



Independent Authority
for Fiscal Responsibility

Report

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2017 Joint assessment of the budget stability target of Public Administrations

The mission of AIReF, the Independent Authority for Fiscal Responsibility, is to ensure strict compliance with the principles of budgetary stability and financial sustainability contained in article 135 of the Spanish Constitution.

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The AireF has to express its view on the compliance of the fiscal rules in several moments of the budget cycle. The reports to be submitted by the AIReF regarding the compliance with the fiscal rules in a specific year start off early on with the submission of the main guidelines and budget projects, and even before, in the case of the Autonomous Regions, when assessing the proposal of horizontal distribution of targets.

The 2017 budget cycle has been determined by the adjustment of the fiscal consolidation path and the existence of a caretaker central government, a situation which affected the AIReF's calendar for the issue of reports. Last August the European Council extended the deadline until 2018 so that Spain could correct its excessive deficit, thus changing the stability target for 2017. The existence of a caretaker central government until October 2016 and the vertical distribution of this new target among the different levels of government have delayed the submission of budgets in the different Public Administrations.

The reports forecasted in the Article 17 section 1 and 2 of the Organic Law on Budgeting Stability and Financial Sustainability (LOEPSF) have been delayed and fragmented in order to speed up the assessment to be carried out by the AIReF as the budgetary documents were submitted. In accordance with the provisions in the LOEPSF and the implementing regulations of the AIReF, this institution has to publish before the 15th of October a report on the project of the State General Budget and the budget guidelines of the Autonomous Regions and Local Corporations taking into account their compliance with the expenditure rule and the targets of budget stability and Government debt. Likewise, prior to the 1st of April, the AIReF has to report the budgets already approved taking into consideration the variations with regard to the previous report. However, the exceptional circumstances formerly mentioned have caused a general delay, yet of uneven duration, in the submission of the budget projects. For this reason, the AIReF has fragmented the content of these reports in order to accelerate the assessment of the budgetary documents as these were available.

Until the submission of the PGE, last 4th of April, the AIReF has not been able to express a view regarding the Public Administrations as a whole. In the months of December 2016 and February 2017, the AIReF assessed the budgetary documents of the Regional Governments which, depending on the situation of each administration, were immersed in different moments of the process of elaboration, debate and approval¹. Last 4th of April the Central Government presented the State General Budget project for its processing by the General Courts, meaning that the AIReF is now able to carry out a joint assessment of the budget projects and/or the budgets approved by the Public Administrations in order to check their compliance with the targets of budget stability, debt and expenditure rule of 2017.

¹ Document published on the 7th of December 2016 [Report on the Projects and Main Budgetary Lines of Public Administrations: Local Corporations 2017](#)

Document published on the 14th of February 2017 [Report on Autonomous Region Initial Budgets for 2017](#)

The target of budget stability for the whole Public Administrations, established at a 3.1% of the GDP for 2017, requires and adjustment of 1.4 points of the GDP with regard to the closure of 2016, which the AIReF deems feasible. The Public Administrations' deficit in 2016 reached a -4.5% of the GDP (see table 1 and 2). The accomplishment of the 2017's target will entail carrying out a consolidation adjustment of 1.4 percentage points of the GDP, non-recurrent operations regarding 2016's closure discounted, with the Central Government (CG) being the subsector with a higher adjustment to carry out.

