Box 8

FISCAL COUNCILS IN EU COUNTRIES

The recently enhanced EU fiscal governance framework inter alia broadened the role and tasks of national fiscal watchdogs in an attempt to foster budgetary discipline and to increase national ownership of EU fiscal rules.[1] Fiscal councils are generally defined as independent public institutions that are aimed at strengthening commitments to sustainable public finances. According to the so-called two-pack[2], euro area countries should have in place an independent body, such as a fiscal council, which is in charge of monitoring compliance with numerical fiscal rules and, where appropriate, assessing the need to activate the correction mechanism foreseen under the Fiscal Compact.[3] Moreover, macroeconomic projections should be produced or endorsed by an independent body, although this does not necessarily have to be the fiscal council. The deadline for setting up a fiscal council was October 2013.

The requirement to have a fiscal council in place is a major step towards strengthening national budgetary frameworks. Experience with such independent institutions, although still limited, shows that they can improve budgetary discipline when they monitor governments' compliance with fiscal targets, critically assess the appropriateness of fiscal policy-making and, as an independent voice, provide recommendations on specific fiscal policy questions.[4]

Generally, in order for fiscal councils to have a positive impact on fiscal policy-making, four features appear to be essential. Fiscal councils should: i) be strictly independent from political interference in order to build up or maintain institutional credibility; ii) have a comprehensive mandate, which also allows them to initiate their own assessments; iii) have sufficient resources to deliver their mandate; and iv) have a public voice, so that they are able, if necessary, to effectively mobilise public opinion in order to counteract political incentives for unsound fiscal policies. The requirements set out in the two-pack broadly meet these features.

This box provides an overview of recent efforts by EU Member States to establish fiscal councils and the specific forms these have taken.

Many fiscal councils have been set up recently

Today, 19 EU Member States have an operational fiscal council in place, which is almost four times as many as in 2007. Of these countries, 13 have recently established a new fiscal council (see table). In five countries, the mandate of existing public institutions – in most cases, a fiscal council – has been broadened to account for the requirements of the enhanced fiscal framework.

1 See the box entitled "Stronger EU economic governance framework comes into force" *Monthly Bulletin*, ECB, Frankfurt am Main, December 2011.
2 See the Official Journal of the European Union, OJ L 140, 27.05.2013, and the box entitled "The 'two-pack' regulations to strengthen economic governance in the euro area", *Monthly Bulletin*, ECB, Frankfurt am Main, April 2013.
3 The requirements for fiscal councils are primarily spelled out in the two-pack, which relates only to euro area countries. However, references to fiscal councils are also made in the Fiscal Compact, affecting all contracting parties, and in the European Commission's common principles, which were issued in June 2012.
4 See, for example, Debrun, X., Hauner, D. and Kumar, M.S., "Independent Fiscal Agencies", *Journal of Economic Surveys*, Vol. 23, 2009, pp. 44-81 for an assessment of the impact of fiscal rules and fiscal councils on fiscal performance, in which it is found that fiscal councils tend to have a positive impact on fiscal performance through the introduction or better enforcement of fiscal rules. See "The functions and impact of fiscal councils", IMF, 2013 for an analysis of how some of the key characteristics of fiscal councils, such as (functional) independence and an effective communication strategy, are correlated with better fiscal performance.

