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July 17, 2013

To: Members of the Executive Board

From: The Secretary

Subject: **The Functions and Impact of Fiscal Councils**

Attached for the **information** of Executive Directors is a paper on the functions and impact of fiscal councils.

It is intended that this paper will be published on the Fund's external website after Wednesday, July 24, 2013.

Questions may be referred to Mr. Debrun (ext. 38321), Mr. Kinda (ext. 39538), Ms. Curristine (ext. 38349), and Mr. Eyraud (ext. 35684) in FAD.

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THE FUNCTIONS AND IMPACT OF FISCAL COUNCILS

July 16, 2013

EXECUTIVE SUMMARY

- Fiscal councils are independent public institutions aimed at promoting sustainable public finances through various functions, including public assessments of fiscal plans and performance, and the evaluation or provision of macroeconomic and budgetary forecasts. By fostering transparency and promoting a culture of stability, they can raise reputational and electoral costs of undesirable policies and broken commitments.

- With commitments to sustainable public finances under close scrutiny since the crisis, policymakers' interest in fiscal councils is growing. This paper addresses three key questions about the potential contribution of fiscal councils to fiscal credibility. What are the main characteristics of existing fiscal councils around the world? Are there specific features in the design and institutional form of fiscal councils that can enhance their effectiveness? What are the main building blocks of effective fiscal councils? The paper relies on statistical analysis based on a unique dataset of fiscal councils, and on selected case studies.

- The paper concludes that all else equal, fiscal councils can promote stronger fiscal discipline as long as they are well-designed. The analysis points to a number of key features of effective fiscal councils: a strict operational independence from politics, the provision or public assessment of budgetary forecasts, a strong presence in the public debate (notably through an effective communication strategy), and an explicit role in monitoring fiscal policy rules.

- Of course, the remit, tasks, and institutional models of fiscal councils should reflect country-specific characteristics, such as available human and financial capacities, political traditions and the specific causes for excessive deficits and debts.

Approved By
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"*A dependence on the people is, no doubt, the primary control on the government; but experience has taught mankind the necessity of auxiliary precautions.*"
(James Madison, 1788, cited by Acemoglu, Robinson and Torvik, 2013).

INTRODUCTION AND MOTIVATION

1. **In recent years, a rapidly growing number of countries have established independent agencies aimed at promoting sound fiscal policies.** Although these institutions vary greatly in terms of their remit, tasks, and institutional forms, they tend to share an explicit mandate enshrined in legislation, a "watchdog" role implying a direct contribution to the public debate on fiscal policy, and strict non-partisanship in their activities. Importantly, fiscal councils do *not* have the discretion to set policy instruments. Unlike independent central banks in the monetary policy area, they are only facilitators of sound fiscal public finances, not decision makers deliberately insulated from politics. Earlier IMF staff analysis of non-partisan fiscal agencies (IMF, 2005, expanded by Debrun, Hauner and Kumar, 2009) referred to the generic term of "fiscal council" to designate these institutions. A handful of similar bodies have been in place for a long time—mostly in advanced economies.

2. **The fiscal legacy of the 2008–9 crisis puts a premium on strengthening the institutional anchor for sustainable public finances.** Thus the number of fiscal councils is likely to continue to rise in the foreseeable future, creating a demand for IMF analysis, advice, and technical assistance.

- In the *European Union*, the Treaty on Stability, Coordination and Governance, which came into force on January 1 of this year, mandates an "independent body" at the national level to monitor compliance with national fiscal policy rules and produce (or at least assess or validate) macroeconomic and budgetary forecasts used for budget preparation in each euro area member state (Article 3, par. 2). Similar requirements can be found in the EU Directive on "requirements for budgetary frameworks" of November 2011 and one of the Regulations of the so-called "two-pack," which came into force at the end of May this year.

- Among *common law countries*, the example recently set by Australia and Canada in establishing fiscal councils nested in parliament may inspire others.

- Among *emerging and developing economies*, a host of new or planned councils in emerging Europe (e.g. Croatia, Serbia, Romania) and Africa (e.g. Kenya and South Africa) could likewise encourage others to follow suit. However, in many developing economies—and also in small advanced economies—the specific institutional arrangements will have to be tailored to binding capacity constraints.

3. **Relying on empirical evidence from an original dataset, this paper aims at identifying operational guideposts to design and implement an effective fiscal council.** As such, the paper provides a consistent understanding of recent experience and an analytical

framework that inform views on (i) the relevance of a fiscal council as a tool to foster fiscal performance in a specific country; (ii) the adequate contours of a fiscal council's remit for that country; (iii) the specific tasks the council can be expected to perform; (iv) the characteristics most likely to facilitate the council's operation; and (v) the prerequisites for its effectiveness, notably in terms of the strength of public financial management processes, and the availability of human and financial resources consistent with the tasks of the council.

4. The paper provides the most comprehensive survey of fiscal councils available so far. [1] Existing studies have focused on selected country cases (e.g. Debrun, Hauner and Kumar, 2009; Calmfors and Wren Lewis, 2011; von Hagen, 2010; and OECD, 2013), while a systematic empirical analysis of fiscal councils' effectiveness and its determinants is at the core of the present paper. Indeed, the paper covers the global population of fiscal councils, adding to the diversity of experiences, institutional forms and political and economic contexts.

5. The paper is structured as follows. The first section reviews the rationale for fiscal councils, proposes a definition, and discusses the range of institutional models consistent with the definition. After a description of the main features of existing fiscal councils (second section), empirical evidence on various dimensions of their effectiveness is presented, using statistical analysis and case studies (third section). Finally, the last section of the paper distills the policy lessons and indicative guideposts of good practice.

RATIONALE, DEFINITION, AND MODELS

A. Fiscal Councils in the Economic Literature

Policy biases and possible solutions

6. For more than three decades, a vast literature has sought to explain why rational and accountable policymakers would choose undesirable policies. The reasons and nature of these systematic deviations from optimal policies—or policy biases—are multiple, and they apply to many policy instruments: monetary policy (inflationary bias), regulatory policy (too little or too much regulations depending on cases), or structural policy (status quo bias).

7. In the fiscal policy area, excessive deficits leading to rising debt-to-GDP ratios, and a tendency to spend temporary revenue windfalls (procyclicality in good times) are two widespread and well-documented biases. They often reflect failures to coordinate competing claims from various constituencies on the revenue pool (the so-called common pool problem), politicians' re-election concerns (leading to myopia when re-election is fundamentally uncertain,

[1] Another useful reference is the "Principles for independent fiscal institutions" prepared under the aegis of the OECD Working Party of Senior Budget Officials, which, however, is based primarily on case studies and a more limited number of country experiences. The Principles flesh out ways to address common areas of concern when establishing a fiscal council, including guarantees on political ownership and operational independence, accountability, transparency and communication. See also Kopits (2011).

or opportunistic pre-election spending), or an imperfect understanding of the government's budget constraint in the population at large ("fiscal illusion").[2] The latter problem is particularly relevant in resource-rich countries, where the complexities of assessing commodity cycles and large short-term spending pressures may lead to insufficient savings. As policy biases are invariably rooted in inadequate policymakers' incentives, the prospective solutions have in common an attempt to get these incentives right.

8. Ways to correct policy biases generally rely on one or a combination of the following approaches:

- **Rules.** Rules seek to impose a *direct and durable constraint* on policy choices, imposing limits on variables that are generally close to policy instruments (i.e. under good control of policymakers). Prominent examples include limits on the growth of monetary aggregates in the late 1970s and 1980s, and ceilings on government deficit and debts laid out in EU law, or balanced budget rules in most US states.

- **Independent authorities.** The *delegation* of policy instruments to independent agencies is another way to get incentives right. The main characteristics of these arrangements are strict guarantees of independence for the agency, a well-defined mandate against which the agency can be held accountable, and complete discretion for the agency in setting the delegated policy instruments to achieve its goals. Perhaps the best illustration of the delegation approach is the exercise of monetary policy by independent central banks.

- **Influence and persuasion.** Softer institutional arrangements exist for policies that (i) are not amenable to rules (mainly because they are inherently complex and not easily measurable, such as structural policies), and/or (ii) cannot be delegated outside the political sphere for clear normative reasons (mainly because they are distributive in nature, such as tax and transfer policies). These soft arrangements include the routine surveillance activities of international or supranational institutions as well as the work of watchdog bodies, whose role is to enrich the public policy debate through analysis, information, and advice.

  Fiscal councils belong to the third category. As such, they are fundamentally different from independent central banks, to which they are often, and incorrectly, compared (Debrun, 2011).

Independent Fiscal Authorities vs. Fiscal Councils

9. Fiscal policy rules have generally been the institutional solution of choice to address excessive deficits. Quantitative limits on debts, deficits, or spending have long been used to contain fiscal profligacy (e.g. Fabrizio and Mody, 2006; Debrun and others, 2008; and

[2] See Calmfors (2005), Morris, Ongena, and Schuknecht (2006) or Debrun, Hauner, and Kumar (2009) for discussions of the causes of deficit bias.

IMF, 2009). Yet, experience has revealed limitations often related to the rules' inflexibility in the face of adverse or unusual circumstances, or to the lack of supportive budget procedures. Inflexibility ultimately threatens the credibility of the rule itself, as the pressure of events can quickly lead to its suspension or even elimination.

10. Difficulties with fiscal rules have led some academics to propose the establishment of independent fiscal authorities. Like central banks, these institutions would receive the power to set binding limits to the budget deficit—or public debt accumulation—each year, including the capacity to use certain tax levers during the budget year to ensure compliance if slippages occur.[3] The theoretical underpinning of such proposals parallels arguments developed in favor of independent central banks after monetary policy rules had proved impractical in a context of unstable money demand (Thomson, 1981; Rogoff, 1985).

11. However, the case for fiscal policy delegation can be dismissed on both normative and positive grounds, and there is no real-world example of independent fiscal authorities. From a normative angle, all aspects of fiscal policy—including the deficit—are primarily distributive (across individuals, social groups or generations), which precludes delegation to unelected policymakers.[4] From a positive perspective, fiscal delegation itself is likely to lack credibility. Indeed, the distributive nature of fiscal decisions often makes excessive deficits and debts irresistible (i.e. individually optimal for the policymaker) *ex-ante*.[5] As a result, the delegation of fiscal policy to an independent authority is never perceived as desirable by policymakers, which explains why there is no example of such authorities (Debrun, 2011).

12. What is left in the quest for discipline-enhancing fiscal frameworks is an analysis of how *influence and persuasion* could be organized in the fiscal realm. A small but growing literature has argued that independent fiscal institutions, labeled as "fiscal councils," could improve policymakers' incentives to opt for sound fiscal policies even in the absence of delegation. First, by fostering transparency over the political cycle, a fiscal council can improve democratic accountability and discourage opportunistic shifts in fiscal policy (e.g. pre-electoral spending spree). Second, through independent analysis, assessments, and forecasts, such bodies can raise public awareness about the consequences of certain policy paths, contributing to a stability culture that directly addresses fiscal illusion. Hence a fiscal council can raise the reputational and electoral costs of unsound policies and broken commitments. Third and finally, a fiscal council can provide direct inputs to the budget process—e.g. forecasts or assessments of

[3] When pressures on the EU fiscal framework became evident in the early 2000's, a host of proposals for independent fiscal authorities—drawing on the seminal insights of von Hagen and Harden (1994)—emanated from academic circles. They are surveyed in Debrun, Hauner, and Kumar (2009).

[4] See Alesina and Tabellini (2003) for a political-economic model of what is ultimately the basic Jeffersonian principle of no taxation without representation. As these authors show, delegation can be advisable for instruments that have distributive implications, but are not conceived as a primary tool to address equity issues.

[5] In other words—and unlike the monetary commitment problem, which results from a mere time-inconsistency problem where high inflation is only preferred *ex-post*—the bias towards excessive deficit is entrenched in the very fabric of the political system: it is optimal ex-ante in the eyes of the decision maker.

structural positions—thereby closing technical loopholes that allow governments to circumvent numerical fiscal rules.

B. Definition and Broad Models

13. A fairly broad definition of fiscal councils is required to accommodate the wide range of institutions considered as such in the literature. Unlike central banks which have fairly uniform goals and instruments across countries, the objectives, tasks and institutional form of fiscal councils depend on the causes and manifestations of the bias affecting fiscal policy and, given the deeply political nature of fiscal policy, on the particulars of the political system. As documented in the following section, institutions considered as fiscal councils in the literature vary greatly in terms of the scope of their remit, the definition of their tasks, and the specifics of their institutional design (degree of legal independence, size, and relations with other public institutions).

14. The consensus view is that a fiscal council is an independent public institution informing the public debate on fiscal policy.[6] This implies a mandate and public funding to perform tasks in insulation from partisan influence. It is generally understood that the council's functions serve the ultimate goal of promoting financially sustainable and economically sound fiscal policies through greater transparency and accountability. More refined definitions seek to specify what these functions could or should be or what the independence of the council really means. IMF (2005, p. 4) suggests that a council's main functions include the provision of independent analysis on fiscal policy developments, the preparation of unbiased projections, and the issuance of "normative judgments" (recommendations) on fiscal policy. OECD (2013) clarifies that the notion of "independence" relates to the non-partisan nature of the council's analysis, and that the work of the council should be forward-looking in essence.

15. For the purpose of this paper, the following definition was used:

A fiscal council is a permanent agency with a statutory or executive mandate to assess publicly and independently from partisan influence government's fiscal policies, plans and performance against macroeconomic objectives related to the long-term sustainability of public finances, short-medium-term macroeconomic stability, and other official objectives. In addition, a fiscal council can perform one or several of the following functions: (i) contribute to the use of unbiased macroeconomic and budgetary forecasts in budget preparation (through preparing forecasts, or proposing prudent levels for key parameters), (ii) identify sensible fiscal policy options, and possibly, formulate recommendations, (iii) facilitate the implementation of fiscal policy rules, and (iv) cost new policy initiatives.

[6] This is close to the definition proposed by Wren-Lewis (https://sites.google.com/site/sjqwrenlewis/fiscal-councils).

16. The definition accommodates a great variety of institutional arrangements, while highlighting some of the key functions a fiscal council would be expected to perform.

a. ***A fiscal council does not need to be a stand-alone institution akin to a central bank.*** The notion of "independence" primarily refers to guarantees of non-partisanship in performing its tasks—or operational independence—rather than the strict legal separation that the delegation of policy prerogatives requires. This explains why fiscal councils with an executive mandate can qualify as "independent" institutions under the definition. In general, and without prejudice of its overarching objective to promote fiscal sustainability, the council would be expected to benchmark its assessments against official policy objectives,[7] as using its own benchmarks could place it in the partisan fray and undermine its legitimacy. The definition thus accommodates fiscal councils embedded in—and therefore directly accountable to—ministries or parliaments, as well as the possibility for existing institutions, such as audit offices or central banks, to have a "fiscal council" leg.

b. ***The work of the council is distinct from audit.*** First, the work of a fiscal council is macro-economic in nature, as opposed to the mainly legal and more micro-economic approach underlying audit. Second, the fiscal council's work is also expected to play a key role at the planning and policy-formulation stage, while audit focuses strictly on ex-post evaluations.

c. ***Fiscal councils can be the instrument of choice to curb the tendency to base budgets on overoptimistic revenue forecasts and unrealistic cost estimates of programs.*** Biased forecasts reduce the effectiveness of numerical fiscal rules and undermine transparency and accountability.

d. ***A fiscal council can be mandated to formulate policy judgments and recommendations.*** Although normative calls can raise concerns about non-partisanship and legitimacy, they could be useful in countries with more consensual decision-making by focusing the debate on economically and financially sensible policy options. Also, there may be highly contentious distributive matters for which policymakers consider that a neutral view should form the base for a consensual agreement.

e. ***Fiscal councils can complement fiscal rules.*** A tendency in the academic literature has been to oppose councils to rules, arguing that the former should replace the latter. The argument was mostly driven by the central bank analogy, which was dismissed earlier. Subsequent sections of this paper elaborate on possible synergies.

[7] These would typically be those guiding the actions of the executive branch.

17. Overall, the paper's definition is consistent with three broad institutional models of fiscal councils:

a. ***Stand-alone institutions*** are the closest to the model suggested in the academic literature. They have no organic link with policymakers beyond appointment procedures and accountability mechanisms, and often emanate from comprehensive Fiscal Responsibility Laws that include explicit guarantees on their independence.

b. ***Fiscal councils formally under the executive or legislative branch of the political system*** range from legally separate entities with a well-defined mandate and strict guarantees of independence to bodies that are integral part of parliament (often known as a parliamentary budget office) or a ministry. The latter tend to extract their operational independence from the reputational benefits associated with their non-partisan role in the budget process and the public debate.

c. ***Fiscal councils associated with other independent institutions*** can be found in central banks, audit institutions, and independent statistical agencies. That approach allows the council to immediately benefit from the independence of its host and from economies of scale, but requires clear procedures to avoid confusions regarding the respective mandates and functions of the host and the guest.

