure ceilings and minimum targets for the net impact of new revenue measures legislated in its Multi-Year Public Finance Planning Act.
- Most other EU member states for which new rules already took effect are transition economies (Poland, Romania, and Slovakia), while others have adopted a transition period.

Table 18.2
New fiscal rules adopted since 2010

Country	Description of rules
Austria	Parliament passed in December 2011 an amendment to the federal budget law stipulating that, from 2017 onward, the structural deficit at the federal level (including social insurance) shall not exceed 0.35 percent of GDP. Operational details are still being prepared in separate laws and regulations. This includes a general government structural deficit limit of 0.45 percent of GDP (split into 0.35 percent of GDP for the federal level and 0.10 percent of GDP for states/municipalities).
Colombia	A structural budget balance rule for the central government was approved by Congress in June 2011. It sets a path that lowers the structural deficit to 2.3 percent of GDP by 2014 and provides a ceiling of 1 percent of GDP effective in 2022. The rule allows for fiscal expansion when the expected output growth rate is at least 2 percentage points lower than the long-term rate and creates a sovereign wealth fund.
Ecuador	A new expenditure rule was adopted in 2010 and took effect in 2011, but the existing budget balance and debt rules were dropped. The expenditure rule states that current expenditure cannot be higher than permanent income including oil revenue. External financing and oil revenues are to be used only to finance public investment.
France	The Multi-Year Public Finance Planning Act from December 2010 sets binding expenditure ceilings and minimum targets for the net impact of new revenue measures for 2011–14. It expands the ceilings from the 2009–12 framework and the "zero volume rule" for central government expenditure introduced in 2004.
Germany	A new structural balance rule (0.35 percent of GDP for the federal government and structurally balanced budgets for the Laender) was enshrined in the constitution in June 2009. After a transition period, starting in 2011, it will take full effect in 2016 for the federal government and 2020 for the states.
Hungary	A debt rule, included in the constitution, will come into effect in 2016 and require cutting the government debt-to-GDP ratio annually until it falls to below 50 percent of GDP. Debt reduction can be suspended when real GDP contracts.
Italy	A constitutional amendment was approved in April 2012 that introduces the principle of a balanced budget in structural terms with details and implementation principles to be specified in secondary legislation by end-February 2013.
Japan	The Fiscal Management Strategy, which includes a pay-as-you-go rule, was adopted in 2010 (by cabinet decision). The rule implies that any measure that involves increases in expenditure or decreases in revenue needs to be compensated for by permanent reductions in expenditures or permanent revenue-raising measures. A Medium-Term Fiscal Framework, including a limit on expenditure, was also introduced.[a]
Namibia	An expenditure rule took effect in 2010 that caps the ratio of expenditures to GDP at 30 percent.
Poland	A new expenditure rule (from 2011) limits the increase in central government discretionary spending and all newly enacted spending to 1 percent in real terms (based on consumer price index inflation) (defined in 2011 budget law).

(*continued*)

Table 18.2
(*continued*)

Country	Description of rules
Portugal	The new budgetary framework law (May 2011) approved a fiscal rule establishing that the general government structural balance cannot be less than the medium-term objective in the Stability and Growth Pact. It also includes requirements for a correction of the multiannual plan whenever deviations from the target occur. The rule will come into effect in 2015.
Romania	From 2010 general government expenditure growth should not exceed projected nominal GDP for three years until the budget balance is in surplus. Moreover, personnel expenditure limits are binding for two years.
Serbia	In October 2010, fiscal responsibility provisions were introduced in the budget system law from 2009. These include numerical fiscal rules and the adoption of a fiscal council. The fiscal rules comprise a budget balance rule that corrects for past deficit deviations and allows a partial operation of automatic fiscal stabilizers. A debt rule provides a ceiling on general government debt of 45 percent of GDP.
Slovak Republic	In December 2011, a constitutional bill was adopted, taking effect March 1, 2012, that caps public debt at 60 percent of GDP. Automatic adjustment mechanisms take effect when the debt-to-GDP ratio reaches 50 percent. The bill also calls for setting up a Fiscal Council to monitor and evaluate fiscal performance.
Spain	A constitutional amendment (2011) and its corresponding organic legislation (2012) require that the structural deficit for all levels of government stay within the limits set by the European Union, and set debt limits for each level of government. The rules will enter into force from 2020, with transition rules in effect until then. The amendment also introduces expenditure ceilings and constrains growth in expenditure for all levels of government.
United Kingdom	The new cyclically adjusted budget balance rule, from 2010, aims to achieve cyclically adjusted current balance by the end of the rolling five-year forecast period (currently by FY2016/17). The new debt rule (from 2010) targets a falling public sector net-debt-to-GDP ratio by FY 2015/16.
United States	Statutory pas-as-you-go rules for revenue and mandatory spending were reinstate in February 2010 but are subject to important exemptions. In August 2011, Congress enacted discretionary spending caps, saving about $900 billion over the next decade. If Congress does not take legislative action, additional spending cuts (sequesters) are scheduled to take effect from March 2013 to produce savings of roughly US$1.2 trillion over a decade, with one half coming from defense spending and the other half from domestic nondefense programs, excluding Social Security, Medicaid, parts of Medicare, and certain other entitlement programs.[a]

Source: National authorities; IMF staff assessment
a. The pay-as-you-go rules are considered to be procedural rather than numerical rules.

- In Spain the constitutional amendment of September 2011 and its corresponding organic legislation (2012) require that the structural deficit for all levels of government stay within the limits set by the European Union and set debt limits for each level of government. The rule will enter into force in 2020.
- Portugal's new budgetary framework law (May 2011) establishes that the structural budget balance cannot be less than the medium-term objective in the Stability and Growth Pact.
- Austria passed an amendment to the federal budget law stipulating that, from 2017 onward, the structural deficit at the federal level (including social insurance) shall not exceed 0.35 percent of GDP.
- Italy approved a constitutional amendment (April 2012) introducing the principle of a balanced budget in structural terms with details and implementation principles to be specified in secondary legislation by end-February 2013.
- Outside the European Union, for example, Colombia adopted a structural budget balance rule with a 1 percent of GDP deficit limit, taking effect in 2022. Serbia introduced balanced budget rules, which correct for past deficit deviations and allow for a partial operation of automatic fiscal stabilizers, and a debt ceiling.

These "next-generation" fiscal rules explicitly combine the sustainability objective with more flexibility to accommodate economic shocks. Following the examples of earlier adopted rules in Chile,[2] Germany, and Switzerland, many of the new rules set budget targets in structural terms (e.g., Austria, Colombia, Germany, Italy, Portugal, Spain, and Switzerland), cyclically adjusted terms (e.g., United Kingdom), or accounted for the cycle in other ways (e.g., Panama and Serbia); see figure 18.5. Some also correct automatically for past deviations with a view to avoiding the "ratcheting-up" effects of debt (e.g., Serbia, and the so-called debt brakes of the structural budget balance rules in Germany and Switzerland).[3] Others combine new expenditure rules with new or existing debt rules, thereby providing operational guidance as well as a link to debt sustainability (e.g., Poland).

