BRATISLAVA LAW REVIEW

PUBLISHED BY THE FACULTY OF LAW, COMENIUS UNIVERSITY BRATISLAVA

ISSN (print): 2585-7088
ISSN (electronic): 2644-6359

INDEPENDENT FISCAL INSTITUTIONS AS A PART OF EUROPEAN TRADITIONS / Maciej Serowaniec

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This research was supported by funding from the National Science Centre, Poland under the project Independent Fiscal Institutions as Non-Identified Constitutional Objects? (grant agreement no. 2022/47/D/HS5/00859).

Abstract: *Fiscal councils are independent public institutions aiming to promote the sustainability of public finances through various functions, such as assessing budgetary plans and their implementation or preparing budgetary and macroeconomic forecasts. Thus, synthesising the attempts made in the literature to define the concept of independent fiscal institutions, it should be emphasised that by providing an independent, impartial and objective assessment of fiscal policy and performance, they promote sound fiscal decisions and sustainable public finances. Independent fiscal institutions also reduce information asymmetries and promote transparency in public finances, thereby raising the reputation and electoral costs for governments that pursue imprudent policies or breach key commitments. As such, they can support contemporary states in addressing the tendency to increase spending and deficits. To better understand the contemporary factual and normative state of the analysed dissertation topic, it is worth tracing, even in some summary, the process of emergence and the directions of development and evolution of independent fiscal institutions. Although independent fiscal institutions are relatively new bodies in the political architecture of the vast majority of the EU Member States, a small group of countries pioneered the creation of these institutions. It is necessary to trace the systemic solutions that have determined the legal and constitutional status of fiscal institutions in recent decades in order to understand the factors that have led to their reassessment.*

Key words: *Fiscal Councils; Independent Fiscal Institutions; Fiscal Policy; Fiscal Deficit*

Submitted: 03 November 2023
Accepted: 21 April 2024
Published: 07 July 2024

Suggested citation:
Serowaniec, M. (2024). Independent Fiscal Institutions as a Part of European Traditions. *Bratislava Law Review*, 8(1), 195-202. https://doi.org/10.46282/blr.2024.8.1.756

1. INTRODUCTORY REMARKS

In the last decade, there has been a marked increase in interest in independent bodies monitoring medium-term fiscal sustainability (so-called watchdog institutions). This trend is confirmed by, among others, the Organisation for Economic Cooperation and Development (hereinafter: OECD), the International Monetary Fund (hereinafter: IMF) and the European Commission. The importance of this solution has increased, especially in recent years, in view of the deteriorating financial state and outlook of individual countries. The ongoing debt crisis has been compounded by phenomena already identified, such as the tendency of politicians to increase deficit bias, the unsustainability of public debt despite good economic times (debt ratcheting), and the ageing population process. A consequence of the above is that the practical role of fiscal councils has increased. The intensity of their establishment has increased, especially in European countries, where supranational criteria are imposed to fulfil the annual general government deficit and debt-to-GDP ratio, but also the medium-term objective (Horvath, 2018).

There are competing definitions of fiscal councils in the literature, highlighting the different structural features of these institutions. In light of the definition proposed by X. Debrun, independent fiscal institutions monitor fiscal policy and evaluate public finance reforms, and their activities should be focused on promoting fiscal policy sustainability. Unlike the central bank and the parliament, Fiscal councils monitor and evaluate government actions independently and autonomously, in other words, 'depoliticising fiscal policy' (Debrun, 2010). The competences of the fiscal councils include, in particular, the preparation of macroeconomic forecasts for the state budget or advising the government on fiscal policy. The delegation of these functions to fiscal councils is primarily justified by the tendency of public authorities to make overly optimistic macroeconomic assumptions that form the basis of their budgets (Kopits, 2011). Therefore, fiscal councils aim to reduce the risks associated with decision-making in this area (Hagemann, 2011). In contrast, according to the broadest definition introduced by the European Commission, fiscal councils are non-partisan public bodies, other than the central bank, the government or the parliament, tasked with preparing macroeconomic forecasts for the budget, monitoring the progress of fiscal policy implementation and/or carrying out advisory tasks for public authorities. They are publicly funded bodies, but have an independent position, especially concerning the government. Fiscal councils are thus a kind of complement to EU fiscal rules, being an important element of sustainable fiscal policy. It is worth noting at this point that in its definition the European Commission also allows for the possibility of the above tasks being carried out by supreme state control bodies. According to the definition worked out by the OECD, fiscal councils are established based on public law, employing non-partisan professionals with a mandate to carry out continuous monitoring and/or advice on implementing fiscal policy. The mandate of such institutions is to increase pressure for fiscal discipline, raise the quality of the debate on public finances and promote fiscal transparency and accountability (OECD, 2014). On the other hand, as the IMF points out in its studies, fiscal councils are independent public institutions that support the sustainability of public finances through various functions, such as assessing fiscal plans and their implementation or preparing budgetary and macroeconomic forecasts. Thus, synthesising the attempts made in the literature to define the concept of independent fiscal institutions, it should be emphasised that by providing an independent, impartial and objective assessment of fiscal policy and performance, they promote sound fiscal decisions and sustainable public finances. Independent fiscal institutions also reduce information asymmetries and promote transparency in public finances, thereby raising the reputation and electoral costs for governments that pursue imprudent policies or breach key commitments. As such, they can support modern states in addressing the tendency to increase spending and deficits (IMF, 2013).

