Joint report on the parallel audit of Medium-Term Budgetary Frameworks

Participating SAIs: Finland, France, Italy,

the Netherlands, Portugal, Slovakia and Sweden

Contact Committee Fiscal Policy Audit Network

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Contents

1 Introduction

This joint report collates and analyses the findings of seven national parallel audit reports and assessments. Within the framework of the EU Contact Committee, the Fiscal Policy Audit Network launched a parallel audit of Medium-Term Budgetary Frameworks (MTBFs) in 2019. The SAIs of Finland, France, Italy, the Netherlands, Portugal, Slovakia and Sweden took part, completing their national audits mostly in 2020 and 2021. The national audits used the same audit questions and the same audit criteria to allow for comparison of audit results (Appendix 1).

The focus of the parallel audit of Medium-Term Budgetary Frameworks has been on central government budgeting and on planning or forecasting expenditure at least three years ahead. MTBF systems in each country differ from each other, as the national MTBF often reflects the institutional legacy of each country rather than being a direct follow-up to EU directives and agreements. There is even more variation between countries in how the MTBF is reflected in annual budgeting. The aim of the audit was to assess the practical implementation of medium-term expenditure objectives or forecasts, and their functionality in both the national and EU contexts.

The main audit question in the parallel audit was: Are medium-term expenditure objectives set up effectively and transparently in the budget process? In order to answer the main audit question, more detailed audit questions were formulated about the following areas (numbers 3.1-3.6 refer to chapters in this report):

- 3.1 Integration into the budget process;
- 3.2 Effectiveness at achieving the stated goals;
- 3.3 Relationship with other national budgetary objectives;
- 3.4 Relationship with the MTO and/or other EU-level fiscal rules;
- 3.5 Monitoring and accountability;
- 3.6 Response to the Covid-19 pandemic.

There is not much information available about the actual functioning of medium-term budgetary frameworks. The Commission gathers information on national budgetary frameworks in its Fiscal Governance Database, mostly from the perspective of institutional set-up rather than about how they actually work. The Budgetary Frameworks Directive has no explicit requirements for the way national medium-term expenditure objectives should be set up. Some requirements in the EU legal framework concerning MTBFs fall short of the international standards and best practices set by the IMF and the OECD[1]. For this reason, the parallel audit questions addressed the actual implementation of MTBFs and their effectiveness in the budget process and annual budgeting.

There is broad consensus in the literature, stakeholders' views and the Commission's analytical work that fiscal rules enhance budgetary discipline. National fiscal rules (NFRs) should promote compliance with EU rules, medium-term planning, fiscal discipline and countercyclical policies. Directive 2011/85 sets overarching objectives to guide the design of NFRs and ensure consistency with the EU fiscal framework. Out of 62 general government rules in place in 2018, about three-quarters replicate or contain important features of the corresponding EU rules. About 51% of them are budget balance rules, 30% are debt rules, and only about 18% are expenditure rules[2].

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[1] ECA Special Report 22/2019 EU requirements for national budgetary frameworks: need to further strengthen them and to better monitor their application

[2] Review of the suitability of Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2020:211:FIN

In February 2020, the Commission published a review of Directive 2011/85/EU on medium-term budgetary frameworks[2]. The Commission reported that progress relating to MTBFs had been significant overall. However, progress has been uneven and there is room for improvement, for example by linking multiannual budgetary targets with the annual budget, involving Independent Fiscal Institutions (IFIs) in preparing national medium-term fiscal plans (NMTFPs), and the level of detail included in the NMTFPs. The impact of Directive 2011/85 on the consistency of annual budgets with the medium-term budgetary plans seems to have been limited. Some Member States require their annual budget to comply strictly with the ceilings/targets in the MTBF. For more than half of the Member States, the link between the annual budgets and the NMTFPs is potentially weaker. While Directive 2011/85 lays down that annual budgets should pursue the medium-term fiscal course charted by the MTBF, its impact in terms of making MTBFs genuinely binding has been limited. As a result, annual budgeting remains the dominant driver of fiscal policy choices in most Member States and can still fairly easily override medium-term fiscal plans.

2 Medium-Term Budgetary Frameworks – mechanisms for planning central government expenditure for future years

Medium-Term Budgetary Frameworks[3] are fiscal arrangements or institutional policy instruments extending the horizon for fiscal policymaking beyond the annual budgetary calendar. The Budgetary Frameworks Directive (2011/85/EU) requires Member States to establish a credible, effective medium-term budgetary framework providing for the adoption of a fiscal planning horizon of at least three years, to ensure that national fiscal planning follows a multiannual fiscal planning perspective. The Directive aims for effectiveness in promoting budgetary discipline and the sustainability of public finance.

In the parallel audit, the requirements of the Directive were applied to the level of central government and general government expenditure. The question was whether national implementation of the MTBF is set in such a way that it serves as a concrete tool for planning budget expenditure. In this report, the terms 'expenditure objective' or 'forecast' are used when referring to translating the MTBF into concrete budget expenditure targets at the central government or general government level. The term 'MTBF' is used in the report when referring to a set of multiple national medium-term rules or targets that are set in the national medium-term fiscal plan.

During the audit, the SAIs defined in greater detail how general government or central government expenditure is planned in each country, in accordance with the requirements of the Directive. The following information boxes contain short descriptions of the audited expenditure objective or forecast in each country:

Finland

In Finland, central government expenditure ceilings have been set at the beginning of each four-year parliamentary term since 2003. The Government decides, usually in the Government Programme, on parliamentary term spending limits, i.e. a limit in euros for budget expenditure for the last year of the parliamentary term. The spending limit is set in real terms. At the same time, the Government decides the rules governing the spending-limits procedure. The spending-limits framework covers approximately 80% of the central government budget and 35-40% of total public expenditure. For instance, automatic stabilisers (mainly expenditure related to unemployment), financial investments and interest payments on central government debt are left outside the expenditure limits.

One objective of the spending-limits framework is to limit the total amount of central government expenditure and to limit the burden for taxpayers. The aggregate ceiling does not bind decisions about individual expenditure. Another objective of the spending-limits system is to break the link between government expenditure and revenue so that an increase in revenue estimates does not lead to a higher level of expenditure.

An expenditure ceiling and spending-limit rules are not statutory, but they are set out in the Government Programme and in the first General Government Fiscal Plan for each parliamentary term. Even if the rule is not legally binding, all parties in Parliament have been strongly committed to maintaining it. However, in 2020 the system was set aside for the first time as a response to the Covid-19 pandemic, and returning to the system in 2021 has not been successful. For the first time since 2004, the spending-limit rule was broken, after an unprecedented Government decision to increase the spending limit for 2022 and 2023.

The spending-limit rule is the most influential fiscal rule at the operational level.

[3] It is important to note the difference between MTBF and MTFF, *Medium-Term Fiscal Framework,* which is part of the EU Fiscal Framework. MTFF refers to a mechanism for setting multi-year macro-fiscal objectives and targets, e.g. a Medium-Term Objective.

France

Under the terms of the organic law of 2012, the French medium-term budgetary framework is set by the public finance programming laws (PFPLs) that set out the multiannual trajectory of actual balances of sub-sectors of the public administration, and present financial trajectories in the form of six expenditure targets.

For each of the programming exercises, the PFPLs must set four expenditure targets: for the central government, the PFPLs must set an expenditure cap on a three-year basis and an expenditure cap for each programme of the general budget. For social security, the PFPLs must determine an expenditure target for the basic compulsory social security schemes ('Robss') and the national health insurance expenditure target ('Ondam').

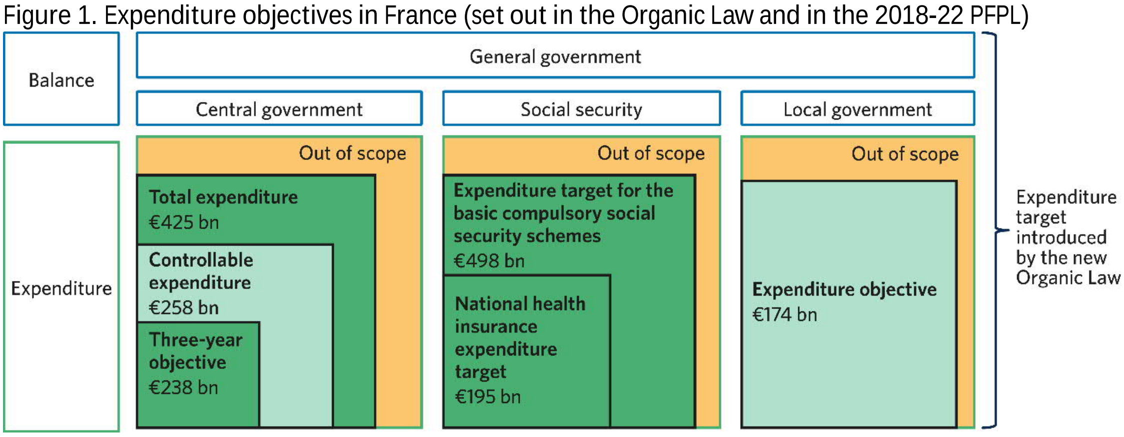
In addition to the controllable central government expenditure objective, the "total central government expenditure target" includes programmes containing "expenditure on investments in new technologies", the debt burden, levies on revenues intended for the European Union and territorial authorities, as well as the fraction of value-added tax allocated to the local government, the pension trust account, and special account programmes mainly involving contributions to local government or financial commitments.

Thus, in total, the trajectory of public administration spending has been broken down since 2018 according to six objectives. As shown in the picture, four of the six expenditure objectives are set out in an organic law rather than in an ordinary law (in bright green, the expenditure rules provided for in the 2012 Organic Law; in light green, the norms not provided for by organic provisions).

An organic law on the modernisation of public finance management aimed at strengthening the multi-year public finance strategy was adopted in December 2021, and will apply to the next PFPL that is due to be adopted in 2022. This new mandatory framework will force governments to submit, in each PFPL, a general government expenditure target expressed in billions of euros and an expenditure growth target expressed in terms of volume, which shall then be set out in the introductory article of the finance law and the social security financing law. Each year, the settlement bill (voted in May) will present how the targets were followed, and show the gap between the PFPL, the annual budget voted and the budget executed.

For specific fields (military, research and innovation, and justice), the Constitution allows Parliament to vote for programming laws that can cover up to 10 years – thus creating a medium-term expenditure ceiling specifically for these expenditure aggregates. According to the new reform of the French IFI (*Haut Conseil des finances publiques*), the HCFP will give its opinion on the draft budget and financing programming bills.

Figure 1. Expenditure objectives in France (set out in the Organic Law and in the 2018-22 PFPL)



Italy

Italy's medium-term budgetary framework is mainly regulated by the Government Accounting and Public Finance Act (Law No 196/2009 and subsequent modifications, the "public accounting law"). Other relevant provisions on this topic are laid down in the "Provision for the application of the balanced budget principle pursuant to Article 81.6 of the Constitution" (Law No 243/2012 and subsequent modifications, the "reinforced law").

The mid-term budgetary framework is outlined in the Economic and Financial Document (the "MTB document"), due in April each year. With regard to the expenditure side, the MTBF provides forecasts for the current year and for at least the following three years, on a rolling basis (i.e. a new year is added annually at the end of the period covered by the previous projection). Expenditure forecasts are not regarded as binding caps on the rate of growth.

The explicit policy goal in the Italian MTBF is to ensure that revenue and expenditure trends, taking into account the budget package to be approved, allow for compliance with fiscal objectives, as defined in accordance with European regulations (in terms of structural balance, the level of public debt, and the expenditure rule). For the purposes of complying with the rate of expenditure growth set at European level and achieving budget targets, financial and budgetary planning documents must specify the level of general government expenditure for the three-year period to which they refer.

The expenditure forecasts are then updated with the Update to the Economic and Financial Document in September, in the light of the expected financial impact of the measures of the next budget package, aimed at achieving the targets defined in accordance with EU regulations.

