ITALIAN CHAMBER OF DEPUTIES

OECD PARLIAMENTARY BUDGET OFFICIALS

Third Annual Meeting

Stockholm

RECENT BUDGET REFORMS IN ITALY

Adjusting the budgetary decision-making system to the new European economic governance system

28-29 APRIL 2011

In view of the recent introduction at EU level of decision-making and operational modules to encourage, within the framework of the "European Semester", closer *ex ante* coordination among the EU Member States' economic and budgetary policies as well as closer fiscal and macroeconomic supervision, and in view of the revision of the contents and timing of the presentation of the updated Stability Programme and the National Reform Programme, the Italian Parliament has resolved to introduce new rules governing the substantive and procedural aspects of Italy's national accounting legislation.

The recently enacted law no. 39 of 7 April 2011[1] introduced amendments to Law no. 196 of 31 December 2009 (the Public Finance and Accounting Act) which are designed to guarantee overall consistency between general government financial planning and the European Union's procedures and criteria.

The economic and financial programming cycle and instruments have therefore been reviewed, and a number of provisions introduced to tighten fiscal discipline in compliance with the guidelines issued by EU institutions to reduce the deficit and the debt.

Furthermore, the most important innovations introduced in 2009 have been confirmed, such as the method for planning resources, policies and targets over a minimum three-year period, the breakdown of public finance targets across the different sub-sectors of general government and the formulation of forecasts - based on unchanged policies - of the main aggregates of the general government accounts.

The new budgetary cycle

The 2009 reform of the accounting rules had deferred to 15 September the deadline date for laying the draft Public Finance Decision before Parliament, in order to provide a more updated overview of public finance and economic forecasts than the one available on 30 June (the deadline previously set for submitting the former EFPD). The new amendments to the accounting law, in line with the new timetable laid down by the EU, bring forward the whole national programming process to the first part of the year, requiring the **Economic and Financial Document (DEF) to be submitted to both Houses of Parliament for** parliamentary consideration **by 10 April**.

The tabling by mid-April of the DEF – which is the government's main economic and financial planning instrument, replacing both the Report on the

[1] (Published in the Official Journal no. 84 of 12 April 2011).

Economy and Public Finance (REF) and the Public Finance Decision (DFP) – will enable Parliament to resolve on the planning objectives in good time to be able to forward the Stability Programme and the National Reform Programme to the European Union Council and the European Commission by the 30 April deadline. The latter document will thus be able to take account of the indications emerging from the Annual Growth Survey published at the beginning of each year by the European Commission.

In order to guarantee **local and regional government participation** in the economic and financial planning process, the DEF must also be submitted by the same 10 April deadline to the Standing Conference for Public Finance Coordination[2] for its opinion to be taken account of during the relevant parliamentary debates.

To guarantee the full and prompt **involvement of Parliament** in examining EU proposals, drafts, and other documents during the European Semester, the amendments made to the accounting law provide that as soon as the government receives these documents, it must forward them promptly to both Houses of Parliament for parliamentary consideration and **oversight**. Similarly, within 15 days of the date on which the economic and budgetary policy guidelines laid down by the European Council are forwarded to the government, the Minister for the Economy is required to report to the relevant Parliamentary Committees and provide them with an assessment of the data and the measures set out in the guidelines, together with their implications for Italy, also for the purposes of drawing up the Stability Programme and the National Reform Programme.

By **30 June** each year, the **DEF** must be supplemented by a specific **Annex** – which the Minister for the Economy is required to forward to the two Houses – setting out the results of **monitoring the impact on public finance balances** - both in terms of revenues and expenditure - of the measures contained in the **budgetary adjustments, including those adopted during the year**, indicating any deviations from the original forecasts, and the reasons for them.

In order to take account of any recommendations from the EU authorities, **a Note** updating the Economic and Finance Document is required to be submitted by **20 September** each year.

[2] The Standing Conference was established as a permanent body for coordinating public finances between different tiers of government by a Legislative Decree which is in the process of being published in the Official Journal, enacting provisions regarding the autonomy of the ordinary regions and the Provinces in respect of their tax revenues, and laying down standard costs and requirements in the healthcare sector.

The novelty here is that, unlike the situation in the past, the presentation of the Note is not merely an option when substantial deviations occur in public finances; it has now been made mandatory, and makes it possible to take account of more detailed information and data than what was available in April, and then to proceed, if necessary, to update the policy goals in the DEF.

In addition to updating the macro-economic and public finance forecasts for the current year and for the reference period, the Note is now required to set out the net state borrowing requirements and the State sector cash requirements, as well as the contents of the domestic Stability Pact and the Convergence Pact on Standard Costs and Requirements for the various tiers of government, together with appropriate measures to ensure the convergence path of service targets in view of the basic levels of benefits and fundamental functions guaranteed by the Italian Constitution.