At the same time the design features of fiscal rules are becoming more encompassing, and supporting arrangements are being strengthened. This includes, for example, enshrining rules in legislation (away from political agreements), adopting explicit escape clauses and provisions for the transition path in case of deviations, and formulating medium-term expenditure frameworks. This evolution is captured by the summary fiscal rules index presented in figure 18.6, which also accounts for the number of rules per country that increased since the crisis in advanced and emerging economies. Figure 18.7 shows the main driving forces: the use of supporting arrangements, in particular expenditure ceilings, independent monitoring of

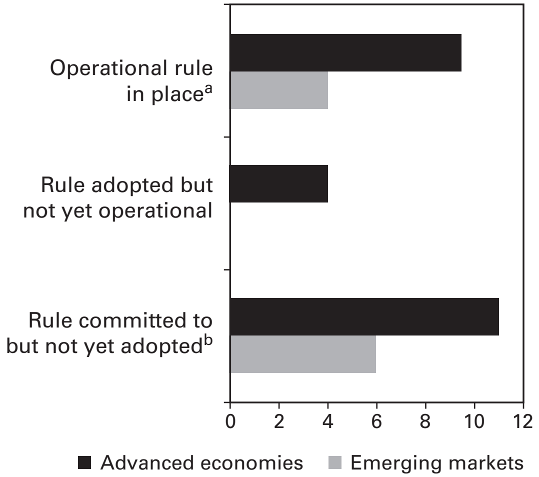

Figure 18.5
Number of countries with budget balance rules accounting for the cycle. (a) Includes countries with a clearly specified transition path. (b) Includes EU member states that have signed the Fiscal Compact but have not yet adopted a rule that accounts for the cycle.
Sources: National authorities; IMF staff assessments

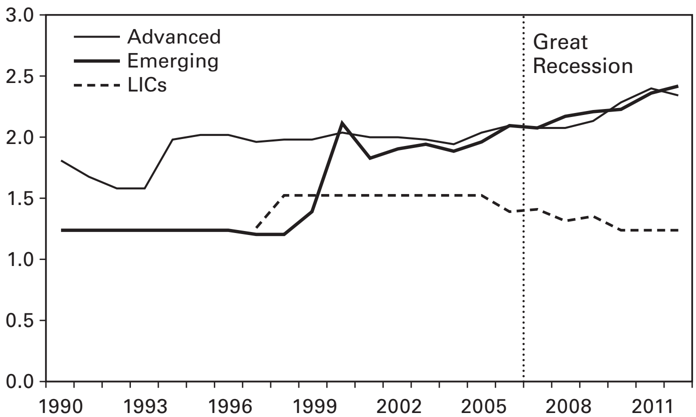

Figure 18.6
National fiscal rules index (index ranging from zero to five)
Source: Schaechter et al. (2012)

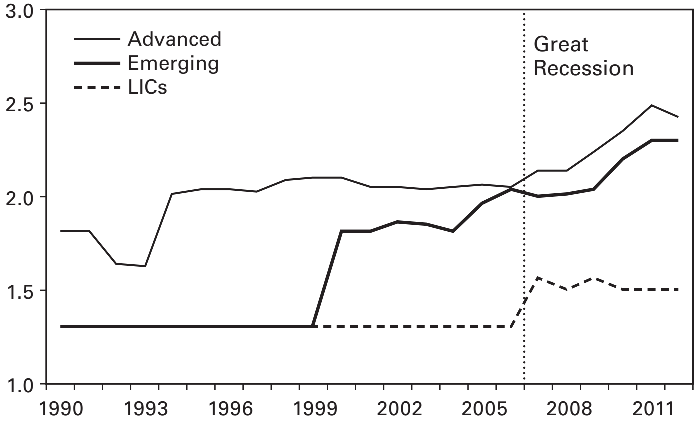

Figure 18.7
Fiscal rules sub-index: Supporting arrangements (index ranging from zero to five). Includes expenditure ceilings, fiscal responsibility laws, independent projections and monitoring.
Source: Schaechter et al. (2012)

rules, independent macroeconomic projections for budget assumptions, and fiscal responsibility legislation.

But the greater complexity of the rules frameworks also creates new challenges. The increased number of rules, their interaction, and sophistication can complicate implementation and make compliance more difficult to explain and monitor. To address the first challenge, several countries are reforming their budgetary procedures and medium-term budgetary framework (e.g., Austria, Greece, Ireland, and Portugal) (section 18.5). Nonpartisan fiscal agencies can potentially play an important role in dealing with the second challenge and a number of countries have set up, or adopted, plans for such institutions (see section 18.4).

18.3.2 Reforming the EU Fiscal Governance Framework

The European Union has taken steps to enhance both the prevention and management of sovereign debt crises. To reduce the main loopholes that were exposed by the crisis, governance reforms have focused on (1) setting more comprehensive limits on fiscal aggregates, (2) tightening enforcement at the national and supranational level, (3) improving coordination, (4) strengthening budgetary procedures, (5) enhancing transparency, and (6) broadening governance beyond the fiscal area. At the same time a crisis management apparatus was created with the EFSF and the ESM. These reforms are captured predominantly in the "six pack" of five new EU regulations and one EU directive, which took effect in December 2011, as well as an intergovernmental treaty signed in March 2012 (the Treaty on Stability, Coordination and

Governance in the Economic and Monetary Union), which incorporates broad guidance for the reform of national fiscal frameworks (the so-called Fiscal Compact; see European Commission 2012a), and the Treaty Establishing the European Stability Mechanism (signed in February 2012).

To foster greater fiscal discipline, in particular in good economic times, the array of numerical budget limits has been broadened (table 18.3). The reforms mandate the adoption in legislation of a national structural budget rule with a maximum deficit limit of 0.5 percent of GDP,[4] and give more prominence to debt and expenditure developments in supranational rules. First, in the corrective arm of the SGP, the debt criterion has been made operational. The failure to reduce the debt-to-GDP ratio by the benchmark 1/20th of the distance between the observed level and the 60 percent threshold on average for three consecutive years can now trigger an excessive deficit procedure even if the headline Maastricht deficit is below the 3 percent threshold. Second, in the preventive arm, expenditure growth is to be used alongside the structural budget balance to assess progress toward the medium-term budgetary objectives (MTOs). Specifically, countries exhibiting an annual growth of primary expenditure—excluding unemployment benefits and subtracting revenue discretionary increases—above long-term nominal GDP growth and therefore not making significant progress to reaching their MTOs can face financial sanctions and fines (for euro area members).