TABLE 1. 2017 BUDGET STABILITY TARGET

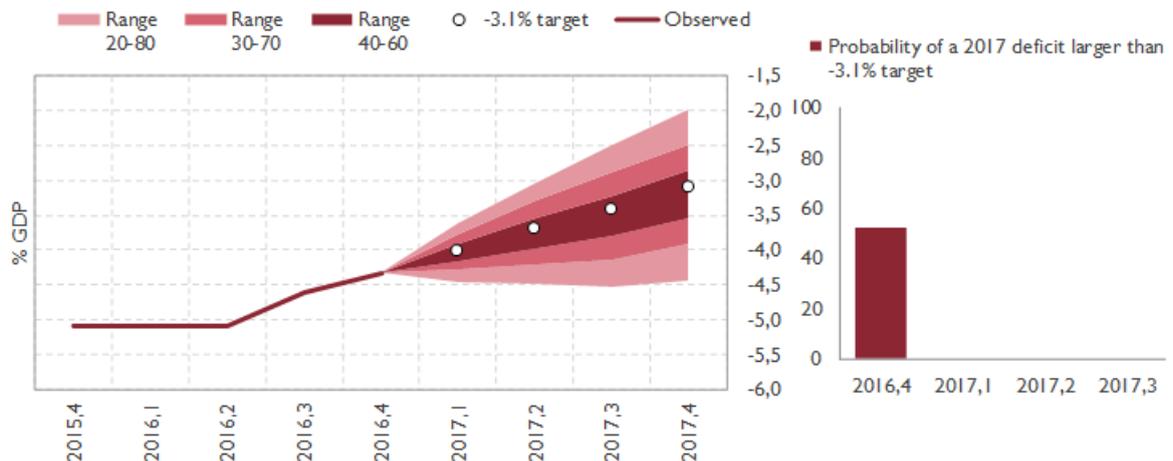
Funding capacity (+)/ necessity (-) in % of GDP	2016 Target	2016 Closure	2016 closure without non-recurrent measures	2017 Target
Central Government	-2.2	-2.7	-2.8	-1.1
Social Security	-1.7	-1.6	-1.6	-1.4
Autonomous Regions	-0.7	-0.8	-0.7	-0.6
Local Entities	0.0	-0.6	-0.6	0.0
Total Public Administrations	-4.6	-4.5	-4.5	-3.1

TABLE 2. NON-RECURRENT OPERATIONS BY SUBSECTORS

Non-recurrent operations	2016
Nominal balance	-4.5
Financial support	-0.2
Pre-payment	0.3
Non-recurrent elements	-0.1
Non-recurrent adjusted balance	-4.5

This feasibility regarding the accomplishment of the stability target relies on the assumption by which the likely deviation of the Central Government and the Social Security will be compensated by the surplus registered by the local subsector. According to the AIReF's estimates, the main risk of non-compliance of the budget stability target for 2017 relies on the CG, which has to carry out an adjustment of 1.7 percentage points of the GDP to reach the target. On the other hand, the Social Security Funds will have to carry out a lower adjustment, around two tenths of a percent of GDP, having to face the structural problems which will hinder the deficit reduction. However, the foreseeable compliance of the subsector of the Autonomous Regions and the consolidation of the surplus of the Local Corporations could be enough to compensate the deviations of the CG and Social Security Funds.

GRAPH I. LIKELIHOOD OF COMPLIANCE WITH THE BUDGET STABILITY TARGET FOR THE PUBLIC ADMINISTRATIONS AS A WHOLE



The lack of adaptation of the stability target to the financial situation of the local subsector, together with the lack of consideration of the expenditure rule with regard to its establishment, distorts the distribution of the joint stability target among the different government levels. The Local Corporations have been recording a surplus of around half a percentage point of the GDP as a consequence of the stability of its revenues and the implementation of the expenditure rule, which keeps the non-financial uses of this subsector underneath its resources. Nevertheless, and although the LOEPSF points out in its article 11 that the Local Corporations *should remain in a position of budget balance or surplus*, the stability target established for this subsector is always 0%, which in practice leads to a budget scenario in which expenditure does not exceed a 60% approximately. The latent surplus in balanced local budgets usually compensates the higher deficits of other administrations whose revenue and expenditure scenarios are quite unrealistic and do not seem to fit in with the assigned budget stability target.

When carrying out a joint assessment of all the Public Administrations, this distortion in the vertical distribution of fiscal targets creates inconsistencies within the framework of fiscal discipline established by the LOEPSF, to be individually implemented by each administration. The fiscal discipline framework provided by the LOEPSF is of a highly preventive nature so that when non-compliance risks towards the deficit, debt and expenditure rule targets are detected, the corresponding administration takes the necessary measures to correct the potential deviations. Besides, the Regional Governments can resort to a phased procedure of activation of measures implemented by the Ministry of Finance and Public Service

(MIHAFP) and the Autonomous Regions ² in the event that the latter would assume the financial guardianship of the Local Corporations in their territorial scope. The lack of acknowledgment of the local surplus within the process of establishment of the budget stability targets in the different government levels could lead to a situation in which the strict compliance with the fiscal rules by each and every administration, by adopting the necessary measures, would end up providing a better result than the one required from the Public Administrations as a whole.

