NATIONAL AND EU BUDGETARY RULES AND PROCEDURES: AN EVOLVING INTERACTION

Jonas Fischer[*]

1. Introduction

The EU approach for budgetary policy surveillance to achieve fiscal discipline and improve co-ordination and transparency is to use rules and procedures. The Excessive Deficit Procedure (EDP) and the Stability and Growth Pact (SGP) introduce a supranational budgetary surveillance and co-ordination framework at the EU-level. The rules in the form of numerical targets allow the monitoring of budgetary aggregates against a common standard. These numerical targets focus on the avoidance of excessive deficits, the achievement of sustainable debt levels and the attainment of budgetary positions that are "close to balance or in surplus". Budgetary positions are monitored on a "Maastricht accounting basis", compiled according to the EU system of economic accounting rules (the ESA) which ensures comparability and equal treatment. Member States must regularly report budgetary data and submit Stability and Convergence programmes where they present and explain their budgetary strategies leading to the attainment of the set objectives and targets. Plans are discussed and assessed in different Council formations (the Ecofin and the euro-group) and EU committees forcing Member States to face the peer pressure of their colleagues.

The budgetary rules and procedures at the EU-level interface with the rules and procedures at national level, in particular through the elaboration and treatment of the stability and convergence programmes. In compliance with the subsidiarity principle, the EU framework does not give any indication on the set-up of national budgetary institutions. In fact, the EU legislation[1] makes it clear that at EU level: 1) governments are responsible for the general government deficit, and 2) Member States must

[*] European Commission. The author works at the Directorate General of Economic and Financial Affairs at the European Commission. The views expressed in this article are those of the author only and in no way reflect those of the European Commission. The author would like to thank especially E. Reitano for her contribution and also A. Brunila, M. Buti and G. Giudice for their valuable comments.

[1] This is made explicit in Article 3 in the Protocol on the Excessive Deficit Procedure annexed to the Treaty.

make sure that national budgetary institutions and procedures allow them to meet their obligations. Therefore, it is the responsibility of each Member State to arrange its domestic procedures on budgetary matters in the way it deems appropriate, in order to ensure that the government can fulfil the Member State's obligations at EU level effectively.

While the traditional national framework focuses on the annual budget cycle of central government, the SGP/EDP package encompasses the whole general government sector in a forward-looking medium-term setting. Indeed, sector coverage and budgeting horizon are the two main areas where some streamlining between the EU and the national level budget frameworks can be expected.

The purpose of this paper is to present a broad overview on, firstly, the extent to which national rules and procedures are at present compatible with the EU framework, in the sense that they operate smoothly together towards the same overriding targets (discipline, control and co-ordination of budgetary policies). Secondly, to investigate what are the areas of "friction" and if we can already, despite the youth of the Pact, observe changes introduced to reduce these. Moreover, we can observe some strategic behaviour by Member States when setting their budgetary targets that reduce the disciplinary power of the peer pressure.

Section 2 explains the EU budgetary surveillance framework. Section 3 focuses on how Member States have adapted national frameworks to the medium term framework of the SGP as well as some strategic behaviour facing peer pressure. Section 4 looks at the co-ordination of budgetary positions over the general government sector. Finally, in section 5 there are some final remarks.

2. The EU framework for budgetary surveillance

2.1 The procedural setting

The EU procedures of budgetary surveillance and fiscal co-ordination centre on: (1) the Excessive Deficit Procedure (EDP)[2]; (2) the

[2] Art. 104 of the Treaty, the Protocol on the Excessive Deficit Procedure annexed thereto and Council Regulation no 1467/97 of 7 July 1997 on the speeding up and clarifying of the Excessive Deficit Procedure.

provisions of the Stability and Growth Pact[3]; and (3) the broad guidelines of the economic policies (BEPG) of the Member States and the Community[4]. Member States are committed to provide information to the European Commission and to implement any policy recommendations the Council may make following the Commission's assessment.

Institutionally, the implementation of the EU procedural framework revolves around the interaction of the Member State with three EU-level actors: the European Commission, the Economic and Financial Committee (EFC), and the Ecofin Council (complemented by the euro-group for the members of EMU). The Commission is involved in the monitoring and evaluation of the budgetary process and policies, preparing assessments, reports and recommendations to the Council. The Council (Ecofin), where the finance or economic ministers of all Member States are members, is responsible for the decision-making, and acts through opinions, recommendations, decisions and, if need be, the application of sanctions upon recommendations/ proposals from the Commission. The euro-group, consisting of finance ministers from the euro-area countries, has no formal decision power but discuss economic policy issues relating to the euro area. The EFC prepares the Ecofin Council and the euro-group meetings and is the framework for dialogue between the Council and the European Central Bank. The members of the EFC are senior officials of the Commission, of the European Central Bank and of the Member States' economic ministries and national central banks, "selected from among experts possessing outstanding competence in the economic and financial field". The Committee therefore also constitutes a framework for dialogue between the Member States and the EU institutions and amongst the Member States, playing a crucial role in developing and engraving a mechanism of peer review and peer pressure.

The Member States are required to report to the Commission twice-yearly their planned and actual deficits and the levels of their debt under the EDP as part of the early warning mechanism under the EDP. In addition to providing this information, the Member States are required to

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[3] Resolution of the European Council of 17 June 1997, and Council regulations 1466/97 and 1467/97 of 7 July 1997.

[4] Art. 99 of the Treaty.

submit regularly each year stability and convergence programmes, on which the Council formulates an opinion[5].

The stability and convergence programmes and their annual updates are the key instrument of the EU budgetary surveillance and fiscal policy co-ordination framework. They establish a medium-term objective for the general government balance and for the reduction in the government debt ratio, delineate a path to reach the objective and contain a description of the main economic assumptions underlying the fiscal framework and of the budgetary and economic policies to achieve the objectives, as well as an analysis of how changes in the economic assumptions could affect the fiscal aggregates. The informational content and the format of the programmes is clarified by a Code of Conduct drafted by the Monetary Committee (now replaced by the EFC) and approved by the Council in late 1998. The Code of Conduct is aimed at ensuring greater standardisation and maximum comparability of the programmes.

The Ecofin Council is responsible for the examination of the stability and convergence programmes. Based on the Commission's assessments of the programmes and its recommendations for a Council opinion, which are followed by a discussion in the EFC, the Council formulates an opinion on each programme. Updated programmes could be examined under a lighter procedure, without the direct involvement of the Council. If deemed sufficient, the assessment could be based only on the EFC examination. However, given the relative youth of the Stability and Growth Pact and the need to build the credibility of the overall framework, so far the updated programmes have been evaluated following the standard procedure, i.e. they have been examined by the Council which has released a formal opinion.