C. Other Institutions

18. Other institutions inform the public debate on fiscal policy. Central banks routinely comment on fiscal policy developments and express their views on desirable trajectories for key aggregates and even on specific measures. Audit offices sometimes venture in ex-ante analyses of policies and programs, while supranational and international organizations analyze and comment on fiscal performance as part of their regular surveillance mandate. Last but not least, private analysts—in financial institutions, or think tanks—also provide their share of forecasts and commentaries which can have a significant impact on budget decisions, especially if they can affect market conditions or enjoy high reputation in the public.[8]

19. However, the fiscal council is uniquely positioned to foster transparency and accountability, and trigger reputational effects. Unlike other institutions commenting on fiscal policy, the official mandate to contribute to the public debate and the budget process magnifies the reputational impact of the council's assessments and analysis. The mandate also carries a degree of legitimacy that could encourage government to "comply or explain," even if it is not legally compelled to do so.

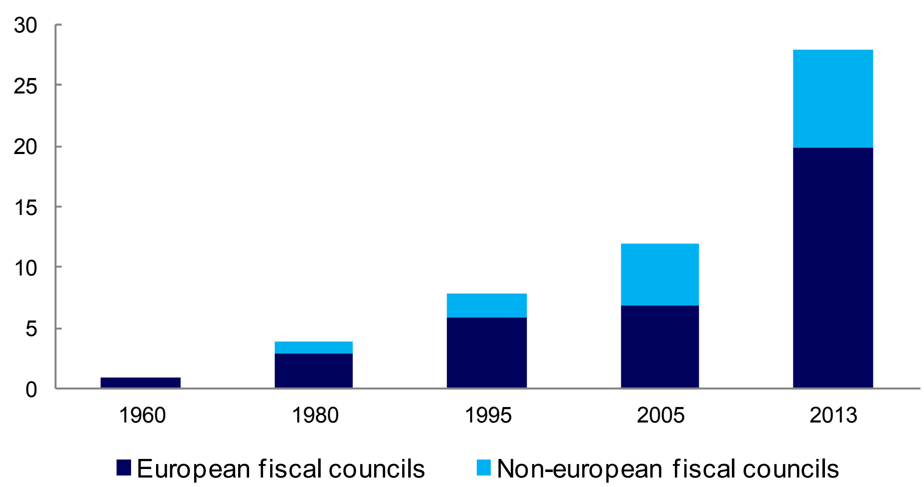
[8] For instance, in the United Kingdom, analyses by the Institute for Fiscal Studies are highly visible and discussed. In Austria, the government generally uses the forecasts provided by the WIFO, a privately funded and reputable research institute.

MAPPING FISCAL COUNCILS

A. Fiscal Councils in the World: A Growing and Diverse Population

20. The number of fiscal councils has increased rapidly since 2005. In 1960, only one country—The Netherlands—had an active fiscal council and only four additional countries—Denmark, Germany, the United States, and Belgium—adopted such institutions over the next three decades. The number surged after 2005, reaching 29 at end–January 2013 (Figure 1).[9] Newcomers include the Fiscal Policy Council in Sweden (2007), the Parliamentary Budget Officer in Canada (2008), the Fiscal Council in Slovenia (2009) and Romania (2010), the Office for Budget Responsibility in the United Kingdom (2011), the Portuguese Public Finance Council (2011), the Irish Fiscal Advisory Council (2011), parliamentary budget offices in Kenya (2009), Australia (2012), Italy (2012) and South Africa (2013), and the High Council of Public Finance in France (2013). This year, Chile has formally established a fiscal council, while Spain is expected to complete legislative work on a Fiscal Authority for Fiscal Responsibility by year-end. Although most of established fiscal councils are in advanced economies, particularly in Europe, there is growing interest in emerging markets and developing economies.

Figure 1. Number of Fiscal Councils



Source: IMF Fiscal Council Dataset.

[9] Note that there are two fiscal councils in Belgium and Slovenia, corresponding to a separation between forecasting and advisory functions. See Bogaert and others (2006) for details on the Belgian case.

Box 1. The IMF Fiscal Council Dataset

The fiscal council dataset assembled for this paper covers existing fiscal councils across the Fund's membership, as well as councils for which the primary legislative texts have been adopted as of end-January 2013, and those that were de facto or de jure eliminated. The dataset used a variety of sources, including fiscal responsibility laws, fiscal councils' websites, IMF country papers, and in some cases, country authorities themselves. The dataset has also benefited from inputs by IMF desk economists. For EU and OECD member states, the dataset draws from the European Commission's Fiscal Institution Database and the background country notes used by the OECD to prepare their draft Principles for independent fiscal institutions. The dataset includes general information such as the name and acronym of the council and its date of creation, the main features of the council's remit, their specific tasks and instruments at their disposal to influence the conduct of fiscal policy, and key institutional characteristics such as the existence of formal guarantees of independence, accountability requirements, and their human and financial resources. The main variables used in the descriptive and empirical analyses (this section and the next) are as follows:

Independence:

- *Legal independence*: The council's independence from political interference is guaranteed by law (Yes: 1, No: 0).

- *Safeguards on budget:* Safeguards on the council's budget are deemed to exist if the budget is (i) set by the central bank, (ii) part of the overall budget of the legislative branch (i.e. protected from executive decisions), (iii) guaranteed by budget appropriations with separate line item in the budget, or (iv) subject to any other guarantee commonly granted to independent institutions, such as regulators.

Fiscal rules monitoring: The council is mandated to monitor compliance with numerical fiscal rules (Yes: 1, No: 0).

High media impact: This variable reflects IMF staff assessment based in the number of publications, media references to these reports, and in the case of EU members, the authorities own assessment reflected in the Fiscal Institutions Database.

Forecasts provision/assessment: The council is mandated to provide or assess macroeconomic forecasts used for budgetary projections (Yes: 1, No: 0).

Costing of measures: The council is mandated to provide costing of measures and reforms affecting public finances (Yes: 1, No: 0).

Box 1 (Concluded)

Table. List of Fiscal Councils in the Dataset

Country	Fiscal Council	Conventional Acronym	Start of activity	Type
Australia	Parliamentary Budget Office	…	2012	Parliamentary Budget Office
Austria	Government Debt Committee	…	2002	Attached to the Central Bank
Belgium	High Council of Finance - Section "Public Sector Borrowing Requiremer	HCF	1989	Attached to the Executive
Belgium	Federal Planning Bureau	FPB	1994	Attached to the Executive
Canada	Parliamentary Budget Office	PBO	2008	Parliamentary Budget Office
Croatia	Fiscal Policy Council	…	2013	Attached to the Executive
Denmark	Danish Economic Council	…	1962	Attached to the Executive
Finland	National Audit Office of Finland	…	2013	Audit Office performs tasks of fiscal counci
France	High Council of Public Finance	…	2013	Attached to the Audit Institution
Georgia	Parliamentary Budget Office	…	1997	Parliamentary Budget Office
Germany	German Council of Economic Experts	…	1963	Stand-alone
Hungary	Fiscal Council	…	2009	Stand-alone
Ireland	Irish Fiscal Advisory Council	IFAC	2011	Stand-alone
Italy[1]	Parliamentary Budget Office	…	2014	Parliamentary Budget Office
Japan	Fiscal System Council	…	1950	Attached to the Executive
Kenya	Parliamentary Budget Office	…	2009	Parliamentary Budget Office
Mexico	Center for Public Finance Studies	…	1999	Parliamentary Budget Office
Netherlands	Netherlands Bureau for Economic Policy Analysis	CPB	1945	Attached to the Executive
Portugal	Portuguese Public Finance Council	CFP	2011	Stand-alone
Romania	Fiscal Council	…	2010	Stand-alone
Serbia	Fiscal Council	…	2011	Stand-alone
Slovak Republic	Council for Budget Responsibility	CBR	2011	Stand-alone
Slovenia	Institute of Macroeconomic Analysis and Development	IMAD	1991	Attached to the Executive
Slovenia	Fiscal Council	…	2009	Attached to the Executive
South Africa[1]	Parliamentary Budget Office	…	2014	Parliamentary Budget Office
South Korea	National Assembly Budget Office	NABO	2003	Parliamentary Budget Office
Sweden	Swedish Fiscal Policy Council	FPC	2007	Stand-alone
United Kingdom	Office for Budget Responsibility	OBR	2011	Attached to the Executive
United States	Congressional Budget Office	CBO	1974	Parliamentary Budget Office

[1] The South African and Italian PBOs are being established and expected to be fully operational by the end of 2014. Chile has established a Fiscal Advisory Council in April 2013.

Remit and Tasks of Fiscal Councils

21. While the common impetus for the creation of fiscal councils has been to encourage sound fiscal policies through independent oversight, there is considerable diversity among them. Beyond the common motivation, the design of individual institutions reflects the legal, political and institutional environments of each country, as well as the specific causes and manifestations of the bias affecting discretionary policies. Fiscal councils can nevertheless be categorized following economically relevant characteristics, including their remit or functions, the tasks performed to accomplish these functions, and basic institutional features, including their governance. The analysis will also make a distinction between "veterans" (established prior to 2005) and the "new generation" (established in 2005 or later). The rationale for that distinction is that the design of new institutions may have been influenced by the intensifying academic debate on their potential role in improving the conduct of fiscal policy[10] , and by the accumulating experience with politically independent agencies in other policy areas

[10] See for instance von Hagen and Harden (1995), Eichengreen, Hausmann and von Hagen (1999), Calmfors (2003), Fatàs and others (2003), Wren-Lewis (2003), Castellani and Debrun (2005), Wyplosz, (2005), and Leith and Wren-Lewis (2006).

such as central banking or the regulation and supervision of specific sectors (banking, energy, media).

22. In line with the definition proposed above, the functions of fiscal councils generally belong to one of the following broad categories (Figure 2):

a. ***Independent analysis, review, and monitoring of government's fiscal policies, plans, and performance.*** This includes reviews of governments' annual or medium term budget proposals generally with respect to compliance with official objectives—such as those enshrined in fiscal policy rules—and/or the long-term sustainability of public finances and the related risks. Typically, fiscal councils focus on a macroeconomic analysis anchored in their ultimate objective to promote sound fiscal policies by informing the public debate. Fiscal councils also provide ex-post assessments of macroeconomic and fiscal performance against official aggregate objectives and targets. More broadly, councils also carry out research with clear relevance for the health of public finances and the conduct of fiscal policy, such as labor market performance, the impact of aging population, or the extent of tax expenditures.

b. ***Developing or reviewing macroeconomic and/or budgetary projections.*** Assessments of macroeconomic and/or budgetary forecasts can be associated with a right to publicly denounce eventual biases or an obligation—de jure or de facto—from the government to "comply or explain" in case of significant differences between the forecasts underlying budget plans and those of the council. The council could also be mandated to prepare the macroeconomic forecasts used for budget preparation or to set key assumptions and parameters, such as a prudent price level for certain commodities with a large budgetary impact (either because the country is a large commodity producer or because of extensive subsidy schemes).

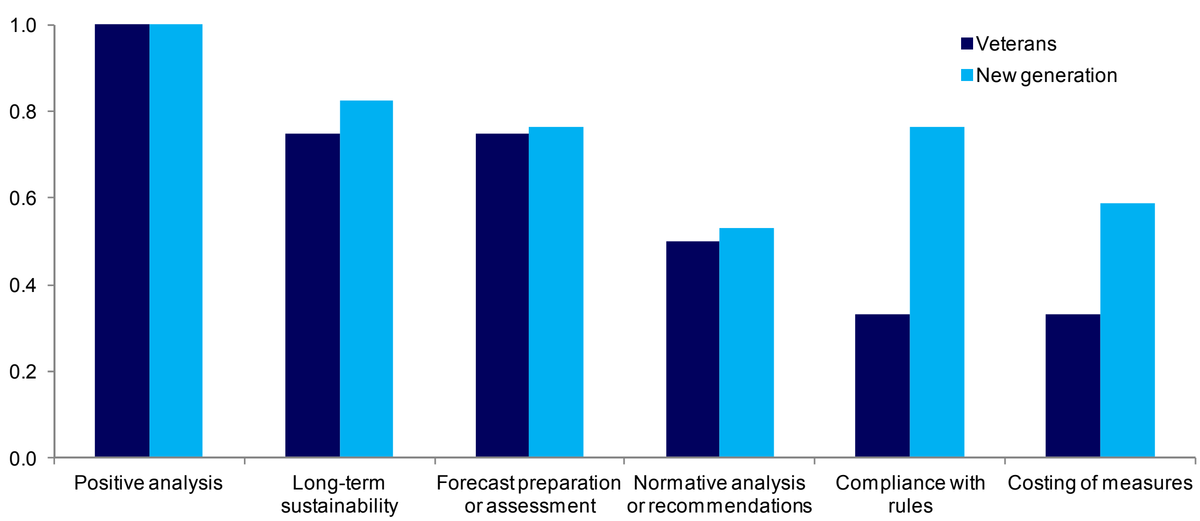
c. ***Costing of budget and policy proposals, including possibly, election platforms.*** Beyond macroeconomic and revenue forecasts, a fiscal council could also be tasked to produce unbiased estimates related to specific spending programs or policy measures.

d. ***Advising policymakers on policy options.*** This function can be general—a right to comment and issue recommendations on any policy issue of its choosing—or specific—limited to a particularly contentious issue that must be solved by consensus. A general function is better suited to countries with an already rich public debate and a relatively consensual approach to policy-making. A specific function can be useful in issues such as the sharing of certain revenues across unequal regions, where a consensus must be found but interests among decision makers diverge strongly. In resource-rich economies, issues related to the regional and intergenerational distribution of revenues from non-renewable commodities is also an area where non-partisan inputs could avoid undesirable biases.

23. While all fiscal councils identified for this study routinely perform broad oversight functions, there is much more variation as regards the other functions described above. For instance, the Netherlands Bureau for Economic Planning Analysis performs extensive forecasting and costing functions. However, it does not make judgments on the appropriateness of the government's budgetary plans. In contrast, the Swedish Fiscal Policy Council and the Irish Fiscal Advisory Council engage in normative analysis, but do not produce their own forecasts or costing. Some countries have even established a division of labor between different institutions. In Belgium, the Federal Planning Bureau focuses strictly on the provision of macroeconomic forecasts, whereas the High Council of Finance (Public Sector Borrowing Requirement Section) performs oversight and monitoring functions, and must provide policy recommendations, including on the distribution of the eventual fiscal effort among central and subnational entities to comply with general government rules.

24. Recent fiscal councils are more often explicitly tasked to monitor compliance with fiscal policy rules and to cost policy measures. While the vast majority of fiscal councils continue to perform positive analyses, evaluate long-term sustainability issues, and prepare or assess macroeconomic forecasts, newly created ones have broader remits (Figure 2). The majority (more than ¾) of the new generation monitor compliance with fiscal rules, more than the double compared to veteran institutions. This trend is associated with the increasing use of numerical fiscal rules (Schaechter and others, 2012) and is likely to continue given new legal requirements mandating such independent monitoring for most European Union member states (see Box 2 in the Policy Considerations Section). The costing of policy initiatives has also become a more common feature among newer fiscal councils.

Figure 2. Remit of Fiscal Councils (relative frequencies)



Source: IMF Fiscal Council Dataset.

25. The approaches taken to perform some of these broad functions vary significantly across countries.

a. ***Fiscal councils' involvement in budgetary forecasts*** ranges from preparing a set of macroeconomic and revenue projections that the government is obligated to use to a mere technical review of the budget assumptions. For instance, the Dutch government uses the macroeconomic, revenue, and expenditure forecasts prepared by the fiscal council, whereas Belgium's budget must be based on macroeconomic forecasts from the Federal Planning Bureau. In the United Kingdom, a core mission of the Office of Budget Responsibility (OBR) is to produce 5-year economic and fiscal forecasts, with the Treasury subject to a "comply or explain" clause—i.e. it has to publicly motivate its eventual choice not to use OBR's forecasts. In the United States, Canada, and Denmark, the fiscal council's forecasts only serve as a comparator to official projections. Elsewhere, the council's role in forecasting is limited to ex-ante and/or ex-post reviews of government's economic and budgetary forecasts, including the underlying assumptions and models used. For instance, the Swedish fiscal council has recently evaluated the quality of government forecasts.

b. **Given the challenges related to entitlement regimes, a number of councils go well beyond yearly forecasts, taking a medium or long term view of fiscal trajectories.** For instance, the US Congressional Budget Office forecasts typically cover a 10 year period, while the British, Canadian, Korean and Dutch councils produce long-term projections (over 40 to 75 years horizons) often in the context of a specific mandate to analyze the sustainability of public finances.

c. **Approaches to the costing of policy measures—an activity in which nearly half of fiscal councils are involved—are also highly country-specific.** These range from simple reviews of tax and spending estimates used in the budget to an extensive costing of specific policy initiatives emanating from government or individual parliamentarians. The latter approach is often seen in countries where the fiscal council takes the form of a budget office associated with the legislative branch, including Korea, Mexico, and the United States.[11] In Canada, the office of the Parliamentary Budget Officer conducts only selected costing of bills and proposals from the legislature and it assesses the government's own costing of existing programs. Nested in the Ministry of Economic Affairs, the Dutch fiscal council routinely responds to requests from line ministries regarding new policy initiatives and provides cost-

[11] The National Assembly Budget Office in Korea produces over 400 cost estimates of bills discussed in the national assembly and tax proposals from individual members. It also examines how new legislation will impact on government revenues and expenditure over a 5-year horizon (OECD). In Mexico, the Centre for Public Finance costs proposals for new bills or amendments coming from the legislature itself and its individual members. In the United States, the CBO has an extensive costing role for all appropriate bills before Congress; bills from congressional committees, and projected cost of proposed federal mandates in legislation on state and local governments and/or the private sector, and short and medium costs of government programs. In addition, the CBO has a scorekeeping function whereby it tracks the cost of individual and cumulative legislation against an established budget constraint (Joyce, 2011).