Several avenues have been pursued to tighten enforcement of the new commitments, though shortcomings remain. A key novelty is to give greater role to enforcing requirements at the national rather than the EU level. This is particularly reflected in the obligation to adopt nationally binding structural budget balance rules combined with legally enshrined automatic mechanisms for correcting deviations from the rule.[5] Moreover the most recent reform initiative ("two pack," enacted in May 2013) advocates the creation of independent bodies at the national level that would assess compliance with the rules and thereby raise reputational costs for deviations (see section 18.4 for more details). Enforcement at the supranational level has advanced by operationalizing the debt criterion and introducing new fines and sanctions in the preventive and corrective arms of the pact. These can be triggered more automatically as they would be proposed by the Commission and implemented unless a qualified Council majority blocks the proposal (so-called reverse qualified majority).

Broader policy coordination is now based on the "European semester" with enforcement procedures still to be established, however (figure 18.8). So far the key new element is a revised timetable that aims to allow assessing all macroeconomic developments and policies together. In addition to raising awareness of spillovers, the new procedure permits timely feedback for the preparation of national budgets. An ex ante peer review and recommendations, including on how to reduce macro-

Table 18.3
EU fiscal rules from Maastricht to the Fiscal Compact

Rules					Level of enforcement and legal basis	Action following violation[a]
Type	**Maastricht (SGP.1)**	**2005 Reform (SGP.2)**	**2011 "Six Pack" Reform (SGP.3)**	**Fiscal compact**		
Debt Rule	Debt/GDP is reduced to below 60 percent	→	Annual reduction in debt/ GDP equal to 1/20th of distance between current level and target	→	Maastricht Treaty	Excessive deficit procedure (Council's decision by qualified majority); fines and sanctions
Deficit Rule	Deficit/ GDP below 3 percent at any time	→	→	→	Maastricht Treaty	Excessivedeficit procedure (Council's decision by qualified majority); fines and sanctions
Structural Budget Balance Rule	Medium-term budget positions "close to balance or in surplus"	Structural deficit/ GDP to remain below 1 percent	→	. . . below 0.5 percent deficit	Stability and Growth Pact (SGP) regulations; National legislation (2014)	Fines and sanctions; European Court of Justice fines and National enforcement
Expenditure Rule			Primary expenditure (exclucing unemploy-ment benefits and tax discretionary increases) grows less than medium-term GDP	→	Stability and Growth Pact (SGP) regulations	Fines and sanctions

Source: Anderson et al. (2012)
Note: Sanctions typically refer to interest or non–interest-bearing deposits of 0.2 percent of GDP. Fines can range from 0.1 to 0.5 percent of GDP. They apply differently to euro area and non–euro area member states.

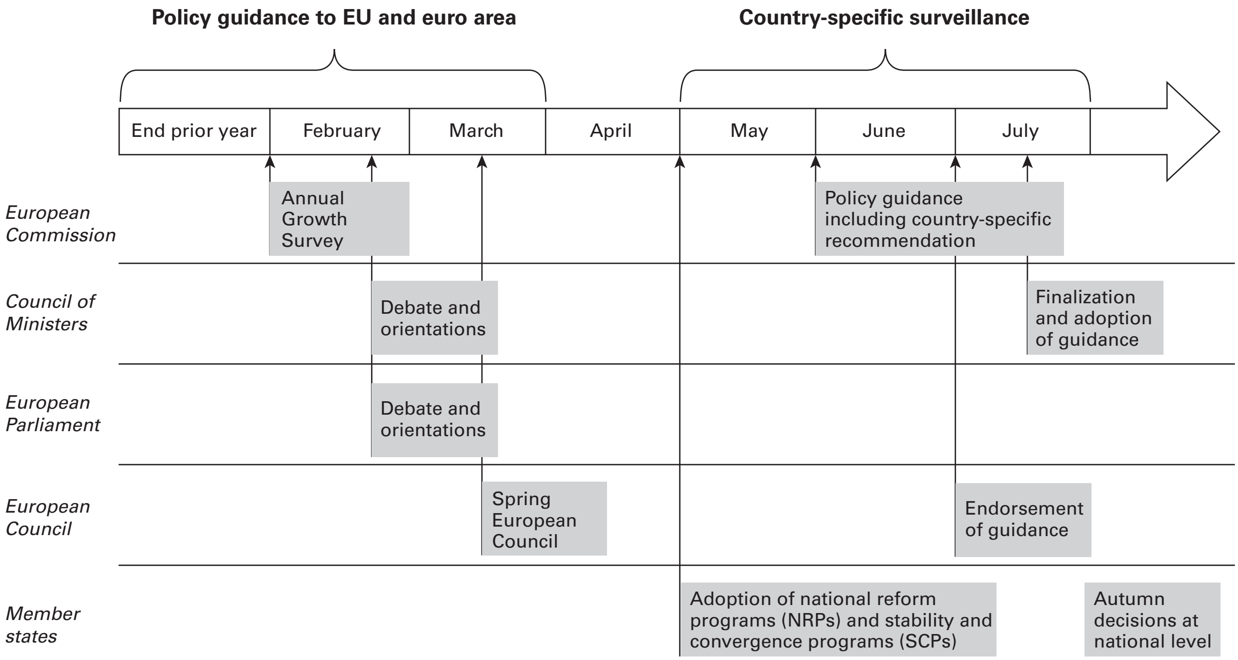

Figure 18.8
European semester
Source: European Commission

economic imbalances, financial sector issues, and growth-enhancing structural reforms, are however not binding at this stage. But the above-mentioned "two-pack" mandates also a common timetable to prepare national budgets, and, in case they are in noncompliance with the obligations of the Stability and Growth Pact, to allow the European Commission to request their revision.

A new excessive imbalances procedure (EIP) recognizes that unsustainable public debts may be rooted in nonfiscal problems. Macroeconomic imbalances, such as private sector financial excesses, may lead to sudden adjustments that result in the realization of implicit or contingent liabilities. The new surveillance mechanism aims to prevent and correct such divergences by establishing an alert system, consisting of a scoreboard of indicators and in-depth country studies, making country-specific recommendations for adjustments, and allowing for sanctions and fines in the case of noncompliance (European Commission 2012b). In the first assessment round in 2012, the European Commission found that 12 EU member states "experience macroeconomic imbalances, which are not excessive but need to be addressed."

With the European Stability Mechanism (ESM) a new crisis management institution has been created. The ESM essentially makes permanent the existing, strictly conditional assistance scheme (European Financial Stabilization Facility), expands its instruments (bond purchases in the primary market and direct recapitalization of banks under discussion), and links assistance to the adoption of stronger national fiscal rules. It will help prevent liquidity stress, including a potential degeneration into a full-blown solvency crisis through adverse market reactions.

These reforms are important steps to encourage fiscal responsibility and address any procyclical bent. A strengthened framework for fiscal rules, budgetary institutions, and crisis resolution mechanism should help prevent a recurrence of fiscal distress if the reforms are implemented coherently.

