



New Institutions: Case Finland

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The independent fiscal institution function (IFI) in the National Audit Office of Finland

- ▶ New function in an old institution:
 - ▶ Originally established in 1695 but continuously in function in Finland since 1824
 - ▶ Established by the Constitution of Finland, independent institution in affiliation with the Parliament
 - ▶ Part of the legislative, complete independence in relation to the Government, independence in relation to Parliament
 - ▶ Supreme audit institution, external government audit
 - ▶ Additional role as the supreme oversight of the political party and election campaign financing

- ▶ Fiscal policy monitoring and evaluation expands the scope beyond classic supreme audit institution and brings in a more forward-looking and macro-economic element



The NAOF as IFI

- ▶ Fiscal policy monitoring and evaluation function evolved since 2008, specific function since 2011
- ▶ Act on the Implementation and Application of the Provisions of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union and on the Requirements of the Frameworks of Public Finances (21.12.2012/869)
 - ▶ => assignment of the task of independent monitoring and evaluation of fiscal policy beginning from 1.1.2013
 - ▶ => fiscal policy audit and evaluation department at NAOF since 1.1.2013



Our role and mandate

- ▶ **(1) independent monitoring and evaluation of fiscal policy**
 - ▶ monitoring of the structural balance of the general government and assuring reliability of the structural balance
 - ▶ giving public assessment and opinion whether the measures decided by the Government are sufficient and adequate to improve structural balance of the general government after the termination of the exceptional circumstances
- ▶ **(2) oversight of fiscal policy rules**
 - ▶ monitoring of the correction mechanism required by European Fiscal Compact
 - ▶ setting the fiscal rules as required by EU Law (Budgetary Frameworks Directive 2011/85/EU)
 - ▶ observance of national fiscal rules
 - ▶ assessment whether the Government has fulfilled its obligations to decide and propose measures to improve structural balance and
 - ▶ assessment whether fiscal policy is exercised in accordance with the medium term objectives



Our role and mandate 2

- ▶ **(3) audit and evaluation of the information bases, effectiveness and governance of fiscal policy (fiscal policy audit and evaluation)**
 - ▶ the long-term sustainability of public finances (general government);
 - ▶ audit and assessment of sustainability analyses including testing of calculus and assumptions
 - ▶ audit of the quality of economic forecasts and government economic analyses in Government proposals
 - ▶ audit of the quality of information concerning tax expenditure
 - ▶ assessment of the effectiveness of the fiscal rules and other fiscal governance tools
 - ▶ assessment whether fiscal policy has attained objectives to it or whether prerequisites for the attainment are available
- ▶ To support Parliament's fiscal and visionary powers and enlighten public debate
- ▶ No stand alone product of forecasting. Policy-recommendations only in the context of evaluations performed



The context of establishment

- ▶ Need to ensure independent monitoring of national fiscal rules
 - ▶ Finland has an expenditure rule, spending limit for electoral period for central government expenditure
 - ▶ Historically low-level of debt bias but in the early 1990s level of government debt increased heavily. Rapid increase of debt since 2009 and a sustainability gap
 - ▶ Ministry of Finance initiative that NAOF shall become active in the field of monitoring of fiscal rules

- ▶ Implementation of the new EU and Euro Area economic governance rules
 - ▶ Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (Fiscal Compact) and
 - ▶ EU Budgetary Frameworks Directive
 - ▶ => link to the Euro Area crisis



Our products 1

- ▶ **Electoral Period Report to the Parliament**
 - ▶ Special Parliamentary Report tabled to the Plenary at the end of electoral period:
 - ▶ a comprehensive assessment of the functioning of fiscal rules and of the effectiveness of fiscal policy prior to the parliamentary elections. Report will also have a focus theme.
 - ▶ Next focus theme for 2015: effectiveness of tax policy
- ▶ **Mid-term Electoral Period Review to the Parliament**
 - ▶ Special Parliamentary Report tabled to the Plenary) which serves also the mid-term review by the Government of its Government Program
 - ▶ Latest: K 2/2013, 15.2.2013 (with policy recommendations)
- ▶ **Spring Parliamentary Report (May each year)**
 - ▶ continuous fiscal policy audit and evaluation
 - ▶ monitoring of fiscal rules and a topical theme



