On the Legitimacy of Fiscal Councils in the European Union: Trustees or Orchestrators of Fiscal Discipline?

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Abstract

This article distinguishes theoretically two conceptual models of a fiscal council – the trustee and the orchestrator model. The article reviews the arguments that prominent advocates of fiscal councils have put forth and finds that those who argue that the deficit bias is caused by the common pool problem prefer the trustee model, while others identifying asymmetric information as the root cause of the deficit bias prefer the orchestrator model. While the latter model relies on throughput legitimacy, the former relies on output legitimacy. The article concludes with a discussion about the contribution of fiscal councils towards strengthening EMU and weakening populism.

Keywords

Technocracy; Trusteeship; Orchestration; Fiscal councils; Legitimacy; Democratic accountability

The Eurozone crisis has reinvigorated a debate about the lack of compliance with the fiscal rules framework devised by the Stability and Growth Pact (SGP). Member states eager to reassure financial markets about their credible commitment to repay their debts through fiscal discipline were willing to seize any commitment device promising relief from short-term fiscal stress. The delegation of specific tasks related to fiscal policy to technocrats was a means to regain fiscal credibility during hard times. These expert bodies - so-called fiscal councils - monitor the fiscal rules and sound the ‘fire alarm’ if the government is in danger of swerving from the path of fiscal rectitude. Their creation dates back to the early economic advisory councils that were first established in Austria (1927) and the Netherlands (1945) (Debrun et al. 2013: 13; European Fiscal Board 2017: 33). After an initial stagnation, their spread continued in the 1970s as a result of oil price shocks that posed a particular challenge for fiscal policy in many countries. International organisations like the IMF, the ECB, the European Commission and the Organisation for Economic Co-operation and Development (OECD) have been prominent advocates of fiscal councils (Fromage 2017: 109; Tesche 2018).

In the literature competing definitions of fiscal councils exist emphasising different design features. The IMF defines a fiscal council as ‘a permanent agency with a statutory or executive mandate to assess publicly and independently from partisan influence government’s fiscal policies, plans and performance’ (Debrun et al. 2013: 8; for alternative definitions, see Debrun, Hauner, and Kumar 2009: 45-6; Wyplosz 2005). According to EU Directive 2011/85 (Art.6(1)(b)) fiscal councils are ‘independent bodies or bodies endowed with functional autonomy vis-à-vis the fiscal authorities’ that carry out reliable and independent analysis in line with the fiscal rule framework (Fromage 2017: 111; Jankovics and Sherwood 2017: 9). Further details are laid down in Art.2(1)(a) of Regulation EU No. 473/2013, which include: (i) ‘a statutory regime grounded in national laws, regulations or binding administrative provisions’, (ii) ‘not taking instructions from budgetary authorities of the member states’, (iii) ‘the capacity to communicate publicly in a timely manner’, (iv) ‘nominating members based on experience and competence’, and (v) ‘adequate resources and appropriate access to information’ (Fromage 2017: 112). Article 5 stipulates further that monitoring the fiscal rules shall be
the main task of the national fiscal councils. This includes assessing whether significant deviations from national fiscal plans are justifiable given the circumstances or whether the so-called correction mechanism needs to be activated to return to the desired fiscal path (Fromage 2017: 113). In sum, European legislation left a lot of wiggle room for the member states to make their national fiscal councils compatible with their domestic economic and political system and still comply with the rules (European Commission 2017b), which in turn paved the way towards the emergence of heterogeneous fiscal council models.

Two opposing views have emerged regarding the democratic legitimacy of fiscal councils. The first sees the rise of fiscal councils as compatible with and even democracy enhancing (Fasone and Griglio 2013; European Commission 2014; Fasone and Fromage 2017). The other argues that it undergirds ‘increasing technocratic tendencies, where experts no longer inform decision making but become the decision-makers’ (Connor 2017: 6) depriving democratically elected representatives of their policy tools. This article argues that these two views are aimed at two conceptually distinct models of a fiscal council. The latter view refers to the trustee model of a fiscal council which foresees that the government (trustor) entrusts a politically independent fiscal council (trustee) with direct fiscal policy instruments (such as setting a debt or expenditure ceiling) (Majone 2001; Abbott et al. 2018; Basso and Costain 2018). Further bolstering the authority of national fiscal councils could entail a ‘comply-or-explain rule’ that would put the onus on the government to provide reasons why it diverted from the advice issued by the fiscal council (European Fiscal Board 2017: 37). This principle could allow fiscal councils ‘to have the right of legislative initiative on issues related to their specific mandate’ (European Fiscal Board 2017: 39). Ultimately, it could be extended towards having the right to propose budgetary amendments to the Parliament. According to such a model an independent fiscal council would make distributive choices, however, not without the interference of elected representatives. Advocates of the trustee model point to the output legitimacy of such an independent fiscal council measured in terms of the boost in fiscal discipline. They emphasise that more independent fiscal councils possess a higher fiscal scrutiny capacity (von Trapp and Nicol 2018). These claims need to be taken with a grain of salt given that the evidence on the effectiveness of fiscal councils on fiscal outcomes is inconclusive (see Debrun et al. 2013: 51-4; Debrun and Kumar 2007; Lledó 2018).

