



Independent Authority  
*for* Fiscal Responsibility

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

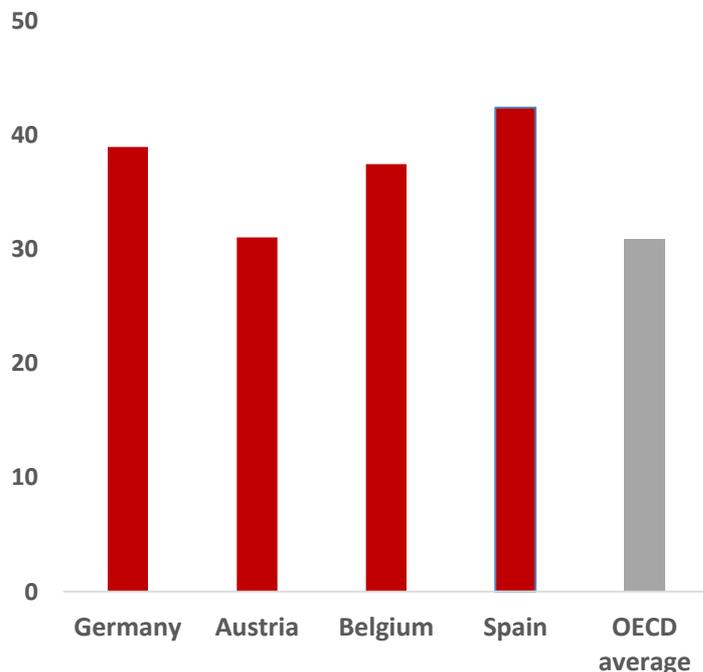
Third Meeting of the EU Network of Independent Fiscal Institutions  
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# 1. Overview of Sub-national Public Finances in Spain

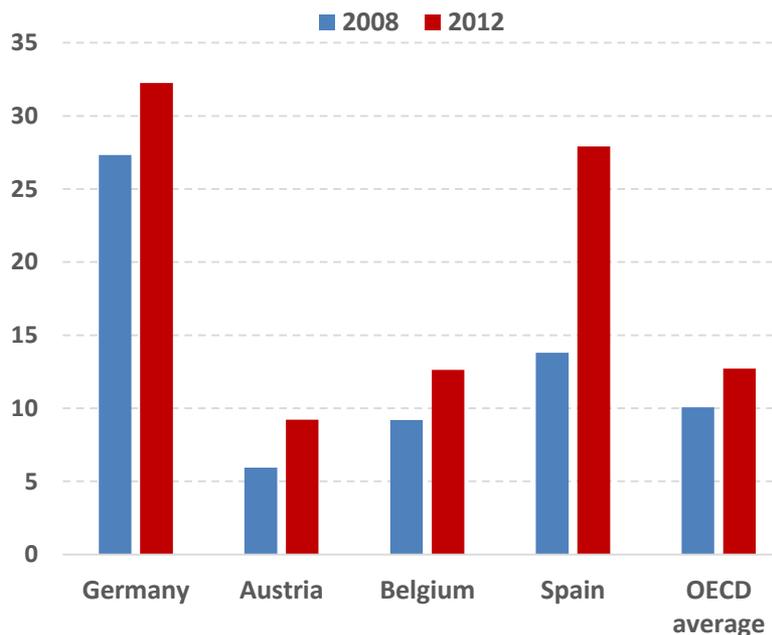
- ❖ One of the countries with the highest degree of decentralization and 2 levels of subnational governments (regions and municipalities).

