Summary

Introduction

The Swedish budgetary framework includes a number of targets and principles that have gradually developed in a broad political consensus since the financial crisis in the 1990s. Certain targets and principles of the budgetary framework are regulated by the Instrument of Government, the Riksdag Act and the Budget Act (2011:203). Other parts are guided by statements in the legislative history and the constitutional practice[1] that has developed over the last 15 years. The budgetary framework includes a central government budget process that is disciplined in its design and application and multiannual fiscal rules in the form of a surplus target for the public sector, an expenditure ceiling for central government and old-age pension system expenditures, and balanced-budget requirements for local governments. Medium-term budgetary policy targets and rules for fiscal policy promote a long-term approach in decision-making processes and clarity in fiscal policy. The framework means that budget decisions are based on a top-down approach, in which proposals for expenditure or revenue changes are examined in the context of a pre-determined fiscal space that is largely defined by the expenditure ceiling and surplus target. This budget process helps ensure that the sum of all budget decisions does not exceed an amount compatible with the budgetary policy targets approved by the Riksdag.

In November 2011, Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States was adopted. This Directive lays down minimum rules concerning the characteristics of the budgetary frameworks to ensure Member States' compliance with obligations under the Treaty on the Functioning of the European Union (TFEU) with regard to avoiding excessive

[1] Although there is no established definition of constitutional practice, in this report it means actual and repeated application by the Riksdag and the Government.

deficits. The Directive requires Member States to establish medium-term budgetary policy targets and numerical fiscal rules that are reflected in the annual budgetary decisions and that entail consequences in the event of non-compliance. The medium-term budgetary framework is to provide a fiscal planning horizon of at least three years. It is also to include a description of the impact of planned fiscal measures on general government finances and realistic macroeconomic and budgetary forecasts. These forecasts are to undergo regular and comprehensive evaluation.

The Directive is to be transposed into national law by 31 December 2013. The inquiry, which has adopted the name 'Budgetprocess-kommittén' (the Budget Process Committee), has been tasked with presenting proposals in response to the Directive, on 1 May at the latest. This interim report considers whether the legal framework established in the legislation, legislative history and practice guarantees a binding and transparent application of the Directive or whether further measures must be taken to implement the Directive.

In the Committee's view, the Swedish budgetary framework has proven to function well and in line with the Directive. It is therefore important that no changes are made to the framework without strong reasons for doing so.

The Committee's analysis shows that certain requirements in the EU Directive have no equivalent in Swedish law or legislative history. However, it is the Committee's view that Sweden, through its practice, fulfils almost all of these requirements. This practice is assessed as being so well-established that deviations from the established procedure are judged likely to generate public criticism, from such sources as independent monitors of the application of the budgetary framework by the Riksdag and the Government. This warrants that the practice can be viewed as being sufficiently binding that most of these requirements can also be considered to be fulfilled.

The Committee's overall assessment is that the Swedish budgetary framework fulfils the requirements of the EU Directive in all areas, except for the requirement concerning regular, objective and comprehensive evaluations of the Government's macroeconomic and budgetary forecasts. The Committee therefore proposes an amendment to the Budget Act (2011:203) to the effect that the Government is obliged to regularly furnish evaluations of the forecasts presented in the Budget Bill and the Spring Fiscal Policy Bill. In addition, the requirement in the Directive concerning comparisons between the Government's forecasts and those of the European

Commission has led the Committee to propose that the Government be obliged to explain any significant differences relative to the Commission's forecasts.

Although the Committee considers that Sweden otherwise fulfils the requirements of the EU Directive, there is reason to somewhat clarify the regulations guiding the Government's forecasts. The Committee therefore proposes some minor amendments to the Budget Act concerning the forecasts that are to be presented in the Budget Bill and the Spring Fiscal Policy Bill. Under the proposal, the Budget Act will explicitly state that the Government, in its Budget Bill and Spring Fiscal Policy Bill, in line with current practice, is also to present forecasts of macroeconomic developments and public sector revenues, expenditures and debts.

The Committee has also considered the fact mentioned in its terms of reference that provisions are lacking to clarify the Riksdag's responsibilities for the medium-term perspective. It is the Committee's view that it can be considered whether provisions on medium-term budgetary policy targets should be introduced in the Riksdag Act in part to better reflect the established practice that has prevailed in this area for the last 15 years. The Committee has also considered the need for certain clarifications in the Budget Act concerning budgetary policy targets. The Committee's view, however, is that these issues should be dealt with in the final report.