The Council must assess whether the medium-term budgetary objectives provide sufficient room for manoeuvre to avoid excessive deficits, whether the economic assumptions underpinning the programme are realistic and whether the fiscal measures announced/described in the programmes are sufficient to reach the targets. The Council must also examine whether the economic policies in the programme are consistent with Broad Economic Policy Guidelines and whether the content of the programme "facilitates closer co-ordination of economic policies".

[5] Council Regulation no 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and co-ordination of economic policies.

2.2 The budgetary numerical rules at the EU-level

Framing a discussion on numerical rules at EU (below) and national level (section 3.2), there are a number of aspects identified in the literature that should be taken into account.

First there is the issue of what is the definition of a rule. A critical feature of a budgetary rule is that it is intended for application on a permanent basis by successive governments (Kopits and Symanski, 1998). A rule should also have an ex-post dimension and be followed up. Needless to say, not all policy targets that guide national budgetary policies qualify as "rules", even if they also serve the purpose of being commitment devices. Therefore, self-proclaimed "targets" by a government should rather be labelled as "guidelines", as they are useful as commitment and transparency devices for the current government's policies, but do not commit successive governments, nor create any legal restraints on their policies.

The credibility of a rule is built over time by reputation and/or by ex-post enforcement mechanisms and sanction systems. Only a credible rule gives ex-ante knowledge about future budgetary policies and can influence agents' expectations. The design of a rule also involves many features. Compliance should be easy to survey, preferably by an independent agent. In this respect, there is a trade-off between simplicity and transparency on the one hand, and flexibility and contingency on the other. In principle, the ideal rule should be state-contingent, but if rules are too contingent they may lose in terms of transparency and become excessively flexible and subject to manipulation. It is then difficult to read what is the real commitment involved. This supports the argument in favour of simplicity.

There is also a trade-off between externally and internally imposed rules. While external rules may help guide "weak" governments in the right direction, they may also be regarded as forced constraints with low social acceptance. The degree of severity of a rule depends on which part of the government sector is covered, on the budgetary indicator chosen and on the threshold targeted.

The EU budgetary numerical rules is set up as a device to promote a low deficit culture with a high degree of budgetary control (3% deficit ceiling), sustainability of budgetary positions (60% debt ratio target) and to ensure that planned budgetary positions contain underlying safety margins

so that the budget can respond to economic shocks without the actual deficit surpassing the 3% ceiling (close to balance target).

To ensure comparability and equal treatment across Member States. Therefore, the ESA economic accounts (the European System of Economic Accounts[6]) have been chosen as the accounting framework for the budgetary surveillance at EU level. The sector coverage encompasses the whole general government, defined as central government, state and regional government and social security funds. Importantly, the general government definition is based on a functional basis rather than on an institutional basis, thus including also "off-budget" items. Only units that produce non-market services (administrative services) are included. Publicly owned units dealing with commercial operations are excluded, such as most public enterprises.

- *The 3% of GDP ceiling on general government net borrowing*

The general government deficit, or net borrowing, is defined in the ESA and refers to the excess of all current and capital expenditure over the corresponding receipts. Importantly, all financial transactions[7] are excluded. Net borrowing must not be confused with the borrowing requirement drawn from the public accounts and used as reference in budget laws. Contrary to the analytical focus of economic accounts, the borrowing requirement focuses on the financing of the State budget. The two concepts are different both in terms of coverage and the recording concepts used. In particular, contrary to the ESA definition, the borrowing requirement normally includes many financial transactions and covers usually only the central government and could include public corporations. Overall, the 3% deficit ceiling is the "anchor" among the EU rules and has the advantage of being simple and transparent to monitor while, being formulated in actual terms, a drawback could be its relative inflexibility over changing economic conditions.

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6 Council Regulation 2223/96 of 25 June 1996.

7 A financial transaction is the sale and purchase of financial assets, such as gold, currency deposits, loans, equity and bonds. Financial transactions must not be confused with capital transactions which cover capital formation (investments) and capital transfers (such as investment grants and capital taxes). Capital transactions influence net borrowing.

- *The "close to balance or in surplus" target*

The "close to balance or in surplus" target in the Stability and Growth Pact relates to medium term budgetary positions as expressed in the Stability and Convergence programmes. There is no precise definition of "close to balance or in surplus" and of how to monitor compliance to the rule. At a minimum, such a position should allow the automatic stabilisers to play freely[8]. To this end, the Commission made a first quantification effort by calculating a set of "minimum benchmarks"[9].

As the target should be read in cyclically adjusted or underlying terms, it becomes less transparent and more difficult to monitor than the actual deficit ceiling. The ESA does not identify underlying budget balances and the the cyclical position of the economy is unobservable and therefore needs to be estimated. Accordingly, any estimate of cyclically adjusted budget balance is surrounded with a large amount of uncertainty. Hence, while this rule suffers from monitoring difficulties it has the advantage of being insulated from changing economic circumstances.

- *The 60% of gross government debt to GDP ratio target*

The gross debt ratio target is probably the most straight-forward of the EU numerical rules, but maybe at the same time the least targetted. The debt rule in the EDP says that the general government gross debt ratio to GDP should be below or approach the 60% of GDP reference target level at a "satisfactory pace". The actual implementation of the debt rule so far seems to suggest that a reduction in the debt ratio is sufficient to qualify as satisfactory[10].

Gross debt is not defined in the ESA but in the Treaty protocol on the excessive deficit procedure annexed to the Treaty. However, the financial assets to be taken into account are defined in ESA terms. The precise definition is: total gross debt at nominal value outstanding at the end of the year and consolidated between and within the sectors of general

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[8] Resolution of the European Council on the Stability and Growth Pact, 17 June 1997, OJ C 236, 2.8.1997.

[9] For a elaboration on this issue see part III in « Public finances in EMU-2000 », the Commission 2000.

[10] See the 1998 convergence report « Euro 1999 » published by the Commission.

government[11]. The "consolidation" means that the only assets taken into account are holdings of general government debt within general government[12]. "Contingent" liabilities, such as PAYG pension liabilities, are not recognised in the ESA and are therefore not included in the debt definition. This is of course a limitation because the gross debt is used as a signal of sustainability although it may neglect the long-term financing pressures.