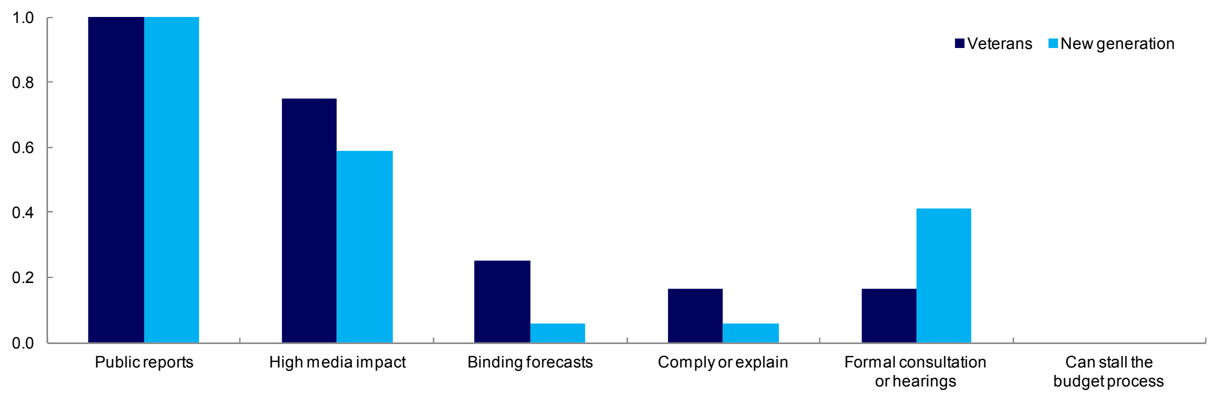
benefit analysis of major infrastructure projects. In the United Kingdom, the OBR must review the tax and spending estimates produced by government ministries as part of the draft budget proposal, but it does not cost specific policy initiatives. In Australia and the Netherlands, assessments go beyond legislative or executive proposals and extend to the economic and budgetary impact of political platforms prior to elections.

26. Fiscal councils can carry out other functions, although they never imply binding constraints on policymakers' discretion. Among these other functions, one finds analyzing the efficiency and/or effectiveness of public expenditure and fostering coordination among the various entities of the general government. In Korea, the NABO has an important evaluation role and makes recommendations for improving the efficiency and effectiveness of government programs (existing or planned). Providing an annual assessment of the effectiveness of public spending is also part of Fiscal Council's mandate in Slovenia. Although these activities are limited to the central government,[12] several councils have an explicit mandate to examine fiscal issues related to state and local governments and/or public enterprises. In Portugal, the Council on Public Finances (CPF) is required to assess the financial position of autonomous regions, local governments, and public enterprises, while in Austria the Government Debt Committee analyzes "the effects of financial operations on the national economy in connection with the indebtedness of all the public authorities," and in Belgium the High Council of Finance makes recommendations on the contribution of each government entity to secure compliance with general government rules.

27. Overall, fiscal councils influence the conduct of fiscal policy mostly indirectly through the public debate, and only rarely through direct action in the budget process. All fiscal councils prepare public reports that often have a significant media impact (Figure 3). This is an essential vehicle for the reputational impact fiscal councils work is expected to have on policymakers. Not surprisingly, the well-established councils are more likely to benefit from a solid reputation of independence and professional competence than younger peers. Direct involvement in the form of providing forecasts that are either binding or linked to a "comply or explain" clause is rare. Interestingly, however, close to one half of post-2005 fiscal councils hold formal consultations with the government or hearings in Parliament on a regular basis, which gives them more direct access to decision makers. Yet no fiscal council has any direct or indirect veto right that could stall the budget process.

[12] In the United States, some individual states—e.g. California—have their own independent fiscal councils.

Figure 3. Tasks and Channels of Influence (relative frequencies)



Source: IMF Fiscal Council Dataset.

Independence, Accountability and Governance

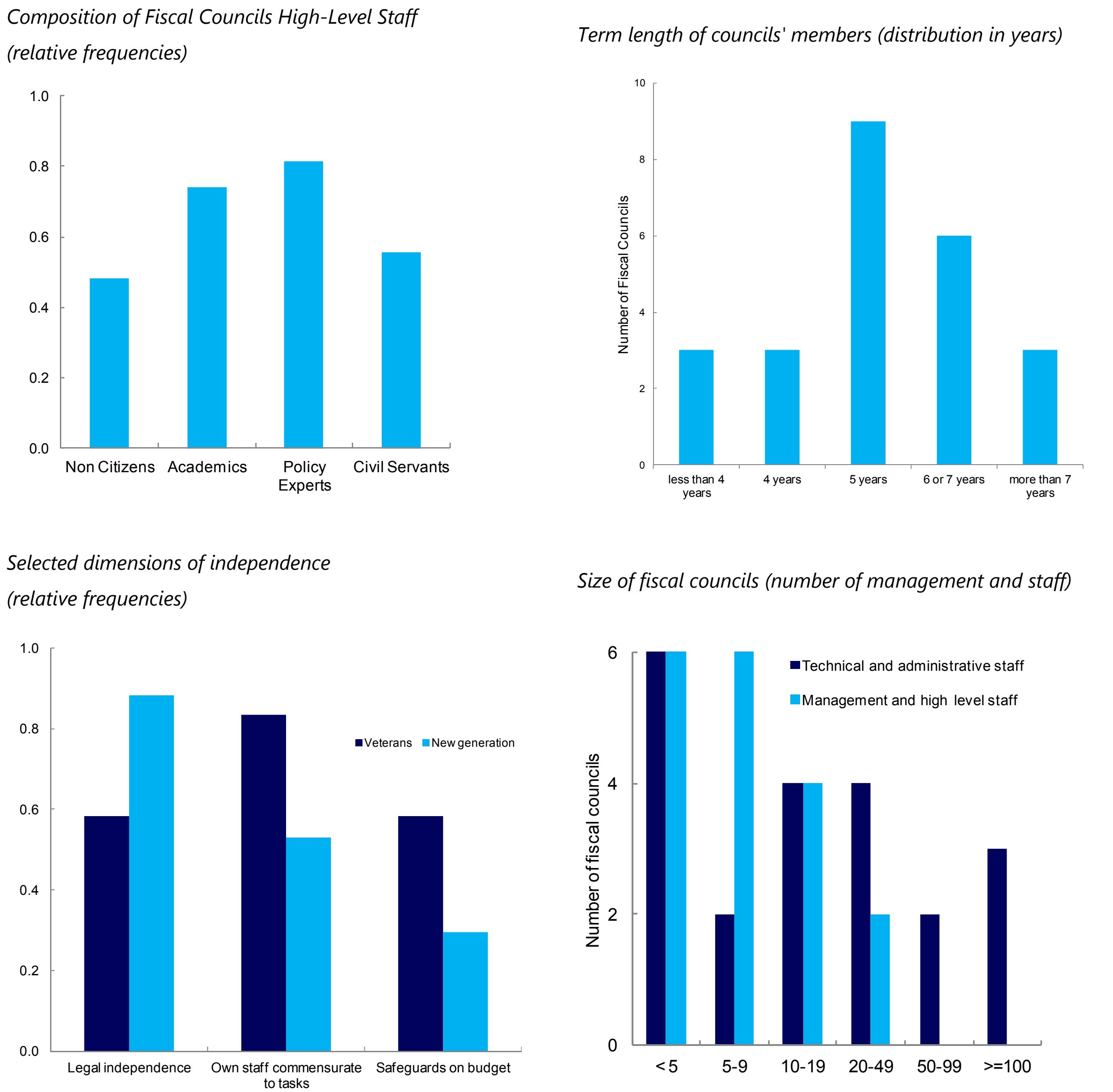
28. Independence from partisan influence is often enshrined in legal provisions banning political interference, especially among newer councils (Figure 4). A majority of fiscal councils enjoy legal protections against partisanship. These include strict requirements of professional proficiency and expertise for the council's management and staff,[13] non-renewable tenures exceeding the normal legislative term, and procedures that reduce the risk of politically-motivated appointments—see Box 3 in the Policy section. Independence also implies the freedom for the council to undertake any analysis it deems necessary to fulfill its mandate and to choose its communication strategy. While a large majority of fiscal councils benefit from such protections, they are noticeably more prevalent among newer institutions, likely reflecting the fact that they have no established record of independence and professional excellence. This may also reflect the evolution of the academic debate emphasizing the need for guarantees comparable to those applied to central banks.

29. The operational independence of the fiscal council also requires that resources remain commensurate (in quality and quantity) to its remit at all times. Unlike central banks, a council has no significant own income, and the risk of politically-motivated changes in their resource envelope should be minimized. Financial starvation could indeed be one way for governments to curtail their fiscal council. On this dimension, well-established fiscal councils fare better than more recent creations, in part reflecting the inertia inherent to the dynamics of public institutions (Figure 4, bottom left panel). Pre-2005 councils are often larger in terms of staff, although there is considerable cross-country heterogeneity (Figure 4, bottom right panel).

[13] A significant and growing share of fiscal councils welcome foreign experts in their senior management, increasing the perception of independence from local politics and allowing to access a greater pool of talents.

Budgets are also more likely to be protected from retaliatory cuts among older councils. Guarantees on the fiscal council's resources range from having a separate budget line subject to vote in Parliament, to multi-year appropriations and even extra-budgetary financing—e.g. through the central bank, as in Austria and the Slovak Republic.[14]

Figure 4. Aspects of Independence



Source: IMF Fiscal Council Dataset. Coverage varies with data availability

[14] Obligating the central bank to fund a fiscal council is technically akin to monetary financing, which is banned in many countries. One way around it—used in the Slovak Republic—is to give the central bank the right to claim a repayment of that transfer to the government.

30. **Legal independence and safeguards on resources tend to be associated with specific monitoring and assessment tasks and a high media impact.** Table 1 below shows the proportion of councils with the characteristic in line that simultaneously exhibit the characteristic in column. The vast majority of fiscal councils benefitting from some form of protection on their budgetary allocations also have strong legal guarantees of independence and a high media impact (roughly 80 percent). By contrast, only a minority of legally independent councils have their resources protected from possible retaliatory cuts, although there remains a comfortable majority to have media impact. Safeguards on the council's budget thus seem to offer a useful complementary signal of genuine independence. Legal independence is also frequently associated (two-way associations) with the council's involvement in forecasting and in monitoring compliance with fiscal rules, two activities which require a strong public perception of independence to be meaningful.

Table 1. Selected Combinations of Fiscal Councils' Characteristics

	Legal independence	Safeguards on budget	Compliance with rules	High media impact	Forecast assessment
Legal independence	1.0	0.4	0.7	0.7	0.7
Safeguards on budget	0.8	1.0	0.4	0.8	0.7
Compliance with rules	0.9	0.3	1.0	0.6	0.6
High media impact	0.8	0.8	0.6	1.0	0.7
Forecast assessment	0.9	0.7	0.6	0.7	1.0

Sources: IMF Fiscal Council Dataset, and staff calculations.

31. **Despite the fairly high frequency of guarantees on independence, only a minority of fiscal councils are subject to formal accountability frameworks.** Like in the case of central banks, explicit accountability requirements could imply regular hearings of the council's head before parliamentary committees,[15] explicit reporting procedures—e.g. in case of a large forecast error made by the council— and independent oversight of the council's performance—including peer reviews or self assessments (like in the Canada, United kingdom or the Slovak Republic).

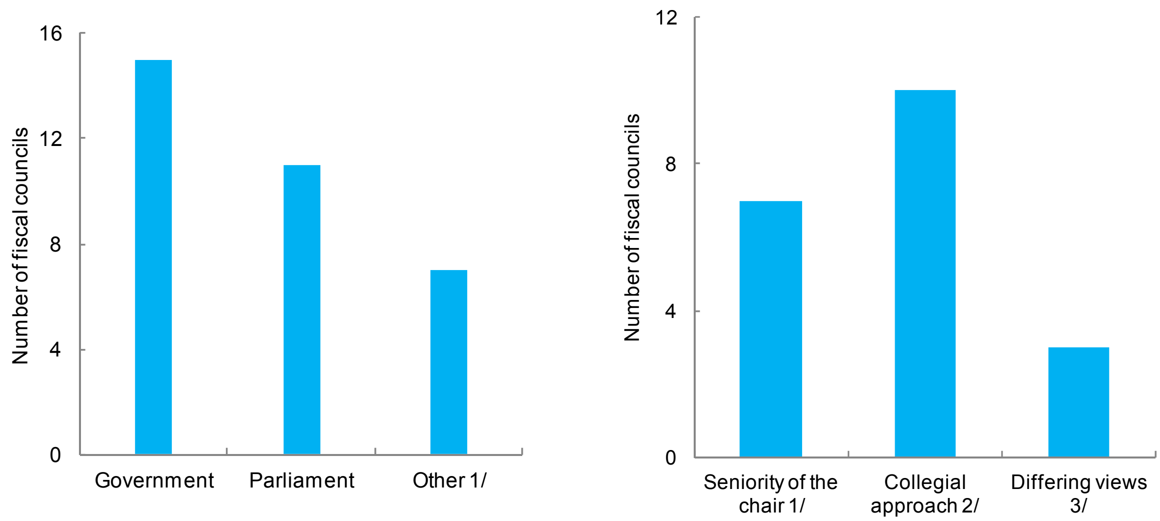
[15] This is notably the case in Finland, France, Italy, Romania, and Serbia.

32. No clear trend has emerged as regards other key dimensions of governance, such as managerial appointments and decision rules (Figure 5). Fiscal councils' management is often appointed by the executive, although government's discretion is sometimes limited, such as in Sweden, where the outgoing chair proposes suitable replacements to the Finance Minister. A growing number of countries have opted for electing council members by parliament, which may offer a stronger guarantee against executive interference during the tenure of council members. In some rare cases, appointments are made by the head of state, or independent institutions, such as the central bank or the audit office. Once in place, many fiscal councils operate as committees making decisions by consensus or majority voting. In a few cases, council members can publicly express dissenting views. In a fair number of countries—typically those with parliamentary budget offices—the chairperson has been given a dominant role.

Figure 5. Aspects of Governance

Who appoints the fiscal council's management?

How does the council decide?



1/ Includes high level staff appointed by the head of state, or independent institutions.

1/ The chair has the decision power, or it has the final say, or it has a prominent role in the decision.
2/ Decision reached through consensus or majority vote in the board.
3/ Public expression of differing views within the council.

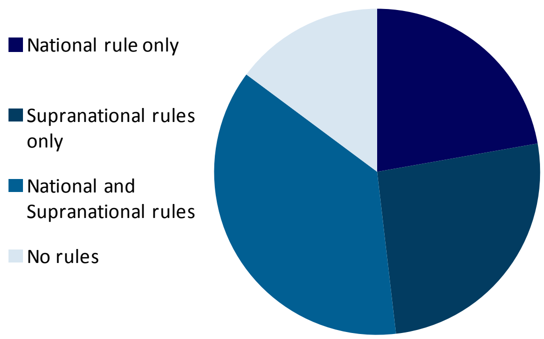
Source: IMF Fiscal Council Dataset. Coverage varies with data availability.

B. Fiscal Councils and Fiscal Rules

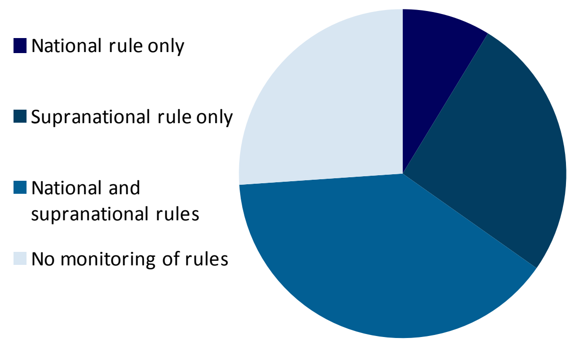
33. Countries often use fiscal councils in combination with fiscal policy rules, not as a substitute to them. An influential academic literature has called for substituting fiscal policy rules by fiscal councils equipped with the power to directly constrain policymakers' discretion (e.g. Fatàs and others, 2003, and Wyplosz, 2005). However, fiscal councils are often present together with fiscal rules, possibly because such agencies "with teeth" are hardly conceivable in practice, and the soft power of real-world fiscal councils cannot be expected to fully substitute for the constraining role of rules. Quite to the contrary, these institutions could reinforce each other. Interestingly, most countries with fiscal councils also have numerical rules (about 80 percent); and among these, the council is mandated to monitor compliance with the rules in about ¾ of the cases (Figure 6).