Independent fiscal institutions are relatively new bodies in the political architecture of the most EU Member States. However, there is a small group of countries that pioneered the creation of these institutions - Belgium (1936), the Netherlands (1945), Denmark (1962), Germany (1963) and Austria (1970). This paper aims to analyse the systemic solutions determining the legal and constitutional status of independent fiscal institutions in the countries mentioned above over the last few decades. Obviously, the competences and mandates of these institutions have undergone significant changes over time, most notably those necessary to adapt to the requirements of the EU regulations. This analysis is essential for a better understanding of the contemporary systemic position of fiscal councils. The analysis will also allow an answer to the question of what factual and normative factors have contributed to the promotion of independent fiscal institutions as a specific element of the European systemic tradition. The analysis of EU regulations determining the development of fiscal councils is left out of the scope of consideration, as this issue is thoroughly analysed in the literature.

The thematic scope of the work made it necessary to use several scientific research methods, namely the legal-dogmatic method, the legal-comparative method and the historical method. The historical method was used primarily to show the formation process and the directions of development and evolution of independent fiscal institutions. In characterising the systemic position of fiscal councils, the legal-dogmatic method, on the other hand, played a fundamental role, while the legal-comparative method was used complementarily.

2. THE EMERGENCE AND DEVELOPMENT OF FISCAL COUNCILS IN EUROPEAN COUNTRIES

The current trend towards creating independent fiscal institutions has two main sources of inspiration. The first derives from the pre-existing institutions whose remit ensured they acted as independent observers of budgetary decisions. Such institutions include the Belgian Supreme Council of Finance (*Conseil Supérieur des Finances*), the Dutch Central Planning Office (*Centraal Planbureau*), the Danish Economic Council (*De Økonomiske Råd*) and the German Council of Economic Experts (*Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung*). An excellent example of the institutions mentioned above is the Belgian Supreme Council of Finance. It was created as an advisory institution of a technical nature, but it was not until the reforms of the 1980s that its fiscal policy position was strengthened. In parallel, it was decided in 1959 to set up a Federal Planning Bureau in Belgium to propose and develop economic plans. The Bureau was reformed in 1970, 1980 and 1994, abandoning some of its former tasks and focusing on preparing economic forecasts and impact analyses. Belgium is thus not only an example of a country with an old and well-functioning fiscal council, but also an example of the dual agency model. The Dutch Central Planning Bureau was set up in the Netherlands in 1945 to research public policy implementation by state bodies. This institution, taking action on its initiative or at the request of the government, parliament, trade unions and employers' federations, quickly became an important forum for opinion and advice to develop a common macroeconomic strategy to support the post-war economic recovery. This body had a broad range of powers to co-create the economic decision-making process of politicians and social partners. Within its remit, it was responsible for, among other things, the preparation of forecasts (also used by the government in the preparation of the annual budget) of short-, medium- and long-term macroeconomic analyses, conducting analyses of the dynamics of the state's finances, and carrying out research and evaluations in the field of public policies. The atypical task of the Central Planning Bureau to analyse, in a politically neutral manner, the economic stability and budgetary implications of the proposals contained in the programmes of the parties and coalitions participating in the elections became particularly important. Over time, such an instrument has proved useful for making political groupings more accountable (Bos and Teulings, 2012). In contrast, the Danish Economic Council (*Økonomiske Råd*) was established in 1962. One of its primary objectives was to monitor