3. Expenditure control and medium-term budgeting

3.1 Overview of the expenditure control mechanisms at national level

The EU framework promotes budgetary discipline and puts public finances in a medium term setting. In this context, medium term expenditure control mechanisms contribute to increase the transparency of the budgetary process by an early identification of overruns and by making the budgetary choices involved more explicit. Member States have various expenditure control mechanisms to help them meet these medium-term commitments.

Moreover, a fiscal strategy resting on expenditure control, while allowing for the automatic stabilisers to operate freely on the revenue side seems largely consistent with the rationale of the EU framework approach emphasising the role of budgetary discipline and national automatic stabilisers. Constrained medium-term expenditure paths producing a gradual decrease in the government expenditure to GDP ratios could also be a useful instrument to produce space for reductions of high tax burdens while continuing and safeguarding fiscal consolidation.

Table 1 gives an overview of the different rules, objectives and guidelines, currently used in some Member States to direct the evolution of public expenditure in the medium-term. Even if the overall aims are similar, the details differ substantially. A number of Member States now apply extensive multi-annual budgeting frameworks including "hard"

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[11] This definition is further specified in the Council Regulation 3605/93 as amended by CR 475/2000 where the debt instruments that should be included are listed: currency and deposits, bills and short-term bonds, long-term bonds, other short-term loans and other medium and short-term loans. Note that government guarantees and contingent liabilities are not included.

[12] While the debt criterion is on a gross basis, the deficit criterion is on a net basis. This implies that there is a discrepency between the change in the debt ratio and the deficit mainly due to the building up/down of financial assets. This is labelled the « stock-flow » adjustment.

expenditure ceilings, while others operate with less formal expenditure growth targets or guidelines.

One of the most encompassing medium-term budgeting framework is in *the Netherlands*. It is based on the coalition agreement of the ruling Dutch government and covers the full period of office[13]. The cornerstone is real expenditure targets. Under the current coalition agreement, real expenditure is allowed to grow by 1 1/2% a year on average. The real expenditure guidelines are translated into actual figures on an annual basis using the GDP deflator. The real expenditure targets are set on the basis of deliberately cautious growth scenarios. Should expenditure overruns occur, then they must in principle be compensated for in the same year. A key feature is the clear separation of the expenditure and revenue sides of the budget, since windfalls in revenues may in principle not be used for financing additional expenditure. As revenues almost always come in higher than assumed (given the cautious growth scenario assumptions), recent years have seen growth dividends relative to plan. The framework stipulates rules how to distribute such “growth dividends” between the alleviation of the tax burden and the reduction of debt[14].

In *Italy*, the government presents a medium-term budget-planning document (DPEF[15]) to Parliament in June each year for a vote. The DPEF contains a four-year budget framework of the main aggregates including budget balances and expenditure and revenue ratios for the general government. The DPEF gives government targets and estimated outcomes based on trend projections, indicating the expected amount of discretionary budget measures necessary. The autumn budget then implements the DPEF for the first year of the plan. Overall, the DPEF does not directly constrain public expenditure, but rather is a framework that reveals the government's medium-term objectives.

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[13] The current cabinet period ends in 2002. It is likely that the current system will be modified after the elections.

[14] In the case of a positive growth dividend on the revenue side, if the EMU deficit is smaller than 0.75% of GDP, the allocation of additional revenues are split 50/50 between lower taxes and improving the deficit. If the deficit is higher than 0.75% of GDP, 75% goes to improve the deficit. In the case of a negative growth dividend, if the EMU deficit is above 2.25% of GDP 50% of revenue losses are covered by borrowing and 50% by tax increases. If the deficit is below 2.25%, 75% is covered by borrowing and 25% by higher taxes.

[15] Documento di Programmazione Economico-Finanziaria.

Table 1

General government medium term budgeting frameworks used in Member States

	Multi-annual budgeting framework	Multi-annual spending targets/ guidelines/ objectives	Additional budget rules and targets
B	-	Annual CG+SS exp. Growth 1.5% in real terms over medium term.	Primary balance objective
DK	-	Annual GG consumption growth of 1% in real terms over medium term.	Average GG budget surplus of 2-3% of GDP. Reduce debt levels.
D	-	Annual GG 2% expenditure growth in real terms	Golden rule for federal government
F	-	GG exp. 4.5% real growth target over 3 years (2002-2004). Growth target set to be below potential growth of economy.	
IRL	Three year departmental «envelopes».	-	
IT	DPEF and multi-annual budget presented to Parliament	-	
NL	CG commitment to expenditure framework over 1999-2002 office period.	CG+SS to grow 9% in real terms over 1999-2002.	Rules on how to deal with growth dividends on the revenue side
FIN	Four-year expenditure set by CG and presented to Parliament.	CG expenditures constant at 1999 real level over 2001-2004 period.	CG budget in surplus in structural and ESA terms
SW	Three-year nominal expenditure ceilings approved by Parliament.	CG exp. growth not higher than projected nominal GDP.	GG 2% surplus over the cycle.
UK	Three-year spending limits for department's covers mainly discretionary expenditures.	-	-Golden rule for public sector -Sustainable investment rule (40% net debt)

Source: 2000/2001 updated SCP and Commission services.

Note (1): GG: general government, CG: central government and SS: social security.

Note (2): Member States not mentioned in the Table do not yet apply a national medium term budgeting framework/mechanism.

In *Finland* and *Sweden*, more explicit multi-year expenditure frameworks are used in the budget process. In Sweden, the Parliament enacts four-year nominal expenditure ceilings for central government spending including pensions but excluding interest costs. These ceilings are fixed in the spring and are the starting point for the budget that is presented during autumn. The ceilings are set so that they are in accordance with the government aim to keep the budget balance at a 2% of GDP surplus over the cycle (see section 2.2). In Finland the system is similar using five-year expenditure ceilings for the central government, which are presented in the spring and updated annually. However, in Finland it is the government that sets the ceilings while the Parliament is only informed. The current government set the ceilings that aim to keep real expenditures at the 1999 level when it took office and provide for a central government surplus in structural terms.

The *UK* and *Ireland* use similar systems with three-year departmental expenditure envelopes. The UK the system is more elaborated, having three year departmental envelopes for discretionary expenditures (not including social security benefits and debt interest) decided in the bi-annual "*Comprehensive spending review*" and subject to approval of government and Parliament. Current government guidelines are set using a cautious 2.25% of GDP trend growth assumption. The envelopes are set to be in accordance with the "golden rule" and the "sustainable investment rule" which form part of the budgetary framework (see section 2.2). In Ireland, the three-year departmental envelopes are set by the government and operate more as guidelines to improve medium-term planning.

