COMMENTS ON SESSION III: FISCAL RULES AND BUDGETARY PROCEDURES

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I would like to start by saying that, as far as fiscal consolidation is concerned, the EU can be considered as a success story since 1995. Unfortunately this is a little disregarded when, in events like this workshop, fiscal policy and fiscal developments are discussed. And the success owes a lot to fiscal rules and budgetary procedures! Of course, there is no room for complacency and budgetary procedures - the topic of this session – can be clearly improved but the truth is that in 2000 the fiscal position of the EU was unambiguously better than five years earlier. This is the result of many factors on which I am not going to elaborate here. Let me just say that the scheme of incentives is by and large proving to be right. Of course, up to 1997 the incentive – the single currency – was very explicit. But we have to accept that fiscal consolidation did not stop there: we can argue that it could have been faster and of better quality, but we cannot deny that fiscal consolidation was not reversed.

Of course, *fiscal rules and budgetary procedures* played a role. Let me tell you my views on this issue, guided by the papers under discussion. As a starting point I think we should separate, as regards the EU countries, also in analytical terms, the *rules and procedures* (R & P) at national level and at the EU level, in particular at the euro-group level. I will argue that, while R & P at national level are in general *weak*, they are *strong* at the EU (euro-group) level. The overall balance, however, tilts towards the *strong* as evidenced by the good budgetary results achieved in 1995-2000. Which seems to suggest that, provided the R & P are adequately set at the EU (euro-group) level it is rather indifferent how the R & P are set at national level. Let me be very clear: of course that R & P must be improved at national level but such an improvement/setting is not a condition *sine qua non* for good fiscal behaviour, provided that at EU (euro-group) level *rules and procedures* are appropriately set and implemented.

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[*] European Commission. The views expressed here are the author's only.

Where does the *strength* of R & P at EU (euro-group) level come from? First, R & P at EU (euro-group) level are transparent in the sense that the rules of the game are known to players and the public in general; these are in the Treaty and the Stability and Growth Pact (SGP), which consists of legal texts. One of the criteria identified by Hemming and Kell seems therefore fulfilled. The first two years of implementation of the SGP provide clear evidence on transparency: stability/convergence programmes were made public annually by the Member State concerned (the Regulation obliges the Member State to make them public!) and the Council gave an Opinion on each of them, which was also made public (and published in the Official Journal); the implementation of the Pact is now in its third year which has allowed the building-up of a Commission/Council *doctrine* on each of the programmes thus constituting a kind of benchmark against which each Member State knows he is going to be judged. This means that we have now available, for each Member State, three programmes (more precisely, one programme rolled-over twice) and three Council Opinions. And all this is public. This is a non-negligible amount of information about budgetary intentions/outcomes of each Member State. Can we find another example of such transparency elsewhere?

Secondly, the intentions of the players are not only public but they consist of a multiannual budgetary programme. The importance of disposing of a multiannual framework for the government finances is emphasised in the papers presented to this session. Member States have, in general adhered to the budgetary projections presented in the programmes. Let me give an example: the table below displays the budgetary targets for 2001 as presented in the initial programme (submitted at least two years ago) and in the most recent updates. In all Member States the target for the actual deficit in 2001 is *better* than in the initial programme, in some cases with a wide margin; the only exception is Germany where the target remains unchanged. Of course we cannot conclude that the current targets for 2001 are those that would be achieved with the same *fiscal effort* as implicit in the initial programmes; probably not, if the method presented by Reitano and Fischer in their paper is correct. But the point I want to make is that no Member State significantly departed from the commitments they made publicly; more importantly, no u-turn was made. This provides evidence, in my view, that the stability/convergence programmes do matter for the budgetary process at national level.

Budgetary targets for 2001
(Government balance in % of GDP)

	Initial programme[1]	Latest update[2]
Euro area		
Belgium	-0.7	0.2
Germany	-1.5	-1.5
Greece	-0.8	0.5
Spain	-0.4	0.0
France	-1.6	-1.0
Ireland	1.6	4.3
Italy	-1.0	-0.8
Luxembourg	1.3	2.6
Netherlands	n.a.	0.7
Austria	-1.5	-0.75
Portugal	-1.2	-1.1
Finland	2.1	4.7
Non euro area		
Denmark	2.6	2.8
Sweden	2.5	3.5
United Kingdom	-0.1	0.6

[1] Submitted late in 1998/early 1999.
[2] Submitted late in 2000/early 2001.