The second model prescribes an orchestrating role to the fiscal council (Tesche 2018: 6-7). Governments establish fiscal councils as orchestrators that rely on intermediaries (i.e. parliaments, media or rating agencies) to influence fiscal policy indirectly. Fiscal councils lack any direct policy instruments that could adjust the fiscal path, so they try to force the hand of a fiscally profligate government through their orchestration capabilities, i.e. the dissemination of non-partisan analyses of fiscal policy choices. This article argues that while the trustee model can rely on output legitimacy, a well-designed orchestration model can improve the ‘throughput legitimacy’ of fiscal policy making by ‘governing with the people’ (Schmidt 2013).

The article is structured as follows. First, the article provides an overview of the origins of the deficit bias, i.e. a government’s tendency to run persistently high budget deficits. It then goes on to make a normative point that the identified root cause of the deficit bias should ideally determine which conceptual model of a fiscal council one prefers. If the common pool problem causes the deficit bias, one should prefer the trustee model. But if asymmetric information has been identified as the cause of the deficit bias, then the orchestration model seems more appropriate to eliminate the deficit bias. In many cases, the contribution of fiscal councils goes beyond deficit and debt reduction. It encompasses the production of macroeconomic forecasts and can even entail an advisory role in national spending reviews. In the subsequent section, the design features of the trustee and the orchestrator model are described in further detail. The main section assesses the legitimacy of fiscal councils using the familiar concepts of input, output and throughput legitimacy (Scharpf 1999;
Schmidt 2013). In general, fiscal councils have the capacity to generate ‘technocratic input legitimacy’ by improving the quality of fiscal policy deliberations through injecting ‘unbiased’ information into the democratic process. Furthermore, a fiscal council’s toolkit is scrutinised from an interdisciplinary perspective. The article concludes with a discussion about the role of fiscal councils in fixing EMU’s design flaws and weakening populism.

THE ORIGINS OF THE DEFICIT BIAS

The literature on the deficit bias has identified a host of reasons for the persistence of budget deficits. The specific cause of the deficit bias should inform the design features of the fiscal council so that the root cause can be effectively eliminated (von Hagen 2013). However, correctly identifying the underlying cause of the deficit bias is not straightforward. After all, fiscal policy is the most important tool to build winning coalitions in electoral competitions. Politicians have no incentive to limit their own fiscal room for maneuver (Alesina and Tabellini 2007). The advocates of the trustee model argue that the origin of the deficit bias lies in the common pool problem (i.e. concentrated benefits but dispersed societal costs of spending choices) (von Hagen 2018), whereas the proponents of the orchestration model suggest that the deficit bias is nourished by asymmetric information and fiscal opaqueness (Beetsma and Debrun 2017). These diverging opinions on the origins of the deficit bias have important downstream consequences for the preferred fiscal council model. If you assume that the common pool problem causes the deficit bias, then a politically independent fiscal council should have direct control over fiscal policy instruments that would enable it to undertake across the board spending cuts (von Hagen and Harden 1995). In essence, a trustee fiscal council would have to possess the capacity to decisively intervene in the government’s budget making process. If on the other hand the deficit bias is caused because voters, parliamentarians and other actors such as credit rating agencies hold asymmetric information vis-à-vis the government, then it would be sensible to instill an orchestrating fiscal council with a mandate that disseminates impartial information about the ‘true’ fiscal policy stance of the government. Governments tend to be overly optimistic with regards to their macroeconomic forecasts which has knock-on effects on their capacity to conduct prudent fiscal policy (Jonung and Larch 2006). Relying on third party intermediaries allows the orchestrator (the fiscal council) to enlist certain capabilities that it does not possess itself (Abbott et al. 2015b). Thus, it can indirectly govern fiscal policy choices of the government by flattening the asymmetrical information between the government and other actors.