Budgetary frameworks with a planning horizon of at least three years

Swedish budgetary policy targets have a medium-term time horizon. Under the Budget Act, the Government is to submit proposals to the Riksdag on surplus targets. Since 2000, the surplus target has had a medium-term definition, as it concerns an average over a business cycle. The Budget Act also requires the Government to include in its Budget Bill a proposed expenditure ceiling for the third year ahead, which means there are always adopted expenditure ceilings for a minimum of a three-year period.

Although the Government is obliged to propose surplus targets and expenditure ceilings, it is not regulated by law that the Riksdag must adopt surplus targets and expenditure ceilings. The assumption, however, is that this is done. Since these targets were introduced, the

Riksdag, acting on the Government's proposals, has decided on the medium-term budgetary policy targets.

Under the Budget Act, the Government in the Budget Bill is also to present an estimate for the distribution of expenditures between expenditure areas in the second and third budget years ahead. These estimates are approved by the Riksdag and function as a guideline for the Government's budgeting. In the Budget Bill, following established practice, the Government also presents an estimate of all of the budget's approximately 500 appropriations for the second and third budget years ahead. The Budget Act also requires the Government to present budget forecasts for the current year and the three immediately following years. The forecasts are to be based on well-defined assumptions which, according to the legislative history, are to include macroeconomic assumptions and volume trends in rule-governed expenditure systems. Following current practice, in the Budget Bill and Spring Fiscal Policy Bill the Government also presents macroeconomic forecasts and forecasts of volume trends in rule-governed expenditure systems for the current budget year and at least the three following years.

According to established practice, the Government uses the Budget Bill to describe the impact of approved and proposed fiscal policy measures on public finances for the current year and a minimum of the three subsequent years. This includes a description of the impact on the budget of the measures proposed in the Bill as well as the overall budgetary effect between two consecutive years of previously approved and proposed measures.

The EU Directive states that the budgetary framework is also to include targets for general government debt. Sweden has no separate numerical target in place for general government debt, and in the Committee's view, neither does the EU Directive require this. One of the original reasons for introducing a surplus target was to reduce net general government debt to zero. The surplus target has remained unchanged, however, although the public sector has shown positive net financial assets. The surplus target has resulted for example in consolidated gross debt falling from over 70 per cent of GDP in the mid-1990s to approximately 38 per cent in 2012. Gross debt in 2012 was lower than it was in the years immediately preceding the financial crisis. General government gross debt in 2011, as a percentage of GDP, was among the five lowest in the EU. There is thus quite a distance to the EU's gross debt target, which in the Government's view should be considered as an upper limit for Swedish gross debt.

The balanced-budget requirement for local governments in the Local Government Act (1991:900) means that individual municipalities and county councils may not approve a budget where expenditure exceeds revenue. Should the year close with a deficit nonetheless, this must be offset by a surplus within three years. If there are special circumstances, for example a strong financial position, a municipality may budget for a temporary deficit. Thus, the balanced-budget requirement for local governments can also to some extent be said to be medium-term in nature, as any potential deficit during a financial year is to be covered by a corresponding surplus in the following three years. The actual target, however, is for one year, and in light of this it can better be said to correspond with the EU Directive's requirements for numerical targets that are to promote compliance with EU fiscal policy targets and be observed in annual budgetary decisions.

In light of the above, the Committee considers that the Swedish budgetary framework fulfils the Directive's requirements for a medium-term budgetary framework.

Promoting EU reference values and the medium-term budgetary target

As mentioned above, Member States are to have numerical fiscal rules in place that specifically promote Member States' compliance with the reference values on deficit and debt of a maximum of 3 and 60 per cent of GDP, respectively. These numerical rules are also to promote multiannual fiscal planning and observance of Member States' medium-term budgetary objectives (MTO), which for Sweden means that the general government structural deficit is not to fall below -1 per cent of GDP according to European Commission measurement methods.