Our products 2

- ▶ Specific fiscal policy audit and evaluation reports
 - ▶ in 2012:
 - ▶ - Parliament's access to information and reliability of Parliament's view on the stability measures in the Euro Area
 - ▶ - Relationship between Spending Limits and Government's Program
 - ▶ - Information on Government guarantees and liabilities
- ▶ Opinions and testimonies to Parliament's Committees on request
 - ▶ Finance Committee, Audit Committee and Constitutional Committee
- ▶ Opinions and expert advice to Government
 - ▶ example: NAOF representatives participated to the Ministry of Finance led assessments and provision of expert proposals on the fiscal rules and Prime Minister Office led projects to improve strategic leadership in Government

Our work programme and approach

- ▶ Planning for electoral periods (electoral cycle)
 - ▶ comprehensive risk analyses
- ▶ Main question in assessments: long-term sustainability of public finances (general government) and the stability of public finances.
- ▶ Expressed as the inter-temporal budget constraint of the general government

$$\underbrace{\underbrace{G_t - T_t}_{PB_t} + iD_{t-1}}_{B_t} = \Delta D_t$$

- ▶ Public finances is sustainable when

$$\Delta D_t / Y_t = 0, t \rightarrow \infty$$

Technical explanations

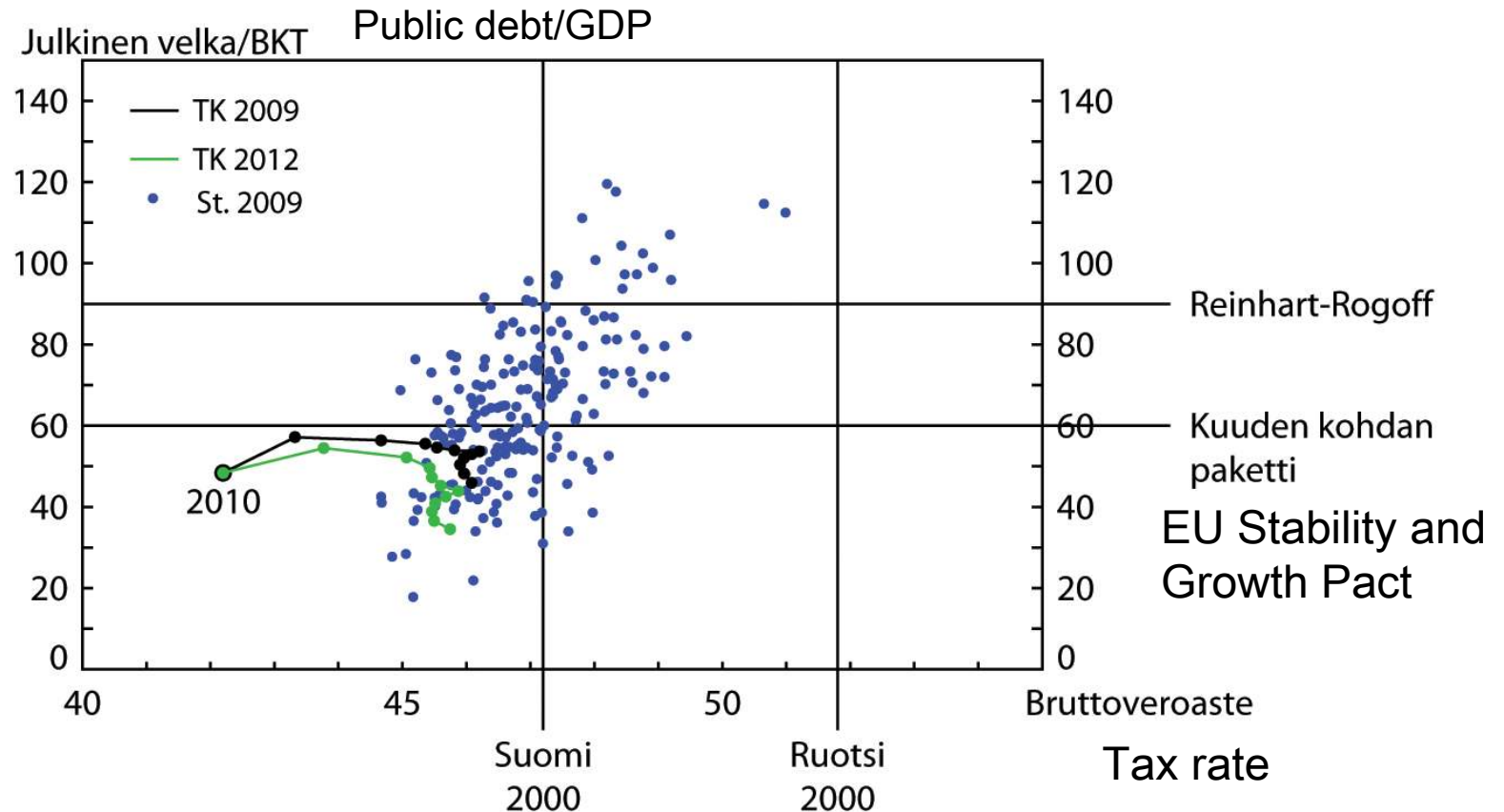
- ▶ G_t = general government expenditure in time period t
- ▶ T_t = general government revenue in time period t
- ▶ PB_t = primary balance of general government in time period t
- ▶ B_t = balance of the general government in time period t
- ▶ D_{t-1} = general government debt in time $t - 1$
- ▶ i = interest rate for general government debt
- ▶ ΔD_t = change of public debt in period $t = D_t - D_{t-1}$
- ▶ Y_t = total production (GDP) in time period t