Several of the governments in other countries use targets for medium-term expenditure growth developments. These objectives are set by the government as a guide for fiscal policy, but are not part of a multi-annual budgeting system as such. In *France,* the government uses three-year rolling growth targets for real general government expenditures. The target is to be applied on average over the three-year period and is updated and rolled over on a yearly basis. Growth targets are set below potential GDP growth estimates, thus aiming at gradually lowering the share of public expenditures to GDP. In *Belgium,* the government has set an annual 1.5% growth target for real primary expenditure for the federal government and social security ("Entity I"). To this end, a cautious 2.5% trend growth

assumption has been used and growth dividends[16] are to be used to reduce debt. In *Germany*, the federal government has presented a 2% nominal expenditure growth objective to be applied for the whole general government sector over the medium term.

In both *Spain* and *Portugal* there are currently plans to introduce more extensive medium-term budgeting frameworks.

- *Common features across Member States*

While the frameworks described above share common features, they are also quite different in several institutional aspects. Firstly, their status differs. Only the frameworks enacted by law, such as in Sweden or the UK, or vested with an important amount of political capital can be regarded as "rules" that provide an external constraint to guide budgetary choices. In addition these frameworks also include enforcement mechanisms in the event of expenditure overruns. Where the government unilaterally declares a certain expenditure growth path as an objective, there is no enforcement mechanism within the system to prevent targets being reformulated or departed from. In these cases, credibility is established over time and the potential loss of built up credibility provides the incentives to stick to set plans.

Secondly, there is a trade-off between flexibility and credibility. The simplest and most focused frameworks are the most operational and transparent. But they also risk becoming inflexible in changing economic conditions creating costs from an economic efficiency point of view. Such inflexibility can imply that the resulting fiscal stance becomes pro-cyclical (see below), or that the frameworks no longer meet the specific concern for which they were designed. Pressures to modify the parameters of the existing framework can build, or indeed for a complete redesign of the overall framework. Both in Sweden and the Netherlands, the frameworks described above have been created at a time when budget deficits were high mainly due to increasing expenditures. Therefore, fiscal consolidation and expenditure control was key. However, in the current circumstances when growth is higher and budget positions are in surplus, there will be pressure for some, at least parametric, change. The benefits of such changes have of course to be weighed against the potential loss of

[16] Growth dividends stemming from the 2.5% to 2.7% interval could be allocated for other purposes.

credibility. Frameworks with a lot of flexibility may end up being less binding. For example in France, the three-year average growth objective given in the 1999 update of 4% over the 2000-2002 period has been increased to 4.5% for the 2001-2003[17].

Third, the sectoral coverage of the expenditure frameworks varies across countries. In general, frameworks aimed to be more directly operational tend to have a relatively narrow coverage encompassing mainly central government expenditures and in some cases also include social security). This is natural as this is under the direct control of the central government. However, expenditure growth guidelines tend to apply to the whole general government sector in order to give guidance to other parts of general government and to act indirectly as a co-ordination instrument. In these cases there tends to be no "hard enforcement" mechanism beyond domestic peer-pressure to respect the guidelines.

Four, there is the aspect of built in pro-cyclicality to be considered when expenditure ceilings are strict and based on cautious growth assumptions. Using cautious growth assumptions can be beneficial to the extent that the costs of not meeting budgetary targets tend to be higher than the benefits of overachieving them. Many countries assume cautious growth assumptions when setting budgetary targets/ceilings, and there is a tendency for growth to turn out higher than assumed. If so, "growth dividends" are likely to materialise on the revenue side. Several of the frameworks contain some guidelines on how to deal with these. For example, in Belgium the government is committed to use growth dividends to reduce the high debt levels that would allow automatic stabilisers to operate fully on the revenue side. However, in countries with lower debt levels it may be deemed more important to reduce high tax burdens than to further reduce debt levels. This could introduce a trade-off between efficiency concerns (i.e. a lower tax burden) and stabilisation concerns (i.e. cutting short the working of the automatic stabilisers in the process). As already said above, in the Dutch framework growth dividends on the revenue side, contingent on the level of the deficit, are in principle to be allocated to tax reductions. In this case, these tax reductions risk being pro-cyclical as taxes are reduced when growth is high. In Sweden, growth dividends leading to budget surpluses above the structural 2% surplus target are earmarked to be returned to the household sector. However it is

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[17] Indeed, in the Council opinion on the French update the Council specifically noted this increase in the expenditure norm relative to last year and found that a lower increase would be desirable.

not specified what form this will take place (higher transfers or reduced taxes).

3.2 The use of numerical rules at the national level

Some countries complement expenditure control frameworks with numerical budgetary rules. In fact the numerical rules could sometimes be seen as having a higher status, with the expenditure frameworks being viewed as means to ensure they are met.

Sweden applies a budgetary rule that incorporates the SGP approach of concentrating on cyclically-adjusted budget balances. To lower the debt burden to prepare public finances for future recessions and the budgetary impact of ageing populations, the government has set an objective of a 2% of GDP budget surplus on average over the business cycle. This could accordingly be considered as a "cyclically-adjusted" budget balance target. In fact, a structural target at a 2% surplus level is more ambitious than the SGP "close to balance or in surplus" objective[18]. Whereas the strength of this type of rule is its flexibility in light of changing economic conditions, the monitoring of compliance is complicated. To translate the "average over the business cycle" target into an operational annual target, it is necessary to identify the position in the business cycle. As a view on the output gap is necessary in this framework, compliance with the target on an annual basis is difficult to assess.

Another interesting is the application of a current account balance requirement, the so-called "golden" rule of deficit financing. The UK and Germany apply a golden rule in their national budgetary framework that is codified by law. In the UK, the golden rule is part of the "fiscal code of conduct[19]" and is framed in a medium term context: over the economic cycle the current budget should be in balance or surplus. The investment concept used relates to net investment; thus borrowing is only allowed for investment that contributes to increasing the capital stock. In Germany, the golden rule applies to the federal budget on an annual basis and is enshrined in the constitution[20]. The definition of physical investment used

[18] The "minimal benchmark" for Sweden discussed in chapter 1 is +0.8% of GDP.

[19] These principles were enshrined in the Finance Act 1998 and the Code for Fiscal Stability, approved by the House of Commons in December 1998. The Code sets out how these principles relate to the formulation and implementation of fiscal policy in practice.

[20] Article 115 in the «Grundgesetz».

also includes investment in human capital and therefore does not follow strictly the national account definition.

