

**IMMEDIATE
ATTENTION**

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To: Members of the Executive Board

From: The Secretary

Subject: **Sweden—Report on Observance of Standards and Codes—
Fiscal Transparency Module**

The attached report on the observance by Sweden of the standards and codes fiscal transparency module was prepared in the context of the 2000 Article IV consultation with Sweden (SM/00/184, 8/1/00), which was approved on a lapse of time basis on August 22, 2000.

It is expected that this report will be published on the Fund's external website at the beginning of January 2001.

Questions may be referred to Mr. Potter (ext. 35669) and Mr. Allan (ext. 38542).

Att: (1)

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INTERNATIONAL MONETARY FUND

SWEDEN

**Report on the Observance of Standards and Codes (ROSC)
Fiscal Transparency Module**

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Approved by Michael Depler and Peter S. Heller

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EXECUTIVE SUMMARY

This report provides an assessment of fiscal transparency practices in Sweden in relation to the requirements of the IMF *Code of Good Practices in Fiscal Transparency—Declaration on Principles* based on the authorities' response to the IMF fiscal transparency questionnaire and other documents provided by the authorities.

Fiscal management in Sweden generally meets the requirements of the fiscal transparency code and has recently introduced reforms to further improve transparency. Under recent reforms, the budget preparation process has been strengthened, and weaknesses in the legislative framework have been addressed. Current reforms center on the development and definition of responsibilities between and within subnational governments, and ensuring a level playing field between the state and private sector.

Noting the importance of ongoing reforms, the staff suggested a number of steps to further improve fiscal transparency, including a more formal review process for macroeconomic assumptions and inclusion of a formal statement of risks within budget documents. The staff also suggested that a clearer indication of the impact of the economic cycle on the fiscal positions be provided.

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ABBREVIATIONS AND ACRONYMS

| | |
|------|---|
| ESA | European System of Accounts |
| ESV | National Financial Management Authority |
| RGK | National Debt Office |
| RRV | National Audit Office |
| SDDS | Special Data Dissemination Standard |
| SGP | Stability and Growth Pact |

I. INTRODUCTION¹

1. This draft report provides an assessment of fiscal transparency practices in Sweden against the requirements of the IMF *Code of Good Practices on Fiscal Transparency—Declaration on Principles*. The authorities have completed the fiscal transparency questionnaire prepared by the IMF staff. The assessment has two parts. The first part is a description of practice, prepared by the IMF staff on the basis of the questionnaire response and additional information provided by the authorities. The second part is an IMF staff commentary on fiscal transparency in Sweden.

II. DESCRIPTION OF PRACTICE

A. Clarity of Roles and Responsibilities

2. **The boundary between general government and the rest of the economy is well defined.** The statistical definition of the general government sector was brought into line with European System of Accounts (ESA 95) standards in Spring 1999. There are, however, continuing issues in ensuring competition on equal terms between the private sector and public agencies involved in commercial activities. The Swedish Competition Authority is responsible for reviewing competition-related questions for the economy as a whole, and from time to time the Agency for Administrative Development is instructed by the government to review specific activities of central government agencies in competitive markets. There are few quasi-fiscal activities and state support for nonfinancial public enterprises is by explicit budget subsidies. Subsidies are regularly reviewed in the budget process to ensure their compatibility with EU directives, to check whether they are justified as a core state obligation, and to assess whether they are the best use of government expenditure. Regulations are clear and there are periodic reviews, although the latter are not published on a regular basis.

3. **Commercial operations of government are being corporatized.** Several public utilities and state-owned enterprises have been incorporated. Pure privatization of agency operations has been relatively uncommon. The Post Office and, until recently, Telia (the telecommunications corporation), for instance, were still wholly-owned state companies.^{2,3}

¹ The assessment of fiscal transparency in Sweden was drafted by Mr. William Allan, with input from the staff of EU1 and PDR Departments on the basis of the questionnaire response and other materials provided by the Swedish authorities.

² On May 17, 2000, the parliament approved the sale of 20–25 percent of the holdings in Telia by mid-June 2000.

³ Under the State Budget Act, sale of equity where government ownership is greater than 50 percent requires parliamentary approval; unless specifically directed otherwise, the government may sell equity in companies where ownership is less than 50 percent without parliament's approval.

4. **Government equity holdings in private companies are reported and are being progressively reduced.** Government equity holdings are limited to the following: aviation services (SAS Sweden, 50 percent); banking (Nordic Baltic Holding, 26 percent); defense industry (Celsius, 25 percent); forestry industry (Assidoman, 50 percent); real estate (Celtica, 39 percent); stock exchange (OM Group, 8 percent).

