



IMF POLICY PAPER

BUDGET INSTITUTIONS IN G-20 COUNTRIES—COUNTRY EVALUATIONS

April 7, 2014

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BUDGET INSTITUTIONS IN G-20 COUNTRIES—COUNTRY EVALUATIONS

April 7, 2014

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ARGENTINA

Summary Evaluation

The central government publishes comprehensive financial statements, which include the social security funds and balance sheets with all financial assets and liabilities. Audited financial statements are published more than nine months after the end of the fiscal year. The 2004 Fiscal Responsibility Law (LRF), introduced a number of key reforms in public financial management which apply to the central and most of the first layer of sub-national governments. The reforms include establishment of a macro-fiscal framework, fiscal rules, a medium-term budget framework (MTBF), a system of quarterly budget execution reports, and the Federal Council on Fiscal Responsibility (FCFR) which is tasked to enforce the provisions of the LRF. However, there are problems with the LRF and its implementation: (i) the out-years of the MTBF are indicative only; (ii) several LRF provisions have been suspended or relaxed since 2009; (iii) some provinces are not complying with their obligations under the law; and (iv) membership in the FCFR is not mandatory and adherence to the LRF is voluntary. The FCFR comprises of representatives of the central government, the city of Buenos Aires,¹ and 21 of the 23 provincial governments. Nonetheless, the law has significantly increased the capacity to coordinate fiscal policies across levels of government and individual jurisdictions. Differences between macroeconomic and fiscal forecasts and outturns are not analyzed. Limited information is presented on fiscal risks. Budget execution control and reporting have been strengthened through a series of upgrades to the Integrated Financial Management Information System (SIDIF), which began operations in 1993.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Macroeconomic and Fiscal Forecasting	Three-year macroeconomic and fiscal forecasts are required by the LRF.

Fiscal Reporting: Financial statements cover the central government, including social insurance funds. The central government balance sheet includes all financial assets and liabilities. The quarterly Physical and Financial Monitoring Report sets out detailed data on central government budget execution. The Office of the Auditor-General, which reports to the National Congress, audits the financial statements; the audited financial statements are published more than nine months after the end of the fiscal year. Accrual-based government finance statistics, generally aligned with GFSM 2001, are produced by the Ministry of Economy and Finance (MECON) covering the general

¹ Hereafter, reference to provinces includes the city of Buenos Aires.

government. Budget outturn reports present analyses of deviations from physical and financial programming and execution.

Macroeconomic and Fiscal Forecasting: A three-year macroeconomic and fiscal framework covering the public sector is published as part of the budget documentation. It includes forecasts for GDP, inflation, and key fiscal aggregates for the general government. Other important macroeconomic indicators, such as the unemployment rate and oil prices, are not included, however. A mid-year budget review is not prepared. However, in September, at the same time the draft of the new budget is submitted to the National Congress, an updated version of the current budget is presented on the basis of the latest macroeconomic projections. There is no systematic comparison of macroeconomic and fiscal forecasts and actual results published by the authorities. There are no long-term fiscal forecasts of twenty years or more. The LRF is not compulsory for provincial governments. However, if governments agree to adhere to the LRF,² compliance to its provisions is mandatory. The LRF requires a number of macroeconomic and fiscal forecasts to be prepared and presented to the FCFR.

Fiscal Risk: A systematic statement of fiscal risks is not prepared. However, new guarantees are presented in the annual budget and must be approved by the National Congress. No information is provided, however, on the stock of guarantees or other contingent liabilities. Macroeconomic or fiscal projections based on alternative scenarios are not provided. There is no significant analysis of risks to public assets.

Independent Fiscal Agency: Argentina does not have an independent fiscal council. However, the FCFR, created following the passage of the LRF in 2004, oversees the implementation of the LRF. The LRF requires disclosure by federal and provincial governments of certain fiscal data, including total revenue, expenditure, and debt for the purpose of promoting accountability and coordinating fiscal policies.³ The FCFR is responsible for assuring the quality of these data and various fiscal reports, including the macroeconomic and fiscal framework.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area	
Type of Institution	Reform since 2010
Intergovernmental Financial Relations	The FCFR provides the opportunity for an unusually high degree of intergovernmental fiscal coordination.

² In addition to the central government, the city of Buenos Aires, and 21 of the 23 provincial governments have formally agreed to adhere to the requirements of the LRF.

³ Individuals taking part in FCFR meetings are the equivalent of the Minister of Economy or the Treasurer of each of its member governments. The FCFR Executive Committee is made up of one representative from the central government and representatives of eight provinces.

Fiscal Objectives and Rules: The LRF is a comprehensive fiscal legal framework, and includes a number of guidelines on spending, debt, and reporting. The law's fiscal objectives and rules are: (i) a spending growth rule, applicable to central and provincial governments, that prohibits the rate of increase in primary spending from exceeding the forecasted rate of increase in GDP (Article 10); (ii) prohibition on the use of debt and proceeds from the sale of fixed assets for recurrent expenditure (Article 12); (iii) a requirement that the budget is balanced both ex ante and ex post⁴ (Article 19); (vi) establishment of funds as instruments of counter-cyclical fiscal policy (Article 20); and (v) a limit on provincial debt service that cannot exceed 15 percent of the net current revenue-sharing with federal government (Article 21). There are no escape clauses in the LRF. Since 2009, as a result of the global economic crisis, Articles 12 and 21 were suspended and Articles 10 and 19 were relaxed. The FCFR annually evaluates compliance with LRF requirements, though since 2010 it has not published its conclusions with regard to provinces.

Medium-term Budget Framework: The LRF requires preparation of a general government MTBF covering the budget year plus two forward years. The two forward-year expenditure and revenue estimates are indicative, intended to guide development of the next annual budget. However, differences between the proposed annual budget and indicative estimates in the prior year MTBF are not explained or reconciled, and the financial impact of new policies is not distinguished. The executive presents the MTBF to the National Congress together with the budget for approval.

Performance Orientation of the Budget: The budget is presented using institutional, program, functional, source of financing, and economic classifications, among others. Budget analysis focuses on programs to ensure adequate resources are supplied to carry out planned outputs. Appropriations are made by program within the main institutional classification. The National Budget Office (ONP) prepares quarterly Physical and Financial Monitoring Reports of the National Administration, as required by the Financial Administration Law (LAF) of 1992, revised in 2006. The reports cover implementation of budget policies and programs, including (i) analysis of key policies, plans and guidelines for the year; (ii) analysis of outputs and performance; and (iii) supplementary data on historical trends and indicators. The reports are not published in a timely manner, which undermines their usefulness. Monitoring is conducted by grouping activities that deliver similar types of public services, irrespective of the institutional linkage or jurisdiction of the agency responsible for execution. This grouping, however, does not necessarily coincide with the program classification.

Intergovernmental Financial Relations: Many of the fiscal rules and requirements in the LRF apply to the provincial governments as well as the central government. Through the FCFR, the central government has access to extensive fiscal information on the provinces, and may use the facilities of the FCFR to coordinate fiscal policy across jurisdictions. The draft central government budget

⁴ Some expenditures, such as debt service and certain capital expenditures, are excluded from the calculation of the balanced budget rule.

includes (i) an analysis of fiscal coordination with the provinces; (ii) medium-term projections covering central and provincial governments; and (iii) presentations of detailed information by individual province. Budget classifications of provinces were standardized in 1994 and efforts continue through the Permanent Forum of Budget and Finance Directorates of the Argentine Republic to apply, update, and harmonize classifications nationally. The FCFR has authority to enforce LRF fiscal requirements, and suggest corrective actions, in the event of non-compliance by any FCFR member. However, since 2010, the FCFR has not done so despite the fact that some provinces have not submitted to the FCFR, as required under the LRF, information on their annual budget plan and execution, medium-term forecasts, and tax expenditures.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Budget Execution Controls	The Integrated Financial Management Information System (SIDIF), which began operations in 1993 and has been upgraded continuously since then, provides capabilities for modern treasury management and expenditure control for central government.

Budget Unity: The central government budget is largely comprehensive though some earmarks, SOEs, public universities, autonomous public entities, state financial sector, and mandatory expenditures authorized in permanent law remain outside of the budget. Tax expenditures are quantified and reported annually by the MECON, although there is no control on their size.

Top-down Budget Preparation: Procedures stipulate that the budget will be prepared in a two-step process. Medium-term ceilings on budget aggregates and ministry expenditures will be proposed by the ONP and approved by the Head of the Cabinet, and the agencies will then prepare their preliminary draft budgets on that basis. Revenue earmarking and standing appropriations are only permitted in some specific cases and represent less than 10 percent of the central government expenditure.

Parliamentary Approval: The executive must submit the annual budget to the National Congress for its approval before September 15. It does not first approve the budget aggregates before voting on detailed spending. Medium-term projections and aggregates are included in the medium-term budget framework presented together with the budget proposal but published after the annual budget has been approved to allow some reconciliation. The National Congress typically defers to the budget priorities established by the executive on the basis of its Governance Plan, and approves the budget largely unchanged.

Budget Execution Controls: The executive has considerable flexibility when executing the budget.⁵ It has authority to change allocations within the total approved central government budget; it also may increase total expenditures through an Emergency Decree, which have represented 10-15 percent of the total executed budget in the last three years. However, any changes made during budget execution to increase or decrease total amounts for unallocated funds (gastos reservados), intelligence services, and debt service require National Congress approval. The executive cannot change the purpose of appropriations. There is no formal contingency funding mechanism aside from the Emergency Decrees. Public entities may enter into multi-year spending commitments if requested as such in the budget process and approved by the National Congress, but there are no qualitative or overall quantitative limits on this practice. Carry-over appropriations are generally not permitted. The executive may defer or cut appropriations without limit. The Integrated Financial Management Information System (SIDIF) began operations in 1993. It has been improved in phases, and now provides capabilities for modern treasury management, including features to record and control commitments, process payments, account for cash and accrual transactions, and prepare financial statements. The SIDIF is used by all central government budget entities, and is being extended to the province of Buenos Aires on a pilot basis. It enables 98 percent of all central government budget expenditures to be processed through the treasury single account.

Recommendations

The following institutional reforms could be pursued to strengthen the Argentinean budgetary institutions:

- Strengthen macroeconomic and fiscal forecasts by publishing a systematic ex-post comparison of forecasts with actual outturns. The secretariat of the FCFR could be tasked with this.
- Re-establish LRF fiscal rules, with appropriate focus on both fiscal sustainability and cyclical concerns, and add escape clauses that take into consideration exceptional economic circumstances.
- Enhance the effectiveness of the MTBF by submitting it to the National Congress for discussions and approval before submission of the annual budget to set the stage for detailed preparation of the annual budget.
- Prepare a comprehensive fiscal risk assessment report and publish it as part of the budget documents. Publish long-term fiscal forecasts to highlight risks that may be developing through trends in revenue, expenditure, stock of debt, and debt service.
- Extend the coverage of the financial statements to include the general government and introduce recording of non-financial assets and contingent liabilities.

⁵ The following practices were applied on an exceptional basis beginning in 2001. The 2006 amendment to the LAF made the practices permanent.

AUSTRALIA

Summary Evaluation

Australia has strong and modern budget institutions. The Charter of Budget Honesty Act 1998 (the Charter) mandates a number of principles of sound fiscal management and requires the Government to release: a fiscal strategy; regular fiscal reports including the budget economic and fiscal outlook, mid-year economic and fiscal outlook and final budget outcome; and an intergenerational report every 5 years. Australia's fiscal reporting is comprehensive and fully accrual-based. Macro-fiscal forecasting is updated twice a year and forecast errors are analyzed and reported on. Budget documents contain a broad, quantified analysis of fiscal risks, including of macroeconomic sensitivities, the government balance sheet, and all contingent assets and liabilities above a certain threshold value. The Fiscal Strategy Statement and forward estimates process provide a credible framework for medium-term fiscal and budgetary planning. Nonetheless, while fiscal objectives are presented for the medium-term and the former government had in place a number of fiscal rules, they lack specificity and are not legally binding. Baseline expenditures are clearly distinguished from new policy initiatives. Budget decisions are, however sometimes taken outside the context of the normal budget process, impeding effective expenditure prioritization. The recent introduction of an independent Parliamentary Budget Office (PBO) will provide further assurance over the prudence of fiscal policy. Performance information on government programs is provided in the budget documents jointly with financial information. Expenditure and strategic reviews are regular elements of the performance management framework. The coordination of fiscal policy between the federal government and the states and territory governments is limited and does not include a binding fiscal rule framework for general government. Annual parliamentary approval processes contain incentives to over-use standing appropriations which now cover some 75 percent of expenditures.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Macro and Fiscal Forecasting	The government published an independent review of macroeconomic and revenue forecasting in 2012.
Independent Fiscal Agency	The PBO was established in 2012.

Fiscal Reporting: Australia produces comprehensive Consolidated Financial Statements for central (Commonwealth) government on an accrual and cash basis which include a full balance sheet. These are audited and certified within six months of the end of the financial year. The budget documents also provide historical central government, general government and non-financial public sector financial data. Fiscal statistics are produced by the independent Australian Bureau of Statistics and

cover stocks and flows of the central government, general government and public sector, as well as each of the constituent sectors. All statistics are aligned with international standards such as GFS2001 and the UN's SNA.

Macroeconomic and Fiscal Forecasting: The official macroeconomic and fiscal forecasts are produced by the Treasury with a four-year forecast horizon twice a year (alongside the budget and for a mid-year update). The budget and mid-year update documentation provide detailed discussions of the underlying economic forecasts, including specifics on underlying assumptions. The forward estimates for revenue and expenditure are also presented in detail, separating between the baseline costs of existing policies and the costs of new policies over the four-year period. The budget and mid-year update also include comparisons of previous forecasts, and on the revenue side a detailed discussion of forecasts errors over recent years. In 2012, the government published a review of macroeconomic and revenue forecasting prepared by an external advisory panel, which assessed the forecasting processes and performance over the period since the last review was undertaken in 2005. The Treasury produces an intergenerational report, which analyses the sustainability of public sector finances, with long-term projections of all key revenue and expenditure areas extending out over 40 years, under the government's current policies. It also provides a reconciliation of change to the forecasts from the previous report.

Fiscal Risk: The budget and mid-year update include a comprehensive fiscal risk statement which reports and quantifies, where possible, all contingent assets and liabilities with a potential fiscal impact of AUS\$20 million or more, including government guarantees, PPP risk-sharing arrangements, contractual disputes, and tax litigations. Explicit parliamentary authorization is sought for major guarantees (such as the recent extension of deposit insurance), and accrual-based forward expenditure estimates presented to parliament include provisions for expected future write-downs, impairments, or losses. There is, however, no annual ceiling for contingent liabilities, nor is it part of the medium-term expenditure framework. Both the budget and mid-year update include an analysis of the sensitivity of revenue and expenditure to alternative economic assumptions. The budget also includes an Asset and Liability Management Statement which discusses the risks around both sides of the government balance sheet. From the 2013-14 Mid-year Economic and Fiscal Outlook, the budget update also contains a Debt Statement which reports in more detail on Commonwealth Securities and the balance sheet.

Independent Fiscal Agency: The PBO was set up in 2012 to provide Parliament with an independent and non-partisan analysis of the budget cycle, fiscal policy, and the financial implications of policy proposals. The PBO has a number of functions, including responding to requests from parliamentarians and parliamentary committees for policy costings and for information related to the budget, as well as conducting research and analysis on the budget and fiscal policy issues. During the caretaker period of the general election, the PBO prepares costing of political parties' pre-election commitments at their request. It can also provide analysis of fiscal sustainability and reviews of macroeconomic and revenue forecasting processes and accuracy. The PBO has released several reports, including one on the structural budget balance, a report on expenditure trends and a post-election report of election commitments.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area	
Type of Institution	Reform since 2010
Fiscal Objectives and Rules	More detailed numerical guidance on the implementation of the Medium-Term Fiscal Strategy was introduced at the time of the fiscal stimulus in 2009.

Fiscal Objectives and Rules: Australia has had a stable medium-term fiscal objective framework for the whole of the Commonwealth (central) Government since 1997-98. The Charter's Principles of Sound Fiscal Management requires the government to specify its long-term fiscal objectives and fiscal targets for the budget year and the following three financial years in an annual Fiscal Strategy Statement. The former government had in place a medium-term fiscal strategy which required it to "achieve budget surpluses, on average, over the economic cycle; keeping taxation as a share of GDP on average below the level for 2007-08 (23.7 per cent of GDP); and improving the government's net financial worth over the medium-term." A variant of this strategy has been in place for a decade. This strategic objective provides considerable leeway on the specific fiscal targets over the medium-term. For example, there is ambiguity around the time frame and methodology for the dating of the business cycle and around the pace and scale of improvement in net financial worth being sought. Between 2009 and 2013, the medium-term fiscal strategy was supplemented by an additional policy commitment to hold real growth in spending to 2 percent a year on average while the economy is growing at or above trend, until the budget surplus is at least 1 percent of GDP. These fiscal strategies are no longer in place as there was a change of government following the September 2013 general election. The current government has committed to detail the fiscal strategy it intends to pursue by the 2014-15 Budget, as required by the Charter. Performance against the central government's fiscal objectives is reported three times a year in the budget in May, by September in Final Budget Outcome and in the mid-year update by January of the following year.

Medium-term Budget Framework: The Government continues to operate fiscal policy within a clearly defined medium-term budget framework. The budget includes four-year forecasts for revenues and expenditures, and the Government publishes detailed information and costings on the impact of its policy decisions over these horizons. The budget also includes ten-year projections of budget aggregates such as net debt and the underlying cash balance. Since 1997-98, Australia's annual budget has been situated within a credible medium-term budget framework based upon a set of rolling, four-year "forward estimates" for each of the Commonwealth (central) Government's programs. These forward estimates act as binding multi-year restrictions on both aggregate and sectoral expenditure. Forward estimates are more binding than mere forecasts and represent a provisional decision on the future expenditure level for each program which, in the absence of any new policy decision or adjustment in the agreed volume/price index, becomes the budget for that program.

Performance Orientation of the Budget: Australia's Commonwealth budget includes an integrated functional and programmatic classification. Since 1999/2000, the budget has been appropriated on the basis of broad outcomes. However, the fact that these outcomes sometimes cut across one or more programs creates some ambiguity about accountability for program performance. Each line ministry is required to specify the outputs needed to deliver on each program and outcome, and report progress against them in the annual Portfolio Budget Statements that accompany the budget. Spending reviews have been a requirement for all programs designated as lapsing by the Cabinet. The government uses strategic reviews to assess the performance of groups of programs that contribute to a single policy area. The independent Auditor General also undertakes performance assessments of agencies and/or spending programs, and reports these directly to the Parliament.

Intergovernmental Financial Relations: The central government's budget contains fiscal forecasts covering all of general government. There is, however, no fiscal objective framework which guides the fiscal policy of the general government, nor is there a centrally-imposed fiscal rule for Australia's states and territories, although some sub-national entities have adopted their own fiscal rules. Commonwealth and state/territorial governments do jointly consider Commonwealth and sub-national borrowing through a forum known as the Australian Loan Council, though over recent years this is more an information exchange, rather than a policy-making body.

C. Implementing the Adjustment Strategy

Budget Unity: While the budget encompasses all central government expenditure and revenue collections, only around 25 percent of the expenditures are approved through annual appropriations, with the remaining 75 percent of expenditures legislated through 'special' or standing appropriations. Comprehensive, quantified estimates of tax expenditures are provided both in the budget document and in an annual Tax Expenditures Statement, but there is no explicit control on the creation or stock of tax expenditures.

Top-down Budget Preparation: While budget preparation does not follow a formal top down process, the interaction of the fiscal targets and internal budget procedures brings some elements of this into budget preparation. The internal budget process often sees the Expenditure Review Committee of the Cabinet giving top-down guidance on overall spending/saving decisions that need to be identified within the budget.

Parliamentary Approval: While budget discussions follow a top-down procedure, more than three-quarters of the Commonwealth budget is subject to a standing appropriation, and recent years have seen some major fiscal decisions taken outside the budget cycle. Forward estimates act as de facto ceilings on budget discussions at both the aggregate and sectoral level. Changes to those estimates are subject to rigorously enforced rules set down by the Expenditure Review Committee of the Cabinet. There are some restrictions on the right of Parliament to amend the government's draft budget. The Constitution says that the Senate cannot amend laws appropriating money for the ordinary annual services of government. In practice (and codified through a Compact between the

two houses of Parliament) this means that the legislature only proposes amendments to that part of appropriations identifying new initiatives. There is, however, no quantitative restriction on the impact of those amendments on the budget balance. There is a separate Parliamentary debate on the government's mid-year budget update.

Budget Execution Controls: Controls over budget execution are in line with advanced country standards but an area of relative weakness in the Australian budget framework. The Government is required to introduce a supplementary budget if expenditure exceeds budget totals for a given portfolio over the course of the year. However, there is no requirement that this supplementary budget be fiscally or expenditure neutral. Furthermore, this provision applies only to the 25 percent of expenditure covered by annual appropriations and not the 75 percent of expenditure covered by "special" appropriations for which overspending does not require a supplementary estimate. Full carryover is allowed for departmental appropriations (i.e., to fund the operation of government), while administered (essentially program) expenditure appropriations expire at year end. There is a large contingency reserve included in the budget equivalent to 1.3 percent of total expenses over the four-year horizon of the forward estimates. Ministry of Finance approval is also required before any line ministry or agency can enter into a multi-year expenditure commitment.

Recommendations

The following institutional reforms could be pursued to strengthen budget institutions:

- Refrain as much as possible from taking budget decisions outside the formal budget process. The latter can impede attainment of fiscal targets and decreases the effective prioritization between competing spending areas.
- Adopt a more clearly specified fiscal rule framework, possibly enshrined in law, in order to increase the credibility and accountability of fiscal management.
- Expand the fiscal objectives of the Commonwealth government to cover general government, and use the coordination framework of the Loan Council to decide on relative contributions to general government fiscal policy.
- Reduce the use of standing appropriations in the budget process. Expenditure appropriations should in principle be subject to annual parliamentary scrutiny in the context of the budget process.
- Powers of parliamentary amendment could be expanded to include baseline expenditures. This would help improve the quality of, and the political support for, government expenditure. Increased scope of amendment could be accompanied by limiting their fiscal impact. Parliamentary rules could require that any amendments to the draft budget are to be budget neutral.

- As recommended in the Joint Select Committee on the Parliamentary Budget Office's report the new PBO should consider publishing analysis that provides an ex-ante evaluation of the government's fiscal forecasts including the underlying assumptions and strategy. In addition the PBO could publish an annual review of the government's fiscal performance over the past year.
- Creation of contingent liabilities and tax expenditures should be subject to annual limits in the budget and be included in the medium-term expenditure framework.

BRAZIL

Summary Evaluation

The 2000 Fiscal Responsibility Law (FRL) is the cornerstone of Brazil's PFM reforms. Over the past decade, this law and other initiatives have successfully contributed to fiscal discipline at the federal and sub-national government levels. Fiscal reporting is comprehensive, covering all levels of government. An extensive fiscal risk statement is presented to Congress annually, though some gaps in the analysis remain. There is an extensive performance monitoring and evaluation system, and strong control is exercised over budget execution. Since 2010, reform efforts have concentrated on fine-tuning existing initiatives and institutions, including by enhancing transparency, restructuring the four-year plan, and improving monitoring of program performance and budget execution. Notwithstanding these achievements, some challenges remain. These include reducing the extensive rigidities in the budget caused by a large share of mandatory spending and revenue earmarking; developing a more medium-term strategic focus to budgeting; focusing congressional approval on fiscal policy and performance oversight, and strengthening the use of performance information in allocative decision-making.

A. Understanding the Fiscal Challenge

Table 1. Main Reforms in this Area

Type of Institution	Reform since 2010
Fiscal Reporting	Reforms focused on improving transparency and public access to fiscal information, underpinned by a new Access to Public Information Law (2011).

Fiscal Reporting: The federal government's consolidated end-of-year financial statement—the General Balance of the Union (BGU)—includes a balance sheet with all assets and liabilities. The Federal Court of Accounts (TCU) audits and certifies the annual accounts of the federal government within six months of the end of the fiscal year. Although the audit report is presented to Congress within the same timeframe, over the last decade legislative scrutiny has taken on average two and a half years. The National Treasury Secretariat (NTS) in the Ministry of Finance and the Statistics Department of the Central Bank of Brazil compile and disseminate government finance statistics in the GFSM2001 format. Financial transactions and stock positions for all subsectors of general government are reported on a monthly basis, thirty days after the end of the month. Data on nonfinancial transactions are reported on a monthly basis for the federal government, but data from the states and municipalities are available only on an annual basis. Consolidated general government numbers are only available 9 months after the end of the reporting period. The National Statistics Office in the Ministry of Planning prepares national accounts statistics. Recent government initiatives to improve transparency and public access to fiscal information include the passage of the Access to Public Information Law (2011), the establishment of budget data and fiscal

transparency websites, and conducting courses to educate the public on the budget process and fiscal performance.