The pros and cons of targeting the overall or the current budget balance have been debated extensively in the literature[21]:, the concern here is the compatibility with the EU rules which do not treat investment expenditures differently from other expenditure[22]. An increase in borrowing to finance higher capital investment could be in conflict with SGP requirement of achieving a budget balance target of close to balance or in surplus.

The consolidation effort in the run-up to EMU has to some extent (relatively small) been based on restricting the growth of government expenditures[23]. Therefore, in the context of meeting the SGP budgetary targets, an application of the golden rule has generally led to any conflicts. Furthermore, the initial years of EMU, favourable growth has meant that the automatic stabilisers have contributed to improve overall actual budgetary position. However, different circumstances may arise in the future if growth conditions worsen and investment levels need to increase. The targets set in the 2000 UK convergence programme provided an indication in this direction. Table 2 shows the UK current budget targets and the compatible ESA budget balance targets as presented in the updated programme. While the national golden rule requirements are clearly overachieved, the planned budget balance deteriorates sharply as a result of increasing investment levels. Obviously, these developments are difficult to reconcile with the "close to balance or in surplus" requirement of the SGP, even though this would be of more concern in countries with higher debt levels or debt still above the 60% of GDP reference value. This development was noted in the Council opinion on the UK convergence programme update (see country section in Part V). Moreover, this type of "target inconsistency" may become more relevant in relation to applicant Member States where there is an evident need for high government investment levels.

[21] See for example Balassone and Franco, 2000, and Buiter, 2000.

[22] However, the Treaty article 104 on the EDP specifies that the Commission should take investment expenditures into account when assessing excessive deficits.

[23] See European Commission, 2000, Part I, chapter 3 on the budgetary adjustment in the 1990s.

Table 2

Budgetary outlook in the UK according to the 2000 updated UK CP

% of GDP	1999/ 2000	2000/ 2001	2001/ 2002	2002/ 2003	2003/ 2004	2004/ 2005	2005/ 2006
Current budget	+2.1	+1.7	+1.6	+1.3	+0.7	+0.7	+0.7
ESA balance	+1.8	+1.1	+0.6	-0.1	-0.9	-1.0	-1.1

A further example of a numerical rule is that of national targets for primary balances, which seem to be a useful complement to the actual balance target, especially in high debt countries. For instance, Belgium over several years has referred to a commitment to keep the primary budget balance over the 6% of GDP level in the medium term so as to bring down public debt at a fast pace. An explicit reference to a figure is no longer made in the stability programme update, mainly because primary balances are kept comfortably above the 6% of GDP level and in fact are closer to 7%.

Several countries use different guidelines for targeting debt levels, but these are generally fully compatible with the EU framework. Only the UK has a numerical rule codified by law (through the "fiscal code of conduct"), which states that the net debt should be below 40% of GDP over the business cycle[24]. In the current situation this ambition is not binding in a policy perspective, as the net debt is already below the 40% of GDP level. Moreover, in practice this is a tighter objective than meeting the 60% of GDP gross debt reference value. In theory the same type of conflict with the EU framework as is the case with the golden rule may arise since the gross, rather than net, debt is targeted.

[24] This is a sustainable investment rule, by virtue of which public sector net debt as a proportion of GDP should be held over the economic cycle at a stable and prudent level and where, other things equal, a reduction in public sector net debt to below 40 per cent of GDP over the economic cycle is deemed desirable.

3.3 Strategic behaviour to limit the discipline of peer pressure

The EU framework builds largely on the effectiveness of peer pressure as a disciplinary device to reach set targets and avoiding policy co-ordination failures. While a government could find external peer pressure a useful support when implementing difficult measures domestically, there are also incentives to reduce the discipline of peer pressure in other cases and maintain a maximum freedom of manoeuvre.

In the EU framework, peer pressure can be exerted both ex-ante and ex-post. *Ex-ante peer pressure* can be exerted if budgetary plans are presented and discussed at EU level before they are implemented or decided nationally. Such a discussion could lead to EU-level incentives to enact specific policies. For example, a country might plan to substantially cut taxes with an implication for the overall policy-mix and EU partners may have views on whether this is optimal given the current cyclical conditions. *Ex-post peer pressure* relates to the attainment of set targets. A Member State may have committed itself to reach a certain budgetary target and when it later appears that the target is not going to be reached there could be peer pressure from EU level to take corrective action.

Looking at the implementation of the Pact so far there are instances of behaviour on the part of Member States that could be read as a way to avoid both ex-ante discussions on budgetary plans and ex-post discussions on the attainment of set targets. An example of the former could be the observed strategy of submitting stability and convergence at a very late stage in the national budgetary process. This is discussed in more detail section 4.1 below. An example of the latter is the use of overly cautious underlying assumptions when setting budgetary targets. This is discussed below.

- *The use of cautious assumptions when setting budget targets*

A relevant issue in the assessment of compliance with programme's objectives is the tendency of many Member States to be overly cautious in their underlying assumptions. While in the run-up to EMU Member States may have had incentives to be overly optimistic, showing quick progress in their consolidation efforts, now, once in EMU, the incentives have diametrically changed, with cautious growth assumptions paying several forms of "dividends" to governments.

If assumptions are overly cautious and budgetary "growth dividends" systematically materialise, targets are generally overachieved giving the false impression that governments are over-performing (in actual terms). Also, an implicit "room for manoeuvre" is built up which can be used for 'ad hoc' discretionary budgetary measures without being restricted by the actual targets set in the programmes. Finally, in the case of surplus countries, cautious targets may help to avoid domestic political pressure to "spend" the surpluses. It should be recognised that there is a general asymmetry of costs and benefits when designing budgetary plans which calls for systematic caution: in general higher deficits than targeted are more damaging than the good-will gained when targets are surpassed.

Even so, biased underlying assumptions contribute negatively to the transparency of budgetary policies and constitutes a less useful basis for policy co-ordination and the actual surveillance of the attainment of SGP targets in this context is problematic. Partially this is because the question whether budgetary positions should be evaluated in actual or in cyclically adjusted terms is still partially open. While the Commission strongly supports the view that emphasis should be on underlying developments, not all Member States agree, mainly because of the uncertainties in the calculation of cyclically adjusted figures. Clearly, if "peer pressure" were on cyclically adjusted targets, then the cautious attitude of Member States would not create big problems for the assessment. Indeed, as higher-than-assumed growth outcome would imply a smaller deficit/higher surplus in actual terms, Member States would automatically be required, in order to respect their original commitment in the underlying terms, to attain better actual budget positions than envisaged in the programmes.