Figure 6. Fiscal Councils and Fiscal Rules

Proportion of countries with fiscal councils also subject to fiscal rules



Proportion of countries with fiscal rules and council mandating the latter to monitor compliance

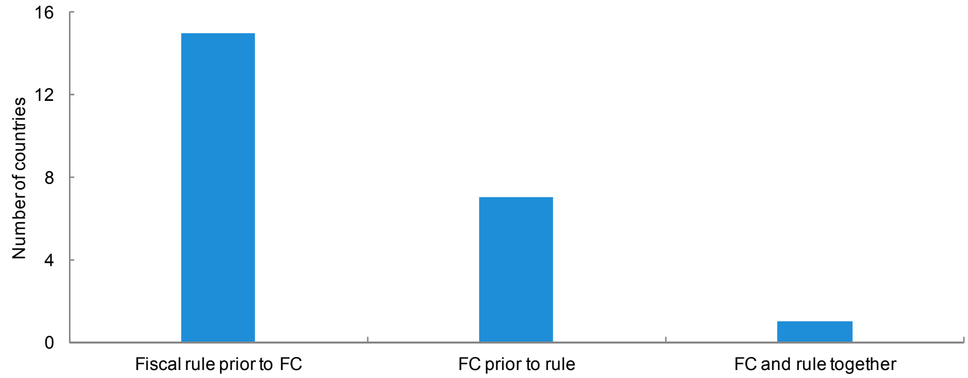


Sources: IMF Fiscal Council Dataset, and staff calculations.

34. The establishment of fiscal councils has tended to follow the adoption of numerical rules. While the number of countries with fiscal rules surged during the last two decades, the growing interest in fiscal councils is more recent, with more than half of the councils created after 2005. Hence most fiscal councils have become active after the introduction of the numerical rules the majority of countries (Figure 7). Only a handful of councils (in Belgium, Denmark, Germany, Slovenia, The Netherlands, the United States, and Mexico) were created prior to the introduction of numerical fiscal rules. These trends would be consistent with a growing awareness of the difficulties to implement fiscal rules and the simultaneous tendency to adopt more sophisticated fiscal policy rules, including rules formulated in structural terms, those with escape clauses subject to technical conditions, and those with an automatic error-correction mechanism.[16]

[16] For instance, in the context of the fiscal governance reform in the European Union, the European Commission recommends that a fiscal council assess whether the "conditions warranting the activation of the correction mechanism" are met, whether any correction taking place is line with the mechanism and whether the conditions triggering the activation of an escape clause are satisfied. The Commission also recommends that the government be subject to a "comply or explain" clause in these matters (Communication (2012) 342 of the European Commission).

Figure 7. Fiscal Councils and Fiscal Rules: The Sequencing



Sources: IMF Fiscal Council Dataset, and staff calculations.

35. A range of functions performed by fiscal councils can explain this revealed preference for combining rules and councils.

a. ***Fiscal councils can help address "fiscal illusion,"*** a cause of excessive deficits outside the reach of a rule because it suppresses incentives to comply. An electorate subject to fiscal illusion has a poor understanding of the mechanics of the government's budget constraint (i.e. the fact that current choices inevitably affect future policies), implying potential electoral *costs* to compliance with a fiscal rule.[17] Thus by informing and educating the general public and policymakers on the merits of sound public finances, fiscal councils can promote a stability culture, contributing to better aligned incentives between voters and their representatives.

b. ***Through their forecasting and costing functions, fiscal councils can close technical loopholes commonly exploited by uncommitted governments to circumvent a rule,*** including the tendency to overestimate expected revenues, underestimate planned expenditure, or unduly exploit escape clauses.

c. ***Similarly, fiscal councils can provide the unbiased inputs needed to implement more sophisticated numerical fiscal rules, such as structural balance rules.*** Ex-post assessments of compliance with the terms of such rules could also strengthen explicit enforcement procedures, including sanctions. Hence by promoting an implementation of smarter rules that is immune from short-term partisan pressures, a fiscal council would buttress the credibility and transparency of these rules and favor their broader adoption.

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[17] A political-economy variant of that argument is that a poorly informed public can encourage governments to opportunistically raise the deficit with a view to increase re-election chances (Debrun, 2011).

36. In addition, a fiscal rule also facilitates the council's work by providing an objective benchmark for its assessments. A numerical rule avoids dragging the council into the potentially contentious choice of its own benchmarks. Of course, the argument applies only if the rule leads to sensible deficit and trajectories in light of the council's ultimate objectives and the country's evolving economic situation.

C. New Fiscal Councils: What is Coming?

37. As the 2008–9 crisis will continue to cast a long shadow over the public finances of many countries, the need to restore fiscal credibility is likely to encourage reforms of fiscal frameworks. The recent surge of new fiscal councils has been part of an effort to improve budget preparation, implementation, and monitoring processes, most prominently in crisis countries such as Ireland (IMF, 2010) and Portugal (IMF, 2011a). In the United Kingdom, the OBR was presented as a tool to "restore confidence in public finances" (IMF, 2011b), while in Serbia, the fiscal council was integral part of new rule-based fiscal responsibility framework that the council is specifically tasked to oversee (IMF, 2011c). The reform of the EU fiscal architecture, which relies more heavily on national institutions, including independent oversight bodies, to foster compliance with the common fiscal rules, will accelerate the creation of fiscal councils. The growing interest in fiscal councils is not limited to Europe, as attested by the recent creation of parliamentary budget offices in Australia and South Africa.

38. The new fiscal councils are likely to remain highly diverse in terms of institutional format, reflecting country-specific traditions and capacities. Despite coordinated reforms of national fiscal frameworks in Europe, the new EU law can accommodate a broad spectrum of institutional models for independent oversight, including expanding the mandate of existing independent institutions. For instance in Finland, the mandate of the Supreme Audit Office has simply been expanded. In France, the fiscal council is explicitly paired with the Court of Audit (*Cour des Comptes*)—some members are shared by the two institutions—although the independence of the council is guaranteed by law. In both cases, the underlying motivation is to benefit immediately from the well-established reputation and independence of the host institution. Reliance on existing institutions could also be a practical response to capacity constraints hindering the creation of a stand-alone institution. In Cyprus, the authorities are considering a fiscal council that would outsource technical tasks to existing independent institutions depending on their respective areas of expertise. Table 2 illustrates the dispersion of new fiscal councils across the broad models discussed earlier.

Table 2. Institutional Models Adopted by New Fiscal Councils

Country	Year	Existing Institution	Parliamentary Budget Office	Under the Executive	Stand-alone Institution
Australia	2012		x		
Chile	2013			x	
Cyprus	ongoing	x			
Finland	2013	x			
France	2013	x			
Ireland	2011				x
Italy	2013		x		
Portugal	2011				x
Serbia	2011				x
Slovak Republic	2011				x
South Africa	ongoing		x		
United Kingdom	2011			x	

Source: IMF staff assessment.

39. **Emerging good practice could nevertheless foster a degree of convergence on some key features of the remit, tasks and some institutional arrangements.** In Europe, the new EU law governing national fiscal frameworks mandates specific tasks for national fiscal councils (see above). More broadly, accumulating evidence on the success or failure of fiscal councils to encourage better fiscal performance is leading to the emergence of a body of good practice. The OECD Principles for Independent Fiscal Institutions—based on case studies covering the Organization's membership—are the first attempt to codify broad guidelines.

THE EFFECTIVENESS OF FISCAL COUNCILS

40. **Given the limited formal evidence on the effectiveness of fiscal councils, this section contribute to the literature by combining a statistical analysis based on the new dataset and the lessons from selected case studies.** By the nature of its work, the effectiveness of a fiscal council is not directly measurable. Moreover, as for any statistical analysis of the potential impact of institutions on policies, reverse causation—the possibility that intrinsically disciplined countries reveal their deep preferences by adopting certain institutions—looms large. Case studies are therefore a useful complement that not only better reflects the great diversity characterizing the population of fiscal councils, but also allows for a more nuanced narrative than mere correlations. The cases have been selected to exploit the contrasting experience between new and older agencies, and between successful and less successful ones.

A. Statistical Analysis

41. Absent a single performance indicator, the analysis relies on broad correlations between the presence of a fiscal council (and some key specific features) and three indicators that would be associated with its effectiveness: fiscal performance (as measured by the level of the primary balance[18]), the media impact of the fiscal council (as measured by the number of quotes in the press), and the quality of budgetary forecasts (both in terms of bias and precision).

Fiscal Performance

42. As the existence of a fiscal council is often associated with a fiscal policy rule, it is essential to disentangle the potential impact of the council from the influence of a fiscal rule. The link between fiscal institutions (rules and councils) and fiscal performance is studied in the context of panel regressions estimated on a large sample of advanced and emerging economies. The regression approach allows taking into account other determinants of the primary balance, such as the output gap and the level of the public debt (see Appendix I). The potential impact of fiscal councils is tested via binary variables (0-1) identifying observations (in time and across countries) associated with a fiscal council in general or with a council that exhibits only certain characteristics. For fiscal rules, an index building on the dataset compiled by Schaechter and others (2012) is used. The index is constructed to measure the extent to which the rule shows features expected to constrain the financial position of the general government (e.g. a constitutional basis).

43. The econometric analysis suggests that certain characteristics of fiscal councils are associated with stronger fiscal performance, but that the mere existence of a council is not. (See Appendix I.) On average, and taking into account the impact of fiscal rules and other determinants of fiscal behavior, having a fiscal council as such appears only loosely related to stronger fiscal outcomes: the (conditional) correlation is positive but not statistically significant (see Figure 8). By contrast, significantly higher primary balances are associated with fiscal councils featuring certain characteristics. Note that because fiscal councils generally combine several of these features, this simple regression analysis does not identify "sufficient conditions" for effectiveness. For instance, the task of monitoring compliance with fiscal rules (point b) is unlikely to be sufficient to impact fiscal performance if it is not paired with strict independence and a presence in the public debate.

a. ***Legal and/or operational independence.*** This result is particularly strong if one considers countries providing legal guarantees on the independence of their councils, and those allowing for a staff commensurate to the tasks of the council—an important element of

[18] The primary balance is the standard measure of fiscal outcomes in regression-based analyses of fiscal policy (Bohn, 1998). Further analysis could usefully look at other indicators, including deviations from pre-announced commitments.

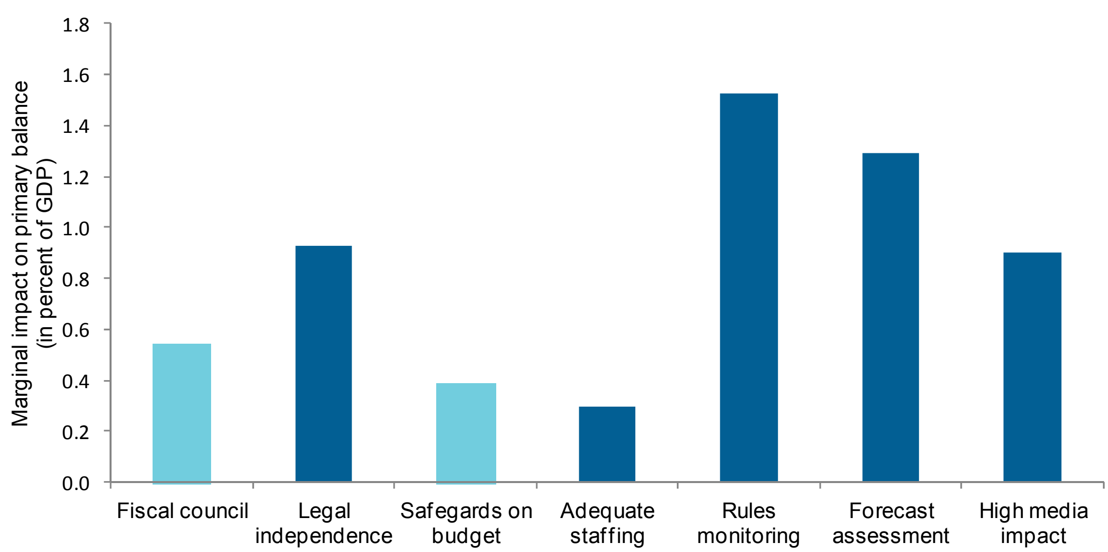
operational independence. While it was argued earlier that explicit safeguards on funding were useful to avoid retaliatory cuts, this feature alone does not seem to characterize the most effective councils in the sample.

b. ***Monitoring compliance with fiscal rules.*** The positive and quantitatively large effect seemingly associated with such fiscal councils is consistent with the likely beneficial combination of the two types of arrangements. That said, the strength of that potential complementarity could not be directly estimated.[19]

c. ***Assessing or producing forecasts.*** This result is arguably linked to the previous one, as overoptimistic forecasts are often a way for governments to escape to the strictures of numerical fiscal rules (Frankel and Schreger, 2013). Although this only increases ex-ante compliance with the numerical targets, the cost of non-compliance ex-post is generally low given the weak enforcement mechanism characterizing many fiscal rules.

d. ***Strong media presence.*** This result is consistent with the fact that the effectiveness of a fiscal council hinges importantly on the reputational and electoral impact of its analysis for policymakers.

Figure 8. Fiscal Councils and Fiscal Performance

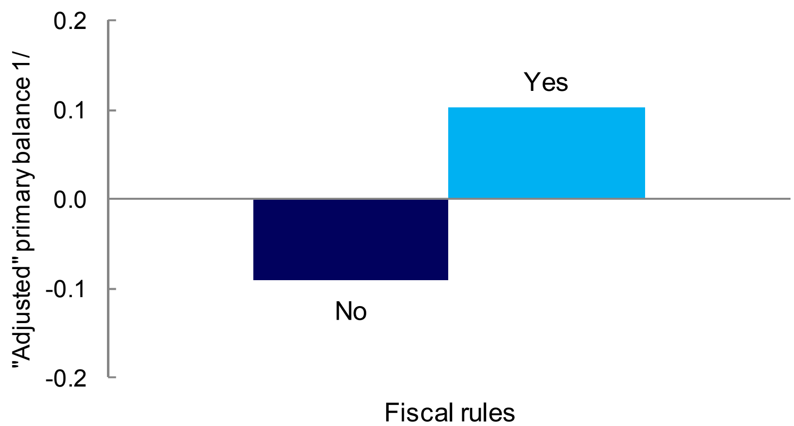


Source: IMF staff estimates (Appendix I).
Note: light-colored bars indicate that the estimated marginal impact of the binary variable is not statistically different from zero.

[19] In technical terms, the introduction of an interaction term between the fiscal council variable and the fiscal rule index did not yield meaningful results.

44. In addition to the existence of fiscal councils with certain characteristics, fiscal rules are also associated with higher primary balances, reinforcing the earlier suggestion that rules and councils could each contribute in their own right to fiscal performance. On top of the positive association between key characteristics of fiscal councils and fiscal performance, fiscal rules designed to be more binding—i.e. greater values of the fiscal rule index—are positively associated with primary balances (Figure 9). This result echoes Fabrizio and Mody (2006) and Debrun and others (2008) who also found positive relationships between their respective fiscal rule index and fiscal outcomes in much smaller samples of European Union countries. This suggests that fiscal discipline might be better served by a combination of a council and a rule rather than by any one of them in isolation.

Figure 9. Fiscal Rules and Fiscal Performance



Source: IMF staff estimates
1/ The chart illustrates the *conditional* correlation between the primary balance and the fiscal rules index based on the regression analysis in Appendix I. The "adjusted" primary balance takes into account all the other determinants of the primary balance included in the regression, in particular the output gap, the debt level, and the existence of a fiscal council.

The Media Channel

45. Evidence that a high media presence of the council tends to be associated with stronger fiscal performance calls for further analysis of that channel of influence. Two main questions arise. First, is there any evidence that certain features of the fiscal framework—including the council itself—favor a strong media presence? Second, does a fiscal council communicate when it should? The rationale for the second question is that an effective communication strategy aims at minimizing the noise-to-signal ratio, implying that a fiscal council would be expected to avoid issuing frequent press statements about any random event likely to affect the budget. The variable used to assess the council's media presence is a standardized and filtered count of references to the fiscal council in newspapers. Filters include the need for the reference to be associated with a number of keywords referring to fiscal policy in the same press article (see Appendix II).

46. Despite a more limited sample and the noise inherent to data on media counts, a number of interesting correlations and tentative conclusions emerge.

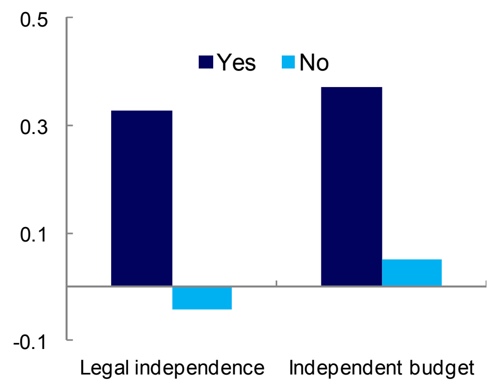
a. ***Independent fiscal councils appear more likely to influence the public debate on fiscal policy.*** The councils deemed independent in the Fiscal Council Dataset have on average a higher media presence score than the others (Figure 10). This suggests that the credibility of the council as a non-partisan watchdog is an important condition for its views to be reflected in the public debate. This result is consistent with earlier econometric evidence on fiscal performance and provides an indication that the media would be an effective vehicle of the council's influence.

b. ***Fiscal councils operating in countries where fiscal rules are designed to be more binding tend to be more present in the press.*** (See Figure 10.) Although subject to clear statistical caveats (small sample and role of outliers), this result echoes earlier econometric evidence suggesting a quantitatively and statistically stronger association between fiscal outcomes and councils when those have a large media presence. It could also indicate that fiscal rules can facilitate the council's work and communication by providing a simple benchmark against which plans and policies can be assessed.