On the other hand, the LOEPSF does not consider implementing for the Central Government a similar preventive procedure to the one existing for the Regional Governments in the event of detecting deviation risks. The LOEPSF aims its preventive side more at the Regional Governments rather than at the Central Government, which can only resort to the self-discipline forecasted, in general terms, in the article 18 for all the Public Administrations. Thereby, the article 19 of the LOEPSF only foresees the warning of non-compliance risk as a device to resort to in the case this risk exists in an Autonomous Region or a Local Corporation. The current situation, in which the risk of non-compliance with the 2017 stability targets by the Central Government is a reality, requires solving this legal gap and urgently establishing an internal monitoring procedure which would allow correcting the likely deviation.

Analysis by subsectors

Central Government

The lack of information regarding the adjustments of national accounting determines significantly the possibility of giving an opinion on the compliance of the State General Budget Project with the deficit target of 1.1% of the GDP. The assessment of the stability target for 2017 has been determined by the lack of information included in the State General Budget Project concerning the adjustments of national accounting which allow comparing the budget deficit with the budget stability target defined in terms of national accounting. The LOEPSF compels the different Public Administrations to include in the budgets the necessary information to verify the compliance with the budget stability and financial sustainability targets. Similarly, the European Community regulation demands this same coherence between the budget implementation data. However, the budgetary documents presented, unlike previous years, do not contain the information concerning the adjustments which establish consistency between the budget balance and the national accounts.

Despite the lack of information regarding the adjustments of national accounting, the AIReF has carried out its own estimates of the compliance with the -1.1% target of the GDP established, unlikely to be accomplished by the CG. Under the assumption that the

² In the case of the Basque Country, the bodies in charge of the financial guardianship of the city councils in the corresponding territorial sphere are the Provincial Councils.

fiscal measures included in the Royal Decree-Law 3/2016 achieve all their effects, the budget scenarios of revenue and expenditure seem realistic overall, even though according to the data presented these would be insufficient for this subsector to carry out the adjustment needed of more than one and a half point of the GDP. The non-financial revenues and expenses of the State in terms of budget, without any adjustment in the national accounting, establish a deficit of 1.8% of the GDP. Without being able still to determine the potential surplus of the different bodies, the adjustments of national accounting which would make the budget balance of the State consistent with the targets in terms of national accounting are around 7 tenths of a percent of GDP, a figure well above that of previous years in the State General Budget Projects.

The State General Budget does not include information about contingent liabilities nor about their possible impact in 2017. The evolution of non-financial uses of the CG could be affected in 2017 by the potential impact of some pending procedures of financial liability such as the “*sanitary cent sentence*” or the one derived from the “*toll motorways*”. In the event of a materialisation of these or other risks linked to the bank restructuring process, the difficulty of accomplishing the stability target would be even bigger.

Social Security Funds

The projections of the AIReF for 2017 estimate a similar deficit to that of the closure of 2016 (1.6% of the GDP), which reveals the risk of non-compliance of the budget stability target, established at -1.4% of the GDP. This deviation with regard to the target would mainly affect the growth of the contributions, which AIReF estimates at a 4.6%, a percentage which is slightly more than one percentage point under the projections of the 2017 State General Budget Project³. Despite the strong growth of contributions, the resources will be affected as a whole by the decrease of transferences received from the CG to balance the State Public Employment Service (SEPE). In respect of the non-financial uses, the AIReF estimates that they will maintain their moderate growth, with an increase in pensions of about 3%, in accordance with the projection of the State General Budget Project.