Macroeconomic and Fiscal Forecasting: Macroeconomic projections for four years ahead are included in the multi-year national plan (Plano Plurianual—PPA) prepared by the Planning Ministry. The PPA is a four-year fixed plan that is developed in the first year of each Presidential term to reflect the President’s priority programs. In mid-April of each year, an Annual Budget Guidelines Law (Lei de Diretrizes Orçamentária—LDO) is presented to Congress for approval, which includes updated medium-term macroeconomic and fiscal projections for the current year and two years ahead along with the government’s major economic assumptions. These projections are prepared jointly by the Ministry of Planning and the Ministry of Finance. There is no published ex-ante comparison of the government’s macroeconomic and fiscal forecasts with those of other institutions. Although the annual presidential budget message describes both existing and new initiatives, annual budget documents do not identify the budgetary impact of new policies. Long-term fiscal projections are regularly prepared for social security variables.

Fiscal Risk Statement: The FRL requires that the LDO include an estimate of fiscal risks and contingent liabilities. These estimates are contained in a comprehensive fiscal risk statement, which includes sensitivity analyses and discloses risks to revenue, expenditures, and public debt levels associated with changes in macroeconomic assumptions. The statement also incorporates various contingent liabilities, including fiscal risks from state-owned enterprises (SOEs), various legal risks, and debt and non-debt guarantees, although contingent liabilities from state-owned banks are not incorporated in the analysis. Congress analyzes and approves the LDO, which includes the fiscal risk statement in an annex.

Independent Fiscal Agency: There is no independent fiscal council in Brazil. The TCU, however, in its annual audit report on the Accounts of the President of the Republic (CPR), reviews and provides an ex-post assessment of the government’s fiscal performance, including compliance with budget and fiscal targets. Two technical budget offices in Congress, one for each chamber, provide technical advice and analysis to committees and individual members of Congress. These offices are not independent entities. The CGU (Controladoria-Geral da União) linked to the Executive branch, is tasked with internal control activities (Corregedoria) and public audits, among other responsibilities.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area	
Type of Institution	Reform since 2010
Performance Orientation	The government has reduced the number programs in the PPA from 300 to 65. It has shifted the focus from outcome targets to output- and activity-based targets. There have been efforts to improve the monitoring and reporting of output indicators included in budget documents. In addition, the executive in 2013 reduced the number of budget line items by 30 percent.

Fiscal Objectives and Rules: The FRL, enacted in 2000, establishes a framework for fiscal planning, monitoring, and transparency at all levels of government. It establishes maximum limits on the levels of total outstanding debt and personnel expenditure (including pensions) as a proportion of net current revenues for each level of government. The law mandates that the President propose to the Senate debt limits for federal, state, and municipal governments. Although the Senate has established a debt limit for the states and for municipalities (200 and 120 percent of annual net current revenue, respectively), it has not done so as yet for the federal government. The FRL also requires that the LDO includes targets for revenue, spending, debt, and for the overall and primary balance (historically, a primary surplus target) for the public sector as a whole for the budget year and following two years. The law provides flexibility for anti-cyclical policy, with the possibility of adjustment of the primary surplus target ex-ante, which works as an escape clause in case of a major slowdown of the economy. The FRL contains extensive provisions for fiscal transparency and monitoring. Penalties for breaches of rules are included in the penal code. Until the recent economic crisis, Brazil achieved or exceeded its fiscal surplus target every year since the creation of the FRL, which has contributed to reducing net public sector debt and payroll expenditure. Despite the success of the FRL, a number of weaknesses have become apparent. Congress has used a provision in the Federal Constitution (Art. 166, § 3º, III. a) allowing for the correction of “errors and omissions” to revise upwards the executive’s revenue forecasts, thereby funding additional expenditure. For a number of years, Presidential decrees withholding spending approved by Congress have played a key role in ensuring that the primary fiscal targets have nevertheless been achieved during budget execution. The current fiscal target methodology does not include on-lending transactions (cumulatively 8 percent of GDP in recent years) and government guarantees. Tax expenditures are included in the fiscal target because they affect revenues.

Medium-Term Budget Framework: Brazil currently does not have a rolling medium-term budget framework. There is a four-year fixed strategic plan, the PPA, and the LDO includes fiscal aggregates for expenditure and revenues for the current year and two forward years, but the estimates are not detailed by ministry or program. The PPA, and the budget overlap in many respects, including that both have the same program structure and both specify financial resources for each program and

action. The budget itself, however, provides limited insight on the objectives of expenditures, or the amount to be spent in subsequent years. The Federal Budget Secretariat (SOF) has established as a strategic objective the development of a full-fledged medium term budget framework.

Performance Orientation of the Budget: For more than a decade, the Brazilian government has been developing performance indicators and evaluations through its planning process and the PPA. The PPA covers all federal government expenditures and includes for each of its 65 current programs high-level performance indicators, objectives and output targets. All programs in the PPA are required to be evaluated each year. Program managers report on progress against PPA targets, using an online system (SIOP). The evaluations and indicator results feed into the annual PPA progress report, which is sent to the President and Congress. In 2011, the PPA (PPA 2012-15) was significantly revised and streamlined. The number of programs in the plan was reduced from over 300 to 65. Outcome targets have been de-emphasized in favor of more output- and activity-based targets. In addition, there have been efforts to improve monitoring and reporting on output indicators included in budget documents. The executive's 2013 annual budget proposal reduced the number of line items by 30 percent. Despite the progress made with reporting performance information, its use in allocative decision-making is reportedly still quite limited.

Intergovernmental Financial Relations: The 1988 constitution and subsequent legislation transferred important fiscal responsibilities to states and municipalities and increased federal revenue-sharing and transfers. Intergovernmental transfers represent a substantial part of federal government expenditures. Nearly all new non-earmarked federal taxes are subject to revenue-sharing. The constitution gives local legislatures responsibility for approving their own annual budget and financial statements. In the 1990s, many states and municipalities built up high levels of debt, culminating in a crisis. In 1997-98, the federal government negotiated debt restructuring agreements with 25 of the 27 states. It provided financial aid conditional on repayment programs, fiscal adjustment programs, and compliance with fiscal targets. States under these agreements were legally required to follow a fiscal adjustment program and to agree on targets with the National Treasury Secretariat, which assesses their progress annually. 180 municipalities (responsible for the most of the municipalities' debt), have also agreed to join a specific fiscal adjustment program (Medida Provisória nº 2185) to consolidate and refinance their debts. The FRL and complementary legislation institutionalized many of the provisions in these agreements and set out sub-national government debt limits, as well as extensive reporting requirements and monitoring procedures. States and municipalities that fail to provide required fiscal reports in a timely manner or breach the requirements of the law can face institutional and personal penalties, such as having voluntary financial transfers from the central government blocked or being refused access to banking credit, or prohibiting political leaders from running for election.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Budget execution controls	The SOF has developed an online system for tracking the physical and financial execution of “budget actions” contained in the LOA, and produces a new quarterly performance report on infrastructure investment programs.

Budget Unity: The federal government’s annual budget covers the majority of central government expenditure, although nearly 90 percent of the budget destination is pre-defined by law. This reflects the extensive earmarking of tax revenues and mandatory expenditures as determined by the constitution or law (e.g., entitlements), or designated as “mandatory” by the President or Congress during the budget process. The combined effect of earmarking and mandatory expenditures is that a large proportion of the budget is not subjected to annual review and there is limited flexibility in adjusting the budget. Tax expenditures are not part of the fiscal ceilings (but are regulated by the FRL). Congress is provided with a quantified list of all new tax expenditures in budget documents, and exercises control over them when analyzing the legislative proposals that submit these types of measures.

Top-down Budget Preparation: The LDO, which is submitted to Congress in mid-April, contains the next year’s fiscal target. In June, the SOF issues ceilings for spending ministries, which reflect the updated list of presidential priority programs and any new expenditure deemed by Congress to be mandatory. Later in the year when the detailed annual budget (Lei Orçamentária Annual--LOA) is discussed, Congress typically re-allocates discretionary spending between ministries and increases total expenditures. Since Congress is required to respect the LDO fiscal target, it uses the “errors and omission” provision in the Constitution to increase revenue forecasts. As discussed earlier, Presidential decrees are then subsequently used during the budget year to ensure actual compliance with LDO targets.

Parliamentary Approval: Compared to most G-20 legislatures, the Brazilian Congress is very active during the budget approval process. Congress can amend the draft LDO presented to it by the executive, and does so particularly with regard to establishing which programs are “mandatory” and thus exempt from reductions by Presidential decree. Usually, Congress makes around one thousand amendments to the LDO and some ten thousand amendments to the LOA. Most amendments are for constituency, state, or special projects. The 2014 LDO foresees, for the first time, that Congress’ amendments to the draft budget are protected in 2014 from withholding of funds by the Executive, for up to 1.2 percent of net current revenues of the Federal Government and provided that half the individual amounts finance public health. The Executive retains, however, the power to discontinue the practice in future budgets. By law, the budget should be approved before the start of the fiscal year. There have, however been delays in recent years. According to the constitution, Congress can

only increase an appropriation if it decreases another. However, as already noted, it uses the “error and omissions” provision to increase expenditures. Other constitutional restrictions are that Congress cannot amend allocations to civil service payrolls and pensions, debt servicing, and constitutional tax transfers. The President has the power to veto any LOA line item.

Budget Execution Controls: In Brazil, the budget execution process focuses on ensuring that spending stays within the fiscal target limits. The executive branch can increase or cut individual appropriations—but not mandatory or earmarked spending—by Presidential decree without prior approval by Parliament, up to a limit established by the LOA. Above this limit, supplementary appropriation laws are required. The executive branch can defer to the next year discretionary expenditures, under some specific conditions without limit.⁶ Deferrals are reported to Congress in regular budget execution reports. The budget execution process begins with a Presidential decree that limits by ministry the discretionary expenditure voted in the budget. There are bimonthly reviews of revenue and expenditure outturns, and of the progress of projects and activities, at which time budget adjustments can be made to discretionary expenditures. These adjustments are limited to specific percentages (set in the budget law) according to the type of adjustment. The government can prepare a supplementary budget in the event overspending occurs, however it must propose offsets to overspending in order to achieve the annual fiscal targets. A budget contingency reserve is provided for in the LDO. The SOF has developed an online system for tracking the physical and financial execution of the “budget actions” in the LOA. The quarterly performance report on infrastructure investment projects is a recently improved reporting practice.

Recommendations

The following institutional reforms could be pursued to strengthen budget institutions:

- The Constitutional powers of Congress to increase revenue estimates and the President’s powers based on the FRL to issue decrees to reduce expenditures regularly lead to an inefficient and time-consuming budget process. At a certain juncture, these countervailing powers would need to be redefined to ensure both fiscal discipline and efficient allocative decision-making.
- The government should introduce a rolling, medium-term budgetary framework.
- To increase flexibility in the budget, the government should strongly consider decreasing earmarks and the relative size of mandatory expenditure.
- The budget should take on a more strategic focus by reducing the accounting line item details in the budget documents and expanding the strategic, program and performance information. This would facilitate a more strategic direction of budgetary decision-making.

⁶ The Federal Government through Decree nº 7,654, 12.23.2011 has implemented changes in the rules for the acceptance of “restos a pagar” (deferrals) and as result of these changes the timeframe for considering the unprocessed “restos a pagar” as valid has been extended by six months.

- If Congress does not accept the executive's revenue estimates, it should be required to use forecasts prepared by independent parties to ensure that the estimates are objective.
- The Joint Committee of Congress, responsible for guiding the budget process within the legislature, should vote on a firm ceiling for total expenditure based on the primary surplus target and then break this down by ministry or sector. The government should consider eliminating the requirement that all programs in the PPA be evaluated each year and rather focus on evaluating key priority programs and introducing spending reviews including of mandatory expenditures.
- The use of program information and evaluation results should be more systematically incorporated into the budgetary decision-making process.

CANADA

Summary Evaluation

Canada exhibits notable strengths in fiscal reporting and the performance orientation of the budget. The Federal budget and financial statements are comprehensive, and include all major Crown corporations. Fiscal statistics cover the full public sector. The Expenditure Management System (EMS), which was enhanced in 2007, is an integrated framework for setting outcomes and program objectives consistent with the government's priorities, aligning spending with these plans, and monitoring performance. Additional improvements have been made with regard to fiscal forecasting through the publication of a long-term fiscal sustainability report, and formation in 2006 of the Parliamentary Budget Officer (PBO), which greatly expands capacity for independent assessment of government proposals and forecasts. While Canada did not experience the same level of fiscal impact from the financial crisis as many developed countries, it weathered the policy challenges without well-defined fiscal rules or extensive assessment of fiscal risks. Expenditure estimates for the forward years in Canada's medium-term framework for fiscal policy and budgeting are not binding and are re-established each year. More than half of Federal budget is accounted for by statutory spending, principally transfers to households and other levels of government, which does not require annual appropriation, and is not systematically reviewed in the annual budget process.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Macroeconomic and Fiscal Forecasting	Publication of a fiscal sustainability report addressing the impact of an aging population on Federal spending.
Independent Fiscal Agency	The Parliamentary Budget Officer, established at the end of 2006, conducts an independent analysis of the nation's finances, government Estimates, and economic trends.

Fiscal Reporting: Externally audited annual financial statements are published within six months after the year-end and consolidate all Federal government-controlled entities, including Crown corporations (through modified equity accounting). The Canada Pension Plan (CPP) is not consolidated in the government's financial statements because its control is shared with provinces, but CPP financial information is included in the Government's annual financial reports for information purposes. Statistics Canada, a government agency with de facto independence, publishes government financial statistics, prepared in accordance with international standards that cover the full public sector but lack adequate consolidation across levels of government. All government pension funds are included in public sector statistics. The Federal Government also

publishes a Fiscal Monitor, which provides details on the Federal Government budget execution on a monthly basis.

Macroeconomic and Fiscal Forecasting: Macroeconomic and fiscal forecasts are published in the budget documentation, as the Economic Action Plan (EAP) and in the autumn (in the Update of Economic and Fiscal Projections) as the basis for pre-budget consultations, and cover the budget year plus four forward years. Since 1994, the government has adopted for its use the average of macroeconomic forecasts made by private sector institutions (13 in the FY2013-14 forecast). The government prepares and publishes in the budget its own fiscal forecasts, including major fiscal aggregates such as revenues, expenditure, and debt. The effects on revenues and expenditures by adjusting assumptions for growth, inflation and interest rates are presented. The annual debt management strategy is also included in the budget, meeting the legal requirement for the government to present to Parliament the annual borrowing requirement. The budget compares the current macroeconomic and fiscal forecasts to the last two semi-annual forecasts. In October 2012, the government released for the first time a report on the economic and fiscal implications of an aging population, including long-term (outlook to 2050) fiscal projections of elderly related benefits and debt. The report covers the Federal government only. The authorities intend to update it on a regular basis. The PBO prepares Fiscal Sustainability Reports for the Federal and other levels of government extending 75 years into the future.

Fiscal Risk: The budget contains an assessment of macroeconomic risks with sensitivity of revenue and expenditure projections to a number of generic economic shocks. Only the net debt (accumulated deficit) position of the Federal government, however, is reported. While the net position provides important information, the potential impact of an economic downturn on the value of assets is not assessed. Contingent liabilities are recognized according to GAAP standards and provisioned for as possible, and loan guarantees are all approved by Parliament, but the risks associated with those liabilities are not thoroughly presented. Other important risks are not assessed or reported, such as legal claims, natural disasters, and the role natural resources play in sub-national fiscal revenue.

Independent Fiscal Agency: The PBO, an office established in December 2006 that operates under the supervision of the Speakers of the House of Commons and Senate, publishes the Economic and Fiscal Outlook in April and October of each year, which covers the budget year plus four forward years. The Outlook contains the PBO's own forecasts, and compares them with forecasts produced by the government and independent economists. The Outlook contains comparisons of PBO's current forecast with its most recent previous forecast for the same period, explaining variances, but it does not produce an ex post analysis of government fiscal policy. The PBO functions with strong policy independence, though administratively it is still part of the Library of Parliament.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area	
Type of Institution	Reform since 2010
Performance Orientation of the Budget	The EMS was revised in 2006, requiring periodic strategic reviews, expanding the use of outcomes and program objectives, aligning spending plans with government priorities, and enhancing analysis of value for money.

Fiscal Objectives and Rules: A fiscal objective—to balance the budget—was announced by the federal government as policy but is not yet embodied in law. In the early years of the financial crisis, the objective was set to be achieved “over the medium term” although a precise target date was not established. Since then, a target date of FY 2015/16 has been announced, without specifying objectives to be met in the intermediate years. A longer-term federal debt-to-GDP target (25 percent of GDP by 2021) has been recently announced and the government is working on implementing balanced budget legislation to help achieve this goal. The government reports on performance against the overall objective in the pre-budget and budget documents. Most provinces have adopted fiscal rules and target dates for achieving balanced budgets, but such rules are at the discretion of each province and most were put on hold during the financial crisis.

Medium-term Budget Framework: The proposed budget consists of several documents that cover different time periods. First, it contains the fiscal framework (including revenues, expenditures, and borrowing) and policy priorities (social, economic and environmental) to be achieved through the budget. These cover the budget year plus four forward years. The budget identifies the effect on revenues and expenditures of new policies. Second, the Report on Plans and Priorities (RPP), which provides detailed information on proposed Federal departments’ and agencies’ spending, covers the budget year plus two forward years. Neither the budget nor the RPP, described in more detail below, is binding for the forward years and both may be revised each year without explicit reference to the previous year’s document. Finally, the Government Expenditure Plan and Main Estimates cover only the first year of the budget and RPP and form the basis for Parliamentary appropriations.

Performance Orientation of the Budget: The performance orientation of the EMS was significantly enhanced starting in 2007. The EMS is the framework for developing and implementing the government’s expenditure plans, including establishing performance targets and measuring achievement of them. Federal organizations, including departments, agencies and Crown corporations that receive appropriations from Parliament, were required to undertake a strategic review of their direct spending and a review of the operating costs of their major statutory programs once every four years. The results of the strategic reviews were announced in the annual budget. A successor framework for spending reviews has not been announced yet. Each Federal department and agency (excluding Crown corporations) annually prepares a RPP. The RPP sets out strategic outcomes, programs with performance objectives monitored through numerous indicators, and

spending proposals for each organization. Following the end of each fiscal year, the same Federal organizations prepare a Departmental Performance Report (DPR) that measures performance against program objectives and financial plans set out in the RPP. While detailed spending proposals are organized by program in the RPP, appropriations are approved by organization and type of expenditure (e.g. operating, capital).

Intergovernmental Financial Relations: Canada is a decentralized Federal state. Total spending by provincial, territory and municipal governments (referred to as sub-national governments) is about twice the level of Federal government spending. Coordination of tax, expenditure, debt, and regulatory policies between Federal and sub-national governments is largely voluntary in nature. However, the Federal government can indirectly influence sub-national government fiscal policy through cash transfers, which represented 24 percent of the Federal government total program expenditures planned in 2013-14. The government does not release fiscal projections for general government.

C. Implementing the Adjustment Strategy

Budget Unity: The Federal budget covers the whole of central government. The CPP is not consolidated in the Federal budget because the Federal government shares its control with some provinces. Each year, the Department of Finance publishes costs estimates and projections for tax expenditures in the Tax Expenditures and Evaluation report. Forward-looking forecasts are provided only when tax expenditure policies are newly established, modified or eliminated in the budget. Despite some discussion of the efficiency of selected tax expenditure, no direct link is made with the EMS.

Top-down Budget Preparation: Budgets are prepared by the executive in a one-step process in which budget aggregates and details are decided concurrently. While appropriations are made on a cash basis, the high-level budget information is presented using accrual concepts that align it with the financial statements, which makes it easier to compare the budget with the financial statements. Own revenues, which can be spent by the department or agency that collects it, account for approximately 4 percent of Federal expenditures. Statutory spending, which accounts for approximately 60 of total Federal expenditure, is authorized in separate permanent legislation and is not subject to annual appropriations. Statutory spending is not systematically reviewed within the budget process, but only on an incidental basis. Estimates of statutory spending are included in the budget documents for information purposes to provide a full picture of total expected expenditure.

Parliamentary Approval: Parliament approves the budget and the fiscal policy and aggregates within it, through a vote of confidence before turning its attention to detailed review of the Main and Supplementary Estimates. Parliament may reject or reduce spending proposed in the Estimates, but not increase it. As a result of these procedures, the fiscal policy and appropriation levels adopted by Parliament do not differ significantly from the government's proposal. RPPs and DPRs are submitted to Parliament for information only. While the budget is generally submitted before the beginning of the fiscal year, the process of adopting the Main Estimates is usually completed

three months into the fiscal year. A specific appropriation act, providing “interim supply for the Main Estimates”, is passed before the beginning of the fiscal year to ensure continuance of Federal government. Decisions regarding statutory spending, as well as revenues, are submitted to Parliament through a separate Budget Implementation Act (also called the Economic Action Plan Act).

Budget Execution Controls: Departments are responsible for managing the resources allocated to them. Departmental officials are required to maintain records of financial commitments and ensure that payments do not exceed funds appropriated. If payments are found to exceed appropriations, the amount of the excess will be a first charge against the appropriation for the immediately subsequent fiscal year. Payments made in the new fiscal year for amounts owed for work performed or goods received by March 31 can be accrued to the previous year. Execution is closely monitored throughout the year by the Treasury Board Secretariat. Statutory spending can exceed the forecast presented in the budget.

Recommendations

The following institutional reforms could be pursued to strengthen fiscal management:

- Publish a comprehensive, forward-looking fiscal risk statement as part of the budget documentation, which would discuss the potential financial impact on public finances of various issues such as alternative macroeconomic scenarios, PPPs, other explicit and implicit contingent liabilities, natural disasters, and intergovernmental financial relations.
- The PBO should provide an ex-post analysis of fiscal performance in light of the fiscal objectives set by the Federal government. The independence of the PBO could be further strengthened by placing it administratively directly under the Speakers of both houses of parliament.
- Strengthen medium-term fiscal policy by adopting a formal fiscal rule, which needs to be simple, transparent, and supportive of macroeconomic stability by avoiding pro-cyclical fiscal stances, or—as a first step—establish numerical medium-term fiscal targets and a credible pre-determined adjustment path to achieve them.
- Publish consolidated general government fiscal forecasts prepared in consultation with the provinces. Further development of a formalized coordination framework for fiscal policy between levels of government should be seen as a medium-term objective.
- Increase information on the cost and effectiveness of tax expenditures.
- A permanent framework for performing regular strategic spending reviews should be announced and statutory expenditure reviews should feed into budget negotiations in a more systematic fashion.

- Pull the budget preparation process forward into the pre-budget year to allow completion of parliamentary approval before the beginning of the fiscal year.

CHINA

Summary Evaluation

China has made significant progress in reforming its budget institutions in the past decade, though important weaknesses remain. The coverage, quality, and detail of government financial reporting have improved noticeably, but a comprehensive quantified statement of fiscal risks is still missing in budget documents. Multi-year macro and fiscal forecasts are prepared within the Ministry of Finance (MOF), but are not published, nor used by the State Council to help define fiscal policy or expenditure ceilings on a multi-year basis. Though China has a strong track record of fiscal discipline, fiscal policy is focused on the year ahead only. Fiscal targets are formulated for both central and the total of local government. While there is regular coordination between levels of government on expenditure and taxation policies, further efforts are needed to control and coordinate general government fiscal policies and risks. In this regard, recent efforts to gradually allow borrowing at the provincial and city levels, restrict the use of local government financing vehicles (LGFVs), and improve the monitoring of government transfers are welcome. Also, a performance orientation has been added to the budget process in recent years. Its use in expenditure review and allocative decision-making could be improved further. Budget execution at the central government level is tightly controlled during the budget year.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Fiscal Reporting and Government Accounting	Fiscal reporting has improved in coverage, quality and detail. A partial balance sheet of central government is now available in the financial statements. Accounting reform, including the move to accrual accounting, is on the government's reform agenda.
Tracking of Intergovernmental Grants	Central government is introducing monitoring mechanisms for tracking grants and transfers on a pilot basis.

Fiscal Reporting: Budget and financial reporting in China has improved in scope, regularity and detail over the past few years. A full annual budget execution report on the central government, including almost all extra-budgetary funds, is provided to the National People's Congress (NPC) for its deliberations on the new budget in March. Tracking of the use of intergovernmental transfers is still problematic, though a number of pilot monitoring schemes have recently been introduced. The end-of-year financial statements contain a balance sheet with financial assets and liabilities. The National Audit Office provides transaction audits of an increasing number of government ministries,

departments and agencies. Audited financial accounts are published in August/September of the following year, i.e. within nine months of the end of the budget year. Government finance statistics cover central and local government, and are produced and published by an independent statistics office consistent with GFS standards.