Work programme and approach

- ▶ In cooperation with a selected research institute, quantitative stochastic assessment of uncertainties in the sustainability calculations
- ▶ Evaluation of different economic and policy scenarios in a dynamic general equilibrium model
 - ▶ actual health data
 - ▶ stochastic population forecasts
 - ▶ effective communication of uncertainties a specific topic of attention

Example of communication: public debt and tax rate in the beginning of 2060, source: ETLA/ Lassila & Valkonen, 2011 and 2013*)



*Studies on the sustainability of public finances carried out by ETLA research institute in cooperation with the NAOF



Our work programme and approach

- ▶ Multi-disciplinary evaluations combining qualitative and quantitative analyses
- ▶ Structural balance:
 - ▶ analyses of the quality and reliability of Ministry of Finance estimates
 - ▶ own independent analyses of structural balance
- ▶ Qualitative and quantitative assessments of the economic forecasts in a smaller scale concluded, no current work but on the work to be done list
- ▶ Assessments of the system of the economic impact assessment in legislative proposals; tax expenditure



Institutional structures

- ▶ Department at the NAOF under the authority of the Deputy Auditor-General of Finland, work directed by Director for Fiscal Policy Audit and Evaluation
 - ▶ 7 senior experts in audit and analyses + technical and communications support
 - ▶ national economics, business economics and finance, financial auditing and management, budgeting and law
 - ▶ Auditor General of Finland reports to Parliament
 - ▶ Auditor General of Finland appoints personnel on the basis of merits and is accountable to the Parliament
 - ▶ Auditor General of Finland elected by a secret vote in the Plenary of Parliament after the assessment of the candidates by the Audit Committee
- ▶ Scientific Council to give advice and to provide quality reviews



Access to information and transparency

- ▶ Right of access to information guaranteed by the Constitution and overriding secrecy (including national security)
 - ▶ in practise: good co-operation with the Ministry of Finance and good access to data
- ▶ All reports are public and forwarded to the Executive.
- ▶ Possibility for confidential exchange of views with the Government and Government ministries