



Independent Authority
for Fiscal Responsibility

CAN IFIs EXTEND THEIR REACH TO SUB-NATIONAL GOVERNMENTS? THE CASE OF SPAIN

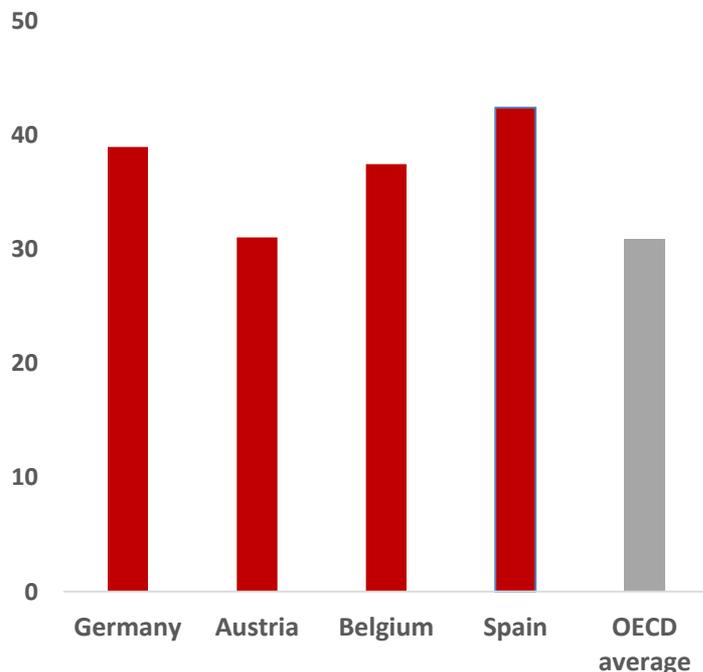
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1. Overview of Sub-national Public Finances in Spain

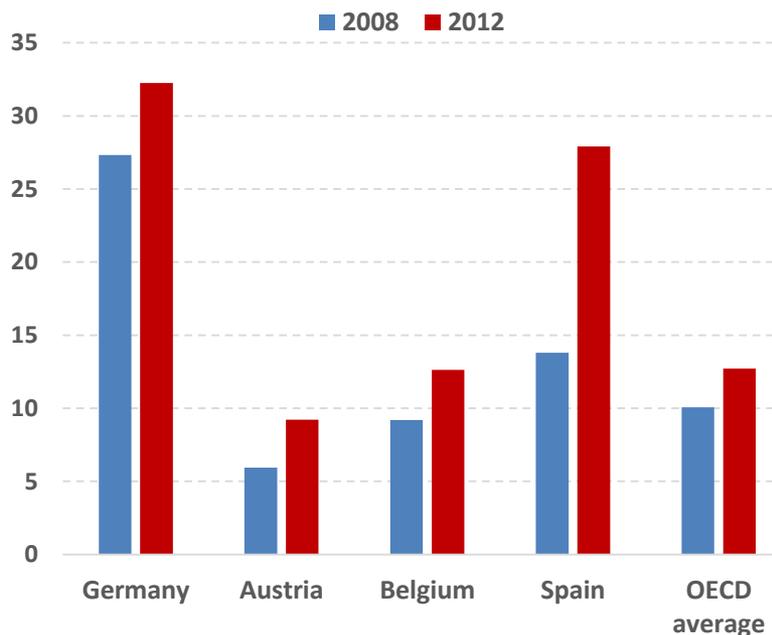
- ❖ One of the countries with the highest degree of decentralization and 2 levels of subnational governments (regions and municipalities).

Share of subnational expenditure
Compared to total public expenditure
(%, 2013)



Sources: OECD Fiscal Decentralisation Database. Social Security included in total public expenditure.

