Irish Fiscal Advisory Council

Annual Report and Accounts for the Year Ended 31 December 2013

IRISH FISCAL ADVISORY COUNCIL

ANNUAL REPORT AND ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2013

CONTENTS:

CHAIRPERSON'S STATEMENT

Although the Irish Fiscal Advisory Council (the Council) was established in the summer of 2011, 2013 was the first year of operation as a statutory body following the enactment of the *Fiscal Responsibility Act 2012*. This is the Council's first annual report as a statutory body. While the focus of the report is on the year 2013, we take the opportunity to reflect on the development of the Council since 2011.

Initially, the Council's mandate covered the following areas:

- To provide an assessment of the official macroeconomic and fiscal forecasts prepared by the Department of Finance.
- To provide an assessment of whether or not the fiscal stance of Government is conducive to prudent economic and budgetary management.
- To monitor and assess compliance with the Budgetary Rule as set out in the *Fiscal Responsibility Act 2012*.

In July 2013, a further strand was added to our mandate:

- To endorse the official macroeconomic forecasts produced by the Department of Finance.

Since our establishment, the Council has sought to ensure that we fulfil our mandate as effectively as possible. We have worked to develop our analytical capacity so that statements included in our *Fiscal Assessment Reports* are well-founded. We have endeavoured to present our analytical work in a way that informs debate and discussion around fiscal policy issues. We have also engaged in public debate through, for example, our appearances before the Joint Oireachtas Committee on Finance, Public Expenditure and Reform.

With regard to analytical capacity, the addition of the endorsement function to our mandate in 2013 brought particular challenges. The Council formed the view that in order to endorse forecasts it would be necessary to generate internal benchmark projections and so models had to be developed for this purpose. The on-going development of these models will form part of the work-programme in the coming years. Through this work we expect to contribute to a wider effort to improve economic modelling and forecasting in Ireland.

The transition to being a statutory body in 2013 meant that the Council adopted the Code of Practice for the Governance of State Bodies. During 2013, we set about adopting and implementing policies and procedures in line with this Code. For example, we adopted a Code of Business Conduct and established an Audit and Risk Committee. The Council also worked with an outside firm of accountants to review internal control systems and procedures.

The primary outputs of the Council are our bi-annual *Fiscal Assessment Reports* which have typically been published prior to the annual *Budget* and *Stability Programme*. These reports have attracted considerable attention and that has helped to ensure that the views of the Council feature in debates on fiscal issues. Detailed responses are also now provided by the Minister for Finance following the publication of each *Fiscal Assessment Report*. With Ireland's exit from the bailout programme in 2013, the Council finds itself in a changed landscape as we look to 2014 and beyond. The Council will continue to strive to provide assessments that are analytically well-founded, well-communicated and independent of Government.

John McHale
Chair

Introduction and Background to the Council

The Irish Fiscal Advisory Council ('the Council') was established on an interim basis in July 2011 and on a statutory basis in December 2012 by the *Fiscal Responsibility Act 2012*. The Council is comprised of a five member Council (details below) and a five-member, full-time Secretariat, headed by a Chief Economist / Head of Secretariat.

The Council's mandate (detailed below) is to provide independent assessments of official macroeconomic and budgetary forecasts, assessments of compliance with the statutory Budgetary Rule, assessments of the overall stance of fiscal policy, and endorsements (as appropriate) of the official macroeconomic forecasts prepared by the Department of Finance.[1]

While the establishment of a fiscal council was a requirement of the *EU/IMF Programme of Financial Support for Ireland* (December 2010), it had been proposed domestically in the *National Recovery Plan 2011-2014* and by the Joint Committee on Finance and the Public Service in November 2010.[2,3] The Programme for Government of the new Government, which took office in March 2011, committed to the establishment of a Fiscal Advisory Council. The policy changes in Ireland were also part of more general moves at a European level to strengthen fiscal governance through reforms to the *Stability and Growth Pact and the Treaty on Stability, Coordination and Governance*.

The *Fiscal Responsibility Act 2012* (December) put the Council on a statutory footing.[4] The Act provides for an annual financial ceiling of €800,000 for the Council.[5] Within this ceiling, the amount incurred by the Council in performing its functions is met from the Central Fund.

The Council has four legally mandated functions. The first three were assigned in the *Fiscal Responsibility Act 2012*. The fourth function (endorsement) was assigned to the Council in July 2013. These functions are as follows:

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[1] The endorsement function was assigned to the Council in mid-2013 following an amendment to the *Fiscal Responsibility Act 2012*. See: http://www.irishstatutebook.ie/pdf/2013/en.act.2013.0029.pdf.

[2] The Joint Oireachtas Committee report is available at: http://www.oireachtas.ie/documents/committees30thdail/j-financepublicservice/reports/20101111.pdf.

[3] The initial Department of Finance proposal was set out in detail in the discussion document *Reforming Ireland's Budgetary Framework: A Discussion Document*, March 2011 available at: http://www.finance.gov.ie/sites/default/files/budgetref.pdf.

[4] Prior to the publication of the Act, the Council published a report *Strengthening Ireland's Fiscal Institutions* (January 2012), outlining our views on the design of a new fiscal framework for Ireland that encompassed both fiscal rules and a permanent independent fiscal council.

[5] This is subject to adjustment in line with inflation.

1. **To provide an assessment of the official macroeconomic and fiscal forecasts** produced by the Department of Finance and published in the *Stability Programme* and in the *Budget*.

2. **To provide an assessment of the whether or not the fiscal stance** of Government (as set out in each *Budget* and *Stability Programme*) is conducive to prudent economic and budgetary management, with reference to the EU Stability and Growth Pact.

3. **To monitor and assess compliance with the Budgetary Rule** as set out in the Fiscal Responsibility Act.[6]

4. **To endorse the official macroeconomic forecasts** prepared by the Department of Finance in relation to each *Budget* and *Stability Programme*. This follows revised EU requirements to have national medium-term fiscal plans and draft budgets based on independent macroeconomic forecasts, which means macroeconomic forecasts produced or endorsed by an independent body. A joint Memorandum of Understanding (MoU) between the Council and the Department of Finance underpins the endorsement process and was formulated and agreed in mid-2013.[7]

The Council publishes bi-annual *Fiscal Assessment Reports* in line with its mandate and submits them to the Minister for Finance. These reports are then published within ten days. The Council is also required, when requested to do so, to account for its performance to a Committee of either House of the Oireachtas.