The budgets of the Social Security System have incorporated for the first time information regarding the calculation of the Pension Revaluation Index (PRI). The Economic and Financial Report of the Social Security incorporates a new section about the revaluation of pensions which includes data of the revenues, the evolution of the number of pensions and of the substitution effect for each one of the years of the period 2011-2017 and the projection of average growth of these variables for the period 2017-2022.

³ Including the Social Security System, SEPE and FOGASA, the contributions foreseen in the budget increase at a rate near to 6%.

Autonomous Regions

The AIReF considers that compliance with the stability target of **-0.6% of the GDP** by the Autonomous Regions is feasible. The increase of resources of the funding system in 2017 puts the whole subsector in a very favourable position in order to carry out the **two tenths of percentage points' adjustment of the GDP needed to accomplish the target established for 2017**. As for the evolution of resources, a growth of more than a 6% is expected for the Autonomous Regions with regard to the previous year. The data of the resources of the autonomous funding system included in the project of the State General Budget for 2017 establish the growth of these resources in a 5.7%. On the other hand, taking into account the 2016's closure, the AIReF considers that the rest of the income could increase at a rate above the 6% due to the expected evolution of the revenues from the European Union (EU). In the case of the uses, the information available indicates that the growth could be around 4% with regard to the previous year's level, keeping its weight in terms of GDP.

At the individual level, with the data from the 2016 closure and once the non-recurrent operations of this year have been discounted, the difference observed in the effort demanded between the best and worst positioned Autonomous Region is of more than one percentage point. For almost half of the Autonomous Regions the target for 2017 allows the increase of their deficit with regard to 2016, although this situation could be corrected, to a greater or lesser extent, with the compliance with the expenditure rule, which could be more restrictive in these regions.

TABLE 3. LIKELIHOOD OF AUTONOMOUS REGIONS' COMPLIANCE WITH THE STABILITY TARGET FOR 2017

In % of the GDP

AUTONOMOUS REGIONS	2016 closure	2016 closure / Non-recurrent operations discounted	2017 Target	Difference	Likelihood of compliance with the 2017 target	Increase of resources
	(a)	(b)	(c)	(b-c)		
Andalucía	-0.6%	-0.5%	-0.6%	0.1%	Probable	0.5%
Aragón	-1.1%	-1.1%	-0.6%	-0.5%	Unlikely	0.4%
Asturias	-0.5%	-0.3%	-0.6%	0.3%	Probable	0.2%
Illes Balears	-0.4%	-0.3%	-0.6%	0.3%	Very likely	0.7%
Canarias	-0.3%	-0.2%	-0.6%	0.4%	Very likely	1.1%
Cantabria	-1.5%	-1.4%	-0.6%	-0.8%	Very unlikely	0.9%
Castilla y León	-0.6%	-0.5%	-0.6%	0.1%	Feasible	0.3%
Castilla-La Mancha	-0.7%	-0.7%	-0.6%	-0.1%	Feasible	0.3%
Cataluña	-0.9%	-0.9%	-0.6%	-0.3%	Feasible	0.5%
Extremadura	-1.6%	-1.3%	-0.6%	-0.7%	Very unlikely	0.4%
Galicia	-0.5%	-0.4%	-0.6%	0.2%	Probable	0.4%
Comunidad de Madrid	-0.6%	-0.7%	-0.6%	-0.1%	Probable	0.4%
Región de Murcia	-1.7%	-1.7%	-0.6%	-1.1%	Very unlikely	0.6%
CF de Navarra	-0.7%	-0.6%	-0.6%	0.0%	Unlikely	0.0%
País Vasco	-0.7%	-0.7%	-0.6%	-0.1%	Feasible	0.0%
La Rioja	-0.5%	-0.4%	-0.6%	0.2%	Very likely	0.4%
Comunitat Valenciana	-1.5%	-1.4%	-0.6%	-0.8%	Unlikely	0.8%
Subsector	-0.8%	0.8%	-0.6%	-0.2%	Feasible	0.5%

The AIReF distinguishes between two groups of Autonomous Regions (see table and graph 3):