Subnational consolidated gross debt
% of GDP

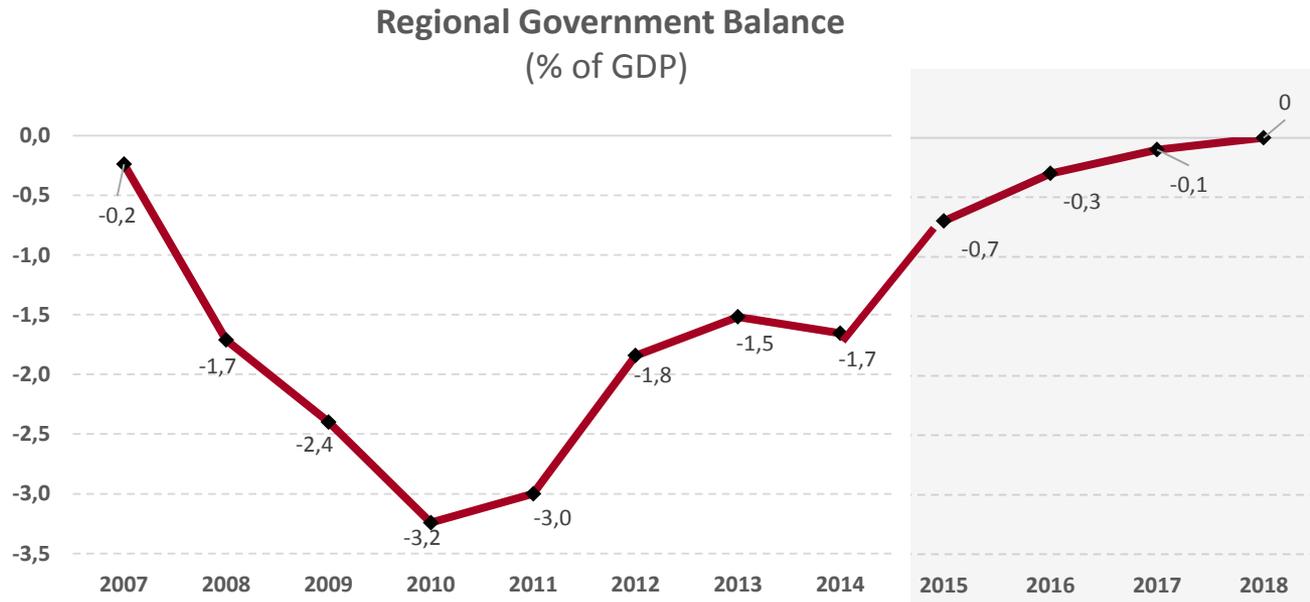


Sources: OECD Fiscal Decentralisation Database



1. Overview of Sub-national Public Finances in Spain:

- ❖ Half way of consolidation strategy: *towards budgetary balance in 2018.*

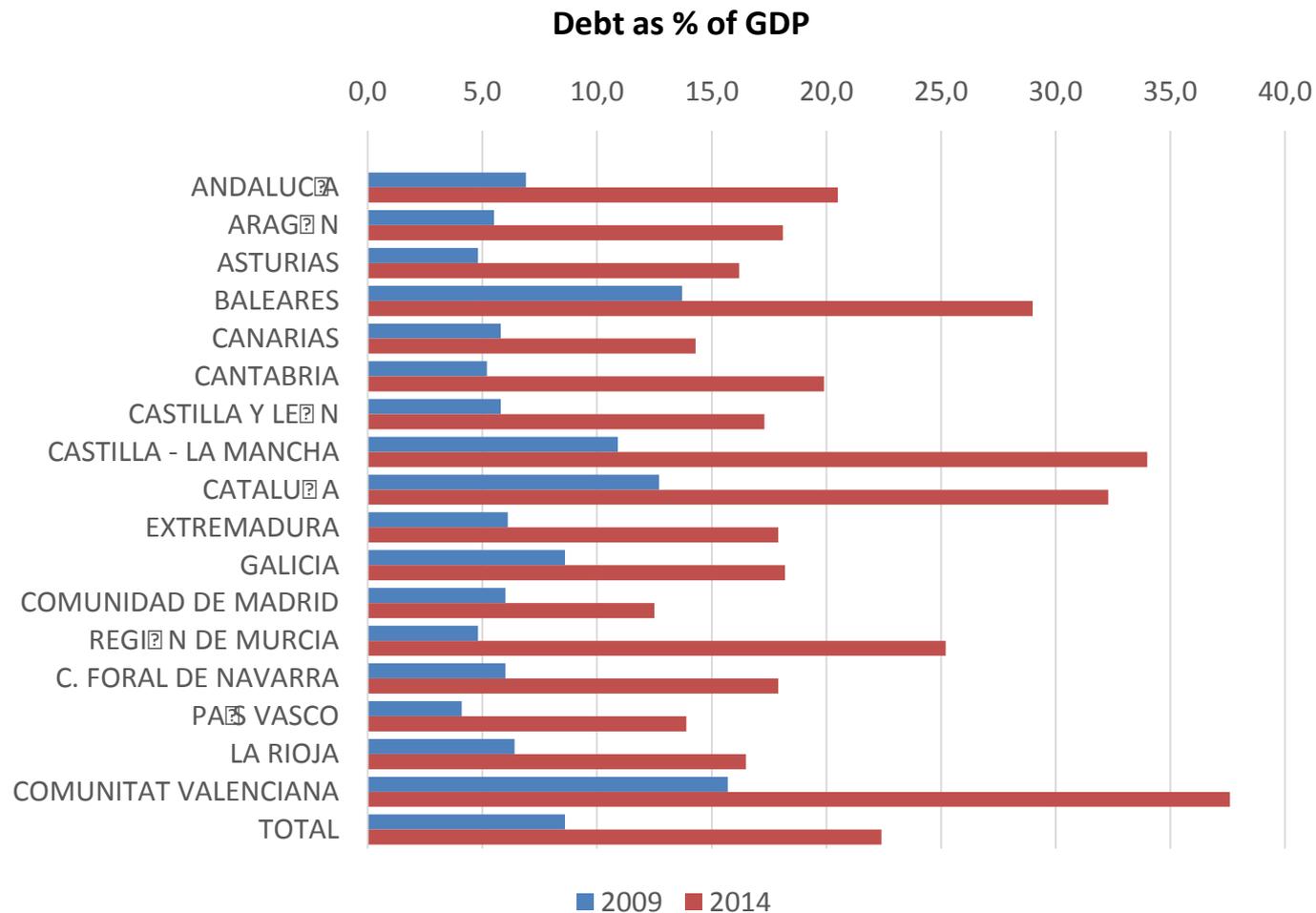


Note: adjusted with the regularisations of commercial debt operations in 2009 and 2011 and excluding for 2010 and 2011 the final settlement of the regional financing system.

Source: IGAE and AIReF calculations.

1. Overview of Sub-national Public Finances in Spain

Significant differences across regions



Source: Bank of Spain.

2. An strategy to address regional imbalances based on 4 pillars

1. Stronger fiscal disciplinary framework

- Budgetary stability principle at the **highest normative level**: Constitution + Organic Act.
- **ALL levels of public administrations** (regions and municipalities) **subject to same rules**: budget balance (no deficits allowed in structural terms for regions); debt rule; and expenditure rule. **Commercial debt and payments arrears included under the fiscal sustainability principle.**
- **Subnational enforcement mechanisms strongly reinforced**:
 - Preventive: risk of non-compliance → early warning by central government.
 - Corrective: non-compliance → automatic measures (i.e., debt authorisations) + rebalancing plans (RP)
 - Penalties: Gradually applied: expenditure freeze; interest-bearing deposit; formal audit missions or even subnational governments are put into receivership.

2. Improving transparency

- **Information requirements become mandatory** (previously not binding): Oct 2012 Ministerial Order.
- **Extremely detailed regulation on**:
 - who provides what and how (electronic means) .
 - Information becomes public and available in a single database: [*The General Government Financial Information Center: Ministerio de Hacienda y Administraciones Públicas*](#)
 - Non-compliance is made public and could trigger automatic corrective measures.
- **Some examples of informational gains**:
 - Ex- ante control: annual draft budgets; medium-term budgetary frameworks.
 - Budgetary implementation: monthly (cash and national accounts) for regions and quarterly for municipalities.
 - RPs and their follow-up reports.
 - Human resources (expenditure, structure, staff size
 - Since May 2015: monthly information on the subnational financing system in national accounts terms.

