



Memorandum of Understanding

between the Irish Fiscal Advisory Council and

the Department of Finance

relating to the

“Endorsement Function” of the Council under

the Fiscal Responsibility Act as amended

2013

1. INTRODUCTION

Under the Fiscal Responsibility Act 2012 (the FRA), the Irish Fiscal Advisory Council (the Council) has been assigned the monitoring and assessment functions required of an independent national institution under the Treaty on Stability, Co-ordination and Governance in the Economic and Monetary Union. The FRA establishes the Council and assigns to it responsibility for examining and reporting on the appropriateness of the fiscal stance.

Specifically, under the FRA, the functions of the Council are to:

- Assess the official forecasts produced by the Department of Finance;
- Assess whether the fiscal stance of the Government is conducive to prudent economic and budgetary management, including with reference to the provisions of the Stability and Growth Pact;
- Monitor and assess compliance with the budgetary rule as set out in the FRA, including assessment of whether exceptional circumstances exist or have ceased to exist;
- Be independent in the performance of its functions.

In addition to this assessment function, following the agreement at European level on the Regulation on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area (EU Regulation No 473/2013), Ireland is required under Article 4.4 to have its national medium-term fiscal plans and draft budgets based on independent macroeconomic forecasts, which means macroeconomic forecasts produced or endorsed by an independent body. In Ireland's case, this endorsement function is set out in the Fiscal Responsibility Acts 2012 and 2013 (henceforth referred to as the Act) that entered into force on 23 July 2013. Under the Act, the Council as an independent body (as defined in Article 2.1.a of Regulation No 473/2013) has been assigned the endorsement function, and shall *"endorse, as it considers appropriate, the macroeconomic forecasts prepared by the Department of Finance on which the Budget and stability programme will be based"*.

The purpose of this Memorandum of Understanding between the Council and the Department is to outline the modalities of the arrangements necessary for the Council to carry out this endorsement function. It deals with:

- the coverage of the macroeconomic projections that are subject to endorsement;

- the informational requirements and the broad approach that will be used by the Council in undertaking the exercise;
- timing issues;
- the form in which an endorsement may be provided; and
- provisions for a periodic review of the arrangements described in this Memorandum.

2. COVERAGE OF THE MACROECONOMIC PROJECTIONS

The overall set of macroeconomic projections to be the subject of formal endorsement by the Council are those underpinning the Budget for the following year and the Stability Programme (SPU).¹ The Government has decided that Budget Day will be on or before October 15th each year from 2013 on. The Stability Programme must be submitted to the Commission by the end of April each year.

The set of key variables taken into account in the endorsement will cover those published in the Budget and the SPU and will include, inter alia, : (i) real and nominal aggregate GDP and GNP changes; (ii) changes in major expenditure components (nominal and real), namely, personal consumption of goods and services, gross domestic fixed capital formation, net expenditure by central and local government on current goods and services, exports of goods and services, and imports of goods and services; (iii) the current account of the balance of payments; (iv) factor income and average wage compensation, employment and unemployment; and (v) HICP inflation and the GDP deflator.

3. INFORMATIONAL REQUIREMENTS AND APPROACH TO BE FOLLOWED

- a. The Department will set out its forecast methodology by way of a periodically-updated staff working paper, and engage in regular technical dialogue to ensure that Council staff and members have a full understanding of the process.
- b. For each endorsement exercise, the Department will provide, as a basis for the Council's endorsement, the full set of macroeconomic variables prepared as part of the Budget and SPU processes along with the other relevant and necessary variables used to generate the published macroeconomic projections referred to in Section 2, at annual frequency. The

¹ Regulation No 473/2013 refers to “the main assumptions of the independent macroeconomic forecasts and important economic developments which are relevant to the achievement of budgetary targets” and “an annex containing the methodology, economic models and assumptions, and any other relevant parameters underpinning the budgetary forecasts and the estimated impact of aggregated budgetary measures on economic growth.”

Department will provide the Council with the information required (including the key quantitative elements) to assess the methodology and internal consistency of the forecasts. It will also outline by way of oral presentation to the Council the elements of judgement involved in its forecasts.

- c. The Department will indicate the assumptions used for all exogenous variables, including interest rates, exchange rates, commodity prices and trading partner demand, as well as the baseline fiscal assumptions.
- d. The Department will provide in a timely manner relevant information used in the preparation of its forecasts that may reasonably be requested by the Council. Most of this information will be provided by Departmental staff. However, if important components of the Department's forecasts (for example, those for private investment or multinational sector exports) are based on views provided by other official agencies or non-official agencies, the Council may engage in direct contact with these agencies.
- e. The Department will indicate to the Council what information shared with the Council as part of the endorsement function is required to be treated as confidential under the Act.
- f. The Council will consider the appropriateness of the forecasts (as most likely projections), taking into account the suitability of the underlying forecast methodology and the plausibility of the judgements embedded in the projections. The Council recognises the inherent uncertainty surrounding forecasts and that appropriate forecasts may lie within a range.
- g. The Council will seek to develop and maintain the technical capacity and analytical expertise to evaluate in detail macroeconomic projections for Ireland. The Council will communicate regularly as to its approach to the endorsement function, including the analysis underpinning its assessments. While point estimates of macroeconomic variables are required as forecast outputs, both parties note that output volatility and the magnitude of revisions to Irish economic aggregates can be large.