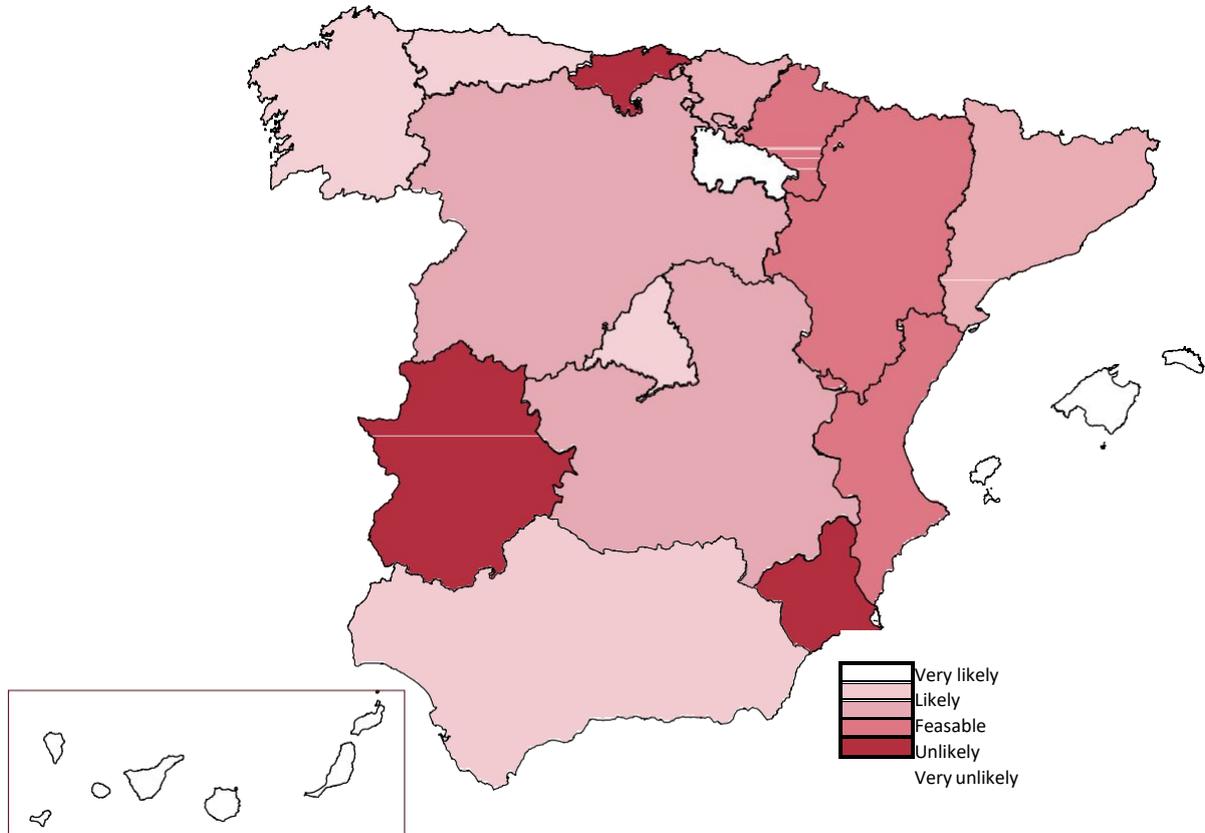
– **11 Autonomous Regions in which the budget implementation would allow to accomplish the target, with a different degree of probability.** This group would include the following Autonomous Regions:

- Very likely: Illes Balears, Canarias y La Rioja
- Probable: Andalucía, Asturias, Galicia y Madrid
- Feasible: Castilla y León, Castilla-La Mancha, Cataluña y País Vasco

– **6 Autonomous Regions in which, with the current information available, the AIReF considers that the implementation of the budgetary documents would not allow accomplishing the target established.** This group would include the following Autonomous Regions:

- Unlikely: Aragón, Navarra y Comunitat Valenciana
- Very unlikely: Cantabria, Extremadura y Murcia

GRAPH 2. SCALE OF LIKELIHOOD OF COMPLIANCE WITH THE 2017 STABILITY TARGET



Local corporations

The AIReF considers very likely that the subsector of Local Corporations will be able to accomplish the budget stability target in 2017 and obtain a surplus at closure which will consolidate, at least, the results of 2016. The foreseeable consolidation in 2017 of the last implementation data published of 2016, together with the potential effect of the delay in the approval of the State General Budget on the implementation of financially sustainable investments, point out that the local surplus at the end of this year could be slightly higher than the one obtained in 2016.