18.4 Nonpartisan Fiscal Agencies[6]

18.4.1 Rationale

Fiscal Authorities versus Fiscal Councils

Fiscal policy rules have historically been the institutional response of choice to the deficit and procyclical biases of discretionary policies. However, as documented in section 18.2, experience has revealed serious limitations related to three interdependent causes: the lack of political commitment (often reflected in weak budget procedures and controls), the rules' inflexibility in the face of adverse circumstances, and the absence of credible enforcement mechanisms. Typically weak commitment and procedures prevent the accumulation of sufficient buffers in good times, when a rigid rule (i.e., noncontingent on the state of the economy) does not bind. This makes the rule vulnerable to even a mild slowdown, when compliance would require procyclical adjustments that policy makers are reluctant to enact. Absent credible enforcement, the rule is ultimately circumvented, suspended or even eliminated. The European Council's decision to put the Stability and Growth Pact (SGP) in abeyance in November 2003 is a vivid illustration of this interaction between weak commitment, inflexible quantitative limits, and flawed enforcement. The subsequent reform of the SGP in 2005 largely addressed the inflexibility problem, but did not correspondingly strengthen enforcement procedures, undermining the effectiveness of the entire system (Beetsma and Debrun 2007) and sowing the seeds of the fiscal crisis experienced today in some euro area countries.

These difficulties have led some analysts to argue that other solutions should apply to eliminate fiscal policy biases. Since the mid-1990s, a number of academics have proposed to "depoliticize" certain dimensions of fiscal policy in the same way as monetary policy was delegated to unelected policy makers. Specifically, they argued that the authority to set the annual deficit or borrowing levels should be delegated to independent institutions with a clear mandate to devise a policy stance consistent with long-term debt sustainability and short-term macroeconomic stability (e.g., for a survey of the early literature, seeWyplosz 2005; Debrun, Hauner, and Kumar 2009). The limits set by those institutions would not only tie the hands of elected policy makers ex ante, but many proposals envisaged automatic adjustments in certain tax levers to ensure ex post compliance in case slippages occurred during the budget year (e.g., see Ball 1996; Blinder 1997; Eichengreen, Hausmann, and von Hagen 1999; Gruen 1997; Wren Lewis 2002).

The case for these Independent Fiscal Authorities (IFAs) has since been dismissed on both normative and positive grounds. From a normative angle, most aspects of fiscal policy are distributive in nature, which precludes delegation to unelected policy makers. This includes the deficit, which directly affects intergenerational equity. Alesina and Tabellini (2007) have formally modeled this generalization of the no-taxation-without-representation principle. From a positive perspective, the fact that fiscal biases are likely rooted in the genes of the political system—rather than in a pure time-inconsistency problem—implies that the system itself cannot credibly delegate fiscal policy to an IFA. The problem is indeed fundamentally different from that of delegating monetary policy to independent central banks because, in that case, elected policy makers fully understand ex ante the benefits of low inflation and the futility of exploiting the Phillips curve to lower structural unemployment (Debrun 2011).[7]

Experience in a handful of advanced economies suggests that another class of independent fiscal institutions could still play a role in promoting more sustainable and more stabilizing fiscal policies even if no policy-making power is delegated to them. These "fiscal councils," as they are best known, would influence the conduct of fiscal policy through independent analysis, assessments, forecasts, and possibly, recommendations driven by well-specified objectives set by elected policy makers.

Effectiveness of Fiscal Councils

The effectiveness of fiscal councils depends on two main transmission channels. The first is increased transparency fostering democratic accountability. By raising voters' awareness about the consequences of certain policy paths, a fiscal council could help them reward desirable options and sanction bad ones, effectively encouraging policy makers to deliver more viable and more countercyclical policies. One could even envisage a more direct contribution of these councils to democratic accountability by providing nonpartisan analyses of electoral platforms, as in the Netherlands (see Bos and Teulings 2011), Australia, and to some extent the United States, where the Congressional Budget Office evaluates the impact of major policy proposals. The second channel is direct inputs to the budget process, including the provision of unbiased macroeconomic and budgetary forecasts, and the costing of individual legislation tabled in parliament.

Proponents of fiscal councils are often keen to emphasize that these bodies could help shape an adequate policy response in practically any circumstances without risking the loss of the fiscal anchor that the demise of a rigid rule could entail. Hence an effective fiscal council could significantly relax the trade-off between credibility and flexibility central to the determination of the desirable pace of fiscal adjustment.

A natural question is whether a fiscal council should be viewed as a substitute for or as a complement to rules. There are at least two reasons to consider that fiscal councils may not necessarily be perfect substitutes for rules. First, the effectiveness of these institutions critically depends on the way the public debate constrains fiscal discretion, which is itself highly contingent on fundamental features of a country's political system, including the intensity of checks and balances between the executive and the legislative branches, and the type of electoral rule in place (proportional vs. majority voting). Second, the design of any incentive scheme—be it a rule or a fiscal agency—aimed at discouraging undesirable policies has to balance the space given to the proper exercise of policy discretion with the need to ultimately impose binding constraints when discretion is misused (Beetsma and Debrun 2007). Given that trade-off, exclusive reliance on a fiscal agency would point to establishing an agency that could in well-specified circumstances supersede elected policy makers. Such a council would arguably be too close to an IFA for comfort.

When fiscal rules are already in place or envisaged, it might therefore be worth exploring how a fiscal council could work with rules rather than how it could replace them. Specifically, a council could ease the enforcement of the more sophisticated fiscal rules described in section 18.3 by contributing to a better balance between flexibility and binding constraints on policy. We can think of three ways this could work. First, through continuous monitoring and analysis, the fiscal council could issue early warnings that compliance with the rule might be at risk. These could be particularly useful in good times, when confusion between permanent and transitory revenue gains may feed complacency and hamper a sufficient build-up of fiscal buffers, even if the rule sets quantitative limits in structural terms. Second, mandating a fiscal council to produce independent macroeconomic and revenue forecasts and to score policy initiatives could lessen the risk of optimistic bias in budget assumptions. This would reduce the likelihood that plans compliant with the rules systematically lead to outcomes at odds with them (Beetsma et al. 2011; Frankel and Schreger 2012). Third, a fiscal council could play a direct role in the enforcement of a rule through the formulation of a motivated opinion about the activation of an escape clause, or the calculation of fiscal indicators particularly vulnerable to manipulations, such as the structural budget balance. Finally, one should also note that the complementarity between rules and councils goes both ways: a simple and transparent fiscal rule can facilitate the council's work by providing an unambiguous and easily monitorable benchmark for assessing fiscal performance (Debrun, Hauner, and Kumar 2009).