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

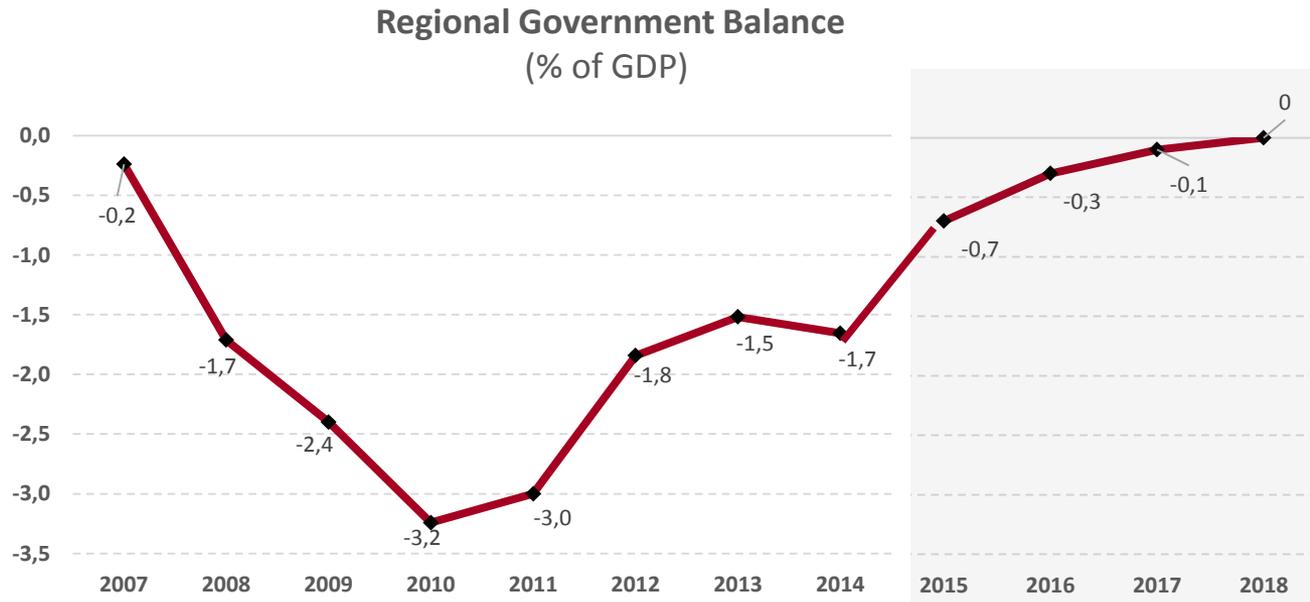


Sources: OECD Fiscal Decentralisation Database



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

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

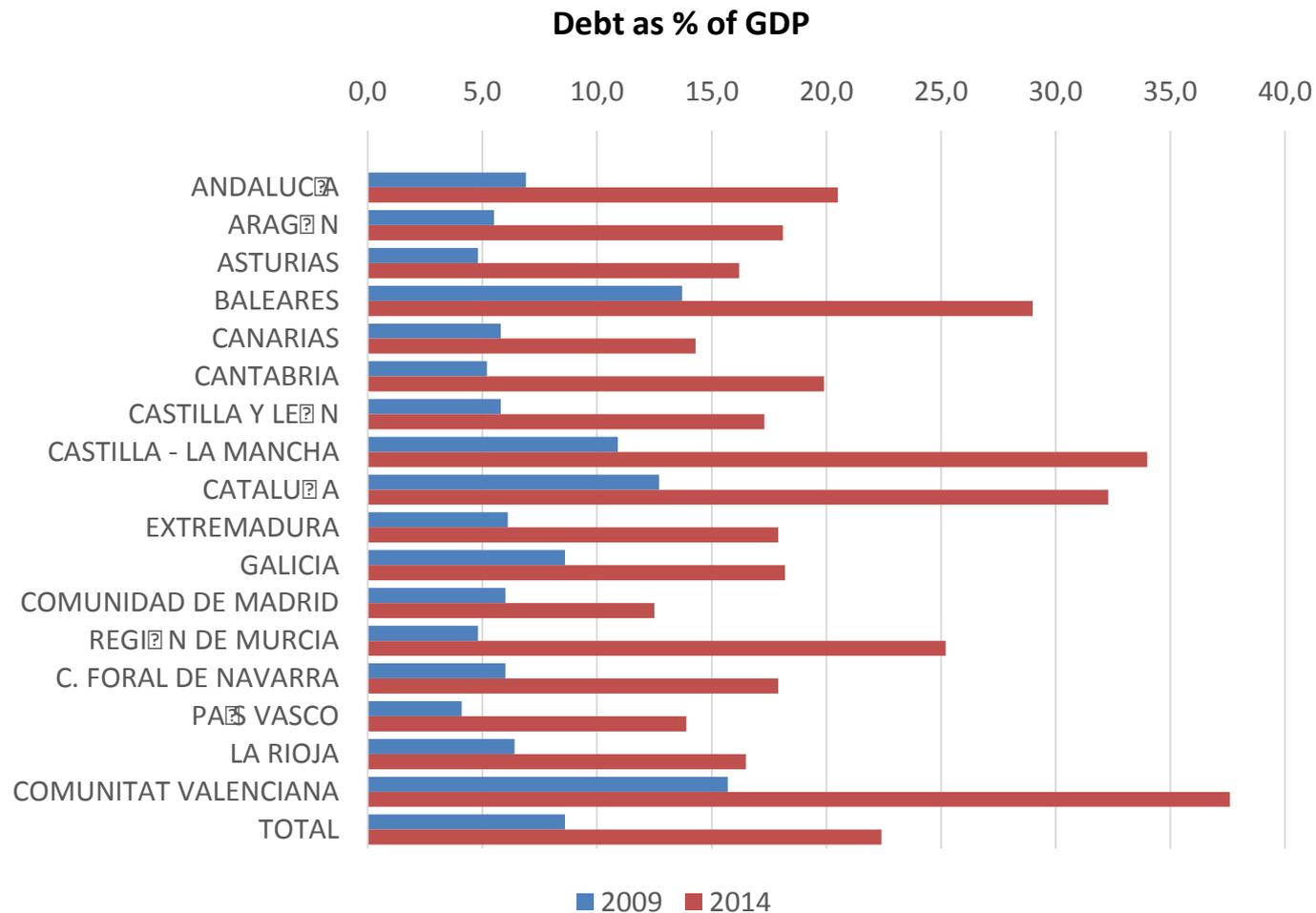


Note: adjusted with the regularisations of commercial debt operations in 2009 and 2011 and excluding for 2010 and 2011 the final settlement of the regional financing system.

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><b>1. Stronger fiscal disciplinary framework</b></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 <b>Targets</b> </div> <div style="border: 1px solid white; border-radius: 10px; padding: 5px; margin: 5px; background-color: #F08080; color: black; text-align: center;">                     Regional macroeconomic <b>Forecasts</b> </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 <b>activate all the preventive, corrective and coercive mechanisms</b> (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;"> <b>Rebalancing Plans</b> </div> </div> </div>
<p><b>2. Improving transparency</b></p>	<ul style="list-style-type: none"> <li>➤ <b>Reports and methodologies</b> are public. <a href="#"><i>AIREF - Autoridad Independiente de Responsabilidad Fiscal</i></a></li> <li>➤ <b>Many recommendations</b> directly aimed at reinforcing transparency. (making assumptions explicit)</li> <li>➤ <b>Comply or Explain</b> principle.</li> </ul>