5. **The central bank has full independence on monetary policy.** The central bank (Riksbank) undertakes no activities of a quasi-fiscal nature and its independence has been assured under amendments to the *Sveriges Riksbank Act* in May 1997. These amendments have established a clear medium-term objective of maintaining price stability and created a two-tier board structure giving greater autonomy to the Executive Board. Its operations in the government securities market are clearly explained to the public.

6. **A clear separation of policymaking and operations is emphasized within government.** Within central government, a long-standing distinction has been drawn between the (relatively small) policy-making ministries and the much larger agencies of government responsible for implementing policy (see Box 1). Overall, the budget process is open to the public, but there is much greater emphasis on provision of information on delivery of service by agencies rather than input allocations within agencies. Over the past decade, as a result of severe economic difficulties and chronic high levels of public debt, the structure of government has undergone major reform and the budget has been successfully consolidated. Public sector reform has resulted in considerably more delegation of decision-making power from the government to agencies, and major changes have also been made in the structure of agencies (see also discussion below of “management for results” and audit of agencies). Since 1990, some 160 agencies have been closed, and 100 new ones formed.

7. **Responsibilities of and within subnational governments are being developed and more clearly defined.** Recent reforms have focused on improving central and local government (councils and municipalities) relations, which in the past have suffered from fragmentation and poor coordination of responsibilities (for example, central responsibility for labor policy but local responsibility for implementation of social policies). Central government sets national standards for various social services. These are implemented by local authorities, but under the “financing principle” any measures introduced by central government that directly affect local authorities must be accompanied by a means of financing that does not involve raising local taxes. Responsibilities within local government have been considerably decentralized to service-providing agencies, and an emphasis placed on service delivery. Local government finances have been strongly affected by the need to cut back overall public expenditure and the limited scope for local tax increases. Around 11 percent of local government revenue comes from general purpose grants from the center, and a further 5 percent from special purpose grants; in recent years, emphasis has been placed on general purpose grants and local setting of priorities. From 2000, the local governments are required by law to balance their budgets.

Box 1. Separation of Government Policy and Operations in Sweden

Government administration in Sweden is characterized by a high degree of decentralization. In terms of employees, central government is relatively small (about 5 percent of the labor force) compared to local government (about 25 percent of the labor force) and, within central government, government policy is administered by 13 ministries with between 100 and 350 staff each. About 99 percent of central government staff are employed by autonomous agencies.¹ About 300 such agencies are responsible for implementing government policies. The split in responsibilities between operations and policy has been in place for around two centuries, but has been subject to substantial reforms and redefinition of roles in recent years.

Government agencies have considerable autonomy (an OECD study in 1998 concluded that managers in Sweden enjoy probably the highest degree of flexibility in management of their organizations among OECD countries).² The autonomy of agencies is protected by the Constitution. The government is prohibited from interfering with agency decisions based on the application of a law. This autonomy has meant that the separation of agencies such as the National Audit Office (RRV) from the executive branch of government is perceived as less necessary than in many other countries. Agencies are free to determine their own organizational structure and, particularly with recent reforms, have great flexibility in managing financial resources and personnel. Generally, agencies receive a one line appropriation, with complete flexibility over choice of inputs. There is also the possibility of carrying forward appropriations from one year to the next.

In return for greater flexibility in operations, more emphasis is now being placed on reporting on performance. Thus far, this objective is achieved through production of annual reports which have emphasized reporting and assessment of agency outputs. Concern with broader outcomes and setting accountability standards is the responsibility of ministries. The 1998 OECD study suggested the need to develop further ministries' capacity in this regard.

¹ Larger agencies are responsible for tax administration, customs administration, police, universities and colleges, and Swedish State Railways. Most agencies have boards including citizens with an interest in the agency operations. These boards are generally advisory, but some operate similarly to a board of directors for commercial enterprises.

² OECD/PUMA *Budgeting in Sweden* A paper presented at the 19th Annual Meeting of Senior Budget Officials, Paris, 25-26 May 1998.

8. **Weaknesses in the legislative framework for budgeting have recently been effectively addressed.** The Swedish Constitution (*Regeringsformen*) contains only basic provisions relating to the relative authority of parliament and the government to manage the budget. No other special legislation had been passed in this area until recently, except for the *Act on State Borrowing and Debt Management* (1988: 1387), which defines the conditions under which the government or a public utility may borrow. In the past, annual budget bills

provided the main vehicle both for seeking annual authority to spend and for procedural aspects of the budget consistent with the constitution. This system gave rise to a variety of ad hoc mechanisms for dealing with different kinds of appropriation. For instance, some expenditures could be recorded on the revenue side (as negative revenue) without requiring the formal approval of parliament. A Government Commission on Budget Law was set up to address these issues.⁴ The proposals of the Commission were enacted with minor modifications as the *State Budget Act* (1996: 1059). The new act clarifies the basic principles of budgeting and specifies a clear separation between revenues and expenditures (the principle of gross budgeting). It emphasizes the need for budget management to achieve effective and efficient use of resources and for financial compliance. The law also emphasizes the need for fiscal transparency and prescribes minimum requirements for periodicity and content of accounting and performance reports.

