

# **Fiscal Discipline: From Theory to Practice [Discussion]**

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**Independent Fiscal Institutions in the EU Fiscal Framework  
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# Outline

- **Fiscal profligacy**
- **Practice: fiscal policy rules**
- **Practice: independent fiscal institutions**
- **Practice: three cases**
- **Proposal for reform of EU fiscal framework**

# Fiscal profligacy

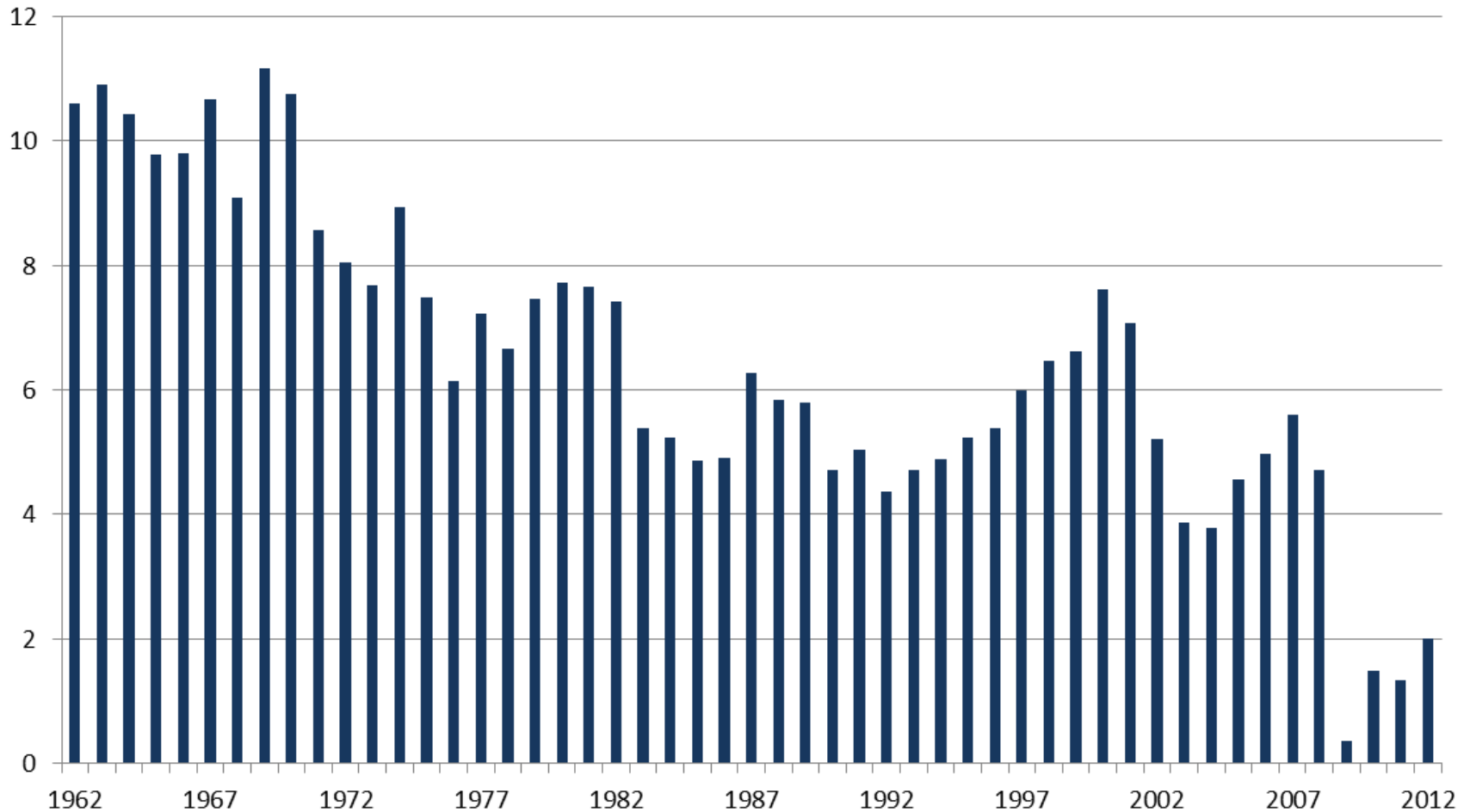
## *Additional symptoms*

- **Opacity: policy, accounts, forecast bias**
- **Expansionary procyclical bias**
- **Expenditure composition bias**
- **Erosion of (discretionary) fiscal space**