Macroeconomic and Fiscal Forecasting: The annual budget documentation provides macro and fiscal forecasts of key aggregates for the year ahead. Medium-term projections are also produced by MOF in the Medium-term Fiscal Plan, but this plan is not published. The information is also not used for discussion or decision-making on fiscal and budgetary policy by the State Council. The key published planning document is the Five-Year Plan of National Economic and Social Development (5YP), which contains a macroeconomic and fiscal outlook over the planning period. The 5YP is updated mid-way of the planning cycle. The annual budget also only provides a one-year outlook of new policy measures. Long-term projections of fiscal expenditures and sustainability are not presented.

Fiscal Risk: In recent years, the State Council has requested investigations into general government fiscal risk, especially of liabilities and contingent liabilities of sub-national government. The National Audit Office has provided (and published) reports on this on a one-off basis.⁷ The budget documents provide only a limited discussion of macroeconomic and fiscal risk.

Independent Fiscal Agency: There is no fully independent fiscal council in China that publishes its own macro and fiscal forecasts and provides opinions on government fiscal policy and performance. However, the Financial and Economic Affairs Committee of the NPC and the Budgetary Affairs Commission of the NPC Standing Committee provide considerable input to the government on fiscal forecasting, policy, and achievements. The Committee and Commission both publish their own, independent macroeconomic and fiscal forecasts on an annual basis. They also provide regular public advice to the State Council on fiscal policy matters. Furthermore, they provide an independent, published assessment of the ex post government budget performance.

⁷ The NAO has produced two reports on local government debt (in June 2011 and July 2013), covering the periods through end-2010 and end-2012, respectively.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area

Type of Institution	Reform since 2010
Medium-term Fiscal Plan	The MOF prepares this plan annually. However, it is not published and only used for internal purposes. It does not inform decisions by the State Council or NPC on medium-term fiscal policy or detailed expenditure decisions. The budget process still has a predominantly annual focus.
Performance Management	Government departments have linked expenditure programs with a host of process and output indicators. The focus on outcomes is still limited as is the use of indicators in the budget review process and allocative decision-making.
Intergovernmental Fiscal Relations	New options for debt issuance are being piloted, while the issuance through LGFVs is being restricted.

Fiscal Objectives and Rules: While China has a long track record of fiscal discipline, fiscal objectives are only presented for the next budget year, and there is no formal fiscal rule guiding central government fiscal policy. For internal purposes, central government uses a 3 percent of GDP deficit limit as an internal guideline for the preparation of the annual budget. Sub-national government has been subject to a balanced budget rule under the 1994 Budget Law, but in practice has managed to finance substantial infrastructure and housing investments through LGFVs. The regulations controlling these vehicles have been strengthened in 2012, but given that the delineation between government and private sector is often unclear in China, liabilities by private sector-dominated LGFVs may still imply major contingent liabilities for sub-national government. In addition to strengthening regulations, the authorities are increasing the scope of sub-national government to incur debt in a well-regulated manner.

Medium-term Budget Framework: China has a medium-term fiscal plan which provides a medium-term orientation to fiscal policy. The plan is not published, however. It includes forecasts of key macro and fiscal aggregates. The fiscal aggregates do not present targets agreed by the State Council. The level of detail includes expenditure and revenue forecasts per ministry, but does not cover expenditure programs. This implies that budgetary policy in essence still has a one-year time horizon only.

Performance Orientation of the Budget: The annual central government budget is compiled by the State Council, adopted by the NPC, and executed on the basis of line ministries and programs. There are nonfinancial performance targets associated with each program, and progress against these targets is published for selected key programs. Sector and program reviews are conducted

periodically in the context of annual budgets and 5YPs. The performance information is not used systematically in budget negotiation or in the decision-making process of the State Council.

Intergovernmental Financial Relations: Central government fiscal policy is prepared based on a view on the consolidated fiscal position of the general government. There are separate targets for the central government deficit and the total local government deficit. While there is regular policy coordination between levels of government on expenditure and taxation policies, a formal coordination framework for fiscal policy is missing.

C. Implementing the Adjustment Strategy

Budget Unity: The central government budget covers more than 80 percent of central government spending. Extra-budgetary funds are reported on in budget documents, including in 2013 for the first time the Social Security Budget. The budget does not contain permanently-mandated expenditure. Tax expenditures are not quantified, nor is there control on their size.

Top-down Budget Preparation: The central government's budget preparation follows a "Two-Up and Two-Down" procedure in which, following an initial exchange of basic data between the MOF and line ministries, the MOF fixes ex-ante ceilings covering both current and capital expenditure. These ceilings are almost always respected by line ministries when submitting their final budget requests. Total revenues for the annual budget have tended to be underestimated. While the resulting surpluses were in the past used for discretionary purposes, since 2008 the NPC has required that any excess revenues be used solely for legally-mandated priority areas (agriculture, education, and science and technology), with the balance to be allocated to a stabilization fund.

Parliamentary Approval: The Budget Affairs Commission of the NPC Standing Committee and the Financial and Economic Affairs Committee of the NPC carry out preliminary examinations and consultations on the draft of the annual budget in December, prior to its presentation to the NPC plenary session for approval in March. Since the government does not present medium-term fiscal objectives or targets, the NPC does not endorse a fiscal strategy beyond the upcoming twelve-month period. Although the NPC's budget amendment rights are not specified in the 1994 Budget Law, in practice the plenary session of the NPC does not amend the State Council's proposed draft budget.

Budget Execution Controls: Controls over budget execution are strong. The 1994 Budget Law specifies that when adjustments are required in the annual budget, governments at each level must prepare an adjustment plan for examination and approval by the Standing Committee of the Peoples' Congress at the corresponding level. Carry-over of budget authority from one year to the next is not permitted for current expenditure. Carry-over of unspent investment expenditure to the next year requires the approval of the finance departments of the respective level before being approved by government at the same level. Central and local governments have contingency reserves of between 1 and 3 percent of total expenditure, but access rules are not clearly specified. Line ministries must submit written requests to the same-level finance department and government

for access. The final accounts submitted by the Central Government to the NPC Standing Committee include an account of how the central reserve was used. The State Council may cut expenditure below budget appropriations on projects within the central government budget under special circumstances with reporting to the NPC, although this has been rare in recent years thanks to the over-performance on revenues. Finally, spending ministries are not authorized to enter into multi-annual spending commitments without the authorization by the State Council.

Recommendations

The following institutional reforms could be pursued to strengthen fiscal management:

- Government accounting needs to further modernized with an emphasis on broadening coverage and consolidation of a wider range of institutions, and recognizing a broader range of assets and liabilities.
- Information flows between sub-national and central governments need to improve, both with respect to government transfers and the incurrence of debt and fiscal risk.
- The MOF should expand the analysis and reporting on fiscal risk both to the State Council and the NPC. Accounting norms for contingent liabilities need to be defined, and regular reporting systems established.
- The government should further develop and publish its medium-term fiscal and budgetary planning tools so they can inform fiscal and budgetary decision-making by the State Council and NPC over the medium-term. The medium-term fiscal plan should include explicit targets for key fiscal aggregates. More detailed expenditure projections should be used to develop medium-term expenditure ceilings.
- The indicator framework to measure the performance of spending programs should be published jointly with corresponding budget information. It should be used during the budget review process and to inform allocative decisions of the State Council.
- While fiscal policy is developed in the context of a general government fiscal target, and an allocation between central and total local government objectives exists, the regulatory and coordination framework for fiscal policy, debt issuance, and incurrence of contingent liabilities across levels of government needs to be further developed.

FRANCE

Summary Evaluation

France's budget institutions are well developed and have strengthened further over the last three years. Fiscal reporting is comprehensive, timely, and detailed but only extends to the general government. Detailed medium-term macroeconomic and fiscal forecasts are published twice a year, but long-term projections are limited to a few indicators and a single scenario. Disclosure and management of contingent liabilities is strong, but analysis and management of macroeconomic and balance sheet risks is limited. A new independent High Council on Public Finances was established in 2013 to evaluate the credibility of official macroeconomic forecasts and fiscal targets. The fiscal rules set out in the EU Fiscal Compact were transposed into an organic law on public finance and governance enacted in 2012. These rules are supported by a multi-year budget framework, strong performance orientation, and strict top-down approach to the preparation, approval, monitoring, and execution of the 30 percent of general government expenditure covered by the State budget. However, State controlled agencies, social security and extra-budgetary funds are governed by somewhat looser rules than the ones applied to the State budget, which has until now contributed to disparities in fiscal performance across different parts of the general government and resulted in a greater share of the consolidation effort coming from the State budget.

A. Understanding the Fiscal Challenge

Type of Institution	Reforms since 2010
Fiscal Reporting	Deployment of a new software package providing commitment, accrual and cash-based recording of state expenditure
Independent Fiscal Agency	Creation of a fiscal council of eleven experts, appointed by Parliament and the Auditor-General, responsible for providing opinions on macroeconomic assumptions underlying the draft budget and fiscal policy and compliance with the fiscal path enshrined in the multi-year public finance law.

Fiscal Reporting: Annual financial statements for all central government entities are produced in a timely manner, independently audited, and include detailed information about assets, liabilities and off-balance sheet liabilities. However, coverage of the government's accounts and statistics is narrower than ideal. While progress has been made since 2010 to consolidate extra-budgetary funds and state controlled agencies, and a new integrated software package—Chorus—deployed, there is still no single, consolidated financial statement for the whole of central government. Fiscal statistics

covering the general government are prepared by the independent national statistics office consistent with ESA 95 requirements.

Macroeconomic and Fiscal Forecasting: The budget presents all the assumptions and macroeconomic forecasts underlying the projected fiscal balance. Supplementary budgets must also include a discussion of the macroeconomic environment and, starting with FY 2014, updated general government fiscal projections for the current year. Comprehensive medium-term macroeconomic and fiscal projections are published only when a multi-year public finance bill is presented to Parliament, namely every other year. Discussions of medium-term updates are however included in Stability Programs and annual budget documentation, but in a less systematic way. Detailed long term projections are routinely published for pensions, and the annual EU Stability Program summarizes the sustainability of public finances using the fiscal gap indicators established by the EC. However, detailed long-term fiscal projections based on a range of demographic and other assumptions are not regularly published.

Fiscal Risk: There is no single, comprehensive statement of fiscal risks. The impact of alternative macroeconomic scenarios is presented only for the coming year in budget documentation. Contingent liabilities related to guarantees and PPPs and, since 2010, callable capital are approved by Parliament and disclosed in financial accounts and, in the case of some guarantees, provisioned for in the annual budget. Financial asset risks are discussed separately in an annual report on ‘Government as a shareholder’.

Independent Fiscal Agency: A new fiscal council, the Haut Conseil des Finances Publiques (HCFP), was established in early 2013 under the auspices of the independent supreme audit institution (Cour des comptes). This council will provide an independent opinion on the macroeconomic assumptions underlying the draft budget, examine whether the annual budget is consistent with medium-term objectives, and identify any significant deviations. Its views will be considered by the constitutional court (Conseil constitutionnel) when judging the compliance of the budget with the constitution, the sincerity of forecasts being a constitutional principle governing public finances.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reforms since 2010
Fiscal Objectives and Rules	The new European fiscal rule has been translated into national legislation. Expenditure rules are now enshrined into law as well.
Medium-term Budget Framework	A new organic law sets the mandatory content of the multi-year finance law and provides that annual budget laws display a table reconciling annual targets with multi-year fiscal objectives.

Fiscal Objectives and Rules: Medium-term fiscal objectives are clearly-stated and have become progressively more sophisticated, comprehensive, and legally-binding. Prior to 2009, fiscal objectives were formulated in terms of a binding limit on the nominal growth of the expenses of the State and a non-binding objective on the nominal growth of healthcare expenditure. Since 2009, these objectives are enshrined in the multi-year public finance law (Loi de programmation des finances publiques), adopted by Parliament every other year. With the implementation of the EU fiscal compact in 2012, the multi-year public finance law must now also set a numerical target for general government deficit both in nominal and structural terms over at least the next three years.

Medium-term Budget Framework: A multi-year budget framework (MTBF) introduced in 2009, covers the State budget (30 percent of general government expenditure) in detail and the social security funds (40 percent of general government expenditure) in aggregate terms. State expenses are planned for three years and strictly capped for two years in nominal terms. Those plans are presented in a consistent manner with the annual budget, including detailed figures for each of the approximately 30 public policies (missions). Allocation between public policies in the annual budget may differ from the MTBF, but has to be justified in the budget documentation. Assumptions and measures underlying the MTBF are presented in general terms, but a comprehensive reconciliation of changes to MTBF ceilings, separately identifying the impact of new policy measures, is not provided

Performance Orientation of the Budget: Since 2006, budget appropriations have been based on a program classification which separates State spending among 30 missions and 150 programs. Objectives and performance targets are set for each program in appendices to the draft budget and results are reported in an attachment to the annual budget review bill. Comprehensive expenditure reviews have been carried-out since 2007 and their results have been used to specify the measures necessary to achieve fiscal targets. However, coverage of those tools remains focused on the State budget.

Intergovernmental Financial Relations: Three rules regulate the control of local government finances by the government. First, public accountants, appointed by the Ministry of Finances, are responsible for controlling the legality of expenses and producing accounts according to standardized norms. Second, all cash collected by local governments must be deposited in the central government's treasury single account. Finally, operating budgets of local governments must be presented in equilibrium. Non compliance with this last rule can result in the government taking over management of the local authority. The respective contributions of central and local governments to meeting the overall general government fiscal targets are set out in the multi-year public finance law and in the annual Stability and Growth Program submitted to the EC. A council for local public finances (Comité des finances locales) convenes the central government and the local authorities to discuss fiscal coordination and has recently been granted some power over the allocation of transfers to local authorities.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Top-down Budgeting	All governmental proposals on tax legislation must be presented in the annual budget law.
Budget Unity	Appropriation of some earmarked expenditures is now annually authorized through the budget process.

Budget Unity: The majority (75 percent) of central government expenditure is covered either by the State budget or by the social security funds' budget, with the exceptions of some revenues earmarked to particular agencies and extra-budgetary funds as well as the unemployment fund and some specific pension funds. Those entities are nonetheless covered by the multi-year public finance law but at an aggregated level. Since 2008, some of these semi-autonomous entities have been subject to additional controls including a cap on staff, regulation strictly prohibiting borrowing, capping part of earmarked taxes, and the passing of a new decree on budgetary management and accounting. All existing tax expenditure is identified and quantified in the documents attached to the budget, and strategic reviews of tax expenditure have been performed on a one-off basis in the recent past.

Top-down Budget Preparation: Budget preparation follows a strict top-down sequence. The state budget is prepared within the limit of the annual aggregate and ministerial expenditure targets fixed in the multi-year finance law. Earmarked revenues account for about ten percent of State and social security expenditure. All major revenue or expenditure decisions are taken as part of the annual budget process, and, since 2010, the government has enacted a rule stating that all governmental proposals on tax legislation must be presented in the annual budget law. As a result, decisions regarding taxes, and tax expenditures, now take place within the context of the annual or supplementary budget debates.

Parliamentary Approval: Budget discussions in Parliament also follow a strict top-down sequence. There is a pre-budget debate (*Débat d'orientation des finances publiques*) in end-June over the general government fiscal stance. While examining the draft budget in October, Parliament votes on the overall budget balance, total revenue, and total expenditure prior to scrutinizing and approving detailed appropriations. Parliamentary procedure prevents any increase in appropriations without approval of Government. The final budget is approved prior to the beginning of the year to which it refers.

Budget Execution Controls: Budget execution controls are strong with tight monitoring of expenditure. The government is required to seek parliamentary approval before the end of the year should actual State expenditure exceed appropriations (except for expenditure on debt servicing and tax reimbursements). By contrast, social security expenses are open-ended. However, remedial measures have to be taken in year should the mid-year forecast for healthcare expenditure

substantially deviate from its target. Full achievement of the annual expenditure targets for the State budget is the norm largely due to strong execution monitoring procedures and contingency reserves provided for in the allocated budget of each line ministry. In addition, the finance minister is authorized to reduce appropriations without limit during execution. Carryover of appropriation is limited to 3 percent of the initial appropriation for each program. Furthermore, multi-year commitments are strictly controlled and authorized by the legislature as part of the budget process.

Recommendations

The following institutional reforms could be pursued to strengthen fiscal management:

- A report on the long-term sustainability of public finances should be published regularly to increase awareness of fiscal challenges.
- Fiscal risks should be discussed more comprehensively in the annual budget documentation.
- The MTBFs should cover total expenditure and specify all the measures needed to meet fiscal targets.
- The tight fiscal objectives for state expenditure in the MTBF as well as the regular spending reviews applied to the State budget, should be progressively deployed over the whole of central government, including social security funds.
- Control over own-revenues taxes and borrowing by state controlled agencies should be enforced more stringently.

GERMANY

Summary Evaluation

The German federal government disseminates a substantial amount of cash and accrual-based financial information in its reports, despite the absence of a comprehensive accrual accounting system at the federal level. Credible multi-year macro and fiscal forecasts and information on financial risks are provided, although a comprehensive quantified statement of fiscal risks is still missing in budget documents. A number of (independent) fiscal institutions collectively perform the tasks of fiscal councils but there is no independent fiscal agency with a broad remit. A debt brake rule has been implemented since 2011 and its permanent structural deficit ceiling will be effective from 2016 at federal level and from 2020 for Länder. A Stability Council (Stabilitätsrat) was established to enforce the fiscal rule at federal and Länder level in 2010 with the mandate to recommend austerity measures. The budget preparation process is not supported by performance information. The medium-term framework has been strengthened through the issuance of the “key figures decision” (Eckwertebeschluss) which is developed through a top-down budget process and discussed by parliamentary budget committee. Budget execution is quite strong although there is some discretion for the ministry of finance to authorize expenditures outside of the annual budget in exceptional circumstances.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Fiscal Reporting and Government Accounting	The Ministry of Finance has established a reform group to modernize the government accounting and budgeting system. The reform seeks to maintain the line-item structure and a cash accounting system but to provide a more comprehensive property account (Vermögensrechnung) and introduce a cost accounting system (Kosten- und Leistungsrechnung).

Fiscal Reporting: The government’s annual financial statements consist of a budget comparison (Haushaltsrechnung) and the property account (Vermögensrechnung). The budget comparison, published in early April each year, provides detailed information on budget execution. The property account provides information on financial assets and liabilities covering all federal entities (Bundesbehörden), except self-governing institutions under public law. The unaudited property account is published with substantial gaps in nonfinancial assets in June each year, while the audit opinion of the Federal Court of Accounts is only available in the fall. A move towards a more comprehensive and inclusive accrual accounting system has not yet taken place. The accounting reform law (Haushaltsgrundsatzmodernisierungsgesetz) covers all levels of government and aims to harmonize accounting practices of governmental entities, but gives federal level and Länder the

option to choose between a cash (cameralistic) and an accrual accounting system based on national accounting standards. According to ESA95, government financial statistics cover general government and are prepared by the independent Federal Statistics Office.

Macroeconomic and Fiscal Forecasting: Germany has a comprehensive macroeconomic and fiscal forecasting model. The medium-term financial plan (Finanzplan) presented to parliament with the budget includes macroeconomic and fiscal projections which are updated twice a year. The Stability Program submitted to the European Commission contains a long-term fiscal sustainability analysis. In addition, the German Ministry of Finance published a more detailed report on fiscal sustainability in 2011 (the third such report after the 2005 and 2008 versions), which contains an assessment of potential risks to the sustainability of public finances and the challenges of demographic developments, using different scenarios up until 2060.

Fiscal Risk: Guarantees, social commitments and public-private partnerships are disclosed in the medium-term financial plan (Finanzplan) and in the property account (Vermögensrechnung). All new contingent liabilities are subject to parliamentary approval. The Stability Program includes sensitivity analysis of medium-term fiscal projections using pessimistic GDP growth forecasts. A comprehensive quantified statement of fiscal risks is not published.

Independent Fiscal Agency: The government decides on the medium-term macroeconomic parameters after considering the forecasts prepared by independent economic institutes. The revenue forecasts are prepared on the basis of these parameters by the independent tax estimation work group. The Court of Audit presents in its annual report an ex post assessment of the financial management of the federal government during the previous year, and the government reacts to its recommendations. The Court of Audit also comments on the budget submissions of line ministries, although its comments are not published. The German Council of Economic Experts (Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung) advises the Government and Parliament on economic policy issues by publishing an annual report to which the government has to respond.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area	
Type of Institution	Reform since 2010
Fiscal Objectives and Rules	A debt brake rule was implemented in 2011 and its structural deficit ceiling will be fully applicable as of 2016 for federal and 2020 for Länder level.
Performance Orientation of the Budget	The German output-oriented budgeting model had not yet been implemented at the federal level, but selected Länder have implemented it (e.g., Berlin, Bremen, Hamburg, Hessen, Nordrhein-Westfalen).
Intergovernmental Fiscal Relations	In 2010, Germany established the Stability Council (Stabilitätsrat) replacing the Financial Planning Council (Finanzplanungsrat) to carry out surveillance of the financial position of both federal and Länder governments.

Fiscal Objectives and Rules: In addition to the fiscal rules set in European legislation, Germany has also implemented a debt brake (Schuldenbremse) in its constitution. Adopted in 2009, the rule restricts structural deficits of central governments to 0.35 percent of GDP and the Länder to 0.0 percent of GDP. As of 2011 the rule has been implemented and its structural deficit ceilings will fully apply in 2016 for the federation and 2020 for the Länder. The fiscal rule includes an escape clause in the case of natural catastrophes, but a debt reduction plan must be developed. The rule also accommodates the business cycle by being defined in structural terms. The existing rules were supplemented by legislation on the domestic transposition of the Fiscal Compact, under which the maximum general-government structural deficit of 0.5 percent of GDP that is permissible under the rules of the Fiscal Compact and the Stability and Growth Pact was enshrined in the Budgetary Principles Act (Haushaltsgrundsatzgesetz).

Medium-term Budget Framework: The federal medium-term financial plan (Finanzplan) includes detailed multi-year estimates of revenues and expenditure by line ministry and is updated annually. Although the ceilings are not binding beyond the budget year, sectoral priorities are transparently identified and changes in resource allocations over the medium term are explained. The medium-term financial plan covers the whole federal budget, with the exception of social security. The fiscal impact of the most important new policies is presented, but the effects of current and new policies are not disclosed separately.

Performance Orientation of the Budget: A comprehensive performance budgeting and performance management system does not exist in the federal budget system. Detailed line items form the basis for budget appropriations, and objectives and targets are not set in the budget and therefore not monitored. "Output-oriented budgeting" (Produktthaushalt) is already in place in some

Länder (e.g., Berlin, Bremen, Hamburg, Hessen, Nordrhein-Westfalen), but not at the federal level. However, at the federal level the line item system has been updated to move in the direction of classification by departmental policies and introduction of a performance orientation. The federal government is also required to submit a report on subsidies to Parliament every two years which includes efficiency analysis for selected policies.

Intergovernmental Financial Relations: The debt brake (Schuldenbremse) described above includes deficit limits for federal and Länder levels of government. The deficits of the different levels of government are presented in the Stability program. For federal and Länder level surveillance purposes, the Stability Council (Stabilitätsrat) was established in 2010 replacing the Financial Planning Council (Finanzplanungsrat). This Council also advises on the coordination of fiscal plans at the different levels of government and is tasked with ensuring compliance with the maximum general-government structural deficit of 0.5 percent of GDP permissible under the rules of the Fiscal Compact. The Council has the remit to recommend austerity programs at individual levels of government to ensure the coordination of and achievement of aggregate fiscal policy.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Top-down Budget Preparation	In 2011, the government implemented “key figure decisions” (Eckwertebeschluss) in March in which binding ceilings for the development of the budget and financial plans are defined.
Parliamentary Approval	The “key figures decisions” (Eckwertebeschluss) are presented by the Minister of Finance to parliament and discussed by the parliamentary budget committee.

Budget Unity: The central government budget excludes social security funds due to their legally independent status. Therefore only around 40 percent of central government expenditure is covered by the budget. The budget does not contain any permanently-mandated expenditure. Estimates of all tax expenditure are reported to the public every two years in the report on subsidies, but there is no binding control on the size of tax expenditure.

Top-down Budget Preparation: The government has introduced a top-down budgeting process in 2011 which is part of the internal budget preparation process of the government. In the “key figures decision” (Eckwertebeschluss), the government defines the aggregate and ministerial ceilings for expenditures and revenues in March. This is the binding basis for developing the medium-term financial plan (Finanzplan) and the annual budget. The budget process for central governmental entities is comprehensive. After a strong increase in the years following reunification, revenue

earmarking through special accounts has fallen in recent years, but these procedures were used again recently to implement post-crisis interventions in the financial sector.

Parliamentary Approval: The parliamentary approval process was not formally changed to accommodate the new top-down procedure, but the “key figures decision” (Eckwertebeschluss) is presented by the Minister of Finance to parliament and is discussed by the parliamentary budget committee in March. However, neither the Eckwertebeschluss nor the financial plan is formally approved by parliament. The constitution does not restrict the right of parliament to amend the government’s draft budget proposal. The parliament has a veto over the government’s proposal to change the aggregate expenditure ceiling, future commitments or expected revenues. The budget is approved before the beginning of the budget year.