The biggest city councils show a trend towards the decrease of the surplus which is not transferred to the rest of the local subsector. The closure data shared with the AIReF from the 16 city councils with more than 250.000 inhabitants show that in 2016 there has been an average decrease in the aggregate surplus of around 1.5%, while the subsector has increased this funding capacity in almost a 40%, meaning that the rest of smaller Local Entities' surplus has grown more than a 60%.

TABLE 4. DISTRIBUTION OF THE LOCAL SURPLUS VARIATION IN 2016

City councils exceeding 250.000 inhabitants						
Funding capacity (+) / necessity (-) (in millions of €)						
City Council	Amounts (in millions of €)			% of non-financial revenues		
	2105	2016	Variation between years	2015	2016	Variation 2016 - 2015
Alicante/Alacant	25	53	108.9%	9.3%	19.6%	10.3%
Barcelona	168	113	-32.7%	6.1%	4.0%	-2.1%
Bilbao	27	11	-59.3%	5.3%	2.0%	-3.2%
C�doba	42	73	76.2%	13.0%	23.2%	10.3%
Gij�n/Xixon	33	16	-49.5%	14.0%	7.0%	-7.0%
Hospitalet de Llobregat (L')	9	37	322.8%	3.9%	15.0%	11.1%
Madrid	1.379	1.115	-19.1%	27.8%	23.0%	-4.9%
M�laga	29	69	137.9%	4.5%	10.7%	6.2%
Murcia	48	-147	-406.3%	12.0%	-38.8%	-50.7%
Palma	5	48	869.8%	1.0%	11.6%	10.6%
Palmas de Gran Canaria (Las)	58	54	-7.2%	15.9%	15.5%	-0.4%
Sevilla	36	59	63.9%	4.3%	7.2%	2.9%
Valencia	131	126	-3.8%	17.1%	14.9%	-2.2%
Valladolid	19	28	44.7%	7.2%	10.3%	3.2%
Vigo	24	19	-21.4%	10.0%	8.1%	-1.9%
Zaragoza	-230	110	-147.8%	30.2%	15.2%	45.4%
Aggregate 16 biggest city councils	1.803	1.784	-1.1%	12.8%	12.8%	0.0%
Rest of the Local Corporations	3.291	5.299	61.0%	5.9%	9.3%	3.4%
Total LCs' Subsector	5.094	7.083	39.0%	7.3%	10.0%	2.7%

After the individual assessment of the 16 city councils with a population exceeding 250.000 inhabitants, as well as of the 5 provincial governments or assimilated bodies with a higher non-financial budget, the AIReF has concluded that, broadly speaking, there is no risk of non-compliance with the stability target in 2017, although the surplus could be lower than that of the previous years. Only the city council of Barcelona and the Provincial Government of Valencia may seemingly be in risk of deviation from the stability targets established in their corresponding Economic and Financial Plans (EFP). In the cases of the city councils of Las Palmas de Gran Canaria, Murcia and Valencia, given that they are in a period of approval of a EFP (for failing to comply with the expenditure rule of 2016) which will establish the targets for 2017 and 2018, compliance could not be assessed at the end of this year, although they do not present risks of non-compliance with the legal targets. On the other hand, the Bilbao city council expects reaching a deficit of 30 million Euros according to the EFP in force, thus contravening the stability regulations under which the local budgets must be approved within a balance or surplus scenario.

