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DIRECTORATE GENERAL EXTERNAL POLICIES OF THE UNION

BRIEFING PAPER

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PARLIAMENT AND PUBLIC FINANCE

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EUROPEAN PARLIAMENT

DIRECTORATE-GENERAL FOR EXTERNAL POLICIES OF THE UNION
DIRECTORATE B
- POLICY DEPARTMENT -

PARLIAMENT AND PUBLIC FINANCE

BRIEFING PAPER

Abstract:

This policy paper is one of a series of papers requested by the EP's Committee on Foreign Affairs in connection with its role as (rotating) chair of the Parliamentary Troika of the Stability Pact for South East Europe in 2006. The Committee has been organising four parliamentary seminars involving representatives from the relevant specialised parliamentary bodies (committees and sub-committees) from the region. This paper examines the role of parliaments and supreme audit institutions in budgetary expenditure, departing from the Belgian model. It will be presented and discussed at the workshop on parliamentary oversight of budgetary expenditure on 8 June 2006 in Brussels, in the specific context of experience and challenges in countries in South East Europe.

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PARLIAMENT AND PUBLIC FINANCE

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PARLIAMENT AND PUBLIC FINANCE

Franz Wascotte*

Introduction

"All powers emanate from the Nation"

This is what article 33 of the Belgian Constitution says.

The provision in this article reflects a principle dating back to the French revolution according to which powers can only be attributed through a system of successive delegation.

Government is allowed to exercise its powers only if they abide by the rules governing the distribution of competence between the three traditional powers and within the limits set by Parliament.

This is even more so in tax and budget matters. In Belgium, Government is required to obtain each year from Parliament a mandatory authorisation to collect taxes; if not, the tax department is not allowed to levy taxes during the financial year concerned. The same applies with respect to expenditure: the tax department is not allowed to exceed the budget allocations voted annually by the legislature. Another example in point is that the treasury unit of the Finance department is not allowed to dispose of property or provide collateral security if it did not obtain the prior approval of the legislative authorities.

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1. Improving the operation of Parliament

Regardless of the goal of the welfare state, public finance still plays a considerable role in the economy of a country.

Budget drafting by Government, its discussion in Parliament and the voting in a law remains one of the key issues of political life.

The purpose of the present paper is not to identify the budget format and structure or budget items. Several international organisations have already published guidelines on this issue and they can be used as valuable reference[1].

Nor is my purpose to identify the basic choices underlying public finance management, such as the significance of tax levies, the option of a direct or indirect taxation, the breakdown of expenditure among the main political components or the public debt level. All these issues, the technical aspect of which is not to be underestimated, are the expression of a **choice of society** that falls under the competence of political authorities.

Nevertheless, these **choices are eventually reflected in the budget**. Budget voting in Parliament is therefore not a mere formal act. Indeed, Parliament is to have a permanent control over the executive power to ensure that the political orientations discussed in Parliament are duly reflected in the State accounts, both in terms of revenue and in terms of expenditure. It has to see to it that budget proposals introduced by Government are adequate and that all budget amendments introduced during the budgetary year and immediately reported to it are accounted for. It also has to make sure that Government and departments have put sufficient systems in place to ensure that taxes are levied and policies conducted in compliance with law and regulatory provisions applicable, on the one hand, and with the principles of economy, efficiency and effectiveness, on the other hand.

In this connection, my paper will elaborate on several suggestions likely to improve Parliament's operation in its capacity of public finance "controller".

2. Obstacles to the exercise by Parliament of its power in the field of budget and finance

In the following part of my paper I suggest adopting an approach that consists in first identifying the main obstacles for Parliament to exercise its power in the field of budget and finance and then propose possible solutions.

It is worth mentioning that in order to improve public finance (or expressed otherwise to obtain additional revenue or reduce expenditure), most Governments have tried to cut down their commitments and decrease their scope of competence, among others by disposing of real assets (buildings, enterprises, shares,…). Tax legislation has become extremely complex and has undergone each year drastic modifications. Diversification of operations,

[1] see, for example, OECD Journal on budgeting

market uncertainties and the risks involved with these transactions has made Parliament particularly attentive to State revenue and expenditure control.

However, the complexity of the newly introduced financial mechanisms, the modification of the scope of competence of public authorities in many fields, the process of regionalisation, the globalisation of the economy as well as the multiplicity of the procedures specific for departments may inevitably threaten the ability of all Parliamentarians to monitor all aspects of public management.

2.1. Parliament's authorisation and supervision of public expenditure in the course of the budgetary process

When does Parliament mainly intervene at the various stages of the budgetary process to exercise its role of authorisation and supervision of public finance?

Budget is to be voted ahead of the beginning of the budgetary year; failing Parliament's authorisation, Government is not allowed to levy any taxes or carry out any expenditure.

Besides, as the budget is a mere projection, it can turn out necessary to amend the budget proposals during the budgetary year as some events were unpredictable before the beginning of the budgetary year. If Government is authorised to amend the budget according to the law, it has to inform Parliament immediately and Parliament then votes additional appropriations or adjusts the budgets.

