Expenditure Rules

Are expenditure rules desirable in Italy?

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Outline

- Italy: some figures
- The consolidation challenge
- Why expenditure rules?
- Difficulties in implementation
- Conclusions
Italy: debt/GDP trend
Italy: deficit, expenditures and revenues

revenues/GDP (left)  expenditures/GDP (left)  deficit/GDP (right)
The consolidation challenge

Deficit targets 2010-2012
The consolidation challenge

Deficit targets and expected revenues on GDP (baseline)

- revenues/GDP (left)
- expenditures/GDP (left)
- deficit/GDP (right)
The consolidation challenge

Expenditure/GDP reduction required to meet deficit targets, given revenues
The consolidation challenge

*Primary expenditure required to meet deficit targets*

- **Millions of Euro**
  - **Primary expenditures**
  - **Expenditures**

- **Yearly Expenditure Growth**
  - **1992**
  - **1993**
  - **1994**
  - **1995**
  - **1996**
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  - **2008**
  - **2009**
  - **2010**
  - **2011**
  - **2012**

- **Target Years**
  - **2010**
  - **2011**
  - **2012**
Why expenditure rules?

Since late 1990s, several European countries have introduced expenditure rules (ER)

*Constraint on the size of the public sector*

- do not hamper stabilizers on the revenue side, consistent with tax smoothing and cyclically adjusted targets;
- governments have a better control on spending than on revenues;
- limit the propensity to increase spending in upturns;
- easier to explain to the public and to monitor;
- bring more transparency and accountability at administrative level too.
Expenditure rules: common problems

ER present some problematic issues:

• Choice of the reference indicator: nominal or real terms?

• which spending items:
  • primary or total?
  • capital expenditures excluded?
  • cyclical expenditures excluded?
  • mandatory and entitlements excluded?

• Annual or medium term? Rolling or fixed?
Italy: the institutional design

- Recent change in organic budget law (December 2009), but final decision was on having just deficit rules;
- The issue was on the agenda: during parliamentary debate a few proposals on introducing ER within the medium term budgetary framework (MTBF);
- Current format of MTBF implies no disclosure of planned deficit; not available expected figures for revenues and expenditures; just qualitative specifications.

*Debate at the European level on asking to member countries to adopt ER*
Italy: implementation features

If and when the decision on expenditure rules will be taken….

• Subnational levels have constitutional autonomy; is it possible to introduce such a constraint on the general government expenditure without hampering their autonomy? Is it better to implement it only at the central level?

• ER involve good capacity of planning and forecasts of expenditure trends; expenditure limits should not be changed for “ordinary” mistakes. Are we ready?

• ER oblige to adapt the format of planning documents:
  • unchanged policies for baselines
  • disclosure of planned target by revenues and expenditures
Conclusions

• tool useful to complement deficit rules, mainly in fragmented political systems;

• in Italy it would help in the consolidation effort;

• sophisticated instrument that require soft institutional design (complex negotiations) and good technical capacity;

• easier to implement it first in terms of planned figures (no actual constraints); accompanied by top down procedures for budget preparation and approval;

• Big cultural change. Different constraints in negotiation (at the executive and parliamentary levels).
THANK YOU FOR YOUR ATTENTION