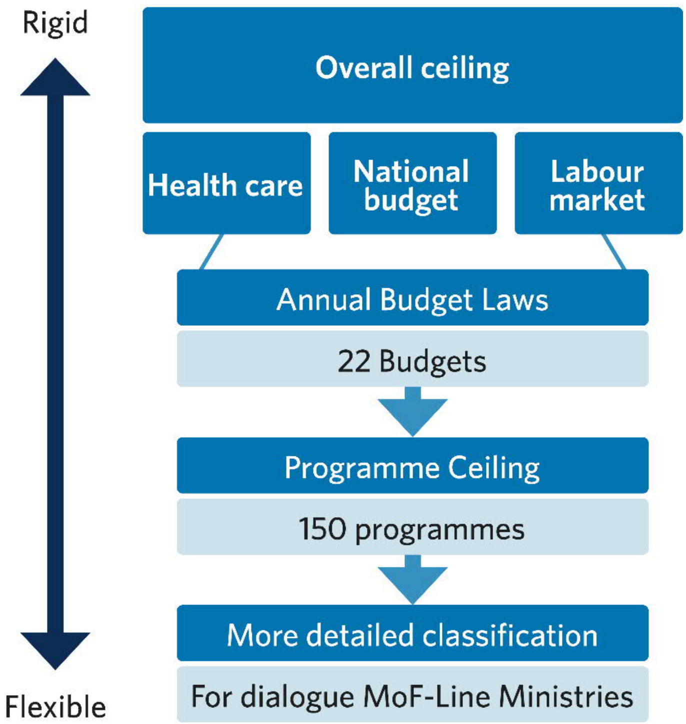
Specific ceilings are set for certain expenditure aggregates. For instance, healthcare expenditure is regulated by the Health Pacts which are discussed and agreed between the central government and regional administrations, which are directly responsible for managing and providing the health service. The agreements cover a three-year horizon and are updated every three years. Under the pact, the evolution of healthcare expenditure over the following three years is capped. The maximum expenditure envelope for the healthcare sector is set in nominal terms.

The Netherlands

The 2013 Sustainable Public Finances Act (Wet HOF) states that the government follows a trend-based fiscal policy. The Wet HOF codified the basic elements of the fiscal policy that was already implemented in 1994. An objective of the trend-based fiscal policy is to control government expenditure. One of the principles of the Netherlands' trend-based fiscal policy is fixed expenditure ceilings for the duration of the four-year government term. These ceilings are based on macro-economic forecasts of the CPB and the coalition agreement. The overall ceiling is divided into three sub-ceilings for the national budget, healthcare and social security. The latest coalition agreement from December 2021 also introduced a fourth sub-ceiling for investments. Expenditure ceilings in annual budget laws correspond to the aggregate ceilings under which they reside, although this relationship is complex due to differences in the definition of expenditure. Other important elements of the trend-based fiscal policy are automatic stabilisation, budgetary rules, and one main decision-making moment a year. The expenditure and revenue sides of the budget are strictly separated during the execution of the coalition agreement. Revenue windfalls are not generally used to finance additional expenditure; rather, they are used to reduce the deficit. Expenditure windfalls are used to compensate for expenditure setbacks elsewhere in the budget. This allows for a countercyclical fiscal policy in which deficits increase during an economic downturn and decrease (or achieve surplus) during periods of economic growth (automatic stabilisation). Thus, the system allows tax windfalls and setbacks to be automatically expressed in the financing gap, but within certain limits. These principles also aim to reduce budgetary and administrative turmoil during the execution of the budget in the four-year government term and the execution of the coalition agreement.

As a member of the EU, the Netherlands is subject to the budget balance and debt rules of the Maastricht Treaty and the SGP. The Wet HOF also codified its obligations under EU fiscal rules.

Figure 2. Framework of expenditure ceilings in the Netherlands



Portugal

The Portuguese MTBF model was introduced under the Budgetary Framework Law of 2011 (which applied between 2011 and 2020). Its scope covers four years of Central Government expenditure (financed by general revenues), in line with the budget balance forecasts of the Stability Programme and of the main budgetary policy documents approved by Parliament.

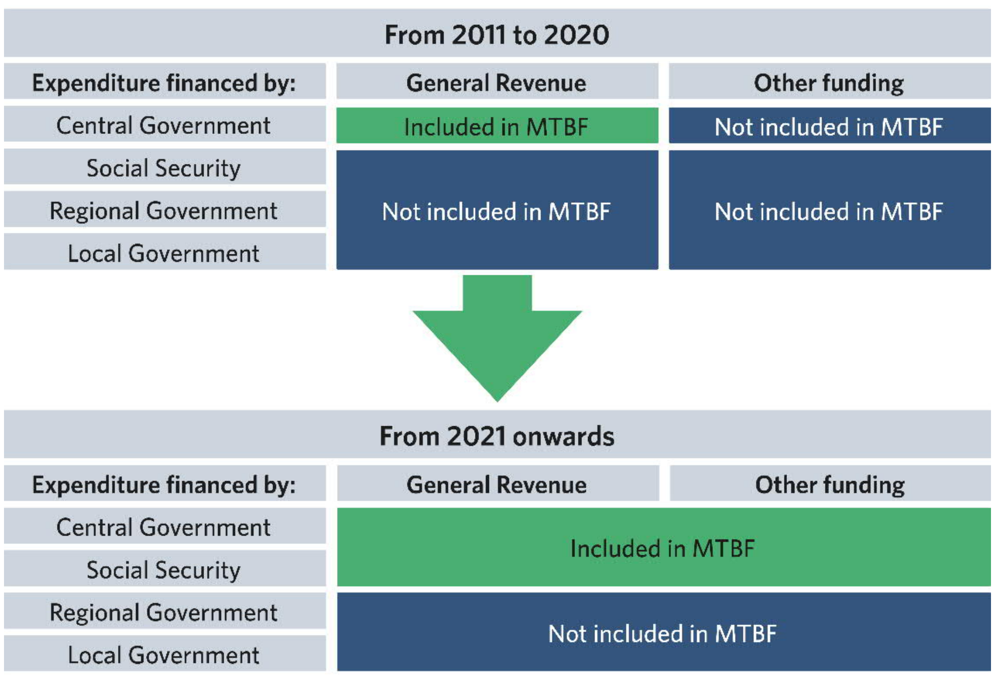
MTBF expenditure limits are set by a programme/Ministry in the first year. In the second year, the scope is reduced to cover each functional sector (bundle of programmes), and for the last two years a limit is set only for overall expenditure. The exact expenditure ceilings depend on the source of funding.

Although the MTBF expenditure limits are binding, they must be revised every year (during the following four years) within the scope of the State Budget approval process, in line with the update of the Stability Programme.

Conceptually, implementing the MTBF is driven by three major goals:
i. devising a medium-term expenditure rule in line with the Stability Programme;
ii. empowering budget management through a medium-term perspective (allowing public managers to have comprehensive financial resources);
iii. promoting multiannual programming by setting public policy priorities.

Since 2021, a new MBTF model has been based on a new budgetary framework law. It is more comprehensive than the previous one because it includes all expenditure, regardless of the source of financing, as well as social security expenditure (pensions, subsidies, and social benefits). The MBTF is binding for the first year and indicative for the following four years, and is subject to annual updates. The expenditure ceiling of the social security sub-sector may be exceeded for the payment of benefits to which beneficiaries are entitled and which are related to the economic cycle. For the time being, the local and regional levels are exempt from the national MTBF, but have their own MTBF, adapted to the local and regional budgetary situation. The changes to the scope of the expenditure limits considered are the following:

Figure 3. Scope of the MTBF in Portugal



Slovakia

Fiscal rules at the national level are incorporated into legislation and consist of the “debt brake”, the balanced budget rule, and the limit of State budget expenditure. The Constitutional Act on Fiscal Responsibility[4] sets a limit for the amount of general government debt – the so-called “debt brake”. Its aim is to prevent Slovakia’s debt from growing to a critical level by applying sanctions and corrective mechanisms. The law sets the upper limit of general government debt at 50% of GDP, while a transitional provision applied until the end of 2017 referred to an upper limit of 60% of GDP and its subsequent decrease by one percentage point annually.

In Slovakia, the general government’s budget is based on a three-year horizon. The State budget approved by Parliament deals with the coming year, and the general government budget with the next three years. The budget is no longer understood only as an accounting tool, but also performs other functions related to the governance of expenditure, the achievement of objectives and the monitoring of added value for citizens (performance budgeting). Expenditure limits in Slovakia are established, and are part of the State budget. Expenditure ceilings were not implemented in Slovakia during the audited period. However, they were publicly discussed, and in 2020 an amendment to the Act on Fiscal Responsibility was prepared to introduce expenditure ceilings.

The basic preconditions for processing the general government budget are the macroeconomic forecast, the medium-term revenue framework, the medium-term fiscal framework (which contains expenditure targets), and the medium-term expenditure framework.

When medium-term expenditure targets are set, total expenditure, the deficit, debt, debt service costs, and the identification and quantification of potential risks are determined.

Sweden

The expenditure ceiling was implemented in the 1997 budget year. The ceiling is a maximum level of expenditure allowed in the central government budget and the off-budget expenditure in the old-age pension system, set by the Swedish parliament (the Riksdag) three years ahead. The ceiling is set in nominal terms.

Each year, the Government is required by law (the Budget Act) to propose a level for the ceiling for the third budget year ahead. The level is then set by the Riksdag. The Budget Act also requires the Government to take measures or to propose necessary measures to the Riksdag to avoid the ceiling being exceeded. There should be a budgeting margin between the ceiling and the expenditure capped by the ceiling, primarily intended to act as a buffer if expenditure does not grow as expected on account of the development of the economy. There is no formal obstacle for the Riksdag to alter a level that has been set previously. It has become a practice not to alter the level unless there is a newly elected Government or if there are new and completely different external circumstances. The ceiling can also be altered due to technical budget rearrangements.

The ceiling is part of the Swedish fiscal policy framework. The framework consists of several targets and principles that steer the design of fiscal policy and are intended to ensure the long-term sustainability and transparency of fiscal policy. One important purpose of the expenditure ceiling is to create conditions for achieving the surplus target (net lending in the general government sector 1/3 per cent of GDP on average over an economic cycle), i.e. to create conditions for a long-term sustainable fiscal policy. The level of the expenditure ceiling is also intended to promote a desirable long-term development of central government expenditure. Along with the surplus target, the expenditure ceiling governs the level of the total tax take and helps to prevent a situation in which the tax take must be increased gradually on account of insufficient control of expenditure.

[4] https://www.rrz.sk/wp-content/uploads/2021/05/constitutional_act_493_2011.pdf

2.1 MTBF categories covering public expenditure

MTBFs that cover public expenditure can be roughly divided into four categories[5]:

1. Indicative framework: A framework in which updates of medium-term estimates can be made without reference to the same estimate set in the previous year, and in which the appropriations in a government's annual budget proposal for t + 1 are not reconciled against the medium-term estimates for t + 2 made in the previous year (or previous budget update, e.g. a prebudget report).
2. Binding framework: A framework that holds government accountable for the multi-year expenditure parameters (estimates or ceilings) that are open for revision. Accountability means that some active measure or action is required if there is evidence that the previously set expenditure parameter is going to be exceeded. A fixed framework is a subset of binding frameworks in which medium-term expenditure limits are set but not subsequently revised.
3. Appropriations: Maximum limits for individual expenditure items as defined in the budget.
4. Expenditure ceiling: Maximum limit on aggregate expenditure.

In the following table, the MTBF systems of the countries participating in the parallel audit are divided according to these categories. The category is selected based on the analysis carried out by the participating SAIs, and could also be interpreted differently. Some MTBF systems might belong to more than one category, in which case only the most representative category is selected. In the case of expenditure ceilings, the category is selected when the ceiling is set in aggregate. If the ceiling is not in aggregate, then a binding framework is selected.

Table 1. Categories of audited expenditure objectives or forecasts by country

MTBF CATEGORY	COUNTRY
INDICATIVE FRAMEWORK	-
BINDING FRAMEWORK	France, Italy, Portugal
APPROPRIATIONS	Slovakia
EXPENDITURE CEILING	Finland, the Netherlands, Sweden

Further explanation of the factors that were considered when choosing the MTBF category for each country:

Finland: The spending-limits system is based on an expenditure target that is set in euros for the last year of the Parliamentary term and that sets an aggregate limit for expenditure.

France: Under the terms of the organic law of 2012, the French medium-term budgetary framework is set by the public finance programming laws (PFPLs) that set out the multiannual trajectory of actual balances of aggregate and sub-sectors of the public administration, and present financial trajectories in the form of six expenditure targets. The next PFPL will also have to submit an expenditure target expressed in billions of euros for the general government and for each sub-sector (central government, social security, and local government).

Italy: With regard to the expenditure side, the MTBF provides forecasts for the current year, and for at least the following three years, on a rolling basis (i.e. a new year is added each year at the end of the period covered by the previous projection). Expenditure forecasts are not regarded as binding caps on the rate of growth.

Netherlands: The Netherlands has a multiannual overall expenditure ceiling divided into three aggregate sub-ceilings. These ceilings are set in compliance with fiscal policy thresholds and are politically binding as they are an integral part of the four-year coalition government agreement.

[5] As in the IMF publication *Public Financial Management and Its Emerging Architecture,* 2013, article by Harris, Hughes, Ljungman and Sateriale

Portugal: The Portuguese MTBF is classified as a flexible binding model because although the expenditure limits are binding, they are reviewed annually for the following four years, within the scope of the State Budget approval process.

Slovakia: In Slovakia, the general government's budget practice is based on a three-year horizon. The State budget approved by Parliament deals with the coming year, and the general government budget with the next three years. Expenditure limits in Slovakia are established, and are part of the State budget.