The Common Pool Problem

Governments often target individual groups of society through increased spending (financed by all taxpayers) to reward the loyalty of their constituency (Weingast, Shepsle, and Johnsen 1981; Calmfors 2010; Calmfors and Wren-Lewis 2011; von Hagen 2013). If the state fails to internalise this externality, for example, through coordinated spending decisions in a structured budget process, it will lead to concentrated benefits with dispersed costs resulting in excessive debts, deficits and spending (von Hagen 2013). A dynamic version of the problem is the ‘war of attrition’ over fiscal consolidation. In the presence of an unsustainable budget deficit various groups in society can holdout in the hope that the burden of adjustment will be shifted to another group. This ‘waiting game’ will delay the inevitable consolidation and simultaneously raise its general costs. Eventually, fiscal consolidation will be more painful due to the high level of accumulated debts (von Hagen 2013). Again, the negative externality could be internalised by a coordinated approach decided upon by a trustee fiscal council that would evenly split the costs of fiscal consolidation between the groups. Nevertheless, it is doubtful whether these trade-offs should be solved through delegation to independent technocrats. Rather, democratic and open deliberation among the different societal groups affected by a certain fiscal policy should guide the decision-making process. Politicians with
short time horizons can shift the burden of adjustment into the future. In older societies the electoral pay-off for ‘kicking the can down the road’ is particularly high but with detrimental consequences for inter-generational justice because future generations will face exploitation through higher taxes (Calmfors and Wren-Lewis 2011). Streeck (2014) has pointed out that the politics of the consolidation state entails pitting the younger versus the older generation. This inter-generational cleavage inevitably creates difficult trade-offs. Delegation to fiscal councils is an attempt to paper over these by suggesting that they could be resolved in a purely technocratic manner. This is indicative of a broader trend towards ‘governing by the rules and ruling by the numbers’ (Schmidt 2015).

Asymmetric Information

Well-functioning democracies require all parties to be fully informed. However, this condition is often unfulfilled because informational asymmetries exist between the government on the one hand and the voters and opposition parties on the other. Thus, the electorate may not be able to observe the ‘true’ fiscal position of the government. In the absence of a sufficient understanding of the intertemporal budget constraint - that postulates that future primary surpluses need to be equal or greater than the outstanding net government debt - voters might be prone to succumb to over-optimism regarding the ‘true’ state of public finances ('fiscal illusion') (Calmfors 2010, 2015). A government claiming that a fiscal policy measure will be budgetary neutral, leaves the average voter struggling to verify this information (Calmfors and Wren-Lewis 2011). If governments exploit this informational asymmetry for electoral gain, the well-known political business cycle will ensue creating persistently high budget deficits. Thus, disseminating non-partisan assessments of fiscal policy can foster a shared understanding of the underlying fiscal policy trade-offs and even out informational asymmetries (Bos and Teulings 2013).

TWO CONCEPTUAL MODELS OF A FISCAL COUNCIL

The trustee model of an independent fiscal council

The success of the independent central bank model has inspired scholars to advocate its application to other policy areas such as fiscal policy (Blinder 1997; Wyplosz 2005; European Central Bank 2010). Politicians with short time horizons face a credible commitment problem which they can overcome by delegating authority over policy instruments in the realm of fiscal policy to independent trustees (Majone 2001). The trustee fiscal council could determine a long-term debt target and outline the short-term fiscal balance required to achieve it (von Hagen and Harden 1995; Eichengreen, Hausmann, and Von Hagen 1999; Calmfors 2003). Existing proposals diverge regarding the optimal mix between objectives and the necessary policy instruments (see Debrun, Hauner, and Kumar 2009). Advocates of the trustee fiscal council argue that it could mimic the success of inflation-targeting central banks (Wyplosz 2005; Blinder 1997). According to Wyplosz (2005: 72), ‘combining short-run flexibility with long-run discipline, can be achieved in the area of fiscal policy in the same way as it has been achieved in the area of monetary policy’.