Budget Execution Controls: Budget overruns are authorized by supplementary budgets, but offsetting reductions in other appropriations are not required. While there is no explicit contingency reserve in the budget, urgent needs are addressed through the excess expenditure procedure. After consultation of the Budget Committee of the Bundestag, the Minister of Finance may authorize unforeseen and compelling expenditure in excess of voted appropriations. The Federal Budget Code (Bundeshaushaltsordnung) and the annual budget define the types of expenditure which may be carried forward to future years. The use of unspent appropriations from the previous year’s budget requires the consent of the Ministry of Finance and an equivalent saving on the budget of the sectoral ministry. Some budget items are, however, exempted from these requirements. The Minister of Finance may impose blocks on voted appropriations, without limit, if they are justified by savings requirements. Commitment appropriations voted by Parliament separately from cash appropriations offer a strong basis for the control of multi-annual commitments.

Recommendations

- The federal government should prepare and publish a more comprehensive balance sheet, including nonfinancial assets gathered by a comprehensive (accrual) accounting system.
- Ongoing efforts to strengthen harmonization of the accounting systems between federal and Länder level should be continued and common accounting policies should be required at all levels of government.
- The detailed line-item budget classification should be replaced by a program budget structure.
- Implementing a model for performance-orientation and integrating performance elements, including policy outcomes and service delivery, into the budget process should be pursued with greater urgency.

INDIA

Summary Evaluation

India's fiscal consolidation measures have focused on improving the fiscal balance over the medium-term and better management of fiscal risks. This effort is enabled by amendments to the Fiscal Responsibility and Budget Management (FRBM) Act, which lays down the path to fiscal sustainability over the medium term. However, opportunities to strengthen budget institutions remain. With respect to fiscal reporting, autonomous bodies and extra-budgetary funds should be included in financial accounts and budgets for information. While provisional fiscal data are readily available, audited financial statements take almost a year to complete. Publishing medium-term macroeconomic projections with the new Medium-Term Fiscal Policy Statement and the annual budget would strengthen the conviction of markets that fiscal targets will be achieved. The recent initiative to publish a Medium-Term Expenditure Statement is a positive step that needs to be developed further. Developing a medium-term fiscal and budget framework, including impact analysis of new policies in expenditure proposals, revenue measures and debt strategy, is essential to assess fiscal sustainability. The robust budget execution process offers scope for further tightening up to ensure adherence to the stated fiscal policy and needs stronger focus on efficiency, transparency, and results. Promoting independent fiscal agencies charged with the responsibility of macroeconomic forecasting and statistical reporting would further promote fiscal transparency and the consolidation objectives.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Fiscal Risk Management	The government is taking steps to improve the disclosure of contingent liabilities arising from the public private partnership (PPP) projects. Government guarantees are subject to a limit of 0.5 percent of GDP. The government is systematically building a fund for servicing any guarantees that may be invoked.

Fiscal Reporting: The Union Finance Accounts (financial statements of the Union Government) cover the central budgetary sector, but not autonomous bodies and extra-budgetary funds. They are audited by the Comptroller and Auditor General (CAG), an independent body authorized by the Constitution, and are published 10-12 months after the end of the fiscal year. Provisional fiscal data are available in the public domain in the succeeding month and in practice differ little from the certified accounts. The CAG also publishes consolidated accounts of central government and states, but lower levels of government are not included. Under its cash-based accounting system, financial

assets and liabilities are well recorded, and under the planned move to accruals disclosure of other assets, liabilities, and contingent liabilities should improve further. The non-disclosure presently of employee pension liabilities under the old defined benefit scheme is a point of concern. Estimates on government nonfinancial assets are provided in an annex to the Receipt Budget, but these are not incorporated in the financial statements. Annual expenditures on nonfinancial assets, however, are presented in Statement No. 10 of the Finance Accounts.

Statistical policies and practices are guided by professional principles and the fiscal data are compiled on an impartial basis, largely consistent with international standards. The Public Finance Statistics prepared annually by the Ministry of Finance, and using national reporting standards, consolidates fiscal data for the central and the state governments, but the report is based on approved budget estimates. This report also excludes information on extra-budgetary operations. The main source of general government data (estimates) is publications of the Reserve Bank.

Macroeconomic and Fiscal Forecasting: Macroeconomic forecasts are published only as part of the Five Year Plan, with the out-years having more the character of assumptions than actual forecasts. The annual Economic Survey and the Macroeconomic Framework Statement submitted along with the budget have some discussion of the economic outlook. They focus mostly on past economic performance, however. The Medium-Term Fiscal Policy Statement contains three-year rolling forecasts of key fiscal aggregates. Supporting macroeconomic projections are prepared within the Executive but not published. There is no analysis of alternate medium-term macroeconomic scenarios. The mid-year review presented by the government carries an analysis of the outlook for the remaining part of the year only. No long-term fiscal projections are published.

Fiscal Risk: Outstanding explicit guarantees are reported in quantitative terms for each ministry. Fiscal risks emanating from other possible sources, such as macro-fiscal developments, international and social commitments, pensions, PPPs, legal claims and implicit contingent liabilities are neither discussed nor quantified. The May 2013 amendments to the FRBM Rules require the government to report explicit contingent liabilities arising on account of annuity payments on PPP infrastructure projects. The FRBM Rules also place an annual limit of 0.5 percent of GDP on new guarantees. This low ceiling will most likely ensure that the stock of guarantees will decrease as a percentage of GDP,⁸ as they have done over the last ten years. The government in 1999 established a Guarantee Redemption Fund, a revolving fund that is built up through transfers appropriated in the budget, to discharge liabilities arising from any guarantees invoked. The government does not publish a medium-term debt strategy but plans to do so beginning in FY2014-15. It does not publish an assessment of the risks associated with government assets.

Independent Fiscal Agency: In India, the macroeconomic and the fiscal forecasts prepared by the finance ministry are scrutinized by the Standing Committee on Finance of the Parliament. However, there is no designated technical, non-partisan body outside of the executive

⁸ The ratio of guarantees to GDP will decrease whenever GDP increases at a greater rate than guarantees.

and legislature that routinely reviews these forecasts, which are the distinguishing characteristics of a fiscal council. The CAG evaluates and reports ex post on the government's fiscal performance, but no independent institution ex ante evaluates the government's fiscal policy.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reform since 2010
Fiscal Objectives and Rules	The fiscal objectives and rules have been freshly articulated in 2012 and clear targets for the medium-term have been specified in the 2013 amendments to the fiscal rules. The targets, however, relate only to central government budget.
Performance Management	An outcome budget containing quantifiable performance indicators has been introduced but is still not fully integrated with the budget and the budget decision making.

Fiscal Objectives and Rules: After abandoning the goals set by the 2003 FRBM Act in the aftermath of the financial crisis, the government has recently articulated fresh medium-term fiscal objectives. Recent amendments to the FRBM Rules require the government to reduce the overall fiscal deficit to 3 percent of GDP by 2017 and eliminate the recurrent budget deficit by 2015. Starting from FY2013-14, the Rules require improvement in the fiscal balance by 0.5 percent or more of GDP every year and in the recurrent balance by 0.8 percent or more of GDP every year. The fiscal objectives do not accommodate the business cycle. The government reports performance against its fiscal objectives on quarterly basis. If the government cannot attain the objectives (measured by the fact that the actual fiscal deficit at the end of the second quarter of a year exceeds 60 percent of the annual target), the Finance Minister must take corrective measures and explain them to the parliament. The fiscal objectives apply only to the central government, but as discussed below state governments have their own FRBMs, and individual borrowing of states is constrained because it is subject to approval by central government.

Medium-term Budget Framework: The Five Year Plan provides a multi-year perspective to fiscal policy and the budget, though it does not cover all expenditures. It also provides a basis for a sectoral multi-year perspective, but the plans may not always translate into budgetary allocations. The annual Medium-Term Fiscal Policy Statement specifies for the central government rolling three-year targets (expressed as percentage to GDP) for the budget balance, aggregate tax revenue, and public debt, but these remain indicative and not legally binding on the government. For the first time, a Medium-Term Expenditure Statement was published in September 2012 providing forward expenditure estimates by economic categories in the central budget. A consolidated presentation of

new revenue or expenditure policies is lacking. As a result, the impact of new spending proposals on expenditures in future years is not available.

Performance Orientation of the Budget: In 2005, the government introduced an annual outcome budget, which contains quantified performance targets for various programs. Although, the outcome budgets carry objectives and targets for the forthcoming year, as well as actual performance for the past year, the linkages between performance and resource allocation are not always clear. Also, the penalties for not achieving the intended program objectives are weak and seemingly ineffective. The Planning Commission routinely conducts performance reviews of the “plan” budget, but not the “non-plan” component of the budget. Beginning in 2009, the Performance Monitoring and Evaluation System (PMES) was established for the purpose of moving departments from a process orientation to a results orientation and evaluating each department’s overall performance at the end of the year. The budget is appropriated by functions (programs).

Intergovernmental Financial Relations: In Constitutional provisions and the Finance Commission, which is constituted every five years, there is a formal mechanism to regulate fiscal relations, including revenue sharing, between the Union and the States. All Indian states have fiscal responsibility laws. However, as with the central government FRBM Act, the application of most of these laws was suspended in the aftermath of the global financial crisis. Despite this relaxation, borrowing by states, and hence fiscal deficits, was constrained in part because approval by the central government of state borrowing is constitutionally required. All states have subsequently amended their FRBM Acts in line with targets recommended by the XIII Finance Commission.

C. Implementing the Adjustment Strategy

Budget Unity: The quantum of extra-budgetary expenditure of the central government is not available in one place, but it is expected to be less than 10 percent of the budgetary expenditure. Nearly one-fourth of the central government budget is in the form of standing appropriations as expenditures “charged” on the Consolidated Fund that are not put to Parliamentary vote. Parliament, however, can discuss these expenditures. Estimates of main tax expenditures are disclosed in the budget documents, but there is no mechanism to control their size.

Top-down Budget Preparation: The budget formulation process in the executive is a robust two-stage combination of top-down and bottom-up processes. In the first stage, line ministries’ proposals are discussed at the Secretary level during the pre-budget meetings and feed into specification of hard aggregate expenditure ceilings for each ministry. The ceilings are consistent with the overall deficit target for the year and the estimated revenues and borrowings. In the second stage, ministries prepare their detailed budgets while adhering to their respective ceilings.

Parliamentary Approval: Parliament approves the budget following procedures outlined in the Constitution. Although the “General Discussion” at the beginning of the budget debate focuses on

the budget as a whole and the broad tax and expenditure policy aspects, there is no requirement for the budget aggregates to be approved before considering the detailed spending proposals. The Constitution prohibits parliament from increasing a budget provision or introducing a new expenditure item as it reviews the government's budget proposal. The budget is usually not approved by the start of the fiscal year. The general practice is to obtain a Vote on Account to enable the government to incur expenditure during the interim period.

Budget Execution Controls: There is no restriction on the government's ability to seek supplementary appropriations. However, in practice, the government generally discourages supplementaries that result in a net increase in expenditures. Supplementary appropriations are mainly obtained for reallocations affecting a parliamentary Vote. Measures, such as no carry-over of expenditure authority, restrictive virement rules, and strong internal controls, are in place to further strengthen fiscal discipline. The mid-year review process, leading to the development of the "Revised Estimates," provides the finance ministry the opportunity to place additional restrictions on expenditure, should it be required. Multi-annual commitments are regulated through a combination of well-defined delegation of financial powers to the spending agencies and a process of ex ante financial concurrence. Plan expenditures are also subject to monitoring by the Planning Commission.

Recommendations

The following institutional reforms could be pursued to strengthen fiscal management:

- Improve the coverage of fiscal reporting and the timeliness of formal financial reports. The audited Union accounts should include autonomous bodies and extra-budgetary funds. Ideally they should be published within six months of the year-end. Under the planned move to accrual accounting, information on assets, liabilities, and contingent liabilities, should be further enhanced.
- Publish annually, medium-term macroeconomic forecasts and link fiscal targets to the forward macroeconomic projections. The fiscal forecasts should be supported by publishing the underlying assumptions. Long-term fiscal forecasts should also be prepared and updated at least for every Five Years Plan.
- A binding medium-term budget framework could be considered. The Medium-Term Fiscal Policy Statement and Five Year Plans should be better integrated to provide rolling multi-year expenditure limits. Fiscal forecasts should systematically identify the impact of all new revenue and expenditure policies. A consolidated view of fragmented fiscal policy initiatives is important.
- Integrate performance information in the budget presentation and the budget decision-making process and strengthen transparency and accountability in budget execution.
- Promote independent agencies for macroeconomic and fiscal forecasting and compilation of fiscal statistics.

INDONESIA

Summary Evaluation

In the early 2000s, Indonesia introduced a series of laws to modernize its public financial management (PFM) system and to delegate extensive fiscal and functional responsibilities to sub-national governments (SNGs). Over the past decade, Indonesia has implemented wide ranging PFM reforms including establishing a comprehensive fiscal risk statement, a fiscal rule for general government, and a unified central government budget. Throughout this period fiscal discipline has been maintained including at the SNG level. In 2009, the government piloted medium-term budget frameworks (MTBF) and performance budgeting reforms in six ministries, and subsequently is rolling out an expanded MTBF and enhanced performance indicators throughout central government. Despite this progress, challenges remain with monitoring the fiscal rule; improving budget execution—the capital budget is systematically underutilized; establishing baselines for the MTBF; establishing and managing the performance monitoring system. A major issue is also Parliament’s focus on the details of budget line items and capital projects rather than fiscal policy and strategic expenditure issues. Since 2010 reform efforts have focused on implementing the MTBF and performance budgeting initiatives government-wide, and improving budget execution and SNGs’ financial reporting.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Fiscal Reporting	The MOF’s PMK 238/2011 regulation on the government accounting system (SAP) seeks to establish a new standardized chart of accounts structure for central and local governments and to improve the reporting of government fiscal statistics.

Fiscal Reporting: The Indonesian government’s annual financial statement (LKPP) includes a balance sheet with assets and liabilities, but it does not cover pensions, SOEs, or all of central government’s activities. The independent supreme audit institution (BPK) certifies the accounts and publishes an annual audit report within six months from the end of the financial year (FY). The National Statistics Office reports data (for GFS publication) for budgetary central government, including external debt. Fiscal reports for general government are available but with approximately one year delay due to the 524 first-tier SNGs’ weak compliance with reporting requirements. Since 2010, the government has introduced a number of initiatives to improve SNGs’ reporting, such as issuing new regulations on submitting financial reports and enhancing the systems for data collection and sharing of information.

Macroeconomic and Fiscal Forecasting: In February of each year, the MOF and other key agencies prepare economic assumptions and forecasts of fiscal variables. These are discussed with a committee of experts from key government ministries. The committee does not forecast an exact fixed point for the key economic variables, such as economic growth, inflation, and oil prices, but rather it proposes a narrow range which is then discussed with Parliament. In mid-May the government presents a pre-budget report to parliament, which sets out its fiscal policies and priorities and its macroeconomic framework including all key economic assumptions (within proposed ranges), as well as revenue and expenditure policies. Through intensive discussions, the government and the relevant parliament budget committees reach an agreement including on macroeconomic assumptions (within ranges), development plan priorities, and fiscal policies. In August, based on the agreement reached, the government presents the annual budget proposal and its financial note to Parliament. The proposed budget includes macroeconomic assumptions in terms of point estimates and medium term fiscal projections for the current year and three following year. A mid-year report is presented to Parliament that includes details of the first six months of budget execution and updated macro-fiscal forecasts over the medium-term.

Fiscal Risk Statement: The Indonesian government submits to Parliament along with the budget an annual fiscal risk statement that identifies risks arising from central government debt and contingent liabilities, among other issues. Many risks are quantified in the statement. Risk reserve allocations or funds have been established to mitigate certain fiscal risks. For example, the Indonesian Infrastructure Guarantee Fund was created to manage fiscal risk arising from government guarantees of infrastructure projects, and the annual budget also contains allocations for contingencies including macroeconomic risk. Although Parliament is informed about new contingent liabilities, it does not approve them, nor is an annual limit set.

Independent Fiscal Agency: There is no independent fiscal council. No independent Indonesian body officially produces alternative forecasts or compares the government's forecasts with those of the private sector or other forecasting institutions. There is no independent institution conducting an ex ante or ex post assessment of government fiscal policies and performance.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area	
Type of Institution	Reform since 2010
Medium-Term Budget Frameworks	Budget documents include estimates for three years beyond the budget year at the spending ministry and program level.
Performance Orientation	The government introduced a new program structure and performance measures, mostly outputs, into planning and budget documents. There are ongoing efforts to develop a systematic monitoring and evaluation system.

Fiscal Objectives and Rules: The State Finance Law 17/2003 establishes a fiscal rule that caps the annual deficit at 3 percent of GDP and general government debt at 60 percent of GDP. In practice, the rule has never been tested as over the past decade Indonesia's deficit and debt have been kept consistently below these limits. The rule contains no formal sanctions or enforcement procedures, nor does it accommodate the business cycle or have well-specified escape clauses. The government's medium-term fiscal balance objectives are presented annually to parliament however, they only cover central government. An annual decree issued by the MOF also sets annual limits for regional deficits and debt levels. For implementation purposes, the government assumes that the SNG's total deficit will be a maximum 0.5 percent of GDP leaving a ceiling for central government of 2.5 percent. Due to lack of timely and comprehensive general government fiscal statistics (especially local government statistics), it is difficult to monitor and report on performance against the fiscal rule.

Medium-Term Budget Framework (MTBF): Indonesia has a strong and long-standing national planning system and is currently introducing a rolling four-year MTBF. In 2009, the MOF and the Ministry of Planning (Bappenas) launched pilot projects on MTBF and performance budgeting (PB) in six spending ministries (SMs), which led subsequently to changes in both planning and budget documents to help introduce a MTBF government-wide. At the start of each Presidential term a five-year fixed plan (RPJMN) is developed to reflect the President's medium term strategic priorities. This now includes an indicative medium-term resource envelope and indicative ceilings for over 170 priority programs. The government-wide annual plan (RKP) elaborates on the RPJMN's priorities to include details of new projects as well as establishing annual indicative ceilings for SMs within the MOF's overall annual resource envelope. Based on the RKP, SMs develop annual work plans (Renja-KL) and annual budget proposals (RKA-KL). The 2011 SMs' budget submissions in the RKA-KL contained three year forward estimates at the program and activity level. These forward estimates, which cover around 44 percent of government expenditure, have been incorporated into the budget documents presented to Parliament. There is no distinction between baseline expenditures and new initiatives⁹ and updated forward estimates are not used as the starting point for the next year's budget. Spending estimates are not used as binding multi-year expenditure restrictions, neither for aggregate central government spending nor for sectoral/ministry spending.

Performance Orientation of the Budget: The government is in the process of introducing performance budgeting government-wide. A key part of this initiative has been reforming the program classification. Previously, the five-year and annual government plans did not align programs with organizational structures. Beginning in 2010, the government's five-year and annual plans, and spending ministries plans, were based on a new program classification aligning programs and organizations and incorporating performance targets and indicators. RKA-KL budget documents include 5000 outputs and performance indicators. However, both the program classification and the output indicators used in the budget are different from those used in planning documents. For the

⁹ In the 2014 budget documents, an initial effort was made to distinguish between new and existing policies but the analysis was incomplete and further refinements of presentation in future budgets are anticipated.

2015 budget the government is working on aligning the structures and indicators used in planning and budget documents. In addition, the government is concentrating on improving the quality of performance information (PI) and developing a system for monitoring and evaluation. Currently, PI is not used extensively in budgetary decision making. There are no comprehensive spending reviews. Non-discretionary spending includes routine operational expenditures which tend to increase incrementally from year to year without any review. Recently the Treasury has been assigned the task of developing comprehensive spending reviews and the MOP is currently piloting a review of infrastructure spending.

Intergovernmental Financial Relations: In the early 2000s, the government began an extensive and rapid decentralization program. Regional governance law 32/2004 transferred responsibilities for all major public services to the regions and provinces. In parallel, the fiscal balance law 33/2004 expanded the regions' fiscal responsibilities and established a system of transfers and revenue sharing. The SNGs account for around 41 percent of total general government expenditures. They receive approximately 90 percent of their funding from central government. Their capacity to borrow is strictly limited; direct foreign borrowing is not allowed and pre-approval of the MOF is required before SNGs can borrow domestically. Regional governments are also required to report to the Ministry of Home Affairs (MOHA) and MOF on their budget balance 30 days after the end of each semester and to provide an approved annual financial report no later than August 31st following the end of the financial year. Challenges have emerged with regard to SNGs lack of timeliness in enacting their budgets, under- and untimely financial reporting, and weak budget execution. As of mid-2012, only 88 percent of regional governments had submitted their annual financial reports for FY2010.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Budget Execution Controls	The government issued new regulations 45/2013 and 94/2013 to improve budget implementation and address issues of rigid and slow budget execution. These regulations introduce commitment controls, allow earlier procurement, and remove other obstacles to budget execution.

Budget Unity: In 2005, the "routine" and "development" budgets were integrated into a single "state budget" for central government. Annual appropriations are required for the majority of central government expenditure, with a few expenditures based on permanent legislation outside the budget and less than 10 percent of total central government expenditures being off-budget. There is a constitutional mandate that earmarks 20 percent of total government expenditures for

education. Since 2003 some tax expenditures have been quantified in the annual budget, but limits are not placed on their size.

Top-down Budget Preparation: The budget process in Indonesia starts as a top-down process but budget ceilings at both the aggregate and ministry level may change during the course of budget preparation. The process starts with the establishment of overall aggregates for non-discretionary and discretionary spending. In March, the MOF and Bappenas issue a circular, with cabinet approved indicative ceilings for SMs and programs, for the current financial year and three forward years. As noted earlier, discussions with Parliament in May result in changes to the aggregate ceilings and revised revenue and economic growth projections. After agreement with Parliament on the macro-economic framework in mid-June the government issues new ceilings to SMs known as budget ceilings. SMs use these to revise their plans and produce the RKA-KL. In August, once the annual budget proposal is presented to Parliament, the ceilings tend not to change although the composition of expenditures may shift. When the budget is approved the final ceilings are issued in the detailed budget execution guidelines. Major revenue and expenditure decisions are taken as part of the annual budget preparation processes. In recent years, however, the government has produced a revised budget prior to the end of the first half of the FY. This extensive use of the revised budget is to correct for inaccurate macroeconomic assumptions which have contributed to over estimations of revenues and underestimation of subsidy spending. Across the board cuts have been applied to all SMs non-priority expenditure as part of these revised budgets.

Parliamentary Approval: The Indonesian Parliament is very active during the budget approval process. In principle, it has unlimited powers to amend the budget. In practice, formal amendments are limited in size. As noted earlier, Parliament negotiates with the executive on the macroeconomic and fiscal forecasts on which the executive's budget proposal is based. While there is a lengthy and detailed review of the budget, Parliamentarians mostly focus on individual line items, capital investments, and constituency interests. There is no separate debate on the government's fiscal policy; its medium term objectives; strategic policy issues, or inter-sectoral allocations. Despite recent improvements, budget documents remain very detailed with limited strategic focus. Parliament plays a very limited role in the ex post evaluation of programs performance, although the recently established State Finance Accountability Committee has started to review audit reports. The annual budget is approved in a timely manner two months before the start of the new FY.

Budget Execution Controls: The MOF can cut or defer expenditure without the pre-approval of Parliament. Regulations place tight restrictions on multi-annual expenditure commitments. There is no carry-over of unspent appropriations to the next year. There is a general contingency reserve, although the rules relating to its use are not transparent. A supplementary budget that increases aggregate expenditure requires the approval of Parliament. There have been two persistent challenges with budget execution: under-spending and a disproportionate amount of spending in the last quarter. Both issues relate particularly to capital expenditures. In 2013, the government introduced new regulations to address these challenges, including no longer requiring the reappointment each year of budget execution officers in the spending units and introducing commitment controls. Additional changes include allowing the procurement process to begin

before the start of the FY and eliminating the “Bintang” practice, which permits the blocking of budget execution by parliamentary committees.

Recommendations

The following institutional reforms could be pursued to strengthen budget institutions:

- Introduce a formal mechanism to monitor and report on the differences between annual outturns and fiscal objectives and rules. This will give greater credibility and accountability to fiscal policy.
- Improve macroeconomic and fiscal forecasting by publishing the following: the underlying economic assumptions, alongside comparison with private sector forecasts, and an ex post comparison of forecasts with actual outturns. Also, publish the changes the legislature makes to the key economic assumptions and forecasts.
- Create an independent fiscal council to review the official forecasts and conduct independent evaluations of the government’s fiscal performance.
- Establish a more strategic annual and medium term focus to budget documents by reducing detail, separating ongoing programs from new initiatives, and aligning the programs and indicators used in planning and budget documents.
- Strengthen the implementation of the MTBF by establishing clear procedures for updating baselines that will support more accurate projections at the SM and program level. Expand the MTBF to cover the entire central government budget, and explain variances between budget year aggregate ceilings and the aggregates forecasted in the prior year MTBF.
- Establish a more clearly defined two-step top-down budget preparation process in which the executive and Parliament agree on fiscal aggregates and SM ceilings before addressing detailed budget issues at the SM or program level. This will make the budget process more efficient as well as strengthening fiscal discipline.
- Improve fiscal reporting by local governments, which execute a large share of general government expenditures and have been the beneficiaries of important fiscal decentralization policies.
- Introduce spending reviews, including of non-discretionary spending, to improve the quality of expenditures and help create fiscal space. In addition, subsidies, revenues, and transfer policies should be part of the broader fiscal discussion during budget preparation.