[6] The budgetary rule requires that the budgetary position of the general government is in balance or in surplus, or is moving at a satisfactory pace towards that position. The Council must also assess whether any non-compliance is a result of 'exceptional circumstances'. This could mean a severe economic downturn and/or an unusual event outside the control of Government which may have a major impact on the budgetary position.

[7] The Council's *Fiscal Assessment Report* (November 2013) detailed the process in the run up to *Budget 2014*. The MoU was subsequently revised in February 2014 and can be accessed here: http://www.fiscalcouncil.ie/wp-content/uploads/2012/08/MoU_Feb2014.pdf

Membership of the Council and its Staff

The Council consists of five members including the Chair. The Council has a strong international dimension with three of the five members based outside of Ireland. Appointments are made by the Minister for Finance on the basis of a range of criteria such as:

- competence and expertise in domestic or international macroeconomic or fiscal matters, and
- ensuring an appropriate balance between men and women in the membership of the Council, where practicable.

All current Council members were appointed upon the establishment of the Council in 2011. Appointments were made on a staggered basis with terms ranging from two to four years. Thereafter a standard term will be four years. Current appointments were reset following the establishment of the Council on a statutory basis at end-2012. Existing (and future) Council Members will be eligible for one additional term.

The Council members are:

John McHale (Chair): Established Professor of Economics, National University of Ireland, Galway.

Sebastian Barnes: Economic Counsellor to the Chief Economist, Organisation for Economic Co-operation and Development (OECD), Paris.

Alan Barrett: Research Professor and Head of the Economic Analysis Division, Economic and Social Research Institute (ESRI), Dublin.

Donal Donovan: formerly a Deputy Director at the International Monetary Fund (IMF), Washington. Currently Adjunct Professor, University of Limerick and Visiting Lecturer, Trinity College Dublin.

Róisín O'Sullivan: Associate Professor of Economics, Smith College, Massachusetts.

Council members can be removed from office by the Minister only under specific circumstances, which are set out in detail in the legislation underpinning the Council. Furthermore, such a decision requires a resolution of Dáil Éireann.

The Council has the power to appoint staff members to the Council's Secretariat. These appointments require prior consent by the Minister for Finance (following consultation with the Minister for Public Expenditure and Reform).

Review of Activities

Prior to the Council becoming a statutory body, the Council operated on an administrative basis (between July 2011 and December 2012). As this is the first Annual Report published by the Council, it reflects on work undertaken by the Council over this interim period as well as the period for which it has been in effect as a statutory body.

IFAC's Interim Phase (July 2011-December 2012)

During the pre-statutory interim phase, the Council published three *Fiscal Assessment Reports* (October 2011, April 2012 and September 2012). All three reports concluded that the fiscal stance of the Government was within the range of appropriate courses of action. However, the Council at the time of each report favoured more front-loaded fiscal adjustment after weighing up the state of the economy and concerns over Irish sovereign creditworthiness.

The *Fiscal Assessment Reports* examined the Department of Finance's economic projections both on an *ex-ante* and *ex-post* basis. The reports highlighted a pattern of downward revisions to growth forecasts but noted that the Department of Finance's macroeconomic forecasts did not appear biased relative to other forecasters. Each report tried to emphasise the high levels of uncertainty surrounding economic forecasts. To illustrate this, the Council developed fan charts for key macroeconomic and fiscal aggregates. The Council developed its own Fiscal Feedbacks model which linked GDP growth, fiscal aggregates and debt dynamics.

The Council also undertook an extensive look at macroeconomic forecasts in Ireland as well as tax forecasts produced by the Department of Finance.

Each *Fiscal Assessment Report* was sent to the Minister for Finance and published within ten days. The Council also appeared before the Oireachtas Committee of Finance, Public Expenditure and Reform following the publication of each of these reports. All reports have been launched at a formal press conference, and each has received extensive print and broadcast media coverage.

Fiscal Assessment Reports

Fiscal Assessment Report, October 2011

This first *Fiscal Assessment Report* was published by the Council in October 2011, based on the *Stability Programme Update* (April 2011). The report noted that the Department of Finance's budgetary and macroeconomic projections were broadly appropriate, albeit with some downside risks. The high levels of uncertainty surrounding macroeconomic and budgetary projections were highlighted. Based on information available at the time, the Council was of the view that additional discretionary adjustments of some €400 million would be needed to comply with the General Government deficit target in 2012.

In terms of the fiscal stance to 2015, the Council favoured a more rapid restoration of sound public finances after weighting creditworthiness and debt sustainability concerns with domestic demand. The Council felt it more prudent to target a lower General Government deficit in 2015 of the order of 1 per cent of GDP, rather than the 2.8 per cent target indicated in the *Stability Programme*. This recommendation was not made lightly and the Council acknowledged the painful measures already taken since 2008.

In light of the manifold risks prevailing at the time, a more rapid restoration of sound public finances was seen as desirable for regaining creditworthiness and providing some insurance against existing EU/IMF Programme targets. Longer term advantages for the economic and financial health of the country in pursuing such a course of action were also paramount in the Council's considerations. The Council also stressed the advantages to the Government providing more detail on planned adjustments while also not reducing margins of manoeuvre by selectively putting certain measures (e.g. changes in tax rates, social welfare and public sector pay) out of bounds.

The Government responded to the Council's report in the *Medium-Term Fiscal Statement*, November 2011.

Fiscal Assessment Report, April 2012

The second *Assessment Report* (April 2012) assessed the macroeconomic and budgetary projections set out by the Government in *Budget 2012,* including the appropriateness of the overall stance to 2015, in advance of the 2012 *Stability Programme*.

The report highlighted further downward revisions to domestic and international forecasts of economic activity and the continued high degree of uncertainty relating to fiscal and macroeconomic projections. This, in part, reflected unknowns relating to external developments and the dynamics of the "post-bubble" domestic economy. The Council noted the increase in the level of budgetary adjustment in *Budget 2012* so as to meet existing targets. This had been signalled in the Council's first *Assessment Report*. The report also looked in detail at tax projections, specifically forecasts for VAT receipts. The Council also undertook simulations to highlight the sensitivity of budgetary aggregates to changes in the macroeconomic outlook using its own Fiscal Feedbacks model. This model was documented in the report.

Assessing the fiscal stance, the Council determined that the headline General Government deficit targets set out in *Budget 2012* were within the range of appropriate courses of action, albeit the Council favoured more fiscal consolidation than planned for the reasons outlined in its October 2011 *Fiscal Assessment Report* and also factoring in the latest economic developments. The report also emphasised that the fiscal adjustment path was not self-defeating in terms of reducing deficit and debt ratios, while also highlighting the need to adhere to deficit targets given the fragile nature of Irish creditworthiness.