Sweden: The expenditure ceiling is a maximum level of expenditure allowed in the central government budget and the off-budget expenditure in the old-age pension system, set by Parliament (the Riksdag) three years ahead. The ceiling is set in nominal terms.

The Budgetary Frameworks Directive notes the need to comprehensively cover public finances with budgetary frameworks. Attention should also be paid to contingent liabilities and the operations of those general government bodies and funds which do not form part of the regular budgets at sub-sector level but which have an immediate or medium-term impact on Member States' budgetary positions. In the audit criteria, a high level of coverage was expected to be an important aspect of the expenditure objective or forecast system.

The expenditure objective/forecast covers close to 100% of central government expenditure in Italy and Slovakia. In Finland, the Netherlands, Portugal and Sweden, most central government expenditure is covered by the expenditure objective, but 5–25% remains outside the expenditure objective.

Coverage of the expenditure objective in relation to general government expenditure varies in the audited countries to a greater extent. In Italy and Slovakia, the coverage is still 100% of general government expenditure. In France and the Netherlands, the expenditure objective covers between 80% and 90% of general government expenditure. The coverage is estimated to be around 55% of general government expenditure in Portugal and Sweden. In Finland, the coverage of the expenditure objective is closer to 35% of general government expenditure.

In France, the new organic law created a new overall expenditure target which covers all general government expenditure. It also introduced three expenditure targets: for central government, social security, and local government expenditure. This is in addition to the "golden rule" of local government expenditure: voted budgets on current expenditure must be in balance in nominal terms, and borrowing capacity can only finance investment and not current expenditure. As of today, it can be estimated that more than 85% of general government expenditure is covered by multiannual expenditure targets. In practice, institutional surveillance is strong on the national health insurance expenditure target and the central government controllable expenditure target, i.e. 35% of general government expenditure, while the other objectives are subject to less scrutiny.

The expenditure objective can be legally binding or based on political commitment. In both cases, political commitment to the system is important, as the laws can be subject to changes. Certain elements of the MTBF take place at the constitutional level in Slovakia. The expenditure objective or forecast is established in some detail in legislation in France (both organic law and ordinary law), Italy, Portugal and Sweden. The expenditure objective is based mostly on political commitment in Finland, Italy and the Netherlands. Political commitment to the expenditure objective has been strong in Finland, the Netherlands, Portugal and Sweden. However, in some countries (Finland, the Netherlands), there have been worries after the Covid-19 pandemic that political commitment to the system might be weakening.

The most common expenditure item left outside expenditure objectives is automatic stabilisers, i.e. counter-cyclical social security benefits such as unemployment benefits (Finland, the Netherlands, Portugal). Other expenditure items that are commonly left outside are central government loan interest (Finland, France, Sweden). This is mainly due to the fact that interest does not fully fall under the control of the Government. Local government expenditure is not covered in some countries (Finland, Portugal, Sweden). In some countries, expenditure that does not affect the deficit in Economic and Monetary Union (EMU) terms is not considered to fall within the objectives, e.g. repayments of government debt, capitalisation of state enterprises, or financial investments (Finland, the Netherlands, Portugal).

During crises, the scope of the expenditure objective has been changed in some countries to exclude certain expenditure. During the financial crisis of 2007–2008 and beyond, it was decided in the Netherlands that any expenditure and revenue resulting from government interventions in the financial sector would not be part of the expenditure ceiling. During the Covid-19 pandemic, it was decided in Finland to exclude all direct expenditure related to the pandemic, such as vaccines and testing.

3 Audit results (Main audit question: Are medium-term expenditure objectives set up effectively and transparently in the budget process?)

3.1 Integration into the budget process

The OECD Principles of Budgetary Governance were used as audit criteria when assessing the integration of the MTBF into the budget process. The second principle, “Closely align budgets with the medium-term strategic priorities of government” addresses integration into the budget process. According to the criteria, the budgetary process should incorporate the medium-term horizon in terms of expenditure. Objectives should have real force in setting boundaries for expenditure, and include sufficient institutional incentives and flexibility to ensure that they are respected. This respect is understood as a commitment by both the administration and political decision-makers to follow the expenditure objective, i.e. there are no attempts to make spending decisions outside the boundaries set in the objective or to use in-built flexibility without justification. The objectives should be set in line with top-down budgetary constraints and government policies, and the process should include all relevant institutions at the centre of government.

The SAIs analysed how well the expenditure objective or forecast was integrated into the budget process, and whether there was real force in setting boundaries for expenditure. The expenditure objectives that belonged to the category of expenditure ceilings seemed to have the highest level of integration into the budgetary process, and also set a boundary for the expenditure (Finland, the Netherlands, Sweden). In other categories, it was more difficult to assess whether the expenditure objective actually did set a boundary for expenditure, due to the different ways the systems operate. All SAIs stated that the expenditure objective or forecast works well on paper. However, some critical aspects can be detected in its practical implementation (Italy, Slovakia, France). One of the problems highlighted was how fiscal targets were translated into more operational budgetary objectives (Italy, Portugal). MTBF targets may not be converted into clear budgetary thresholds or ceilings, expressed in budgetary accounting language and functional classification. In all the assessments made by the SAIs, it appeared that the expenditure objective has some level of integration into the budget process, but the non-binding nature of the system or annual revisions make it difficult to assess whether there has been real force in setting a boundary for expenditure. Some SAIs (Italy, France, Slovakia) mentioned that the spending review process had been a useful tool when linked with the MTBF to allow for more efficiency and integration into the budget process.

MTBFs should extend the horizon for fiscal policymaking beyond the annual budgetary calendar. Most SAIs acknowledge that even if the budget is traditionally based on an annual perspective, the expenditure objective has also brought more forward-looking aspects into annual budgeting. The SAIs of Finland, the Netherlands and Sweden consider the forward-looking medium-term perspective to be at least as relevant in budgeting as the annual perspective.

The expenditure objective or forecast was noted to have both top-down and bottom-up elements in most countries (Finland, the Netherlands, Slovakia, Italy, Portugal). Top-down processes are usually derived as a response to EU fiscal rules. However, the link between the bottom-up and the top-down approaches is often weak, as reconciling different types of information has been difficult.

MTBFs and their related expenditure objectives should allow for flexibility in times when unforeseen events occur during the planning timeframe. A certain amount of flexibility also strengthens political commitment, as the expenditure objective should not restrict all decision-making on budget expenditure. All expenditure objectives are ultimately based on political commitment. The level of commitment and the use of expenditure objectives in decision-making on annual budgets vary in different countries. Some systems have more built-in flexibility, whereas others use escape clauses that are activated only in predetermined circumstances. The quality and correctness of the underlying data could be argued to be more important than the final decisions on expenditure, which are considered to reflect the political landscape at the time. However, breaches of EU fiscal rules are not taken lightly. In the national debate and budgeting, the focus has been on ensuring that the budgets are in line with EU legislation.

3.2 Effectiveness at achieving stated goals

In order to audit the expenditure objective's effectiveness at achieving the stated goals, the SAIs applied different criteria reflecting their national systems, e.g. targets limiting the expenditure or expenditure growth, counter-cyclical spending, or limiting the deficit/debt. As these goals are determined at national level, this chapter will go through each audited country individually.

Finland

The level of expenditure has remained under the limit set by the Government in 2004–2019. Some inconsistencies and breaches were noted in applying the principles of the spending-limits rule during the parliamentary term, although they did not influence how the main national objectives of the spending limits were achieved.

The national objectives for the expenditure ceiling are (1) to limit expenditure growth, or "the taxpayers´ burden"; (2) to break the link between revenue and expenditure so that an increase in revenue does not lead to an increase in expenditure; (3) to ensure balanced budgets over the long term and countercyclical measures in the short term; and (4) to signal a prudent expenditure policy to markets (debtors).

The audit findings regarding the aforementioned objectives were as follows:

(1) and (4): There was some growth in real-term expenditure over time. In relation to GDP, expenditure has been stable. The system can be used to support a prudent expenditure policy.

(2) and (3): There was no evidence of increases in revenue leading to increases in expenditure. However, revenue has not been at the level of expenditure since 2008, which has led to an increase in debt. It looks like countercyclical measures have not sufficiently supported gathering a budget surplus during periods when the economy was growing. It was recommended that, in the future, the revenue level should be more directly linked to the expenditure level.

France

While the principle of “annuality” is legally and practically central to the governance of public finances, France has adapted and overcome its historical annual framework in order to comply with its European commitments, and has gradually adopted a normative framework aimed at conducting public policies over a medium-term timeframe and ensuring the sustainability of public finances. Public finance programming laws were created by the 2008 constitutional revision. Article 34 of the Constitution thus provides that the "multiannual orientations of public finances are defined by programming laws". Without limiting itself to this objective alone, the Constitution specifies that these orientations "fall within the objective of balancing the accounts of public administrations". Therefore, it is important to note that the constitutional reform of 2008 has legally aligned the mechanisms that underpin the MTBF.

The programming laws have always provided for a stabilisation and then a reduction in the ratio of public debt to GDP. However, the objectives set have not yet been fully achieved in terms of structural adjustment, expenditure, revenue or public debt targets.

The targets for the evolution of public expenditure were met or nearly met for the 2011–2014 and 2012–2017 PFPLs. With regard to the 2014–2019 PFPL, the increase in public expenditure observed over the 2015–2017 period led to a marked overshooting of the target, with public expenditure in volume terms increasing over the entire period by almost 1.2%, whereas it was initially expected to be contained under 0.3%.

The *Cour des comptes* (Court of Audit) recently pointed out elements that may prevent an efficient steering of public finance and public expenditure. The standards for the progression of State expenditure set in the budget law, the objectives for the evolution of health insurance expenditure provided for in the Social Security Finance Acts, and the contract mechanisms for the operating expenditure of local government remain incomplete. Spending norms do not prevent the emergence of deviations from medium-term trajectories, as annual or amending financial laws may themselves decide to deviate from them. Moreover, these regulatory mechanisms have leakage points, and the objectives they set can be achieved through multiple bypasses. For central government, these bypasses involve debudgetisation or the creation of tax expenditure; in the case of health expenditure, by mobilising revenue outside its scope. For local administrations, the contract mechanism leaves open the possibility of transferring charges to entities (inter-municipalities, local public establishments) or expenditure lines (ancillary budgets) not subject to contracts. Overall, the fragmented financial architecture of public administrations, combined with the fragmentation of powers and a distribution of revenues that is difficult to understand, hampers understanding of the respective balances of the different administrations, and harms the articulation of public policies between administrations and the coordinated management of their expenditure, revenues and debt.

Italy

On the one hand, the non-binding nature of the Italian MTB document ensures a high degree of flexibility in addressing the new priorities and the changing economic background; on the other hand, it hinders its effectiveness in governing future public expenditure trends. The possibility of reviewing and updating the expenditure forecasts every year, depending on the legislative and macroeconomic outlook, increases uncertainty in the growth path, making it hard to measure the degree of effectiveness of the MTBF.

A comparison of the expenditure forecasts made over time (in the sequence of MTB documents) for the same year can help to assess the framework's ability to keep public expenditure under control. However, it must be acknowledged that, besides a revision of the projections, there are other factors that can affect the steadiness of MTBF projections over the years, such as any modifications in the extent of general government or changes in data for statistical reasons (e.g. switching from a European System Accounts version to another one).

Although the Italian MTBF proves to be effective in the forecasting process, it would benefit from the introduction of a more stable operational expenditure rule/benchmark, besides the European fiscal rule, which is only focused on the current and the following year, and depends on unobservable variables with frequent revisions. The definition of expenditure ceilings for a multiannual horizon would help to manage public spending, and would add pressure on public bodies to carry out effective spending reviews on a regular basis in order to comply with the expenditure caps and free resources for new priorities. Currently, the framework appears to be mostly focused on the achievement of fiscal targets (the structural balance in line with the MTO or with the convergence path). In such a framework, expenditure control is not fully guaranteed, since the structural balance objective can be met even if public expenditure grows at a higher rate than expected, provided that the excess is financed with new or higher revenues. In this respect, it must be underlined that the risk of an uncontrolled increase in public expenditure is mitigated by the need to respect the European expenditure benchmark, which does not allow for high-expenditure growth rates.

The Italian legal framework ensures that new expenditure is properly financed, since every bill has to be accompanied by a prospect which records the impact of each measure on the basis of three accounting systems: legal authorisation of commitments, and the impact in cash terms and in terms of ESA2010. However, while preserving the budget balance, such legal requirements do not prevent public spending from exceeding forecasts.

Moreover, to enhance its effectiveness, a newly introduced expenditure rule should provide detailed sub-targets at least for the current expenditure aggregate. This would help to preserve the quality of public spending, limiting the risk that deficit targets are pursued at the expense of public investments, as was the case in Italy several times during the 2010–2019 period.