ITALY

Summary Evaluation

Fiscal reporting is reasonably comprehensive and timely, though central government financial statements remain incomplete. Medium-term macro-fiscal projections and long-term scenarios are produced regularly and a partial reconciliation between successive fiscal plans and outturn is provided in planning documents. Budget documents contain information on major fiscal risks, but this still falls short of a comprehensive statement of fiscal risks. Italy has now enshrined in its Constitution a budget balance principle, introduced a spending rule and developed a more detailed MTBF which provides more transparent guidelines for budget planning. However, the medium-term expenditure limits can be exceeded in subsequent years. The April 2012 constitutional amendment created a Parliamentary Budget Office (PBO), which is expected to become operational in 2014, to provide an independent assessment of macroeconomic and fiscal projections to the Senate and the Chamber of Deputies. Recent legislative reforms have the potential to improve aggregate expenditure control which has traditionally focused more on the legal regularity of expenditure than on ensuring compliance with the government's overall fiscal objectives.

A. Understanding the Fiscal Challenge

Type of Institution	Reforms since 2010
Independent Fiscal Agency	Enacted legislation to establish an independent and well resourced Parliamentary Budget Office (PBO) with a broad mandate.

Fiscal Reporting: Fiscal reporting is reasonably comprehensive and timely. The central government's annual financial statements consolidate all of central government, with the exception of some entities and balance sheet items. The State's final accounts cover the budgetary central administrations (the line ministries) and some agencies supervised by the ministries. A balance sheet for the State sector is produced but a comprehensive and complete balance sheet for the central government is not compiled. The accounts are audited by an independent institution, the Italian Court of Auditors, which publishes, by the end of June of the year following the reference year, its report on the State's final accounts. General government finance statistics are produced by the independent Italian statistical office and by Banca d'Italia (the so-called Maastricht and financial accounts), according to the National Accounts framework, in line with ESA95 methodologies, following European statistical standards for EDP reporting and Eurostat guidelines.

Macroeconomic and Fiscal Forecasting: Italy's medium-term macroeconomic and fiscal forecasts are produced in the context of the annual Economic and Financial Document (DEF), which includes

the Stability Program Update, and are then updated later in the year for the purpose of budget preparation. Long-term fiscal projections on age related spending are prepared annually and included in the Stability Program Update. The planning documents provide some reconciliation between successive fiscal plans, by explaining the revisions which occurred in the macroeconomic assumptions underlying the fiscal projections. A detailed reconciliation, which breaks down any differences between the DEF and the budget for each ministry, policy areas, or program into various factors (macroeconomic determinants, operational parameters, accounting changes and policy measures), is not provided.

Fiscal Risk: Some qualitative information on contingent liabilities, macroeconomic risks and tax expenditures are regularly disclosed. The Stability Program Update contains additional information on fiscal risks, including those related to financial sector and those stemming from ageing and different underlying growth projections. However, it still falls short of a comprehensive statement of fiscal risks.

Independent Fiscal Agency: The April 2012 constitutional amendment created a Parliamentary Budget Office (PBO) to provide an independent assessment of macroeconomic and fiscal projections to the Senate and the Chamber of Deputies. Its tasks and architecture are laid out in Law 243 of December 2012 which closely follows international good practice in the design and operation of independent fiscal agencies. The PBO will be chaired by a three-person council with a broad mandate which encompasses assessing (i) fiscal developments, including compliance with fiscal rules; (ii) macroeconomic and fiscal government forecasts; (iii) long-term public finance sustainability; and (iv) fiscal impact of major legislative packages. In addition, the PBO will provide advice on the activation of the correction mechanism and escape clause for the government's new fiscal rules. The PBO is expected to become operational in 2014.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reforms since 2010
Fiscal Objectives and Rules	Law 243/2012 details the principle of balanced budget set in the Constitution and introduces some amendments in the Italian legislation in line with the provisions in the EU Stability and Growth Pact and Fiscal Compact.
Medium-term Budget Framework	An indicative medium-term budget framework is now being produced, which provides three year forecasts of government expenditure by mission and program.

Fiscal Objectives and Rules: Following the provisions of the EU Fiscal Compact, Italy has enshrined in its Constitution a budget balance principle, to be effective in 2014, which applies to general

government and takes into account economic cyclical fluctuations and exceptional circumstances. Law 243/2012 includes also rules for general government spending and debt. The spending rule (effective 2013) limits planned growth rates of public expenditure to the benchmark set at European level. Similarly, the debt rule (to be applied in 2016) requires that debt ratio should decline by one-twentieth of the amount by which it differs from the 60 percent of GDP reference value per year, calculated over the previous three years.

Medium-term Budget Framework: Since 2011, the Economic and Financial Planning Document (DPEF) has been replaced by the DEF, which includes planning targets for the budget balances and debts of the general government and its sub-sectors, which are then further broken down into a three-year forecast of State Budget expenditure by mission and program in the budget. As a result of these reforms, Italy now has a more detailed MTBF which provides more transparent and detailed guidelines for ministerial budget planning. However, the current framework still does not constitute a binding constraint on future budgets, as the medium-term debt and deficit targets and expenditure benchmark are recalculated each year on a rolling basis. Some reconciliation between successive fiscal plans is included in planning documents.

Performance Orientation of the Budget: Italy introduced a program classification in 2008, although performance monitoring by the parliament has been relatively limited. Systematic reporting on progress with respect to the performance targets and objectives is lacking. Spending reviews now cover all ministries and are carried out at three year intervals, in order to properly reallocate central administration spending across programs.

Intergovernmental Financial Relations: The Domestic Stability Pact, originally introduced in 1999, establishes the main constraints for regional and local governments by establishing a target for budget balance for municipalities and provinces and a constraint on the nominal growth of expenditures for regions. The Pact also includes sanctions in case of nonobservance of the targets which however have not always been effective in preventing overspending against the targets. Regional governments' spending for health services is controlled by a separate Health Pact which sets limits to current and capital expenditure for healthcare by region.

C. Implementing the Adjustment Strategy

Type of Institution	Reforms since 2010
Expenditure Control	<p>Initiated reforms to budget management designed to unify budget legislation, consolidate the number of appropriations, reduce earmarking and eliminate special funds.</p> <p>Introduced a spending rule limiting planned growth rates of public expenditure to the benchmark set at European level.</p>

Budget Unity: The central government budget covers more than 90 percent of central government spending and more than 90 percent of budget spending requires annual authorization by parliament. Tax expenditures are quantified, but there is no control their size.

Top-down Budget Preparation: The budget preparation process notionally follows a top-down procedure but is fragmented. The DEF sets the overall fiscal strategy and planning targets for the budget balances and debts of the general government and its sub-sectors, and an indication of maximum resources for an unchanged policy scenario. The composition of the balance between revenues and expenditures can however be modified later in the so-called Update of the DEF which is approved by the parliament at the start of the budget session. As from 2010, the Financial Law was replaced by a Stability Law. However, this did not modify the possibility given to any other law to increase spending, provided it is financed by tax increases or cuts in spending affecting other budget items. Many policy decisions with fiscal implications may therefore still be taken outside the regular budget process.

Parliamentary Approval: Planning targets are endorsed by the parliament at an early stage of the preparation of the annual budget. Parliament cannot change the targets during parliamentary approval but, when discussing the Stability Law, it can increase expenditure or reduce revenues provided that it identifies compensatory funding.

Budget Execution Controls: Budget execution controls have been more focused on the legal compliance of expenditures than on the achievement of the government's fiscal targets. Recent legislative reforms have the potential to improve aggregate expenditure control. Law 196 of 2009 established programs as the basic unit of expenditure authorization. The basic units of expenditure management and control remain the budget "chapters" which have been reduced in number from about 6000 lines in 2008 to about 4500 in 2013. It also reduced the complexity of the expenditure control system by initiating a progressive re-enforcement of cash-based appropriations (Law 196/2009 as amended by Law 243/2012). The legislative changes introduced by Law 39/2011 also prohibited the spending of windfall revenues during the year. Since 2011, carried-over balances

expire after two years for both operational expenditure and capital expenditure, but there are no limits for the draw-down of these balances.

Recommendations

The effectiveness of fiscal policymaking in Italy could be further enhanced by:

- Strengthen multi-year budget discipline by fixing a multi-year expenditure ceiling covering the bulk of the central government, tightening controls on carryovers, and providing a transparent reconciliation of changes to multi-year expenditure projections between budgets.
- Reinforce the independence and impact of the PBO by clarifying the selection criteria for members, integrating PBO interventions into the budget cycle, reinforcing the role of the chair of the PBO, ensuring coordination with other independent bodies, and providing the PBO with security of funding.
- Enhance expenditure control and fiscal risk management by establishing the supremacy of the annual budget law over other legislation, reinforcing cash-based controls, publishing a comprehensive fiscal risk statement, and expanding the coverage of fiscal reports.

JAPAN

Summary Evaluation

Japan has a traditional incremental, input-based, annual budget process. Fiscal reporting for the central government is comprehensive, with reports audited by the independent Board of Audit and published eight months after the end of the financial year. The government articulates short- to long-term objectives for fiscal policy and prepares medium-term forecasts of all major fiscal aggregates. These seem to be based, however, more on macroeconomic assumptions than on actual forecasts. Budget preparation is not guided by a fiscal framework with concrete measures. Mid-year budget updates have been re-introduced, but the extent of detail is limited. The Cabinet Office produces long-term economic and fiscal projections. Disclosure of fiscal risk, including of various economic scenarios and contingent liabilities, is comprehensive. Expenditure reviews lack clear savings targets and are not aligned with the government's agenda. Budget unity is incomplete, as the budget is divided into several accounts and government-affiliated agencies, whose budgets are presented in separate documents.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Macroeconomic and Fiscal Forecasting	Re-introduction of a mid-year budget update.
Independent Fiscal Agency	Revival of the Council on Economic and Fiscal Policy, which, although not an independent fiscal agency, may strengthen quality and objectivity in fiscal planning.

Fiscal Reporting: Fiscal reporting is comprehensive and detailed. The consolidated financial statements prepared by the Ministry of Finance cover the full range of central government activities. Budget execution reports for the central government are audited by the independent Board of Audit, approved by the Diet, and published eight months after the end of the financial year. While a comprehensive central government balance sheet is also published, delays of around 15 months in its production limit its usefulness as an input into policy-making. Fiscal statistics for the general government are produced by the Economic and Social Research Institute (ESRI), a part of the Cabinet Office, in line with international standards. The ESRI also produces financial statistics for public corporations in the context of national accounts, but these are not consolidated with the general government. GFS data are only reported on an annual basis, with a lag of up to two years.

Macroeconomic and Fiscal Forecasting: Forecasts of all major fiscal aggregates, including revenues, expenditures, balance, and debt for the central government and their underlying economic assumptions are published. The baseline scenario used for budget preparation and the

medium-term fiscal framework is more a set of assumptions than an actual forecast, and has in the past tended to be optimistic. Mid-year budget updates have been re-introduced, but the extent of detail is limited. The Cabinet Office does produce real long-term economic and fiscal projections with two scenarios, which are included alongside the budget. The long-term projections span 11 to 30 years, and take account of factors such as the economic growth rate, unemployment trends, fiscal-gap projections, effects of significant policy reforms, health care costs, demographic changes, and civil servant pension obligations. There is no link to the content of the annual budget, however.

Fiscal Risk: Accounting and reporting of contingent liabilities is comprehensive, detailed, and quantified to a large degree. The approval of the Diet is required for new government guarantees, loss-compensation contracts, and international commitments. Alternative macroeconomic scenarios are discussed in connection with the budget documents and the implications for the main fiscal aggregates are quantified and presented. The Ministry of Finance publishes an annual Debt Management Report, but it assesses only the financial risks arising from the debt portfolio.

Independent Fiscal Agency: The Fiscal System Council is an advisory body to the Minister of Finance on fiscal policy issues. It has provided constructive proposals for fiscal consolidation, including drastic expenditure cuts. A recent development is that the current government resurrected the Council on Economic and Fiscal Policy (CEFP), which in the past played an important role in advising on fiscal consolidation. The Cabinet Office which functions as secretariat of the CEFP has been made responsible for preparing a medium-term fiscal/budgetary framework. The CEFP is part of the executive. It includes the prime minister, four ministers, the chief cabinet secretary, and the governor of Bank of Japan, in addition to two academic experts and two business leaders.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reform since 2010
Fiscal Objectives and Rules	Introduction of a rule for the primary balance of the General Account of the central government.
Medium-term Fiscal Framework (MTFF)	Introduction of a basic MTFF in 2013.

Fiscal Objectives and Rules: In recent years, the government has set—and revised—its short- to long-term objectives for debt and the deficit through Cabinet decisions. These decisions are, however, not based on a rule-based framework that integrates both sustainability and stability concerns in a balanced way. The Fiscal Management Strategy (FMS), initially adopted in 2010 and broadly reaffirmed in subsequent years, had as objectives to achieve a primary budget surplus for the central government and local governments by FY2020 and to put debt on a downward trajectory from FY2021. It also mandated an aggregate expenditure ceiling that held spending fixed, in nominal terms, over a three-year period, excluding recovery and reconstruction-related spending.

The expenditure ceiling was not formally breached in the 2010-13 period, but exceptions were made for earthquake recovery and stimulus purposes. The FMS also established a number of principles for fiscal management, including a budget-neutrality rule that, whenever policies that increase expenditure or reduce revenue are introduced, countervailing permanent reductions in expenditures or revenue-raising measures are required. The Medium-term Fiscal Plan (MTFP), approved by Cabinet in August 2013, replaced the FMS. It retains the long-term objectives in the FMS, but it substitutes the expenditure ceiling with a rule that the primary balance of the General Account of the central government should improve by at least JPY 4 trillion in FY2014 and again in FY2015.¹⁰ In addition, the MTFP calls for expenditure to be reduced, and revenue increased, as percentages of GDP.

Medium-term Budget Framework: The budget is formulated under the single-year budget principle stipulated by the Public Finance Act, and no law requires the presentation of a medium-term fiscal framework (MTFF). A basic MTFF was introduced in August 2013, however, wherein expenditure is divided into five broad economic categories (debt service, local government transfers, social security, other current expenditure, and investment). Expenditure ceilings for each category are set only for one-year ahead. Fiscal forecasts do not systematically identify the impact of new versus ongoing policy.

Performance Orientation of the Budget: The budget has been presented using a program classification since 2008, and programs are the basis for legislative appropriation of expenditure. The impact of performance measures on budget allocation, however, is limited. Evaluations of program performance are conducted and published primarily by line ministries themselves, while cross-ministerial programs are evaluated by the Ministry of Internal Affairs and Communications. These evaluations are linked to the budget cycle and are studied by the Ministry of Finance during the budget preparation process. Also, program evaluations do not require savings options to be discussed. Program evaluations carried out by the independent Board of Audit focus on legal compliance, and on efficiency and effectiveness in project implementation, rather than on priority and relevance for the government's agenda.

Intergovernmental Financial Relations: The financial relationship between the central and local governments, including matters regarding the budget process and the division of roles in terms of expenditure and revenue, is regulated through a number of laws. The FMS introduced, and the MTFP retains, the principle that both the central and local governments are to take measures for fiscal consolidation in mutual cooperation. In addition, there is the principle that the central

¹⁰ The General Account represents general expenditure of the central government. Special Accounts are set up to carry out projects and administer and manage specific funds or revenues. Reforms of the Special Accounts system are underway, in order to promote more efficiency and transparency in fiscal management. The number of Special Accounts has been reduced from 31 to 17 in recent years, but total expenditure through Special Accounts is still over four times that of expenditure through the General Account. In 2014, the authorities will further reduce the number of Special Accounts from 17 to 14, excluding the Special Account for Reconstruction from the Great East Japan Earthquake.

government not transfer expenditure burdens to local governments or hinder their autonomy. The fiscal objectives and the rule for the primary balance are inclusive of spending by local governments.

C. Implementing the Adjustment Strategy

Budget Unity: All revenues and expenditures are incorporated into the annual budget, but budget unity is undermined by separating the budget into the General Account, Special Accounts, and government-affiliated agencies, which are presented in separate documents. There are no permanent appropriations. Although no law requires the government to include a statement of tax expenditures in the budget, the Ministry of Finance every year provides a report on tax expenditures to the Diet. The report states the annual revenue loss attributable to each specific tax expenditure over a multi-year period, including the budget year. In addition, tax expenditures, when authorized, have sunset clauses.

Top-down Budget Preparation: The process for preparing the annual budget follows a top-down procedure that is generally well respected. The Cabinet Office is given a strong role in budget formulation, including responsibility for issuing the basic principles of budget formulation to be followed by the Ministry of Finance and line ministries. They are decided by Cabinet, after having been discussed in the CEFP. There is no legal constraint on the number of supplementary budgets. Frequent recourse in recent years to expansionary supplementary budgets in order to stimulate sluggish demand has compromised integrity of both the fiscal rule and the annual budget as tools for enforcing overall fiscal discipline.

Parliamentary Approval: The governing parties are consulted during preparation of the medium-term framework and the annual budget. There is no separate strategic budget framework debate, however, early in the year before detailed budget submissions are prepared; the Diet approves the budget aggregates and detailed appropriations at the same time. The time available for legislative debate of the government's budget proposal is typically two months. Notwithstanding that the legal framework for PFM does not impose any formal limitation on the legislature's power to amend the government's budget proposal, there are in practice strong self-imposed constraints, with the result that substantive amendments to the budget proposal by the Diet are rare.

Budget Execution Controls: The approved budget represents a ceiling on expenditure, and the government is authorized to spend less if desired. Line ministers may reassign funds within their responsibility up to certain thresholds with prior consent from the Ministry of Finance, but ex post approval of the Diet is needed. An increase in spending beyond the voted budget requires the Diet's approval ex ante in the case of investment spending, but ex post in the case of mandatory or discretionary operational spending. Overspending requires a supplementary budget, but there is no presumption that the additional spending will be offset. Clear rules and procedures for access to the government's general contingency reserve are in place; there are no rules for its relative size.

Carryover of unspent appropriations is permitted only for a subset of expenditure items that are specified in the budget documents. In other instances, carryover to the following year is permitted

with the approval of the Ministry of Finance, subject to an ex ante resolution by the Diet, if the carryover is attributable to the nature of the expenditure or is due to reasons unforeseen when the budget was initially approved. The Diet's approval is required for all multi-year expenditure commitments, which are limited in duration to two or five years, depending on the type of expenditure.

Recommendations

- Define a fiscal rule framework that will ensure an appropriate balance between fiscal sustainability and stability concerns over the medium-term, and possibly, in due course enshrine this framework in law. The present regime of exceptions to fiscal objectives provides flexibility to budget management but insufficient assurances for fiscal consolidation. A new framework should encompass all supplementary budgets, and allow for flexibility through accommodation of automatic stabilizers and appropriate escape clauses.
- Develop the MTFF gradually into a more detailed medium-term budget framework (MTBF), including expenditure ceilings by line ministry and possibly by major programs. The framework should reflect Cabinet decision-making on expenditure and revenue measures over the medium-term.
- Base the MTBF on prudent macroeconomic forecasts rather than on optimistic macroeconomic assumptions. Macroeconomic forecasts should be compared in the budget with forecasts of other institutions and/or commercial banks. Forecast errors of previous years should also be reported and explained.
- Limit the conditions under which supplementary budgets can be used so as not to undermine the integrity of the fiscal rule framework and the annual budget as tools for enforcing overall fiscal discipline.
- Transform the Fiscal System Council into an independent, impartial body to monitor and evaluate fiscal performance both ex post and ex ante.
- Reform expenditure review processes to include independent assessment of program performance, and enforce presentation of savings options.

KOREA

Summary Evaluation

Korea has made good progress in implementing public finance reforms over the last fifteen years. Its macroeconomic and fiscal forecasting provides a sound policy framework for budgeting. Top-down budgeting is well established, providing clear policy guidance from the center for line ministries' budget development. Performance budgeting informs budget choices and program management. The independent fiscal agency, the National Assembly Budget Office (NABO), strengthens the process by developing independent macroeconomic forecasts and analyzing executive budget proposals and pending legislation. The Board of Audit and Inspection (BAI) provides an external review ensuring the accuracy of fiscal reports and assessing the effectiveness of government performance. Fiscal risks, however, are not well-defined nor quantified. Significant portions of government spending occur through special accounts, extra-budgetary funds, and dedicated revenues, and almost half of all central government spending in FY 2013 was made through mandatory programs that are not subject to annual review or appropriation.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Fiscal Reporting	Accrual accounting standards were adopted effective 2011; GFSM 2001 reporting was initiated, effective 2012.
Fiscal Risk	The 41 largest State-Owned Enterprises (SOEs) were required to submit five-year financial plans to the Parliament, effective 2012.

Fiscal Reporting: Beginning in 2011, financial statements were prepared on the basis of full accruals, although budgeting and budget reporting remains on a cash basis. Financial statements are audited, and published within six months of the end of the fiscal year by the Board of Audit and Inspection (BAI), which is a constitutionally independent body that reports to the President and the National Assembly (NA). Financial statements cover the general government (the consolidated budget was expanded in 2006 to include local governments) and include a comprehensive balance sheet. Two sets of government finance statistics are prepared, one using national definitions and the other using international standards. The government shifted from GFSM 1986 to GFSM 2001, with the first set of financial reports based on the reformed framework released in 2012. However, timeliness of these data does not yet comply with the Special Data Distribution Standards (SDDS), mainly due to the lack of timeliness of local government source data.

Macroeconomic and Fiscal Forecasting: Korea's budget is based on the National Financial Management Plan (NFMP), which was established through the National Finance Act of 2006. It contains comprehensive macroeconomic forecasts and a description of the major economic variables underpinning the forecasts. It is prepared by the Ministry of Strategy and Finance (MoSF). A mid-year budget update is not published. Ex post comparisons of forecasts and actual outturns are not systematically prepared. The NABO is preparing long-term fiscal projections to capture issues related to aging population, but is not yet publishing this analysis.

Fiscal Risk: The budget does not contain a fiscal risk statement or a systematic description or quantification of major risks, such as contingent liabilities or future pension liabilities. Fiscal risks related to macroeconomic uncertainty are not well developed, though some assessment of alternative economic assumptions is provided. While fiscal risks arising from SOEs are not presented in budget documents, effective 2012 the largest 41 SOEs are required to prepare for the NA five-year financial plans on which monitoring of those firms is based. Locally-controlled SOEs, whose debt level has recently grown rapidly, are not monitored. Starting 2014, the authorities plan to compile public sector statistics as a first step to address this issue.

Independent Fiscal Agency: The NABO was established in 2003 to support the NA in analyzing and evaluating issues related to the national budget. The office is independent from the executive. The NABO reviews the macroeconomic and fiscal forecast of the executive, and provides its assessment of the government's policy in an annual report, the most recent being the Economic Outlook and Fiscal Analysis: 2013 and the Medium Term. It conducts research and analyses of budget bills, settlement accounts, fund operations, and cost estimates for legislation with budgetary effects. Finally, it evaluates major government programs and analyzes medium to long-term fiscal prospects.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area

Type of Institution	Reform since 2010
Performance Orientation of the Budget	In 2010, the government initiated a policy to cut the budgets of ineffective programs, as assessed by a performance assessment tool, by at least 10 percent.

Fiscal Objectives and Rules: In the 2011 NFMP, Korea introduced a fiscal objective that would keep the growth rate for expenditures 2-3 percent lower than that for revenues. However, the NFMP, and hence the fiscal objective, is not enacted in law. Binding Pay-As-You-Go and other expenditure growth rules have been proposed by the executive but have not yet been agreed by the NA. The National Finance Act requires the government to submit to the NA reports comparing actual results with the previous year's NFMP and Debt Management Plan.

Medium-term Budget Framework: The National Finance Act of 2006 requires that a five-year budget framework be submitted to the NA. The NFMP is a rolling plan, which permits annual revisions to any of the five years in the plan. The budget is aligned to year one of the NFMP but is separate from it. The NFMP presents resource allocation strategies for twelve sectors comprising the entire budget, and identifies changes between the prior year and the budget year. The composition of these changes in terms of baseline and new policies is not consistently presented. The impact of key revenue policies are shown in separate documents.