The output legitimacy of a trustee fiscal council

The trustee model raises a host of democratic legitimacy issues which renders its implementation fragile. Insulating fiscal policy from politics is contestable because it would mean giving up a degree of democratic control. Decision-making on taxing and spending, however, is a sovereign prerogative of elected representatives and should not be delegated (‘no taxation without representation’)
Thus, the redistributive implications of fiscal policy and the lack of clearly measurable objectives are an obstacle for entrusting it with independent experts (Alesina and Tabellini 2007, 2008). A trustee fiscal council could suffer from a democratic legitimacy deficit unless a strong societal consensus existed about its objectives. But society’s preferences on fiscal policy do not seem to be stable and public opinion regarding budget deficits is highly susceptible to media and elite framing (Barnes and Hicks 2018). While there is no trustee fiscal council conducting fiscal policy instead of the government (Wren-Lewis 2013), fiscal councils with trustee-like features do exist.

One way of measuring the impact on the conduct of fiscal policy making could be to measure the variation in the sovereign risk premium demanded by financial markets. Trustee-like fiscal councils that raise the credibility of a government’s fiscal policy by promoting fiscal transparency might see the spreads of government bonds declining. Alternatively, the output legitimacy of trustee fiscal councils could be measured by assessing whether the fiscal council has increased the compliance with the fiscal rules or whether the forecasting error of the government’s macroeconomic and budgetary forecasts has been reduced. Furthermore, fiscal council’s output legitimacy could be assessed by measuring the fiscal literacy of mass publics, i.e. the publics’ skills and knowledge enabling them to take an informed stance on fiscal policy matters. Regardless of which measure one ultimately uses, it would be already an improvement if fiscal councils could improve the parliamentary debate about fiscal policy by forcing parliamentarians to be transparent about the distributional impact of their policy proposals.


Hungary experienced a prolonged period of rising debts and deficits in the early 2000s due to a rampant common pool problem which culminated in a financial assistance programme jointly monitored by the EU and the IMF. In 2008, the Hungarian parliament passed the fiscal responsibility law which created a fiscal council (Kopits and Romhanyi 2013). Even though the parliament ultimately decided against bestowing any legally binding instruments of enforcement upon the fiscal council, the latter operated in many respects as a quasi-trustee with a high level of political and operational independence. Its wide mandate enabled it to intervene in parliamentary debates and steer fiscal expectations to reduce the sovereign risk premium. For example, the fiscal council prepared its own ‘macro-fiscal projections, conducted real-time evaluation of the effects of each fiscal proposal prior to parliamentary debate, and monitored fiscal rules’ (Kopits and Romhanyi 2013: 212). Three fiscal rules were of particular importance (Kopits and Romhanyi 2013: 223): (1) prevention of any legislation proposal to produce a net deficit in the current and subsequent year (pay-go rule); (2) cap on primary expenditure growth; (3) limit on the real stock of central government debt. During the 2010 budget bill debate the fiscal council scrutinised numerous MP proposals to assess whether they were in line with the pay-go rule (Kopits and Romhanyi 2013: 223). However, shortly after the 2010 general election MPs of the ruling Fidesz party proposed significant budget cuts and later disbanded the fiscal council completely to narrow its mandate. Stripped off its responsibilities, the fiscal council is now merely ‘a part-time deliberative body without remuneration’ (Kopits and Romhanyi 2013: 227). In sum, the Hungarian fiscal council fell prey to its own success as a highly independent expert body with trustee-like features. A less powerful fiscal council might have survived the populist onslaught with some minor budget cuts without being coopted. But a fiscal council with such a high capacity for fiscal scrutiny compelled the Hungarian government to dismantle its core.
**Fiscal councils as orchestrators of fiscal discipline**