Finally, at the end of the budgetary year, Government has to inform Parliament about the financial outcome of the budgetary year.

According to this frame, Parliament can only exercise its power in as much as certain conditions are met in practice.

2.2. The budgetary procedure is not a mere formality

One can regret that as years went by the budgetary procedure in Parliament has become a mere formality because what is at stake has already been decided primarily by Government, on the proposal of departments and sometimes with the help of advisory institutions or organisations.

In Belgium, for many years budgets were often voted after the budgetary year and sometimes even at the beginning of the following budgetary year so that Parliament's role has lost all meaning. Even nowadays the State general account is introduced so late that it's being discussed in Parliament has no relevance. Discussing this account several years after closure of the budgetary year is just a mere formal exercise devoid of any interest.

It could be observed that draft budgets were submitted late so that Parliament has not enough time to make an adequate control. Moreover supporting documents produced are

often insufficient and are only a replicate of documents drawn up previously. It could also be noticed that failing detailed budgetary proposals Government was carrying out budgetary transfers within the budget or amendments under the pressure of urgency in the course of the budgetary year concerned.

A parliamentary discussion on the budget is only relevant if **objective and sufficient information is furnished** to the legislative authorities to account for the level of the tax levy and to support the requests for appropriations.

Draft budgets are to be introduced **within sufficient time** to allow Parliament not to have to examine and vote budgets under the pressure of urgency and deprive Parliamentarians from the opportunity to receive an appropriate answer to the questions addressed to the minister concerned.

The primary condition is thus the introduction, in due time, of draft budgets duly documented by Government.

After the closure of a budgetary year Government has to account for its policies and informs the legislative authorities on the State financial situation by giving a **statement of revenue and expenditure** as well as of the public debt level. It is up to Parliament to ensure that Government introduces a pertaining report in due time.

2.3. Parliamentary control over revenue and expenditure

Public expenditure covers salaries and wages of public officials, public contracts, subsidies and, of course, social security (public sector pension schemes, unemployment benefits, child's allowances, etc.).

Public finance management entails various risks. A major risk has to do with the temptation to implement public policies or have public policies executed outside the budget. This can be the case if through subsidies, attributed revenue or any other financial mechanism, policies falling normally under the competence of public departments are managed by third parties, outside all budgetary frame and any public finance control.

It is worth pointing out that subsidies account for a large part of public expenditure. They exist in the form of financial contributions charged on the budget in favour of public enterprises, private companies or private individuals with the aim to instil a behaviour or support an economic activity (transport,…). Unlike a market where public authorities can acquire goods or services a subsidy is a "non recoverable" grant, as goods or services acquired by the beneficiaries are obtained for their sole profit.

Therefore, **special safeguards** have to be provided for by laws **to ensure that the subsidies are used in compliance with the goal** they were allocated for and to the sole beneficiaries mentioned in the law.

Parliament will have to ensure among others that the subsidies will not be perceived as a windfall, in as much as a **subsidy is assumed to change a behaviour and not simply to bring an additional income to the beneficiary.**

In Belgium another trend has developed these last few years in the form of so called *tax expenditure*. Tax expenditure refers to provisions whereby taxpayers are allowed to reduce their taxable basis by way of an exceptional expenditure allowance. The aim is to encourage a specific economic behaviour (house insulation, Council housing, strengthening of company's capital structure, …). They are de facto subsidies that fall under the direct management of the tax department. The main difficulty with these *tax expenditures* is to assess its financial impact and the economic ex ante and ex post effect.

2.4. Pluriannual management of public finance

The budget is an authorization given each year by Parliament to Government to cash receipts and carry out expenditure. When Parliament checks the relevance of public expenditure is it has to rely on correct and adequate information. It thus has to see to it that the information furnished contains a sufficient justification for the requests for appropriations.

Actually, public finance management cannot be examined without considering the **implications of State commitments from previous budgetary years**. These commitments refer more particularly to long term contracts for constructions, research and development, etc. Besides having an economic impact on tax and social revenue, on employment level, on economic development, these expenditures have also an impact on the budgets of later years. The point is thus to **find a way to accommodate the yearly budgetary process with a pluriannual public finance management** in the instance when a policy (affecting agriculture, education, health, …) has a multi-year or even a multi-decade or multi-generation impact.

As an illustration, it should be reminded that the State as the Nation's largest employer in general stands for the "continued salary" payments of retired officials. The large-scale recruitments in the seventies to meet the economic crisis at the time inevitably raised the problem of the funding of Government officials retirement pensions. The budgetary techniques used at the time did not allow to implement the present State commitments. Obtaining information on these commitments from Government is still today a prerogative that belongs to Parliament.

3. Ways of implementing a better public finance control

Here above we have tried to identify the main obstacles for any parliamentarian to exercise his power in the budgetary field.

Our purpose is now to suggest a few ways for a solution to allow Parliament to exercise its power but while doing so we will not go through the whole set of rules found in the law

relating to public finance. These solutions entail both improved accounting and legal instruments in the field of public finance management and enhanced and enlarged powers of the Supreme Audit Institution in the field of public accounts.