To illustrate the cautious approach by Member States it is possible to adjust the actual budgetary targets in the programmes by the expected growth dividends and outdated starting positions. This is done in Table 3[25] below, where the first two columns show the deficit targets for 1999 and 2002 as announced in the 1999/2000 updates. The change in the budget deficit from 1999 to 2002, in column 3, is the "committed effort" over the period. Column 4 shows the starting position adjustment for 1999, while in

[25] The starting position is calculated as the difference between budget balance outcome figures for 1999 used in the programmes and in the latest Commission forecast. The growth dividends are calculated as the difference in GDP growth assumptions in the programmes and the latest Commission forecast times the Commission budget sensitivities to growth (around 0.5 on average, see report «Public finances in EMU-2000» for more details).

Table 3

Deficit targets from the 1999/2000 round of updates, adjusted to take into account changes in the starting position and expected budgetary growth dividend

% of GDP	SP/CP deficit target 1999	**SP/CP deficit Target 2002**	SP/CP "effort"	Starting position 1999	Growth divi-dend 2000	Growth divi-dend 2001	Growth divi-dend 2002	Starting and growth dividends	Adjusted "effort" 99/02	**Adjusted deficit target 2002**
	1	2	3 = 2-1	4	5	6	7	8= 4 to 7	9 = 3 + 8	10 = 1 + 9
B	1.1	**0.0**	-1.1	-0.4	-0.8	-0.6	-0.5	-2.2	-3.4	**-2.3**
DK	-2.9	**-2.3**	-0.6	0.1	-0.7	-0.2	-0.1	-0.9	-0.3	**-3.2**
D	1.2	**1.0**	-0.2	0.2	-0.3	-0.2	-0.0	-0.3	-0.5	**0.7**
EL	-1.5	**-0.2**	-1.7	0.3	-0.1	-0.1	-0.2	-0.1	-1.8	**-0.3**
E	1.3	**-0.1**	-1.4	-0.2	-0.2	-0.0	-0.0	-0.4	-1.8	**-0.5**
F	2.1	**0.9**	-1.2	-0.3	-0.2	-0.2	-0.1	-0.8	-2.0	**0.1**
IRL	-1.4	**-2.6**	-1.2	-0.5	-1.2	-0.7	-0.5	-3.1	-4.3	**-5.7**
IT	2.0	**0.6**	-1.4	-0.1	-0.3	-0.1	-0.0	-0.5	-1.9	**0.1**
L	-2.3	**-2.9**	-0.6	-0.1	-0.4	-0.4	-0.3	-1.2	-1.8	**-4.1**
NL	0.6	**1.1**	0.5	-1.6	-1.3	-0.8	-0.6	-4.3	-3.8	**-3.2**
AT	2.0	**1.4**	-0.6	0.1	-0.2	-0.0	-0.1	-0.2	-0.8	**1.2**
P	2.0	**0.7**	-1.3	0.1	-0.1	0.3	0.3	0.8	-0.5	**1.5**
FI	-3.1	**-4.6**	-1.5	1.2	-0.7	-0.8	-0.8	-1.1	-2.6	**-5.7**
SW	-1.7	**-2.0**	-0.3	-0.2	-0.7	-1.1	-0.8	-2.8	-3.1	**-4.8**
UK	-0.4	**0.0**	0.4	-0.9	-0.5	-0.3	-0.3	-2.0	-1.6	**-2.0**

Source: Fischer and Giudice (2001).
Note: a minus sign for the targets indicates a budget surplus.

columns 5-7 is indicated the expected growth dividends over the 2000-2002 period on the basis of the Commission autumn 2000 forecast. Column 10 indicates the "new" targets in actual terms. From the table it is obvious that, if the 2002 targets are assessed only in actual terms (column 3), they are not very ambitious at all in comparison to the adjustments effort Member States have (implicitly) committed to (column 10). In other words, an assessment only in actual terms can be very misleading and become non-binding in a high-growth environment.

Interestingly, a new strategy from Member States seems to have emerged in the 2000 round of programmes. Several Member States (B, I, NL, SW) now make a separate in the programmes between budget balance “forecasts/ projections” and “targets”, where the targets are generally less ambitious. A distinction is therefore made between the “hard commitments” which is the target, and the possible “room for manoeuvre” building up through cyclical developments and measured by the difference to the “target”. How to allocate this “state contingent budgetary margin” is generally not committed to in a hard way. It can be used for other policy purposes, such as tax cuts or investment, or to reduce deficit and debt sometimes conditioned on policy-mix concerns. The positive in this trend is that what is the “hard commitment” is made explicit rather than implicit as is the case when using overly cautious growth assumptions. In fact the incentives to use cautious growth assumptions are reduced, while at the same time the “hard commitments” are easier to assess and monitor. Accordingly, this creates a better basis for policy co-ordination discussions. It will be up to the Commission to evaluate the appropriateness of the targets and the quality of the plans for the “budgetary margin”.

4. Co-ordination of general government positions at the national level

The budgetary commitments of Member States set down in Treaty and the SGP concern the general government sector and not only central government. At the national level, several players other than the central government are involved in determining the overall budgetary stance, and consequently influence Member States’ decisions regarding their EU commitments. In particular, national Parliaments are actively involved in the elaboration of SGP targets and programmes. Within the general government, lower levels of governments make up an important part,

especially on the spending side. How the central government interacts with these other national budgetary players on issues relevant for the SGP are examined below.

4.1 Stability and convergence programmes: the involvement of Parliament and the interaction with the national budget procedure

Whereas governments interact directly with the Parliament in the annual budgetary process, they operate with a large degree of autonomy when deciding the medium-term targets and commitments in their stability and convergence programmes, At present, national Parliaments are not formally involved in the process leading to the submission of the stability/convergence programmes (Table II.5)[26]. In fact, no Member State's Parliament formally endorses the programme before it is submitted to the EU and in most case the Parliaments are informed about the programmes at the same time or after they have been submitted to the EU.

However, a form of indirect Parliamentary endorsement of the contents and the commitments of the programmes exists to the extent that the programmes mirror documents, which have already received, or are due to receive, Parliamentary endorsement. Therefore, the timing of submission of programmes as compared to the national budget cycle and the stage in the parliamentary process is important.

The SGP (regulation 1466/97) required that the first set of stability and convergence programmes be submitted before 1 March 1999, a deadline that was synchronised with the first reporting of data on deficits and debt for use in the Excessive Deficit Procedure. Since then they have submitted updated programmes around the end of the year, in some cases as early as September or as late as March.

In most Member States the annual budget cycle runs during the autumn months, with Parliament adopting the final budget towards the end of the year or early the following year. The submission of updated programmes to the EU therefore takes place at different stages in the

[26] Formal involvement implies a voting procedure, a debate followed by a resolution or some form of official endorsement of the programme.