2. An strategy to address regional imbalances based on 4 pillars

3. Central government financial support to face liquidity constraints

➤ **Subnational governments suffer severe financing problems:**

- Loss of access to financial markets
- Arrears to suppliers

} ***Requiring central government financing***

- **Strict financial and fiscal conditionality in exchange for this extraordinary financing.**
- **Average period of payment starting to be closely monitored.**

4. Voluntary agreements between central and subnational governments

➤ **Rationalise the regional public sector:**

- 2010 and 2012 agreements adopted within the Fiscal and Financial Policy Council – FFPC- (25% reduction in the units of the regional public sector since 2010)

➤ **Seek efficiency gains in the subnational administration:**

- Measures to remove duplicities (Commission for the Reform of the Public Administrations).

➤ **Efficiency on public expenditure:**

- Working group on efficiency and rationalisation of expenditure (in progress)

3. AIREF significant contributes to 3 of the pillars

Pillars	AIREF's contribution
<p>1. Stronger fiscal disciplinary framework</p>	<p>AIREF monitors the whole budgetary cycle: grey (regions and municipalities); pink (only regions).</p> <div style="display: flex; justify-content: space-around; align-items: flex-start;"> <div style="border: 2px solid #800000; border-radius: 15px; padding: 10px; width: 30%; background-color: #800000; color: white;"> <p style="text-align: center; color: #4169E1; text-decoration: underline;">Fiscal Policy Planning</p> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #F08080; color: black; text-align: center;"> Regional budgetary Targets </div> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #F08080; color: black; text-align: center;"> Regional macroeconomic Forecasts </div> </div> <div style="border: 2px solid #800000; border-radius: 15px; padding: 10px; width: 30%; background-color: #800000; color: white;"> <p style="text-align: center; color: white;">Budgetary monitoring</p> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #D3D3D3; color: black; text-align: center;"> <u>Ex ante</u> Draft budgets </div> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #D3D3D3; color: black; text-align: center;"> <u>In year</u> Approved budgets Identification of risks </div> </div> <div style="border: 2px solid #800000; border-radius: 15px; padding: 10px; width: 30%; background-color: #800000; color: white;"> <p style="text-align: center; color: white;">Enforcement</p> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #D3D3D3; color: black; text-align: center;"> Asking central government to activate all the preventive, corrective and coercive mechanisms (7 regions in 2014) </div> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #F08080; color: #4169E1; text-align: center; text-decoration: underline;"> Rebalancing Plans </div> </div> </div>
<p>2. Improving transparency</p>	<ul style="list-style-type: none"> ➤ Reports and methodologies are public. <i>AIREF - Autoridad Independiente de Responsabilidad Fiscal</i> ➤ Many recommendations directly aimed at reinforcing transparency. (making assumptions explicit) ➤ Comply or Explain principle.
<p>3. Financial support</p>	
<p>4. Voluntary agreements</p>	<ul style="list-style-type: none"> ➤ Attending meetings of the two coordinating bodies. ➤ Studies requested by: <ul style="list-style-type: none"> ○ the coordinating bodies. ○ individual regions and municipalities, provided their scope does not go beyond their powers. In such a case, the request must be made by the coordinating bodies. ➤ Close dialogue with subnationals.



FISCAL POLICY PLANNING

Regional fiscal targets (forthcoming- July 2015)

Two-fold aim of this report:

- Report on the central government proposal for the following 3 years
- Input for the FFPC debate.

Open regulation : *“the specific situation of each administration must be taken into account”.*

2015 is the first year it will be done: a **challenge** for AIReF since regional fiscal performance in 2015 may require changes in the way targets have been set so far (same target for all regions).

Timing :

- June: methodology
- First half of July: publication.

Regional macroeconomic forecasts for 2015 (Dec-2014)

Aim: endorse and detect bias.

Scope: restricted to regions with different forecasts from the State Budget (13 regions in 2015).

Main conclusions :

- Forecasts **endorsed** but in 2 cases described as unlikely.
- Macro forecasts no direct influence on budget planning.

Main recommendations:

- Compare forecasts with other independent forecasts.
- Make assumptions and methods explicit.