Lastly, under an effective expenditure rule, ceilings should be further detailed for general government subsectors in order to increase their responsibility and accountability in preserving sound and sustainable public finance.

The Netherlands

The trend-based fiscal policy aims to enhance control of public finances, contribute to economic stability, and ensure an efficient allocation of resources. Expenditure ceilings are part of the fiscal policy and contribute to the goals. The expenditure ceilings help to control public finances. As for the years 2014–2019, the Government reported that it had met the overall expenditure ceilings set at the start of every budgetary year.

However, the Council of State noted that the Government did not always comply with the national fiscal rules. In 2019, the Government raised the expenditure ceiling that was set at the start of the government's term of office. This also happened in 2020 because of the Covid crisis, since the Government considered it unwise to cut regular expenditure to fund support packages. In 2018, the State Council noted that the Government covered the structural budgetary effects of the new policy with windfall benefits from social security and health care. The State Council questioned if this was in line with the principle that windfalls should not be used for new policies.

An evaluation of the fiscal policy by the Studiegroep Begrotingsruimte (SBR) concluded in 2016 that the economic crisis after 2008, the tightening of the European budget agreements, and political fragmentation in Parliament had had a major impact on the conduct of fiscal policy. Of the three main fiscal policy objectives (healthy public finances, efficient allocation, and stable economic growth), the emphasis had been on sound public finances. The SBR concluded that this had been at the expense of the other goals.

In our 2021 audit of budget programmes under the National Budget sector, we stated that a focus on spending control and thus on the enforcement of expenditure ceilings is a risk for the quality of departmental bottom-up forecasting processes, which are important for conducting efficient allocation. Also, a one-sided focus on spending control can divert attention from the efficiency and maintenance of public services.

Portugal

The Portuguese MTBF basically fulfils a formal mission of establishing limits for central government expenditure in the medium term, supported by information provided through broad institutional coordination. The annual revisions of the MTBF limits, based on State Budget forecasts, point to its subordination to the annual cycle, contrary to the purpose of an expenditure rule that should limit the expenditure increase over a multi-year horizon.

There is no clear link between expenditure limits, budgetary objectives and public policy priorities.

The Budgetary Framework Law does not include any rule to prevent pro-cyclical spending, namely a rule on how the revenue collected above its forecast should be used.

The expenditure limits were met in the 2016–2019 period. The execution of expenditure was below the limits set both in the initial MTBF and in the annual updates, with an average execution rate of 98.1% in the period. Between 2016 and 2019, expenditure subject to the limits set in the MTBF increased by 7.4% (€3,554 million).

However, the sub-limits for some budget programmes – the Basic and Secondary Education and Health programmes – were not met, which revealed deficiencies in the budgeting for those programmes.

Regarding the revisions of expenditure limits, the State Budget reports include justification for the changes (i.e. due to new policy measures being adopted in the State Budget and other circumstances identified at budget programme level). However, this justification is insufficient because it only covers the budget year and is not always quantified.

Slovakia

Slovakia failed to meet its fiscal objectives during the audited period. The MTO in the form of a structural balance of 0.5% of GDP was not achieved, nor was it possible to maintain the trajectory towards it, and achievement of the objective was postponed. The average deviation between the predicted and actual structural balance reached 0.8 percentage points and, in the case of consolidation efforts, 0.6 percentage points. The development of the gross debt ratio in relation to GDP maintained the predicted downward trajectory, despite the average deviation between actual and predicted values at 1 percentage point (GDP). Actual total general government expenditure was more than predicted throughout the period, with an average annual variation of €2.49 billion, or 6.8% of actual expenditure.

In our audit, we also focused on lower-level objectives (goals/targets), and the goals of individual public policies – not individual goals but the system of setting, achieving and evaluating them, which is implemented through so-called programme (performance) budgeting. Budget chapters approach programme budgeting differently, while the relevant methodological instructions from the Ministry of Finance (MoF) are not followed and quality is very uneven. We also identified significant changes in spending over the year, which indicates a lack of budgetary management. Programme budgeting is used to collect and monitor data of varying quality, and there is no emphasis on a medium-term framework, nor a consistent approach. Through programme budgeting, budgeted and spent resources are linked to their purpose, the objective of their use and monitoring by indicators. Programme budgeting in Slovakia is working only partially.

Sweden

The Swedish expenditure ceiling has never been exceeded. In the years when the budgeting margin was small (especially in the early 2000s), the Government used measures on several occasions to prevent the ceiling from being exceeded. The latest example was in 2015, when the Government – among other things – moved expenditure to 2015 to avoid exceeding the level in 2016, when expenditure was expected to increase markedly due to the significant increase in immigration. The Government has been criticised by the Swedish Fiscal Policy Council and the Swedish National Audit Office for some of the measures taken.

One important purpose of the expenditure ceiling is to create conditions for achieving the surplus target, i.e. to create conditions for a long-term sustainable fiscal policy. The level of the expenditure ceiling is also intended to promote desirable long-term development of central government expenditure. Evaluating this is difficult, as there is no obvious measure of effectiveness or a target to follow up. Moreover, as the expenditure ceiling was one of several measures taken roughly at the same time, it is difficult to evaluate the impact of individual measures.

However, the National Audit Office's assessment is that the expenditure ceiling has had a disciplining effect on the expenditure trend (the long-term decrease in central government expenditure as a share of GDP). At the start, in 1997, the expenditure ceiling's share of GDP was 34 per cent. In 2019, the share was 27 per cent. This is partly because the ceiling has been a restriction in budget work, and partly because the ceiling indirectly required improved expenditure control. In addition, the Government has not utilised large parts of the occasionally substantial budgeting margin. Also, Swedish public finances have improved substantially since the expenditure ceiling was introduced. From 1997 to 2019, average net lending in the general government sector amounted to 0.4 per cent of GDP. Moreover, Maastricht debt amounted to 67 per cent of GDP in 1997, and by 2019 the share had fallen to 35 per cent.

3.3 Relationship with other national budgetary objectives

The OECD Principles of Budgetary Governance state that expenditure objectives should support a sound[6] and sustainable[7] fiscal policy. This requires expenditure objectives or forecasts to be clear and useful in aligning policies with available resources.

Two SAIs confirmed that there is a direct link between the expenditure objective and other national budgetary objectives (Italy, Slovakia). The explanation for this was that public policy objectives were based on budgetary constraints imposed by fiscal budgetary objectives. Either the constitution defined the national budgetary and fiscal objectives on which budgetary planning was based (Italy), or the national objectives and MTBF objectives (Slovakia) were the same. It can be noted that, in both cases, the practical implementation of the MTBF included annual flexibility, which made it more difficult to assess whether the MTBF was a functional tool in achieving other national objectives.

Four SAIs answered that the expenditure objective was to some extent connected to other national budgetary objectives, although there were also discrepancies (France, Finland, Sweden, the Netherlands). One question that was brought forward concerned the coverage of the expenditure objective and other national budgetary objectives. In Sweden, in addition to the expenditure ceiling, there is a surplus target, a debt anchor, and a requirement for local governments to maintain a balanced budget. The budgetary policy targets with the widest coverage are the surplus target and the debt anchor. The expenditure ceiling limits expenditure in two out of three sectors in the general government, i.e. expenditure in central government (excluding interest on central government debt) and the old-age pension system. The local government balanced budget requirement covers the third sector in the general government. The budgetary policy targets are interconnected, although covering different parts of the general government sector. Despite the link to other national budgetary targets, the level of the expenditure ceiling is not derived directly from budgetary policy targets. The considerations behind the Government's proposed level should include several factors, the surplus target being one of them. The level of the ceiling is an expression of the Government's view of how public commitment should develop. This highlights the complicated relationship between, on the one hand, the Government's possibility of pursuing the policy for which it has been given a mandate and, on the other, the need for fiscal policy rules that are intended to make it easier for the political process to take account of the long-term effects of the policy pursued as regards the public finances.

Also, all budgetary policy targets are not defined according to the same accounting system, which makes the connection more complex as the targets do not fully overlap (Finland, the Netherlands, Sweden). In the Netherlands, due to different definitions of SGP fiscal rules and the data from the budget system that Parliament receives, the latter needs to be converted by the MoF and the CBS specialists (Statistics Netherlands). Although this conversion is shown on the MoF website, the complexity reduces transparency.

In Finland, it was noted that, even though the expenditure objective was aligned with national budgetary objectives, the actual achievement of a balanced budget was dependent on some other national objectives, such as GDP or the employment level. However, these other objectives were often not met, and reaching the expenditure objective alone was not sufficient to achieve a balanced budget. There seems to be an imbalance between the measures that public decision-makers could control more directly (the expenditure objective) and those that were not under their direct control (GDP, employment).

In France, the objectives that underpin the MTBF set by the 2018–2022 PFPL are to reduce the public deficit, public expenditure, and taxes. The MTBF goes along with the transformation of public administration in order to reduce public expenditure by more than 3%. The public finance trajectory, expressed in terms of annual actual and structural balances, covers a period of at least three years. For each of the years of the programming period, the PFPL must also present the structural effort, i.e. the

[6] A "sound fiscal policy" is one which avoids the build-up of large, unsustainable debts, and which uses favourable economic times to build up resilience and buffers against more difficult times, so that the needs of citizens and stakeholders can be addressed in an effective and enduring manner.

[7] In a "sustainable fiscal policy", the change in expenditure level is under control (i.e. perhaps allowing a slow or steady rise/change, but no major unexplainable fluctuations), and there is no obvious conflict between the expenditure objective and fiscal policy targets (that would be manifested in meeting the expenditure objective while not meeting other national or EU fiscal objectives).

share of variation in the structural balance attributable to "discretionary" factors, which can be controlled by public decision-makers[8].

The SAI of Portugal noted that there was no clear connection between the MTBF spending limits and other budgetary objectives, i.e. the evolution of public deficit and debt. The relationship between the expenditure limits and other budgetary objectives, i.e. the budget balance estimate, is assured by the top-down approach, considering the process for setting expenditure limits. However, information about the reconciliation between the other budgetary objectives (in national accounts) and the expenditure limits envisaged in the MTBF (using cash-based accounting) is not disclosed in a clear and complete manner.

3.4 Relationship with the Medium-Term Objective and/or other EU-level fiscal rules

The Budgetary Frameworks Directive calls for procedures for establishing comprehensive and transparent multiannual budgetary objectives in terms of the general government deficit, debt and any other summary fiscal indicator such as expenditure, thus ensuring that these are consistent with any numerical fiscal rules provided for in Chapter IV. This can be interpreted so that medium-term expenditure objectives should also be consistent with any numerical fiscal rules. Consistency is further defined as compliance with the reference values on deficit and debt set in accordance with the Treaty on the Functioning of the European Union (TFEU). In this parallel audit, the criterion for consistency with numerical fiscal rules is also understood as the expenditure objective or forecast being consistent with the Medium-Term Objective (MTO).

As was mentioned in section 3.1, political decision-makers place emphasis on the question of whether national fiscal policy also follows EU-level fiscal rules. However, there seems to be no clear way to establish whether the expenditure objective in place is also in line with the MTO or any other fiscal rules.

The link between the MTO and the MTBF is established. However, the link between the national expenditure objective and the MTO, or the MTBF, is not reported. One explanation may be that these objectives describe different types of phenomena. Some countries may use the MTO as part of their MTBF, but there is still the question of translating the MTO and the MTBF into an estimate of future budget expenditure. Moreover, central government expenditure may not cover such a large percentage of public expenditure that it would make a difference to EU fiscal targets that focus on public expenditure. In other countries, the link between the MTBF, budgetary planning documents and the MTO is very strong, since the MTBF serves to establish the balance of the consolidated accounts (ESA 2010) for the following three years, further broken down into subsectors, so as to ensure attainment of at least the medium-term objective or adherence to the adjustment path towards it. In Italy, the reconciliation between the nominal and structural balance of the general government for the three-year period is disclosed. Such a strict link, however, does not exclude the possibility that slippages in fiscal targets may occur.

In France, to encourage compliance with the MTO, the 2012 organic law has established a correction mechanism: in the event of a gap between the executed structural deficit – which derives from general expenditure – and its trajectory as noticed in an opinion by the French IFI, the Government has to submit corrective measures. The new organic law adopted in December 2021 adds "gap metering" (*un compteur des écarts*) between each budgetary programme expenditure objective in the programming bill and its execution.

In some cases, only an ex-post assessment could give certainty as to whether the national MTBF and the EU-level targets were aligned at some point in the past. However, merely noting that in some past year national targets were met while EU fiscal rules were not followed may not give information on the reasons that led to the misalignment. It may be difficult to establish whether government fiscal policy was not in line with the economic picture at the time, or whether the economic picture for the year in question has changed in retrospect.

[8] In particular, the structural balance depends on spontaneous fluctuations in government revenue in relation to GDP.