Table 4

Involvement of Parliament in the 2000 round of updates

	Time of programme submission	Stage in budget process	Parliament informed relative to submission	Possible parliamentary treatment
B	12/2000	Budget adopted by Parliament	Same time	
DK	12/2000	Budget adopted by Parliament	Same time	
D	10/2000	Parliamentary debate underway	Same time	
EL	12/2000	Parliamentary debate underway	Same time	
E	01/2001	Budget adopted by Parliament	Same time	
F	12/2000	Budget adopted by Parliament	Before	Presented by Gov. and discussed in Parliament
IRL	12/2000	Budget submitted to Parliament	Same time	Parliament can discuss
I	12/2000	Budget adopted by Parliament	Same time	
L	12/2000	Budget adopted by Parliament	Same time	Relevant Parliament committee debate
NL	09/2000	Budget submitted to Parliament	Same time	Parliament can discuss and can vote on resolution
A	12/2000	Parliamentary debate underway	Same time	
P	01/2001	Budget adopted by Parliament	Same time	
FIN	09/2000	Budget submitted to Parliament	Same time	Presented by Gov. and discussed in Parliament
S	11/2000	Parliamentary debate underway	Before	
UK	12/2000	Start of consultation phase leading to draft budget	Same time	

national budgetary procedure across Member States[27].

It can be argued that the submission of the programmes after the parliamentary adoption of the budget means that they better reflect the outcome of the national budgetary process. However, a late submission could also be a way to avoid a parallel discussion at EU and at national level, and could mitigate concerns on national sovereignty that debate at EU level might pre-empt national political discussion.

However, If the programmes are submitted before the start of the annual budget process (i.e. ahead of the government presentation of the draft budget to the national Parliament), this could enhance the commitment of Parliaments to the main budgetary aggregates, and moreover provide an opportunity for the concerns expressed at EU level to be taken into account in setting national budgets.

For similar reasons, there could also be a deliberate intention to submit programmes very early in relation to an upcoming sensitive national policy discussion. In both cases, the programmes risk quickly becoming outdated, reducing their value importantly and affecting the transparency of the whole process. Overall, given that draft budgets are usually very close to final budgets, an early submission would seem to be more in line with the rationale of the SGP, allowing the EU discussions to feed back into the national discussions.

A low degree of formal involvement does not fully reflect the real degree of parliamentary involvement in the SGP process. As regards the short-term commitments, the degree of indirect endorsement of the programmes is in fact quite high, as generally there is a strong link between the programme targets and the annual budget for all Member States except the UK[28]).

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[27] Over the past three years, a number of Member States (Belgium, Spain, France, Italy, and Portugal) have consistently submitted the programmes after the adoption of the final budget by the Parliament. In a few cases (Ireland, Finland), the submission has taken place around the moment of the presentation of the draft budget to Parliament, while in others (Austria, Sweden) it has always taken place before the conclusion of the parliamentary debate on the budget. Only in the case of the UK, due to the fact that the budget is not presented until the Spring, does the submission of the programme take place during the preparation of the draft budget. Beyond the regular pattern of submission dates that emerges for the majority of the Member States, it can be observed that in some countries (notably Denmark, Germany and the Netherlands) the date of submission has not been constant in time.

[28] This is because the budget is not run a calendar year basis. The UK figures are based on the mid financial year autumn statement.

However, the implicit endorsement by Parliament of the medium-term target is much more tenuous. The medium-term target and adjustment path set down in stability and convergence programmes are not a budget proposal or on an existing budget, and thus signal ambitions rather than plans. In most Member States, the medium term objectives are merely based on a government forecast, or a forecast made by an independent planning bureau and thus remains exclusively the government's responsibility.

The situation is qualitatively different in the limited number of countries in which there is a medium-term framework based on parliamentary decisions. In Finland and Sweden (see section 3), multi-annual expenditure ceilings are agreed or discussed by Parliament in the spring, and thus constrain the major aggregates ahead of the adoption of the annual budget in the autumn. The objectives presented in the programmes by the government must be consistent with the expenditure ceilings implying that the medium term targets are endorsed by Parliament. In Italy, Parliamentary involvement goes even further as the DPEF is adopted by a vote of Parliament. The Italian stability programme is based on the budget law and the DPEF and if the programme objectives deviate from the DPEF the Parliament must be informed.

4.2 Setting the general government targets: local and regional government involvement

- *The contribution of each level of government to the general government balance*

Under the SGP, the central government undertakes commitments on behalf of the general government as a whole. While the central government is responsible for observing the Treaty and the SPG requirements, regional and local authorities may play a significant role in determining aggregate budgetary developments. Therefore the arrangements (or lack thereof) which oversee the relationship between the central and decentralised government could be an issue to the extent that the SGP requirements impact on state or local government finances.

Table 5 shows the general government budget balance for 2000 as reported in the March 2001 with a break down by government sector level. The figures indicate that local governments on average run roughly

Table 5

Budget balance, general government and government sub-sectors as reported in the March 2001 EDP reporting

2000, percent of GDP	General government	Central government	State government	Local government	Social security
B	0.0	-0.7	0.1	0.1	0.5
DK	2.5	1.4	-	-0.2	1.3
D	1.3	1.4	-0.5	0.3	0.1
EL	-0.9	-3.3	-	0.1	2.4
E	-0.3	-0.6	-0.3	0.0	0.5
F	-1.3	-2.2	-	0.3	0.6
IRL	4.5	4.2	-	0.0	0.4
I	-0.3	n.a	n.a	n.a	n.a
L	5.3	2.8	-	0.6	1.9
NL	2.0	0.3	-	0.2	1.5
A	-1.1	-1.4	0.2	0.1	-0.1
P	-1.4	-1.4	-	0.0	0.0
FIN	6.7	3.3	-	0.1	3.3
S	4.0	1.3	-	0.1	2.7
UK	2.1	2.0	-	0.1	-

Note: The EDP figures include UMTS receipts.

balanced budgets, and in any case do not inflict major deficits in national account terms. However, this does not mean that local governments do not run operating deficits as budget balances does not tell how much of expenditures are covered through transfers from central government. Planned operational deficits must generally be covered by transfers to balance the budget. However, higher than budgeted operational deficits must find additional financing, either through increased revenues (typically additional central government transfers implying higher central government expenditures) or by additional borrowing (implying a local government deficit).