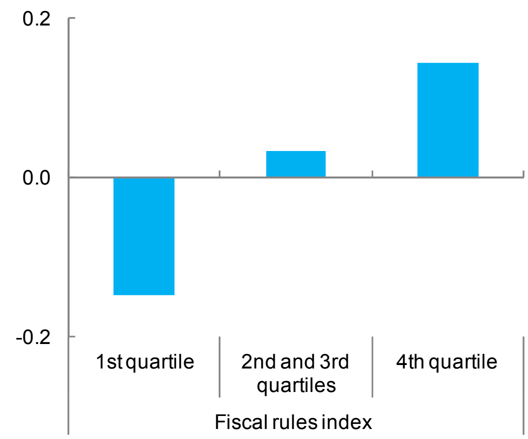
c. ***Evidence pertaining to the focus of fiscal councils' interventions is less convincing.*** Working on a smaller sample of mature European fiscal councils and two case studies, Debrun, Gérard and Harris (2012) found that fiscal councils tended to be more vocal in the press when significant fiscal developments were taking place—large slippages or announced changes in the fiscal stance—and around the most important steps of the budget process. This is less clear for the overall population of councils gathered in this paper's dataset, which exhibits only a weak positive correlation between the planned change in the overall fiscal balance and media presence (Figure 11). Several case studies discussed in the next sub-section nevertheless shed a more positive light on the focus of council's communication

Figure 10. Determinants of Media Presence

Independence of the fiscal council



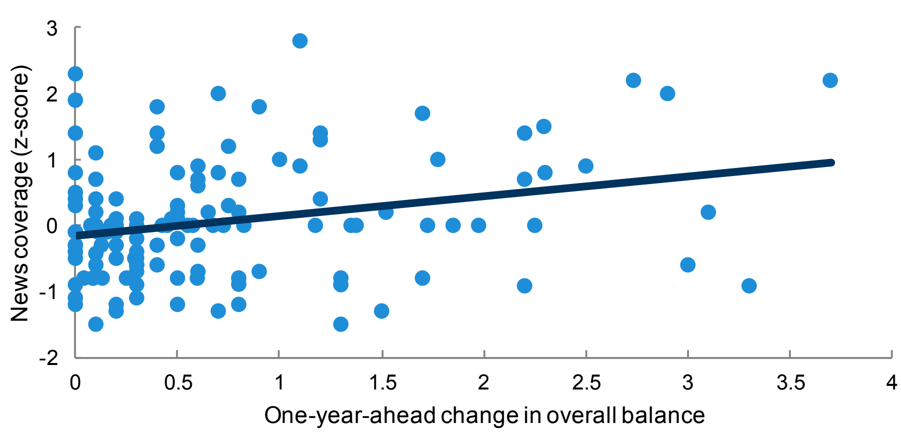
Fiscal rule index



Source: IMF staff estimates.

Note: Vertical axes measure for each group the average z-score of the number of media reports quoting the fiscal council along with relevant fiscal concepts (e.g. fiscal balance, deficit, public debt).

Figure 11. Media Presence and Large Planned Policy Changes



Source: IMF staff estimates.

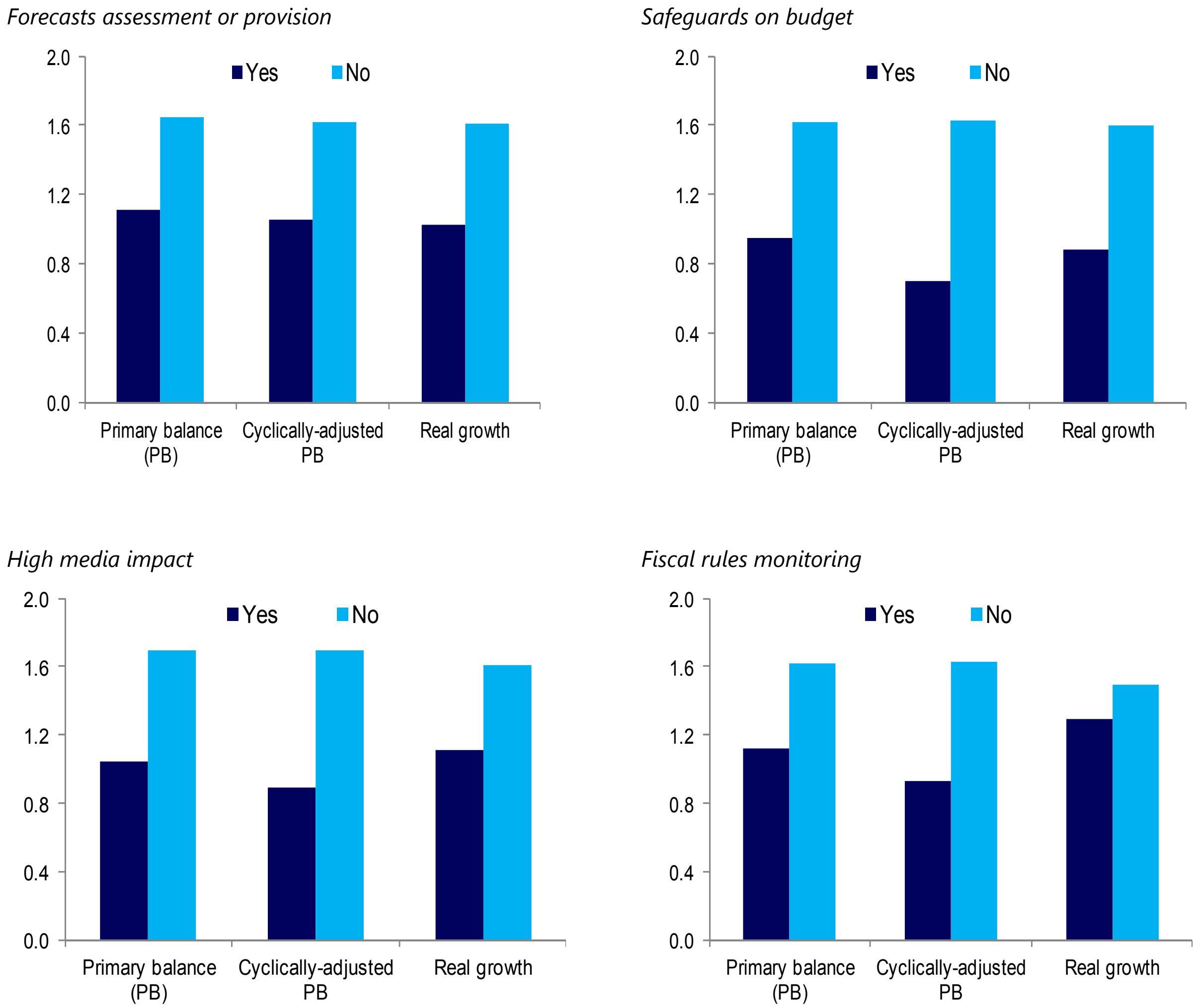
Fiscal Councils and Forecasting

47. As expected from earlier discussion, countries with fiscal councils tend to have more accurate and less optimistic macroeconomic and budgetary forecasts than others. This is particularly the case if the council has some of the main features seemingly associated with effectiveness (independence and high media impact) or if it is mandated to assess or produce forecasts and to monitor compliance with fiscal rules. This suggests that the potential impact of a fiscal council on fiscal performance could also operate through its capacity to avoid that governments use overoptimistic forecasts to deceive parliamentary oversight or circumvent fiscal policy rules.

48. Precision and bias are measured for 3 key variables: the primary balance, the cyclically-adjusted primary balance, and real GDP growth. A thorough discussion of the underlying econometric evidence—which expands the work of Jonung and Larch (2006) and Frankel and Schreger (2013)—is provided in Appendix II. ***Greater precision*** is evident from Figure 12 where the absolute forecast errors for all 3 variables are systematically lower in countries with a fiscal council featuring one of the 4 selected characteristics. Likewise, Figure 13 shows that fiscal councils contribute to ***unbiased*** or slightly conservative forecasts for primary balances, while other countries have overoptimistic projections on average. Interestingly, real growth forecasts remain overoptimistic,[20] suggesting that the presence of a fiscal council tend to encourage more conservative budgetary forecasts only. This may reflect the fact that manipulations of basic macroeconomic forecasts tend to be more easily detected given the many alternative sources providing similar forecasts. By contrast, estimating the budgetary impact of economic activity is technically more involved and offers more opportunities for manipulation. This result could also be related to the potential impact of the council's presence on fiscal behavior itself, as greater transparency reduces incentives to deviate from ex-ante targets.

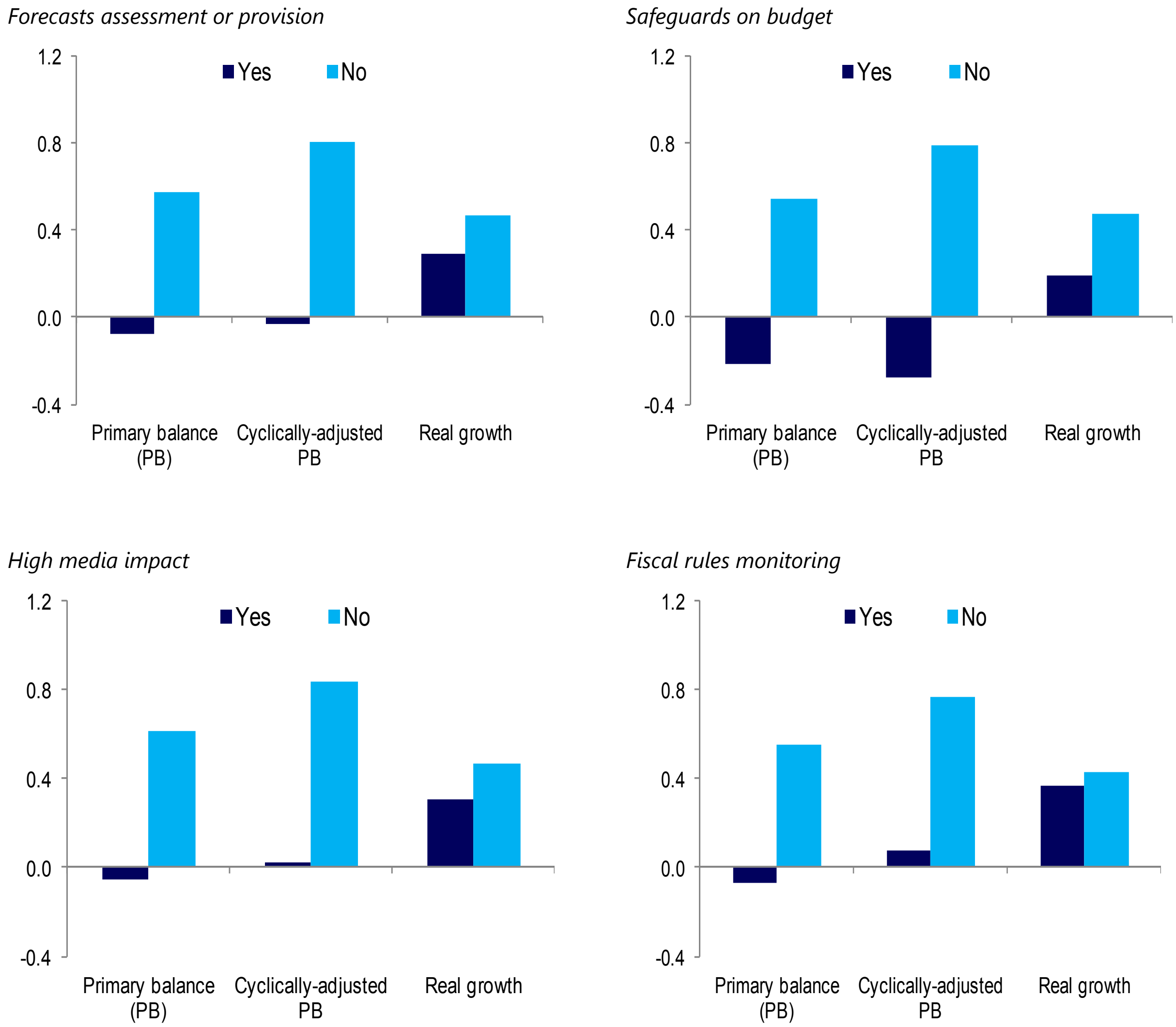
[20] The smallest bias is observed in countries with formally independent councils.

Figure 12. Absolute Forecast Error and Selected Fiscal Councils' Characteristics



Source: IMF staff estimates.

Figure 13. Mean Forecast Error and Selected Fiscal Councils' Characteristics



Source: IMF staff estimates.

Note: The forecast error is defined as the forecast minus the actual value so that a positive number for the mean error indicates an optimistic forecast.

B. Findings and Lessons from Case Studies

49. Case studies are used to identify design and operational features that can contribute to successful outcomes and those that could be avoided to prevent failure. To provide guidance for establishing new councils, this section draws general lessons from the experiences of seven fiscal councils: Belgium (Conseil Supérieur des Finances—HCF), Canada (Parliamentary Budget Officer—PBO), Hungary (Költségvetési Tanács), Korea (National Assembly Budget Office—NABO), Netherlands (Centraal Planbureau—CPB), Sweden (Finanspolitiska rådet), and the United States (Congressional Budget Office-CBO). These institutions have been selected based on the following criteria: length of operation (at least three years); functions performed (at least two of the three core functions) and diverse regional and contextual environments. The case studies cover three regions Asia, Europe, and Western Hemisphere and incorporate a variety of political systems. Each case study in the Supplement to this paper examines how the council performs its core functions and if and how the fiscal council impacts the fiscal policy debate.

Designing Effective Fiscal Councils

50. Each institution's design needs to be adjusted to country-specific legal and political contexts and traditions. While the United States' CBO has served as a model for other fiscal councils (Korea, Mexico, Canada and Hungary), in each case countries have sought to adjust the model to their particular system with different degrees of success. In Korea and Mexico, the PBOs are well established. In Hungary and to a lesser extent Canada, the councils faced challenges to their independence. In Canada's case these issues reflect the difficulty of transposing the CBO model to a parliamentary system of government.

51. One size does not fit all. The impetus for creating fiscal councils varies across countries. The initial conditions leading to the establishment of a fiscal council determine its remit, the initial focus of its work, and how its performance and effectiveness are judged by politicians and the public. Although the theoretical literature focuses on establishing fiscal councils to address the roots of excessive deficits and debts, in practice, councils are created for a broad range of reasons which are both political and economic in nature. While a number of newer fiscal councils were established in reaction to an acute economic crisis, several others emerged as part of wider reforms aimed at addressing political issues. The countries with presidential systems (Korea and the United States) have established their council in a context of strengthening legislative oversight of the executive by providing expertise on fiscal issues.[21] In the United Kingdom, the main motivation was to improve forecasts, and in Australia, to cost the electoral proposals of the government and the opposition political parties. As the experience of older fiscal councils demonstrates, however, the initial remit can evolve over time as councils gain new tasks.

52. For new councils, a strong legal basis for independence is important to give them time to become established and build reputational capital. The two oldest councils, the Belgian High Council of Finance (HCF) and the Dutch Bureau for Economic Analysis (CPB) have no or limited legal guarantees of independence, but in practice they have operated independently for decades and build up a reputation for good quality non-partisan analysis. Newer councils—for example Sweden and Canada—benefitted from a strong legal basis for independence. As the case of Canada illustrates, ambiguities in the mandate, guarantees of independence or relationship with the political principal must be avoided.

53. Political interference is not uncommon. In case of conflicts between the government (or the legislature) and the fiscal council, politicians have not hesitated to curtail independence. This has been done by cutting the council's resources, controlling its work program, delaying

[21] Note that the same initial conditions apply to the Mexican Centre for Public Finances.

appointments of members, or changing its size and mandate altogether.[22] The most egregious example is the Hungarian fiscal council, which in its second year of existence, had its mandate restricted and staff virtually eliminated. The Belgium HCF experienced a two year delay in the appointment of key members after its recommendations were at odds with government's objectives. Canada and Sweden also faced threats to their budget after being critical of government policies.

Resources and Remit

54. Resources commensurate to the remit and tasks of the fiscal councils are essential for its effectiveness. The various tasks of a fiscal council have very different resourcing requirements. In Sweden, fiscal policy assessments have been performed by a staff of 5 at the overall cost of about USD 1 million (including the outsourcing of some background studies). At the other end of the spectrum, policy costing is the most resource intensive and time consuming activity requiring a larger and highly specialized staff. In the US, the CBO has a staff of 240, and a budget of USD 45 million to prepare costing of legislative proposals in addition to fiscal policy analysis, forecasts and long-term sustainability assessments.

55. Although it is difficult to formulate specific guidance on the optimal size of a fiscal council, some broad principles can be outlined. The quantitative ranges given below are for professional staff experienced enough to garner the respect of other experts and commentators of fiscal issues within the relevant country (Figure 14). These ranges are purely based on experience with existing fiscal councils and could vary substantially with the size and complexity of the government system and the institutional coverage of the council's activities.

- Undertaking an assessment of fiscal policy, including compliance with fiscal rules, demands relatively few resources, say 2 to 10 full-time professionals.