Contributing to the implementation of fiscal rules is central to the remit of most existing fiscal council (see below) as well as of many academic proposals (e.g., Fatás et al. 2003; European Commission 2004; Ubide 2004; Jonung and Larch 2006). In the European Union, the Fiscal Compact assumes (Article 3, par. 2) that independent agencies will monitor compliance with national fiscal policy rules in each euro area member state, as now mandated by the "two pack".

In the remainder of this section, we clarify the concept of fiscal council, and map existing fiscal councils along a number of key aspects of their remit, tasks and institutional form.

18.4.2 Fiscal Councils in Practice

What Qualifies as a Fiscal Council?

In principle, any organization seeking to inform the public and foster the quality of the public debate on fiscal policy in a nonpartisan way could fit the concept of a fiscal council as discussed above. This includes specialized think tanks or research institutes—for example, the Institute for Fiscal Studies in the United Kingdom, or the Austrian Institute of Economic Research (WIFO) in Austria.

However, the literature generally focuses on a much narrower set of institutions. First, only institutions with an official mandate from elected policy makers qualify as fiscal councils. The existence of a mandate is more likely to generate significant reputational costs when the council has to report and comment on undesirable policy developments or bias. In principle, an official mandate also implies public funding commensurate to the tasks of the council and some form of legal guarantee against partisan influence. Thus the mandate criterion excludes private bodies, such as think tanks and self-proclaimed watchdogs or whistle-blowers. Intergovernmental agencies are also excluded. Their surveillance responsibilities are arguably too broad to generate the large reputational effects a national body with a well-defined remit can deliver; they lack the local anchorage and the deep understanding of political customs needed to effectively influence the national policy debate through continuous interaction with policy makers and the media; and last but not least, they are not expected to fully internalize the country-specific preferences regarding the objectives assigned to fiscal policy and therefore cannot be held accountable before national parliaments. In sum, the official mandate criterion crystallizes the full ownership of the institution required to effectively shape the national public debate and foster accountability, a point theorized by Debrun (2011) and emphasized by Kopits (2011) as part of best practice.

Also audit institutions are generally not considered as fiscal councils. Although they contribute to democratic accountability and transparency, their approach is in most cases backward-looking and legalistic, as opposed to the mostly forward-looking and economic work of fiscal councils. That said, some audit bodies perform tasks that are of a prospective and economic nature—the French *Cour des Comptes* is a case in point. One potential problem with that approach is that ex ante assessments are likely to constrain ex post analyses. For instance, if the audit body was tasked to assess the costs and economic impact of budget plans and policies, reputational concerns would likely taint the ex post evaluation of these policies, especially if they ended up having unforeseen consequences.

The question as to whether strict formal guarantees against any type of interference by elected officials must exist to qualify as a fiscal council is less clear-cut than in the case of central banks. Experience with long-standing watchdogs is that incomplete *de jure* independence does not exclude considerable *de facto* autonomy. Since fiscal councils are not expected to impose binding constraints on policy choices, the immediate reward for politicians to interfere with their activity is unclear. Of course, de facto independence is unlikely to survive repeated and public divergences of views between elected officials and the fiscal council, especially if the latter has some leverage on the conduct of fiscal policy through high-impact normative analysis and recommendations, or the provision of forecasts. The experience with the High Council of Finance (HCF) in Belgium is very telling in that respect (Coene and Langenus 2011).

In the remainder of this section, we review key features of actual institutions that have been commonly classified as fiscal councils. We identified 24 councils in 22 countries (Belgium and Slovenia have two separate fiscal councils, according to our definition), most of them in Europe. The sample includes two defunct institutions: the original Hungarian Fiscal Council and the Parliamentary Budget Office of Georgia. As Debrun and Takahashi (2011), we distinguish between the "veterans" and the new generation of fiscal councils.

Role and Main Features: Veterans and the New Generation[8]

The universe of institutions qualifying as fiscal councils is limited, albeit expanding rapidly (figure 18.9). Nonetheless, the population of fiscal councils is also extraordinarily diverse, making it difficult to establish robust trends that would point to obvious best practice. As a first step, it is useful to distinguish between veteran institutions with a well-established reputation and newcomers with little or no track record. In 1960, only two fiscal councils were in operation; Belgium's High Council of Finance, created in 1936 to advise the Ministry of Finance, and the Dutch Central Planning Bureau, established in 1945 to provide forecasts and economic analysis supporting the design of fiscal policy. By 1995, only six new fiscal councils had

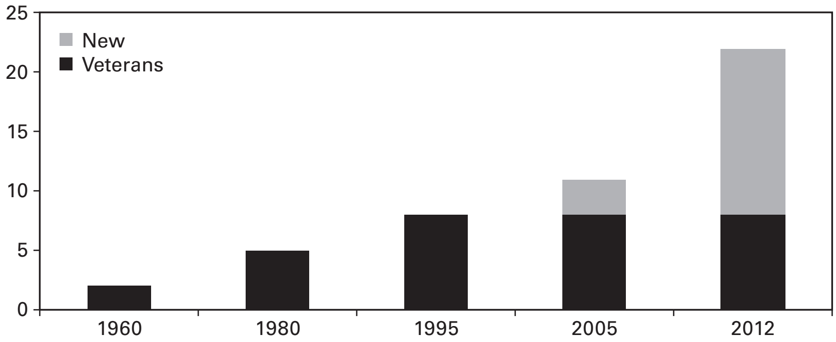

Figure 18.9
Number of active fiscal councils
Source: IMF staff assessment based on publicly available information

emerged, including those in Denmark, Germany, and the United States—the Congressional Budget Office, created in 1974. The number of fiscal councils then doubled between 2005 and 2012 to reach 22 active institutions at the time of writing. These new institutions include the Swedish Fiscal Policy Council, the United Kingdom's Office for Budget Responsibility, the Parliamentary Budget Offices in Australia and Canada, and other fiscal councils in Portugal, Ireland, and emerging Europe (Bosnia-Herzegovina, Hungary, Romania, Serbia, the Slovak Republic, and Slovenia). Overall, only two fiscal councils were dismantled (Georgia in 2008) or reduced to insignificance (Hungary in 2010).

The distinction between veterans and newcomers is useful because the design of new institutions could have been influenced by the intensifying academic debate on their potential role in improving the conduct of fiscal policy (with the most prominent contributions by von Hagen and Harden 1995; Eichengreen, Hausmann and von Hagen 1999; Calmfors 2003; Fatás et al. 2003; Wyplosz 2005) and by the experience with politically independent agencies in other policy areas such as central banking or the regulation and supervision of specific sectors (banking, energy, and media). Based on publicly available information, a few notable differences emerge between the two groups.