The Government responded to the *Assessment Report* in the *2012 Stability Programme Update*.

Fiscal Assessment Report, September 2012

The third *Assessment Report* - and also the final report in the Council's interim phase - was published in September 2012 in advance of *Budget 2013* (and following the *Stability Programme Update 2012*). The report followed the structure of the previous two reports but contained a more detailed study on macroeconomic forecast errors and also introduced the usage of fan charts to illustrate uncertainty.

Assessing the budgetary forecasts, the Council pointed to several recent developments including spending overruns that had emerged in Health and Social Protection. The report highlighted that deficit targets had been overachieved owing to revisions to interest payments and the impact of banking related revenues. The Council called for more comprehensive and timely explanations to be provided on methodological changes and data revisions that impact on the fiscal outturn or official forecasts, on sources of major modifications to forecasts, and on the components of non-tax revenues.

The Council considered the Government's fiscal stance at the time of the report to be prudent. However, both debt sustainability and the creditworthiness of the State remained fragile. Reflecting these vulnerabilities, the Council proposed an alternative fiscal stance involving a total of €1.9 billion in additional adjustments over the period to 2015 compared to the Government's baseline. This level of additional adjustment was scaled back by €0.9 billion relative to the previous *Fiscal Assessment Report* due to continued weakness in demand and some further improvement in market assessments of Ireland's creditworthiness.

The report noted the fragile nature of debt sustainability and how judgements on the issue are coloured by whether GDP or GNP provides the most appropriate measure of Ireland's fiscal capacity. Recognising the limitations of these measures, the Council developed a "hybrid" measure of Ireland's fiscal capacity. The hybrid measure put differential weight on the fiscal capacity of a euro of GNP and a euro of GDP-GNP excess. The hybrid measure showed that fiscal adjustments were more challenging than under the standard GDP comparison.

Finally, the report provided an assessment of compliance with fiscal rules under the *EU Stability and Growth Pact*. A policy and economic scenario extended to 2020 showed that existing plans were consistent with compliance with all rules, but implied the need for a sustained period of expenditure restraint – effectively flat expenditure in real terms – in the absence of discretionary tax increases.

The Government provided a more detailed response to the September 2012 *Assessment Report* in the *Medium-Term Fiscal Statement, November 2012*.

THEMED REPORTS IN 2012

The Council published two themed reports in January 2012; *Fiscal Rules for Ireland* and *Strengthening Ireland's Fiscal Institutions*.[8] The first report was commissioned by the Council from an external consultant to provide guidance on the design of fiscal rules in Ireland in advance of the *Fiscal Responsibility Act.*[9] It provided the Council with background analysis on Irish fiscal performance, the international experience of fiscal rules and provided a critique of the Government's planned fiscal rules.[10]

The second report, *Strengthening Ireland's Fiscal Institutions,* was issued at a time of discussion of major changes in economic governance in the Euro Area. The report was the Council's response to the Department of Finance's proposed fiscal framework. It assessed elements of the proposed framework and made a series of recommendations for the design of a set of fiscal rules and for a permanent independent fiscal advisory council.[11]

ACTIVITIES IN 2013

The Council became a statutory body in December 2012 with the passing of the *Fiscal Responsibility Act 2012* (FRA). During 2013, the Council published two *Fiscal Assessment Reports* (April and November) as well as one themed report providing an in depth analysis of the Government's balance sheet.

FISCAL ASSESSMENT REPORT, APRIL 2013

In April, the Council published a *Fiscal Assessment Report* following *Budget 2013* and in advance of the *Stability Programme*. The report noted the significantly better than expected 2012 budgetary outturn

[8] http://www.fiscalcouncil.ie/publications/

[9] Hagemann, Robert. Fiscal Rules for Ireland, January 2012.

[10] Department of Finance, "Reforming Ireland's Budgetary Framework: A Discussion Document," March 2011.

[11] However, the subsequent Fiscal Compact Treaty restricted the degrees of freedom available to Euro Area governments in relation to fiscal rules. The Fiscal Compact Treaty is formally known as the *Treaty on Stability, Coordination and Governance in the Economic and Monetary Union*.

relative to the outlook in *Budget 2013* based on a higher level of nominal GDP and Exchequer data. Furthermore, the promissory notes transaction was adjudged to have reduced the projected 2015 General Government deficit by 0.6 per cent of GDP relative to previous forecasts.

The combination of these factors saw projected General Government deficits for 2013-2015 improve and served to accomplish the “margin of safety” sought by the Council in its previous *Assessment Reports*. As such, it was deemed that there was no longer a case for additional budgetary tightening beyond existing plans. The Council cautioned, however, against any easing in the planned discretionary adjustments of €3.1 billion for 2014 and €2 billion for 2015 on foot of recent positive developments. The overall fiscal stance of Government was again assessed to be conducive to prudent economic and budgetary management.

Significant uncertainties in relation to growth prospects and the challenging nature of planned expenditure reductions were stressed in the report. In an analysis of the past forecasting performance of the Department of Finance, the Council highlighted a pattern of domestic demand being overestimated with net exports underestimated. The uncertainty surrounding growth forecasts for the Irish economy was again emphasised in the light of the complex dynamics of household, business, bank and Government balance sheet repair.

As part of background work to this report, two representatives of the Council met with officials in the Department of Finance, the Central Bank of Ireland and the Economic and Social Research Institute to develop a better understanding of their approaches to short- and medium-term macroeconomic forecasting. The same representatives also met with officials in the CPB Netherlands Bureau for Economic Policy Analysis to discuss their approaches to forecasting. The report included details on findings in relation to economic forecasting with particular emphasis given to the approaches being followed by the Department of Finance.

Based on the better than expected 2012 outturn and the promissory note transaction, the General Government deficit to GDP ratio in 2015 appeared likely to be closer to 2 per cent of GDP (compared to the official target at the time of 2.9 per cent) based on technical adjustments made by the Council to *Budget 2013* projections. This assumed the full implementation of the Government’s planned €5.1 billion in consolidation measures in 2014-15 taking the nominal GDP growth outlook from *Budget 2013*.

While the budgetary outlook had improved, the Council highlighted the expenditure pressures in Health and Social Protection and the need to deliver sizable expenditure savings. Fan chart analysis by the Council served to once again highlight the sensitivity of key budgetary aggregates to changes in the macroeconomic outlook. The analysis suggested a one-in-three probability that the General Government deficit will exceed the 3 per cent of GDP target in 2015 based on unchanged policies. While the report noted compliance with the budgetary rule, the serious measurement challenges posed by the structural budget balance were emphasised.