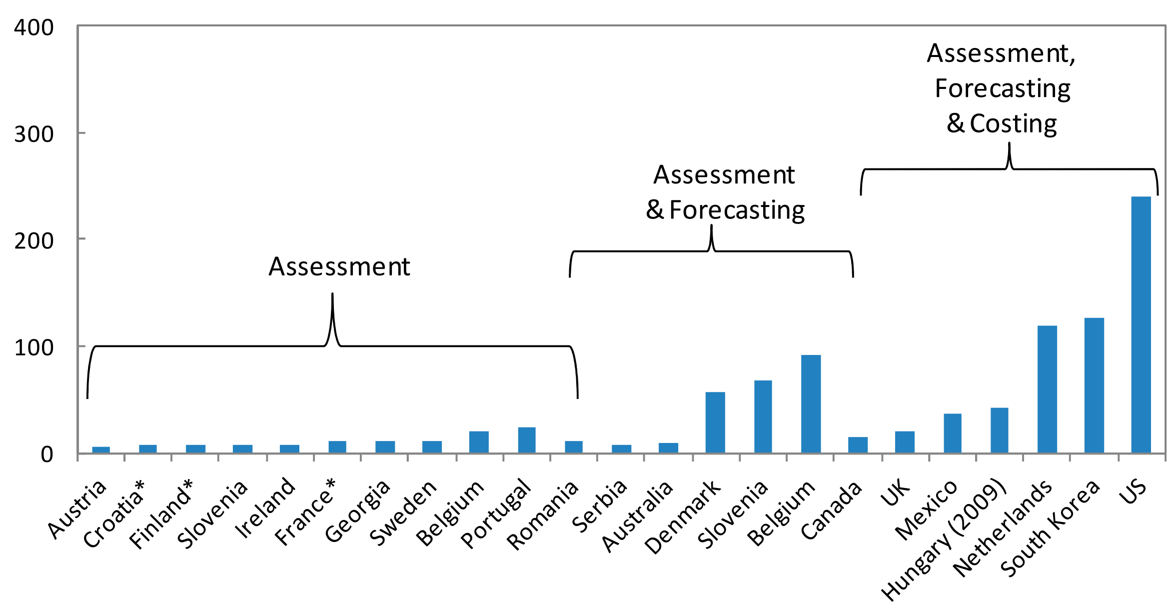
- Similarly, assessing economic and fiscal forecasts can be done with a relatively small resource base by comparing the government's forecasts to those of other high quality institutions. Moreover, simple forecasting tools are sufficient to raise alarms when the government's budgetary forecasts seem out of line without obvious reasons.

- As the remit is extended to producing independent economic and fiscal forecasts, the resourcing requirements increase significantly, as more sophisticated models and specific expertise—e.g. on certain tax issues—are needed. Although much depends on the extent to which the council can rely on outside expertise (central bank or ministry), experience suggest that fiscal councils involved in forecasting operate at the minimum over 20 professional staff.

[22] In Belgium, the Netherlands and Sweden the budget is part of the Ministries of Finance budget. In Korea, Canada and the United States, the council's budget is part of the legislature's budget.

- Finally, policy costing is the most resource intensive and time consuming remit requiring a larger staff base, with an expertise in revenue and expenditure policies, combined with access to data and models that have often taken decades to develop within ministries of finance. To the extent that strong guarantees of independence exist, these resourcing needs can be reduced through data and model sharing agreements with the government agencies which traditionally perform these roles for the government (Australia).

Figure 14. Number of FTE Staff and Functions



Sources: IMF Fiscal Council Dataset.

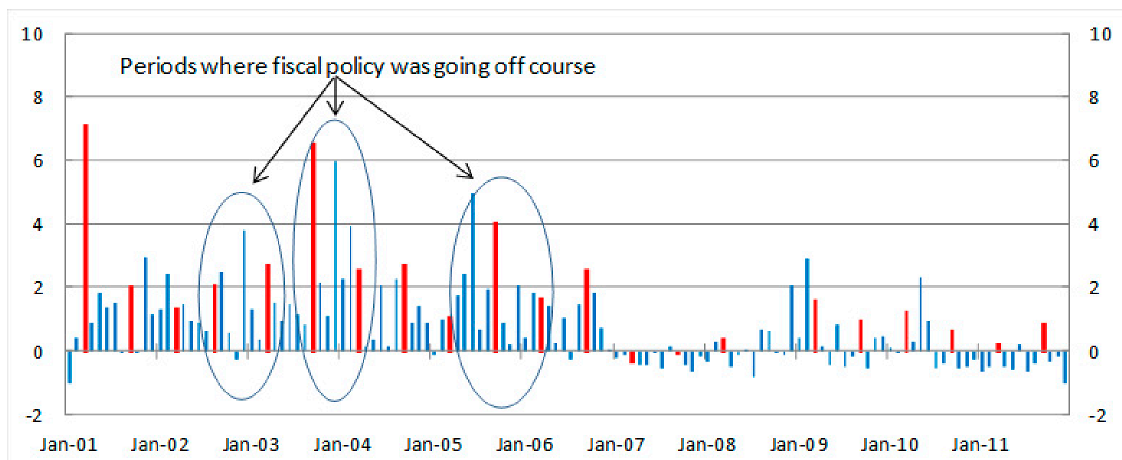
Operational Lessons

56. To remain effective across political cycles, fiscal councils need to actively develop their non-partisan credentials. Political support across party lines for the creation of the council clearly reduces the risk of subsequent partisan threats. In Hungary, the reform of the council in 2010 could be related in part to the lack of strong bi-partisan support for the 2008 fiscal responsibility law, which established the council. Similarly the creation of the Swedish council was not supported by the opposition parties, who feared it would be a mouth piece of the government. However, the Council quickly established its independence through normative analysis critical of the government. The Dutch CPB and the United States' CBO have instead sought to avoid normative analysis. In the case of the CBO, this neutral position helped build a reputation of non-partisanship, which has been critical to its survival and impact.

Assessment of Fiscal Policy

57. For fiscal councils to influence the policy debate it is important to have a strong media presence to communicate their assessment of government's fiscal policy to the public. This is particularly important when fiscal councils need to raise the alarm as when proposed budgets are not in line with stated objectives, when forecasts are over-optimistic and unlikely to be realized, when unsustainable spending or tax policies are being debated, or when the fiscal outturns are coming out significantly worse than projected. By identifying such episodes, and mapping them against the volume of media reporting of the findings of the council, it is possible to get a sense of the effectiveness of the council's communication with the public. The Dutch experience through the 2000s provides a good example of effective communication, with the council increasing its public activity, as evidenced by spikes in media reports, at the specific points of time where fiscal policy was going off course (Figure 15).

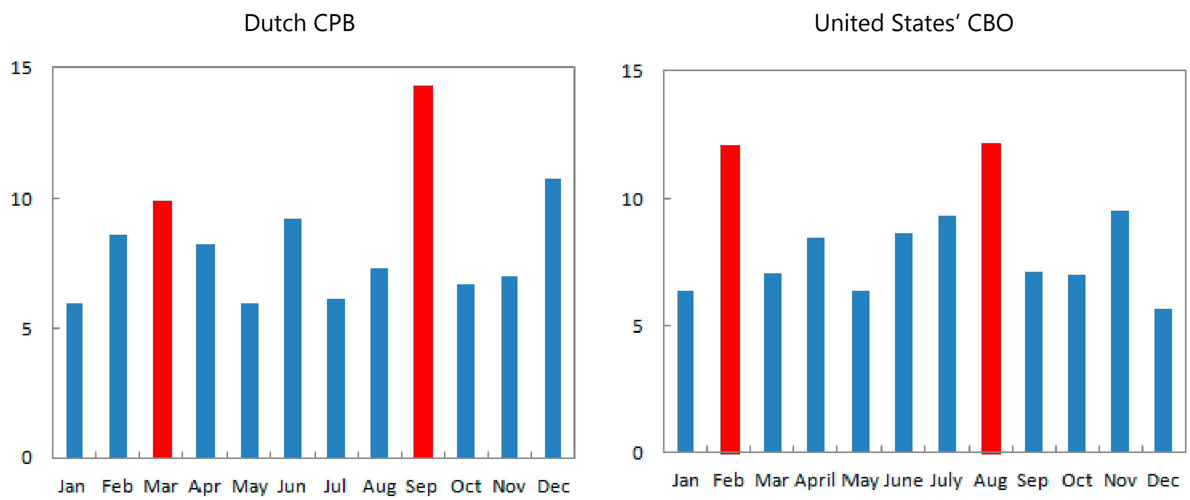
Figure 15. Media Reports of the Dutch CPB
(Number of media articles relative to 4-year rolling average)



Sources: Factiva and IMF staff calculations.

58. While fiscal councils should have a steady media presence, it is important to ensure that key messages on fiscal policy are focused and provided when they matter most during the budget process. If media interventions focus on topics outside of the council's immediate remit and become too numerous, this can reduce the power of their messages when fiscal policy is actually veering away from stated goals. The Dutch CPB is an example of an effective approach. Its interventions systematically take place around the release of its most extensive reports, in March and September—key points in the framing and passage of the budget (Figure 16). Similarly, the CBO's interventions are focused around press briefings twice a year in February and August, when the budget and economic outlook updates are released. The director and staff of the CBO are also easily accessible for journalists, providing background briefings to ensure that they understand the work.

Figure 16. Average Seasonal Pattern of Media Reports



Sources: Factiva and IMF staff calculations.

59. Councils tend to have a stronger impact when combined with a political and public consensus on sound public finances. In Sweden and Canada, there is a public consensus on the need for sound public finances, a legacy from their experiences of economic crises in the 1990s. Politicians are aware of the electoral risks of running deficits and emphasize balancing the budget. A similar consensus exists in the Netherlands. This has the advantage that when the councils raise the alarm, the media are more likely to pay attention. In contrast, when fiscal discipline is not well-anchored in electoral preferences, the task of the council is more difficult. In Belgium, the recommendations of the High Council of Finance had a major influence over fiscal policy when politicians focused on the fiscal convergence criteria to enter the euro area in 1999. That influence dramatically weakened in the immediate post euro era, culminating in open conflict with the government.

60. Clear benchmarks that fiscal performance can be judged against increase the traction of the council. These benchmarks often emanate from a fiscal rule, such as the Swedish expenditure ceilings or the SGP deficit ceilings, or other public commitments such as the deficit ceilings that are part of Dutch coalition agreements. Rules reduce the risk for the council of being perceived as partisan. Without such benchmarks, the council may find it difficult to leverage its positive analysis. In the United States, the absence of medium-term political commitments on fiscal outcomes along with other factors has limited the CBO's capacity to influence politicians to constrain deficits (Hemming and Joyce 2013).

Forecasting

61. **Case studies generally support the econometric findings that fiscal councils have more accurate forecasts, albeit with some cross-country variations.** In the US, both the CBO and the Administration have a long track-record of preparing economic and fiscal forecasts. For the two-year ahead forecasts of real GDP, the CBO has a slightly pessimistic bias, compared to a slightly optimistic bias for the administration, with the CBO's forecasts proving only marginally more accurate. That said, the degree of optimism in the Administration's forecasts is relatively small compared to other advanced economies, and is largely limited to the early 1980s. Over a longer-term forecasting horizon, the administration's bias is slightly more pronounced, but comparable to the bias in CBO or Consensus forecast (Table 3). Of course, the very presence of the CBO forecasts may have a disciplining effect against bias in the Administration own forecasts, though the revenue forecasts in the pre-CBO period didn't appear to have any major bias.

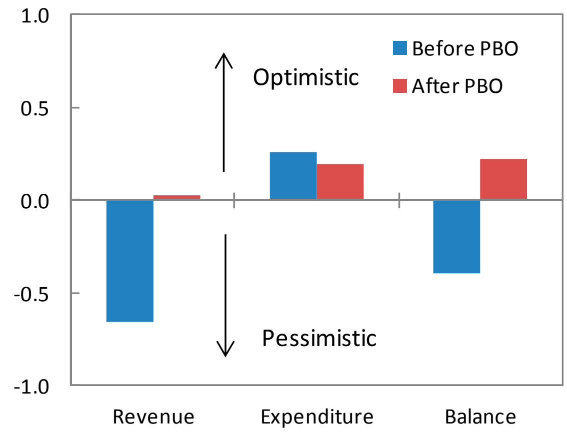
Table 3. United States: CBO and Administration Real GDP Forecast (1982-2010)

	Real GDP Forecast Error			
	Average		Absolute Error	
	2-year	5-year	2-year	5-year
CBO	-0.1	0.1	1.1	0.9
OMB	0.1	0.3	1.2	1
Blue Chip Consensus	-0.1	0	1.1	0.9

Sources: CBO, 2013, CBO's Economic Forecasting Record: 2013 Update, January 2013.

62. **The quality of government forecasts improved after the establishment of fiscal councils in Canada and Sweden.** Interestingly though, both countries exhibited a pessimistic bias in the government's forecasts prior to the council's introduction. Beginning in 2008, the Canadian PBO began producing its own economic and fiscal forecasts that immediately disciplined the government's forecasting exercise, with forecasts becoming more accurate and less pessimistic (Figure 17). Over a similarly short period of time, a move from overly pessimistic fiscal balance forecasts (average bias of 1.6 percent of GDP pre-council) to a small optimistic bias of 0.2 percent followed the introduction of the Swedish Fiscal policy Council.

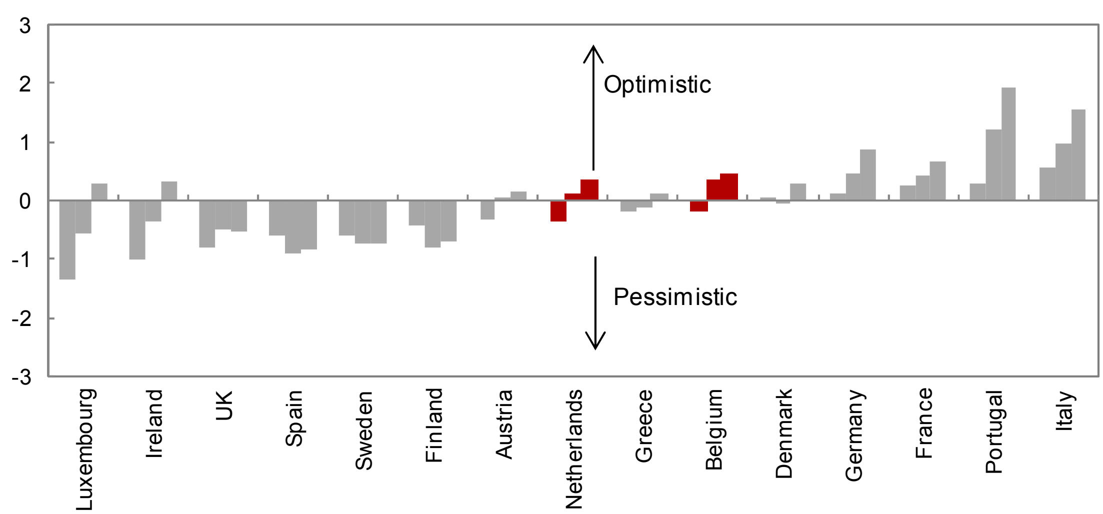
Figure 17. Canadian Government's fiscal forecast errors 2000-2010 (Percent of GDP)



Sources: Canadian budget, PBO and staff calculations.

63. The independent macroeconomic forecasts from the Belgian and Dutch fiscal councils in general have been more accurate than elsewhere in the European Union. Over the ten years prior to the crisis, there was a small pessimistic error in real GDP forecasts on average in the short term, with a slightly optimistic error as the forecast horizon extended. These average errors were relatively low compared to other European countries, although it must be noted that they were matched by countries with no fiscal council (Figure 18).

Figure 18. EU Average Real GDP Forecasting Error 1998-2007 (percent of GDP)



Sources : European Commission (SCPs) and authors' calculations.

Costing Policies

64. In a number of countries, independent costing of policy proposals and programs actively contribute to the public policy debate, improving transparency, and curbing governments' tendency to underplay the full cost of their policies. In Canada, the PBO's costing generated a public debate about the affordability and approach to different policies. In the United States, the CBO focuses on costing or scoring legislative proposals relative to the baseline. This has helped discourage Congress from making unaffordable proposals, especially when the PAYGO rule was enforced. Several commentators have argued that it is through its costing function that the CBO has been most influential and effective.[23] In the Netherlands and Australia, fiscal councils form a key part of the election debate because they cost different political parties electoral platforms. This can discourage unaffordable election commitments.

POLICY CONSIDERATIONS

65. While the need for a fiscal council and the order of priority of such a reform should be assessed on a case-by-case basis, the analysis in this paper points to useful policy implications for those countries that decide to set up such an institution. The underlying objective shaping the normative messages gathered in this section is to set up fiscal councils—or reform existing ones—that effectively contribute to the formulation and execution of more sustainable and stabilizing fiscal policies.

A. Pre-requisites and Enabling Factors

66. Solid Public Financial Management (PFM) systems and good statistical governance are key to the effectiveness of fiscal councils. PFM procedures and the availability of reliable data with adequate institutional coverage both play a critical role in translating policymakers' objectives into implementable policy plans and in properly executing those plans. Major dysfunctions at these levels would disrupt the transmission between the council's tasks and fiscal performance. However, even where only poor PFM processes and data systems are in place, a fiscal council could foster needed reforms, by monitoring budget execution, preparing high-quality reports with broad institutional coverage, and improving forecasts. Of course, the creation of a fiscal council should come as part of a well-sequenced PFM strategy, and in some cases, other reforms—such as a stronger budget execution system—may need to receive higher priority.