Looking at the remit, all the fiscal councils are mandated to provide nonpartisan positive assessments of fiscal policy (figure 18.10). A large majority of them are also required to analyze long-term sustainability and to either assess the quality of macroeconomic and/or budgetary forecasts, or to prepare such forecasts themselves. However, only a few countries (Belgium, the Netherlands, and Slovenia) generally (or are obliged to) use these forecasts for budget preparation.[9] Only a minority of fiscal councils is expected to provide normative assessments and policy recommen-

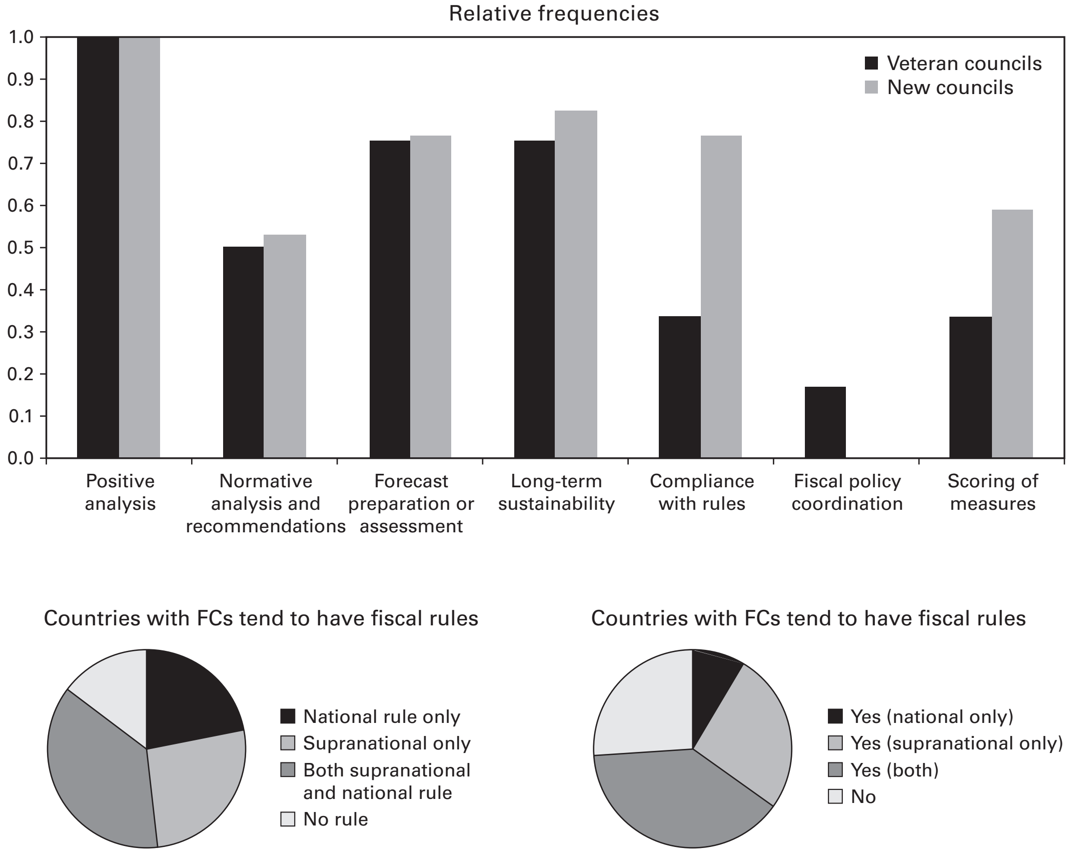

Figure 18.10
Tasks of fiscal councils
Source: IMF staff assessment based on publicly available information

dations (regardless of the group), and fiscal councils are rarely involved in coordinating policy among government entities. Newly established councils are more often mandated to score specific policy initiatives than the veteran agencies, perhaps reflecting a growing awareness of the importance of transparency in policy-making. And in contrast to veterans, new institutions are also more frequently tasked to monitor compliance with national or supranational fiscal policy rules, pointing to a growing perception that rules and councils are complements rather than substitutes, as discussed above. The mid and lower panels of figure 18.10 confirm that most countries with fiscal councils have fiscal rules and that among that subgroup, about three-quarters of fiscal councils monitor compliance.

The channels through which councils can influence fiscal performance vary widely, ranging from informal or technical advice to public communications and formal procedures specifically aimed at magnifying the reputational and political costs of deviations from ex-ante commitments. In line with theory, which rules out delegation and direct constraints on discretion, relatively "soft" channels of influence—public reports, analyses, communication—seem preferred to "harder" channels whereby the council's activity creates an obligation for the government, including requiring public explanations of policy slippages or biased forecasts, the compulsory use of council's projections for budget preparation, and the possibility for the council to access elected representatives through formal hearings in Parliament. The latter feature is more prominent in recent councils, possibly to compensate for the lack of pre-existing reputation and the correspondingly lower visibility of (and lesser public trust in) their work. Indeed, veteran councils generally enjoy significant media impact which helps them influence the public debate on fiscal policy (figure 18.11).

Still reflecting a revealed preference for soft influence, the new councils are rarely tasked to provide binding forecasts for budget preparation and governments are in general not compelled to formally respond to the council's assessments. Of course, such an obligation need not be enshrined in law and can emerge spontaneously, as the council's work progressively gains traction in the public. It is important to note

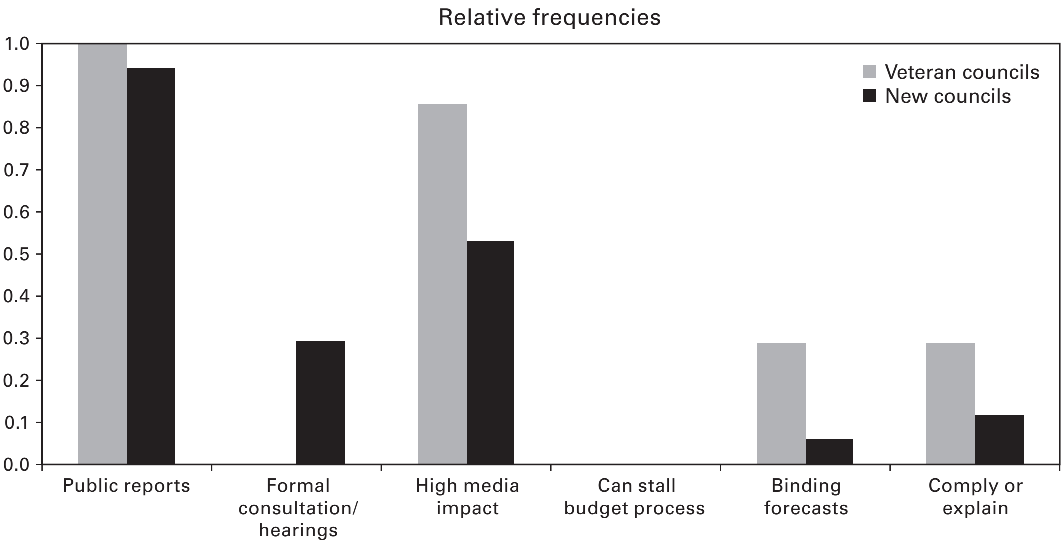

Figure 18.11
Fiscal councils' channels of influence
Source: IMF staff assessment based on publicly available information