The report observed that the creditworthiness of the State in financial markets could be further reinforced by post-programme precautionary funding arrangements and extensions to the maturities on official loans. The report also contained an extensive discussion of fiscal multipliers.

The Government provided a detailed response to the report in the *Stability Programme Update, April 2013.*

Fiscal Assessment Report, November 2013

The *Fiscal Assessment Report, November 2013* was published following the publication of *Budget 2014* in October. The report acknowledged the continuing progress being made in repairing the public finances and concluded the Government's planned fiscal stance remained "conducive to prudent economic and budgetary management". The *Budget 2014* projections also implied compliance with all national and European fiscal rules. However, the Council stressed the need for a fuller assessment of risks, particularly those stemming from contingent liabilities, growth and interest rates.

The report drew attention to the Government's decision to reduce the planned fiscal adjustment in *Budget 2014*. This had removed the previously existing "margin of safety" relating to the key 3 per cent Stability and Growth Pact deficit ceiling for 2015. Analysis by the Council suggested the probability of breaching the 3 per cent ceiling in 2015 had risen from an estimated one-in-three to an estimated one-in-two as a result of the decision to do less adjustment.

The Council also highlighted the public confusion on the size and composition of the budgetary adjustment contained in *Budget 2014*. While acknowledging recent improvements in fiscal reporting, the Council suggested that future Budget statements should identify clearly the impacts of consolidation measures. The Council also re-iterated concerns over expenditure pressures in certain key areas (notably Health). The report also noted that the Government's current expenditure ceilings had not been binding and that the majority of the slippage appeared to arise from weaker economic conditions and policy decisions.

The report also marked the completion of the first endorsement exercise (detailed below). While the Council endorsed the macroeconomic projections underlying *Budget 2014,* a significant reservation was expressed about the implied quarterly profile for consumption spending. However, following clarifications by the Department of Finance on the assumptions relating to data revisions, the Council assessed that the macroeconomic forecasts were within its endorseable range.

Indicating its earlier support for an application for a precautionary credit line, the Council cited the fragility of the international financial environment. Provided it had come with reasonable terms and conditions, the Council assessed that such a facility would have represented valuable additional protection against any renewed funding pressures as Ireland exited the EU/IMF Programme.

On the 19 December 2013, the Minister for Finance formally responded to the Council's November 2013 *Fiscal Assessment Report* by way of a letter. This letter was published on the Council's website.

Oireachtas Appearances

In 2013, the Council appeared twice before the Oireachtas Committee on Finance, Public Expenditure and Reform (on 24 April and on 5 December). These appearances followed the publication of the *Fiscal Assessment Reports*.

While the focus of each appearance was the preceding *Fiscal Assessment Report*, discussions with the Committee dealt with broader macroeconomic and fiscal issues. Many of the issues discussed in 2013 were of a technical nature, such as, for example, the impact of fiscal multipliers, although there was much discussion on policy-related matters, for example the use of a precautionary credit line.

Appearing before Committees of the Oireachtas is consistent with the Council's goal to "promote awareness of fiscal policy issues" set out in the Council's *Strategic Plan 2014-2016*. The Council has reviewed each of its Oireachtas appearances and has taken a number of suggestions on board in its subsequent reports. For example, the *Fiscal Assessment Report* (November 2013) contained extended economic projections to the end of the decade following queries by the Finance, Public Expenditure and Reform Committee relating to this period. Under reasonable assumptions, this analysis indicated that the most difficult phase of the adjustment should be broadly complete in 2015/2016.

The role and functions of the Council have been also discussed at Oireachtas appearances, including the Council's endorsement of the Department of Finance's macroeconomic forecasts for *Budget 2014*.

Finally, the extent to which the Council has influenced Government policy has also been raised. In particular, the extent of the Government's engagement with the Council has been discussed. On these points, the Council has emphasised that each of the *Fiscal Assessment Reports* has concluded that the Government's fiscal stance is "conducive to prudent economic and budgetary management" and so the gap between the Government's position and that of the Council should not be overstated.

However, if a Government began to pursue imprudent fiscal policies in the future, the Council's would highlight this.

THEMED REPORTS IN 2013

In September 2013, a themed report *The Government's Balance Sheet after the Crisis: A Comprehensive Perspective*, was published. This report took a comprehensive look at the financial assets and liabilities of Government, as well as implicit and contingent liabilities. The paper also considered the decision to wind-up the Irish Bank Resolution Corporation and to replace the promissory notes with long-term government bonds.[12] The paper highlighted the need for a broader approach to be taken when assessing the public finances while also drawing attention to the sharp increase in overall indebtedness as a result of the financial crisis. The main findings of this paper were presented to the Dublin Economics Workshop Annual Economic Policy Conference in October.

ENDORSEMENT EXERCISE FOR BUDGET 2014

Following the agreement at the Euro Area level Ireland is now required 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.[13] This endorsement function was assigned to the Council following an amendment to the *Fiscal Responsibility Act* in July 2013. The Council is required to "endorse, as it considers appropriate, the macroeconomic forecasts prepared by the Department of Finance on which the Budget and stability programme will be based".

A joint Memorandum of Understanding (MoU) was drawn up between the Department of Finance and the Council to facilitate endorsement. The MoU was published on the websites of both organisations.

The Council developed its own forecasting methods and analytical capacity to support the endorsement function. Endorsement by the Council is based on whether the Department of Finance's forecasts are within an "endorseable range" of appropriate forecasts, taking into account the methodology and the plausibility of the judgements involved. This range is also informed by benchmark projections prepared by the Council's Secretariat, past macroeconomic forecast errors and other information available at the time of the endorsement exercise.

This endorsement function was carried out for the first time by the Council for *Budget 2014*. Given the tight timelines involved between the amendment to the Act and the finalisation of the forecasts for

[12] The results of modelling work to assess the impact of this decision were included in the paper. This work was also made available on the Council's website.

[13] EU Regulation No 473/2013 - 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.

Budget 2014, the Council was required to work extensively on forecasting over the June to October period.[14] As part of this work, representatives of the Council met with some domestic forecasters.[15] There were also teleconferences held with the IMF and European Commission. The purpose of these discussions was to get a range of views on issues forecasters were dealing with, both data-related as well as substantive economic matters.

This work culminated in the preparation of a set of staff benchmark projections prior to the official endorsement meetings between the Department and the Council. These projections were subsequently published in the *Fiscal Assessment Report* (November 2013).