9. **All taxes have a clear basis in law.** Tax laws, regulations, and administrative procedures are clearly defined. There are in practice few discretionary concessions available through the tax and customs administrations and these are disclosed when exercised. Taxpayers' rights are clearly stated in the relevant tax laws and an appeals system provides assurance of taxpayers' rights to have their cases tried by court. Scrutiny of Swedish tax regulations in the framework of EU and OECD work on harmful tax competition has not resulted in any criticism of the transparency of tax laws.

B. Public Availability of Information

10. **Budget documents provide a comprehensive coverage of general government.** The information provided in the budget documents has been greatly improved as a result of reforms in 1996. Most extrabudgetary funds have now been incorporated into the budget. All central government expenditure, excluding interest payments and including the supplementary pension fund, is considered within the overall expenditure ceiling set as a key element of fiscal policy. The budget is on a calendar year basis. Forecasts of key budget aggregates for the two years following the budget are presented in the annual budget and the Spring Fiscal Policy Bill (presented before April 15). The Spring Bill gives a report on public finances, sets the main fiscal policy parameters well prior to the presentation of the Budget Bill in September, and as a rule contains supplementary estimates for the current budget. Budget publications are made available through the government website (<http://www.regeringen.se/>).

11. **Reports are provided on government guarantees and tax expenditures.** A statement on guarantees and deposit insurance for the preceding fiscal year is made in a separate report to parliament, and reference is made to that report in the Budget Bill.⁵ Tax

⁴ See Report (SOU 1996: 14) *Proposal for a State Budget Act in Sweden*.

⁵ An annual fee, reflecting financial risk and administrative cost, is levied for all guarantees unless the parliament decides otherwise—in which case a corresponding amount is appropriated in the budget. Revenues from fees and appropriations are set aside in an off-budget account at the National Debt Office. This account covers administrative costs and indemnities.

expenditure estimates have been published annually since 1996 in an annex to the Spring Fiscal Policy Bill, and since 1998 in the annual Budget Bill. Central government assets and liability transactions are reported weekly by the National Debt Office (RGK).

12. **Government debt and financial assets are regularly reported.** The gross debt position is reported monthly by the RGK and the debt position is reported to the Parliament twice a year in the Spring and Budget Bills. Financial asset (including equity and public enterprise net worth) transactions and central government asset holdings are reported quarterly in the Financial Accounts.

13. **There is a public commitment to produce regular fiscal reports.** Sweden subscribes to the IMF Special Data Dissemination Standard (SDDS) and meets all data dissemination standards for fiscal data; it produces an advance release date calendar showing times of release of fiscal data as required under the SDDS.

C. Open Budget Preparation, Execution, and Reporting

14. **The budget preparation process is open and clearly documented.** Sweden has taken a number of steps to strengthen its budget preparation process in the light of weaknesses diagnosed in the early 1990s. Since 1996, a “framework” budget process, which sets a rolling, nominal, multiannual expenditure ceiling, has been adopted. The overall ceiling and broad allocations for 27 expenditure areas are set in the Spring Fiscal Policy Bill submitted to parliament in mid-June. The detailed estimates are then finalized by spending ministries and submitted in the Budget Bill in late September.⁶ As well as strengthening controls, this provides a clearer statement of government policies. New policy proposals are clearly identified and distinguished from existing policies during the budget process.⁷

15. **Clear fiscal targets are set.** The government fiscal target, first introduced in the Spring Bill in 1997, is a surplus of 2 percent of GDP, measured as an average over the business cycle. This target is set in the context of the high cyclical sensitivity of the budget balance and to help adjust to demographic trends, and is designed to meet commitments for convergence under the EU Stability and Growth Pact (SGP). To help achieve the fiscal balance target, a system of nominal ceilings for central government expenditure excluding interest was introduced in 1997. The ceilings are projected for three years and rolled forward each year and submitted to parliament with the budget. The State Budget Act obliges the government to take remedial action, either within its own authority or by proposing necessary measures to parliament. It should be noted, however, that use of tax expenditures can reduce

⁶ In addition to allocations for each expenditure area, a budget margin is provided for three years' budget estimates to provide a buffer for errors in forecasting and provide scope for new allocations in later years.