Performance Orientation of the Budget: In 2003, Korea began a renewed effort to introduce performance budgeting. The focus has been on developing and integrating performance budgeting and management more fully. Major elements of that reform have been: (i) an in-depth program evaluation by creating every year an evaluation panel for each of a selection of ten programs to collect data, conduct surveys, analyze data and write reports on the relevance, efficiency and effectiveness of programs; (ii) improvements of on-going program assessments by conducting self-assessments of budgetary programs of one-third of public programs annually; and (iii) integrating performance into budgeting by receiving feedback on budgetary programs that do not meet their goals. Unique in the Korean performance assessment tool is the direct linkage between assessment results and savings targets. There have been several rules used by MoSF, the latest being an automatic 10 percent reduction in expenditure if a program is found to be ineffective.

Intergovernmental Financial Relations: Central government provides about 80 percent of sub-national government financial resources. Consequently, the fiscal policy of the central government determines, in effect, the fiscal policy of the general government. The public consultation process for establishing central government spending priorities includes representatives of sub-national governments. Local governments are subject to a balanced budget rule for current expenditure. Local government borrowing is monitored by the central government.

C. Implementing the Adjustment Strategy

Table 3. Main Reforms in this Area

Type of Institution	Reform since 2010
Budget Unity	A tax expenditure budget was prepared for the first time in 2011.

Budget Unity: Information is provided on most government economic and fiscal activity through either the budget or other reports to the NA. In 2013, 53 percent of the budget was annually appropriated; the remaining 47 percent of central government spending was authorized by permanent legislation, without requiring annual appropriations, for purposes such as welfare, grants to sub-national governments, public pensions, senior care, social insurance, and child care for the handicapped. As of 2013, there are 64 extra-budgetary funds divided among four categories: Social Security Funds, Financial Funds, Account Funds and Project Funds. SOEs are substantial, with the largest seven accounting for aggregate debt equal to 25 percent of GDP. Beginning in 2012, multi-

year tax expenditure reports were introduced, which among other things present tax expenditures by functional classification. No control is exercised over specific amounts.

Top-down Budget Preparation: The budget is prepared in a two-step process. The NFMP establishes fiscal aggregate targets, as well as policy priorities and spending limits for each ministry. Line ministries generally adhere to the spending limits given to them during budget preparation, with excesses typically within 5 percent of the limit. While a significant portion of government spending is channeled through special funds, extra-budgetary funds, and earmarking of revenues, aggregate and ministerial expenditure constraints incorporate these expenditure channels.

Parliamentary Approval: Article 54 of the Constitution gives authority to the NA to review and amend the executive's proposed budget. However, Article 57 of the Constitution states that the NA cannot increase spending for any program in the budget without the executive's consent, though it may decrease spending at its discretion. Only the executive can introduce budget bills. Consequently, the Parliamentary budget process is characterized by extensive negotiation with the executive. The NA typically adjusts the total budget by less than 1 percent, and in the majority of years since 1995 this adjustment has been to reduce total spending. The NA budget process is dominated by the Special Committee on Budget and Accounts (SCBA), which, with its responsibility for fiscal aggregates, carefully screens spending proposals submitted by the 16 sectoral committees. The NA considers the NFMP, but does not formally approve it. The NA is taking an increasing role in reviewing government performance, both in budget formulation and in reviewing the BAI audit reports.

Budget Execution Controls: Once the budget is approved by the NA, the MoSF issues a quarterly allocation of the approved budget by organization and program. Line ministries then develop monthly expenditure ceilings within the allocation. Budgets must be executed within the approved allocations; expenditure controls are enforced through the Digital Budget and Accounting System which became operational in 2007. Adjustments among programs must be approved by the NA; adjustments among line items are approved by the MoSF. The budget contains a contingency of 1 percent of total budget expenditures but the system for allocating contingency funds is not rule-based. Article 23 of the National Finance Act of 2006 permits disbursing funds over a period of up to five years for construction projects and other purposes that require more than one year to complete, based on an initial appropriation approved by the NA. The MoSF may withhold expenditures or budgetary allocations at any time to protect the fiscal balance and in the interest of efficient public spending.

Recommendations

The following institutional reforms could be pursued to strengthen fiscal management:

- Publish a mid-year budget update that reviews macroeconomic assumptions, expenditures and revenues at least by major categories of spending and revenues for the budget year and updates the projections for the medium term.

- Report on the accuracy of macroeconomic and fiscal projections in the budget documents on a regular basis and present analysis of forecast errors.
- Prepare a comprehensive fiscal risk statement and publish it as part of the NFMP, including analyses of contingent liabilities and future pension liabilities, and the fiscal impact of alternative macroeconomic assumptions.
- Improve monitoring of SOEs to anticipate contingent liabilities and improve the understanding of the sustainability of government sponsored borrowing.
- Implement periodic long-term budget projections, at least once every three years, to better understand the fiscal implications of aging and other fiscal risks.
- Reduce the number, and size, of special funds, extra-budgetary funds, and the earmarking of revenues.

MEXICO

Summary Evaluation

Since 2006, Mexico has pursued a multi-pronged fiscal reform program. They have focused primarily on fiscal rules, fiscal reporting, and enhancing performance management and budgeting. A balanced budget rule, with an escape clause, and an improved means for smoothing expenditure by managing oil-related windfalls has been put in place. Fiscal reporting is being enhanced through the adoption of modified accrual accounting standards and the harmonization of budget classifications across all levels of government, although implementation is suffering from delays. Improved fiscal reporting and performance evaluation measures are being introduced at the sub-national government level. Some weaknesses in Mexico's public financial management (PFM) system remain, notably in the area of medium-term budgeting, fiscal risk analysis, mid-year budget review, and independent assessment of macro-fiscal forecasts. Specifically, Mexico presents budget policy in the context of an aggregate medium-term outlook, but has not yet expanded its medium-term focus to the level of sector, ministry, or major programs. There is no mid-year budget review and there are still gaps in the government's fiscal risk analysis. In 2013, the new government proposed a fiscal reform package, which includes a fiscal rule framework that incorporates a target for a broader deficit measure, covering most of the public sector, and an expenditure growth rule that should help limit the pro-cyclicality of the balanced budget rule. Stabilization funds are being simplified to strengthen their ability to save revenue windfalls.

A. Understanding the Fiscal Challenge

Table 1. Main Reforms in this Area

Type of Institution	Reform since 2010
Fiscal Reporting	The introduction of modified accrual accounting and harmonized budget classifications at all levels of government is in progress.

Fiscal Reporting: The Cuenta de la Hacienda Pública Federal, or Federal Public Financial Accounts, are prepared by the Ministry of Finance and Public Credit (MoFPC). The public accounts consolidate all central government budget entities and state-owned enterprises (SOEs) under direct government control, including PEMEX, the state oil company, and CFE, the state electricity company. It includes a comprehensive balance sheet. The 2008 Government Accounting Law requires that all levels of government (federal, state, and municipality) move in a phased manner to accrual accounting standards. The public accounts are audited by the Federal Supreme Audit Office (ASF), an independent audit agency that reports to Congress. The public accounts are submitted by the government to the ASF and the lower house of Congress not later than four months after the close of the fiscal year. The ASF submits its opinion to the lower house of Congress only by February 20 of

the following year, or 14 months following the end of the fiscal year. Audits of individual budget institutions are conducted selectively based on an assessment of risk. In addition to the public accounts, the MoFPC prepares internationally comparable government finance statistics on a monthly, but not annual, basis according to GFSM 1986. It also publishes fiscal statistics that follow national reporting concepts covering central government and principal SOEs but not sub-national governments.

Macroeconomic and Fiscal Forecasting: The medium-term macroeconomic and fiscal framework, submitted to Congress each September as part of the Paquete Económico, is called the “General Economic Policy Criteria for the Tax Law and Expenditure Budget” (hereafter called the Economic Report), which provides a comprehensive overview of the economy and its impact on fiscal policy. The Economic Report is prepared by the MoFPC. The assumptions in the macroeconomic forecast are stated within the Economic Report and include inflation, oil prices and production, interest rates, financial sector conditions, economic conditions in major trading partners, and the exchange rate. The effect of macroeconomic conditions on fiscal revenue is covered as well. The fiscal forecasts extend to five years beyond the budget year under discussion. Forecasts are also included in the Pre-Budget report, issued in April of each year. Forecasts are updated in quarterly reports to Congress, which provide a basis for ex post analyses of previous forecasts. There are no ex ante comparisons with other forecasting institutions of the macroeconomic assumptions. There is no formal mid-year budget review.

Fiscal Risk: The Economic Report includes discussion of fiscal risks caused by short-term macroeconomic fluctuations (GDP growth, price of oil, interest rates and the exchange rate), and long-term risks and contingencies (demographics, health and pensions, development bank credit risk, deposit insurance, SOE losses, and natural disasters). This discussion does not cover certain specific risks such as legal actions, international treaties, financial assets, physical assets, or public-private partnerships. Congress must approve increases in net new federal borrowing annually. While states can borrow domestically on their own initiative, they cannot borrow externally or in foreign currency.

Independent Fiscal Agency: The Center for Public Finance Studies, created in 1988, is in the Mexican Chamber of Deputies and is the legislative branch’s center for fiscal studies. It cannot be considered a fully functioning fiscal council such as have been developed in other OECD countries in recent years. The Center provides mostly descriptive reviews of the executive’s reports on budget execution and public accounts, the implementation of the National Development Plan, and assesses the fiscal implications of proposed laws and initiatives. The Center provides a limited assessment to parliamentarians on the assumptions underlying the forecasts included in the Economic Report. Even though it has the mandate to do so, it does not produce its own forecasts nor does it perform an ex post comparison of the government’s forecasts or ex post evaluation of fiscal policy.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reform since 2010
Fiscal Rules	Adoption by law of a balanced budget rule (with an escape clause) that was modified in 2013 to include a target on the broader fiscal measure of public sector borrowing requirements and to limit current spending growth by introducing a cap on real growth in current expenditure. A new approach to saving oil-related revenue windfalls is being developed with the secondary laws of the energy reform.
Performance Orientation of the Budget	Significant expansion of indicators, monitoring and evaluation relating to performance of budget programs and management.
Intergovernmental Financial Reforms	Giving more (taxing) responsibility to sub-national government and improving oversight through improved government accounting, strengthening audit capacity, and establishing performance indicators and evaluations for transfers to sub-national government.

Fiscal Objectives and Rules: Mexico's balanced budget rule, authorized in the 2006 Budget and Fiscal Responsibility Law (BFRL), applies to the federal public sector, including the central government, social security, and public enterprises. In 2008, the BFRL was modified to exclude investment expenditure of the national oil company, PEMEX, with the intent of promoting investment in the oil sector. The balanced budget rule has an escape clause that allows deficits under exceptional circumstances. The escape clause was used extensively in the aftermath of the global financial crisis (in 2010, 2011, 2012 and 2013). The public accounts annually, certified by the ASF, verify compliance with the rule. In 2012, oil revenue constituted approximately one-third of government revenue. The BFRL has helped stabilize the fiscal effects of volatile oil prices by defining windfall revenue and its allocation. The BFRL established a formula-based reference price for oil when forecasting oil-related revenue. Windfall oil revenue is used first to offset any revenue shortfalls below the budget forecast and to compensate for additional, uncontrollable costs of items such as interest payments, revenue sharing and natural disasters. Remaining money is distributed among several funds, including the Oil Revenue Stabilization Fund, created in 2000. In 2013, the government proposed a modification to the balanced budget rule to cap the real growth in current primary spending, excluding several items (covering about 50 percent of total budgetary spending) when growth is above trend, while retaining an escape clause for exceptional circumstances. This should reduce pro-cyclical spending. The balance under the balanced budget rule was broadened to cover a wider definition of the public sector.

Medium-term Budget Framework: Rolling medium-term estimates are included in budget documents for five years beyond the budget year, and include oil and non-oil related revenue; and expenditure for personnel services, pensions, subsidies and transfers, and capital expenditure. Estimates of transfers to sub-national governments and payments for social security and health care are made as a percent of GDP. The estimates are not part of a medium-term expenditure framework, and are thus not binding. Medium-term estimates of total net debt are also provided.

Performance Orientation of the Budget: Over the past decade, Mexico has worked to improve public sector efficiency and effectiveness, and to enhance accountability, through various forms of performance measurement. The latest requirements were established by the 2006 BFRL and the 2007 Integral Fiscal Reform (IFR), which are implemented primarily through the Sistema de Evaluación del Desempeño, or SED (Performance Evaluation System). SED has two sets of performance indicators, monitoring systems, and evaluation procedures, one for budget programs and another for management processes and public services. The budget is coded using three major classifications: program (function), organization, and economic. Appropriations are made by a mix of programs and organizations. The program structure used in the budget is aligned with that of the National Development Plan; goals, objectives and indicators are shared between the budget and planning systems. The Annual Evaluation Program sets out the programs that will be evaluated. The National Council for the Evaluation of Social Development Policy (CONEVAL) is responsible for evaluating social programs and the MoFPC for evaluating all other programs.

Intergovernmental Financial Relations: Sub-national governments are highly dependent on federal government transfers, which account for approximately 90 percent of sub-national financial resources. While there is no explicit mechanism to coordinate sub-national federal fiscal policy, much coordination occurs indirectly through this financial dependence. Medium-term fiscal forecasts in the Economic Report do not include local sources of sub-national revenue. Efforts are being made to simultaneously give more responsibility to sub-national government and improve oversight. More taxing power has been given to sub-national governments to raise their own funds. The 2008 Government Accounting Law, as amended in 2012, increased oversight of federal funds at the subnational level by harmonizing accounting and budget classifications across all levels of government. Other reforms include strengthening sub-national governments' audit capability, establishing indicators to measure the results of federal financial transfers, and conducting regular performance evaluations that must be made available to the public.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Budget Execution Controls	A new government financial management information system, SIDAFF is being designed.

Budget Unity: All major federal government expenditures, excluding social security, trust fund spending and transfers to sub-national governments, are appropriated annually. A detailed annual report on tax expenditure is prepared, but the size of tax expenditures is not subject to prior approval or control.

Top-down Budget Preparation: Mexico's budget system is driven by the balanced budget rule, which places a cap on total annual spending, and on expenditure ceilings issued for each ministry. The limits are established for the year ahead; medium-term forecasts are not binding. Expenditure caps are effective in part because a majority of appropriations are made annually. For example, while some revenue is earmarked for certain expenditures, these cases do not constitute a significant proportion of revenue. In addition, permanent appropriations, which do not require annual renewal, are not a significant portion of total annual expenditure.

Parliamentary Approval: Article 74, Part IV of the Constitution gives Congress the authority to examine, discuss, and approve the budget. It is a two-stage process, the revenue law is approved by Congress on October 31 and the budget spending proposal is approved by the lower chamber on November 15. However, Congressional authority is not unlimited. It is subject to the balanced budget rule and the executive's fiscal forecasts, and thus it cannot increase the overall budget balance proposed by the executive. While Congress is given the Pre-Budget report for review, it does not approve the document and thus does not have a role in deciding fiscal policy before the detailed budget is submitted to Congress in September. Congress approves the budget in a timely manner by November 15. There is no provision for authorizing expenditure in the event of a budget not being passed in time.

Budget Execution Controls: The Federal Integrated Financial Management System (SIDAFF), used for controlling expenditure and expediting reporting is still in the process of being designed. Any increase in expenditure by budget Chapter (ministry) must be approved by the MoFPC, which must be offset by decreases in authorization to spend in other budget Chapters or from windfall revenue. The budget law designates what shifts in spending within Chapters and programs may be authorized by ministries internally and those that require external approval by the MoFPC. Unforeseen revenue shortfalls or additional expenditures are handled by withdrawals from the Oil Revenue Stabilization Fund or, if the Fund balance is insufficient, from a pre-determined list of expenditures to be reduced. Other important technical controls are in place, such as restrictions on carried-over appropriations while allowing for budgeting and control of contracts and projects crossing fiscal years.

Recommendations

The following institutional reforms could be pursued to strengthen fiscal management:

- Pursue the complete implementation of modified accrual accounting and harmonization of budget classifications across all layers of government.
- Broaden coverage of fiscal and public debt accounts to also include sub-national governments.

- Produce a mid-year budget review, providing updates on performance of the economy, the budget outlook, and the fiscal forecast over the medium-term.
- Expand multi-year estimates and government decision-making to provide a rolling, medium-term expenditure framework by sector, ministry, and major program.
- Broaden the analysis of fiscal risks by including risks caused by PPPs and physical and financial assets.
- The Center for Public Finance Studies should produce more in-depth analytical work and consider publishing an independent ex-ante review of the government's macroeconomic and fiscal forecasts, and an analytical ex-post review of the government's fiscal performance, including compliance with the fiscal rule. Over the medium-term it could consider, producing its own macro-fiscal forecasts.

RUSSIA

Summary Evaluation

Russia has actively developed its budget institutions over the past decade. Accounting, reporting and financial control for general government is well developed. However, fiscal reporting generally does not cover the large state-owned enterprise sector. There is scope to develop the framework for assessing various types of fiscal risks, and to formalize the independent evaluation of macro-economic and fiscal projections. Policy formulation is facilitated by a comprehensive fiscal policy framework supported by a strong multi-annual budget framework. A recent initiative to further develop performance-oriented budgeting is designed to help identify low-value expenditure areas. Implementation of the fiscal strategy is facilitated by an orderly budget preparation and parliamentary approval process, and strong controls during budget execution.

A. Understanding the Fiscal Challenge

Fiscal Reporting: Based on audited financial statements from first level budget holders, the Ministry of Finance submits an annual financial statement covering the Federal Budget to the Supreme Audit Institution (Schetnaya Palata) no later than June 1, i.e., within five months after the end of the fiscal year. The financial statement is audited, with an opinion as to whether the statement represents a true and fair view, and is submitted to parliament no later than September 1, i.e., within eight months. The financial statement includes a statement of operations, a balance sheet covering both financial and nonfinancial assets and a cash-flow statement. Together with the annual financial statement, the government also issues a consolidated budget execution report, covering extra-budgetary funds. The Federal Treasury issues financial statistics in accordance with GFSM 2001, covering general government. However, the annual financial statement and the financial statistics do not cover the aggregate state-owned enterprise sector and the consolidated public sector.

Macroeconomic and Fiscal Forecasting: The Ministry of Economic Development publishes three updates of medium-term macroeconomic forecasts: a limited update of a few parameters in May and full updates in September and December. The Ministry also publishes a long-term macroeconomic forecast, currently covering the period up until 2030, but this does not cover fiscal developments. In the President's Budget Directions, typically submitted to parliament in June, key medium-term fiscal aggregates are presented. The budget proposal, submitted to parliament no later than October 1, includes projections for revenue, expenditure, balance and debt for the upcoming year and the following two years at an aggregate level and broken down into sub-categories. While the Ministry of Economic Development regularly assesses the accuracy of macroeconomic forecasts, these assessments are not published.

Fiscal Risk: Government guarantees and credits require parliamentary approval, and are presented in the budget. The government's debt management policy, issued in a comprehensive document, provides an estimate of the stock of guarantees and an estimate of the cost of their servicing. The

debt management policy provides a comprehensive debt management strategy, but does not present the impact of alternative assumptions on the cost of debt service. While the Ministry of Economic Development prepares and publishes several macroeconomic scenarios, there is no estimate of the fiscal impact of the alternative assumptions. There is no published assessment of risks from the large state-owned enterprise sector.

Independent Fiscal Agency: There is no independent fiscal agency in Russia. However, the Accounts Chamber has a broad mandate, and assesses the government's compliance of its fiscal objectives. In addition, the Ministry of Economic Development engages a number of institutes such as the Economic Expert Group and the Academy of Science during the preparation of macroeconomic forecasts.

B. Developing a Credible Fiscal Adjustment Strategy

Table 1. Main Reforms in this Area	
Type of Institution	Reform since 2010
Fiscal Rule	A new oil-price-based fiscal rule went into effect in 2013.
Performance Budgeting	A new program budgeting model is being introduced starting in 2014.

Fiscal Objectives and Rules: Legislation mandating a new fiscal rule went into effect in 2013, capping federal government expenditure at the ex ante projection of non-oil and non-gas revenues, plus oil and gas revenues using a benchmark oil price, plus financing of 1 percent of GDP. The new rule replaces a suspended rule targeting a non-oil deficit of 4.7 percent of GDP. The new rule allows for the automatic stabilizers on the revenue side to operate without restriction, and without requiring expenditure adjustments. The rule also allows the surplus from oil and gas revenue to be used to cover shortfalls in privatization revenue. During a prolonged decline in the oil price, the benchmark price is reset to a three-year average, rather than a ten-year average. The rule has ability to address non-oil shocks by permitting the government to divert flow oil savings to cover non-oil revenue shortfalls.

Medium-term Budget Framework: The federal budget covers the upcoming year and the two following years, and provides a medium-term assessment at a detailed level for all budget parameters. The fiscal rule sets a ceiling on total federal expenditure, but this ceiling is updated annually with the revised oil revenue using the updated benchmark oil price, and the revised non-oil revenue forecast. Expenditure for the upcoming three years is presented according to 14 main functional areas and undistributed expenditure as given by the expenditure ceiling. While there is a discussion on how expenditure will evolve over this period, there is no reconciliation with changes from the previous year's budget. The budget includes an assessment of the revenue impact of tax proposals, but no analogous estimate of the impact of new expenditure policies.

Performance Orientation of the Budget: Expenditure is classified according to programs in the budget, but a detailed organizational and economic classification remains as the basis for parliamentary appropriations. Program objectives are defined for all main spending units, and they report back on their performance annually. These performance reports are consolidated by the Ministry of Economic Development. The government is reforming its program budgeting model in 2014 by identifying broad medium-term programs covering both the federal and regional (oblast) levels. The reform includes a requirement that the achievements and efficiency of each program is assessed each year. The Accounts Chamber has also been given a broader mandate to review program expenditure.

Intergovernmental Financial Relations: The budget contains medium-term forecasts for total general government expenditure, broken down by sub-sector. The maximum debt and deficit level for regional (oblast) and municipal governments are subject to fiscal rules set by the Budget Code. The Ministry of Finance monitors the actual fiscal performance and can impose sanctions if the fiscal rules are breached, including putting in place a temporary administration to bring finances back on track. In accordance with the Budget Code, the preparation of regional and municipal budgets has to be coordinated with the Ministry of Finance.

C. Implementing the Adjustment Strategy

Budget Unity: The budget and social security is comprehensive, covering more than 95 percent of central government expenditure. All spending is authorized annually by the federal budget, the social security budget or by regional or municipal budgets. The Budget discusses existing tax expenditures, but without a comprehensive quantification.

Top-down Budget Preparation: The budget preparation process is separated into two distinct phases. In April, the government approves a no-policy-change ministerial allocation based on an inflation adjustment of the previous year's budget. Following this, the room for new spending initiatives for each ministry is approved. Allocations generally do not change much during the continued budget preparation. There has been a successful reduction of ministries' and government agencies' off-budget revenues and expenditures. Supplementary budgets, while following the procedures of the Budget Code, have been sizable in recent years yet not increasing the non-oil deficit.

Parliamentary Approval: The Duma (lower house) approves in the first reading the main directions of fiscal policy, including medium-term tax and expenditure policies and a limit for the federal debt, together with budget aggregates of total revenue, expenditure and the budget balance. In subsequent readings, detailed appropriations within those budget aggregates are voted. Although parliament has the power to introduce amendments that change the balance, any changes that increase expenditure or the deficit of the Federal Budget require the approval of the government. The Budget Code contains detailed deadlines for the various approval stages by the Duma and Federal Council (upper house), and provisions for resolving disagreements, to ensure that the budget is adopted and signed into law by the start of the fiscal year.

Budget Execution Controls: There are limited possibilities to exceed individual appropriations, but any increase that leads to an increase in total expenditure has to be authorized through a supplementary budget. New spending initiatives always require a supplementary budget. Carry-overs for the investment fund are allowed, but only after approval by the Ministry of Finance. The budget includes a general reserve fund, which cannot exceed three percent of total expenditure, and a President's reserve fund, which cannot exceed one percent of total expenditure. In addition, the oil Reserve Fund, which serves as a macroeconomic stabilization fund, is targeted at 7 percent of GDP. The Budget Code authorizes the Minister of Finance to impose expenditure limits during the budget execution. Ministries are allowed to enter into multi-annual commitments within the limits of the multi-annual budget framework.

Recommendations

- Extend fiscal reporting to cover the aggregate state-owned enterprise sector.
- Include a comprehensive fiscal risk analysis in budget documentation.
- Supplement existing long-term macroeconomic projections with an assessment of long-term fiscal projections.
- Include an estimate of tax expenditures in budget documentation.
- Formalize the independent evaluation of the official macroeconomic and fiscal forecast.

SAUDI ARABIA

Summary Evaluation

The government currently provides highly aggregated information about fiscal developments and prospects and no information about fiscal risks, but work is in train to produce more detailed fiscal reports in line with international standards and information on the country's fiscal developments and risks are published in the annual IMF Article IV staff report. The Gulf Cooperation Council's Fiscal Code provides transparent, comprehensive, and stable objectives for fiscal policymaking. A medium-term plan is published only for investment expenditure but a more comprehensive medium-term budget framework is currently being developed starting with the 2014 budget. A Five-Year Development Plan sets objectives and targets for major sectors of the economy but these are not regularly evaluated or reviewed between plans. The budget covers the vast majority of central government revenue and expenditure and is prepared and approved by the Council of Ministers in a top-down manner. The legislature (Majlis Ash-Shura) does not approve the annual budget but does monitor its implementation through annual reports submitted by the government. Additional budget expenditures during the fiscal year require the approval of the Council of Ministers but not the presentation of a supplementary budget and have averaged 26 percent since 2006.