The Council endorsed the macroeconomic forecasts underlying *Budget 2014* based on a provisional final set of projections provided by the Department of Finance in advance of the Budget. The Council was satisfied that these forecasts were within its endorseable range. As part of the endorsement exercise, the Council expressed a significant reservation relating to the quarterly profile for personal consumption expenditure given the Central Statistics Office's estimates for the first half of 2013. This was resolved following clarifications by the Department of Finance regarding their assumptions relating to possible data revisions.

Other Activities by the Council in 2013

During 2013, the Council participated in a number of meetings, seminars and presentations.[16]

- The Council met with the Department of Finance on seven occasions.
- The Council met with the Troika on four occasions.
- The Council appeared before the Joint Oireachtas Committee on Finance, Public Expenditure and Reform on two occasions.

[14] This resulted in an additional economist being hired on a short-term basis.

[15] In September 2013, the Secretariat had discussions with forecasters at the Central Bank, the European Commission, the ESRI, the IMF, Davy, Goodbody, Investec, the Nevin Economic Research Institute and Mr Joe Durkan of University College Dublin. The Secretariat also met with the Central Statistics Office to gain further insights into topical economic issues and to gain more information on the statistical treatment of a number of key variables.

[16] References to the Council here refer to meetings in which at least one member of the Council was present.

Sample of Presentations and Appearances in 2013

March

The Functions and Impact of Fiscal Councils - Sebastian Barnes at a joint workshop by the IMF Fiscal Affairs Department and Offices in Europe.

April

John McHale appeared before the Joint Committee on European Union Affairs in relation to Completing the Economic and Monetary Union.

June

Whither Irish Fiscal Policy? – John McHale at the Irish Tax Institute and Revenue Joint Conference 2013: Technology, Tax Compliance and the Future, Limerick.

October

Economic and Fiscal Outlook – John McHale at Human Resources Conference, National University of Ireland, Galway.

The Government's Balance Sheet after the Crises: A Comprehensive Perspective - Sebastian Barnes and Diarmaid Smyth at the Dublin Economic Workshop 2013 Annual Policy Conference.

November

Resolving the Crises: Where do we stand? - John McHale at the Irish Small and Medium Enterprises Association (ISME) national conference.

Getting Started: Ireland's Fiscal Advisory Council - John McHale at the European Commission network meeting of independent fiscal institutions.

Irish Fiscal Advisory Council - Diarmaid Smyth at the PEM PAL conference in Dublin.

December

Looking Beyond the Bailout: A View from the Irish Fiscal Advisory Council - John McHale at the Institute of International and European Affairs (IIEA) Economists Group.

External Meetings Attended

February

John McHale chaired the session *Independent Fiscal Institutions and Access to Information* at the annual meeting of the OECD Parliamentary Budget Officials and Independent Fiscal Institutions.

October

Sebastian Barnes participated in a network meeting of independent fiscal institutions hosted by the Slovak Council for Budget Responsibility.

Meetings of the Council

In 2013, the Council held eleven meetings in Dublin. The dates of these meetings and the attendees are set out in Table 1. The Council also held a number of teleconferences in 2013. For completeness, Council meetings in 2011 and 2012 are shown in Table 2.

Table 1: Council Meetings in 2013

	John McHale	Sebastian Barnes	Alan Barrett*	Donal Donovan*	Róisín O'Sullivan
Council Meeting Attendance	11/11	11/11	11/11	11/11	11/11
10 January	Y	Y	Y	Y	Y
07 February	Y	Y	Y	Y	Y
08 March	Y	Y	Y	Y	Y
25 April	Y	Y	Y	Y	Y
24 May	Y	Y	Y	Y	Y
28 June	Y	Y	Y	Y	Y
02 August	Y	Y	Y	Y**	Y
29 August	Y	Y	Y	Y	Y
29,30 September	Y	Y	Y	Y	Y
25 October	Y	Y	Y	Y	Y
06 December	Y	Y	Y	Y	Y

*Also members of the Council's Audit and Risk Committee. **Part attendance.

Table 2: Council Meetings in 2011 and 2012

	John McHale	Sebastian Barnes	Alan Barrett	Donal Donovan	Róisín O'Sullivan
2011	6/6	6/6	5/6	6/6	6/6
2012	11/11	11*/11	11/11	11/11	10*/11

*Part attendance for one of the meetings.

Internal Audit, Governance, Fees and Staffing

The Council secretariat is based in the offices of the Economic and Social Research Institute (ESRI) as was agreed by the Department of Finance when the Council was established in 2011. Office accommodation and support services, mainly in the areas of Accounts, IT, and Corporate Services, are provided to the Council by the ESRI.

Audit and Risk Committee

The Audit and Risk Committee of the Council was set up in 2013 and met for the first time in April. It comprises of two Council members.[17] It reports to the full Council on a periodic basis. The function of the committee is to:

- ensure the Council's compliance with its corporate governance obligations;
- provide oversight of key risks facing the Council.

In 2013, the Committee met on two occasions and it commenced work on reviewing internal controls. To assist in this work, external consultants were hired. The review of internal controls within the Council was finalised in February 2014. A risk register was prepared by the Council and was also finalised in March 2014. The Committee has begun the process of reviewing the operation of those services provided to the Council by the ESRI.

In early 2014, the Committee felt there was a need to expand its membership to include a person with significant audit knowledge. In this context, Mr John Buckley (former Comptroller and Auditor General) joined the Committee.

Internal Audit

The Council operated on an administrative basis from July 2011 until its statutory establishment on the 31 December 2012. Accounting services were provided by the ESRI and in the interim phase the Council's income and expenditure was audited under the ESRI's internal and external audit systems.

On becoming an independent statutory body, IFAC began the process of developing its own internal audit function. In 2013 the Council engaged external consultants to undertake its preliminary independent internal audit work. The audit work undertaken was designed to provide the Council with the information necessary to evaluate the organisation's system of internal control under the following key components: control environment, risk assessment, control activities, information and communication, and monitoring. The outcome was reviewed by the Audit & Risk Committee and by

[17] The members are Alan Barrett (Chair of the Committee) and Donal Donovan.

the Council, and contributed to its assessment of the organisation's system of internal controls in relation to 2013.

Disclosure of Interests

In accordance with the Code of Practice for the Governance of State Bodies, the Council has a Code of Business Conduct which includes guidance in relation to the disclosure of interests by Council Members. These procedures were complied with.

Council members are designated directors for the purposes of the *Ethics in Public Office Acts 1995 and 2003*, and have obligations in relation to disclosure of material interest and an annual statement of interest under the terms of the Acts.