3.5 Monitoring and accountability

The OECD Principles of Budgetary Governance state that there should be an inclusive, participative and realistic debate on budgetary choices. The criteria for transparency and accountability in the audit were that information on the setting of the expenditure objective or forecast, and the corresponding follow-up, should be openly available and that major decisions should be handled within the context of the budget process. Parliament, citizens and civil society organisations should have a possibility of a realistic debate about key priorities, such as expenditure objective or forecasts, in the budget. There should be accountability in the event of non-compliance with the expenditure objective.

In general, the SAIs reported some limitations concerning transparency and accountability in their national MTBF and expenditure objective. Information is usually publicly available, but does not necessarily lead to public debate if the system itself is very complicated or the information is presented in a complex way. As the MTBFs and the expenditure objective tend to be complex, only experts in a certain field could be expected to understand the reporting on many parts of the system. This can contribute to uneven parliamentary and public debate, as some parts of the system are more easily understood and thus often better monitored than others. It was noted that this could cause unevenness in decision-making, as there is a "risk of excessive pressure on certain closely monitored expenditure, to the benefit of others that are not subject to the same constraints" (France).

None of the SAIs reported any sanctions for non-compliance with the expenditure objective. However, both internal and external monitoring and sufficient reporting are generally used to ensure that any non-compliance either in budgeting or in the use of funds would be noted. Internal and external monitoring of budgeting and the use of expenditure seemed to work in all countries, meaning that there was enough information available for both parliamentary and public debate. The SAIs did not report any problems with the quality of data or with data not being published at all.

If the expenditure objective is flexible and there are checkpoints that allow for any necessary adjustments, there may not be any need for sanctions or there is no possibility for identifying excessive spending.

Countries with expenditure ceilings (Finland, Netherlands, Sweden) reported that there would be a political cost for exceeding the ceiling. In Sweden, the ceiling has not been exceeded. In Finland, no government has wanted to be the first to exceed the ceiling. However, after the ceiling was exceeded for the first time in 2020 because of the Covid-19 pandemic with virtually no political cost (e.g. negative media attention, or a lack of trust in the Government's capacity to make decisions), the Government has exceeded the ceiling every year during the remainder of the 2019–2023 parliamentary term as well. This is most likely explained by the uncertainty surrounding the situation with the Covid-19 pandemic, and common support for measures to handle it. It will not be possible to determine whether the expenditure ceiling system in Finland has lost credibility until the next government term.

Parliamentary discussion is often more focused on the annual budget, and there is very little discussion of the multiannual perspective (Portugal, Finland). Parliamentary discussion can be hindered if the costs of public policies are not monitored and analysed in the long term, or if there are many different types of expenditure steering instruments (France, Finland). The SAI of Sweden reported that there is a possibility of a realistic debate about key priorities, e.g. the expenditure ceiling in the budget, and information on the setting and follow-up of the expenditure ceiling is mainly openly available. However, there are deficiencies in the Government's reporting on the arguments for the proposed levels of the expenditure ceiling. The Government's reporting on the proposed levels of the expenditure ceiling has varied over time. It has not always been clear what steers the Government's choice of level for the coming year's expenditure ceiling. Nor is it clear what tax take is needed for the level of expenditure to be consistent with the surplus target in the medium term.

Improvements could be made in communicating the budget and budget planning to citizens. As the published documentation is often very technical, essential information can be lost. The SAI of Slovakia recommended preparing a "Budget for People", whether in the form of a brief summary, an infographic or a separate document, as this would show what is being achieved, what the money will be spent on in the next period, and what citizens will benefit from. The SAI of Slovakia also recommended an "Evaluation for People", similarly summarising what has been achieved in a brief and readable form.

France's IFI model (the *Haut Conseil des finances publiques* is chaired by the First President of the French SAI) gives its IFI an effective influence in public debate. The Government is thus under public scrutiny in each opinion submitted by the IFI, for which the next PFPL will be another moment of public scrutiny and debate.

3.6 Response to the Covid-19 pandemic

When the parallel audit was started at the beginning of 2020, the Covid-19 pandemic had also just begun. It was evident that the pandemic would cause a strain on national MTBF systems, as it was an unforeseen event that occurred within a very short time. Governments encountered a lot of pressure to increase budget expenditure while revenues were falling. For this reason, the audit included an open question about the effects of the Covid-19 pandemic on the expenditure objective. The national audits were completed before the pandemic was over, but we have summarised part of what happened in the first year of the crisis. The answers to this question are descriptive, as at this stage it is difficult to establish criteria or recommendations about how this kind of situation should have been managed.

The Commission activated the general escape clause in March 2020 to allow Member States to respond to the Covid-19 pandemic, while derogating from the budgetary requirements that would normally apply under the European fiscal framework. Preliminary indications suggest that the general escape clause will still apply in 2022 and might be deactivated in 2023[9]. It is unclear what kind of EU fiscal rules will be applied when the general escape clause is deactivated. This decision gave Member States a lot of room for manoeuvre in their response to the pandemic, without the need to consider the previous limitations set by the European fiscal framework.

As a response to the pandemic, the SAIs reported that the Member States either updated the expenditure limits by increasing expenditure within the level of the existing system, or suspended the expenditure objective temporarily. The response depended on the flexibility and specifics of the various national MTBF systems. We have not analysed whether there was any difference in the levels of expenditure increase in 2020 that could be explained by the flexibility of the MTBF. As the crisis has continued, there has been more ambiguity about what expenditure decisions are directly linked with the response to the pandemic and what decisions are not in line with the national expenditure objective. For example, the SAIs of both Finland and Sweden have assessed the Government response in 2020 as being justified, but the budgeting for the following years has not been completely in line with the existing expenditure objective. There is a risk that the response to the pandemic has undermined the credibility of expenditure objectives.

The expenditure objective was maintained, although updated, or escape clauses were activated in the following countries:

Italy

The non-binding nature of the Italian MTBF contributed to providing the necessary flexibility to face the Covid-19 pandemic and address the new needs. Under the relevant legislation (Law No 243/2012 enforcing the constitutional balanced budget rule), the pandemic qualifies as an exceptional event, justifying deviations from the MTO and the extra deficit. In the 2020 MTB document, this flexibility allowed for an increase in expected net borrowing (from -2.2% of the last updated MTB document to -10.4% for 2020, and from -1.8% to -5.7% for 2021), resulting in a surge in the public debt/GDP ratio (from 135.2% to 155.7% in 2020, and from 133.4% to 152.7% in 2021). In the event of necessary deviations from the fiscal objectives, the Government shall, after consultation with the European Commission, submit a report to the Houses of Parliament. The report shall contain an updated set of public finance targets, as well as a specific authorisation request disclosing the expected magnitude and duration of the deviation from the original target, stating the purposes for which the resources available as a consequence of the deviation will be allocated, and setting out its plan for realigning the public accounts with the budget targets. The Government shall also ensure that the duration of the plan is commensurate with the seriousness of the events triggering it. With due account being given to the economic cycle, the realignment plan shall come into effect in the fiscal year subsequent to those in which, as a result of extraordinary events, the deviation from the budget target was authorised. Each House of Parliament shall authorise the deviation and approve the realignment plan with an absolute majority vote of its members.

[9] https://ec.europa.eu/commission/presscorner/detail/en/ip_21_884

Due to the Covid-19 crisis, in 2020 the Government resorted to this extra deficit procedure four times, obtaining parliamentary approval for a total increase in net general government borrowing of over 108 billion euros in 2020. Derogating from the applicable legal framework, the Government did not approve and submit to Parliament the legally requested adjustment plan to be implemented in the following years. This was due to the high level of uncertainty.

The Netherlands

Going into 2020, the Government was working with the multiannual expenditure ceilings set in 2017. In response to the Covid-19 pandemic in the spring of 2020, the Government announced many new expenditure measures. Under normal circumstances, it would have been necessary to integrate the new measures into the existing expenditure ceilings, because the measures were expected to be relevant for the EMU balance. This would have meant that the Government should have taken compensatory measures (reallocation of funds) in order to comply with the expenditure ceiling objective.

However, in the Spring Memorandum the Government announced that they had decided to correct the expenditure ceiling objective for the emergency measures. This meant that the expenditure ceiling was raised to accommodate the extra expenditure that was related to the emergency measures. This had two effects:

- the extra Covid-19-related expenditure measures did not impact regular expenditure;
- the Covid-19-related expenditure resulted in a deterioration of the EMU balance and an increase in EMU debt.

The Government also decided that lower-than-expected Covid-related expenditure does not allow for new non-Covid-related expenditure.

The Government stated that the estimated budgetary impact of many emergency measures was characterised by uncertainty, and depended strongly on the ultimate use of the newly created support measures.

During the crisis, the trend-based fiscal policy principle of one main decision-making moment a year was supplemented with continuous budgetary decision-making. Furthermore, the fiscal rules and procedures aimed at limiting the use of State guarantees and loans were not always followed. This caused pressure on the comprehensive character of decision-making, and limited the transparency of budgetary decisions.

Portugal

The Covid-19 pandemic led to the approval of a supplementary budget in 2020 and, in parallel, to the updating of the expenditure limits in the MTBF 2020–2023, but only for 2020. However, this revision did not include the estimated budgetary impact of the emergency measures. The update of the MTBF for the 2021–2024 period covers all expenditure, in accordance with the 2015 Budgetary Framework Law, and therefore includes the expenditure linked to the crisis response measures. However, the lack of a link between financial resources and policy measures continues to reduce the medium-term fiscal framework to a formal exercise.

Slovakia

In terms of the national fiscal framework, two laws are relevant. The first is the Constitutional Act on Fiscal Responsibility, which allows exceptional circumstances to be applied in relation to the limit of general government debt for a period of up to 36 months. The escape clause has clearly defined rules, and can be activated if GDP for the previous year has fallen by at least 12 percentage points year on year, or to rescue the banking sector or eliminate the consequences of a natural disaster, or if war or a state of war is declared. The second is the Act on Budgetary Rules, according to which the obligation to apply a correction mechanism does not apply to the period of exceptional circumstances. The Government, on a proposal from the Minister of Finance announces the beginning and end of the exceptional circumstances, and the proposal is assessed by the CBR before their announcement. In accordance with this, exceptional circumstances were declared on 24 June 2020 in connection with the impacts of Covid-19.

During the audited period from 2015 to 2019, the Act on the State Budget was not amended, but the need for amendment occurred only in 2020. The Government has adopted this amendment in order to be able to respond to situations that will be decided politically by the end of the year. Total expenditure increased by almost €7.8 billion, from €18.6 billion to more than €26 billion. Of the increased spending, €4.9 billion will go to spending directly related to the pandemic, and €2.9 billion to spending on uncovered titles in the budget.

The implementation of escape clauses should not lead to an increase in non-exceptional expenditure, nor should it reduce the credibility of existing fiscal rules and weaken compliance with them. It is not clear how the country should return to the application of the rules in normal times. This is especially important in a situation where, following the end of exceptional circumstances, the level of debt is within the upper limits of the sanction zones (in national law).

Sweden

In the spring of 2020, the Government proposed – and the Riksdag subsequently approved – an increase in the level of the expenditure ceiling for 2020. In the budget bill for 2021, the Government proposed – and the Riksdag subsequently approved – increases in the levels for 2021 and 2022. The increases for 2020–2022 were unique in size and entailed large increases in nominal terms, as well as a share of GDP. The Swedish National Audit Office published an audit report in December 2020 addressing these and other fiscal policy issues related to the budget bill for 2021 (*The fiscal policy framework – application by the Government in 2020, RiR 2020:29*).

The Swedish National Audit Office considers the raised level of the expenditure ceiling for 2020 to be in line with the Swedish fiscal policy framework. Uncertainty regarding the budget year 2020 was very high at the time of the Government's proposal. Consequently, a sharp increase was justified without any clear explanation for the size of the increase.

However, the increases in the expenditure ceiling for 2021 and 2022 that were proposed by the Government were not in line with the Swedish fiscal policy framework, according to the Swedish National Audit Office. The reason for this is that the levels have been chosen to create room for both the current fiscal readjustment and an alternative scenario of active fiscal policy that has not yet been announced. If economic development is in line with the picture otherwise drawn up in the budget bill, the sharply raised ceilings for 2021 and 2022 entail a risk that expenditures will not be tested against each other as the expenditure ceiling is intended to do. All in all, the Swedish National Audit Office assesses that the expenditure ceilings for 2021 and 2022 have been adjusted in a way that lacks support in the framework and that risks weakening budgetary discipline.

In the budget bill for 2021, the Government proposed a level for the third budget year ahead, i.e. 2023. The level was subsequently set by the Riksdag. The level for 2023 is set at the same share of GDP as in 2019, i.e. before the Covid-19 pandemic. The expenditure ceiling thus has a restrictive effect on central government expenditure in the medium term by restricting the possibilities of permanent increases in expenditure between 2020 and 2023. The return from the expansionary fiscal policy in 2020 to structural net lending in line with the surplus target is supported by the Government's proposal for a new expenditure ceiling level for 2023. By returning to the same ceiling level in relation to GDP as the one applied before the Covid-19 pandemic, the Government limits the scope of permanent spending increases during the crisis period.