The Swedish numerical fiscal policy rule that primarily promotes compliance with the EU budgetary policy targets is the surplus target. The surplus target, apart from a technical adjustment of its level, has remained unchanged since its introduction in 2000. The Government has stated it aims to maintain the current surplus level of an average 1 per cent of GDP over a business cycle as long as is necessary to enable general government finances to develop in a sustainable way. The 1 per cent of GDP level provides a considerable margin for increased expenditure and lower tax revenue during a recession without threatening the EU's 3 per cent of GDP deficit reference value. This level also normally contributes to a successive reduction over time of the central government debt. Although Sweden's medium-term budgetary objective is defined differently than the surplus target, the difference of two percentage points between these two means that the surplus target normally includes a margin for active economic policy without threatening Sweden's medium-term objectives.

The expenditure ceiling does not have the same close link to EU fiscal policy targets, but provides indirect support to these targets by comprising an important instrument for ensuring the surplus target is achieved.

In conclusion, the Committee considers that Sweden's numerical fiscal policy rules, particularly the surplus target, promote compliance with EU budgetary policy targets and that Sweden, in light of this, fulfils the requirements of the Directive in this respect.

Target definition and scope of the rules

The EU Directive states that the target definition and scope of the rules is to be specified for country-specific numerical fiscal rules, which for Sweden is mainly its surplus target and expenditure ceiling.

According to the legislative history of the Budget Act, the surplus target is formulated so that it should apply to the medium-term net lending of the entire general government sector. The reasons for the surplus target – for example, that it is to contribute to long-term sustainable general government finances and to maintaining adequate margins to ensure large deficits can be avoided in times of recession – are clearly stated in the 2010 Spring Fiscal Policy Bill, which also includes a description of the indictors used to assess how well the targets have been achieved. The surplus target is of great importance in the practical application of setting the space for new reforms or the need for budget reinforcements in the Budget Bill.

According to the decisions taken by the Riksdag since the introduction of the expenditure ceiling in 1997, the expenditure ceiling in principle covers all expenditure in thecentral government budget, with the exception of central government debt interest, and off-budget expenditures for the old-age pension system. Since its introduction, the expenditure ceiling has also covered the same expenditure categories and sub-sectors of the general government sector. The legislative history of the Budget Act also states that expenditure covered by the ceiling is to be clearly defined when decisions concerning the level of the ceiling are to be taken, which is particularly important in determining whether technical adjustments of the set expenditure ceilings are justified in budgetary changes. The expenditure ceiling represents an upper limit for the expenditures subject to the ceiling and is used, consistent with what is laid down in the Budget Act, both in preparing the proposed central government budget and in carrying out budgeted activities.

Based on both explicit regulations, such as the legislative history, and established practice, it is the Committee's view that Sweden fulfils the Directive's requirements in this respect.

The link of budgetary policy targets to annual budgetary decisions

The EU Directive requires the annual budget legislation of the Member States to reflect their current country-specific numerical fiscal rules and the provisions of the medium-term budgetary framework. For the Riksdag and the Government, this means that the surplus target and set expenditure ceilings are to be taken into account when preparing and approving the state budget.

The Budget Act states that the expenditure ceiling is to be used when preparing the proposed central government budget and that the Government must take measures if there is a risk that an approved expenditure ceiling will be exceeded. This means that the Government must take into account the impact on the expenditure ceiling of both the current year and the coming years in the annual budget proposals.

The Budget Act also stipulates that the Government must report at least twice a year on how the surplus target is being met. The legislative history of the Act states that the report is to consider both how the target has been achieved and how it is expected to be achieved. The legislative history also makes it clear that the surplus target is to have a guiding role in fiscal policy. The fact that the target has a central role in determining the total room for new reforms or the need for consolidation measures is also made clear in the separate section on budgetary policy targets and room for reform that, in line with current practice, is included as part of the Budget Bill.

In the Committee's view, the legislation and established practice result in the Swedish budgetary framework being considered to fulfil the requirements of the EU Directive concerning compliance with the budgetary policy targets in the annual budget process.

Consequences of non-compliance with budgetary policy targets

The EU Directive requires Member States to specify the consequences of non-compliance with the country-specific numerical fiscal rules and the medium-term budgetary framework to contain procedures for establishing a description of the planned measures in the medium term that show how deviations from the medium-term budgetary targets should be corrected.

If there is a risk of the expenditure ceiling being exceeded, the Budget Act requires the Government to take measures within its powers or propose necessary measures to the Riksdag.

With regard to the surplus target, the Budget Act requires the Government to report twice a year on how the target is being met. Alongside this requirement, the Government has explained in several different contexts, including in the 2010 Spring Fiscal Policy Bill and in the Government Communication 'Fiscal Policy Framework', how deviations from the surplus target are to be managed.