DOI: 10.46282/blr.2024.8.1.756

the country's economic situation and analyse its long-term development dynamics. The Economic Council comprised four experts, usually representing the academic community (the so-called 'wise men'), whom the government formally elected. The Council's activities mainly focused on the preparation of seminal reports on issues of an economic nature. The analyses concerned the main public policies (among which the budget gained the most prominence) and were always of great interest to the public. The executive often implemented the recommendations adopted. The term 'wise men' is also customarily used to refer to the Council of Economic Experts members, an 'academic body' established in Germany in 1963. The primary task of the Council of Experts was to assist all bodies responsible for economic policy and the general public in formulating sound opinions on economic issues. Appointed, by the Federal President at the government's request, the experts advised the Federal Government on economic policy issues and the assessment of national macroeconomic development. In addition to special reports, the Council of Experts still produces an annual report to this day, the content of which has already become an important reference point in the political debate on economic issues, directly influencing some important decisions of the federal government. Over the last sixty years, the Council of Experts has steadily strengthened its position, thanks to the independence, transparency and precision of its analyses of the national economic situation. In Austria, on the other hand, the Public Debt Committee (*Staatsschuldenausschuss*) was established in 1970. The appointment procedure for the fourteen members of the Committee involves not only the government, but also the Federal Chamber of Commerce and the Chamber of Labour. Initially, as part of its advisory activities, the Committee focused exclusively on public debt issues (Kopits, 2011, pp. 2–5). Since 2002, this institution has also conducted budgetary policy and public finance analyses. Thus, from the very beginning of the existence of these institutions, their primary objective has been to mitigate the risks associated with the pursuit of irresponsible fiscal policies and, above all, to monitor them, control the budget deficit and assess the long-term effects of the actions taken by public authorities in this area. It is worth noting, however, that some European countries have given up creating a new body tasked with monitoring fiscal policy and public debt dynamics, preferring to entrust this task to already existing institutions (e.g., France) (Viney and Poole, 2019).

A second source of inspiration for creating such institutions has come from proposals from the research community. In particular, the OECD and the IMF have published a significant number of policy papers, reports and reports on international financial institutions, providing an economically, fiscally and politically oriented assessment of the performance of these institutions, where they have been established, without taking into account the constitutional dimension of their existence: namely, the impact on constitutional principles and dynamics, including representative democracy, separation of powers, checks and balances and democratic accountability (Jankovics and Sherwood, 2017).

These documents point to two main reasons for creating independent fiscal institutions. The first relates to the objective of countering the trend towards deficits. Fiscal councils are meant to reduce the focus of most governments on short-term expansionary economic policies, particularly public spending, to increase electoral popularity through their decisions, instead of looking after the long-term interests of society to reduce the deficit and public debt. From this point of view, fiscal councils serve the purpose of 'intergenerational constitutional justice' against the 'pressure of time inconsistency'. In this context, it has even been argued that fiscal councils can be a 'weapon against populism', being able to foster more responsible and technically informed policy decisions. Independent fiscal institutions, at least in concept, can prevent the risk of political manipulation of macroeconomic forecasts and fiscal policies by populist governments just looking to please voters (Tesche, 2019).

The second objective that fiscal councils can help to achieve is to respond to the problem of the information asymmetry faced by citizens and parliaments, especially the parliamentary opposition and minorities, in controlling the budgetary process. The 'financial hegemony of the executive' has affected parliaments for decades and is more or less evident depending on the system of government. Economic and fiscal governance in the eurozone has further complicated this picture and exacerbated the problem of information asymmetry, given how the European and national semesters develop, in constant interaction between the EU institutions and member state governments. Properly functioning democracies require that all parties are fully informed. However, this condition is often not fulfilled because there is an information asymmetry between the government on the one hand and the voters and opposition parties on the other.

Consequently, voters may be unable to observe the government's 'true' fiscal situation. In the absence of sufficient understanding of the intertemporal fiscal constraint - which assumes that future primary surpluses must be equal to or greater than the outstanding net public debt - voters may be inclined to succumb to excessive optimism about the 'true' state of the public finances ('fiscal illusion'). A government claiming that a fiscal policy measure will be budget neutral makes it difficult for the average voter to verify this information (Calmfors and Wren-Lewis, 2011). If governments exploit this information asymmetry for electoral gain, a well-known political virtuous cycle will ensue, leading to persistently high budget deficits. Therefore, the dissemination of non-partisan assessments of fiscal policy can foster a common understanding of the trade-offs underlying fiscal policy and even out the information asymmetry.