Overview of fiscal councils in the EU and their mandates

	Name	Year of establishment[1)]	Attached institution[2)]	Mandate					Appointment[4)]	Comply or explain
				Compliance fiscal rules	Correction mechanism	Macroeconomic projections				
						Produced[3)]	Endorsed	Assessed[3)]		
Belgium	High Council of Finance	2014 [1989]		x	x	S			G	x
Bulgaria		draft		x	x				P	
Czech Republic	--									
Denmark	Danish Economic Council	2014 [1962]		x		x			G	x
Germany	Stability Council/ Council of independent experts	2013 [2010]		x					G/O	
Estonia	Fiscal Council	2014	Central bank	x	x		x		O	x
Ireland	Irish Fiscal Advisory Council	2012		x			x		G	x
Greece		draft		x						x
Spain	Independent Authority of Fiscal Responsibility	2014		x	x		x		P	x
France	High Council on Public Finances	2013	National audit office	x	x			x	P/O	x
Croatia	Fiscal Policy Committee	2013		x	x			x	P	x
Italy	Parliamentary Budget Office	2014		x	x			x	P	x
Cyprus	Fiscal Council	2014		x	x		x		G	
Latvia	Fiscal Council	2014		x		x			P	
Lithuania		draft	National audit office	x	x		x			x
Luxembourg	Fiscal Council	draft		x	x			x	P/G/O	
Hungary	Fiscal Council	2008							O	
Malta	Fiscal Council	draft	National audit office	x				x		
Netherlands	Independent Budgetary Authority	2014	Council of State	x		S			G	x
Austria	Fiscal Advisory Council	2013 [1970]	Central bank	x	x	S			G/O	
Poland	--									
Portugal	Public Finance Council	2012		x	x				G/O	
Romania	Fiscal Council	2010		x	x		x		P	x
Slovenia		draft				S				
Slovakia	Council for Budget Responsibility	2012			x				P	
Finland	National Audit Office	2013		x				x	G	x
Sweden	Fiscal Policy Council	2007		x					G	
United Kingdom	Office of Budget Responsibility	2010		x		x			G	x

Source: ESCB.
1) Year of creation of the fiscal council, with the year given in brackets if the mandate has been broadened.
2) In case the fiscal council is attached to another public institution, such as the central bank, national audit office, etc.
3) Marked with "S", if done by a separate institution. For example, in Belgium, the Netherlands, Austria and Slovenia, macroeconomic projections are produced by a separate independent institution.
4) The column "Appointment" relates only to appointments of fiscal council members. "G" stands for appointed by the government/ministry; "P" stands for appointed by the parliament; "O" stands for others (e.g. the central bank).

The number of operational fiscal councils will increase further in the coming months. In several countries, a fiscal council has either already been legislated for, but the process of establishing the council still needs to be finalised and council members are being recruited, or draft legislation is currently being prepared or discussed. The only EU Member States in which no concrete legislative initiatives to establish a fiscal watchdog are currently being discussed are the Czech Republic and Poland; these two countries are not bound by the two-pack regulations.

In most countries, the fiscal councils are separate, independent public institutions that have their tasks and degree of functional autonomy defined in national legislation. In a few countries, however, fiscal councils are attached to another public institution, such as the central bank, the national audit office or the parliament (see table). Moreover, in some countries, the different tasks are assigned to various independent public institutions, such as in Belgium, the Netherlands and Austria, where a separate independent institution is in charge of conducting the macroeconomic projections.

What are the mandates of the fiscal councils in the EU?

The mandate of the fiscal councils in the EU differs considerably across countries. Not all fiscal councils in the euro area countries seem to have mandates that are fully in line with the requirements set out in the two-pack (which is not binding for non-euro area EU Member States). In most countries, the mandate of the fiscal council typically focuses on monitoring compliance with fiscal rules. In less than half of the EU Member States, fiscal councils also play a role in monitoring or assessing the activation of the correction mechanism, as spelled out in the Fiscal Compact, in case of considerable deviation from fiscal rules.

However, the involvement of fiscal councils in the preparation of macroeconomic and budgetary projections is less widespread. Only in some countries are own macroeconomic forecasts produced by fiscal councils or separate independent institutions (see table),[5] while, in a few countries, fiscal councils are expected to endorse the government's macroeconomic projections.[6] In turn, budgetary projections, which are produced in all countries by the government, are only scrutinised by an independent body for endorsement in Romania, Slovakia and the United Kingdom.[7] In several countries, the fiscal council is obliged to assess the government's projections, which as a tool is less strong than endorsement. Public assessments can play an important role in influencing public opinion. For example, in its advice of 23 April 2014 the High Council on Public Finances in France considered that, although the GDP growth assumptions of the government for 2014 were seen as realistic, the scenario for 2015, which also included substantial planned spending cuts, was regarded as being too optimistic, as it was based on the simultaneous realisation of several favourable assumptions.