# Fiscal profligacy

## *Erosion of fiscal space*

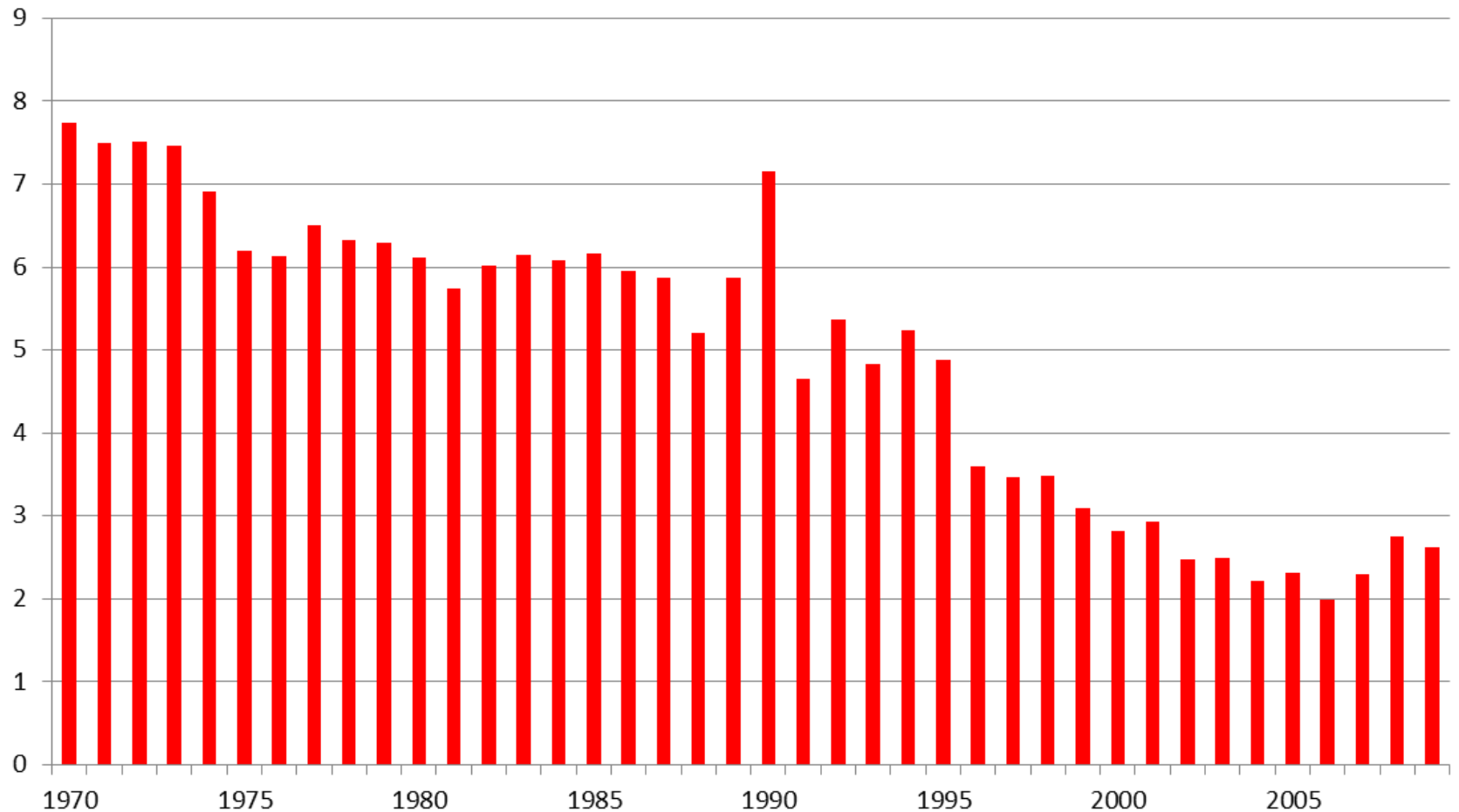
**United States: Cyclically-Adjusted Fiscal Space, 1962-2014**  
(in percent of potential GDP)



# Fiscal profligacy

## *Erosion of fiscal space*

**Germany: Cyclically-Adjusted Fiscal Space, 1970-2009**  
(in percent of potential GDP)



# Practice: fiscal rules

## *Conditions for effectiveness*

- **Design: K-S criteria of good practice**
- **Local ownership, political will  
(regardless of statutory basis)**
- **Oversight by IFI (FR and IFI are complementary)**
- **No-bailout clause, letting markets exert pressure**

# Practice: independent fiscal institutions

## *Key characteristics*

- **Very wide range in mandate, size, structure**
- **Approach: clinical, forward-looking (baseline projections)**
- **Promotion of fiscal transparency**
- **Assessment of fiscal sustainability and risks**
- **Very few have formal advisory role; none decision-making role**
- ***De facto* matters more than *de jure* independence**
- **They include monocratic structures, besides councils**

# Practice: independent fiscal institutions

## *Conditions for effectiveness*

- **OECD Principles for IFIs**
- **Local ownership, broad-based political support**
- **Non-partisan opinion (not bi-partisan)**
- **Technical expertise (no “black box”)**
- **Anticipation of need for adjustment**
- **Consistent communication, outreach**



# Practice: three cases

## *Euro Area*

- **Contribution to debt crisis (not a design problem)**
  - demonstration effect of 2003 violations (France, Germany)
  - procyclical expansionary stance
  - no-bailout clause was not credible

**Note: original design met most K-S criteria (Buti and Giudice, 2002)**

- **No-bailout clause: mixed implementation ?**
- **Present deficiencies of EU framework**
  - most complex worldwide
  - unenforceable (both Commission and Council are political)
  - reduced transparency
- **EU framework is not legitimate, democratic ?**

# Practice: three cases

## *United States*

- **Federal: only 1990 pay-go rule, effective through 2000**
- **States (fiscally sovereign): golden rule, plus rainy-day funds**

## *New Zealand*

- **Highest degree of budgetary transparency (OBS)**
- **No fiscal rule ?**
- **NZ Treasury is an IFI ?**

# Proposal for reform

## *Market-based approach* (Kopits, 2018)

- **Member states choose their own national fiscal rules, well-designed per K-S criteria**
- **IFIs: oversight of compliance with national rules, in line with OECD Principles**
- **Commission/EFB: technical surveillance and guidance**
- **Council/ECB: effective enforcement of no-bailout clause**
- **Need to deal with legacy public debt**

# References

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