The orchestrator-intermediary-target (O-I-T) model (Abbott et al. 2015a, 2015b) provides a useful heuristic device to understand the functioning of a fiscal council. Orchestration is defined as ‘the mobilisation of an intermediary by an orchestrator on a voluntary basis in pursuit of a joint governance goal’ (Abbott et al. 2015b: 722). First, orchestrating fiscal councils lack the authority to directly exert control over the targets they want to govern (Abbott et al. 2015b: 720). They neither possess decision-making authority nor do they have legally-binding enforcement powers (Kopits 2011; Hemming and Joyce 2013). A fiscal council might want to reduce the budget deficit to comply with the European fiscal rules but lacks control over the fiscal instruments to achieve this goal. Governments can easily dismiss the orchestrator’s fiscal recommendations unless it is politically costly to do so. To raise the reputational costs to governments a fiscal council should possess a degree of focality in budgetary politics and a strong ability to communicate with the public. Second, an orchestrator enlists a voluntary intermediary whose goals are aligned (Abbott et al. 2015b). Fiscal councils (orchestrators) can enlist voters, the media, credit rating agencies or parliamentarians (intermediaries) with a strong preference for fiscal discipline (target) by providing ideational support, such as independent budgetary forecasts, normative assessments and recommendations or costing of specific fiscal policy measures (soft inducements). If the electorate cannot check and balance the government on fiscal issues due to informational asymmetries, fiscal councils can send a credible signal to voters about the ‘true’ fiscal stance of a government (Beetsma and Debrun 2017). This signal will be the stronger, the higher the reputation of the fiscal council for non-partisanship. Third, by enhancing fiscal transparency better informed citizens will make better decisions when judging the government’s fiscal competence (Beetsma, Debrun, and Sloof 2017). Hence, the ideational support provided by the orchestrator is crucial in flattening out any existing informational imbalances. In sum, fiscal councils as ‘producers of reliable information’ can harness the benefits of expertise without having formal decision-making powers (Tucker 2018: 94-5).

**The throughput legitimacy of an orchestrating fiscal council**

An in-built incentive of orchestrating fiscal councils is to be as transparent, inclusive and open as possible. Even if a larger share of the public will be enabled to adequately judge the fiscal competence of the government, this does not necessarily lead to lower deficits. Hence, the traditional concept of output legitimacy might fail to capture the contribution of orchestrating fiscal councils. Given that fiscal councils have only indirect means of influencing fiscal policy it would be difficult to measure their impact on fiscal policy outcomes. Against this backdrop, a more process-oriented, ‘real-time’ measure of legitimacy is ‘throughput’ legitimacy or ‘governing with the people’ (Schmidt 2013). Located in-between input and output, ‘throughput’ legitimacy relates to the quality of the decision-making process (Torres 2013: 291-2) and, thus, is key to the work of orchestrators. ‘Throughput legitimacy demands institutional and constructive governance processes that work with efficacy, accountability, transparency, inclusiveness and openness’ with an emphasis on consultations with the people (Schmidt 2013: 7-8).

A major advantage of the orchestration model is that it is democracy-compatible. Fiscal councils can function as ‘accountability multipliers’ and enhance the role of national parliaments due to its improved fiscal scrutiny capacity (Fasone and Griglio 2013; European Commission 2014; Fasone and Fromage 2017). Importantly, a fiscal council can ‘nudge the intermediary toward governance goals that are compatible with its own goals’ (Abbott et al. 2015b: 722). However, the legitimacy of an orchestrating fiscal council will ultimately depend on the public’s support for its goals (i.e. the degree of local ownership). In many European countries orchestrating fiscal councils have become highly reputable bodies which makes it harder for parties to ignore their recommendations (Horvath 2018).
But it is often a balancing act for an orchestrating fiscal council to preserve its aura of nonpartisanship and to critically assesses the government’s fiscal policy at the same time.

**Empirical case: The Portuguese fiscal council - an orchestrator with throughput legitimacy**

The case of the Portuguese fiscal council shows that well-designed fiscal councils can reconcile accountability with democratic legitimacy when a broad political compromise provides the foundation for strong national ownership. The mandate of the Portuguese CFP explicitly mentions the enhancement of the quality of democracy as one of its core tasks. The Conselho das Finanças Públicas (CFP) was set up in May 2011 as part of the fifth amendment to the 2001 Budget Framework Law (Law 22/2011) and became operational at the beginning of 2012. Several beneficial circumstances have facilitated the CFP’s high effectiveness. First, already in 2010 (before the arrival of the troika) a cross-party consensus to set up a fiscal council between the Socialist government and the largest opposition party (the Social Democrats) emerged (von Trapp, Lienert, and Wehner 2016, 190). An independent working group was tasked with drawing up the CFP’s statues, which cumulated in the signing of law 54/2011. The resulting high level of local ownership has proven beneficial for the CFP’s democratic legitimacy. Second, the CFP has a broad mandate that covers eight different tasks. Among them are assessing macroeconomic and fiscal projections, public debt sustainability, compliance with the budget balance rules and the rules on expenditure by the central government, autonomous regions and local governments. In sum, the CFP is not merely in charge of conducting assessments of the compliance with the fiscal rules but, crucially, assesses the government’s overall fiscal strategy. Third, the CFP’s financial independence is guaranteed through state budget appropriations which can only be modified under ‘exceptional circumstances’. The CFP’s budget of €2.53 million (in 2014) accounts for the breadth of its mandate and allowed it to hire a sufficient number of qualified research staff (von Trapp, Lienert, and Wehner 2016: 189-203). Fourth, the CFP is supposed to have access to all information that it needs to perform its tasks. Fifth, the CFP’s strong commitment to transparency and democratic accountability requires it to publish all its reports on the its website. They are sent to the President of the Republic, the government, the parliament, the Court of Auditors and the Central Bank. The use of social media and media outreach ensure that the CFP sends credible signals to the public at large as foreseen in the orchestration model. In doing so, the CFP multiplies its impact and lives up to its full orchestration potential.