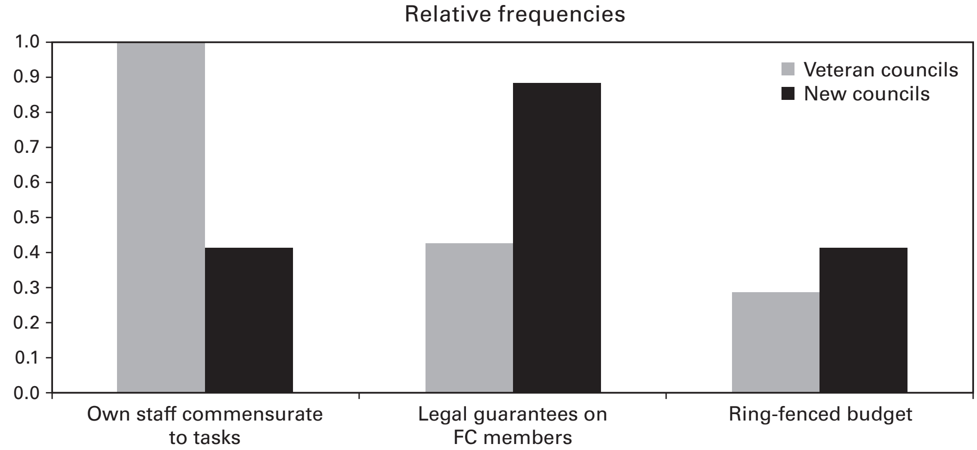

Figure 18.12
Fiscal councils: Determinants of independence
Source: IMF staff assessment based on publicly available information

that no fiscal council is allowed to block the budget process in case a draft budget violates objectives or constraints the council is mandated to monitor.[10]

Turning to the degree of political and operational independence, three dimensions are relevant: (1) legal guarantees similar to those in place for central banks (e.g., long, nonrenewable tenures for the council's management, prohibition of political activities prior to the appointment), (2) the appointment and retention of professional staff commensurate in skills and number to the tasks of the council, and (3) secured financing (figure 18.12). The latter dimension is particularly important because, unlike central banks, fiscal councils cannot generate significant own income. And it is through financial starvation that certain governments—most egregiously in Hungary—have attempted to curtail (or virtually eliminate) their fiscal council. Interestingly, only a minority of fiscal councils enjoy some form of safeguard on the financing of their activities. This could be viewed as another manifestation of elected policy makers' instinctive reluctance to permanently cede influence on the power to tax and spend.

Regarding the other dimensions of independence, there appears to be a sharp contrast between the veterans and the new generation. The latter rely more on legal safeguards similar to those preserving the management of central banks from political influence. However, based on our own assessment of publicly available data on staffing and budget, many new fiscal councils do not appear to have adequate resources to perform their duties. The opposite applies to the group of veterans which do have significant resources in terms of expertise and size of their staff. This is in line with our conjecture above that *de facto* independence acquired through reputable analyses is perhaps as important as *de jure* independence. And the reliance of new councils on the latter is only understandable given the absence of preexisting reputation. Of course, this stylized fact is a reflection of history based on the total population of fiscal councils; it is not the manifestation of an ex ante trade-off between adequate staffing and legal guarantees of independence. Clearly, the two should go hand in hand.

A key question is whether certain combinations of those features are more likely to contribute to better fiscal performance than others. Assessing the effectiveness of fiscal councils is clearly beyond the scope of this paper and existing attempts are rather unconvincing. The only solid evidence regarding the impact of fiscal councils is that they prepare less biased and more accurate macroeconomic and budgetary forecasts (Jonung and Larch 2006; Frankel and Schreger 2012). Testing other aspects of the influence of fiscal councils on fiscal performance remains vexingly difficult. Not only the small size of the population severely impedes a rigorous statistical analysis aimed at unveiling causalities, but the subtle and varied ways in which a fiscal council can shape policy outcomes dramatically complicates attempts to quantify its influence on the conduct of fiscal policy. Of course, as more fiscal councils are likely to emerge, the universe of potentially interesting case studies will expand significantly.

18.5 Improving Public Financial Management

Effective implementation and monitoring of fiscal rules should be supported by strong public financial management arrangements. These arrangements play an important part in the formulation of overall fiscal policy; supporting the design of specific policies that are consistent with the overall fiscal rules; and helping delivering and implementing budgets in line with what is intended. Reforms are underway in many countries, in particular in those where significant institutional weaknesses compounded the imbalances of public finances during the crisis.

The *budget formulation and execution cycle* should be well-integrated with fiscal rules to form a cohesive public financial management. In particular, a top-down budgeting process, where the aggregate expenditure limit is decided before the distribution of expenditures helps alleviate the common pool problem (i.e., the conflict between unlimited spending demands from line ministries and a finite budget constraint) at the root of excessive deficits. For example, in Germany as of 2012, the federal budget is being drawn up using a top-down approach so as to better accommodate the requirements of the structural budget balance rule.

Medium-term budget frameworks (MTBF) can reinforce fiscal rules and can in turn be strengthened by the adoption of a numerical fiscal rule. MTBFs enable governments to demonstrate the impact of current and proposed policies over the course of several years, set future budget priorities, and ultimately achieve better control over public expenditure. Presenting the budget over a multiyear horizon, demonstrates ex ante whether government policy is consistent with the fiscal rule, and what policy actions are necessary to bring it into line in the event that it is not. In countries with high budget deficits, MTBFs can also serve as a transition regime toward a meeting the requirements of a fiscal rule. Greece, Ireland, and Portugal are moving toward setting up MTBFs. Greece has adopted a medium-term fiscal strategy, Ireland has established three-year expenditure ceilings for each ministry, and Portugal's Stability Program now includes indicative ceilings on program level expenditures.

Good technical forecasting capacity, both of the fiscal aggregates and of the key macroeconomic variables is needed to ensure that the budget is developed on a realistic basis—particularly so when combined with MTBF, where the potential for errors is much greater. This should include quantifying the impact of new policy measures from the baseline forecast on the fiscal and macroeconomic environment as well as the risks around the baseline forecasts, through sensitivity analysis. This allows identifying policy adjustments needs to ensure compliance with fiscal rules. Since overly optimistic forecasts in some countries with weak or pro-cyclical public finances pre-crisis were not so much a result of limited technical capacity but rather a lack of independence, a response is to mandate independent agencies with this task (see section 18.4).

Effective budget execution systems, such as commitment controls, arrears monitoring, and cash management systems are essential to ensure that budget outcomes are in line with budget appropriations and that hidden liabilities that can endanger the overall fiscal rules are not being accumulated outside of the budgetary systems. To be effective, these systems need to be comprehensive in coverage, as many problems have emerged outside of the immediate budgetary central government, where systems tend to be stronger. For example, Portugal is in the process of strengthening and broadening its budget execution system to cover the whole general government and control expenditure at the point of commitment rather than payment, thereby preventing the accumulation of arrears.

