Comhairle Fhioscach Chomhairleach na hÉireann
Irish Fiscal Advisory Council
www.fiscalcouncil.ie | admin@fiscalcouncil.ie | (+353 1) 8632005

Embargo: 00:01 a.m. Thursday 26 January, 2012

Press Release

Strengthening Ireland's Fiscal Institutions, January 2012

This report is issued at a time of discussion of major changes in economic governance in the Euro Zone and the commitment by Ireland to introduce numeric fiscal rules as part of the forthcoming Fiscal Responsibility Bill. In this context, the report assesses elements of the fiscal framework proposed in the Department of Finance's March 2011 Discussion Document *Reforming Ireland's Budgetary Framework* and contains recommendations for the design both of a set of fiscal rules and a permanent independent fiscal advisory council.

Main Findings of Report

Fiscal Institutions for Better Fiscal Policy

- Sound management of the public finances should follow three key principles: sustainability; stability and counter-cyclicality. Committing to these principles is difficult, as evidenced by the persistent deficits and high debt-to-GDP levels in many industrialised countries.
- Well-designed fiscal rules and independent fiscal agencies can help to narrow the gap between unconstrained fiscal outcomes and desirable budgetary policies.
- Designing effective fiscal rules is challenging, as this requires an appropriate balance between the principles of sound fiscal management (flexibility) and the capacity to influence fiscal policy (credibility).
- There is a growing interest in the use of independent fiscal councils, which can both substitute for, and be a complement to numerical fiscal rules. Fiscal councils can provide an additional mechanism for raising the political costs of inappropriate policies and can be used for monitoring fiscal plans and performance.

Fiscal Rules

- Last March, the Department of Finance proposed three fiscal rules as part of the forthcoming Fiscal Responsibility Bill: a Public Finance Correction Rule (PFCR), a Prudent Budget Rule (PBR), and a Sustainable Expenditure Growth Rule (SEGR).
- While the proposed rules have many good features, the Council sees a risk that they do not always strike the right balance between prudent management of the public finances and the desirability of pursuing counter cyclical policies. Moreover, the proposed "comply or explain" enforcement mechanism is insufficiently strong.
- On rule design, the Council advocates increased flexibility, including specifying required fiscal adjustments in cyclically adjusted terms and setting reasonable limits on required rates of debt reduction.
- On enforcement, the above rules should form part of legislation. The Council also proposes that each new Government be required to set out in a Fiscal Statement explicit five year targets for the debt to GDP ratio that would include planned consolidation measures. The Government should also be required to formally report annually to the Oireachtas on its retrospective fiscal performance and prospective fiscal plans. Consistency of policy plans with legislated fiscal rules would be assessed by the Fiscal Council.

- At an EU level, the debate over the precise form fiscal rules continues to evolve in the context of discussions on the design of a new "Fiscal Treaty". The treaty may narrow the degrees of freedom available to the government in the design of Ireland's fiscal rules.

The Design of the Fiscal Council

- The Council needs to be viewed as a body that is both sound in terms of its economic analysis and independent of political influence. The design of the Fiscal Council must contain some key elements to be effective in supporting sound fiscal management.

- Members of the Council must be qualified professionals with expertise in the areas of macroeconomics and fiscal policy to ensure analytical competence. The council should have sufficient resources to allow it to produce and disseminate high-quality analysis.

- The Council's report contains detailed recommendations on the principles that are critical for the establishment and modus operandi of the Council:

    - Independence with respect to membership and budgetary management. The Council needs to be protected from the risk of inappropriate involvement in detailed budgetary/staff matters or from the risk of termination of appointments due to policy differences.

    - Full transparency concerning the work of the Council.

    - Accountability with regard to the quality of the Council's output and fulfilment of the mandate it has been given, including periodic international peer review.

Notes to Editors:

1. Strengthening Ireland's Fiscal Institutions Report, January 2012 is embargoed until 00.01am Thursday 26th January. The report will be available to download from www.fiscalcouncil.ie.

2. The report will be laid before the Oireachtas.

3. Council members and authors of the publication: Prof. John McHale (Chair, and Head of Economics NUI Galway), Mr Sebastian Barnes (OECD), Prof. Alan Barrett (TCD, on secondment from ESRI), Dr. Donal Donovan (adjunct professor University of Limerick and formerly IMF staff), Dr. Róisín O'Sullivan (Associate Professor, Smith College, Massachusetts).

Ends

Irish Fiscal Advisory Council, Whitaker Square, Sir John Rogerson's Quay, Dublin 2.