A. Understanding the Fiscal Challenge

Type of Institution	Reform since 2010
Fiscal Reporting and Government Accounting	A common chart of accounts and budget classification is currently under development in accordance with the IMF's Government Financial Statistics Manual 2001 (GFSM2001).

Fiscal Reporting: A common chart of accounts and budget classification is being developed in accordance with GFSM2001, together with the implementation of a new government financial management information system (GFMIS). However, publicly available fiscal data is still limited, although information on fiscal developments and risks are published in the annual IMF Article IV staff report. The Annual Statement about the National Budget publishes figures for aggregate central government revenue and expenditures, but there is no information on in-year budget developments. However, income statements and balance sheets are published for extra-budgetary investment and pension funds. The Saudi Arabian Monetary Agency publishes a monthly balance sheet of its foreign and domestic financial assets and liabilities. The Charter for Saudi Arabia's supreme audit institution (the General Audit Bureau or GAB) states that the GAB is independent. Its reports on budget execution are submitted directly to the King and Prime Minister and are not published. Fiscal statistics are produced on an annual basis for central government by the Ministry

of Finance rather than an independent statistics agency. The level of detail provided to the public is limited—expenditure is broken down into ten functional categories and revenue is split into oil and non-oil.

Macroeconomic and Fiscal Forecasting: The government produces but does not publish multi-year macroeconomic and fiscal forecasts, which are highly dependent on uncertain and volatile oil prices. The published forecasts focus on the year ahead, show total revenue and expenditure on the six main expenditure areas (education; health and social affairs; municipality services; infrastructure and transportation; water, agriculture, industry, and other economic resources; and specialized credit development institutions and government financing programs), and do not distinguish between existing and new policies. Although long-term economic projections are published on the Ministry of Economy and Planning’s website based on the Five-Year National Development Plans, these projections only provide summary data and are not updated regularly.¹¹

Fiscal Risk: Fiscal risk disclosure is minimal, although the government conducts internal analysis of the sensitivity of the fiscal aggregates to oil prices and volumes. The government also uses conservative assumptions for the oil price when preparing its macroeconomic and fiscal projections and maintains very large cash buffers (in excess of 90 per cent of GDP) to mitigate against any adverse oil-related shocks. There is no discussion or quantification of tax expenditures, though the tax code itself is relatively simple.

Fiscal Council: There are no independent fiscal agencies that prepare macro-fiscal projections or evaluate fiscal policies or performance.

B. Developing a Credible Fiscal Adjustment Strategy

Fiscal Objectives and Rules: The fiscal convergence criteria set out in the 2004 GCC Fiscal Code of Conduct apply to Saudi Arabia. These include a ceiling on the debt-to-GDP ratio of 60 percent for the central government and 70 percent for the general government. There is also a ceiling on the general government fiscal deficit of 3 percent of GDP in normal circumstances and 5 percent when oil prices are below target. GCC members’ performance against these criteria are reviewed at the quarterly GCC governors’ technical committee meetings and assessed at the annual GCC Ministers of Finance and Governors meeting. Fiscal outturns have remained well within these limits since they were established. As of the end of 2012, Saudi Arabia had general government debt of just 3.7 percent of GDP and surplus of 12.4 percent of GDP.¹² The Ministry of Finance continues to report on performance against the balance and debt criteria at the time of the budget announcement. Separate fiscal rules at the sub-national level are absent, but the size of this sector is small.

¹¹ The Ninth National Development plan (2010-14) is currently being implemented as part of the Long-Term Strategy for the Saudi Economy that was first announced in 2004: <http://www.mep.gov.sa/themes/GoldenCarpet/index.jsp>

¹² IMF 2013 Article IV Staff Report for Saudi Arabia.

Medium-term Budget Framework: While, the government does not have a comprehensive and detailed medium-term budget framework, due in part to the dominance of the volatile oil sector in the overall economy and fiscal accounts the Ministry of Finance is currently developing a more comprehensive medium-term budget framework with the 2014 budget including analysis of the impact of alternative fiscal policy scenarios. New expenditure requests by line ministries must be first articulated in the Five-Year National Development Plan before they can be approved. The annual budget also sets rolling three-year ceilings on public sector investments, which accounts for slightly less than 50 percent of total budget expenditure but comprehensive and detailed multi-year projections of expenditure by sector, ministry or project are currently not published. .

Performance Orientation of the Budget: The Development Plan sets five-year objectives and targets for major sectors of the economy. There is no regular public reporting or evaluation of expenditure performance between five-year plans. However, the Supreme Economic Council (SEC), chaired by the King, does review the reports prepared by each government body at the end of each year regarding their implementation of the Development Plan.

Intergovernmental Financial Relations: There is no published information on sub-national fiscal developments or prospects. There are also no separate fiscal rules at the sub-national level. However, local government is a very small part of the fiscal accounts.

C. Implementing the Adjustment Strategy

Budget Unity: Most central government revenue flows through the consolidated treasury single account and earmarking of revenue is limited to less than 10 percent of total expenditure. All major budgetary decisions are taken through the annual budget process.

Top-down Budget Preparation: The annual budget by the Ministry of Finance follows a top-down procedure in which the economic assumptions, fiscal policies, and expenditure ceilings are determined by the SEC prior to the preparation of the detailed draft budgets by individual agencies.

Parliamentary Approval: Saudi Arabia's appointed legislature (the Majlis Ash-Shura) has no fiscal mandate and does not scrutinize, amend, or approve the annual budget. However, the Majlis Ash-Shura does monitor the implementation of the budget through annual reports submitted by the government.

Budget Execution Controls: Actual spending has consistently exceeded budgeted amounts—by 26 percent on average since 2006.¹³ This has been due, in large part, to conservative assumptions

¹³ Source: IMF 2013 Article IV Staff Report.

regarding oil prices and revenues and subsequent consumption of oil revenue windfalls during budget execution. While the government is not required to publish a supplementary budget if expenditure exceeds appropriations during the year, any increase or decrease in budget items during the year must be approved by the Council of Ministers. The three-year rolling ceiling on the government investment program acts as a limit on future capital commitments by line ministries. Carry-over of expenditure from one year to the next is limited to certain projects and categories of expenditure. The annual budget includes an explicit contingency reserve and procedures for transfers from this reserve are set out in the annual budget decree.

Recommendations

- Complete the development of a chart of accounts and budget classification consistent with GFSM2001.
- Publish multi-year projections of macroeconomic developments, oil and non-oil revenue and the fiscal aggregates.
- Publish an assessment of fiscal risks, including the impact of alternative oil price scenarios for the fiscal position.
- Develop a more comprehensive medium-term budget framework, including with detailed multi-year projections for expenditure by sector, ministry and project.
- Develop the budget execution process with the aim of reducing the degree of over-spending compared to budget plans.

SOUTH AFRICA

Summary Evaluation

South Africa's fiscal reports and forecasts provide a comprehensive overview of the general government's financial position and medium-term prospects. Long-term fiscal projections have been prepared but not yet published. There is a quantified discussion of fiscal risks in the budget documentation but the fiscal implications of alternative macroeconomic scenarios are not presented. A new Parliamentary Budget Office was established in 2013 which, once fully operational, should enhance independent scrutiny of the budget and fiscal policy. In the 2011 Budget, the government published, for the first time, a set of qualitative principles to guide fiscal policy. These are supported by a rolling medium-term expenditure framework and comprehensive program and performance budgeting system at both national and sub-national level. The 2012 Budget introduced a main budget¹⁴ non-interest expenditure ceiling which applies to every year of the medium-term expenditure framework. The 1999 Public Financial Management Act (PFMA), 2009 Money Bills Amendment Procedures and Related Procedures Act (MBAPRPA) and annual Appropriation Acts provide a disciplined top-down framework for budget preparation though Parliamentary approval typically happens after the start of the financial year.

A. Understanding the Fiscal Challenge

Table 1. Main Reforms in this Area	
Type of Institution	Reform since 2010
Independent Fiscal Agency	A new Parliamentary Budget Office has been established to provide Parliament with independent scrutiny of the budget and fiscal policy.

Fiscal Reporting: Consolidated financial statements cover all central government ministries and agencies and all enterprises in which the government has a majority share. These statements are audited and published within six months of the end of the financial year. All national departments produce asset registers and the consolidated financial statements feature extensive notes on government's financial and nonfinancial assets and contingent liabilities including loans, finance leases, derivatives, employee benefits and other provisions. However, no consolidated government balance sheet is provided. The independent National Statistics Agency produces consolidated fiscal statistics for general government which includes central, provincial, local government and their non-commercial entities in line with GFSM 2001 standards.

¹⁴ The main budget consists of (i) appropriations for national departments and transfers to provinces, local government and public entities; and (ii) direct charges against the National Revenue Fund including the provincial equitable share, debt-service cost and the salaries of judges and representatives.

Macroeconomic and Fiscal Forecasting: South Africa’s medium-term macro economic and fiscal forecasts are published annually in the Budget Review in February. A midyear early indication of economic forecasts and fiscal aggregates in the upcoming budget is provided in the Medium-Term Budget Policy Statement (MTBPS) which is tabled in Parliament in October. Comparisons between projections and actual outturns, are included in the Budget Review, MTBPS, and the Adjusted Estimates of National Expenditure. The budget document provides outturns for the last three years, an estimate for the current financial year, and three-year forward projections. A long term fiscal report which provides 30-year projections of revenue and spending for key sectors has been developed, and substantially informed the 2013/14 Budget, but has not yet been published.

Fiscal Risk: The Medium-Term Budget Policy Statement includes a qualitative discussion of fiscal risks. Contingent liabilities in the form of guarantees to major SOEs and private sector, claims against government departments, public-private partnership obligations and employee benefits are quantified for the three-year period covered by the Budget Review. However Parliament does not explicitly approve these guarantees or other contingent liabilities incurred. There is no published evaluation of the fiscal implications of alternative medium-term macroeconomic scenarios. The legislation governing the finances of local government prohibits central government guarantee of local government debt and municipalities are required to borrow on the strength of their own balance sheets.

Independent Fiscal Agency: The Financial and Fiscal Commission (FFC) established under the Constitution comments on the division of revenue, broader fiscal policy and macroeconomic outlook of government. The Minister of Finance is legally required to table a memorandum accompanying the budget on how recommendations of the FFC have been taken into account in allocating the division of revenue. The 2009 MBAPRMA also established a Parliamentary Budget Office (PBO) with a remit to provide Parliament with independent scrutiny of the government’s fiscal policy, macroeconomic and fiscal projections, and budget. The first director was appointed in June 2013 but the office is not yet fully operational.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reform since 2010
Fiscal Objectives and Rules	The 2011 Budget introduced qualitative guidelines for fiscal policy over the medium-to-long-term. The 2012 Budget introduced a main budget non-interest expenditure ceiling.

Fiscal Objectives and Rules: The 2011 Budget introduced qualitative guidelines for fiscal policy over the medium-to-long-term based on principles that general government debt is sustainable, intergenerational equity is preserved and fiscal policy is countercyclical. However, these fiscal

objectives are not explicitly quantified and no time horizon is given for their realization. The Government does not currently report on their performance against these qualitative guidelines.

Medium-term Budget Framework: The Medium-Term Expenditure Framework (MTEF) provides detailed expenditure projections for the next three years for the central, provincial, and local government and all new budget priorities per sector are presented separately from existing policies over the medium term. The framework includes social security funds and public entities funded primarily from the fiscus. Expenditure financed from provincial and municipal own revenue is excluded. In the past, the MTEF did not constitute a binding framework and medium-term forecasts were adjusted in line with actual revenue. The 2013 budget maintains an aggregate non-interest expenditure ceiling established by the 2012 Budget. New and expanding programs were funded through reprioritization and savings within function groups and votes.

Performance Orientation: Each department's budget vote is divided according to purpose, programs and subprograms, and Parliament appropriates resources per department at the program level. Key performance indicators per department are provided for the medium term in the Estimates of National Expenditure document. Until recently, there were no regular expenditure reviews assessing the efficiency of and impact of programs. However, since 2012/13 the Department of Performance Monitoring and Evaluation (DPME) has conducted program evaluations, together with departments that aim to understand performance and identify ways to improve value for money. The results of evaluations are shared with relevant departments, tabled in Parliament and published on DPME's website. Joint evaluations conducted by National Treasury and DPME will be published in the 2014/15 fiscal year.

Intergovernmental Financial Relations: The principles for intergovernmental financial relations are enshrined in the Constitution of South Africa and provides for an equitable share of revenue to central government, provinces and municipalities. Revenue-sharing formulas and multi-year allocations per province and municipality are published with the budget in the annual Division of Revenue Act. The 2003 Municipal Finance Management Act (MFMA) requires municipalities to maintain an operating balance and includes mechanisms for enforcing compliance.

C. Implementing the Adjustment Strategy

Type of Institution	Reform since 2010
Budget Unity	A tax expenditure statement is included in Annexure C of the Budget Review and quantifies the tax proposals for the fiscal year.

Budget Unity: The appropriated budget covers more than 93 percent of central government expenditure, leaving out only debt service costs and other direct charges against the National Revenue Fund authorized by the PFMA. Since 2010, estimates of the revenue loss from tax

expenditures are provided in Appendix C of the Budget Review, but there is no limit placed on their size or growth.

Top-down Budgeting: The Government introduced a main budget non-interest expenditure ceiling in the 2012 Budget Review that covers all government departments and programs. Debt service costs and other direct charges against the National Revenue Fund are a first call on the budget. Typically, all major revenue and expenditure decisions are taken as part of the annual budget process and supplementary budgets are typically less than 1 percent of the approved budget. Supplementary adjustments are normally funded entirely from within the non-interest expenditure ceiling.

Parliamentary Approval: Parliament's authority to amend the budget is legislated in the 2009 MBAPRMA. The Act requires the Minister of Finance to submit a Medium-term Budget Policy Statement to Parliament at least three months prior to the tabling of the annual budget. Legislators are required to debate and approve the budget in a top-down sequence by first accepting or amending the fiscal framework and revenue proposals and later voting on the Division of Revenue and the Appropriations. Parliamentary amendments to the latter Bills must be affordable within the fiscal framework endorsed at the start of the process. While the budget is typically approved after the start of the financial year, the PFMA caps spending at 45 percent of the previous years' appropriation until the budget is passed.

Budget Execution Controls: Although the Minister of Finance is authorized to overspend the appropriations approved by Parliament by up to 2 percent in an emergency, this practice is seldom followed.¹⁵ Carry-over of unspent appropriation is limited to particular categories of expenditure and an overall limit set by the Minister of Finance. Multi-annual commitments for capital expenditure must be authorized through an annual Appropriation Act. A contingency fund of 1 percent of expenditure has traditionally been provided for unforeseen expenditures, but there are clear criteria for access and funding is regularized by an Adjustment Appropriation Act. While the Minister of Finance is authorized to withhold funds appropriated in the budget, this is typically only done where the funds have been transferred to another institution or earmarked for a particular purpose.

Recommendations

- Strengthening macro-fiscal forecasting by (i) publishing the long-term fiscal analysis; (ii) considering alternative macro-economic scenarios and their implications for the main fiscal aggregates ; and (iii) comparing actual macroeconomic data against MTEF forecasts.
- Implementing a numerical benchmark to guide existing fiscal policy.

¹⁵ The provision has only been utilized once in the past 20 years to pay for bus subsidies in 2007/08.

- Providing binding medium-term expenditure ceilings to contain non-interest spending within fiscal policy guidelines.
- Drawing together analysis of fiscal risks in a comprehensive fiscal risk statement.
- Submitting all SOE guarantee applications to Parliament for approval to strengthen oversight and limit exposure due to drawdowns.

TURKEY

Summary Evaluation

Turkey's fiscal reports are relatively comprehensive and detailed and have further improved in institutional coverage since 2010. Government publishes detailed, three-year macro and fiscal forecasts, but provide only a single, central scenario without long-term fiscal projections. The legislature approves limits on guarantees and on-lending. The budget contains information on public-private partnership contracts, but no comprehensive fiscal risk statement is prepared. There is no independent evaluation of the credibility of government's macro-fiscal forecasts or performance. The macro forecasts, along with public sector and general government balances, are published in the Medium Term Program (MTP) by the Ministry of Development (MoD), while expenditure ceilings for each of 194 central budget institutions on a multiyear basis (for the following three years) are published in the Medium-Term Fiscal Plan (MTFP) by the Ministry of Finance (MOF). However, fiscal policy focuses mainly on the year ahead and authorities respect overall balances rather than expenditure ceilings set in MTFP. A pilot process to introduce a greater performance orientation in the budget process was launched in some budget institutions in late 2004, but the budget is still presented and approved by line item. The budget is comprehensive and its preparation follows a disciplined, top-down process within the executive but is approved in a bottom-up manner by the legislature. There are relatively strong controls over budget execution as evidenced by the lack of supplementary budgets over the past ten years, however appropriations for personnel expenditure can be exceeded without parliamentary approval. These additional personnel expenditures were presented to the parliament as an ex post complementary appropriation in the final account laws.

A. Understanding the Fiscal Challenge

Table 1. Main Reforms in this Area

Type of Institution	Reforms since 2010
Fiscal Reporting	The institutional coverage of general government fiscal statistics has expanded to consolidate revolving funds and other self-financed entities.
Fiscal Risk	Since 2010, the MoD has been publishing information on the number and value of PPP projects by sector

Fiscal Reporting: The coverage, detail, and integrity of fiscal reporting in Turkey have steadily improved over the past decade. Fiscal statistics prepared by the Turkish Statistical Institute (TurkStat) are presented in line with ESA95 standards. Fiscal statistics prepared by the MOF cover the vast majority of general government institutions, and include a full balance sheet covering both financial and nonfinancial assets and liabilities. Since 2010, the coverage of fiscal statistics has been extended to include all revolving funds and a number of other self-financed entities. Annual financial

statements cover all central government ministries and agencies. Year-end accounts of individual entities have been subject to regularity, compliance, and performance audit by the Court of Accounts (*Sayıstay*) within nine months of the end of the years. The Court of Accounts will also be able to audit the consolidated accounts of the central government as a whole from 2016 onwards after receiving accounts of the individual entities. However, differences in institutional coverage and accounting basis between the MTP prepared by the MoD, and fiscal statistics, financial statements prepared by the MOF mean that forecast and outturn data are not fully comparable.

Macroeconomic and Fiscal Forecasting: The MTP provides detailed macroeconomic and fiscal forecasts of key aggregates for the next three years, but no mid-year update is published. Regular quality control, through ex post comparison of previous forecasts with actual outturn of key macroeconomic and fiscal aggregates is not carried out. Long term fiscal projections including demographic scenarios are prepared and discussed by the government internally in detail and also discussed in development plans prepared for five year period. The latest development plan was published in July 2013 and covers the period of 2014-2018.

Fiscal Risk: Limits on government guarantees and on-lending are included in the annual budget which also includes a risk account to cover the potential costs from called guarantees. Total contingent liabilities arising from guarantees and on-lending are provided in the debt management report which also analyzes risks associated with government's conventional asset and liability holdings. Since 2010, the MoD has been publishing information on Public Private Partnerships (PPPs) including total number and value of the projects sector by sector. While the government makes use of alternative macroeconomic and fiscal scenarios for internal planning purposes, these are not published.

Independent Fiscal Agency: There is no independent fiscal council in Turkey that publishes its own macro and fiscal forecasts or provides opinions on government fiscal policy and performance.

B. Developing a Credible Fiscal Adjustment Strategy

Fiscal Objectives and Rules: The MTP includes rolling three-year targets for the overall and primary balances of the general government and public sector which are reported against in subsequent MTPs and MTFPs. The most recent MTP in 2013 committed the government to reaching a general government primary surplus of 1 percent of GDP and a program defined general government primary surplus of 1.3 percent of GDP by 2016. While legislation on a formal fiscal rule was prepared and discussed in 2010, it has not been enacted.

Medium-term Budget Framework: The MTFP includes rolling three-year expenditure ceilings for all 47 General and 147 Special Budget units. These ceilings are generally not binding beyond the next budget and have tended to be revised upward over time to accommodate revenue overruns and emerging expenditure pressures. Budget documentation does not systematically distinguish the fiscal impact of existing and new policies.

Performance Orientation of the Budget: Ministries submit, alongside their annual budgets, a Strategic Plan showing their expenditure classified on a program basis. However, these programs do not form the basis of legislated appropriations. These Strategic Plans also include performance objectives and targets for each Ministry. The Ministry of Finance monitors achievements against performance programs on a quarterly and annual basis electronically by using reports submitted online by budget organizations. The MOF is currently designing a new budget structure which reflects programs, objectives, and outputs of the budget organizations. There are no regular comprehensive spending reviews.

Intergovernmental Financial Relations: The contribution of the central and local government sectors to the general government position is outlined explicitly in the MTP, but there is no mechanism to enforce the contribution of each sector. The Municipality and Special Provincial Administration Laws limit the ratio of the debt stock including interest to 100 percent of revenue in municipalities and 150 percent of revenue in metropolitan municipalities. Local authorities need the approval of a majority of municipal/provincial council and the Ministry of Interior for any borrowing above 10 percent of their revenues. The Treasury's approval is required for any external borrowing by local authorities. The Municipalities Law includes a range of mechanisms for enforcing compliance with these borrowing rules including penalties for misconduct as defined in the Criminal Law.

C. Implementing the Adjustment Strategy

Budget Unity: The central government budget covers the vast majority (90 percent) of central government spending excluding the five extra-budgetary funds, the contributory unemployment insurance and social security funds. There are no standing appropriations and all expenditure is authorized on an annual basis. Since 2006, the government has regularly published estimates of the revenue loss from tax expenditures, which stands at around 1.4 percent of GDP, but there is no limit on their size.

Top-down Budget Preparation: The MTFP is approved by the High Planning Council of Cabinet, a sub-committee chaired by the Prime Minister, which fixes ex ante ceilings covering both current and capital expenditure at the start of the budget process. These ceilings are almost always respected by line ministries when submitting their final budget requests. Earmarking of revenues and standing spending commitments are limited. Although major revenue and expenditure decisions are generally taken as a part of annual budget law, it is possible to introduce a law with fiscal effects outside the annual budget process.

Parliamentary Approval: There is no formal legislative debate or vote on the MTP and MTFP which been published in the Autumn rather than in the Spring in the last three years. The Plan and Budget Committee of the Parliament carries out preliminary examinations and consultations on the draft annual budget in October and November, prior to its presentation to the Parliament plenary session for approval in December. However, the Turkish Grand National Assembly votes on the Draft Budget Law on chapter by chapter basis and cannot introduce amendments which increase total expenditures or reduce revenues. Expenditures and revenues as well as the draft law can be amended in the Plan and Budget Committee. There are clear rules regarding the timing of final approval of the budget, and the budget has always been approved before the end of the year over the last ten years.

Budget Execution Controls: Controls over budget execution are strong. Supplementary budgets are required for any newly initiated spending during the financial year. Over the last ten years there have been no supplementary budgets. However, the appropriation for personnel expenditure can be exceeded without parliamentary approval to allow for mid-year increases in civil servant salaries. In recent years, this has contributed to general overspending as resources from the personnel have been transferred to other appropriations. These additional personnel expenditures were presented to the parliament as an ex post complementary appropriation in the final account laws. Central government bodies can carryover up to 5 percent of their appropriations between years. There is a contingency appropriation included in the budget which cannot exceed 2 percent of General Budget expenditure and was equal to 0.6 percent of total expenditure in 2013. Ministries can make multi-annual commitments for investment or other multi-annual engagements of up to four years, but only with Ministry of Finance's opinion.

Recommendations

- Government fiscal reporting should be further improved with an emphasis on ensuring consistency of data disseminated by the MOF and the MOD, and reporting of the realization of MTP targets during the year.
- Not only balance target but also the expenditure ceilings set in the MTFP should be respected to increase fiscal discipline and to protect the credibility of the MTBF.
- A comprehensive quantified statement of macroeconomic and fiscal risks should be included in budget documents. The risks from PPPs should also be incorporated into these reports.
- The impact of current and new policies on the fiscal figures should be separately analyzed.
- To facilitate more policy-based discussions, the government should introduce a program classification into the budget; and performance information should also be used during the budget review process to inform allocative decisions. In addition, spending reviews should be introduced.