67. The effectiveness of fiscal council is not tied to narrow institutional models or specific economic environments. A fiscal council can play a useful role in fairly diverse governance systems, although the effectiveness of certain transmission channels such as democratic accountability are by nature contingent on specific institutional factors, including the mode of election of people's representatives and the role of the legislative branch in the budget

[23] Hemming and Joyce (2013) and Joyce (2011)

process. However, the usefulness of a fiscal council that fosters transparency, promotes a culture of macroeconomic stability, and provides a neutral input to the budget process—forecasts, certain recommendations, etc.—is in principle not limited to any specific political system. Severe limitations on resources and capacities can be met by establishing very lean bodies outsourcing most of the background technical and analytical work to other independent institutions or professionals.

B. Remit and Tasks

68. The remit should be broad, clearly defined, and implementable. Specifically, particular tasks assigned to council should be fully consistent with the remit, and the council should have the freedom to determine its work agenda within that remit. A broad mandate is useful to address the multiple and possibly changing sources and manifestations of the deficit bias. At a minimum, a fiscal council should have a monitoring role, involving the typical tasks of a watchdog: ex-ante assessment of the consistency between fiscal plans and the stated objectives of the government (including commitments to adhere to certain numerical targets or limits), an analysis of long-term sustainability (including medium to long-term risks), and an ex-post evaluation of fiscal performance against official aggregate objectives and targets. The freedom for the council to determine its own work agenda is essential to avoid undue constrains on that monitoring role. In addition, a fiscal council should be mandated to perform tasks aimed at addressing specific sources of deficit bias. Table 4 below formally maps potential causes of deficit bias into specific tasks that could be assigned to the council to encourage stronger policies.

Table 4. Mapping the Sources of Excessive Deficits into Tasks of a Fiscal Council

	Causes and manifestations of the deficit bias	Tasks of the fiscal council
Policymakers	Myopia, re-election concerns, partisanship: overoptimistic revenue forecast, unrealistic spending estimates, efforts to circumvent fiscal rules (creative accounting).	Produce unbiased macro-fiscal forecasts or at least assess official forecasts; analysis of short and long-term implications of current policies, costing fiscal measures; monitoring of compliance with fiscal rules, report on government statistics integrity.
	Time inconsistency (policies that were agreed to ex ante are not adhered to ex post)	Examine fiscal outcomes in light of government commitments; monitor compliance with fiscal rules.
	Common pool problem between line ministries (at the central government level) and/or between different government levels	Analysis covers the general government. Issue public recommendations (strengthening centralization of the budget; coordinating fiscal policy among government entities to avoid soft budget constraints).
	Imperfect information: underestimation of risks and costs, overoptimistic views on growth, misperception of the government's budget constraint (notably in cases of abundant commodity revenues), lack of timely data.	Analysis of complex issues such as fiscal sustainability, intergenerational equity and fiscal risk analysis; assessments of long term trends, and possibly recommendations on appropriate of fiscal policy.
	Asymmetric information (lack of transparency); insufficient background analysis and information received by the legislative power (weakened accountability)	Report on a regular basis to Parliament and provide responses to questions; contribute to legislative debate on fiscal matters
Voters	Imperfect information: misperception of the government's budget constraint.	Provide unbiased assessment of medium and long-term sustainability; raise public awareness on fiscal issues.
	Neglect for future generations and impatience	Impact analysis of unsustainable policy paths and costs of adjusting to the intertemporal budget constraint.

Source: IMF staff assessment.

69. **By virtue of its non-partisan nature, a fiscal council is expected to confine its work to positive analysis and technical work, although normative statements and recommendations could be envisaged in specific contexts.** Normative analysis and recommendations raise the risk of open conflicts between the council and the government and may undermine the public perception of neutrality and non-partisanship. The result could be reduced legitimacy—and a corresponding loss of influence on the public debate—and a stronger temptation for the government to put pressure on the fiscal council. Councils are vulnerable to such pressures because they depend on budget appropriations and they do not perform policy tasks. Budgets can be cut and mandates put in abeyance or changed without immediate costs for policymakers. That said, there are political contexts and policy areas where policymakers might welcome non-partisan recommendations as a basis for consensus. Consensual decision-making may result either from the broad political culture of a country, or from necessity, such as the need to forge a broad-based agreement on contentious distributive issues. In these cases, recommendations could usefully reduce negotiation costs. It remains that a broad mandate to

make recommendations on any aspect of fiscal policy should always be considered with caution given the implied risks to the council's independence.

70. Countries with rules-based frameworks should specify the remit and tasks of their fiscal councils so as to maximize compliance with the rules. A well-designed rules-based fiscal framework facilitates monitoring and communication to the public. In turn, where a rules-based framework is in place, a fiscal council can foster compliance through various activities, such as producing unbiased forecasts, verifying the conditions under which an escape clause or a correction mechanism should be activated, estimating targets expressed in structural terms. Synergies between rules and council are reflected in recent EU-wide requirements for "independent bodies" at the national level (Box 2).[24]

Box 2. EU requirements for "Independent Bodies"

Independent bodies should monitor compliance with fiscal rules. Several European legislative acts require that fiscal rules be monitored by "independent bodies," including fiscal councils. According to the Council Directive on budgetary frameworks of November 2011, "independent bodies or bodies endowed with functional autonomy vis-à-vis the fiscal authorities of the Member States" should carry out "the effective and timely monitoring of compliance with the rules" (Chapter IV, Article 6b). This obligation was reaffirmed by the Treaty on Stability, Coordination, and Governance (TSCG) (Title 3, Article 3.2) without being further spelled out. This Directive entered into force in November 2011 as part of the "the six-pack" and applies to all EU27 member states.

An independent body should have an advisory role in the activation of the correction mechanism and escape clauses. The regulations forming the two-pack provide additional details about the role of the council in case of "significant deviation from the medium-term objective or the adjustment path towards it."[25] In particular, the council should advise on the activation and operation of the correction mechanism, and provide an assessment about the circumstances allowing temporary deviations from targets (Chapter II, Article 4).

An independent body should ensure that budget plans are based on unbiased macroeconomic projections. The two-pack specifically requires that "independent macroeconomic forecasts" be "produced or endorsed" by "independent bodies" in the context of the budget preparation (Chapter I, Article 2.1.2). FCs can indeed address the tendency in some finance ministries to produce over-optimistic macro forecasts either by providing unbiased forecasts themselves or by exposing the bias to the public.

EU law leaves ample flexibility regarding the institutional format of the independent bodies. In particular, the two-pack stipulates that "given the diversity of possible and existing arrangements, while not the preferred option, it should be permitted to have more than one independent body in charge of monitoring compliance with the rules, as long as there is a clear allocation of responsibility and as long as there is no overlap of competencies over specific aspects of the monitoring. Excessive institutional fragmentation of monitoring tasks should be avoided" (Article 7 of the preamble).

[24] The notion of "independent bodies" does not necessarily refer to a fiscal council, as these tasks could as well be performed by an existing independent institution, such as the audit court or office.

[25] The two-pack regulations only apply to euro-area Member States, while the Treaty only binds its 25 signatories.

71. A fiscal council should not be given veto right on the budget or receive any specific policy prerogative. As discussed earlier, the delegation of fiscal powers is neither desirable nor credible. It is not desirable because all aspects of fiscal policy—including the deficit—are distributive in nature. And it is unlikely to be credible because the government would probably perceive little or no ex-ante benefit to let an independent council decide on the total amount it can spend (Debrun, 2011).

72. In a federal or highly decentralized setting, fiscal councils should cover the general government, monitor sub-national entities, and contribute to the coordination of fiscal policy within the general government. A high degree of decentralization raises coordination and common-pool issues that a fiscal council could contribute to alleviate. Although the reach of the council may be constrained by the basic design of intergovernmental arrangements, neutral analyses of intergovernmental transfers and even recommendations on complex distributive issues—including the sharing of fiscal effort to reach general government targets—could facilitate cooperation among entities. Such cooperation is critical to improve compliance with fiscal policy rules applying to the general government.

73. In resource-rich countries, fiscal councils could help chart a financially sustainable and inter-generationally equitable expenditure path. By limiting political manipulations of commodity price-cycles and estimated reserves of non-renewable resources, a fiscal council can alleviate immediate spending pressures fueled by cyclical peaks in prices or overoptimistic assessments of medium-term revenue paths. One option is to devise a "second-generation" fiscal rule explicitly incorporating these parameters and task to fiscal council to produce them.

74. In performing its tasks, a fiscal council should be mindful of quickly establishing an effective communication strategy. This ranges from the format of its publications (concise and readable reports, simple "chartbooks" laying out key issues, well-designed website) to the diversity of its communication channels (press events around the publication of key reports, focused communiqués, and a solid informal network in the press and among policymakers).

C. Independence

75. Strict guarantees against political interference are essential, especially for new institutions. Indeed, the latter cannot benefit from prior reputation and public support in case of open conflict with the government, and for those councils expected to make recommendations or issue opinions on sensitive matters.[26] Box 3 lists typical guarantees.

[26] Guarantees are required by the EU "Two-pack" regulation, although in broad terms. "National legal provisions ensuring a high degree of functional autonomy and accountability, including: (i) a statutory regime grounded in national law, regulations or binding administrative provisions; (ii) not taking instructions from the budgetary authorities [...] or from any other public or private body; (iii) the capacity to communicate publicly and in a timely manner; (iv) procedures for nominating members on the basis of experience and competence; and (v) adequate resources and appropriate access to information to carry out their mandate" (Chapter 1, Article 2.1.1 of Regulation No 473/2013).

76. Independence implies predictable funding commensurate to the council's mandate. First, the size (in terms of staff) of the council could be set in legislation subject to periodic independent reviews. Second, the council's funding should not be subject to discretionary executive decisions. One possibility is to ensure that the council's appropriation forms a separate line item in the budget. Secured multi-year financing is another option. The most radical option is to take the council's financing entirely off budget, for instance by mandating the central bank to provide funding.

77. Independence alone is not a guarantee of influence; and specific provisions pertaining to the channels of influence of the council on policy could be useful:

a. ***Regardless of the chosen governance structure (committee or single person), the council should speak with one voice.*** The council's capacity to shape the public debate would be severely undermined if various members of its board or senior staff were allowed to publicly voice divergent views or analyses. Where decisions are made by a committee, the chairperson should at a minimum cast the tie-breaking vote.

b. ***The council's freedom to communicate its messages and analysis to the general public could be clarified.*** This could imply specific guarantees on unrestricted access to the media. At the same time, an obligation for the council to publicize well in advance the calendar of its publications and press conferences could also contribute to the signaling value of the council's communication. In particular, it would avoid misperceptions about the timing of communications as being deliberately favorable or unfavorable for the government.

c. ***The direct inputs of the fiscal council on the budget process should be precisely defined.*** Specifically, it should be clear that requests for costing particular measures or producing ad-hoc analyses should be kept within reasonable limits to preserve the council's ability to independently develop its own work program. Giving to the council the discretion to decline certain requests could be guaranteed by law.[27] Clarity is also at a premium in the assessment of forecasts. Ideally, an explicit "comply-or-explain" clause should be introduced.

[27] A memorandum of understanding could establish criteria for prioritizing costing requests from legislative members, for instance by focusing on those that potentially have a significant impact on the government's financial position.

Box 3. Legal Safeguards on Independence

Prohibition for elected officials to give instructions to the council. For instance, the legislation establishing the Australian Parliamentary Budget Officer (PBO) provides that the PBO "*is not subject to direction from anyone in relation to: (a) whether or not a particular function is to be undertaken; or (b) the way in which a particular function is to be undertaken; or (c) the priority to be given to any particular matter.*" In Romania, the law bans the fiscal council to "*seek or receive instructions from public authorities.*"

Merit-based selection of the council's senior management. Management and staff should be selected on the sole basis of merit and professionalism. The qualifications could be made explicit—including professional standing and relevant government or academic experience. In practice, this involves proven competence in economics and public finances and familiarity with the budget process. The council's management should preferably combine a mix of academic and administrative experience. For instance, in Sweden, the law requires that "*the Council includes members with a high level of scholarly expertise in economics and members who have practical economic policy experience and there is a balanced representation of expertise and experience.*"

Appointment of council's senior management. Various provisions can minimize the risk of a politically motivated appointment. Bans on holding prior political positions or significant cooling-off period between a political position and a senior management appointment in the council are the strongest options. Election or formal confirmation of the council members by the legislature, as in Australia, France, Romania or the United States can also emphasize the independent standing of the council, and depending on the country's institutional tradition may reduce the risk of a biased appointment. In case the council's senior management is selected by the executive, discretion should be restricted. One option is to have council itself (Denmark and Sweden) or an independent expert panel to propose a short list of eligible candidates to the executive.

Long and non-renewable terms of office for senior management. The terms of office of the council's management should be relatively long—higher than a legislative term to reduce the risk of a political cycle—and non-renewable—to avoid that career/reappointment concerns lead to political capture.[28]

Own employment policy. To attract and retain the best professionals and reduce the risk of conflict of interest with other employers, the council's senior management and staff should consist of full-time positions with a competitive salary determination process delinked from civil service rules. The council's management should have full responsibility for recruiting, retaining, and motivating its staff.

Clear dismissal procedures. The Council's management should only be dismissed under well-defined circumstances, including conflict of interest, criminal or fraudulent activities, incapacity, or lack of performance. For instance, in Ireland, "*the Minister may remove a member of the Fiscal Council from office if the removal of the member appears to be necessary for the effective performance by the Fiscal Council of its functions.*" (Fiscal Responsibility Act of 2012, Art. 4.(2).d)

Access to information. Functional independence requires full access to all relevant information from the government (data, policy *objectives*,...), which should be guaranteed by law. Of course, safeguards must be in place to protect confidential information (e.g. individual tax returns,...).

[28]One potential problem with long tenures is that they could discourage academic candidates and hinder the influx of new ideas.

D. Institutional Models and Relations with Other Independent Institutions

78. When setting up a new fiscal council, a stand-alone institution should be preferred to alternative models. The stand-alone format offers the best guarantees of legal and functional independence, in part because it is more likely than other models to require a strong legal basis—constitutional amendment, organic law, etc.—and could more easily imply a dedicated staff and an autonomous personnel policy, including possibly recruitment and remuneration outside the constraints of the civil service. That model is also likely to offer greater visibility from the start, which helps new institutions to establish a reputation more quickly. However, should a country prefer to attach the council to the legislative or executive branch of government, explicit and strict guarantees of functional independence along with secured resources would be even more critical. While this model has been dominant so far, institutions in this category often owe their success to a gradual reputation buildup that cannot be replicated in the case of new institutions aimed at sending a strong signal from the start.

79. Attaching the fiscal council to another independent institution should in general be avoided due to the risk of confusion between the respective mandates and tasks of the host and the guest. However, if the council is hosted in an audit office, the ex-ante and ex-post assessment tasks of each body will have to be clearly defined. In particular, the audit office should not produce ex-ante analyses of fiscal plans, programs and forecasts that would normally fall under the responsibility of the council. Also, placing the fiscal council in the central bank should be avoided—in spite of the implied protection of financial resources—because the council's views and approaches might be tainted by the policy mandate of the bank (or the suspicion thereof would undermine the perceived neutrality and legitimacy of the council).

80. Fiscal councils should establish formal communication channels with other institutions commenting on fiscal policy. Multiple signals about fiscal performance are a mixed blessing. On the one hand, a multiplicity of analyses and forecasts can encourage the council to keep the highest professional standards needed to remain the authoritative voice it is officially mandated to be. On the other hand, conflicting objectives and informational asymmetries among the institutions can lead to cacophony, undermining the council's efforts to clarify and focus the public debate on the most relevant issues. Regular exchanges of views and information between the council and other official institutions (domestic, supranational or international) could go a long way in pre-empting conflicting signals. As regards private institutions, keeping open communication channels with the most influential actors would be useful.

81. The need for a regular dialogue is particularly important in the context of the new fiscal architecture of the Economic and Monetary Union in Europe. Conflicting messages between Union-wide budgetary surveillance and national institutions could be mutually detrimental to the supranational authorities (European Commission and EU Council) and the national fiscal council. Such risk could be reduced by ensuring regular exchange of views, and information on methodologies and assessments with the Commission. This implies that national fiscal councils should be free to engage directly with supranational and international organizations. Equally important would be to establish regular interactions among national fiscal councils to level the playing field and reduce informational asymmetries.

E. Accountability and Transparency

82. Fiscal councils should promote the adoption of best practice in matter of fiscal transparency. A fiscal council directly contributes to greater fiscal transparency by raising the general degree of understanding of the government's underlying financial position and the risks around it. This is the essence of its watchdog function and a consequence of its eventual role in producing forecasts, long-term scenarios, and sustainability assessments. Beyond that role, the fiscal council could promote the adoption of best practice at all level of governments, first of all by being a raw model of transparency in its own operations. In particular, the methodologies and models used in its activities should be fully disclosed.