Corporate Governance

The Council carries out the statutory functions assigned to it under the *Fiscal Responsibility Acts 2012 and 2013*. Over the period of our operation on an administrative basis (July 2011 to December 2012), the Council began to put in place systems of internal control such as a travel policy and systems relating to the processing of transactions. In our first year of operation as a statutory body, our systems of governance, control and risk management have further evolved. For example, a Code of Business Conduct was adopted and, as noted above, an Audit and Risk Committee was established. Further work will be undertaken in 2014 so that our systems continue to evolve.

Fees and Expenses of Council Members

Council fees payable are sanctioned by the Minister for Finance and set by the Department of Public Expenditure and Reform - €20,520 for the Chair of the Council and €11,970 for Council members. Where members, including the Chair, are employed by a body within the Irish public sector, no fee is payable to the member concerned. Fees incurred in 2013 totalled €39,770 inclusive of Employer PRSI of €3,860. Fees payable to Mr Sebastian Barnes are directed to his full-time employers, the OECD, as compensation for time spent on Council business.

Expenses incurred by Council Members amounted to €28,315 in the year, mainly reflecting travel and subsistence costs incurred by international and non-Dublin based members attending Council meetings in Dublin.

Compensation for Employer Costs Incurred

Due to the time commitment necessary to fulfil the functions of the Council, a time buy-out is in place to compensate the full-time public sector employers of the Chair and one Council Member for costs incurred due to their absence on IFAC business. In 2013, €19,750 was paid to the National University of Ireland, Galway and €11,970 to the ESRI.

STAFFING

Since its inception the Council has operated with a full-time secretariat of three persons, all of whom were seconded from various organisations. In 2013, the Council ran three recruitment competitions with the aim of increasing staff numbers to five. As part of the process, three individuals were recruited, one on a secondment basis and two others on direct contracts with the Council. [18] All recruitment competitions run by the Council followed prior sanction being granted from the Minister for Finance (following consultation with the Minister for Public Expenditure and Reform) in line with the legislation.

As part of the endorsement exercise in 2013, the Council elected to hire an additional economist on a part-time basis from June through to September to work extensively on short-term macroeconomic forecasting.

[18] As of mid-February 2014, the Secretariat had five full-time employees.

Strategic Objectives

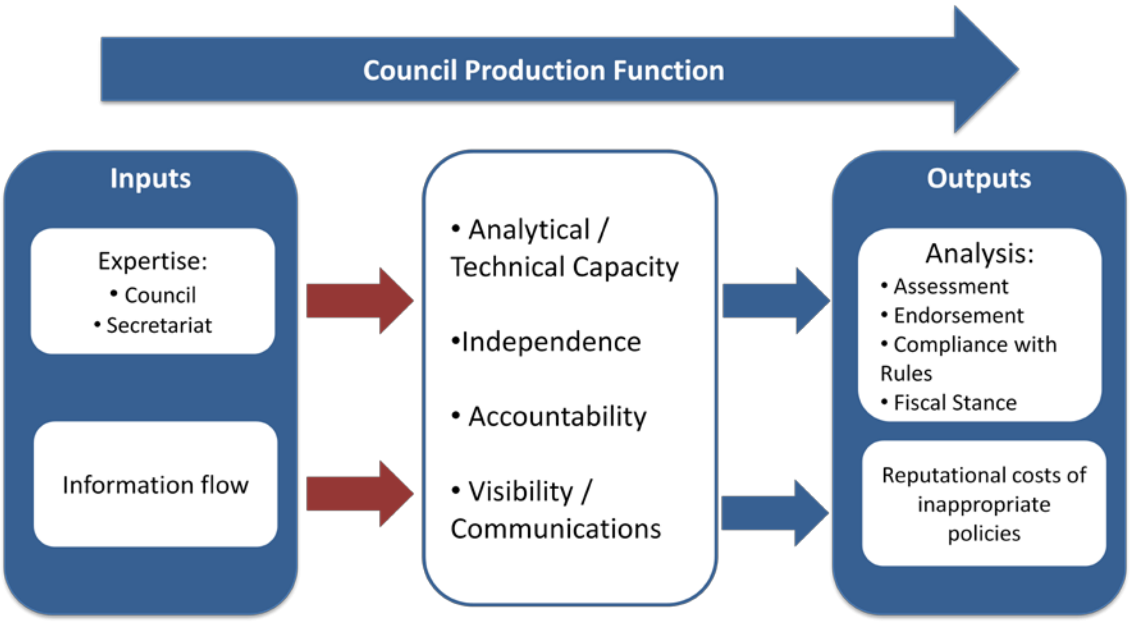
The Council's vision is for an economy with broadly based growth in incomes and employment founded on sustainable policies.

The Council's mission is to support the effectiveness of fiscal policy in the near- and medium-term through delivery on each element of its mandate as set out in the legislation underpinning the Council. To fulfil this mission, we have identified one central goal and three supporting goals. These are set out in detail in the Council's *Strategic Plan 2014-2016* (published March 2014) and are summarised here:

- **Central Goal.** Deliver on all elements of our **mandate**: assessment, endorsement and compliance.
- **Supporting Goal 1.** Ensure **compliance** with all requirements for a statutory body.
- **Supporting Goal 2.** Promote **awareness** of fiscal policy issues.
- **Supporting Goal 3.** Continuously improve **analytical capacity**.

The Council's intentions to deliver on these goals is encapsulated visually in Figure 1.

Figure 1: Council Production Function



IRISH FISCAL ADVISORY COUNCIL

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2013

CONTENTS:

COUNCIL MEMBERS AND OTHER INFORMATION

COUNCIL MEMBERS As at 31 December 2013

John McHale (Chair)

Sebastian Barnes

Alan Barrett*

Donal Donovan*

Róisín O'Sullivan

All current Council members were appointed upon the establishment of the Council in 2011. These appointments were reset following the establishment of the Council on a statutory basis on 31 December 2012.

*Audit Committee Members

AUDITORS

The Comptroller and Auditor General

Treasury Building

Dublin Castle

Dublin 2

BANKERS

Bank of Ireland

Lower Baggot Street

Dublin 2

STATEMENT OF COUNCIL RESPONSIBILITIES

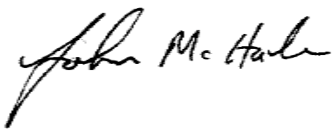
The Irish Fiscal Advisory Council (the Council) is required by the *Fiscal Responsibility Act 2012* to prepare financial statements in respect of its operation for each financial year.