**FISCAL COUNCILS AND THEIR TOOLKIT**

**Macroeconomic indicators and forecasting**

Macroeconomic forecasting is based on economic formulae that make distributional choices by default. This is because macroeconomic indicators such as public deficits are calculated on the basis of deeply political formulae engrained with significant distributive implications (Mügge 2016). Powerful neoliberal ideas linger in the background and govern these indicators. If one follows this line of argument, it would mean that even a fiscal council with a narrow mandate to only produce macroeconomic or budgetary forecasts inevitably makes deeply distributional choices. Accordingly, these forecasts can never be completely ‘unbiased’ because a specific measurement will always lead to an advantage for some societal groups over others (Mügge 2016). However, the mere production of ‘unbiased’ macroeconomic projections can improve the conduct of fiscal policy significantly (Jonung and Larch 2006).

Beckert (2016: 231) argues that ‘forecasting should be considered as an instrument for the construction of fictional expectations’. Orphanides and van Norden (2002) have shown that using
measures such as the output gap will lead to persistent measurement errors due to the unreliability of real-time data. This raises doubts about the capacity of fiscal councils to produce accurate forecasts. Beckert, however, cautions that it is not the actual accuracy that is important but the ‘credible claim for correctness’ (Beckert 2016: 231). Given that future contingencies cannot be foreseen, forecasts turn into focal points around which actors’ expectations converge (Beckert 2016: 234). Macroeconomic and budgetary forecasts have a special responsibility because they influence the economic behavior of domestic households. Overoptimistic governmental forecasts that falsely predict a balanced budget might incentivise households to reduce savings when they should have created saving buffers for future consumption smoothing. These ‘fiscal fictions’ will ultimately lead to coordination failure. Fiscal councils have, thus, an important role to play in ‘de-politicizing’ forecasting and in creating a reliable coordination device for households’ economic activities.

**Fiscal rules**

In the EMU, the fiscal rules devised by the SGP have often been criticised as arbitrary and overly intrusive to the point that some have advocated a complete renationalisation of fiscal policy (Eichengreen and Wyplosz 2016). The rule-based approach to fiscal policy has aimed at constraining discretionary fiscal policy. This might be successful at creating long run debt sustainability but comes at the expense of short-term output stabilisation. It bears the risk that fiscal policy becomes procyclical as tax revenues decline and automatic stabilisers kick in during economic downturns (Wyplosz 2005). Because fiscal rules are either too lax or too tight they should be substituted with an independent fiscal council that does not exhibit a deficit bias and can use its discretion to engage in deficit targeting (Wyplosz 2005, 2008). The practical reality is that most fiscal councils function as complements to the existing fiscal rules (Debrun et al. 2013; Calmfors 2015). This is due to the rule complexity trade-off. The more complex a fiscal rule is, the more difficult it is to monitor and the more likely that its implementation will be outsourced to experts (Calmfors 2015). Vice versa, the simpler the fiscal rule, the easier it is to monitor without the need for an independent fiscal council. However, a simple fiscal rule like a cap on the annual budget deficit can provide for inadequate fiscal policy for a given state of the business cycle. In this regard, it is important to understand the role of fiscal councils in fiscal regimes that exhibit permanent budget surpluses like Sweden. The Swedish fiscal council, for example, criticised the government that clinging to an expenditure ceiling irrespective of the general economic developments can be costly (Haffert and Mehrtens 2015: 138). The example shows that fiscal councils can also turn into champions of Keynesian stimulus spending if governments leave their fiscal space unexploited.