UNITED KINGDOM

Summary Evaluation

Detailed fiscal reporting is provided for the whole of the public sector on an accruals basis. The Government has enhanced its fiscal reporting through publication of audited Whole of Government Accounts, which consolidate financial statements across the public sector, and through the Clear Line of Sight project which has better aligned fiscal reporting across budgets, statistics, and accounts. An independent fiscal council—the Office for Budget Responsibility (OBR)—was established in May 2010 and produces detailed macroeconomic and fiscal forecasts and provides information on various fiscal risks, although the Government does not produce a comprehensive quantified fiscal risk statement. The Government introduced two new fiscal rules in 2010—for the cyclically-adjusted current balance and net debt of the public sector—with progress against these rules being assessed by the OBR. The Government operates fiscal policy within a binding medium-term budget framework and in 2015-16 plans to extend the coverage of multi-year expenditure ceilings to around half of social security expenditure, and to introduce a ceiling for the costs of investment financed through public-private partnerships. Since 2010, the performance management of expenditure has been decentralized to line ministries. Controls are in place to manage borrowing by sub-national government. The budget covers all of central government expenditure. There are clear procedures governing Parliamentary oversight of the budget, though the Westminster model means that in practice expenditure and revenue decisions are largely passed with little amendment. Parliament does not approve expenditure in a top-down sequence and is not required to approve the budget until well after the start of the fiscal year. Budget execution controls are strong and in 2010 the Government introduced a new system which placed tighter controls on the amount of unspent expenditure that can be carried over by departments to future years.

A. Understanding the Fiscal Challenge

Type of Institution	Reforms since 2010
Fiscal Reporting	The Government now publishes audited Whole of Government Accounts on an annual basis.
Independent Fiscal Agency	The independent Office for Budget Responsibility (OBR) was established in 2010.
Macro and Fiscal Forecasting	The forecasts used in the budget are now produced independently by the OBR.
Fiscal Risks	The OBR includes sensitivity analysis in its medium-term forecasts and analyses balance sheet and long-term risks.

Fiscal Reporting: The publication of the first audited Whole of Government Accounts (WGA) in 2011 has been an important development in the UK's fiscal reporting. WGA consolidates the accounts of over 1500 public sector bodies and provides comprehensive information on the contingent liabilities and provisions facing the whole public sector. WGA is audited by the UK's independent National Audit Office (NAO). While the financial statements of the individual central government bodies on which the WGA is based are typically produced and audited within six-months of the year end, the latest consolidated WGA was published and audited with a 16 months lag. Implemented for the 2011-12 fiscal year, the Clear Line of Sight project has also improved the transparency and comparability of fiscal reports by better aligning reporting concepts used in the departmental budgets set by the Treasury, the departmental accounts audited by the NAO, and expenditure estimates presented to Parliament for approval. Previously these reports were based on different measures of expenditure, and Parliament approved expenditure controls that bore little relation to those used internally within Government. The Office for National Statistics is the UK's independent statistical agency and produces government financial statistics on a general government and public sector basis.

Independent Fiscal Agency: The UK's first independent fiscal council—the Office for Budget Responsibility—was established in May 2010 with a remit to produce independent macroeconomic and fiscal forecasts for use by the Government in the annual budget, to assess the Government's performance against its fiscal rules, and to examine the long-term sustainability of the public finances. The OBR's remit does not permit it to make normative analysis of the Government's fiscal policy. The OBR's reports have introduced a number of significant improvements in transparency and risk analysis, discussed below.

Macroeconomic and Fiscal Forecasting: The official macroeconomic and fiscal forecasts are produced by the OBR over a five-year forecast horizon twice a year: alongside the spring Budget and in a mid-year update alongside the Government's 'Autumn Statement'. The OBR's documentation provides greater detail than previous UK government forecasts, including on the economic drivers of revenue and expenditure forecasts and on the impact of new policy announcements on the fiscal forecasts. The OBR produces an ex-post evaluation of its forecast performance on an annual basis which analyses in detail the differences between outturn and forecast for both the macroeconomic and fiscal forecasts. The Treasury has also improved the transparency of the costings of revenue and expenditure policies by publishing a document explaining the assumptions and methodologies used to produce these costings, which are now independently scrutinized and certified by the OBR. The OBR also produces an annual fiscal sustainability report which analyses the public sector balance sheet, contingent liabilities and provisions, and provides long-term projections (50 years) of public sector revenue, expenditure, the primary balance and net debt under a number of economic and demographic scenarios.

Fiscal Risk: Alongside its medium-term forecasts the OBR publishes a comprehensive macroeconomic risk assessment including (i) sensitivity analysis showing the impact on its central forecast of changes to key macroeconomic and fiscal assumptions; (ii) alternative macroeconomic and fiscal scenarios; and (iii) fan charts illustrating the likelihood of outturns deviating from forecast

based on historical forecast errors. There have also been improvements in the reporting of specific fiscal risks over the last three years. The Government's exposure to contingent liabilities and provisions across the public sector are now presented in the WGA. The OBR assesses the implications of these data for long-run fiscal sustainability in its annual fiscal sustainability report. However, the Government does not currently respond in any systematic way to the OBR's sustainability report and it does not publish a single comprehensive fiscal risks statement of its own.

B. Developing a Credible Fiscal Adjustment Strategy

Type of Institution	Reforms since 2010
Fiscal Objectives and Rules	The new Government introduced two new fiscal rules in 2010.
Medium-term Budget Framework	A new ceiling has been introduced for around half of social security expenditure which will operate from 2015-16.
Performance Orientation	The Government has replaced a system of centrally-managed performance monitoring with a decentralized approach

Fiscal Objectives and Rules: The Government introduced two new fiscal rules in 2010: to balance the cyclically-adjusted current budget by the end of the rolling five-year forecast horizon; and to see public sector net debt falling by 2015-16. The first rule is not time-bound as the forecast horizon rolls forward each year. While the first rule takes account of the cycle, as it is specified on a cyclically-adjusted basis, the second rule is potentially pro-cyclical. In practice, as the Government is currently choosing to miss the rule on the basis of the OBR's latest forecast rather than introduce a potentially pro-cyclical policy adjustment, the second rule has not provided a binding constraint on fiscal decision-making. The Government's chances of meeting each rule are independently assessed by the OBR twice-yearly alongside its fiscal forecasts. Primary legislation requires the Government to set out fiscal rules, while the rules themselves are specified in a "Charter for Budget Responsibility" which is laid before Parliament and voted on. The legislation permits the Government to change the rules through a new Charter being approved by a vote in Parliament. In December 2013, the Government announced a review of the current fiscal framework which will report in Autumn 2014.

Medium-term Budget Framework: The Government continues to operate fiscal policy within a clearly defined medium-term budget framework. The OBR produces five-year forecasts for revenues and expenditures and the Government publishes detailed information and costings on the impact of its policy decisions over these horizons, as explained above. In the budgeting framework, public sector expenditure is split into "departmental expenditure limits (DEL)," for which fixed plans have been set over three-years at spending reviews which take place every two or three years, and "annually-managed expenditure (AME)," mainly social security and debt interest, which has not been subject to fixed spending controls. Fixed DEL plans currently only extend to the end of the current

Parliament in 2015-16 and the expenditure projections for the remainder of the five-year horizon are a combination of indicative total DEL plans and AME forecasts. The Government has recently announced plans to extend the coverage of multi-year expenditure ceilings to encompass around half of social security expenditure in 2015-16. It also intends in 2015-16 to place a ceiling on the total capital, interest and service costs of investment financed through public-private partnerships.

Performance Orientation of the Budget: The UK previously had a systematic approach to performance management where a set of Government-wide performance targets were monitored centrally against a basket of indicators. The Government abandoned this system in 2010 so reducing the performance orientation of the budget. In its place, the Government has introduced a decentralized approach to performance reporting where departments, agencies and sub-national government are required to publish information on their expenditures and on a broad range of output indicators. Central government departments are required to set out an assessment of progress against their policy objectives each year in an annual report.

Intergovernmental Financial Relations: Self-financed borrowing by local authorities is permitted only for capital investment and only by those authorities that comply with a code of prudential indicators of the affordability, sustainability and value for money of their borrowing plans. Central government has the power to limit the borrowing of local authorities that do not comply with the prudential code. There are specific agreements in place governing borrowing in the devolved administrations in Scotland, Wales, and Northern Ireland.

C. Implementing the Adjustment Strategy

Type of Institution	Reforms since 2010
Parliamentary Approval	A draft finance bill is now published three months before the start of the fiscal year.
Budget Execution Controls	A new system has been introduced to control end-year carry-overs of expenditure.

Budget Unity: While new revenue and expenditure policies are often proposed outside the budget cycle, firm and final decisions on fiscal measures are almost always taken at the Autumn Statement or spring Budget. The budget covers all of central government expenditure. Earmarking of revenue and standing expenditure commitments are limited largely to EU financing commitments with the vast majority of revenues and expenditures being authorized through the annual Parliamentary estimates process.

Top-down Budget Preparation: Parliament endorses the Government's medium-term fiscal strategy as set out in the Charter of Budget Responsibility. There is also a debate on the overall fiscal policy stance set out at the Autumn Statement and the Budget. However, Parliament does not explicitly vote to approve this stance. The expenditure limits set out in the Budget are not voted on

in a top-down sequence; rather Parliament approves expenditure on a department-by-department basis through the year.

Parliamentary Approval: In theory there are no restrictions on the right of Parliament to amend the Finance Bill which is the legislative vehicle for revenue measures introduced in the Budget. Parliament's right to amend expenditure is limited to those which reduce the amount of resources or cash being sought. In practice, the Westminster system means that the Government typically has a majority in Parliament which means its expenditure and revenue decisions are largely passed with little amendment. There are a clear set of Parliamentary procedures for approving the Government's revenue and expenditure decisions. However, these do not require these decisions to be approved until well after the start of the fiscal year in which they take effect. The Finance Bill is typically approved more than three months after the start of the fiscal year (temporary resolutions allow tax changes to take place at the start of the tax year and these are then given permanence through the approval of the Finance Bill). However, to allow for better scrutiny since 2011 the Government has published a draft Finance Bill around three months before the start of the fiscal year.

Expenditure is approved retrospectively on ongoing basis through and after the end of the fiscal year. The main expenditure estimates are typically not approved until three months after the start of year and so expenditure for the first few months of the year is approved through a "Vote on Account" process which authorizes departments to spend up to 45 percent of the previous year's plans. However, as set out above, the Clear Line of Sight Project has improved the information provided to Parliament allowing it to better scrutinize expenditure.

Budget Execution Controls: There are firm controls over the execution of departmental budgets once they have been agreed by the government and voted by Parliament. The Government's spending plans include an unallocated reserve of around 3 percent of expenditure. Expenditure in excess of the initial estimates voted by Parliament requires parliamentary approval of a Supplementary Estimate. Departments need Treasury approval for all multi-year expenditure commitments that exceed agreed "delegated limits." The Government is entitled to spend less than appropriated by Parliament without limit. In 2010 the Government introduced a new system of "Budget Exchange" which placed tighter controls on the amount of unspent expenditure that can be carried over by departments to future years. Departments need to receive permission from the Treasury for carry-over and must show that the expenditure is needed for specific projects. Any agreed carry-over must be used in the subsequent year so that departments cannot build-up a stock of unused expenditure, reducing fiscal risk for the Treasury.

Recommendations

- The Treasury should produce WGA more quickly after the end of the fiscal year.
- The Government should make a substantive response to the OBR's fiscal sustainability analysis and produce a comprehensive fiscal risk statement.

- The Government's review of the fiscal framework should consider how the fiscal rules can be made more binding on the fiscal outturn while maintaining flexibility to deal with exogenous shocks.
- The Government could introduce a more systematic and consistent approach to monitoring and managing ministries' performance.
- Parliament should play a more active and timely role in endorsing and monitoring delivery of the government's medium-term fiscal strategy.

UNITED STATES

Summary Evaluation

Fiscal reporting and forecasting at the federal level are comprehensive, timely, and of good quality. Medium-term macroeconomic and fiscal projections by the Office of Management and Budget (OMB) present detailed information on assumptions and produces mid-year updates. The independent Congressional Budget Office (CBO) provides high-quality independent forecasts and analyses of fiscal policies. A number of fiscal risks are disclosed and fiscal sustainability information is included in the annual financial statements. While consolidated historical data are available, there are no fiscal forecasts at the general government level. State and local government budgets, statistics, and forecasts are published and discussed separately from the federal budget. Constitutional obstacles exist to formulating and enforcing fiscal policies covering the general government. The federal government does not have specified medium-term fiscal objectives. A variety of fiscal rules are in place to guide budget preparation, however, exemptions to these rules for large mandatory programs limit their effectiveness in controlling total spending. About two-thirds of federal government spending is authorized by permanent legislation, and thus is not subject to annual review or appropriation in the budget process. The lack of political consensus on key fiscal and budgetary policies, together with a fragmented budget process, prevent fiscal adjustment from proceeding at a more steady pace and in the most desirable composition. Performance management reforms place a strong emphasis on setting and monitoring priority goals and on increasing program evaluation. Performance information is, however, not sufficiently incorporated into the budget process.

A. Understanding the Fiscal Challenge

Table 1. Main Reforms in this Area	
Type of Institution	Reform since 2010
Fiscal Reporting	A statement of fiscal sustainability has been introduced.

Fiscal Reporting: The consolidated financial statements give a comprehensive view of the federal government's finances and cover both budgetary and off-budget social insurance programs. It is audited by the Government Accountability Office (GAO), an independent, nonpartisan agency that reports to Congress, and is typically published within two months, but no later than six months after the end of the fiscal year. Government-Sponsored Enterprises (GSEs), such as the Federal Home Loan Banks and the Federal National Mortgage Association (Fannie Mae), are not included in the consolidated financial statements, although the value of investments in GSEs is presented on the balance sheet, and the liabilities, including contingent liabilities, are discussed separately. The Bureau of Economic Analysis (BEA) produces the National Income and Product Accounts (NIPA) statistics which cover the general government. These are updated quarterly and are aligned with the

United Nations System of National Accounts (SNA) 2008. Budgets are prepared on a modified cash basis, while accounting is conducted primarily using modified accrual standards. In 2010, the Federal Accounting Standards Advisory Board began phasing in a new financial reporting standard to enhance the transparency of the government's balance sheet over the long term. The reforms include a requirement to produce a statement of fiscal sustainability.

Macroeconomic and Fiscal Forecasting: OMB publishes in budget documents medium-term macroeconomic and fiscal projections, including for all major fiscal aggregates, for the upcoming budget year and nine years beyond in order to reflect the effect of budget decisions over the longer term. The budget documents also include a comparison of the Executive's macroeconomic assumptions, which can be on the optimistic side, with those of CBO and the private-sector Blue Chip Consensus forecast, as well as an analysis of the sensitivity of estimates to changes in economic variables. Ex post comparisons are made for key assumptions used in previous forecasts. OMB updates the budget estimates for the mid-session review. These updates include revised budget estimates resulting from changes in economic assumptions, technical re-estimates, Presidential initiatives, and completed Congressional actions that have occurred since the presentation of the budget. No consolidated fiscal forecast for the general government is provided. The Analytical Perspectives volume of the budget does however include a brief fiscal outlook for State and local governments. OMB, CBO, and GAO independently prepare long-term fiscal projections for the federal government with a range of alternative scenarios.

Fiscal Risk: The budget documents include a comprehensive discussion of fiscal risks. Nevertheless there is no formal fiscal risk statement and not all risks and contingent liabilities are quantified. The Analytical Perspectives volume of the budget, presents a quantified assessment of risks associated with alternative economic assumptions. Since 1992, the budgetary treatment of credit programs moved from cash to accrual accounting principles. This requires the budget to recognize the estimated subsidy cost of direct loans and loan guarantees as they are incurred and treats these subsidies as obligations, which consequently must be appropriated by Congress. Accrual accounting principles are, however, not applied to a number of large programs, including the Federal Deposit Insurance Corporation, Pension Benefit Guaranty Corporation, National Flood Insurance, National Insurance Development Fund and Crop Insurance. Contingent liabilities in these and other programs appear in the budget only when events trigger the need for expenditures. There is no systematic assessment of risk to government assets. However, the consolidated financial statements do present these programs on an accrual basis.

Independent Fiscal Agency: Among G-20 countries, the United States CBO is the largest and best-resourced fiscal council. It prepares a number of macroeconomic and fiscal forecasts, analyzes forecasts made by the executive, and presents fiscal options for Congress to consider, but does not make recommendations on policy. This independent "re-estimate" of the President's budget allows Congress to compare the administration's spending and revenue proposals with CBO's baseline spending and revenue projections using a consistent set of economic and technical assumptions. While most of CBO's analyses are forward-looking, its monthly and year-to-date analyses of federal spending and revenue totals also form the basis for ex post comparison

of outturns to previous fiscal forecasts. An ex post comparison of outturns to previously forecasted macroeconomic aggregates is also published.

B. Developing a Credible Fiscal Adjustment Strategy

Table 2. Main Reforms in this Area

Type of Institution	Reform since 2010
Fiscal Rules	The Budget Control Act of 2011 reinstated limits ("caps") on the amount of discretionary budget authority. Reinstatement of PAYGO rules, which expired in 2002. The PAYGO Act of 2010 requires offsets to any increased expenditures or tax cuts so that there is no net increase in the deficit.
Performance Management	The Government Performance and Results Modernization Act of 2010 places increased focus on setting high-priority performance goals for agencies and encourages program evaluations on a selective basis.

Fiscal Objectives and Rules: The U.S. has enacted several fiscal rules in recent years but there are no comprehensive time-bound fiscal objectives. The Budget Control Act of 2011 reinstated limits ("caps") on the amount of discretionary budget authority that can be provided through the annual appropriations process. Separate caps are set on security and non-security spending in fiscal years 2012 and 2013, while a single cap will apply from 2014 to 2021. As a result of the failure to adopt a medium-term comprehensive deficit reduction plan, additional automatic spending cuts (the so-called sequester) came into effect in March 2013 and are scheduled to remain in effect until 2023.¹⁶ The sequestration cuts, will require \$1.2 trillion in deficit reduction spread evenly over 2014-23 with one-half coming from defense spending and the other half from domestic programs. However, Social Security, Medicaid are exempt, as are other entitlement programs. The Pay-As-You-Go (PAYGO) rule, reinstated by law in 2010, requires that legislation enacted by Congress must be deficit neutral, meaning any act which would increase the projected deficit must be off set and financed by other measures over a specified time period. However, because of several exemptions, including mandatory spending by off-budget entities such as the Social Security Trust Funds, the Act's effectiveness in promoting fiscal restraint is limited. Some of the exempted programs, such as unemployment insurance, are sensitive to the business cycle and thus serve an important role in counter-cyclical fiscal policy. There is a statutory limit for total federal debt. However, the debt limit

¹⁶ The original cuts were scheduled to last until 2021, but the Bipartisan Budget Act of 2013 extended the cuts in certain programs to 2023.

is not updated concurrently with the approved budget, which creates the anomalous situation where borrowing authorized in an approved budget may exceed the debt limit. States have balanced budget rules in various forms, but there are no federal sanctions for violation.¹⁷

Medium-Term Budget Framework: Every February, the President sends a budget proposal to Congress that lays out the administration’s projected revenue and expenditure paths for the next ten years, policy priorities, and the recommended tax and spending changes. The budgetary projections are presented on the basis of existing law and a “policy” basis, which means that no laws or policies other than the President’s proposed policies are expected to change over the period of the forecast. The President’s budget is not prepared with a prior decision on multi-year expenditure ceilings for aggregate or agency expenditure, although the 2011 Budget Control Act, introduced caps on the discretionary portion of the budget. Congressional budget procedures require a plan for spending and revenue in the form of an annual budget resolution but it does not include medium-term fiscal goals.

Performance Orientation of the Budget: The Federal government has been pursuing performance-informed budget reforms for decades. Past efforts have significantly increased the availability of performance information and the understanding of program success, however, increasing the use of this information in decision-making has been challenging. The Government Performance and Results Modernization Act of 2010, builds on previous reforms. The Act places heightened emphasis on priority-setting; cross-organizational collaboration to achieve shared goals; and the use of goals and measurement to improve outcomes. In 2014, all agencies will be required to conduct strategic reviews to be presented along with their budget submissions to OMB. Appropriations are made by budget accounts, which are generally, though not exclusively, aligned with programs. The Act also promotes selective in-depth evaluation of government programs.

Intergovernmental Financial Relations: The President’s budget projections do not include a consolidated forecast for the general government and there is no regular fiscal policy coordination between different levels of government. However, the Economic Report of the President, which is an important and widely-read document, provides information on state and local governments, including current fiscal conditions, a longer-term fiscal outlook, and estimates of the cyclicity of state and local government expenditures. Since 2007, GAO has also published a fiscal outlook through 2060 for state and local governments as a whole, using NIPA as the primary data source.

C. Implementing the Adjustment Strategy

Budget Unity: Congress annually appropriates discretionary spending, which makes up about one-third of federal spending. The remaining two-thirds of federal spending, comprised of mandatory

¹⁷ Because of their high level of independence in the U.S. system, states are subject to considerable market discipline in the municipal bond market, where they are assumed to stand on their own without backing from the Federal government.

programs and interest, occurs on the basis of permanent legislation, which does not require annual review or appropriation. However, budget documents provide information on mandatory spending, thus clarifying the total of estimated expenditures and revenues. Tax expenditures are reported by both the Congressional Joint Committee on Taxation in a special study each year and by the U.S. Treasury Department as a special appendix to the President's annual budget proposal. The quantification of tax expenditures is comprehensive, but the size and composition of tax expenditures are not explicitly recorded in the budget as outlays or as negative receipts, nor are limits set on total amounts.

Top-Down Budget Preparation: There is no aggregate budget ceiling for overall expenditure including both mandatory and discretionary. The 2011 Budget Control Act, however, did introduce caps for discretionary expenditure. Functional or agency level ceilings are not announced at the beginning of the executive's budget process. OMB provides agencies with policy guidance for preparing their budget requests. The forward year estimates included in the previous budget serve as a starting point for estimating the next year's budget, unless specific guidance indicates otherwise. The annual budget formulation process within the executive does not include a detailed review of mandatory expenditures, which are based on permanent legislation. Tax legislation, may be considered and approved outside of the formal budget process, and is subject to the PAYGO rule. Budget resolutions in Congress provide a top-down approval of the budget. However, it is not coordinated with the executive budget process, and a budget resolution is frequently passed late and in some cases not at all (for example, in 2005, 2007, and 2011).

Parliamentary Approval: Congress considers the President's budget proposal but it has unlimited power to amend it. The budget resolution approved by Congress sets overall fiscal policy on an annual basis, including targets for total receipts and outlays, and the budget balance. The Congressional timetable calls for the budget resolution to be passed by April 15 of each year. However, Congress has not passed a budget resolution in a timely manner in several years. Appropriation bills generally have not been enacted on schedule in recent years. When this happens, government operations continue under the authority of Continuing Resolutions (CR) passed by Congress. If no CR is passed, partial shutdown of government ensues. In some years, multiple CRs are passed in a fiscal year, which creates substantial uncertainty for spending agencies and impedes efficient operations.

Budget Execution Controls: Agencies are not permitted to transfer funds between budget accounts without legislative authority. At any time during the year, the President may submit to Congress proposals for supplementary appropriations that are deemed necessary because of laws enacted after the approval of the budget or that are in the public interest. Supplementary appropriations, however, are normally reserved for situations that are too urgent to be postponed until the next regular appropriation cycle. Appropriations are generally available for obligations for one year, but the appropriations bills sometimes provide multi-year obligations or permanent authority to obligate funds, especially for construction and other similar activities. In principle, expenditures approved by Congress are meant as both a ceiling and a floor of agency spending. Under the procedures established by the Budget and Impoundment Control Act of 1974, the

President has limited authority to reduce or withhold agency funding. Unforeseen expenditures can be covered through supplementary appropriations. There are no contingency funds or reserves.

Recommendations

The following reforms could be pursued to strengthen budgetary institutions:

- Reduce risks associated with macroeconomic projection uncertainty by adopting more conservative growth and interest rate assumptions and improve efficiency in government operations, by establishing binding medium-term fiscal objectives to be observed by both the executive and the legislature. These objectives would be recalibrated on an annual basis, based on clear specification of changed economic policy and conditions.
- Strengthen the top-down approach to annual budget preparation by specifying early in the budget cycle aggregate expenditure ceilings to be observed by both the executive and the legislature. All exemptions to pay-as-you-go rules that do not serve counter-cyclical macroeconomic policy objectives would need to be eliminated.
- Take steps to limit the fragmentation of the budget approval process. Budgetary decision-making by Congress should be based on adoption of a single comprehensive appropriation bill, as has been the practice in the past with omnibus appropriation bills consistent with the budget resolution.
- Within the context of a medium-term fiscal framework, establish medium-term spending ceilings which incorporate both mandatory and discretionary expenditure. These should help enforce greater fiscal discipline and promote a clearer understanding of the available fiscal space over the medium term.
- Establish a procedure stipulating that last year's approved budget authority (in nominal amounts) automatically comes into effect in the event appropriation bills are not approved by Congress on time, or a continuing resolution is allowed to lapse, allowing government operations to continue without disruption.
- Align increases in the debt ceiling with the annual comprehensive budget resolution. This will increase the debt ceiling with the expected annual deficit, and thus will reduce the fragmentation of budgetary decision-making.
- Prepare a fiscal risk statement, including measurement of all major contingent liabilities, and publish it as part of the budget documents.