Parliament has thus first to accurately delineate the legal frame of public accounts laws.

The law could set the **time, the form and the lay-out** conditions for the introduction of draft budgets, draft budgetary adjustments as well as budgetary situation reports at regular intervals. The law could define the **level of budgetary specificity** and require that budgetary appropriations requests are supported by **adequate and relevant documents**. The law could also provide for **Government pluriannual budgetary proposals** to make up for the insufficient character of the principle of the annual nature of the budget. To ensure that budgets are voted within the time stated, the law could **cap the authorized expenditure level** for the budgetary year concerned as long as the budget is not voted (*provisional twelfth system*). As far as *tax expenditure* is concerned, the law could provide for the introduction by Government of a **report at regular intervals on the level and impact of these tax concessions** on tax revenue as well as on the expected and real economic effect of these special techniques.

Parliament could ask for **advice from non-Government institutions** which have the capacity and the powers to collate the information necessary, to carry out an analysis of this information and thus be able to communicate objective, verifiable and exhaustive information to Parliament.

A **supreme audit institution**, such as a Court of audit can play a **meaningful role auxiliary to Parliament**.

The law could provide that a supreme audit institution sends Parliament a **report on the budgetary proposals** concerning revenue as well as expenditure. The Court could identify possible revenue or expenditure overestimates, confirm, supplement or criticize Government's supporting programme and expose any infringement on law and regulatory provisions in the field of public finance.

Moreover, the law could provide that under certain conditions the Supreme Audit Institution could be **requested to send** Parliament a **report on the effect of draft changes in the social or tax laws**.

In the event of late introduction of the report at the close of the budgetary year, the law could provide that the Court would **draw up a *provisional account,* a statement of revenue, expenditure and commitments** for the year ended 31 December on the basis of the budgets newly adopted and amended by Parliament.

Finally, while ensuring that the right of information would be guaranteed for all people the law could provide that each parliamentarian would have **a right of inspection of department's files with the Supreme Audit Institution**. There should, however, be some limit to the exercise of that right of information to guarantee, among others, the protection of privacy and not hinder the operation of the department or the Court.

* * *

4. CONCLUSIONS

Parliament's budgetary role is essential.

Budget voting is the implementation of Government's political and economic agenda.

It has become particularly difficult for Parliament to fulfil its task of oversight of public finance management due to the limited time it has to review the budgetary proposals and the growing complexity of State management.

Nevertheless all these difficulties could be overcome if, on the one hand, specific provisions are written in laws on state accounts and if, on the other hand, the Supreme Audit Institution concerned is involved in the budgetary process.

Annex

PowerPoint presentation for the workshop on 8 June 2006 in Brussels

RESTORE
PARLIAMENT OVERSIGHT
OVER
PUBLIC FINANCE
~

F. WASCOTTE
Member of the Belgian Court of audit

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PLAN (1)

Role of Parliaments

Importance and Scope of Public Finance

The budgetary processus

Risk Analysis – And response

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PLAN (2)

Tax and revenue

Expenditure

The Public debt

The performance of the Administration

3

ROLE OF PARLIAMENTS (a)

« Tous les pouvoirs émanent de la Nation »
Primary source of legislation
Appointment of Governments

~

Authorise :

- Collection of taxes
- Commitments and payments
- Loans when disbursements cannot be covered by revenues

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ROLE OF THE PARLIAMENT (b)

Political surveillance of Government

~

Permanent oversight over public Finance

~

Approval of budget

Amendment to approved budget

Examination de budget outcome

5

SCOPE OF PUBLIC FINANCE

Tax and revenue of the State

Commitments expenditure and disbursement

Public debt management

6

THE BUDGETARY PROCESS

Approval

Amendment

Budget execution report

7

RISK ANALYSIS (Budget) (1)

- Delays in the process of approval of the budget before the fiscal year
- Non submission of budget amendments during the fiscal year
- Delays in submission of budgetary reports after fiscal year

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RISK ANALYSIS (Revenues) (2)

Tax expenditure

Lack of adequate assessment of changes to legislation on tax and social security revenues

Sales of assets and properties

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RISK ANALYSIS (Expenditure) (3)

- Lack of sufficient evidence to support budget proposals and amendments
- Inadequate forecast of Costs (long term projects)
- Grants and subsidies
- Decentralisation
- Transaction outside the budget (extra budgetary funds)
- Human resource management
- Hidden commitments

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RISK ANALYSIS
(Treasury and Public debt) (4)

- ✓ Cash and loans management
- ✓ Excess of public debt

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RESPONSE TO RISK ANALYSIS

Adequate provisions of legislation on Public Finance management

Role of the Supreme audit institution

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ROLE OF SAI

- Review and report regularly to Parliament on
  - budget proposals
  - budget amendments
- Review documentation to support budget proposals
- Analysis of reports submitted to Parliaments
- Evaluation of financial impact of modification of tax or social legislation
- Provide Parliament with provisional budget reports when delays in issuing budget outcome
- Access and information rights

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