<p><b>3. Financial support</b></p>	
<p><b>4. Voluntary agreements</b></p>	<ul style="list-style-type: none"> <li>➤ <b>Attending meetings of the two coordinating bodies.</b></li> <li>➤ <b>Studies</b> requested by:                     <ul style="list-style-type: none"> <li>○ the coordinating bodies.</li> <li>○ 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.</li> </ul> </li> <li>➤ <b>Close dialogue</b> with subnationals.</li> </ul>



# 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><b>Regions:</b> main source of risk to meet the 2015 general government target (revenues overestimated; consolidation fatigue)</p> <p><b>Municipalities:</b> 2015 target feasible but risks (uncertainty on the impact of the local reform)</p>	<p>Need to adopt measures &amp; more information</p> <p>Closer monitoring of the local reform</p>
Dec	<p>High risk of deviation of the <b>2014</b> target in 7 regions.</p> <p>High risk of deviation of the <b>2015</b> target for the whole sector. But <b>significant differences across regions:</b> risk of deviation identified in 9 ARs, being particularly high in 5 of them.</p>	<p><b>Case to activate the warning mechanisms (art.19)</b> so that regions can adopt measures before the deviation materialises.</p> <p><b>Case to activate automatic preventive measure</b> 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 1<sup>st</sup> 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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