The expenditure objective was temporarily suspended in the following countries:

Finland

A new Government assumed office in 2019 and set the spending limits for the 2020–2023 parliamentary term. The Government gave up the spending-limit system completely for the year 2020, as it was not possible to respond to the pandemic using the flexibility within the system. This led to an increase in expenditure (compared to the previous expenditure limit) of approximately €7 billion in 2020, which was mostly targeted at Covid-related expenses. The NAO of Finland assessed the decisions concerning the year 2020 as justified. In 2021, the Government returned to the spending-limits system, but applied several exceptions. Expenses directly related to the pandemic and part of the support for businesses were left outside the spending limit (€2.3 billion). The mechanism for exceptional circumstances was activated in 2021 and 2022, allowing an increase in expenditure of €1 billion in total. Moreover, a reservation of €1.8 billion was made within the spending limit for one-off expenditure that was necessitated by the pandemic.

This kind of reservation was not in line with the earlier principles of the spending-limit system, and the terms for using the expenditure were vaguely defined.

After the Government decided to increase the spending limit in 2022 and 2023 for reasons unrelated to the pandemic, the NAO of Finland stated that the spending-limit system was no longer used according to the principles that should be guiding expenditure decisions within the system. Political commitment to the system has been severely compromised, and it looks like the spending-limit system is broken for the entire parliamentary term, without a possibility to achieve the pre-pandemic level of expenditure. At this point, it is difficult to assess whether the system will regain the credibility it used to have. The spending-limits system has proved in the past to be a very efficient tool for limiting and planning expenditure, and these qualities will also be needed in the future.

France

The current MTBF, established by the 2018–2022 PFPL, has been rendered obsolete by the exceptional context of the health and economic crisis. This same context has led the Government to postpone the presentation of a new programming law. However, it is essential that a new medium-term perspective be established in order to ensure that public finance choices are sustainable and comply with the requirements of the organic law. In June 2021, the *Cour des comptes* stressed in an audit requested by the Government on the post-Covid public finance strategy that it should adopt a new programming law in autumn 2022[10]. In its opinion on the draft budget and financing bills[11], the High Council of Public Finance also expressed its views in this regard, and pointed out the need to present a new programming law.

[10] *Une stratégie de finances publiques pour la sortie de crise, Communication au Premier ministre, juin 2021* https://www.ccomptes.fr/sites/default/files/2021-06/20210615-Rapport-strategie-finances-publiques-sortie-de-crise.pdf

[11] Opinion n° HCFP - 2020 – 5 – *21/09/2020* *http://www.hcfp.fr/sites/default/files/2020-10/HCFP%20opinion%20n%C2%B02020-5-PLF-PLFSS%202021-EN.pdf*

4 Analysis and conclusions

The main results of each parallel audit are summarised in Table 2 below. The political component of the functioning of MTBFs complicates the analysis of audit results due to a lack of uniform norms. Therefore, it is hard to draw universal conclusions about what works best under which circumstances.

However, a level of common features could be identified from the audit results. Although they may not be universal for all audited countries, countries with similar systems may have noted similar issues. These issues are addressed in this chapter.

Conclusions based on the parallel audit findings

As a summary of Table 2, the following conclusions can be drawn for Finland, France, Italy, the Netherlands, Portugal, Slovakia and Sweden:

(3.1) Expenditure objectives are well integrated into the budget process in all audited countries. Despite this integration, the actual performance of the expenditure objective differs in each audited country. There are differences, for example, in whether the expenditure objective sets a boundary for expenditure.

(3.2) Expenditure objectives have different goals in these countries. The goals can be set in a flexible or strict way, which has an effect on how comprehensively the achievement of goals can be assessed. National implementation of the MTBF also allows for differences in national expenditure objectives.

(3.3) The inbuilt flexibility of the expenditure objective helps to address changing circumstances, but it makes it more challenging to align the expenditure objective with other national budgetary objectives. Information about the relationship of the expenditure objective with other budgetary objectives is commonly available. In some cases, there were gaps in the information about the relationship of the expenditure objective with other objectives. At least one country noted a lack of consistency between different objectives.

(3.4) There were big differences between the Member States in how elaborate the reporting about the link between the EU fiscal rules and the expenditure objective was. Some Member States report a very strong link between the expenditure objective and the EU fiscal rules, yet in some countries the reporting was lacking. The countries seemed to have either one set of rules that included the EU and national rules, or two sets of rules – EU and national – that were challenging to connect with each other.

(3.5) Information about expenditure-objective systems is available in all audited countries, and most of the information is public. All systems can be held to account, and monitored externally by SAIs and/or IFIs. The complexity of the systems reduces transparency somewhat for non-professionals and the public in general. It may be difficult to explain the benefits of these systems to citizens and encourage public debate.

(3.6.) The Covid crisis led to increased public spending within existing systems, making use of inbuilt flexibility in most of the audited Member States. In some countries, the expenditure-objective system had to be put temporarily aside to allow for increases in expenditure. At the time of writing, it remains unclear how best to return to rules-based and predictable public finances. A discussion is needed about how exceptional circumstances of this magnitude should be dealt with in expenditure planning and annual budgeting. Public debate on this issue could be supported by IFIs/SAIs.

Are medium-term expenditure objectives set up effectively and transparently in the budget process?

Four parallel audits found the answer to this question to be “yes”, while three answered “partially”. Some of the problems that were found were the transparency of the system and the difficulty in assessing whether the system was directing the level of expenditure or reacting to it and not achieving the objectives. It was noted that even in the case of those that answered “yes”, the actual functioning of the system and how it is used often relies heavily on political commitment.

Table 2. Summary of parallel audit results

Question	Finland	France	Italy	Netherlands	Portugal	Slovakia	Sweden
(3.1) Integration into the budget process	Fully integrated and sets a boundary for expenditure.	Fully integrated, but some difficulties in performance. The spending review process was a useful tool when linked with the MTBF.	Integrated: it sets revenue and expenditure forecasts for the budgetary process. All the general government subsectors are covered.	The expenditure ceilings are integrated into the budget process.	Integrated into the budget process, but the annual perspective prevails over the multiannual perspective – limits are revised annually based on the values of the Budget – contrary to the purpose of an expenditure rule that should limit the expenditure increase in a multi-year horizon.	Fully integrated (at least on paper) [YES for compliance, NO for performance]. Problems with linking: spending <-> fiscal objectives <-> public policy objectives.	Fully integrated and sets a boundary for expenditure.
(3.2) Effectiveness in terms of achieving the stated goals	The system can be used effectively to maintain the required expenditure level.	The targets have been met or nearly met for the 2011–2014 and 2012–2017 PFPLs. With regard to the 2014–2019 PFPL, the increase in public expenditure observed over 2015–2017 led to a marked overshooting of the target.	The system has proved to be effective in the first year of expenditure forecasts, while the non-legally-binding nature of the MTBF and the possibility of revising and updating it on a yearly basis hinders its effectiveness in governing future expenditure trends.		The expenditure limits were met. The MTBF does not cover the evaluation of programmes and their policies.	The goals were achieved late, or not at all. Programme/performance budgeting was not effective (helpful in achieving the stated goals).	The expenditure ceiling has never been exceeded. The ceiling has had a disciplining effect on the expenditure trend.
(3.3) Relationship with other national budgetary objectives	The relationship with other national budgetary objectives is presented. It may not be consistent with achieving other objectives (e.g. nominal balance).	The expenditure objective is to some extent connected to other national budgetary objectives: the objectives that underpin the MTBF are reducing the public deficit, public expenditure and taxes, and transforming public administrations in order to reduce public expenditure by more than 3%.	MTBF expenditure rules are not considered expenditure ceilings: they allow for considerable flexibility in addressing new priorities, but struggle to govern public expenditure trends. A cyclical spending review is included.	Expenditure ceilings in annual budget laws correspond to the aggregate ceilings under which they reside. The multi-year focus on top-down expenditure control can lead to less attention being paid to the quality of bottom-up budget estimates and their alignment with the agreed-upon policies and service level.	Reconciliation between expenditure limits and budgetary objectives is not reported in a clear and comprehensive manner. Information about the underlying public policies that should support the MTBF proposal is also not disclosed in detail.	No expenditure ceiling; only spending limits for budgetary chapters / ministries. Considerable flexibility within the annual budget – a few thousand so-called budgetary measures (changes in the budget).	Budgetary policy targets are connected, but the expenditure ceiling is not derived directly from other targets. All targets are not defined according to the same accounting system.

Question	Finland	France	Italy	Netherlands	Portugal	Slovakia	Sweden
(3.4) Relationship with the MTO and/or other EU-level fiscal rules	Not reported in detail.	To encourage compliance with the MTO, France has instituted a correction mechanism. The new organic law adopted in December 2021 adds ”gap metering” (*un compteur des écarts*) between each budgetary programme expenditure objective in the programming bill and its execution.	A very strong link: the MTBF sets the MTO and other fiscal targets in compliance with the EU regulation for the three-year period. The reconciliation between the nominal and structural balance is fully disclosed. The escape clause is clearly regulated.	Legally, budgetary policy is conducted with due regard to the European requirements that apply to the EMU balance, the EMU debt and the MTO.	The MTBF limits are compatible with the MTO. However, they do not share the same accounting methodology and, as such, the alignment between the two indicators is difficult to validate, considering that this information is not reported in detail.	National objectives are directly linked to the MTO. The target is moved annually to the end of the period.	The Swedish fiscal policy framework sets tighter boundaries for fiscal policy than the Stability and Growth Pact. No reported link between the expenditure ceiling and the MTO.
(3.5) Monitoring and accountability	Information is publicly available, and the system is held to account. Complexity reduces accountability. There was no political cost when the objective was not followed in 2020–2023.	Information is publicly available, and the system is held to account.	The MTBF macroeconomic and public finance assumptions are validated by an independent body. The MTBF is discussed and deliberated in Parliament, and the main financial institutions are involved in the discussion. All relevant MTBF documents are publicly available.	Information on expenditure ceilings is publicly available. The national IFI monitors compliance with national budgetary rules and reports to Parliament.	Information is readily available, but there is no real political debate about expenditure limits besides the annual budget. The information regarding the annual limits included in the Budget Proposal Report is not sufficient to fully state that there is effective accountability control of the MTBF limits. No sanctions for non-compliance with the expenditure objective. The publicly available documents are too technical for citizens to understand.	All important documents are publicly available. They are technical and hard for citizens to understand. The SAO SR recommended preparing a Budget for People & a Final Account/Annual Report for People.	Information is mainly publicly available, but there are some deficiencies in the Government’s reporting, according to the Swedish National Audit Office. The system is held to account. External monitoring is carried out by external government bodies.

Question	Finland	France	Italy	Netherlands	Portugal	Slovakia	Sweden
(3.6) Covid	Expenditure ceilings were suspended in 2020. In 2021, they were reinstated, with multiple exceptions, and by activating the escape clause. Due to reasons unrelated to the pandemic, the expenditure ceilings were broken in 2022 and 2023.	The Government postponed the presentation of a new PFPL. In June 2021, the *Cour des comptes* stressed in an audit requested by the Government on the post-Covid public finance strategy that it should adopt a new programming law in autumn 2022.	The escape clause was activated four times in 2020; parliamentary authorisation was granted for a total increase of over 100 bn euros in net borrowing. Derogation from the approval of an adjustment plan as requested by the legal framework.	In 2020, expenditure ceilings were adjusted for additional Covid spending, leading to continuous budgetary decision-making. The ceilings for non-Covid-related expenditure were left intact.	The Covid-19 pandemic led to the updating of expenditure limits in the MTBF 2020–2023, but only for the year 2020. This revision did not include the estimated budgetary impact of the emergency measures.	The implementation of escape clauses should not lead to an increase in non-exceptional expenditure. The EU agreed in March 2020 to release the so-called general escape clause. The Act on the State Budget was amended in 2020, something which has not occurred in recent years.	Increases in the expenditure ceiling for 2020–2022. The increases for 2021 and 2022 are not in line with the Swedish fiscal policy framework according to the Swedish National Audit Office. The level for 2023 is set at the same share of GDP as before the Covid-19 pandemic, which limits the scope for permanent spending increases during the crisis period.
Are medium-term expenditure objectives set up effectively and transparently in the budget process?	YES – The system can be used, and was in practice used successfully in 2004–2019 to set the level of expenditure for the entire parliamentary term. The ceiling has been followed, and the level of expenditure has remained constant, compared to GDP. Since 2020, the ceilings have not been used fully according to the earlier principles.	PARTIALLY – The targets and objectives have been partly achieved (especially as regards social security spending). However, the new framework that was adopted in 2021 and that will govern the new PFPL (autumn 2022) will contribute to achieving the objectives with more transparency.	YES – Expenditure forecasts are fully covered in the MTBF on both a cash and an accruals basis. Problems can be detected in their translation into the budget process and accounting system. The rolling structure of the MTBF, together with its non-binding nature, affects its ability to outline a stable path in the evolution of public spending.	The system of expenditure ceilings is set up to contribute to the objective of expenditure control. The focus on a top-down expenditure ceiling can reduce the quality of bottom-up budgetary estimates. Apart from the set-up, the system relies on political commitment.	PARTIALLY – The MTBF fulfils the mission of establishing limits for central government expenditure in the medium term. However, the annual revisions of the MTBF limits, based on the State Budget forecasts, point to its subordination to the annual cycle, reducing the MTBF's effectiveness. Regarding transparency, there is no clear link between expenditure limits, the budgetary objectives and public policy priorities.	PARTIALLY – Fiscal budgetary targets/objectives were achieved late or not at all. Setting up processes for achieving public policy objectives through programme (performance) budgeting during the audited period did not work as intended, and did not significantly contribute to the achievement of objectives. In the area of transparency, a large number of small changes were identified through budgetary measures.	YES – The expenditure ceiling has had a disciplining effect on the expenditure trend, partly because it has served as a restriction and partly because it has indirectly required improved expenditure control.