Thirdly, the R & P at the EU level provide for a sort of an Independent Fiscal Authority (IFA) which is the European Commission. Hemming and Kell argue that the existence of an IFA can be very helpful to ensure fiscal discipline. In the framework of the institutional balance provided by the Treaty, the Commission has a unique role to play. I was already convinced of this, *et pour cause*… but I was definitely convinced when reading the papers presented to this session. In fact, in none of the R&P analysed in the papers one can find an institution like the Commission, although some would like to have one… I would just recall

that the Commission is an independent body, someway between the Member States and the Council and that (i) the Council acts upon recommendations/proposals from the Commission; for example, the Council Opinions on the programmes were all based on Commission's recommendations, which in turn were based on the Commission assessments of the programmes (ii) the public finance data are provided by the Commission, as regards the excessive deficit procedure and (iii) the Commission has the power to change the public finance data reported by Member States.

Last, the R & P include a sanction element, *strictu sensu* in the occurrence of an excessive deficit in the framework of the SGP or in the simpler form of a rebuke from the Council.

Of course, for the R & P at EU level to be efficient, Member States have to play the game right. And here the R & P at national level do matter. It goes without saying that stronger R&P at national level contribute to stronger R&P at EU level. Let me say a word about the fiscal rules in NL and SW in the light of the paper by Heering and Lindh. The NL have a very good record as far as budgetary outcomes are concerned. The budgetary results have been good, usually much better that expected. This is a positive aspect of the Dutch fiscal rule. But the Dutch fiscal rule is not very helpful as regards assessing ex-ante what are the intentions of the government and to assess compliance with the Stability and Growth Pact. This was expressed by the Council in its opinion on the 1999 updated stability programme: "*The Council considers that the Dutch method of using cautious growth assumptions and expenditure targeting and control has been instrumental in achieving the good results registered until now. However, this method also tends to make it more difficult to assess whether the medium-term outcome of the deficit is compatible with the requirements of the Stability and Growth Pact*"[1]. In addition the fiscal rule does not take into account, ex-ante, the cyclical position of the Dutch economy which, in phases of expansion, may lead to a wrong appreciation of the budgetary stance. As important as achieving better than planned results is to allow the other participants, in particular the eurogroup members, to understand if the fiscal stance will be appropriate. The fiscal rule in Sweden is from this

[1] Official Journal C 60, 2.3.2000, p. 1.

point of view clearer: in the budgetary bill for year t+1 the government (in September of year t) states how it will use the margin (if any) above the 2% of GDP surplus target, which is to be achieved over the cycle. For example in September 2000 the Swedish authorities stated that they would accept a surplus of 3.5% of GDP in 2001, clearly above target, but made possible by high projected growth and to avoid risks of overheating. In both countries the rules have so far worked well, but the test of *bad times* was not yet passed (hopefully there will never be a need for that!).

A final comment on Hemming and Kell's paper, where following Alesina and Perotti, they argue that a problem with the (balance budget) deficit rules is that they are inflexible, in particular because they are inconsistent with the use of fiscal policy to stabilise output. They might be right, but this criticism does not apply to the SGP, the fiscal rule of which is defined in terms of underlying budgetary position or structural balance. Indeed, the SGP objective of a "medium-term budgetary position of close to balance or in surplus" is to be interpreted in terms of structural, or cyclically-adjusted, budgetary balance. Once such a structural balance has been reached fiscal policy can (again!) play a stability role through the operation of the automatic stabilisers; this, in normal cyclical fluctuations, should not lead the government deficit to breach the 3% of GDP threshold. These have been the views of the Commission and the Council; to give just an example, in the Council opinion on the 2000 update of the stability programme for Finland it can be read *"The underlying budgetary position corresponding to the 4.5%* [of GDP] *expected surplus for 2000 will allow Finland to continue to fulfil the requirements of the Stability and Growth Pact"*[2].

[2] Official Journal C 374 of 28.12.2000, p. 5.