**The ‘scientisation’ of fiscal policy**

Leeper (2010: 2) has observed that ‘monetary policy tends to employ systematic analytics, while fiscal policy relies on unsystematic speculation’ or what he terms ‘fiscal alchemy’. He advocates for a ‘fiscal science’ that would anchor the fiscal expectations of households in order to improve economic decision-making. In the current regime of ‘fiscal alchemy’ uncertainty about entitlement reform might incentivise individuals to hold savings above the optimal level. Unanchored fiscal expectations are likely to create negative spill-over effects on the ability of central banks to curb inflation. Leeper (2010: 4) cautions further that ‘in the coming era of fiscal stress with no credible government plans to confront the growing fiscal strains, unanchored fiscal expectations become a certainty’. Thus, if fiscal policy would be subject to the same scrutiny as monetary policy by independent fiscal councils, it would offer more reliable guidance for private households. For this purpose, the ‘less political’ aspects of fiscal policy that are ‘more amendable to science’ should be separated and a societal consensus should be formed on them. Among these aspects Leeper (2010: 6) lists the debt target, the adjustment path of tax rates and spending to ensure debt sustainability and specific
circumstances under which a change in the debt target is permissible. Larch and Braendle (2018) argue that the Musgravian stabilisation function of fiscal policy should be entrusted with independent technocrats. An independent fiscal council would then set the ceiling for the nominal budget deficit for a certain period.

The fiscal rules enshrined in the SGP have set tight limits on the debt-to-GDP ratio and the permissible budget deficits but have become increasingly complex and flexible over time. Yet, they have contributed to the ‘scientisation’ of fiscal policy that has pervaded monetary policy (see Marcussen 2009). As political deliberations about the redistributive implications of fiscal policy are gradually ‘crowded out’ by technocratic discourses, fiscal policy is being ‘apoliticised’. Technocrats that are nominated to serve on fiscal councils on the basis of their expertise and knowledge gain in legitimacy and expert authority. At the same time, this increases the likelihood that more and more tasks related to fiscal policy will be subject to delegation as fiscal policy appears to be ridden of ideological debates. This is a governance process that Schmidt (2015) has described as ‘governing by the rules and ruling by the numbers’. Since a complete contract including all unanticipated contingencies can never be written, the question remains what the reaction function of a fiscal council would be during an emergency situation when fiscal stress renders its forecasts obsolete.

What can a fiscal council do if the central bank engages in fiscal policy by stealth? Does the national statistics office collect the type of data that allows to measure a government’s hidden off-balance sheet debts? These questions only scratch the surface of the problems that fiscal councils will have to tackle going forward.

DISCUSSION: FISCAL COUNCILS AND THE FUTURE OF EMU

Strengthening market discipline and fiscal literacy, weakening populists

Fiscal councils can contribute to a stable EMU governance architecture in various ways. First, fiscal councils can strengthen market discipline. Financial markets have repeatedly been criticised for not being able to adequately fulfill their watchdog function because they tend to overreact during bad times. Thus, market discipline only works ex post and fails to exert sufficient ex ante pressures for fiscal discipline during good times. Fiscal opaqueness of governments contributes to the failure of market discipline because credit rating agencies do not possess the adequate information to assess a government’s fiscal stance correctly which results in rapid downgrading cascades during a crisis. A fiscal council that manages to rebalance the informational asymmetries in favor of third parties will decisively contribute to more accurate credit ratings. Moreover, if the fiscal council enjoys a high reputation and credibility, it will contribute to faster upgrades of ratings after an asymmetric shock has hit the economy. In 2014, Moody’s referred extensively to the CFP’s assessments in its decision to upgrade Portugal’s government bond rating (Moody’s 2014). As credit rating agencies benefit from better information, financial markets will move closer to perfect discrimination between euro area sovereign bonds. During good times fiscal councils help to encourage a government to undertake counter-cyclical fiscal policy and remain committed to long-term debt sustainability. By avoiding stirring negative market sentiments and bringing sovereign bond ratings in line with economic fundamentals positive spill-over effects for the stability of the euro area as a whole are likely to ensue.