83. As an independent public institution, the fiscal council should be accountable to its political principal (Parliament, Executive or both) and to the broader public. These would typically involve the right for the political principal to dismiss the council's management on a limited number of objective grounds in accordance with due process (e.g. serious cases of infringement of the mandate or misconduct). In addition, ex-post assessments on the fulfillment of the mandate and the efficient use of resources (possibly by the audit institution or peer reviews), the publication of a comprehensive Annual Report submitted to the political principal, and regular hearings before parliamentary committees could be part of normal accountability requirements.

84. The quality of the council's work and its impact should be independently assessed on a regular basis. The effect of a fiscal council on credibility critically depends on the quality and integrity of its work, and on the way it manages to shape the public debate. Regular external evaluations can help maintain the highest professional standards and suggest improvements to the council's operations and even design. However, evaluating the council's effectiveness is challenging given the multiplicity of tasks and indicators, and the largely qualitative nature of the evaluation.

85. The oversight arrangement for the fiscal council should produce clear signals to encourage the council to maintain strong performance. In practice, this implies striking the right balance between medium and low frequency checks on the council's work. High-frequency evaluations (annual) could become a source of distraction in the fiscal policy debate and should be avoided. At medium (3-5 years) frequency, an Advisory Committee could review the overall quality of the work (reporting, methodologies) and report to the council and its political principal. Those reviews could also be done by peers, as is routinely the case among audit institutions.[29] A summary of the review could be appended to the Annual Report of the council, although the risk of creating noise around the council's work should always be kept in mind. At low frequency (5-10 years), an ad-hoc committee could provide a more thorough review aimed at detecting design flaws and recommend reforms. The precise institutional format of those oversight committees may vary, but they should ideally be composed of high-level experts, preferably foreigners appointed by the council to avoid undue constraints on the pool of qualified candidates and ensure strict independence from local politics.

[29] The International Organization of Supreme Audit Institutions (INTOSAI) has codified best practice for voluntary peer review of state audit institutions. A similar approach could be emulated in the context of the OECD network of independent fiscal institutions or a future EU-wide network.

Appendix 1. Can Fiscal Councils Improve Fiscal Performance?

Fiscal councils can help improve fiscal performance. Fiscal councils could contribute to improved fiscal performance through two main channels. The first channel is the limitation of political influences on the design and conduct of fiscal policy. By informing the public on the real state of public finances, thereby raising their awareness, fiscal councils could increase the political cost of fiscal indiscipline and encourage sound fiscal policies. The second, more direct channel, for fiscal councils influence on fiscal performance is through technical contributions to the budget process and the conduct of fiscal policy. Fiscal councils can be tasked with the provision or the assessment of macroeconomic forecasts underlying the budget. In countries with numerical fiscal rules, fiscal councils can also support the implementation of the rules by monitoring them or assessing conditions to activate escape clauses.

Empirical evidence on the impact of fiscal councils on fiscal performance is limited. Hagemann (2011) surveyed few country-specific case studies (Belgium, Chile, United Kingdom, and Hungary) that compare fiscal performance indicators before and after the establishment of a fiscal council. Some of these studies suggest that fiscal councils contributed to improved fiscal performance (Lebrun, 2006; Coene, 2010). The European Commission (2006) illustrates the effectiveness of fiscal councils on fiscal performance by combining answers to its questionnaire with a literature survey and descriptive statistics. Only Debrun and Kumar (2008) provide cross-country evidence on the effectiveness of fiscal councils for fiscal discipline for mature EU countries (EU-15 excluding Luxembourg). The authors used survey data from the EC to assess the impact of fiscal institutions (fiscal rules and fiscal councils) on fiscal performance. They show that fiscal rules are associated with higher fiscal performance and fiscal councils could impact fiscal outcomes through numerical rules. Indeed, the authors show that fiscal councils tend to contribute to the emergence of numerical rules or their better enforcement.

Staff undertakes a novel cross-country panel empirical analysis covering the spectrum of fiscal councils around the world. The empirical analysis is based on a cross-country panel data covering 58 advanced and emerging countries over the period 1990-2011. About half of the countries in the sample established a council during the period of analysis. The estimated model is an augmented regression-based solvency test proposed by Bohn (1998). It explains the primary balance by its lagged term (to allow for persistence), the lagged gross debt (to capture long-term solvency constraint), and the output gap (to control for the cyclicality of fiscal policy). The regression model also includes a fiscal rule index to capture the comprehensiveness of numerical fiscal rules and a dummy variable indicating the existence of a fiscal council. Because the number of observations (N) is large and the time dimension (T) is finite in our dynamic specification, standard estimation techniques such as least squares dummy variable estimators are not consistent. The bias-corrected Least Square Dummy Variable (LSDVC) dynamic panel estimator suggested by Bruno (2005) is therefore preferred as it approximates the bias inherent to dynamic unbalanced panels and constructs a consistent estimator.

The results highlight that the mere existence of fiscal councils is not associated with better fiscal outcomes but key features of the councils do help fiscal performance (Table 1).

Controlling for fiscal rules, which are consistently associated with better fiscal performance, and other classical determinants of the primary balance, fiscal councils do not seem to encourage better fiscal outcome. However, key characteristics of the councils are associated with improved fiscal performance. Countries with independent fiscal councils, either with legal guarantees through legislations or with operational guarantees through adequate human resources, have on average better fiscal outcomes. Fiscal councils evolving within a clear fiscal framework, with a numerical fiscal rule that they monitor, are associated with higher fiscal performance. This reflects the benefits associated with fiscal rules as they provide a clear benchmark to evaluate fiscal performance, helping fiscal councils' to fulfill their mandate. More technical contributions from fiscal councils such as the scoring of governments' measures or the assessment of official forecasts are also associated with better fiscal outcomes. These inputs to the budget process could be instrumental in reducing the deficit and procyclicality biases that often impact discretionary fiscal policy. As fiscal councils do not directly impact fiscal policy, their influence mainly stem from the political cost of fiscal indiscipline that they tend to enhance by better informing the public. The results indeed confirm that countries where the fiscal councils have a higher media impact tend to exhibit better fiscal outcomes.

The results should be interpreted with some caution for a number of reasons. First, as noted in previous sections, more than half of the fiscal councils around the world have been created after 2005. The limited time span of a good number of fiscal councils could potentially affect the empirical results. Reassessing the issue in the future as longer time series become available would be sensible. Second, the econometric analysis is rigorous but still subject to some limitations. Reverse causation may explain the results as it is possible that only fiscally-conscious governments establish fiscal councils, reflecting their unobservable preferences and commitment to fiscal discipline. There is still a small possibility of an omitted variable bias despite the presence of the lagged dependent variable in the econometric model that should reduce such bias. Indeed, important omitted variables could jointly affect fiscal performance and fiscal institutions. In this situation, any causal inference between fiscal councils and fiscal performance could actually capture the impact of the omitted variables on fiscal performance. Third, the key characteristics of fiscal councils are highly correlated (Table 2). This makes it complicated to assess their combined impact on fiscal performance. Because of these potential limitations, the analysis considers the empirical results as reflecting robust conditional correlations and prefers to not draw causation conjectures.

Appendix Table 1. Fiscal Councils and Fiscal Performance
Bias Corrected LSDV Dynamic Panel Model

	Dependent Variable: Primary Balance in percent of GDP							
Primary	0.823	0.824	0.821	0.821	0.826	0.826	0.826	0.824
Balance (t-1)	(27.07)***	(26.84)***	(26.53)***	(24.03)***	(26.96)***	(27.49)***	(28.07)***	(27.13)***
Debt	0.015	0.017	0.016	0.023	0.016	0.016	0.016	0.017
(t-1)	(2.92)***	(3.37)***	(3.24)***	(3.69)***	(3.24)***	(3.14)***	(3.31)***	(3.40)***
Output Gap	-0.095	-0.094	-0.096	-0.091	-0.098	-0.095	-0.092	-0.093
(t-1)	(3.05)***	(3.03)***	(3.09)***	(2.40)**	(3.17)***	(3.06)***	(2.98)***	(2.99)***
Fiscal Rules	0.277	0.275	0.283	0.249	0.232	0.289	0.295	0.280
Index (FRI)	(2.62)***	(2.59)***	(2.66)***	(2.26)**	(2.27)**	(2.73)***	(2.79)***	(2.65)***
Fiscal	0.543							
Council	(1.42)							
Legal		0.930						
indep.		(2.38)**						
Indep.			0.386					
budget			(0.71)					
Staff number				0.296				
(High level)				(2.34)**				
Fiscal rule					1.524			
monitoring					(2.80)***			
Costing of						1.355		
measures						(2.57)**		
Forecast							1.293	
Assessment							(2.78)***	
High media								0.904
Impact								(2.32)**
Time dummies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	901	901	901	890	901	901	901	901
Countries	58	58	58	58	58	58	58	58

Absolute bootstrapped t-statistics in parentheses.
* Significant at 10%; ** significant at 5%; *** significant at 1%.

Appendix Table 2. Correlation Matrix

	Legal independence	Independent budget	Fiscal rule monitoring	Forecast assessment	High media impact
Legal independence	1				
Independent budget	0.75*	1			
Fiscal rule monitoring	0.43*	0.39*	1		
Forecast assessment	0.80*	0.65*	0.32*	1	
High media impact	0.89*	0.77*	0.61*	0.81*	1

* Significant at 1%

Appendix 2. Fiscal Councils and Forecasting Bias

The accuracy of budgetary forecasts is a key element for the conduct of fiscal policy. Budgetary forecasts, in conjunction with tax and expenditure policies, determine the direction and goal of fiscal policy. Discrepancies between actual and forecasted real growth significantly affect ex-post assessments of fiscal policy and could also help in evaluating the adequacy of counter-cyclical fiscal policies. Optimistic growth projections that are reflected in budgetary aggregates could have similar impact to an active expansionary fiscal policy. If forecast errors are the causes of excessive deficits, discretionary fiscal tightening would not be the appropriate policy. Instead, developing realistic budgets by using more accurate macroeconomic projections would be more suitable.

Fiscal institutions providing or assessing official forecasts can help reduce forecasting errors. The existing literature on the potential impact of fiscal institutions on official forecasts essentially focuses on European countries. Jonung and Larch (2006) show that forecast bias in the EU may be politically motivated and that forecast by an independent authority such as a fiscal council would be preferable to forecast provided by the Ministry of Finance. Frankel and Schreger (2012) find that official budget forecasts are over-optimistic, particularly in Euro area countries. The authors also show that real GDP forecasts are over-optimistic during booms. They find that independent fiscal institutions producing budget forecasts reduce the over-optimistic bias when countries do not comply with the 3 percent cap on budget deficits.

Staff analyzes empirically the impact of fiscal institutions on macroeconomic forecasts. Official forecasts are assessed on the basis of their accuracy as well as their bias. The forecast error is defined as the difference between the forecast of the aggregate for t made in t-1 and the outcome, which is the estimate for t made in t+1. The mean forecast error thus captures the extent of forecasting bias in official projections. The mean of the absolute value of forecast errors assesses forecasts accuracy. Simple pooled regressions, controlling for the output gap, fiscal rules, and time dummies are used to evaluate the impact of fiscal institutions and their key characteristics on forecasting errors. The sample includes 26 countries over the period 1998-2010.

The results illustrate that fiscal councils and their key characteristics are associated with lower forecast errors. Countries with fiscal councils tend to have lower bias in their official budget forecasts as well as better forecasts accuracy (Table 3 and 4). Specifically, countries where fiscal councils are independent, have a high media impact, provide or assess macroeconomic forecasts, and monitor fiscal rules have lower bias in their official forecasts of the budget balance. Fiscal councils with the above mentioned characteristics are also associated with better forecast accuracy of the budget balance. Similarly with Frankel and Schreger (2012) our results illustrate that real growth forecasts tend to be over-optimistic during booms (Table 5). Only independent fiscal councils seem to be associated with lower bias of real output forecasts. In opposite, fiscal councils and their key characteristics (independence, provision or assessment of macroeconomic forecast, and high media impact) are associated with better accuracy of real output forecasts (Table 6). Real GDP forecasts also tend to be less accurate during booms.

Appendix Table 3. Fiscal Councils Characteristics and Primary Balance Forecast Error

	Dependent Variable: Forecast Error (Primary Balance)					
Output gap	0.059	0.060	0.067	0.059	0.064	0.059
	(0.63)	(0.65)	(0.72)	(0.63)	(0.69)	(0.63)
Fiscal rules index	-0.215	-0.252	-0.213	-0.215	-0.261	-0.193
	(1.70)*	(1.95)*	(1.58)	(1.70)*	(1.98)**	(1.43)
Fiscal council	-0.783					
	(3.32)***					
Legal independence		-0.911				
		(3.76)***				
Independent budget			-0.821			
			(3.14)***			
High media impact				-0.783		
				(3.32)***		
Forecasts provision /assess					-0.863	
					(3.35)***	
Fiscal rules monitoring						-0.653
						(2.28)**
Constant	-0.107	-0.001	-0.378	-0.107	-0.004	-0.406
	(0.16)	(0.00)	(0.68)	(0.16)	(0.01)	(0.76)
Time dummies	Yes	Yes	Yes	Yes	Yes	Yes
R^2	0.32	0.33	0.32	0.32	0.32	0.31
Observations	225	225	225	225	225	225
N. of countries	26	26	26	26	26	26

Robust t-statistics in parentheses.
* Significant at 10%; ** significant at 5%; *** significant at 1%.

Appendix Table 4. Fiscal Councils Characteristics and Primary Balance Absolute Forecast Error

	Dependent Variable: Forecast Error (Primary Balance)					
Output gap	0.000 (0.00)	0.002 (0.03)	0.007 (0.08)	0.000 (0.00)	0.006 (0.07)	0.002 (0.02)
Fiscal rules index	-0.082 (0.74)	-0.122 (1.07)	-0.098 (0.83)	-0.082 (0.74)	-0.131 (1.13)	-0.074 (0.63)
Fiscal council	-0.813 (4.11)***					
Legal independence		-0.857 (4.13)***				
Independent budget			-0.576 (2.70)***			
High media impact				-0.813 (4.11)***		
Forecasts provision /assess					-0.770 (3.41)***	
Fiscal rules monitoring						-0.549 (2.31)**
Constant	1.105 (2.88)***	1.187 (3.01)***	0.857 (2.64)***	1.105 (2.88)***	1.171 (3.04)***	0.819 (2.45)**
Time dummies	Yes	Yes	Yes	Yes	Yes	Yes
R^2	0.21	0.22	0.19	0.21	0.20	0.19
Observations	225	225	225	225	225	225
N. of countries	26	26	26	26	26	26

Robust t-statistics in parentheses.
* Significant at 10%; ** significant at 5%; *** significant at 1%.

Appendix Table 5. Fiscal Councils Characteristics and Real Growth Forecast Error

	Dependent Variable: Forecast Error (Primary Balance)					
Output gap	0.377	0.377	0.380	0.377	0.378	0.377
	(4.48)***	(4.49)***	(4.51)***	(4.48)***	(4.49)***	(4.46)***
Fiscal rules index	0.140	0.126	0.151	0.140	0.123	0.155
	(1.56)	(1.42)	(1.66)*	(1.56)	(1.37)	(1.57)
Fiscal council	-0.285					
	(1.28)					
Legal independence		-0.297				
		(1.27)				
Independent budget			-0.456			
			(1.73)*			
High media impact				-0.285		
				(1.28)		
Forecasts Provision/assess					-0.192	
					(0.75)	
Fiscal rules monitoring						-0.300
						(1.07)
Constant	-1.707	-1.679	-1.824	-1.707	-1.708	-1.827
	(1.45)	(1.41)	(1.65)	(1.45)	(1.47)	(1.66)*
Time dummies	Yes	Yes	Yes	Yes	Yes	Yes
R^2	0.60	0.60	0.60	0.60	0.60	0.60
Observations	225	225	225	225	225	225
N. of countries	26	26	26	26	26	26

Robust t-statistics in parentheses.
* Significant at 10%; ** significant at 5%; *** significant at 1%.

Appendix Table 6. Fiscal Councils Characteristics and Absolute Real Growth Forecast Error

	Dependent Variable: Forecast Error (Primary Balance)					
Output gap	0.266	0.267	0.271	0.266	0.270	0.267
	(3.01)***	(3.00)***	(3.03)***	(3.01)***	(3.04)***	(2.97)***
Fiscal rules index	-0.004	-0.031	-0.002	-0.004	-0.034	0.003
	(0.05)	(0.36)	(0.02)	(0.05)	(0.40)	(0.03)
Fiscal council	-0.512					
	(2.48)**					
Legal independence		-0.441				
		(2.02)**				
Independent budget			-0.555			
			(2.52)**			
High media impact				-0.512		
				(2.48)**		
Forecasts Provision/assess					-0.635	
					(2.88)***	
Fiscal rules monitoring						-0.364
						(1.35)
Constant	1.649	1.671	1.470	1.649	1.739	1.466
	(4.38)***	(4.48)***	(3.21)***	(4.38)***	(5.04)***	(3.14)***
Time dummies	Yes	Yes	Yes	Yes	Yes	Yes
R^2	0.48	0.48	0.48	0.48	0.48	0.48
Observations	225	225	225	225	225	225
N. of countries	26	26	26	26	26	26

Robust t-statistics in parentheses.
* Significant at 10%; ** significant at 5%; *** significant at 1%.

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