- *Differing degrees of budgetary autonomy*

In most Member States, an important share of general government spending is carried out at local government level while the majority of taxes are raised at central government level. While depending on central government transfers, local and regional government are still autonomous to different degrees and can have an important impact on the general government budget position if operational deficits are channelled through to central government.

Therefore, the "financial significance[29]" of sub-national governments in an SGP context depends upon the part of total general government expenditure they account, and the existence of independent powers of borrowing and the possibility to claim transfers from the central government to cover financial shortfalls. A higher level of financial autonomy on the revenue side (defined in terms of the level of own receipts, including shares in centrally collected taxes, relative to expenditure), could reduce the "financial significance" of decentralised government as they would be able to find own financing in case of expenditure overruns. If, on the other hand, financial significance is high then the central government faces the problem of achieving a degree of control, be it through a mechanism of consultation and co-ordination or through a credible system of budgetary co-ordination rules.

[29] The term "financial significance" is used here to describe to what degree the development of local government finances needs to be controlled as they pose a risk for the general government budgetary position.

The Member States with the highest levels of financial autonomy are federal states such as Belgium, Germany[30], Spain and the Nordic Member States (where local governments traditionally have a high degree of autonomy). Also, Italy is going through a process of decentralisation. Member States that could be said to have a low degree of sub-national financial autonomy are France, the Netherlands, Ireland and the UK. In terms of the part of total expenditure which is accounted for by sub-national government, it would seem that Germany, Spain and the Nordic countries are at the higher end of the spectrum, while Ireland, the Netherlands and Portugal are at the lower end.

- *How central governments guide general government public finances*

Given these differences it is not surprising that Member States have different frameworks to guide general government finances. In countries where lower levels of government have a substantial financial autonomy, their inclusion in the elaboration of and responsibility for stability and convergence programme objectives may be an important issue. In other countries, borrowing by lower levels of government is firmly restricted and to the extent that these arrangements are reliable and effective, the need for a direct involvement of local government in the elaboration of the programmes is reduced. In general, the relative autonomy of local and regional governments is acknowledged and spending decisions and budgets can be made without interference from the central government. However, the central government keeps overall control by restricting lower levels of governments power to tax or change tax rates complemented by restrictions on borrowing possibilities.

In practice, as a pre-emptive co-ordination device, the central government in practically all Member States puts a boundary of some sort on lower level's finances. In a majority of Member States, local governments are only allowed to borrow to cover for investment expenditures, thus a "golden rule" applies. In addition, it is not uncommon that borrowing has to be directly sanctioned by the Ministry of Finance. A more radical form of arrangement is the adoption of a direct balanced budget constraint. Such a rule exists in Sweden local governments since

[30] Although in the case of Germany it may be questioned whether the degree of autonomy enjoyed by the Länder in setting revenue levels is really so high, given the important level of equalisation transfers.

1.1.2000, and requires local authorities to balance their budgets in every year (if they fail to comply, the situation must be corrected within two years). The Spanish government is also planning to introduce a similar law.

In addition to the possibility to restrict borrowing there may also be more explicit co-ordination frameworks. In federal states (Belgium, Germany, Spain and Austria) or Member States with strongly regionalised structure (Italy), this tends to be more important than in highly centralised countries.

In Belgium, the High Finance Council sets budgetary objectives for lower levels of government and the central government concludes agreements with communities and regions. In Germany, representatives from the federal government, the Bundesbank and Länder governments meet in Finance Planning Council ("Finanzplanungsrat") to discuss overall budgetary developments and plans. In Spain, central government and individual regions meet in the Fiscal and Financial Council to discuss budgetary matters and establishing the indebtedness limits for each region. A consultation system also exists in Denmark where there are negotiated agreements between central and local government. These normally encompass overall financial ceilings, a guideline for the overall development of expenditures and revenues. It is important to underline that these agreements are not legally binding, but rather a type of gentlemen's agreements.

A few countries have gone further and established so called "internal stability pacts" which are arrangements among the different levels of government aiming to clarify division of responsibility for budget discipline. This relates more directly to the requirements on general government finances introduced in the SGP. In such internal pacts, negotiations between the different levels of government can revolve around four axes: setting the objectives, ensuring their respect, identifying the responsibility for taking corrective action and sharing possible pecuniary sanctions in case of an excessive deficit. The internal pact can also contain a set of rules, which establishes the part of responsibility of local and regional authorities for the general government deficit. The pacts often set up joint committees to monitor budgetary developments at sub-national level and require sub-national governments to submit annual and multi-annual plans for their debt. Some agreements go so far as specifying the procedure to be followed in case of sanctions being applied at EU level for a breach of the excessive deficit procedure.

In Germany, the Länder have agreed that it is a common task of all levels of government to ensure the respect of the deficit target. Agreements of this sort can take the form of a joint declaration on the willingness to consolidate the budget balance. In Austria, each government entity is to pay a proportion of the sanction, in relation to its share of excessive deficit (in turn this depends to a large extent on the share of population living the territory). In Italy, the DPEF establishes budgetary targets for lower levels of government. Should Italy have an excessive deficit then "guilty" regions have to contribute to the potential fine. In addition, there are positive financial incentives to meet the targets also when the general government is not in excessive deficit.

Overall, of course the credibility of the internal pacts depends on the enforceability of the commitments, which in turn requires mechanisms such as a supervisory authority, conditionality of central government transfers or borrowing restrictions*)*. The jury is still out on the effectiveness of these domestic arrangements in ensuring that the goal of budgetary discipline is fully embodied in the political priorities of all government levels.

5. Concluding remarks

The discussion in this paper indicates budgetary procedures at the national level have allowed Member States to meet SGP requirements to date. National procedures have developed to improve their interaction with the EU multilateral surveillance framework. This particularly relates to developing medium term budgeting mechanisms and improving the co-ordination of national budgetary positions of the general government. Both these aspects are currently evolving.

Institutional change takes time and in general existing systems are only adapted when new demands create friction. In EMU, focus starts to shift away from pure budgetary consolidation towards aspects relating the "quality and sustainability" of public finances, that is, new issues come to the fore. Also, focus is turning towards the co-ordination of economic policies in the euro area and the role of how to integrate the BEPG in this context. There are currently ideas floating to streamline the submission dates of programmes and improve feed back mechanisms as well as creating a proper ex ante dimension in the EU surveillance process.

Against this background there could be pressure for additional institutional change at country level in the future, both from external and internal sources. Externally from the EU level as the EU framework is elaborated creating new demands. Domestically to the extent that budgetary players outside the central government become more directly affected by the commitments made at EU level making it more in their direct interest to become more involved.

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