In preparing those statements, the Council:

- selects suitable accounting policies and then applies them consistently;
- makes judgements and estimates that are reasonable and prudent;
- prepares the financial statements on a going concern basis unless it is inappropriate for us to do so;
- discloses and explains any material departure from applicable accounting standards.

The Council is responsible for keeping in such form as may be approved by the Minister for Finance all proper and usual accounts of moneys received or expended by it and for maintaining accounting records which disclose with reasonable accuracy at any time the financial position of the Council.

The Council is also responsible for safeguarding assets under its control and hence for taking reasonable steps in order to prevent and detect fraud and other irregularities.



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Professor John McHale

Chairman

Date: 25 July 2014

STATEMENT ON INTERNAL FINANCIAL CONTROL

RESPONSIBILITY FOR THE SYSTEM OF INTERNAL FINANCIAL CONTROL

I acknowledge, on behalf of the Council, the Council's responsibility for ensuring that an effective system of internal financial control is maintained and operated. The system can only provide reasonable and not absolute assurance that assets are safeguarded, transactions authorised and properly recorded, and that material errors or irregularities are either prevented or would be detected in a timely manner.

KEY CONTROL PROCEDURES

When the Council was established on an administrative basis in July 2011, the Department of Finance set up on behalf of the Council an arrangement whereby the accounting functions of the Council were undertaken by the Economic and Social Research Institute (ESRI). Since then, and in particular over the course of its first year of operation as a statutory body, the Council has taken steps to ensure that an appropriate control environment exists in the context of the ongoing arrangement with the ESRI.

Among the steps that were taken were the following:

- The establishment of procedures for authorising payments and procedures for procurement;
- The adoption of a travel policy which essentially matches public sector guidelines;
- The establishment of an Audit and Risk Committee;
- The adoption of a Code of Business Conduct;
- The generation of a risk register.

The system of internal financial control is based on a framework of regular management information, administrative procedures including segregation of duties and a system of delegation and accountability. In particular, it includes the following:

- A comprehensive budgeting system with an annual budget which is submitted to the Department of Finance;
- Regular reviews of periodic and annual financial reports which indicate financial performance against forecasts.

Recognising the small scale of the Council, the internal audit function has been outsourced to a firm of accountants. This firm recently undertook a review of internal control. The report noted that good progress had been made in the development of the Council's systems and practices and it noted a number of areas where further development is required. The report will be used in the on-going development of control policies within the Council. Further review work is planned for 2014.

ANNUAL REVIEW OF CONTROLS

I confirm that for the year ended 31 December 2013 the Council conducted a review of the effectiveness of the system of internal financial control.

Professor John McHale

Chairman

Date: 25 July 2014

Comptroller and Auditor General

Report for presentation to the Houses of the Oireachtas

Irish Fiscal Advisory Council

I have audited the financial statements of the Irish Fiscal Advisory Council for the year ended 31 December 2013 under the Fiscal Responsibility Act 2012. The financial statements, which have been prepared under the accounting policies set out therein, comprise the statement of accounting policies, the income and expenditure account, the balance sheet and the related notes. The financial statements have been prepared in the form prescribed under section 10 of the Act, and in accordance with generally accepted accounting practice in Ireland.

Responsibilities of the Irish Fiscal Advisory Council (the Council)

The Council is responsible for the preparation of the financial statements, for ensuring that they give a true and fair view of the transactions of the Council and of its state of affairs and for ensuring the regularity of transactions.

Responsibilities of the Comptroller and Auditor General

My responsibility is to audit the financial statements and report on them in accordance with applicable law.

My audit is conducted by reference to the special considerations which attach to State bodies in relation to their management and operation.

My audit is carried out in accordance with the International Standards on Auditing (UK and Ireland) and in compliance with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements, sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of

- whether the accounting policies are appropriate to the Council's circumstances, and have been consistently applied and adequately disclosed
- the reasonableness of significant accounting estimates made in the preparation of the financial statements, and
- the overall presentation of the financial statements.

I also seek to obtain evidence about the regularity of financial transactions in the course of audit.

Opinion on the financial statements

In my opinion, the financial statements, which have been properly prepared in accordance with generally accepted accounting practice in Ireland, give a true and fair view of the state of the Council's affairs at 31 December 2013 and of its income and expenditure for 2013.

In my opinion, proper books of account have been kept by the Council. The financial statements are in agreement with the books of account.

Matters on which I report by exception

I report by exception if

- I have not received all the information and explanations I required for my audit, or
- my audit noted any material instance where public money has not been applied for the purposes intended or where the transactions did not conform to the authorities governing them, or
- the information given in the Council's annual report is not consistent with the related financial statements, or
- the statement on internal financial control does not reflect the Council's compliance with the Code of Practice for the Governance of State Bodies, or
- I find there are other material matters relating to the manner in which public business has been conducted.

I have nothing to report in regard to those matters upon which reporting is by exception.

Seamus McCarthy

Seamus McCarthy
Comptroller and Auditor General

29 **July 2014**

STATEMENT OF ACCOUNTING POLICIES

The principal accounting policies adopted by the Council in determining the amounts included in the balance sheet and in reporting its transactions for the year are as follows:

1. Basis of Accounting

   The Irish Fiscal Advisory Council was established with effect from 31 December 2012 under Section 7 of the Fiscal Responsibility Act 2012. Prior to that date it operated on a non-statutory basis.

   These financial statements are prepared on an accruals basis under the historical cost convention and in accordance with generally accepted accounting practice. The unit currency is the euro.

   As this is the first period of account of the Council no prior year figures are presented. The outturn for 2012 is included at note 17 to the 2012 accounts of the Economic and Social Research Institute (ESRI).

2. Expenditure

   The expenditure recognised in the Income and Expenditure Account represents the amount incurred by the Council in the year in the performance of its functions.

3. Income

   The Income reported in the Income and Expenditure Account reflects the amounts receivable from the Central Fund in respect of the expenditure in the year in accordance with section 9 of the schedule to the Fiscal Responsibility Act 2012.

4. Fixed Assets and Depreciation

   Tangible fixed assets are shown at cost less accumulated depreciation. Depreciation is charged at rates designed to write off the assets over their useful lives. The only assets held by the Council at year end were computer equipment which are depreciated at an annual rate of 33%. A full years depreciation is charged in the year of acquisition.

5. Capital Account

   The Capital Account represents the unamortised value of state funding used to purchase fixed assets.