Budget reporting systems should be comprehensive in terms of aggregates covered, able to produce reports on a consistent basis, and sufficiently developed to produce in-year and timely end-year reports to allow monitoring adherence to rules-based requirements. Given that fiscal strategies and budgets are typically prepared and approved before the start of the financial year, timely information on the state of public finances for the current year is critical in establishing the baseline for new fiscal settings. This is particularly true in the case where fiscal rules relate past fiscal performance to future fiscal policy setting and require adjustments in case of deviations as, for instance, in Germany's debt brake system and as requested for the new structural budget balance rules in the EU. A number of south eastern European countries, such as Croatia, have strengthened their fiscal reporting systems in order to meet EU accession requirements. Other countries have taken steps to improve the consistency of the reporting between budgets and outturns, through initiatives such as the "alignment project" in the United Kingdom.[11]

Internal and external audit systems are also important to ensure accountability and credibility of fiscal rules. Fiscal data—consistent with the budget reporting system—should be publicly released in line with a pre-announced calendar to allow external monitoring. In addition, externally audited financial statements are needed to scrutinize budget performance, to understand the extant position, and to provide a basis for the budget process. Development of external audit capacity in the public sector has been a key reform area for all new EU member states though further strengthening is needed in many cases. The internal audit function should provide support and assurance to the managers of public sector agencies on the adequacy and effectiveness of internal control systems. Again new EU member states and EU candidate countries, for which improvements in internal audit and internal control systems are a prerequisite for EU membership, have been active in developing capacity in this area in recent years.

Guidance to strengthen national budgetary institutions and procedures as well as accounting practices is also provided through the EU governance reforms ("six pack").[12] This includes, for example, broad recommendations to make medium-term budget frameworks more binding, prepare budgets in a more top-down sequence, report more frequently, timely, and comprehensively on fiscal developments and risks. While minimum benchmarks are provided, they miss some important elements—for example, statistical coverage of the public sector, rather than the general government, and certain elements of budgetary institutions—and provide little operational details. Progress in the areas for which guidance is provided is currently being assessed in an EU peer review with progress underway in many countries.

18.6 Conclusion

From a macroeconomic perspective, good fiscal institutions provide incentives at all levels of government to plan and execute fiscal policies that preserve the long-term financial sustainability of the public sector, deliver public services in an efficient way, and contribute to stabilizing the economy. While countries have generally understood the importance of getting the incentives right, institutional reforms have often suffered from the intrinsic reluctance of elected officials to directly limit their discretionary power to tax and spend. The result was partial reforms that often failed the test of time. A typical example is the adoption of fiscal policy rules that do not bind in good times—such as caps on headline deficits—and cannot be enforced in bad times, when fiscal adjustment is even more politically and economically unpleasant than otherwise. Incomplete and ineffective institutional arrangements are partly to blame for the fiscal vulnerabilities revealed by the crisis.

The discussion in this chapter nevertheless points to encouraging developments in the aftermath of the crisis, suggesting efforts to find a better balance between preserving policy discretion when needed, while establishing fiscal institutions that can effectively constrain such discretion in a legitimate and transparent manner when fending off undesirable trends is required. A first interesting development is the preference for fiscal rules that account for cyclical factors, and are therefore more likely to bind in good as well as in bad times, delivering greater macroeconomic stability. The need for a credible enforcement of the rules is also part of recent reforms, with the adoption of automatic correction mechanisms that reduce the risk of political interference when the implementation of the rule mandates difficult measures. Second, the rapid increase in the number of fiscal councils suggests that countries are prepared to envisage other forms of constraints on fiscal behavior, involving a better operation of checks and balances in the political system and greater awareness of the electorate. Fiscal councils could also play a formal role in facilitating the implementation of the new rules. Finally, public financial management reforms aimed at a stronger medium-term orientation of the budget should provide a supportive environment for the elimination of the deficit and procyclicality biases.

While welcome, these developments are no magic bullets. First, there will always be circumstances where political commitments will be tested to an extent that could threaten the very existence of good fiscal institutions. Second, the more sophisticated macroeconomic frameworks implied by the new rules, and the design and operation of fiscal councils and full-fledged MTBFs pose important implementation challenges. Many essential questions remain open. How can we implement an effective structural budget balance rule for the general government in a highly decentralized or federal context? How can we set up an effective fiscal council in a fractious political environment? How can limited administrative capacities be overcome when establishing full-fledged MTBFs and fiscal councils? The answers to these questions are highly country-specific, and pragmatism will be at a premium, as it will take some time for a robust set of best practices to emerge.

Notes

Jason Harris provided input for section 18.5 (Public Financial Management).

1. A comprehensive review on the design options of public financial management tools is provided in Cangiano, Curristine, and Lazare (2013).

2. The fiscal rule in Chile not only accounts for the economic cycle but also for deviations of copper and molybdenum prices from their long-term trends.

3. Automatic corrections of ex post deviations from the deficit or debt rule can raise their enforceability. They require policy makers to "undo" past fiscal excesses and determine the path back to the fiscal rule. For example, Germany and Switzerland use notional accounts in which ex post deviations (positive or negative) from the structural budget balance rule are stored. When the accumulated deviation exceeds a threshold, improvements in the structural balance are required within a predefined time frame to undo these deviations.

4. One percent of GDP for countries with debt levels below 60 percent and low sustainability risks.

5. The European Court of Justice (ECJ) will verify the transposition of structural balanced budget rules to national legislation; it will, however, not verify compliance with the rules.

6. This section draws on Debrun and Takahashi (2011) and Debrun et al. (2013).

7. In contrast, governments have an ex ante incentive to delegate monetary policy to independent central banks because the inflationary bias under discretion reflects a pure time-inconsistency problem where ex ante and ex post incentives are not aligned.

8. This section updates and expands Debrun and Takahashi (2011).

9. Jonung and Larch (2006) and Frankel and Schreger (2012) show that independent forecasts reduce the risk of an optimistic bias.

10. This was a feature of a first proposal of the Hungarian fiscal council. According to the proposal, the council would have had the right to prevent—through a ruling of the Constitutional Court—that a draft budget deemed inconsistent with the overarching principle of budget responsibility be tabled in parliament.

11. The UK government previously used three different methods for preparing its budget, presenting the expenditure estimates for parliamentary approval, and producing its end-of-year resource accounts, resulting in significant misalignment of up to around 4 percent of GDP. The Alignment Project has reduced and clarified the discrepancies and brought the three reports closer to the International Financial Reporting Standard (IFRS).

12. Council Directive 2011/85/EU on "Requirements for Budgetary Frameworks of the Member States."

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