The Committee also considers that the Government has taken these principles into account in their practical application in connection with deviations from the surplus target. For example, when there has been a risk of exceeding or falling short of the target, the Government has explained why, for example on economic grounds, the room for reform or need for saving the following year do not necessarily correspond with the adjustment of net lending that would be required to meet the surplus target for the year in question.

In the Budget Bill, the Government traditionally presents the medium-term impact on general government finances of approved and proposed measures and the measures announced in the bill.

In the Committee's view, the legislation and established practice mean that the Swedish budget framework can be considered to fulfil the Directive's requirements concerning the impact of deviations from the targets and the requirement concerning an account of the impact of medium-term policies on general government finances.

Forecasts

The Directive imposes a number of requirements on the macroeconomic and budgetary forecasts used by Member States in budgetary planning. These requirements state that the forecasts are to be realistic and comparable to the forecasts of other bodies, including those of the Commission. The forecasts are to include an analysis of the sensitivity to alternative assumptions and relevant risk scenarios, and be available to the public together with the methodologies, assumptions and relevant parameters on which the forecasts are based. The forecasts are to include projections of general government finances, even if policy remains unchanged, and an analysis of how fiscal policy measures impact the long-term sustainability of public finances. Finally, the forecasts are to be subject to regular and comprehensive evaluation based on objective criteria that are made public together with the measures deemed necessary to manage any significant bias affecting the forecast.

Past comparisons of budgetary forecasts have shown that the Government's accuracy in forecasting is at least equal to that of other independent forecasters. The Committee considers that the Government normally seeks to base its forecasts on the most likely scenario. The requirement that forecasts are to be realistic is therefore considered to be fulfilled. The practice over several years of describing sensitivity analyses and risk scenarios is also considered to meet the requirements of the Directive.

The Budget Act requires the Government in its Budget Bill and Spring Fiscal Policy Bill to present budgetary forecasts for the current budget year and the three subsequent years that are based on well-defined assumptions, which according to the legislative history of the Act are comprised of macroeconomic assumptions. In addition to this, the Government has traditionally presented detailed forecasts of medium-term general government finances. The fact that the Government is to make public its forecasts of general government net lending also follows from the legislative history of the Budget Act. The methodologies and models used in forecasting activities are largely made public in the form of details provided in the Government's economic policy bills or in separate reports published on the Government's website. The Committee considers, in light of this, that current established practice meets the Directive's transparency requirements for forecasts, including models, methodologies and assumptions.

The forecasts in the Budget Bill and the Spring Fiscal Policy Bill are in line with the Budget Act's requirements that forecasts are to be based on well-defined assumptions, including the fiscal policy decisions and proposals included in the forecasts. The impact on general government finances of fiscal policy measures included in the forecasts is presented separately in the Budget Bill. On the expenditure side of the budget, an account is also given in the Budget Bill for each expenditure limit, as are appropriation tables showing how the medium-term trend for appropriations is dependent on approved and proposed policies, changed macroeconomic conditions and, for rule-governed transfer systems, changes in volume trends as well. For taxation, the budgetary effects arising each year from regulatory changes are shown. Practice is therefore considered by the Committee to comply with the Directive's requirements on projections of general government finances based on unchanged policies.

As a result of the system that has been established for several years of reporting annually on the long-term sustainability of fiscal policy in the Spring Fiscal Policy Bill, which includes the impact of approved and proposed fiscal policy measures on sustainability, the Swedish budgetary framework is considered to fulfil the requirements of the Directive even in this respect.

The assessments of the Government's forecasts that are currently conducted by the National Institute of Economic Research, the Swedish Fiscal Policy Council and by the Government itself are largely considered to fulfil, though not completely, the Directive's requirements for regular, comprehensive and transparent assessments. In light of this, the Committee proposes the introduction of a provision in the Budget Act that obliges the Government to regularly present an evaluation of its forecasts. Deeper and more comprehensive evaluations can require considerable resourcesand should in this light be conducted approximately every third year. Considering the need for transparency both regarding methodology and background material, conducting deeper evaluations is a responsibility best conducted by the forecaster, that is the Government. However, it should be possible to engage external expertise in connection with these evaluations. The results of the evaluations are to be made public and be considered in future macroeconomic forecasts and budgetary forecasts.