The need for fiscal councils stems primarily from developing, implementing and adhering to a fiscal framework that aims to achieve a sustainable fiscal policy based on fiscal balance and preserving the stability of the public financial system. The literature points to two main objectives of the fiscal policy pursued:

1) a short-term goal that primarily serves to achieve *fiscal sustainability* outcomes, and
2) the need to take long-term measures is primarily related to ensuring the solvency of the public finance sector and maintaining an appropriate relationship between public debt and the country's level of economic development.

The definition of these 'rules of the game' should help to reduce the discretionary nature of the fiscal policy implemented in favour of its accountability. With commitments to the sustainability of public finances coming under scrutiny since the crisis, policymakers are looking for new ways to maintain fiscal discipline and restore public confidence in their ability to manage public budgets prudently and transparently (Tesche, 2019). While budgetary decision-making is ultimately the responsibility of democratically elected constitutional organs of the state, Independent fiscal institutions, often in addition to credible fiscal rules, are seen as a mechanism to help combat tendencies to increase spending and deficits and, more generally, to enhance fiscal discipline, promote greater fiscal transparency and accountability, and improve the quality of public debate on fiscal policy. Therefore, the fundamental objective of constituting independent fiscal institutions is increasing control over budget formulation and implementation. However, several basic requirements must be met for a fiscal council to function efficiently and effectively. The first is properly identifying national needs from analysing the existing legal, organisational and political circumstances. The second requirement is to keep the fiscal council members apolitical and independent and to apply transparent rules for their

DOI: 10.46282/blr.2024.8.1.756

selection. *Last, but not least,* fiscal councils must also be provided with access to up-to-date statistical data and an efficient analytical apparatus capable of preparing and presenting analyses illustrating economic and financial status and developments in national, European and global terms (Hagemann, 2011).

At this point, two opposing views on the democratic legitimacy of fiscal councils have emerged in the literature. The first one sees the emergence of fiscal councils as compatible with and even reinforcing the idea of democracy (Fasone, 2022; European Commission, 2014; Fasone and Fromage, 2017). Fiscal councils can function as 'accountability multipliers' and strengthen the role of national parliaments through increased fiscal control capacity (Fromage, 2017). Fiscal councils do not have direct policy instruments to correct the fiscal path, forcing a fiscally profligate government to act through their orchestrating capacity, i.e., disseminating non-partisan analyses of fiscal policy choices. Thus, fiscal councils can generate 'technocratic legitimacy' by improving the quality of fiscal policy debates by introducing 'impartial' information into the democratic process. The second argues that it underpins 'a growing technocratic tendency where experts no longer inform the decision-making process but become decision-makers' (Fasone, 2022, p. 265), depriving democratically elected representatives of their policy tools. The government (trustees) thus entrusts the politically independent fiscal council with direct fiscal policy instruments (such as setting the debt ceiling or spending) (European Commission, 2014).

3. SUMMARY

Summing up the findings so far, it is safe to say that independent fiscal institutions have become part of the European systemic tradition. Indeed, some European countries (Belgium, the Netherlands, Denmark, Germany and Austria) were established long before the adoption of EU regulations defining their role in national fiscal policies. The analysis shows that the role of fiscal councils initially focused on designing, implementing and adhering to a fiscal framework aimed at achieving sustainable fiscal policies based on fiscal balance and preserving the stability of the public financial system. Over time, their role began to grow steadily by monitoring the executive based on the financial implications of its policy options, by providing, validating or assessing macroeconomic forecasts and by making the results of their analyses publicly available, independent financial institutions are now able not only to enhance the credibility and transparency of fiscal decisions, but can also strengthen *ex ante* parliamentary scrutiny and *ex post* oversight in budgetary matters. It should be stressed, however, that the ability of fiscal councils to strengthen democratic accountability depends on several factors, such as the increased transparency of the budgetary procedures they can trigger and the extent to which they can force the executive to be publicly accountable for its budgetary choices and to justify to parliament deviations from the medium-term objective (Fasone, 2021).

As C. Fasone and E. Griglio point out in the inter-institutional struggle that tends to dominate budgetary and financial procedures, the creation of independent financial institutions may determine a change in the long-standing dominance of the executive in budgetary matters in most EU countries. In all EU Member States, parliaments have often been marginalised in fiscal decision-making and are less equipped to inform fiscal policy than governments. This evidence is further reinforced by the fact that European New Economic Governance measures, urging stricter fiscal discipline within a certain timeframe, essentially limit the room for manoeuvre of national parliaments in a context such as the EU, where these legislative bodies have usually been considered 'losers' of the European integration process (Fasone and Griglio, 2013).

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