General analysis of the MTBF, expenditure objectives and annual budgeting

The European Council has underlined the need for complementarity between national frameworks and EU fiscal rules. In the Council's view, national rules should complement the Member States' commitments under the Stability and Growth Pact (SGP), and national governance arrangements should complement the EU framework. The Council considered that national institutions should play a more prominent role in budgetary surveillance to strengthen ownership, enhance enforcement through national public opinion, and complement economic and policy analysis at EU level[12]. The following analysis addresses, in more general terms, the thoughts and discussions within the audit group in the area of the MTBF, expenditure objectives and annual budgeting. The analysis is based on the parallel audit findings that were common to at least two Member States were concerned, but it does not necessarily reflect all the audit findings.

One of the main findings of the parallel audit was that EU fiscal rules have been a source of continuous improvements in national fiscal regulation. Even though different Member States apply the major principles using different methodologies, there is a common understanding that the MTBF and its related national fiscal targets are necessary instruments for steering a course towards sustainable public finances and fiscal policy. In the current important discussions about reactivating the standards of the SGP in modified or unchanged form, the MTBF requires dialogue between the EU and Members States on budgetary discipline.

4.1 Linking annual budgets to MTBFs

The question of linking annual budgets to MTBFs can be viewed from two perspectives. First, there should be a forward-looking plan (a minimum of three years) for a suitable level of budget expenditure that is either directly linked to the MTBF or that is within the scope of MTBF targets, i.e. not in direct conflict with the MTBF. This link is not easy to establish, and there are different ways of doing it. This perspective is addressed in 4.1.1. Secondly, there is the question of establishing whether the planned expenditure levels are met in the annual budgeting, and what kinds of revisions can be made. This issue is addressed in 4.1.2. Both of these questions are equally important, but they are addressed in this analysis by different approaches.

The Commission's review of Directive 2011/85 highlighted that *"the MTBFs are still to an overly large extent subordinate to the annual budget processes and do not create a sufficiently stable and credible medium-term perspective for fiscal policy. No provision prevents Member States from updating their MTBFs yearly in terms of multiannual objectives and the path towards them. Moreover, there is no obligation to explain adjustments between successive plans, except when a new government takes office. As a result, with the exception of a limited number of Member States with fixed or highly binding MTBFs, short-term budgeting remains a high priority, as annual budgeting plays a very prominent role in the overall budgetary process. This in turn leads to annual adaptations of the MTBF to suit the more immediate needs of annual budgeting, which is the opposite to what was envisaged in calling for Member States' annual budgets to be consistent with the MTBF"*[13].

The Commission's review also addressed the need for conceptual clarification regarding the MTBF, as the meaning of the MTBF lends itself to more than one interpretation in the text of Directive 2011/85. Within national budget planning, its implementation is a conceptual and practical challenge, and leaves room for varying national implementations. It is difficult to see a driver for changes in the area of annual budgeting and the MTBF, at least to a direction where the EU countries would share similar practices due to the requirements in the Directive.

4.1.1 Translating the MTBF into an expenditure objective

The difficulty of translating the MTBF into an expenditure objective was highlighted in the parallel audits. There are many different perspectives and practices as regards how this issue is addressed in practice. Most issues relate to reconciling the information between the MTBF and the expenditure objective, as well as the scope of the central government budget expenditure, in relation to the MTBF and the MTO.

[12] https://ec.europa.eu/info/sites/default/files/economy-finance/swd_2020_211_en.pdf, page 6
[13] https://ec.europa.eu/info/sites/default/files/economy-finance/swd_2020_211_en.pdf, pages 61 and 77

Some audits noted that it may be difficult to justify transposing the MTBF into annual budget expenditure from a top-down perspective. Some explanations were that the coverage of annual budget expenditure is not sufficient to guarantee achieving the EU fiscal targets; the fact there are many other factors outside the decision-making powers of governments that also affect achieving the fiscal targets; and the fact that reconciling information between the national accounts and accounting terms is time-consuming.

However, some Member States have – for historical or other reasons – decided to create a binding medium-term budget expenditure ceiling that could well function as a link between the MTBF and annual budget expenditure. Even in these cases, however, it is not always clear whether the annual expenditure is affected by the MTBF, or whether the MTBF is a result of the medium-term plan for budget expenditure.

In many parallel audits, reconciling the information between the national accounts and the budget (usually in accounting terms) was found to be fairly work-intensive, and that the result – i.e. the information provided – was of only limited use. It requires specialists and many hours of work, while the complexity of the result might reduce its transparency.

An MTBF has both a top-down (macro estimates and budget targets) and a bottom-up (spending pressures from ministries) component. Some audits noted that due to a one-sided focus on expenditure control, the bottom-up element can be under-emphasised.

A good practice seems to be to use both bottom-up and top-down targets to tie the MTBF into national fiscal targets, and to report on how the targets are aligned and could be reconciled, while acknowledging that the reporting may not be completely accurate. The spending review process can be a useful tool for reconciliation.

The functioning of MTBFs in creating stability and accountability relies on the degree of political commitment. Political commitment benefits from the MTBF being used to set multiannual budgetary ceilings at the beginning of the government period. This applies, in particular, to systems in audited Member States which feature multi-party coalition governments.

4.1.2 The relationship between the expenditure objective and annual budgeting

The parallel audits addressed the relevance of linking budget planning to the annual budget process. In order for an expenditure objective to operate effectively, annual budget preparation should also take place within the scope of the expenditure objective. If the annual budget process is not related to the multi-year expenditure objective, the MTBF will not contribute to a responsive budget or to expenditure control.

There were some examples where the expenditure objective and annual budgeting were, in effect, the same process, but in many cases the link between the annual budget and the expenditure objective was weaker. Even when the process is fully interconnected, it is very important how much flexibility there is to make changes to annual budgeting within the process, and in what kinds of situations those changes are allowed. A certain degree of flexibility increases the commitment to expenditure objectives, but too much flexibility makes it impossible to set a limit on expenditure.

4.2 Aligning MTBFs with other national objectives

Expenditure objectives are an important part of national budgetary targets. Public expenditure can be seen to be under more direct influence of political decision-makers than some of the other budgetary rules. For this reason, there is special value in setting realistic yet ambitious (whether in the direction of investment, recovery measures or prudent expenditure policy) targets for the expenditure level, and to make sure that expenditure objectives are aligned with or even support other budgetary targets, e.g. debt, surplus/deficit targets.

The parallel audit results highlight that there are differences in implementing the MTBF to reflect national budgetary objectives or the expenditure objective. One way of exploring this issue further is to consider how the alignment is made both on paper and in practice. When the targets are very flexible, it surely helps to address changing economic situations and makes it easier for political decision-makers to commit to a rules-based fiscal policy. However, with flexibility comes more uncertainty about the future, and it also weakens the possibility of directing public spending levels efficiently or achieving national budgetary objectives.

Even though the MTBF is a forward-looking tool and is not meant to provide accurate information on future spending decisions or public finances, it is also necessary to report ex post whether the expenditure objective was reached. The availability of this information was noted as an issue in some of the audits. Information about how accurately the level of expenditure can be targeted a few years in advance also gives more credibility to the scope for reaching other national budgetary targets. It would also bring light to a situation where there seems to be no clear link between the expenditure objective, budgetary objectives and public policy priorities.

4.3 Accountability

All the audits reported that the national system for setting and following up the expenditure objective can be monitored by external auditors or other similar institutions. The information is generally available, but usually requires expertise to interpret and analyse it. The complexity of the systems reduces transparency, and may result in a situation where public or parliamentary debate focus more on certain expenditure items than others, and there is less discussion of the overall level of expenditure.

A culture of public and political debate about annual budgets already exists. Translating MTBFs into central government expenditure objectives is a concrete way to promote more practical debate around the issue.

Further transparency and accountability could be achieved by encouraging public debate through the availability of well-analysed information on the functioning of these systems. SAIs or IFIs can have a role in supporting public debate through their own publications and analyses, aimed at the public as well at politicians.

In the parallel audit it was noted that there were no sanctions for non-compliance with expenditure objectives. The main sanction was the reputational cost for any Government that breaches expenditure targets. As the systems are complex in nature, accountability for breaching the targets might be low in practice. The MTBF and expenditure objectives would benefit from reducing this complexity, as it would also increase the level of accountability.

4.4 Pandemic response

The Covid-19 pandemic started while most of the audits were still ongoing. Although the years 2020 and 2021 were left outside the audited period, it was possible to monitor how the expenditure objectives were affected by the crisis, even when there was no scope for using the benefit of hindsight to interpret and analyse the effects of the crisis in the long term. The risks that materialised in the Covid-19 pandemic also illustrate more broadly how such exceptional circumstances can be addressed within expenditure objectives, annual budgets, MTBFs and budgetary frameworks in general.

For exceptional circumstances, the EU fiscal framework and individual countries offer escape clauses which Member States can trigger in a given situation. In the event that escape clauses are triggered, existing fiscal rules will cease to apply in the short term. However, the implementation of escape clauses should not lead to an increase in non-exceptional expenditure, nor should it reduce the credibility of existing fiscal rules and weaken compliance with them.

After escape clauses have been activated, it is not clear how best to return to applying the rules in normal times. This is true both for national rules and the EU framework. This is especially important in a situation where, following the end of exceptional circumstances, the level of debt is within the upper limits of the sanction zones (in national law). Consideration should be given to adapting the national fiscal framework so that the Government can respond promptly to significant adverse effects in situations such as the ongoing pandemic without moving away from trajectories to sustainable public finances after the exceptional circumstances have ended.

During the crisis, the previously used trend-based fiscal policy principle of one main decision-making moment a year was supplemented with continuous budgetary decision-making. As the pandemic has continued, it has become more difficult to assess whether expenditure in response to the pandemic is in fact directly related to Covid-19. Also, as more information becomes available on the more effective measures and spending decisions, it is possible to shed new light on the usefulness of past expenditure decisions. At least in some cases, it seems that the pandemic has increased the level of government expenditure possibly even in the long term, and it can be difficult to return to the expenditure level before the pandemic.

Some of the audited expenditure-objective systems seem to have worked well throughout the pandemic, and the ability to predict and control expenditure levels has remained. However, there is a risk that the response to the pandemic has undermined the credibility of expenditure objectives in some Member States. In some cases, the political commitment to fiscal rules and expenditure objectives has been compromised, and there is no way to achieve the pre-pandemic level of expenditure. At this point, it is difficult to assess whether the credibility and trust that have been lost can be regained in such cases.

It is difficult to assess whether it is possible or beneficial to make expenditure objectives flexible enough to endure these kinds of sudden shocks. However, it was noted that without any system for limiting or forecasting expenditure, it is more difficult to make decisions on expenditure and there is an increased risk of overspending. It looks like some level of forward planning needs to be retained even when there is uncertainty about the expenditure level needed.

Appendix 1: Audit questions and criteria

Main audit question: Are medium-term expenditure objectives set up effectively and transparently in the budget process?

Integration into the budget process

The process for setting the expenditure objective or forecast

Background questions
- Description of the process for setting the expenditure objective or forecast, including relevant decision-makers, e.g. in the format of a timeline.
- Information used in setting the objective or forecast:
  - Data (accounting forecast, other)
  - Bottom-up or top-down approach, or both?
  - Is there a link to government policy priorities?
  - Is the information revisioned eg. annually?
  - How are medium-term projections and information utilized in target setting?
  - How is reconciliation done between different types of information?
  - Does the level of strictness of the expenditure objective affect the process and how? Is there an incentive to set the objective at a level that is easily achieved?