In addition, in some countries, the tasks which fiscal councils have been assigned go beyond the requirements under the two-pack. In particular, almost half of the euro area fiscal councils or independent institutions assess the long-term sustainability of fiscal policy, while several of them

5 These countries include Belgium, Denmark, Latvia, the Netherlands, Austria, Slovenia and the United Kingdom. However, in Denmark and Latvia, the government is not obliged to use the forecast prepared by the fiscal council.
6 If fiscal councils are expected to endorse the projections, a procedure should be specified, including a deadline for action and provision of details on the potential consequences. Thus, a negative decision by the fiscal council should trigger a review of the forecasts, which would go beyond the "comply or explain" principle.
7 According to the two-pack regulations, governments may decide to involve an independent body in the preparation of the budgetary projections, but there is no obligation to do so.

also assess compliance with the debt/expenditure rules, the economic and financial situation of public enterprises, the cost of fiscal measures or the quality of public finances. Moreover, in some countries, fiscal councils are in charge of guiding the allocation of fiscal targets across different government layers, with the Independent Authority of Fiscal Responsibility in Spain being a recent example.

How effective will the fiscal councils be in fostering budgetary discipline?

Since, in most EU countries, fiscal councils have either only been created recently or their mandate has just been amended, and as there is considerable variation across countries in the precise set-up of fiscal councils and their (potential) influence on fiscal policy, it is difficult to assess their effectiveness at this stage.

Nevertheless, for a preliminary assessment of their effectiveness, it is already informative to look at how much potential room for manoeuvre they have. On average, the fiscal councils' room for manoeuvre and their leverage seem to be rather limited. The government is not obliged in any of the euro area countries to take into account the policy recommendations of the fiscal council.[8] In a number of countries, however, a softer tool for peer pressure is in place in the form of the "comply or explain" principle.[9] This requires that governments either comply with the fiscal councils' recommendations or publicly explain the reasons for deviating from them. In the majority of euro area countries, no corrective follow-up is foreseen in case of non-compliance. Nevertheless, even without any legal requirement for the government to react to the recommendations, fiscal councils can make effective use of the possibility to exert peer pressure on the government through their influence on public opinion. One recent example in this respect is the critical assessment issued by Austria's Fiskalrat (Fiscal Advisory Council) on 19 May 2014 of the government's budgetary plans, which was cited widely in the national media.

Moreover, the effectiveness of fiscal councils will largely depend on whether they are independent from political interference and whether they have functional autonomy. A fully independent and credible fiscal council increases the political cost for the government to deviate from its commitments. It is thus important that political interference is legally prohibited and that the council members are appointed based on competence and experience rather than political preference. Indeed, there are some encouraging examples among EU Member States with regard to the way in which the fiscal councils are set up. For example, in most countries the fiscal council members are academics or experts outside of the government. Also, their staff is mostly recruited on the basis of competence and experience. However, in some countries, there are also risks related to political interference, in particular where the government appoints fiscal council members rather than the parliament, and the supporting staff members are seconded from public entities (see the table). Moreover, in some countries, the resources of expert-level staff may not always be sufficient, which could prevent the fiscal councils from carrying out their tasks to a high quality. In most cases, the number of expert staff supporting the fiscal council members ranges from between two and ten staff members. However, there are also notable exceptions, with some councils having considerably more staff (in particular where the fiscal council is also involved in the projections).

8 Outside the euro area, the fiscal council of Croatia has, for example, a high degree of leverage.
9 These countries include Belgium, Germany, Ireland, Spain, France, Italy, Lithuania, the Netherlands and Finland. One important weakness of the two-pack legislation is that it neither requires the countries to establish the "comply or explain" principle (with the exception of macroeconomic projections, which need to be produced or endorsed) nor obliges governments to take the council's recommendations on board.

Conclusions

The revised EU fiscal framework requires Member States to establish a fiscal council that is in charge of monitoring compliance with numerical fiscal rules and assessing the need to activate the correction mechanism. This is an important step towards achieving better fiscal discipline and increasing national ownership of EU fiscal rules. It is very encouraging that all euro area countries have already set up a fiscal council or are in the process of doing so. Those countries that have not yet legislated for a fiscal council, should complete the process as quickly as possible. There is heterogeneity across countries in the way in which the fiscal councils are set up. While this also reflects country-specific circumstances, in some countries the features of the fiscal councils might raise concerns regarding their independence from government interference, their resources and mandate, as well as their room for manoeuvre. However, it will only be possible to perform a full assessment in order to determine their effectiveness once they have been operational for a few years.