Tools: 2 models developed to robustly assess forecasts:

- Extrapolation of the historical performance of each region with respect to the whole economy.
- Statistical forecasting model including information on regional economic indicators.

Since June quarterly estimates of regional GDP have been published. AIReF is first institution to provide this information.

BUDGETARY MONITORING: EX ANTE

Aim: assessing adequacy to meet the fiscal targets (deficit, debt and expenditure rule)

Draft budgets - (Oct and Dec-2014)

Information problems: reports on each region postponed to December/ municipalities only at aggregate level.

Tools: in-house models to estimate most relevant budgetary items.

	Conclusions	Recommendations
Oct	<p>Regions: main source of risk to meet the 2015 general government target (revenues overestimated; consolidation fatigue)</p> <p>Municipalities: 2015 target feasible but risks (uncertainty on the impact of the local reform)</p>	<p>Need to adopt measures & more information</p> <p>Closer monitoring of the local reform</p>
Dec	<p>High risk of deviation of the 2014 target in 7 regions.</p> <p>High risk of deviation of the 2015 target for the whole sector. But significant differences across regions: risk of deviation identified in 9 ARs, being particularly high in 5 of them.</p>	<p>Case to activate the warning mechanisms (art.19) so that regions can adopt measures before the deviation materialises.</p> <p>Case to activate automatic preventive measure envisaged (art 18.1)</p>

BUDGETARY MONITORING: IN YEAR

Approved budgets (March-2015)

Updates to draft budgets report with new information.

Conclusions: draft budgets assessment confirmed.

Focus on enforcement is reinforced - AIReF encourages:

- the Ministry to facilitate timely adoption of the rebalancing plans.
- and consider the adoption of coercive measures

Risks assessment (forthcoming – 15 July 2015)

- **Aim:** assess risk of non-compliance in the current year and inform directly those regions and municipalities at risk. The Ministry of Finance and Public Administrations must also be informed.

Key report to trigger the mechanisms to prevent and correct fiscal deviations.

- **It will cover all public administrations. As for subnationals the report will assess:**
 - **Regions:** the whole subsector + each of the 17 regions
 - **Municipalities:** the whole subsector + municipalities (capital of province) with more than half a million people (Barcelona, Madrid, Málaga, Sevilla, Valencia y Zaragoza).
- **Information: differences in availability:**
 - **Regions:** monthly information on national accounts basis with 2 months time lag (data up to April).
 - **Municipalities :** quarterly information (latest data March).

ENFORCEMENT

Assessment of Rebalancing Plans (RP) of regions

- One of the **main corrective measures**.
- Mandatory assessment **prior to approval by the FFPC**.
- **2014 implementation:**
 - 1 out of the 6 RPs were approved in due time.
 - The remaining RPs approved in December or even January 2015 so hampering effectiveness.
- **2015 situation:**
 - 14 RPs to be presented.
 - Extension of the deadline (end June) following request by some regions.
 - Difficult political context.



This 1st year of activity proves AIReF can certainly reach sub-nationals

Positive and encouraging outcomes:

- **Recommendations** are delivering (i.e. those on approved budgets issued in May)
- **Information** requests are being met.
- **Constructive** dialogue.

Why?

- Non-partisan and independent entity that safeguards a **consistent monitoring** of the fiscal framework and ensures **equal treatment**.
- Making an effort to develop **analytical tools appropriate for assessing subnationals** (i.e. quarterly GDP estimates; sustainability analysis at regional level). Analytical capacity.
- AIReF is absolutely **transparent and predictable with everything** (reports and methodologies published)

It seems AIReF is gaining credibility vis a vis regions and is increasingly perceived as useful institution



Some areas of improvement

Reinforcement of the effectiveness of the “comply or explain” principle if needed

One step further in the current strategy?



March Resolution 2015 already established a new and clear follow-up procedure

- More active **communication strategy**?
- Be more **reiterative**?
- Reinforce **direct communication**?
- **Normative** reinforcement?

Address the **information management challenge** posed by the high number of entities to monitor.

Work in progress



- Development of analytical tools for **early detection** of risks
- The particular case of **municipalities**
- Workload linked to the assessment of **regions** **RP**



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