The National Institute of Economic Research is tasked with comparing the Government's forecasts and forecast errors with those of other forecasters. In addition to this, the National Financial Management Authority makes comparisons with the Government's budgetary forecasts. No comparison is conducted, however, with the European Commission's forecasts. The requirement concerning regular evaluation of the Government's forecasts should include conducting an analysis of forecast differences in relation to the forecasts of other independent bodies, such as the European Commission, and furnishing explanations for any significant differences between the Government's forecasts and those of the Commission.

Although the Committee considers that in this area Sweden otherwise fulfils the requirements of the EU Directive, there is still reason to clarify the regulatory framework on a few points concerning the Government's forecasts. The Committee proposes introducing an obligation in the Budget Act for the Government to present an assessment of the long-term sustainability of general government finances and forecasts of macroeconomic developments and public sector revenues, expenditures and debts. This comprises a codification of current practice. Regulations will ensure that the Budget Act will better provide a true and fair view of the forecasts that are of particular importance in designing the state budget and the Government's proposals for guidelines for budgetary and economic policy.

Independent analysis and monitoring

The EU Directive requires specifications to ensure effective and timely monitoring of compliance with the country-specific numerical fiscal rules. The monitoring is to be carried out by an independent body.

The Swedish National Audit Office has been tasked with examining the central government annual report, which under the Budget Act is to include a follow-up of the budget policy targets adopted by the Riksdag. The Swedish Fiscal Policy Council has also been tasked with following up how the fiscal policy targets are being achieved. In light of this, the Committee considers that the Swedish framework fulfils the requirements of the EU Directive concerning independent monitoring of the fiscal rules.

Other considerations

The Committee has also considered the fact mentioned in its directive that provisions are currently lacking to clarify the Riksdag's responsibility to ensure there is a medium-term perspective. In the Committee's view, it can be considered whether provisions on medium-term budgetary policy targets should be introduced in the Riksdag Act in part to better reflect the established practice that has prevailed in this area for the last 15 years. The provisions could refer to how the Riksdag is to decide on budgetary policy targets and their relationship to annual budgetary decisions.

It can also be considered whether it should be clarified in the Budget Act that the Government is to account for significant deviations from the surplus target, and in that case how any correction to realign policy to the target should be carried out. Furthermore, it can be considered whether it should be clarified in the Budget Act that the Government in its Budget Bill, in line with established practice, is to account for the impact of proposed medium-term fiscal policy measures on public finances as part of reconciling the proposed fiscal policy measures with the surplus target.

Finally, it can also be considered whether the Government as a rule should be obliged to ensure that an independent analysis and monitoring of the budgetary targets takes place.

These questions, however, given their link to the Committee's task in other respects, should be managed within the framework of the Committee's main report.

Horizon for the expenditure ceiling

Alongside ensuring that Sweden fulfils the requirements of the EU Directive, the Committee is also to analyse the advantages and disadvantages of a three-year versus a four-year perspective for the state expenditure ceiling and consider whether any amendment is needed in this respect.

There are advantages and disadvantages with both three- and four-year expenditure ceilings. These advantages and disadvantages can also vary over time. The Budget Act states that the Government is to propose an expenditure ceiling in the Budget Bill for the third year ahead. However, there is nothing to prevent the Government from also proposing for the fourth year ahead. The

Committee considers that the current regulations in the Budget Act already include a desirable level of flexibility regarding the horizon for the expenditure ceiling and that therefore no amendment is required to the regulation.

The European Semester

The Committee is also to consider whether there are grounds for introducing provisions clarifying the link between the national budget process and the European Semester for economic policy coordination within the EU. This includes clarifying the powers of the Government and the Riksdag regarding the convergence programme and the national reform programme.

Although time for coordination between the national budget process and the European Semester are limited, particularly in connection with publication of the convergence programme and the national reform programme in late April, the process in the Government Offices has now progressed in a way that ensures a consistency between these programmes and the Spring Fiscal Policy Bill. That the contents of the programmes in all essential respects are based on Riksdag decisions and proposed guidelines to the Riksdag may also be considered to comprise a system that should be maintained but that does not need to be regulated.

The Government's efforts to inform and consult with the Riksdag on the European Semester are considered to take place in accordance with the Instrument of Government and the provisions of the Riksdag Act on the Government's obligations in this area. In light of this, it has not been possible to identify any need for further regulation of the European Semester.