TABLE 5. AIREF'S ASSESSMENT OF THE SITUATION OF THE LOCAL CORPORATIONS OBJECT OF INDIVIDUAL ANALYSIS WITH REGARD TO THE FISCAL RULES

LOCAL CORPORATIONS	Stability target		Expenditure rule		LOCAL CORPORATIONS	Stability target		Expenditure rule	
	2016 closure	2017 projection	2016 closure	2017 projection		2016 closure	2017 projection	2016 closure	2017 projection
Madrid	✓	✓	✗	✗	Córdoba	✓	✓	✓	✗
Barcelona	✓	✗	✓	✗	Valladolid	✓	✓	✓	✗
Valencia	✓	EFP Pending	✗	EFP Pending	Vigo	✓	✓	✓	✓
Sevilla	✗	✓	✓	✓	Gijón	✓	✓	✓	✗
Zaragoza	✓	✓	✓	✓	L'Hospitalet de Llobregat	✓	✓	✓	✓
Málaga	✓	✓	✓	✓	Dip. Barcelona	✓	✓	✓	✓
Murcia	✗	EFP Pending	✗	EFP Pending	Dip. Valencia	✗	✗	✓	✓
Palma de Mallorca	✓	✓	✓	✗	Dip. Sevilla	✓	✓	✓	✗
Las Palmas de Gran Canaria	✓	EFP Pending	✗	EFP Pending	Cabildo Insular de Tenerife	✓	✓	✓	✗
Bilbao	✓	✓	✓	✓	Consejo Insular de Mallorca	✓	✓	✓	✗
Alicante	✓	✓	✓	✓	Compliance	✓	Non-compliance		✗

Recommendations

The AIReF prescribes different recommendations mainly aimed at guaranteeing the accomplishment of the budget stability target and improving the consistency and effectiveness in the implementation of the framework of fiscal discipline. The following, among others, are the recommendations made by the AIReF in the budget reports of each subsector:

1. Incorporate the necessities of expenditure, the adequacy of revenues and the expenditure rule to the process of distribution of the budget stability target among the different levels of government, avoiding the inconsistencies detected between the individual application of the LOEPSF to each administration and the joint assessment of the Public Administration sector. More specifically, take into account the estimate of local surplus when establishing the targets, without expecting of this surplus to compensate the deviations of other subsectors at the closure of the year.

2. Attach the necessary information to the State General Budget project in parliamentary process in order to make the budget balance consistent with the necessity of funding calculated in terms of national accounting. This information, required by the LOEPSF, is essential to be able to assess the coherence of the State budgets with the set stability target.
3. Given that the main deviation risks are detected in the Central Government, the AIReF deems necessary that:
 - a. There is a control of the implementation of the CG through a monthly monitoring carried out by the MINHAP of the instrumentation of fiscal measures adopted and of the evolution of expenditure, giving an account of this assessment to the Parliament and the AIReF.
 - b. The necessity of revising the LOEPSF is analysed in order to establish automatic measures of correction applicable to the Central Government, following the path of those existing for the Regional Governments in case of non-compliance with the obligations of Law.
4. Continue with the actions under way and adopt the necessary decisions to guarantee the financial balance of the Social Security System within the framework of the Toledo Pact Commission.
5. In the case of the Autonomous Regions, irrespective of the EFPs which have to be elaborated due to non-compliance with the 2016's target, it is important that each administration monitors its own budget implementation (article 18 of the LOEPSF). In particular, the Autonomous Regions of Aragón, Comunitat Valenciana⁴ and Navarra, which will unlikely accomplish the stability targets in 2017, should adjust their budget scenarios to compensate the risks detected. The region of Aragón, whose budget is still in the project stage, should incorporate to the initial budget the necessary information to sustain the forecasted evolution of revenues and expenses, adjusting, in each case, the budget scenarios.
6. As for the Autonomous Regions of Cantabria, Extremadura and Murcia, it is recommended that they reach an agreement with the MINHAFP on a multiyear path of deficit decrease in which they jointly set a yearly calendar of targets and elaborate the EFP that these regions have to present due to non-compliance with the deficit targets of 2016.
7. Finally, within the scope of Local Corporations, several recommendations are prescribed in order to standardize the actions of the financial guardianship entities, whose margin of operation must be coordinated in the whole territory and limited to the compliance with the legislation currently in force.

⁴ The Autonomous Regions of Aragón and Comunitat Valenciana have to present an EFP due to non-compliance with the deficit targets of 2016.