INCOME AND EXPENDITURE ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 2013

	Notes	*2013* €
INCOME		
Amount Receivable from Central Fund	1	478,608
Transfer (to)/from Capital Account	13	2,333
		480,941
EXPENDITURE		
Salaries	2	237,649
Council Members Fees and Expenses	3	68,085
Payments to Public Bodies	4	31,720
Administration	5	143,487
		480,941
Surplus/Shortfall for the Year		-

STATEMENT OF GAINS AND LOSSES

There were no gains or losses in the year other than those recognised in the Income and Expenditure Account.

The statement of accounting policies and the attached notes numbered 1 to 15 form an integral part of these financial statements and should be read in conjunction therewith.

John McHale

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Professor John McHale

Chairman

Date: 25 July 2014

BALANCE SHEET AS AT 31 DECEMBER 2013

	Notes		*Year Ended 31 December 2013* *€*
FIXED ASSETS			
Fixed Assets	6		461
CURRENT ASSETS			
Cash at bank and on hand	7	281,301	
Debtors	8	1,560	282,861
Total Assets			283,322
CURRENT LIABILITIES			
Sundry creditors and accrued expenses	9	261,063	
Amount due to Central Fund	1	21,798	282,861
TOTAL ASSETS less CURRENT LIABILITIES			461 ===
Represented by			
Capital Account	13		461 ===

The statement of accounting policies and the attached notes numbered 1 to 15 form an integral part of these financial statements and should be read in conjunction therewith.

John Mc Hale

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Professor John McHale

Chairman

Date: 25 July 2014

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2013

1. Central Fund Income

The Irish Fiscal Advisory Council is funded from the Central Fund. Under section 9 of the schedule to the Fiscal Responsibility Act 2012 the amount chargeable to the Central Fund is the amount expended by the Council in carrying out its functions.

The Central Fund operates on a receipts and payments basis whereas these financial statements have been prepared on an accruals basis. The table below sets out the reconciling items.

	2013
	€
Opening amount due to/(from) Central Fund[i]	468
Received from Central Fund	499,938
Amount due (to)/from Central Fund at year end	(21,798)
Central Fund Receivable for the year	478,608

[i] Due to an overstatement of accrued expenses of €3,736 at 31 December 2012 the (adjusted) opening amount due to the Central Fund of €468 does not agree to the closing position for 2012 as set out in Note 17 to the 2012 accounts of the ESRI.

2. Staff Salaries

Salary costs represent the cost of staff seconded from other organisations.

The number of persons seconded (full-time equivalents) in the financial year was 3 (2012:3).

3. Council Members Fees and Expenses

Council fees payable are sanctioned by the Minister for Finance and set by the Department of Public Expenditure and Reform - €20,520 for the Chair of the Council and €11,970 for Council members. Where members, including the Chair, are employed by a body within the Irish public sector, no fee is payable to the member concerned (see note 4). Fees incurred in 2013 totalled €39,770 inclusive of Employer PRSI of €3,860.

Expenses incurred by Council Members amounted to €28,315 in the year, mainly reflecting travel and subsistence costs incurred by international and non-Dublin based members attending Council meetings in Dublin.

Council Members Fees and Travel Expenses incurred in 2013			
Council Member	Fees €	Travel and Subsistence Expenses €	Total €
John McHale (Chairman)	See Note 4	4,265	4,265
Alan Barrett	See Note 4	202	202
Sebastian Barnes[ii]	11,970	5,956	17,926
Donal Donovan	11,970	7,447	19,417
Roisin O'Sullivan	11,970	10,445	22,415
Total	35,910	28,315	64,225

[ii] *Fees payable to Mr Barnes are directed to his full-time employers, the OECD, as compensation for time spent on Council business.*

4. Payments to Public Bodies

Due to the time commitment necessary to fulfil the functions of the Council, a time buy-out is in place to compensate the full-time public sector employers of the Chair and one Council Member for costs incurred due to their absence on IFAC business. In 2013, €19,750 was paid to the National University of Ireland, Galway and €11,970 to the ESRI.

5. Administration Expenses

	2013
	€
ESRI Administration fee[iii]	104,083
Travel Costs of Staff	456
Consultancy	7,095
Professional Fees	861
Computer Software	13,172
Staff Training	590
Meeting Costs	1,800
Report Production	3,622
Audit Fee	5,100
Other Costs	4,375
Depreciation	2,333
Total	143,487

[iii] *The ESRI Administration fee for 2013 includes a charge for accommodation and building services on a pro rata basis and support services relating primarily to accounts, IT, and other corporate services.*

6. TANGIBLE ASSETS[iv]

	Computer Equipment
	2013
	€
Cost:	
Assets transferred in at beginning of year	6,999
Additions	-
Disposals	-
At end of year	6,999
Accumulated Depreciation:	
On transferred Assets	4,205
Provided in year	2,333
Disposals	-
At end of year	6,538
Net book value at end of year	461
Net book value at beginning of year	2,794

[iv] *The opening figures represent the cost and accumulated depreciation of IT equipment incurred prior to IFAC being established as a statutory body on 31 December 2012.*

7. BANK AND CASH

	2013
	€
Current Accounts	281,301

8. DEBTORS

	2013
	€
Debtors	1,560

9. Creditors and Accrued Expenses

	2013 €
Payroll Taxes	6,703
Value Added Tax	732
Accrued Expenses	52,780
ESRI[v]	200,848
Total Creditors	261,063

[v] *This figure represents the balance due to the ESRI at year end regarding payments made on behalf of the Council in 2013.*

10. Taxation

The Council is exempted from liability to corporation tax under Section 227 Schedule 4 of the Taxes Consolidation Act 1997.

11. Commitments – Capital and Others

The Council had no capital or other commitments at the balance sheet date.

12. Contingent Liabilities

The Council Members were not aware of any material contingent liabilities at the balance sheet date.

13. Capital Account

The Capital Account represents the amount of funding used to purchase fixed assets reduced by the amount amortised in line with depreciation on the related assets.

	2013 €
Unamortised Funding at 1 January 2013	2,794
Amortisation in year	(2,333)
Balance as at 31 December 2013	461

14. Council Members' Interests

The Council adopted procedures in accordance with the guidelines issued by the Department of Finance in relation to the disclosure of interests by Council Members and these procedures have been adhered to in the year. As Alan Barrett is a member of the Council and also a member of the management committee of the ESRI, he absented himself from Council decision-making with respect to the services arrangement with the ESRI. There were no other transactions in the year in relation to the Council's activities in which the Council Members had an interest.

15. APPROVAL OF FINANCIAL STATEMENTS

The Financial Statements were approved by the Council on 25 July 2014.