Consistently with the provisions governing the DEF, if it proves necessary to adjust the public finance targets, by 10 September of each year the government is required to submit guidelines for the breakdown of targets to the Standing Conference for Public Finance Coordination, for its prior opinion to be submitted by 15 September. The guidelines are to be forwarded to both Houses by 10 September to be followed by Conference's opinion.

Furthermore, under Law No. 39 of 7 April 2011, in the event that the government deems it necessary to **review public finance targets** for the purpose of providing updated data or because of exceptional events, or else in the event of any substantial deviations in public finance trends making **corrective adjustments** necessary, the government is required to send a report to **Parliament**, setting out the reasons for the update or for the deviations, and indicating the corrective measures it intends to adopt.

As far as the other steps of the budgetary cycle are concerned, the reform introduced by law 39 of 2011 did not change the policy objective implementation phase, which must take place in the autumn, by laying before Parliament the **Stability Bill** and the **State Budget Bill** representing the three-year budget package, by no later than 15 October each year.

By the following January, the government is required to submit any **Bills accompanying the Budget package**, previously specified in the DEF or in its Update Note.

The following table compares the planning cycle and instruments in the original version of law 196/2009 with those provided by the recent reform.

<table>
<tr><th>LAW no. 196/2009</th><th>LAW no. 196/2009 as amended by law no.39/11</th></tr>
<tr><td>Report on the economy and public finance
(15 April)</td><td>Abolished</td></tr>
<tr><td>Public Finance Decision (DFP)
(15 September)</td><td rowspan="2">Economic and Financial Document (DEF)
(10 April)</td></tr>
<tr><td>Stability Programme Update
(According to the EU-agreed timetable)</td></tr>
<tr><td></td><td>DEF Annex
on monitoring the impact of budgetary adjustments, also in the course of the year
(by 30 June)</td></tr>
<tr><td>DFP update Note
(Only if the targets have changed or there are deviations in trends)</td><td>DEF update Note
(20 September)</td></tr>
<tr><td>Stability Bill
(15 October)</td><td>Stability Bill
(15 October)</td></tr>
<tr><td>State Budget Bill
(15 October)</td><td>State Budget Bill
(15 October)</td></tr>
<tr><td>Budget Review Bill
(30 June)</td><td>Budget Review Bill
(30 June)</td></tr>
<tr><td>Accompanying bills
(By February)</td><td>Accompanying bills
(By January)</td></tr>
</table>

Financial stability provisions

The amendments made to the accounting law have introduced new **prudential criteria in financial management**, designed to facilitate the oversight of performance and the pursuit of public finance targets.

Complying with the request of the European Union to reduce the deficit and debt using any unforeseen increased revenues under current legislation, article 3 of law no. 39/2011, amending the provisions of article 11 (6) of law no. 196 of 2009, permit **the use of public savings** to cover current charges under **the Stability Law** for the **sole purpose of financing reduced revenues** and only on condition that a positive balance of public savings is guaranteed.

The same rationale underlies the new paragraph (1-bis) added to article 17 of the Accounting Law which **prohibits the use of increased current revenues** to cover any additional unbudgeted financial charges arising in the course of the fiscal year because of variations in performance under current legislation, and expressly provides that any **"increased revenues"** resulting from an improvement in the economy **may only be used to improve public finance balances**.

One further change designed to **strengthen fiscal discipline** based on the budgetary and planning scheme inspired by **top-down** type procedures and rules was introduced in enabling legislation conferring delegated powers to the government to complete the state budget reform: article 40 of law no. 196/09 authorises the government to set **expenditure ceilings on aggregate budgeted resources**, including non-adjustable resources, notwithstanding the need to take account of their specific nature.

The structure of the Economic and Financial Document

Following the amendments made to budgetary legislation, the DEF is now the principal financial and economic planning instrument, comprising the outline of the Stability Programme and the outline of the National Reform Programme, which must be forwarded to the European Union Council and the European Commission by 30 April.

The contents of the Document are divided into three specific sections.

The **first section** sets out the outline of the **Stability Programme**, which must contain all the elements and information required by European Union regulations and in particular by the new Code of Conduct for implementing the Stability and Growth Pact, referring specifically to the objectives to be pursued to accelerate the reduction of public debt.

Confirming the principle introduced by law no.196/09 on three-year resource planning, it is necessary to indicate the breakdown of the measures required to achieve the public finance targets across the sub-sectors of general government - central government, local government and social security agencies – accompanied both by a rough indication of the **measures whereby it is expected to attain the targets**; this section should also contain long-term public finance forecasts and the measures planned to guarantee their sustainability, as well as the various **possible net borrowing and debt scenarios** in terms of alternative forecasts for GDP growth rates, the structure of interest rates and the primary balance.