Other considerations when setting the expenditure objective or forecast; answer if relevant:
- Are reallocations already considered when setting the objective? If yes, then to what detail and are the decisions binding?
- Is there a spending review procedure, and what is its level of integration into the budget process?
- Is the expenditure objective or forecast linked to performance budgeting and describe how that link is ensured?
- Are central government guarantees and liabilities assessed when setting the expenditure objective(s)? In what way?

Medium-term objective or forecast revisions; answer if relevant:
- When has the objective or forecast been revisioned between 2014-2019?
- Is there a system for updating the objective or forecast after it is set? What is this system like? (automatic revision points, revision in case defined changes, escape clauses?)
- Is there an escape clause? Describe the clause in detail. Has it been used? If yes, has the criterion/criteria for use been respected?

Audit criteria (E)- effectiveness (T)- transparency
(E) Budgetary process should incorporate a medium-term horizon in terms of expenditure
(E) Objectives should have real force in setting boundaries for expenditure, and include sufficient institutional incentives and flexibility to ensure that objectives are respected.
(E) The objectives or forecasts should be set in line with top-down budgetary constraints and government policies.
(E) The process should include all relevant institutions at the centre of government.
(T) Major decisions are handled within the context of the budget process.

Question: Your assessment based on the relevant questions and the criteria stated above:

Effectiveness at achieving stated goals

Background information:

- Has the expenditure objective or forecast been achieved in terms of national criteria for the evaluation of the effectiveness of the objective or forecast?
- If the objective has not been met at some point, what have been the reasons? Could it have been avoided?
- In your opinion, would meeting this objective be sufficient for achieving the stated goals? If not, what other things should be considered? (Answer if relevant)

Operationalised criteria (E)- effectiveness (T)- transparency
National criteria
(E) The numerical objective has been met.
(E) The objective or forecast has been successful in achieving its primary goal.
(E) The objective or forecast has been successful in achieving its secondary goal.
Common criteria
(E) Expenditure objective or forecast should support sound and sustainable fiscal policy.
(E) Expenditure objective or forecast is clear and useful in aligning policies with available resources.

Question: Your assessment based on the relevant questions and the criteria stated above. Also include any perspectives based on the questions below, concerning additional information.

Additional information:

There are general considerations about the qualities that a well-designed expenditure policy should achieve. Please consider the following statements in relation to the audited expenditure objective:

- Can the objective or forecast help to reduce procyclicality bias? What kind of components are there to reduce procyclicality – escape clause(s)?
- Can the objective or forecast help to reduce deficit bias? (political decision-makers have a bias towards a budget deficit)
- Can the objective or forecast help to limit increases in spending?
- Can the objective or forecast be used in reducing the amount of spending?
- Does the objective or forecast allow for making investments?
- Does the objective or forecast support improving the quality of public finances?
- Does the objective or forecast incentivize toward impractical or unsustainable spending choices in some other way?
- Have there been attempts to allocate spending outside an expenditure objective or forecast?

Relationship with other national budgetary objectives

Background questions:

- Is a link to other national budgetary objectives (e.g. debt, deficit) presented, and how are the links described?
- What is the relationship between different national objectives, e.g. is the expenditure objective or forecast derived from other national budgetary objectives such as deficits?

Audit criteria (E)- effectiveness (T)- transparency
(E) There should be a link to other national budgetary objectives, e.g. whether the expenditure objective or forecast is derived from other national budgetary objectives such as deficits.

Question: Your assessment based on the relevant questions and the criteria stated above:

Relationship with the MTO and/or other EU-level fiscal rules

Background questions:

- Is there a link between country-specific fiscal rules and the expenditure objective or forecast?
- How is the link to country-specific fiscal rules, especially the MTO, presented?
- Has the national MTO been set at the minimum level, or tighter than the EU requires?

Audit criteria (E)- effectiveness (T)- transparency
(E) There should be a link either through the process or a top-down/bottom-up approach between the expenditure objective or forecast and the MTO.
(E) There should not be inconsistency between reaching the expenditure objective or forecast, and reaching the MTO.
(T) The consistency between the expenditure objective or forecast and the MTO should be explained.

Question: Your assessment based on the relevant questions and the criteria stated above:

Monitoring and accountability

Background questions:
What kind of accountability system is there in place to follow up if the expenditure objective or forecast is met:

- What happens if the objective is not met?
- If the objective is not met, where is the point for first reaction? Is there still time to change course so that the objective would again be met?
- How much weight is put to the opinion of the internal monitoring?
- If there is external monitoring (IFIs, [press], other?), how much weight is placed on the external monitoring opinion?
- What kind of information is available for public/parliament/government about the objective or forecast:
  - Background information that was used when deciding on the objective or forecast?
  - How the expenditure objective or forecast functions?
  - The decision-making process?

Audit criteria (E)- effectiveness (T)- transparency
(E) There is accountability in case of non-compliance with the expenditure objective.
(T) Information on the setting of expenditure objective or forecast and the follow-up is openly available.
(T) Parliament, citizens and civil society organisations have the possibility to engage in realistic debate about key priorities, such as an expenditure objective or forecast, in the budget.

Question: Your assessment based on the relevant questions and the criteria stated above:

Additional audit question on the 2020 financial crisis related to the Covid-19 pandemic

Please describe how the MTBF in place/expenditure objective or forecast has worked in exceptional circumstances related to the Covid-19 pandemic and its financial effects. Has the 2020 Covid-19 crisis led to changes or needs to update the MTBF/expenditure objective or forecast? Has there been a need to use any in-built flexibility or escape clauses? Have reallocations for handling the crisis been possible?

General criteria for evaluating the effectiveness of the objective or forecast and the budget process, including monitoring, and transparency

The Budgetary Frameworks Directive aims for effectiveness in promoting budgetary discipline and the sustainability of public finance. The Directive notes the need to comprehensively cover public finances with budgetary frameworks. Also operations of those general government bodies and funds which do not form part of the regular budgets at sub-sector level and that have an immediate or medium-term impact on Member States' budgetary positions should be given particular consideration. Similarly, due attention should be paid to the existence of contingent liabilities. In this audit it is seen as important aspect of the expenditure objective or forecast, the wider coverage in terms of expenditure or any other aspects of public funding and liabilities it has.

The Budgetary Frameworks Directive (2011/85/EU) addressed the need to enhance national ownership for multiannual budgeting and execution. The Directive called on the Member States to have frameworks in place that are consistent with EU legislation by the end of 2013. Chapter V of the Budgetary Frameworks Directive describes the medium-term budgetary frameworks: Article 9(1) Member States shall establish a credible, effective medium-term budgetary framework providing for the adoption of a fiscal planning horizon of at least three years, to ensure that national fiscal planning follows a multiannual fiscal planning perspective. For this reason, in this audit the medium-term planning horizon is defined as at least three years planning horizon.

The Budgetary Frameworks Directive does not specifically call for procedures for establishing medium-term objectives in terms of expenditure, yet that possibility is brought forward in Article 9 as follows: (2) Medium-term budgetary frameworks shall include procedures for establishing the following items: (a) comprehensive and transparent multiannual budgetary objectives in terms of the general government deficit, debt and any other summary fiscal indicator such as expenditure, ensuring that these are consistent with any numerical fiscal rules as provided for in Chapter IV in force. In the Directive, it is expected that medium-term expenditure objectives should be consistent with any numerical fiscal rules, which is further defined as compliance with the reference values on deficit and debt set in accordance with the TFEU. In this audit, the criteria for consistency with numerical fiscal rules is also seen as whether the expenditure objective or forecast is consistent with the MTO.

The OECD's Principles of Budgetary Governance are used as audit criteria in this parallel audit. The following principles are highlighted in this audit:

1. Manage budgets within clear, credible, and predictable limits for fiscal policy, through:

a having procedures in place to support governments in effecting counter-cyclical or cyclically neutral policies, and in using resource endowments prudently;
b committing to pursue a sound[14] and sustainable[15] fiscal policy;
c considering whether the credibility of such a commitment can be enhanced through (i) clear and verifiable fiscal rules or policy objectives which make it easier for people to understand and to anticipate the government's fiscal policy course throughout the economic cycle, and (ii) other institutional mechanisms (see recommendation 10 below) to provide an independent perspective in this regard;
d applying top-down budgetary management, within these clear fiscal policy objectives, to align policies with resources for each year of a medium-term fiscal horizon; noting that in this context, Adherents should adopt overall budget targets for each year which ensure that all elements of revenue, expenditure and broader economic policy are consistent and are managed in line with the available resources.

Criteria for the effectiveness of expenditure objectives or forecasts: Expenditure objectives should support sound and sustainable fiscal policy. This requires that expenditure objectives or forecasts be clear and useful in aligning policies with available resources.

2. Closely align budgets with the medium-term strategic priorities of government, through:

a developing a stronger medium-term dimension in the budgeting process, beyond the traditional annual cycle;
b organising and structuring the budget allocations in a way that corresponds readily with national objectives;

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[14] a "sound fiscal policy" is one which avoids the build-up of large, unsustainable debts, and which uses favourable economic times to build up resilience and buffers against more difficult times, so that the needs of citizens and stakeholders can be addressed in an effective and enduring manner.

[15] "sustainable fiscal policy" – the expenditure level change is under control (i.e. perhaps allowing a slow or steady rise/change, but no major unexplainable fluctuations) and there is no obvious conflict between expenditure objectives and fiscal policy targets (as would be manifested in meeting an expenditure objective while not meeting other national or EU fiscal objectives).

c recognising the potential usefulness of a medium-term expenditure framework (MTEF) in setting a basis for the annual budget, in an effective manner which (i) has real force in setting boundaries for the main categories of expenditure for each year of the medium-term horizon; (ii) is fully aligned with the top-down budgetary constraints agreed by government; (iii) is grounded upon realistic forecasts for baseline expenditure (i.e. using existing policies), including a clear outline of key assumptions used; (iv) shows the correspondence with expenditure objectives and deliverables from national strategic plans; and (v) includes sufficient institutional incentives and flexibility to ensure that expenditure boundaries are respected

d nurturing a close working relationship between the Central Budget Authority (CBA) and the other institutions at the centre of government (e.g. prime minister's office, cabinet office or planning ministry), given the inter-dependencies between the budget process and the achievement of government-wide policies;

e considering how to devise and implement regular processes for reviewing existing expenditure policies, including tax expenditures (see recommendation 8 below), in a manner that helps budgetary expectations to be set in line with government-wide developments.

Criteria for the effectiveness of the budgeting process: budgetary process should incorporate medium-term horizon in terms of expenditure. Objectives should have real force in setting boundaries for expenditure, as well as include sufficient institutional incentives and flexibility to ensure that objectives are respected. This respect is understood as commitment to follow the expenditure objective from both the administration and the political decision-makers, i.e. there are no attempts to make spending decisions outside the boundaries set in the objective or use in-built flexibility without justification. The objectives should be set in line with top-down budgetary constraints and government policies and the process should include all relevant institutions at the centre of the government.

4. Ensure that budget documents and data are open, transparent and accessible, through:

a the availability of clear, factual budget reports which should inform the key stages of policy formulation, consideration and debate, as well as implementation and review;

b the presentation of budgetary information in comparable format before the final budget is adopted, providing enough time for effective discussion and debate on policy choices (e.g. a draft budget or a pre-budget report), during the implementation phase (e.g. a mid-year budget report) and after the end of the budget year (e.g. an end-year report) to promote effective decision making, accountability and oversight;

c the publication of all budget reports fully, promptly and routinely, and in a way that is accessible to citizens, civil society organisations and other stakeholders;

d the clear presentation and explanation of the impact of budget measures, whether to do with tax or expenditure, noting that a "citizen's budget" or budget summary, in a standard and user friendly format, is one way of achieving this objective;

e the design and use of budget data to facilitate and support other important government objectives such as open government, integrity, programme evaluation and policy coordination across national and sub-national levels of government.

5. Provide for an inclusive, participative and realistic debate on budgetary choices, by:

a offering opportunities for the parliament and its committees to engage with the budget process at all key stages of the budget cycle, both ex ante and ex post as appropriate;

b facilitating the engagement of parliaments, citizens and civil society organisations in a realistic debate about key priorities, trade-offs, opportunity costs and value for money;

c providing clarity about the relative costs and benefits of the wide range of public expenditure programmes and tax expenditures;

d ensuring that all major decisions in these areas are handled within the context of the budget process.

Criteria for transparency and monitoring: Information on the setting of expenditure objective or forecast and the follow-up is openly available and major decisions are handled within the context of the budget process. Parliament, citizens and civil society organisations have a possibility to a realistic debate about key priorities, such as expenditure objective or forecasts, in the budget. There is accountability in case of non compliance with the expenditure objective.