

## **Strengthening Medium-Term Budgetary Frameworks**

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Sound public finances require comprehensive fiscal frameworks covering adequate budgetary information, good budgetary procedures and practices, a more medium term approach underpinned by numerical rules and adequate arrangements between different levels and institutions of public administration. The Directive on Requirements for Budgetary Frameworks of the Member States has been an important step forward in the efforts to promote good standards in all these areas.

There is, however, evidence that practical implementation of the Directive's general principles has been uneven across areas and lagging behind with respect to medium-term budgetary frameworks (MTBFs).

The aim of this paper is to propose steps towards contributing to reinstate a dual – procedural as well as rule-based – approach to medium-term budgeting in EU Member States. It identifies action that can be taken to reinforce the importance of national institutions as well as national public finance management procedures and practices in the functioning of the national and EU fiscal framework.

Whilst recognizing that the bulk of the improvement in practice must come from solutions at the Member State level, and that national IFIs also have a relevant role in promoting a medium-term approach to fiscal policy, it calls for a comprehensive review by the European Commission to provide impetus for national-level dialogue and initiatives concerning MTBFs. On the basis of this review, the Network sees the scope for an increased role for the evaluation of the soundness of MTBFs by the Commission as a part of the EU Semester.

### **1. Importance of medium-term budgetary frameworks**

Effective MTBFs can be useful in supporting a predictable, accountable, transparent and efficient conduct of fiscal policy at the national level. In this sense, the requirement that Member States establish a credible and effective MTBF, as set out in the Council Directive 85/2011 on requirements for budgetary frameworks of the Member States, is a welcome step forward. The Directive specifies that plans for budgetary scenarios should involve at least a three-year time horizon. The budgetary plans must also be consistent with each country's fiscal rules, based on projections for the main revenue and expenditure items detailed for every subsector (under the assumption of no policy changes), involve the identification of policies which would ensure the compliance with the medium-term fiscal

objectives, and accompanied by an assessment of the impact on long-term sustainability of public finances.

Some of these provisions were better defined and reinforced by Regulation (EU) 473/2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area. In this Regulation, a common budgetary timeline was identified for Member States in the euro area. By the end of April, Member States must make public their national medium-term fiscal plans that should be consistent with the recommendations issued in the context of the Stability and Growth Pact. By mid- October, Member States must make public the draft budget for the forthcoming year whose final version should then be adopted by the end of the year. Moreover, Member States must establish independent bodies for monitoring compliance with numerical fiscal rules.

However, some provisions of the Stability and Growth Pact have sidelined important public finance management initiatives aiming to put an effective MTBF in place. Article 4 from the mentioned Regulation, for example, allows for the Government's stability program and medium-term fiscal plan to be the same document. Many governments as well as the EU institutions have subsequently been focussing their attention on aggregate numerical targets rather than multi-horizon planning supported by well-defined measures and clear sectoral policies with significant budgetary impact.

## **2. Definitions and good practices**

Medium Term Budgetary Framework (MTBF) is a framework for integrating fiscal policy and budgeting over the medium-term by linking a system of aggregate fiscal forecasting to a disciplined budgetary process. Its aim is to ensure better control over the evolution of the aggregate fiscal position through a set of institutional arrangements for prioritizing, presenting, and managing revenue and expenditure in a multiyear perspective.

The Network has agreed that well-designed MTBFs share many of the following features:

- They are supported by strong political commitment across the political spectrum and national legislatures play an active role in their implementation and monitoring.
- They have a planning horizon that spans the life of a government or of a trajectory towards a planned fiscal target.
- They are characterized by a wide coverage of the public sector in many different dimensions, including levels of public administration, sectors of the general government as well as categories of revenues and spending.

- They ensure consistency between numerical fiscal rules and annual budget documents. To this aim, they use accounting practices that allow evaluation of numerical fiscal rules on the basis of budget documents. A link to goals defined in terms of measures of long-term sustainability seems particularly useful.
- They are supported by identifiable and quantifiable measures at the time of formulation of the MTBF or any refinements to an existing one.
- They strike an appropriate balance between being binding and flexible enough to accommodate well justified and publicly explained amendments. Any carry-over arrangements across years are clearly specified and limited in terms of nature and volume.
- Their fulfilment is independently evaluated by an institution with the mandate, resources and skills to do so at least ex post.

### **3. Proposals for action at the EU level**

There is a clear scope and rationale for action at the EU level to reinforce MTBFs, whilst recognizing that specification of the relevant procedures as well as their implementation must happen at the national level. Action at the EU level could generate the key impetus for dialogues at the national level. This would be in line with current EU legislation and consistent with the idea of ownership of MTBFs and budgetary accountability at the national level.

The Network, therefore, calls on the Commission to accelerate the work on a common scheme for MTBFs assessment and conduct a comprehensive review of the implementation of MTBFs at the Member State level.

On the basis of this review, the Network also sees a scope for raising the profile of the procedural aspects of MTBFs by including regularly this subject in the European Semester evaluations. It is indeed in the interest of the credibility of the EU fiscal framework to pay due attention to the existence, the nature and the effectiveness of the budgetary processes that underlie the pursuit of numerical fiscal targets.

The Network recognizes that national IFIs could have a key role to play in the promotion of MTBFs in their respective countries. For instance, in many cases national IFIs can help identifying weaknesses of national MTBFs and/or providing some of the key elements of sound MTBFs. With full respect to the national IFIs' country-specific mandates, the Network could help to foster the development of MTBFs in EU countries by contributing with analytical work and policy insights on a number of issues, possibly in a joint effort with EU institutions. The Network stands ready to consider concrete requests by the Commission.