The **second section** contains a set of data and information which the government was previously required to provide in the Economic and Public Finance Report and in the Public Finance Decision. This section also contains **general rules on the evolution of general government expenditure** to meet the requirement, laid down at the European level, to identify effective ways of controlling public expenditure, also by setting expenditure ceilings.

In addition to confirming the detailed information on the **outturns** and the **forecasts for the main expenditure areas,** with particular reference to public sector employment, social protection and health care, and on general government **debt** and its average cost, this section must also contain **forecasts based on unchanged policies** in respect of the main aggregates of the general government accounts referring to at least the following three-year period.

In this latter respect, the second section of the 2011 DEF contains the forecasts, under unchanged current policies, for the 2014 Fiscal Year using the methodology adopted by the European Commission, which takes historical revenues and expenditure as its basis, over a 4-6 year timescale, supplemented by detailed information making it possible to conduct an analysis disregarding typically cyclical interventions.

This section must also specify the **resources to be used to develop under-utilised areas**, indicating any supplementary national funding. Lastly, annexed to the section is a **methodological note**, which was already provided by law 196/09**,** setting out in analytical form the criteria used to forecast trends.

The **third section** lastly, contains the **outline of the National Reform Programme (PNR),** specifying the information and data required by European Union regulations and by the specific guidelines for that Programme.

The PNR – which is the most important novelty in the DEF – is a strategy document, consistent with the Stability Programme, which defines the measures to be taken to achieve the national targets in terms of growth, productivity, employment and sustainability set out in the new **"Europe 2020 Strategy"**.

It includes:

- **Progress with the reforms under way,** indicating any deviation between expected and actual results;
- The **national priorities** with the **main reforms to be implemented**, the **timing** planned for their implementation, and compatibility with the policy objectives set out in the Stability Programme;
- The national **macroeconomic imbalances,** and macroeconomic factors affecting competitiveness;
- The foreseeable **effects** of the **reforms** proposed in terms of economic growth, strengthening the **competitiveness** of the economic system and increasing **employment.**

In its updated version, set out in DEF 2011, the PNR illustrates the objectives and reform actions which are deemed necessary to remove the macroeconomic imbalances, improve national competitiveness, stimulate competition on the product market and improve conditions on the labour market, against the background of the enhanced sustainability of the public finances. The measures described in the PNR are consistent with the priorities listed in the Commission's Annual Growth Survey, with the actions provided for by the Euro Plus Pact to increase competitiveness and convergence, and with the specific objectives laid down in the Europe 2020 Strategy as transposed into the national objectives. The indication of the reforms already embarked upon and those planned to achieve the national targets set out in the Europe 2020 Strategy is preceded by a quantitative analysis, conducted using the methodology developed for the *Lisbon Assessment Framework* (LAF), which has played a significant part in identifying economic policy priorities and in the Member States' critical policy areas, contributing to define the bottlenecks, that is to say, the factors which are hampering national growth, and which demand intervention.

The main measures set out in the National Reform Programme are summarised in a table, given at the end of the third section of the DEF, comprising various items describing the reforms, quantifying the impact on public accounts and highlighting their functionality in terms of the EU objectives.

For each measure, the legal provisions are indicated, followed by a short description of the measure showing the progress made with its implementation, with specific indications regarding the timing of implementation.

Annexed to the DEF – that is to say in its Update Note – is a list of any **bills accompanying the budget package**, and required to be **submitted** to the two Houses of Parliament **by January each year.** Each bill shall contain homogeneous provisions by subject matter, taking account of the competences of the relevant government departments and helping to attain policy objectives, also by means of legislative, organisational, economic stimulus and growth initiatives.

Lastly, according to the new accounting law a series of documents have to be **annexed** to the DEF, containing:

a) A single summary report of all the **measures implemented in under-utilised areas**, in respect of which the Minister for Economic Development is required to indicate the contribution in terms of additional national funding and the results obtained, with particular reference to social cohesion, environmental sustainability, and the territorial breakdown of the measures to be implemented;
b) The **Strategic Infrastructure Programme** for which provision is made in the *"Legge Obiettivo* (Target Law)*"* and progress in implementing the same programme during the previous year, drawn up by the Minister for Infrastructure and Transport;
c) A document by the Minister for the Environment on **progress made in implementing commitments to reduce greenhouse gas emissions** stemming from Italy's obligations undertaken within the European Union and internationally, and the related policy guidelines;

d) A document specifying **the State budget resources earmarked for individual regions,** with reference to the latest outturn data available, separately indicating the economic categories relating to current and capital investment transfers to local authorities and the Autonomous Provinces of Trent and Bolzano;
e) A specific report on progress in **implementing the accounting and public finance reform law**.