4. TIMING

4.1 BUDGET

- a. It is expected that the process described in Section 3 will be ongoing, involving both written exchange of information and informal interaction. Interaction will mainly occur between members of the Council Secretariat and the relevant Department of Finance staff. The Council Secretariat and the Department will each designate one person to be the central point of contact for these exchanges (in the Department's case a member of the forecasting team), with all requests for information to be copied to the Central Budget Office, Department of Finance. Council members may also, on occasion, participate in the discussions, as appropriate.
- b. In order to ensure that the Council is in a position to carry out its formal function in an effective and timely fashion, the following timetable, will apply:
 - (i) By no later than 10 September the Department will communicate in writing to the Council the day in October on which the Budget is to be held.
 - (ii) As early as possible, in any event, by no later than fifteen working days prior to Budget day, Departmental staff will provide to the Council Secretariat their preliminary set of forecasts in electronic form. It is understood that these are provisional in nature, will necessarily not take into account data released subsequently but prior to Budget day, and serve as a basis for informal discussion. Such discussion will include a presentation by Departmental staff at a meeting with the Secretariat in which individual Council members may participate.
 - (iii) Following such interaction, no later than ten working days prior to Budget day, the Department will provide at a meeting with the Council its "provisional final" macroeconomic forecasts. These forecasts will incorporate the impact of any *aggregate* consolidation/expansionary measures foreseen in the Budget, although the *composition* between expenditure and tax measures (as well as the precise details of individual measures) may not be available, pending subsequent Cabinet decision. To the extent that such details become known, the "provisional final" forecasts could be subsequently

modified after the completion of the endorsement exercise (see Section 5), although it is not anticipated that any such modifications would have a major impact on the overall set of macroeconomic projections.

- (iv) Any revisions to the “provisional final” forecast in the light of interactions with the Council or other factors would be provided to the Council at least two working days before the final deadline to send the endorsement letter referred to in Section 5.

4.2 STABILITY PROGRAMME

The timing arrangements for the endorsement of the macroeconomic forecasts underpinning the SPU will be agreed and inserted in an amended MOU by end 2013.

5. ENDORSEMENT

An endorsement would be provided via a formal letter from the Chair of the Council to the Secretary General of the Department of Finance, and simultaneously in electronic format. This letter would be sent after the meeting referred to in 4.1.b.(iii) and no later than five working days in advance of Budget day. This letter would be made public by the Council and the Department of Finance on Budget day, once the Minister for Finance begins speaking, and will be included in the Budget book.

The letter from the Chair of the Council would not typically contain any commentary on the macroeconomic forecasts. Any Council views regarding the forecasts or parts thereof (including any possible late modifications referred to in 4.1.b.(iii)) would be contained in the Council’s subsequent Fiscal Assessment Report.

In the event that the Council were to conclude on a preliminary basis that it had significant reservations as regards the preliminary or the “provisional final” forecasts referred to above, this would be communicated to the Department immediately on an informal basis. Further discussions could then take place between the Department and the Council and a revised “provisional final” forecast addressing the concerns raised could be provided to the Council as a basis for endorsement subject to the timing set out in 4.1.b.(iii).

If, at the end of the process, the Council was not in a position to endorse the macroeconomic forecasts underlying the Budget, the Chair of the Council would write to the Secretary General prior

to the publication of the Budget outlining the reasons why such was the case, no later than five working days prior to Budget day. Such a letter would also be made public by the Council and the Department on Budget day, once the Minister for Finance begins speaking.

Departmental staff and the Council secretariat will meet no later than six weeks after each endorsement to review the implementation of the process. Council members may attend as appropriate.

6. PUBLICATION AND REVIEW

This Memorandum of Understanding will be posted on the websites of both the Council and the Department.

It is understood by both parties that the implementation of the endorsement function is a novel activity, some adjustments may be required after the initial exercise to ensure that the process is as smooth and efficient as possible.

In any event, the content of this Memorandum will be reviewed by both sides no later than one year from the date of signature. Any revisions that may prove necessary as a result of this review will be introduced subject to the agreement of both parties.

/s/ John Moran, Secretary General, Department of Finance

John McHale, Chair, Irish Fiscal Advisory Council