⁷ The process is subject to periodic review. A recent report by the *Commission on evaluating the budgetary process (SOU200:61)*, while saying that the process works well, suggests that it could be streamlined and also that the statistical base and the budget forecasts could be improved

the effectiveness of the nominal expenditure ceiling and there have been some recent examples where this practice has been applied.⁸

16. **Some analysis of budget risks and policy sustainability is undertaken.** Sensitivity of budget aggregates to macroeconomic changes are published in the convergence program and in some budget bills, but sensitivity of the projections to the cyclical position is not indicated. Medium-term fiscal sustainability is addressed in the context of the SGP, and long-term sustainability studies have been undertaken in connection with the new pension system—the latter indicate that the pension scheme is financially stable under reasonable assumptions. The *Long-term Survey* of 1999/2000 (SOU 2000: 7) gives a broad survey of economic trends and prospects to 2015 using different scenarios prepared by the National Institute of Economic research.

17. **Performance against aggregate fiscal targets is carefully monitored.** Monitoring is an integral part of the budget execution process and is also emphasized in the context of SGP reviews. The government is required to report to parliament at least twice a year on the expected budget outturn and the state debt, and to explain significant discrepancies between budgeted amounts and the expected outcome. Detailed monthly reports on the fiscal outcome are published about a month after month-end by the National Financial Management Authority (ESV) on its website (<http://www.esv.se/>). From July 1, 1998, the National Audit Office (RRV), which formerly carried out both auditing and accounting functions for government, was split into two. The RRV, as discussed further below, is the external auditing agency for government. The ESV is responsible for oversight of financial management and produces accounts and budget forecasts for government. The RGK produces monthly budget forecasts. Each agency produces both an interim and an annual report, which is audited. An end-year summary of government accounts, based on audited reports, is presented to parliament within nine months of year-end.

18. **Internal management controls are open and effectiveness has been improved.** Controls over finances, procurement, and employment in general government are adequate. Accounts of agencies and final accounts of the central government are prepared on an accrual basis (though budgeting remains on a cash basis). A statement of accounting policies is provided with the annual accounts report. Considerable emphasis has been given to management by results and decentralization of decision-making in the recent reforms. The ESV has used financial management ratings to monitor agencies—and significant improvements in ratings (as well as in timeliness of reporting to the ESV) have been achieved since the system was introduced. Monitoring of results of government activities has focused mainly on measurement of outputs and has been applied most effectively at local levels and to agency programs. Their performance against targets is monitored in the annual reporting process and by RRV audit.

⁸ For instance, local authorities in recent years have been charged lower value added taxes in return for reduced expenditure transfers.

D. Independent Assurances of Integrity

19. **External audit is carried out by an autonomous agency, the RRV.** The RRV in Sweden is an arm of the executive rather than an independent body attached to the legislature. RRV reports, however, are submitted to and debated by parliament. Since the split in functions between RRV and ESV, the RRV's mandate gives particular emphasis to performance and value for money audit. The RRV attaches a statement on the final accounts prepared and submitted to parliament by the ESV. This statement covers financial compliance as well as value for money aspects. RRV publications are available through its website (<http://www.rrv.se/>).

20. **Integrity of macroeconomic forecasts is achieved through the input of several different forecasting groups.** Macroeconomic forecasts are prepared by the Budget Department, which has recently upgraded its capacity in this regard. In addition, independent forecasts are prepared by ESV and the National Institute of Economic and Social Research, both government agencies. The economic assumptions used by the ministry of finance are clearly stated in the budget documents, though there is no formal review of these assumptions by an independent agency.⁹

21. **Independence of the national statistics office is covered by law.** Statistics Sweden is a government agency and has the same degree of autonomy as other agencies. Neither the government nor parliament can annul or otherwise interfere with decisions made by an individual agency concerning the application of a law pertaining to that agency. The Official Statistics Act prescribes that statistics are to be objective and available to the public.

III. IMF STAFF COMMENTARY

22. **Fiscal management in Sweden generally meets the requirements of the fiscal transparency code.** Recent reforms have enhanced transparency in a number of respects. The Swedish model of fiscal management places emphasis on public provision of services but it stresses clear definition of functions as between policy and implementation, decentralization of responsibilities, and results oriented management. There are continuing issues to resolve as regards the appropriate division of responsibilities between central and local government, and to ensure a level playing field between the state and the private sector. These are, however, a central focus of current reforms.

23. Possible areas where further improvements in transparency could be made are as follows.

- Give a clearer indication of the impact of the economic cycle on the fiscal position by publication of an output gap estimate. This could also be supplemented by a structural balance estimate.

⁹ As is the case in the United States and the United Kingdom, for instance.

- Include consideration of tax expenditures in assessing performance against nominal expenditure ceilings.
- Further develop fiscal risk analysis by including in the budget documents a formal statement of risks.
- Establish a more formal process of review of macroeconomic assumptions.
- Strengthen the autonomy of the RRV by promulgating an audit act and improve the capacity of parliament to review action on audit findings.