Second, fiscal councils can help to contain populism. The populist governments across the EU have rattled the financial markets and led to a spike in sovereign bond rates. They show disdain of fiscal rules and a tendency to politicise them for electoral gain. Their policy prescriptions are characterised by an excessive short-term bias resulting in a neglect for future-oriented investments. The longer time horizon of fiscal councils could provide an effective remedy against populist myopia. Jacobs
(2016: 442) has argued that to cope with the political problem of the long term, institutions need to (i) ‘enhance the relative quality of information about the long-run consequences’, (ii) ‘stabilise political commitments over time’, and (iii) ‘minimise distributive opportunism by organized groups’. Fiscal councils make a strong contribution to each of these dimensions. In the Netherlands, for example, all parties submit their economic proposals to the Dutch fiscal council (CPB) for an independent assessment of their policy proposals to facilitate a better understanding of the fiscal consequences of different electoral platforms (Bos and Teulings 2013; European Fiscal Board 2017: 36). This allows voters to take an informed vote that is more aligned with voters’ own fiscal preferences. Interestingly, all parties voluntarily participate in this exercise even though the fiscal council has no legal means of enforcing their participation (Bos and Teulings 2013). The example of the CPB shows that fiscal councils can govern effectively even with a thin legal and political basis because it is reputationally costly for parties to withdraw from the process (especially shortly before a general election). Thus, the Dutch model facilitates the stabilisation of the political commitments over time by providing an effective check on excessive spending promises of populist parties. Moreover, the costing of policy proposals contributes to minimising distributive opportunism by stating explicitly which societal groups will bear the brunt of the adjustment burden. In a nutshell, fiscal councils have an important role to play in preventing the rise of populism by continuously fact-checking the fiscal policy debate. Even in countries in which fiscal councils have been weakened through budget cuts (like in Hungary) their tasks have been partially taken over by private initiatives like the Fiscal Responsibility Institute Budapest (Kopits and Romhanyi 2013: 228). These bottom-up initiatives could also help to regain trust in the work of experts. Promoting fiscal transparency could broaden political participation and build trust in the reliability of information. This would increase the overall quality of democratic decision-making.

Third, a policy proposal by 14 French and German economists called for ‘more independent fiscal watchdogs at both national and European levels’ (Bénassy-Quéré et al. 2018: 5). The authors advocate to delegate the fiscal and macroeconomic watchdog role to the European Fiscal Board (EFB), which is currently an independent advisory body of the Commission. They sketch out a scenario in which fully independent national fiscal councils propose a rolling 5-year medium term debt reduction target (subject to approval by the euro area fiscal watchdog) and forecast nominal growth projections. In a second step, national fiscal councils would determine the nominal expenditure ceiling compatible with the debt reduction target. This proposal would mirror the European System of Central Banks and pave the way towards a European System of Fiscal Councils (ESFC) (Asatryan et al. 2017). Given that national fiscal councils have been careful to avoid deepened cooperation with the EFB in order not to tarnish their institutional independence (Asatryan et al. 2017), it is unlikely that an ESFC will emerge. In December 2017 the European Commission has proposed a directive that would enhance the enforcement capacity of national fiscal councils (European Commission 2017a). According to the proposed directive national fiscal councils should command more tools to ratchet up compliance with the fiscal rule framework. Yet, unless governments are willing to guarantee a minimum level of operational independence, fiscal councils would merely function as ineffective ‘smokescreens’ (Debrun and Kumar 2007). Strengthening the operational independence of fiscal councils would make rapid strides towards improving the general ‘fiscal literacy’ of the electorate. In other words, increased throughput legitimacy can generate various positive spill-over effects despite the fact that governments might still be able to simply ignore the fiscal council’s recommendation and get off scot-free.

CONCLUSION

This article has argued that the underlying assumptions about the causes of the deficit bias have led to two distinct conceptual models of fiscal councils. While proponents of the trustee model argue
that the common pool problem causes the deficit bias, others championing the orchestrator model point to asymmetric information as the cause of the deficit bias. Furthermore, while the trustee model relies on output legitimacy, the orchestrator relies on throughput legitimacy. The short-lived experience of the Hungarian trustee fiscal council points to the challenges that powerful fiscal councils face. In contrast, the Portuguese example shows that an orchestrating fiscal council can be even democracy enhancing. In addition, this article has argued that fiscal councils are likely to foster market discipline and fiscal literacy in the EU and could even contribute towards tackling the rising threats to democracy stemming from populism.

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